FOUNDATIONS IN TAPE READING

by Pete Renzulli

STOCK TRADING PRO

Why do Some Traders Always Seem to Make Money?

Imagine expecting to make money…

This week or this month, you fully expect to earn a trading income. And next month too.

Not because the market gives us a gift. Not because you get lucky.

But because you know what you're doing. Because you know how to make money.

Because you know what to do, regardless of what the market does. No gimmicks, no secrets, no hoping. You simply understand how to make money, and you're ready to execute.

The best traders expect to make money. The best traders have a plan. The plan tells them exactly what to do, before the market opens. These traders exude confidence.

Struggling traders hesitate. Struggling traders react. Struggling traders always feel close, but never achieve financial stability.

Which trader are you?

How to Trade With Consistency

What if you could see your next trade, before it happens?

How would this affect your decisions? How would this make you feel?

The best traders have this vision, and you can too. This process begins by eliminating one side of the market. By focusing your resources on your edge.

A seven-figure trader once told me "If I have a long bias, and my stock traded five dollars lower, I bought the one-dollar bounces."

This extreme example sounds ludicrous but the point is clear. To trade with consistency requires an edge. An edge you believe in. My edge is tape reading.

Consistency begins with clarity. Knowing exactly what to do, becomes your top priority.

I struggled with boom and bust trading too. The inconsistency vanished when I planned my trades in advance.

You may exit winners too soon. You may hold losers too long. You may feel your stop-loss always get hit. You may think these problems need solving.

They don’t. They are symptoms of the real problem.

Becoming a better chart reader won’t make you a better trader.

If these symptoms sound familiar, the consequences stem from how you view price action.

You have those “problems” because you’re missing a process. Get the process, the problems go away.

If you’re ready to kick your trading up a few levels (where the money is plentiful and less stressful)… then it’s time to organize your resources around reading the tape.

It’s time you learned the same trading system I taught to my prop traders.

Tape Reading the Stock Market. Lessons from Jesse Livermore

Tape reading is not as popular as it was in the old days. Computers have taken care of that.

Savvy traders have adapted and are skillfully implementing tape reading in a much different way today. Chart reading is one method. Another technique is interpreting news and volume traded off the news.

When I say the old days, I am referring to 2007. This is when the NYSE expanded to allow increased amounts of electronic trading. (More on this at the end of the report)

Traders would read the ticker tape (invented by Edward A. Calahan, updated by Thomas Edison) to determine the recent buying and selling pressure.

It was much easier to spot a large buyer or seller because daily volume was incredibly light so it was easier to spot a big player. The down side to light volume was liquidity. It could be difficult to exit a trade at a reasonable price.

In the early days there were "bucket shops" to place your trades. I guess you could say they were the first brokerage houses, but without brokers. Prices were posted to a chalkboard as they crossed the ticker tape.

An interesting book to read is Tape Reading and Market Tactics. It is a terrific $7.95 education from 1931. It includes actual numbers and volume from the stock market. A classic trading book to have in your office.

This is how I first came to take an interest in the message of the tape. The fluctuations were from the first associated in my mind with upward or downward movements.

Tape Reading Methods

“Of course, there is always a reason for fluctuations, but the tape does not concern itself with the why or wherefore. It doesn’t go into explanations. I didn’t ask the tape why when I was fourteen, and I don’t ask it today at forty…”

This is an important quote by Livermore. Too many traders want to know “why” after the fact. Tape readers by the very definition, don’t interpret THE WHY.

Tape reading is interpreting price action.

"The reason for what a certain stock does today, may not be known for two or three days, or weeks, or months. But what the dickens does that matter? Your business with the tape is now-not tomorrow.

The reason can wait. But you must act instantly or be left. Time and again I have seen this happen..."

To put this quote by Livermore in context for the modern trader, we could call them momentum traders.

"You'll remember that Hollow Tube went down three points the other day while the rest of the market rallied sharply. On the following Monday you saw that the directors passed the dividend. That was the reason..."

Notice Livermore wasn't making notes to potentially trade the reason in the future. He didn't care why.

He was simply reading it and found the reason amusing. Modern tape readers can use the news to trade stocks in play.

The correct way to implement this strategy is to use the news as a catalyst to find stocks in play, but…you are ultimately going to trade the price action.

There is a difference between a catalyst and trade management. Struggling traders believe a catalyst or an edge will translate into profitability. Your edge, or any reason to be in a trade, is only the first part of the trading equation.

The money is made or lost in trade management.

An amazing educator and trader, Marian Boyle, writes a must-read post each day for the community Good Morning Wall Street. It is a great source to find stocks in play each morning.

"Well, I kept up my little memorandum book perhaps six months. Instead of leaving for home the moment I was through with my work, I'd jot down the figures I wanted and would study the changes, always looking for the repetitions and parallelisms of behavior -learning to read the tape, although I was not aware of it at the time."

Jesse Livermore made it clear he was keeping a trading journal. He also points out that he stayed late to improve. I can't tell you how many traders I have witnessed over the years leave when the bell rang at 4pm.

It was sad to see. If this is you, you have absolutely no shot at success. I used to joke about a daily fire-drill at 4pm.

Trust me. Those who understood, knew I wasn't joking. How you spend your spare time will dictate how you spend your future.

How Technology Affected Tape Reading NASDAQ Stocks in 2001

There was a giant difference trading a listed stock versus trading a NASDAQ stock at this time.

You traded NASDAQ or listed NYSE (or AMEX at that time) but few traders traded both.

There was an edge day trading NASDAQ stocks prior to 2001.

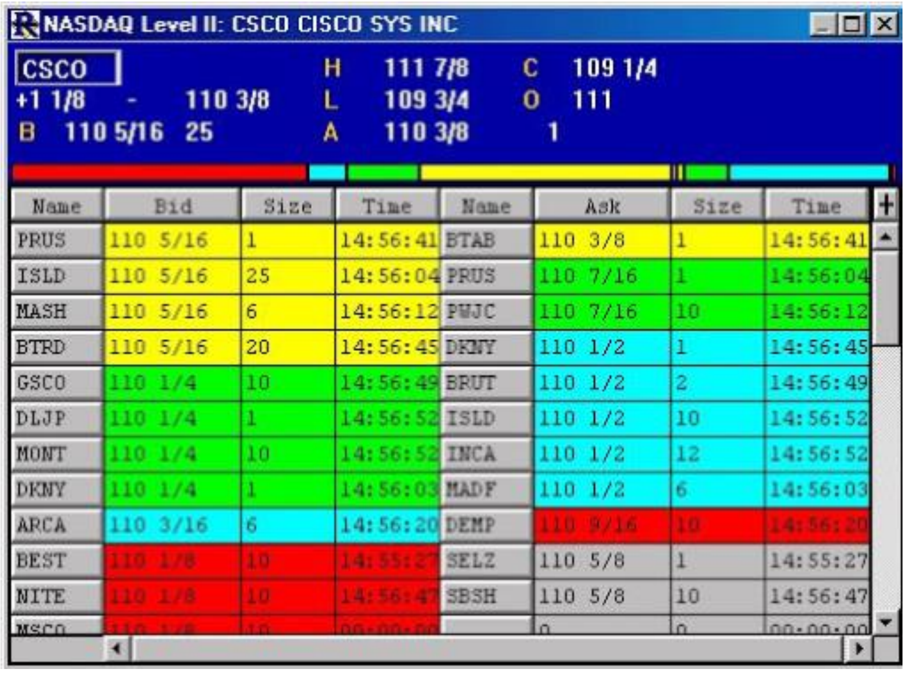
At this point NASDAQ and their market making structure was automated and ECN activity was gathering a large share of activity. Market makers fulfilling order flow for institutions decreased dramatically.

The most popular trading style implemented by active traders was all but gone for NASDAQ. Monitoring the bid/ask quotes for size vanished quickly. For those of us trading full-time it was mind boggling.

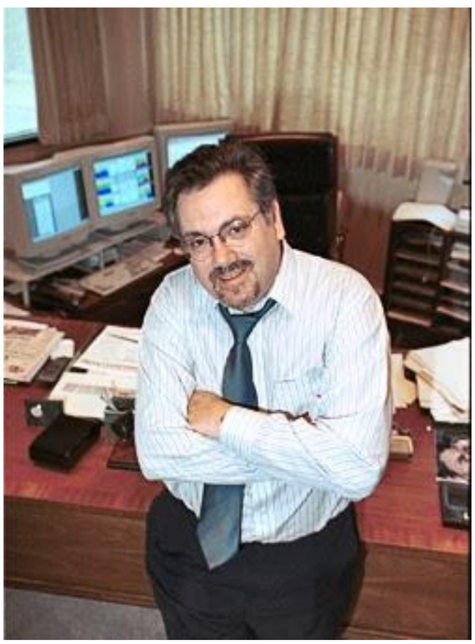
It was like owning a hamburger restaurant being told chop meat distributors don't exist anymore.

Reading the tape in NASDAQ stocks relied heavily on whether a stock was "well-bid" or well-offered." If you went long (bought stock) and Goldman Sachs was quoting a large number of shares to buy on the bid, you felt safe.

Your risk in the trade was implied to be manageable because you could "hit the bid" and exit the trade by selling to Goldman.



If a big market-maker was quoting large size, you had every reason to believe it was a real quote. Essentially you were tape reading by monitoring the size of bid/ask quotes and WHO the quotes belonged to.



I worked for Harvey Houtkin back then. He was not a popular guy but he was usually right and he fought to level the playing field for the retail trader.

His ECN (electronic communication network) was a growing force on Wall Street at this time.

Many traders like to claim the SOES Bandit title. He was the Father. No one disputes that. (His biggest battle was to get SOES, the small order execution system, implemented for retail traders)

How NASDAQ Traders Read the Tape Prior to 2001

The first part of the trade set up was stalking bid/ask quotes. The second part of a NASDAQ tape reading strategy was following time and sales. This section of a "level 2 box" was where a NASDAQ day trader monitored the actual transactions.

You were looking for obvious buying or selling pressure. This was modern day tape reading. Green "prints" represent active buying. Red "prints" are actively selling.

"Active" means someone is actively buying or selling advertised shares of stock.

For example, a bid/ask quote of GSCO 2,000 25.25 x MLCO 3,000 25.27 means 2,000 shares are advertised to buy at 25.25 and 3,000 shares to sell are advertised at 25.27.

I can advertise to buy at the bid (and hope someone actively sells to me (this would be a red print in time and sales).

Or I can buy actively from the shares advertised at 25.27 (this would create a green print in time and sales).

In the above example GSCO was a bid (advertisement to buy) by Goldman Sachs and MLCO was an offer to sell advertised by Merrill Lynch.

To complete the strategy of reading the tape for a NASDAQ stock, we would look for a "well bid stock" and "green prints" on the tape (time and sales).

As long as active buying was occurring (Large and consistent green prints, I would continue to be a buyer.

When the prints started to look like a Christmas tree ornament (red and green active trades), this means indecision and it was time to sell.

Technology began to change as did executions. NASDAQ implemented the SELECT-NET system and the tsunami started.

Select-net was an active trade you could execute for shares against a market-makers quote.

You could buy or sell actively. The problem for traders was a market make could hold your trade 31 seconds before deciding IF they wanted to fill you. It was ludicrous but real.

This began the downfall for NASDAQ market-makers.

Additional electronic executions came into play and then decimalization destroyed the spread between the bid/ask price.

The game was over when "super-montage" was introduced and market makers essentially became liable for unlimited shares against their quote.

This meant traders (and now computers) could quickly make active trades for unlimited amounts. (Prior to this the market-maker had to physically fill your order)

With this increased risk they started to quote less size, automate updates and use ECN's more.

Market making for a living was dead. And along with it was old school tape reading methods. (Don't feel bad for market makers. They made a fortune)

How Technology and Volume Affected Tape Reading NYSE Stocks in 2007

There was an edge day trading NYSE stocks prior to 2007. Tape reading was easier, there was far less electronic trading. The floor of the New York Stock Exchange was dominated by "specialists."

A specialist is in charge of making a "fair and orderly market." This meant they were in control of the price action on the NYSE. The floor was a giant community of specialists, floor brokers, clerks and institutional players.

A fascinating book written by Charles Gasparino about this history and how the floor operated called King of the Club is a must-read for any student of the stock market.

If you wanted good fills on your price there were two methods to execute a trade.

Physically speak to a specialist (which meant you needed to be a part of the community)

Place an order from off the floor using a Super-Dot system.

In scenario #1 the greater the potential order, the better the fills, or at the very least the more attention you received. You see a specialist would make money on this “order flow.” The more shares safely they could match buyers and sellers, the more money they made. This is why they needed to know “what’s behind your first order?”

The more you had to buy or sell the easier their job was. Whoever controlled the order flow controlled the stock. A specialist who worked hard to get you better fills (or as close to VWAP for that day-value weighted average price) would get lots and lots of order flow.

Meanwhile… the retail trader sends orders to the floor and had to wait for a fill.

YES, YES, YES, I know there were order handling rules and “we take care of the public” and all of that stuff. Who would you give priority to? A million shares of order flow or a 100-share order to buy IBM?

Anyway, I am sure you could see the edge reading the tape for a NYSE stock. Follow the specialist!!

From your computer, a trader could see the specialist bids/offers and the price action in time and sales. Trade with the specialist and you were in good shape.

To make it even easier there is a “specialist book” you can lease electronically each month to see the shares advertised to buy or sell at levels outside of the inside market (the highest bid and lowest offer).

How cool was that? My friend Rob C. would say the specialist was “stepping up or stepping down his quote.” He made a great living following the specialist. He was trading over a million shares per DAY using this method of tape reading.

Then things changed. More and more money was being earned by executing electronic orders.

The exchanges wanted more volume on these risk-free transactions so the powers that be on the NYSE shook up the specialist world by announcing the Hybrid trading system.

Remember how I said your DOT order (direct order turn around -later super-dot) was physically filled by the specialist?

Well not only did they have this privilege but there were rules in place for how many shares you could attempt to buy or sell against a specialist quote.

As things evolved you could execute a trade against a specialist quote with limits. You were able to buy up to 1099 shares, on one side of the market every 30 seconds. So in other words you could not buy, then buy immediately again.

You had limits in time and size. Though you could buy, then sell. This is considered different sides of the market.

Well hybrid wiped away 100 years of the specialist privilege in one bold move by the NYSE. The limit rules for electronic executions against a specialist quote were essentially removed. I say essentially because they were expended to 999,999.

The specialist was now exposed to a barrage of executions against a quote and could not possibly handle the flood. The result was never quoting size on the bid/ask (at the inside market).

This meant the massive order flow that was “worked” by the specialist, was now traded in 100 share lots over the course of a day, week and months.

The orders are filled electronically. Specialist firms now employ algorithms to make a market and the floor of the NYSE is a ghost town. It’s a place for CNBC to have in the background during a broadcast.

Following the specialist no longer works. Traders like my friend Rob are now swing trading. His edge is gone.

Were market-makers and specialists doing anything “wrong?” I guess that depends on who you ask but they weren’t doing anything illegal.

They took advantage of the system in place. As any good capitalist would do.

At one point I had over 25 former NYSE specialists, clerks and brokers trading in my NYC office. The education they gave me on order flow was amazing.

Tape Reading in the Modern Stock Market

Sounds pretty grim doesn't it?

How in the world does the modern trader read the tape? Great traders adapt. If there is any guarantee in the market, change is constant. You adjust or move on.

"I think Linda Rashke said it best: "Modern day tape reading from a computer is determining if price is moving closer to or further away from a significant reference point."

For the modern trader this means charts. It can be moving averages, candlesticks, Fibonacci numbers or any other method of monitoring price action.

The method doesn't matter.

The key is to have a system for determining who is in charge. Can you look at price action and clearly say buyers or sellers are in control of this stock?

FOUNDATIONS FOR TODAY'S TAPE READER

Let's start with a few questions.
Does it feel like when you have a really good trade, you have the least amount of shares and you get out too soon?

Or when you have the most shares and you really loaded up on a position, are those the trades that never work out?

Do you end up taking bigger losses than you expected on the bad trades or the trades that don't work out? And do you have the fewest amount of shares on the trades that keep going and keep going and keep going?

Probably one of the most annoying things that we can do as a trader is to have the wrong shares at the wrong time.

I’ve been working with traders with different levels of experience. Some have a fresh perspective, where it's the first time they're actually getting involved in the market. Others are coming in with baggage.

Those are the traders that have put in a lot of work and are holding onto what they've done in the past. They’ve developed their own style. It's not working, and they know that they need help.

Generally, they’re the hardest to work with. Because of the time they’ve invested, they want to either hold onto what's not working or try to adapt what they know is not working to something else.

➡ My number one point to any level trader, you need to have a solid game plan going into the day.

LEARNING TO TRADE

There are three stages of active trading.
First learn how to read charts, you're a chart reader.

The next part is learning how to read the tape so you go from chart reader to tape reader. Tape reader simply means that you learn how to build an argument for a great idea.

The last part stage three is when you learn how to make money. It's what happens between enter and exit that separates you from everybody else who's struggling.

Let’s walk through tape reading.

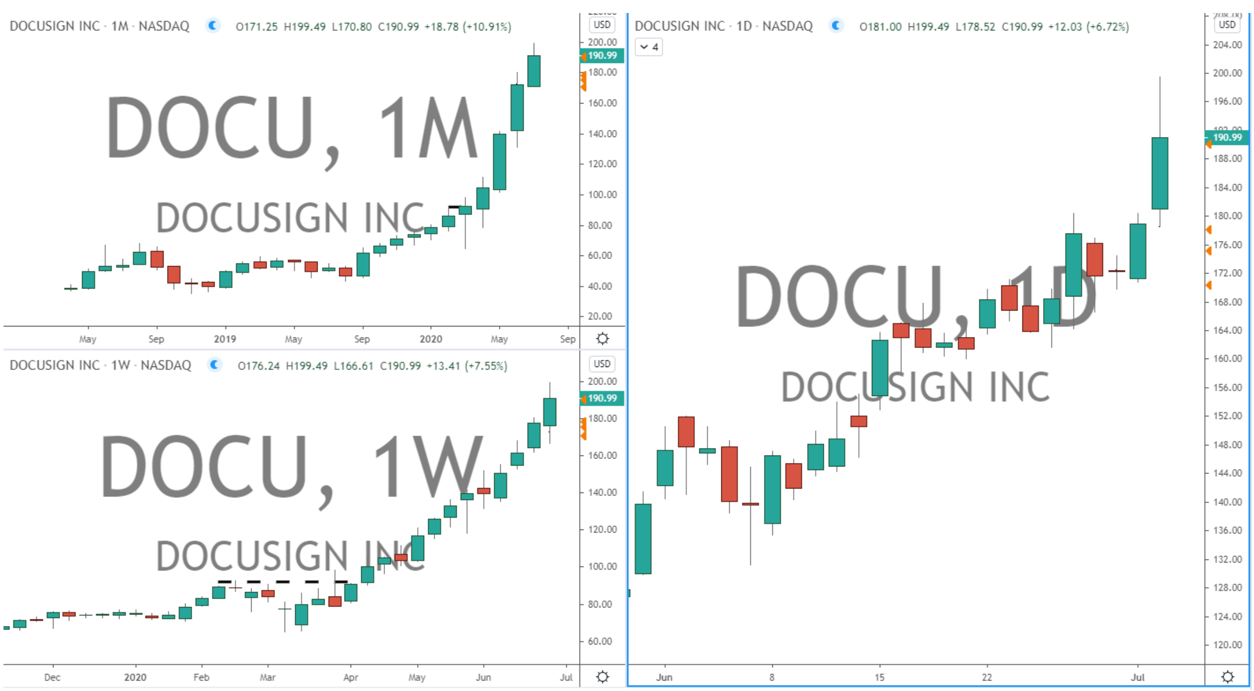
Tape reading is when a stock is moving closer to or further away from a certain price, in addition to having the bias, in addition to having an idea of whether or not that stock is bullish or bearish.

BUILDING A COMPLETE TRADE ARGUMENT

The entry points are actually the last simplest, most rudimentary part of trading, because anybody could look at a chart and say, "Is this the right spot to get in?" Where you get in is not the most important part of a trade.

Sure, you want to get the right price. More importantly, you want to get the price that matters to you where you can manage risk, where there's reward potential.

But determining if there is something to do in the first place and how strong that idea is, is the number one thing to do. That's what tape reading is.



Tape reading is looking at the market, putting all of the pieces together and saying, "That's worth taking risk on," or, looking at the charts and saying “There's nothing going on right now. Why am I even logged in?”

There’s a quote that I use often - first pick a side, then pick a spot.

Many new traders come into the market and get absorbed in, "I want to make money now, which means I need to look for a spot to get in now." They jump right past understanding whether or not you have a good idea in the first place, because the quality of your idea is the real risk in the trade.

The other part of the risk is whether or not you have discipline to manage the trade accordingly. The quality of the idea, or in my terminology - we need to build an argument first for the ideas, before we even look for an entry.

The first couple of things I want to know when building an argument:

- Is there an obvious direction?
- Is there a price or prices that the stock is having a hard time getting through?

As you look through your charts, I strongly recommend that you start doing it without moving averages, just to start to learn how to read the tape, learn to read whether or not it's super obvious or not super obvious.

You want it to be so obvious that you could pick a side, only then do you pick a spot if there's profit potential.

What we're walking through right now is the core, the basic part of tape reading, which is you want to leave being a chart reader and become a tape reader.

Once you learn to read the tape better, then the next part is actually learning how to be a trader and learning how to make money on those better ideas that you're finding.

Seek first to read the tape and understand if there's an opportunity, and only then do we start to drill down. Now, if you're in the market and you're struggling, that means that what you're doing right now is not working, so you need to be open to new ideas.

Because if you don't, and I'll tell you, it's a very expensive time investment, where you could spend years feeling close.

There's no worst situation for a trader, where you spend years not making money and not losing money anymore, but you're continuing to do what doesn't work.

Get to the point where your number one priority is paying attention, asking the right questions and adapting to what is the results that you're getting and making fast decisions to improve.

You need to really learn how to spot great opportunities before you put money in harm's way. A lot of what I keep preaching is patience. Because if you don't throw your money away when it's not obvious, it's easy to make money when it is obvious.

YOUR PERFECT TRADE & EVERYTHING ELSE

Building an argument for a trade, your **A+ trade** and that's the perfect trade. And then, everything that's not your perfect trade, you should be able to recognize in an instant and say, "Okay, even if I take this trade, what does that mean for risk management?

What does that mean for leverage? What does that mean for potential profit taking? “Building all of those pieces into the argument is what we call tape reading.

Tape reading means you're putting all of the pieces together to determine whether or not a trade is worth it and how much it's worth it to you by justifying the risk in exchange for the potential profit. Putting all of those pieces together is the argument.

There are so many different things you can look at. There are so many different news stories that you could pay attention to. It really comes down to, can you look at a stock?

Can you look at the market and say, "I absolutely know what I'm looking at. Now, I have to learn how to make money."?

You know that better than anybody because you have a number. You have a significant level that that price is moving closer to or further away from. That's how you read the tape.

But the trick is how do you do that before you get into a trade because that's actually how you build the argument. That's how you build the argument for your trade. So, when you understand tape reading, you'll be able to look at a stock, look at any market and say, "Okay, that's my reference point and that's where I'm going to look from," before you put the trade on.

Once you understand what you're looking at, you can see if it's an idea is good because it has not moved too far already where it's difficult to manage the risk. Then you can start to allocate real money to the market and feel like you are in control.

You want to be the asset that produces that money. Think about all of the Wall Street firms that have algorithms spitting out ideas and making consistent money. You want to be the reason that happens for yourself, so you want to develop yourself as the asset.

Tape reading is really old. Thomas Edison developed the ticker tape and that's where old-school brokers would actually read the tape. They would read what they would come across and you would actually see the ticker going up or down.

But, the mystery behind tape reading is how do you actually do it. It sounds really exciting. I get all these warm and fuzzy, nostalgic feelings about it.

How do you actually do it? I'm going to tell you flat out; you already know how to do it.

Ask yourself - is a price moving closer to or further away from another price or another reference point?

Tape reading is the entry price that you have. You know if that stock is moving further up, that's your entry price and you know the stock is moving that way, or if the stock is going this way and it's going nowhere.

But you know that better than anybody because you have a number. You have a significant level that that price is moving closer to or further away from. That's how you read the tape.

The trick is how do you do that before you get into a trade because that's actually how you build the argument. That's how you build the argument for your trade.

So, when you understand tape reading, you'll be able to look at a stock, look at any market and say, "Okay, that's my reference point and that's where I'm going to look from," before you put the trade on.

TAPE READING FOUNDATION: THE OPEN PRICE

Now, here's the key. Once you understand this one price, you'll never look at the market again the same because now you'll know exactly what you're supposed to look for. It works on every timeframe.

It doesn't matter if you're a day trader. It doesn't matter if you're a swing trader. Quite frankly, it doesn't matter if you're a longer-term position trader where you buy something in January and you get out in March.

It's all the same. It’s called the **open price**. There's also the previous high and the previous low. Those three levels are what we're going to talk about.

But, the number one level we're going to focus on is the open price. We're going to actually go back to the charts and we're going to take a look and do a lesson on tape reading.

We're looking at a Square weekly chart.

Now, you know that the color of the candlestick represents the distance between the open and the close. So just reading one individual candlestick is tape reading because you're watching the color of the candlestick.

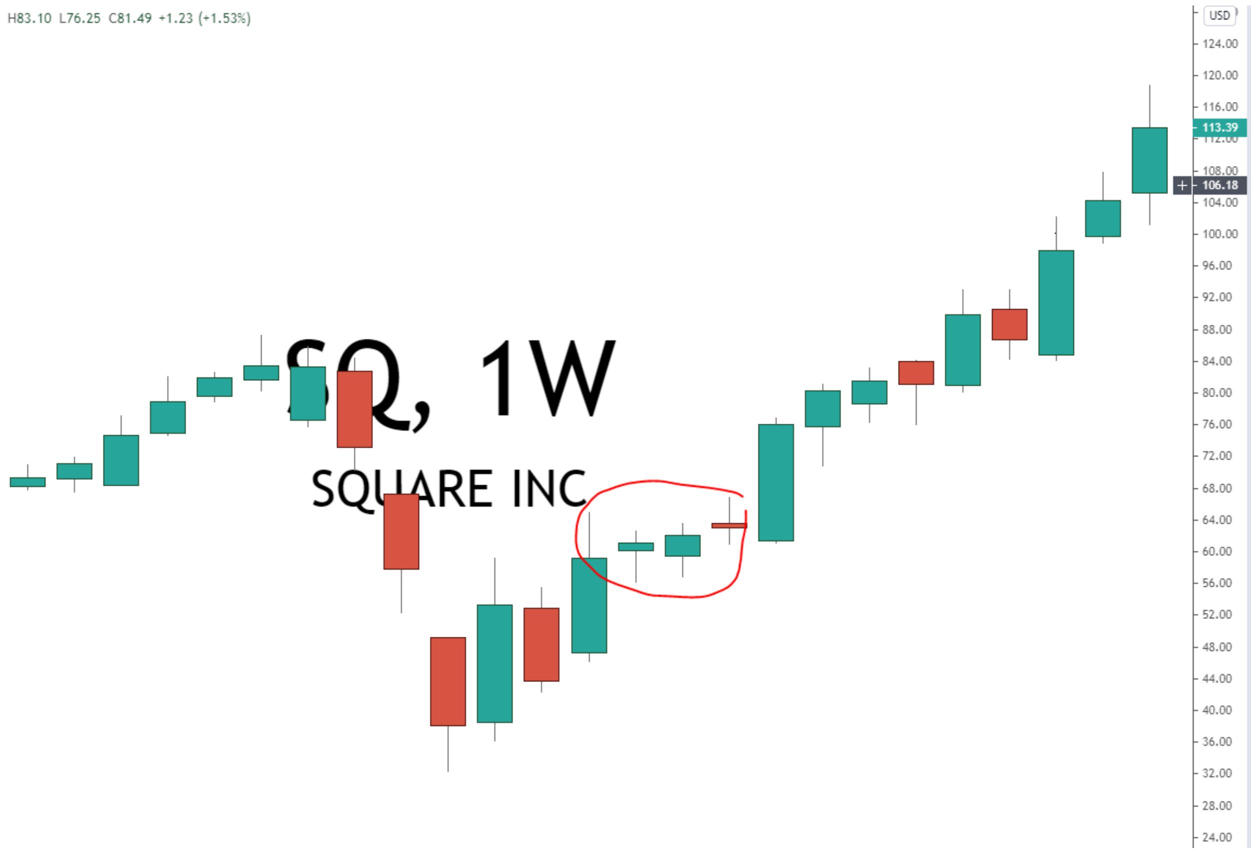
In this case, it's green, which means that it opened down here. Looking at the open price and the relationship of the last price to that open price. A large green candle means it opened down here, so you focused on the open price.

As long as it stays above that open price, that means that right now, while you're reading the tape, buyers are in charge of that stock.

Then, you have an example, where that's the open price and that's the close, which is why this candlestick is red. So, reading the tape in this particular example is bearish and sellers were in charge for most of that window because it's red. It's a large red candlestick. There's a big distance between the open price and where it closed. You are tape reading based on the relationship between the last price and the open.

You're going to make that move from chart reader to tape reader because now you're asking what is the open price and where is the last price compared to the open price? Is it moving further away or is it moving closer to,"

In this case right, a very small body candlestick means that they open and the close are basically in the same place. That's why I call them indecision candlesticks.



Once you have a reference point (entry price), I call them significant reference points, you can make your plan.

Then, you go down to what we would call a lower time frame, which is the daily timeframe.

As long as the daily chart is doing the same thing as the weekly chart, you can feel comfortable looking for spots to buy.

Let's say you start with the weekly candlestick. Monday, had an opening price. As Tuesday unfolds, then Wednesday unfolds, no matter what, the first trade on Monday is where you're going to read the tape from.

When you say is price above that or is price below that, that tells you if buyers or sellers are in charge during that time period.

Always remember, tape reading means you have a price, use the opening price. And then, is it moving above that or is it moving below that? And then, you look for entries on what we would call the lower timeframe.

Now, you're 100% in control saying, "Okay, I understand what I'm looking at. That was green yesterday. It's not green anymore. I'm going to make a different decision."

That's really where trading starts to get fun. This is the beginning part of learning how to read the tape. It shouldn't be a mystery anymore.

TAPE READING ADJUSTMENTS FOR VOLATILITY

Day trade and risk go together, it's tough to say one without the other.

The problem for most new day traders is they never learn to adjust risk with volatility. A $500 risk is not the same in every stock or from day-to-day.

Stocks have different volatility, known as average true range. This is the amount price action fluctuates from high to low (on average). New traders should assess risk tolerance, capital and decision-making ability and coordinate these resources with volatility.

The truth is, new day traders can't handle faster, wider movements. They have not learned to make good decisions yet. They don't have enough experience.

This is one of the top reasons talented day traders fail. They trade too much volatility too soon. They are focused on potential profits before learning how to handle risk.

Day Trade and $500 Risk

I can't tell you how many traders want to day trade $NFLX simply because it moves a lot. There is nothing wrong with this, if it fits your skills and risk parameters.

A day trade in this stock with a risk of $500 can be wiped out in 5 minutes without choosing the correct combination of share size to stop-loss target.

As volatility rises in your stock, you can reasonably expect wider swings from entry to stop-loss target. This means you can still risk $500 but you would allocate fewer shares to compensate for the difference.

Could you trade with a tight stop and use the same shares? Yes, but you are setting yourself up to get stopped out on normal price action. You need to set your stop outside of this noise.

Volatility Adjustment and The CBOE $VIX

This chart of the CBOE Volatility index demonstrates expected future volatility. It is also known as the fear index.

As the $VIX rises, volatility rises and selling pressure tends to increase.

Tape Reading Lesson: You should monitor the reading of the $VIX and the trend of the $VIX so you can adjust share size to be in line with accepted risk.

*This also means short-selling if there is an obvious up trend in the $VIX is a good play (assuming the stock in not in a valid uptrend)

Rules to Protect Capital While Taking Advantage of Wider Price Swings

#1: Pick a dollar amount you are willing to risk and then choose the correct amount of shares. The sign of an amateur is a day trader who trades the same amount of shares every trade. Reverse engineer the trade.

Accept the risk and then determine how many shares based on the difference between your entry price and stop loss.

#2: Accept the risk and stick to it. Putting on a trade and accepting the risk is not the same thing. You are guilty if you have ever moved a stop loss. If your stop loss is going to get hit, let it get hit.

Exit the trade and simply look for another spot to enter if the trade scenario is still valid. Under no circumstances should you add to a losing trade-especially in this environment with the increased volatility.

#3 Take quick profits: Increased volatility translates into wind-fall profits. Well executed trades can pay quickly. Be smart, don't be greedy. You are a swing trader not an investor, take the profits and move on. If your profit target is reached in two days instead of seven book it!

#4: Learn to short-sell or stay out of a market decline. If the concept of earning money as the market moves lower is un-American to you or you simply don't understand how it works, step aside and find a stock that has a bullish edge. You don't need to be involved all the time.

Recap: Increased volatility means increased opportunity. If you are prepared with correct risk and disciplined, this can be an exciting time to day trade. If you are a new trader and not sure how to recognize this scenario make it a point to watch the $VIX. As it rises the average range of stocks increases. Adjust your share size lower in sync with a rising $VIX and you will have a sound money management plan.

Trading Losses: How to Act Like a Pro

Trading losses are guaranteed, yet for some reason, new or struggling traders seem surprised when they happen.

A few years ago, I was hosting a seminar in NYC and I asked this question to the room:

Is placing a trade, accepting risk?

I asked for a show of hands to see who believed this was true. Virtually every hand went up.

OK, that was the answer I expected (which is the wrong answer).

On to question #2:

Have you ever moved or cancelled a stop-loss just as it was about to get hit?

Again, most traders in the room admitted to this attempt at avoiding a trading loss. So many traders agree it looked like the room was doing the wave.

And this is why most traders have a problem with trading losses. They never expect to have them.

Here is the reason why, this hidden flaw, prevents a trader from succeeding.

Placing a trade is not accepting risk. Placing a trade is taking risk.

If a trader truly accepted risk, which means accepting the possibility of a trading loss, before the trade, the trader would never move the stop-loss or cancel it.

This is because prior to the trade, she accepted the dollar amount at risk, in exchange for the potential profit.

In other words, you accept the risk/trading loss as a business expense. And if it happens you simply move on to the next trade.

TAPE READING RULES THAT LEAD TO CONSISTENT P&L

Day trading rules are the gorilla glue that hold your trading together.

Without rules you don't stand a chance. With rules, well, it's less difficult.

Yes- day trading is that challenging.

Day Trading Rules are the Ultimate Sign You Take Trading Seriously

There are so many moving parts, it's easy to get seduced into the action. The action is what we crave, but it's patience that pays the bills.

We need day trading rules because we can't predict the market. You may think you can, but trust me, you can't. Nobody can.

What you can do however, is know exactly what you are going to do. This is where the money is. The more specific your rules, the more consistent your P&L will be. Take that to the bank.

Let's dive into my trading rules.

Day Trading Rule #1: Make a commitment.

The minute you make a commitment to a strategy, you immediately have focus.

It's no accident this is day trading rule #1. Far too many traders overestimate their resources. It is incredibly difficult to trade everything.

Decide exactly how you define an edge. This means everything else is off your board. You're not going to be swayed into a trade you didn't plan. This is incredibly difficult if you are trading in a proprietary trading office. The adrenaline gets pumping and you want to do something. Resist it.

Stick to your strategy and master it. Make it a rule to trade one strategy, and one only until you are making consistent money.

Day Trading Rule #2: Accept Risk, Don't Take Risk.

Traders who move a stop-loss never expected to need it.

They never expected to face a loss. If they did, they would simply exit the trade.

If you learn to accept risk in exchange for the potential profit, you never hesitate. It's the cost of doing business.

What does it mean to accept risk? It means before the trade you decide on a dollar amount you are willing to put in harm's way. You adjust share size for volatility but you don't change the risk amount.

As you gain experience you can adjust risk based on the quality of the idea but in the beginning, you want this to be a hard rule.

Day Trading Rule #3: Get Your Game Plan Homework on the Schedule

Game Plan on the 7's.

Set a scheduled time to craft your daily game plan. Make it an appointment. Don't wait for the last minute, don't ask your buddy what she is trading. Man up and get prepared.

I do mine at either 7pm or 7am. I want to give my list of stocks to trade some time to breath. My best game plans are done at 7pm, then I review 7am. This gives me time to review, and lets me make adjustments in case of news.

The absolute power, that results from a solid game plan, can't be measured in numbers. To trade like a pro, you need to get serious about scripting your success.

Day Trading Rule #4: Journal Fast-Edit Later

You don't need to write a book, but you do need to write. Don't worry if it's perfect. Just write what you observe.

Yes-you need to journal while you are trading. You will NEVER remember at 5pm what you noticed at 10:15am. Not with clarity and context anyway.

Don't tell me you are too busy to write when you are trading. That's saying you don't have time to document how to be successful. It doesn't need to be detailed. Bullet points are fine, you can add to the point later.

If you are diligent, you will find yourself writing the same thing. Maybe not 2 days in a row but most likely twice in the same week. Most often it's a mistake. Something you need to stop or do more often. Either way it's in print so you can review.

Your day trading rules will change as your skills evolve, but this rule should never be let go. It's that important.

Day Trading Rule #5: Don't Change Your Bias Intraday

Institutions build positions over time. You should join them.

Find an obvious bias and stick to it. Especially for day trading.

Yes, I know. You will send me charts of big reversals from high to low and low to high. I don't care.

You will never make consistent, big money flip-flopping from long to short and short to long. Even scalpers should pick a side. It's easier and the right thing to do.

If a stock is reversing, let it go. It's perfectly OK to step aside.

Day Trading Rule #6: Be Aggressive When the Market and Change from the Open is on Your Side

This is a RULE, not a “once in a while” or “gut feeling” decision.

You can’t turn a $3,000 day into a $1,000 day. You must have rules in place for when to trade bigger.

I use the word aggressive but it’s really criteria that leads to trade management. You aren’t doing anything different other than paying attention with a purpose.

Aggressive means 3 things:

1. More share size.
2. More positions.
3. Hold longer.

According to William O’Neill in his classic trading book How to Make Money in Stocks, 38% of a stock's move can be attributed to the direction of the general market. You think it makes sense to identify when the market and your stock are in sync?

To add a little more spice to this rule let’s add time frame continuity. Each day your stock has an opening print. The first trade of the day. Start paying attention to the last price relative to the open price. This tells you today’s order flow.

Let’s think it through.

Your game plan says to be a buyer today, yet your stock is trading lower from today’s first trade. This means today, right now, sellers are in charge. Change from the open is negative.

Time to set an alarm. Set it for when the last price is positive from the open. You now have long-term order flow, in sync with today’s order flow. Sit up straight and hold to the close.

Day Trading Rule #7: Stick to Your Draw-down Number

We can't help it. We always believe we can trade our way out of a bad day.

The fact is most traders can't. It might be the market, it might be you. Either way it's difficult to turn around.

Admit it and log off.

Don't throw away valuable capital with stubborn blindness. It's too hard to earn.

I am referring to a draw-down in two situations:

Giving back existing P&L.

Hitting a predetermined stop-loss and trading through it.

I have witnessed (and participated in) epic melt-downs that ruined weeks or months of consistency. One bad trade is all it takes.

Let's end the article on day trading rules with a TRUE story: I once had a trade who I backed in my NYC office. His daily stop-loss was $1,023 (yes he was a Michael Jordan fan). This particular day I was out of the office doing a seminar in Chicago.

His P&L was +$5237 at 11am.

At 4pm his P&L was -$1,100.

When I got back to the office, I asked why he didn't stop at some point and book some profits. He said he was allowed to lose $1,023 so he doesn't see what he did wrong…

He is no longer in the trading business.

TRADE "A+ STOCKS AND ADJUST EXPECTATIONS WITH THE MARKET

Day trade the market or day trade your stock and ignore the market?

What is your game plan current order flow? What is your plan if the order flow changes?

It's bound to happen, the situation with the pandemic is too much for the general market to overcome. In my opinion we are about to collapse in a big way.

But I don't trade my opinion. I trade the tape.

Day Trade for Today, or Know Your History?

Did you learn from 2007-08? What about February of 2020? Are you prepared with strict stop-loss orders? Are you ready to be in cash if you can't find awesome risk/reward scenarios for new long positions?

Most day traders like to be "long." We like to be buyers.

It's easier to understand than short-selling and technically has defined risk (you know where zero is). If this is you, it's time to get prepared.

Great tape readers look for new ideas regardless of existing positions. You should do the same.

Only plan day trades that match your strategy. It's very tough to be profitable with spur of the moment ideas.

Always be assessing probabilities for your next move. Always be building if/then scenarios. Day trading is hard work. The stock market has been kind to investors the last few years. (2016-2020) We aren't investors. It's time to make a trading plan for a bearish tape.

If you never need it, good for you.

The day trading community was littered with wealthy traders who went broke when the stock market turned down in April 2000. I personally witnessed dozens of day trader's freeze while in long positions, waiting for a favor that came in March of 2003.

If you believe the market "always goes up" you are not a student of trading history.

The "stay at home" stocks are in play right now. How would you trade them?

Your best, next move, could be adding to an existing position or it could be initiating your first entry in a tiered structure. This is how hedge funds allocate money.

They never open an entire position at once and neither should you. Not only does this method put tremendous pressure on you (to find the perfect entry), it is simply bad math.

You never want your full position unless a trade has started to move in the intended direction. There are old-school day traders that will tell you to initiate a full position as close to a definitive stop loss position as possible, but those are ideas from a different generation.

The days of a specialist, floor broker or pit trader as the dominant force handling retail orders are gone. The odds of your stop-loss being triggered near a significant number are great. This means you need to plan to enter a day trade in multiple positions.

Relative Strength and Relative Weakness

What do you do if selling pressure starts to overtake the buying? Do you change your plan and start to short-sell? Do you day trade the short-side or continue to look for longs?

The professional who has a clear strategy would say no. You don't change your edge. You continue to do what works for you. To give you an extreme example, I have a friend who is one of the top day traders in NYC. He trades long 95% of the time.

Here is his exact quote; "I'm a buyer. I'm only looking for a place to get long."

Should you be that extreme? Yes and no. Yes, you should focus only on your edge, but no in the sense that if I was your mentor, I would tell you to find another stock to be long.

Which brings me to the core of this lesson. How to find stocks to day trade if the general market is not offering opportunities that are aligned with your strategy.

Great trading happens before the trade.

This means you stack the odds in your favor, then make the day trade. The best traders do this in the direction of the general market. So, plan "A" is to monitor the market every day (even if you are swing trading) and have a strict set of guidelines that tell you when and if, to be aggressive and hold good trades longer.

This also means to monitor which sectors, industries and stocks are not following the market. By doing this, you are setting yourself up for future trades, and gauging the strength or weakness of institutional pressure.

In "trader talk" this is relative strength or relative weakness.

Here is how you apply the concept.

The main pillar in this day trading strategy is the general market. What is the current phase of price action on the longer-term charts?

For a swing trader this means the previous quarter or 3 months. For a day trader it means the last month, week and yesterday.

We are looking for obvious buying order flow in the market and those stocks that are trading in sync with the general market. These are the best day trading scenarios and have high-probability. Any day trades that do not fit this criteria can still be a good trade, but not necessarily a great trade.

Remember you want to allocate money to great ideas. Even the best day trading ideas will not earn money sometimes, but you never want to accept risk on a weak premise.

The next scenario is the one that most day traders miss. On June 10, 2020, the Dow Jones Industrial Average declined 1,808 points. It appears the market is starting to change hands and distribution is taking place.

It's time to make note of stocks that hold sideways or even rally as the market get weak. These stocks are showing relative strength. They are showing institutional buyers who have interest and are supporting the stock.

Next, have in place a strategy to identify when the market has found support, and appears ready to move higher again. If and when the market rallies, your first day trade to consider are the stocks in your relative strength list.

Remember, you don't want to change your strategy if your plan is to be a buyer. Stick to your edge and use relative strength to filter out the best day trading ideas when everyone else is losing their shirt and hoping weak stocks find buyers.

**If you short sell the concept works the same on the opposite side of the market. They key is to identify bearish swing trading trends and then make note of stocks that do not rally.

This is by no means a complete day trading game plan but it should give you ideas to make an outline.

Trading Losses: Connie Consistent Versus Struggling Steve- a Matter of Belief and Track Record

Ever wonder why trading losses don't seem to bother experienced traders as much as new traders?

Think about running another type of online business. If you had a track record of consistent revenue, would it bother you to spend money on marketing?

Of course not. At that moment, you believe you can spend money to make money. You believe you can produce profit.

The trader/entrepreneur believes this, because she has a track record.

New traders don't have this belief, because they don't have the track record yet, so trading losses take on a much bigger meaning for them.

So how does struggling Steve become Connie consistent? With a trading plan. A trading plan is a script. A script for profitable ideas.

Dependable trading revenue is a direct result of having a structure for producing winning trades.

If you're winging it" you don't have a plan. If you are inconsistent, you don't have a plan. If you have a plan and you're inconsistent, my guess is you have more than one strategy.

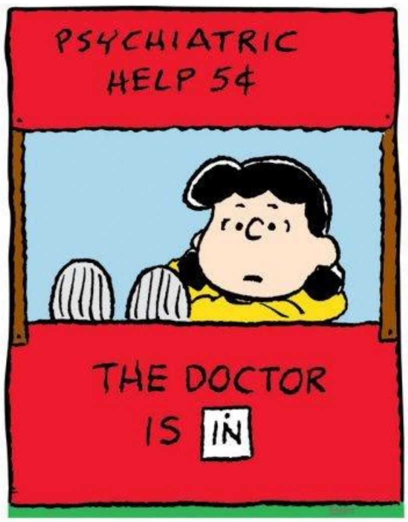
Stick to one strategy, test it, improve it and own it before you move on to multiple strategies.

Before a trader can accept losses flawlessly, they need to believe they can produce profits. Otherwise every loss is a life and death, roller coaster of emotions.

To produce profits, consistent profits, and then big profits, you need an edge, a strategy that gets molded and adjusted into a trading plan that matches your unique goals and resources.

When a trader reaches this stage, trading losses are a business expense. Expected and accepted.

Successful Trading = No Ego



Successful traders understand the importance of taking losses by minimizing them.

When a trade doesn't follow through, I exit my position with as little damage as possible. No ego here. Wrong is wrong!

No trader makes money all the time, and the best traders in the world are successful because they know the importance of accepting and taking trading losses.

If one-third of your trades are winners and one-third are losers, and the remaining third were negligible then perhaps you can see the importance of controlling your losing trades. Taking trading losses are necessary and essential to successful trading.

I know I'm trading well if my biggest winner was three times the size of my biggest loser (3:1 risk/reward)

I have watched some of the best traders in the country trade over the past 23 years, and the common pattern I see with all of them is that they focus on managing their losing (red) positions far more closely than their winning (green) trades.

We are successful and profitable because we TAKE OUR LOSSES when it's time to do so.

Of course, many of you reading this will find a reason to hold onto your losses well past the proper technical exit price. This will inevitably cause you to fail at trading and part of the unfortunate statistical base of losing, non-disciplined traders.

You can do it your way or better yet, the right way. Taking losses is the key to making money.

From this moment forward, you'll do that before you put on a trade so you can put on trades that you are 100% comfortable accepting the risk in exchange for those nice, juicy profits that we're looking to take from the market every day.

Our next steps together are putting these pieces together in real-time for both day trades and swing trades.

You'll be amazed at the new power you'll possess. Control to do nothing and control to hold the winners.

A magical moment happens when you say "I don't see anything to do."

Why is that good? It's because you know what you want and you'll not accept risk on any trade that doesn't justify the reward.

Now it's your turn. Let's make some money together.

See you in the Tape Reading Room!

Pete