Trade Orders

How To Get In, How To Get Out and How To Protect Yourself

By Robert Miner, Dynamic Traders Group

Many new traders have not become familiar with the variety of orders that may be given and which orders are the most appropriate for a particular market condition. Which order is given to the broker depends on the market position and what are your objectives. Experienced traders will also find this review of trade orders helpful. Experienced traders may find there are trade orders to enter or protect a position that they have not used that will be beneficial to meet their trading strategy objective.

Day Orders and Open Orders

A day order is only good for the trading day that it is given. If the order has not been filled by the end of the trading day, it is automatically canceled by the broker. The order does not carry over to the next trading day. An open order remains open until the trader cancels the order. Open orders are also called good till canceled (GTC). A few brokers will not take open orders. If this is the case, get another broker. You do not want your trading strategies to be limited by the broker.

The order number given by the broker for day orders and open orders are usually a different series of numbers so each will be distinguished. My broker gives a three-digit number for a day order and a four-digit number for an open order. With most brokers, if you don't specifically state your order is an open order, he or she will assume it is a day order. Be sure there is no misunderstanding with the broker.

The most important thing to keep in mind about open orders is that they are open or able to be executed until they are canceled. Don't forget about them. This is why it is critical that you are organized with a written order log and you review the order log at the end or beginning of each trading day in order to be aware of any open orders and if you want to maintain them. I have received a fill call from my broker several weeks after placing an open order that I had forgotten about when I didn't keep good order records. You don't want this surprise, especially if the call comes when you are on vacation and you're not there to receive the call! You will learn this lesson when you return from vacation and find you have an open order fill call on your answering machine.

Protective Stop-Loss Order

Trade orders may be used to enter a position and to protect an open position. The only traders who do not have an open protective stop-loss order for any open positions are those traders who are doomed to failure. Under no circumstance should you ever have an open position and not have an open protective stop-loss order. This is an inviolate rule.

Market Order

The market order is the simplest type of order. When it is given, the trade is executed by the pit broker as promptly as possible and at the best price possible after he or she receives the order. Depending on the volatility and liquidity of the market, you may or may not get filled at the price that was being traded when the order was given. The "at the market" order may include a price limit.

Market orders are also known as 'get-me-in-now" or "get-me-out-now" orders.

Stop Orders

A stop order may only be executed if the specified price has been 'touched" by the market. The market must either trade at that price or through that price. If the specified price is touched by the market, it becomes a market order. A buy-stop order is placed above the current market price and a sell-stop order is placed below the current market price. In other words, the stop order is used to get into the market if the market is moving in the anticipated direction. A stop order may be used to either enter a position or as a protective stop-loss order to liquidate an open position.

Bull Market Example To Enter A Trade On A Stop Order: You want to buy if the market advances above a prior swing high which we'll say is at 55.00. You feel that an advance above the swing high confirms the bull trend will continue. You place your order at 55.10, one tick above the swing high. The order would be "buy at 55.10 on a stop." If the market advances and trades to or through 55.10, the buy order would become a market order. You may or may not get filled at the 55.10 price depending on the volatility of the market. In a very liquid market, your fill should be within a few ticks of the stop price. In a fast moving market but illiquid market, your fill will inevitably be several ticks or more above the stop price. Under some conditions in these types of markets, you may want to use include a price limit with the stop order. See price limit orders below.

Stop Loss Order: The stop order is also typically used as a protective stop-loss order. Let's say you are long and feel if the market declines below the previous swing low at 55.00, it would invalidate the long position and you would want to be out of the market. You would place the order 'sell at 54.90 on a stop." If the market declines to 54.90, the sell-stop order becomes a market order.

A protective stop order is often adjusted closer to the market as the market progresses. This is usually accomplished by a cancel-and-replace order. The same order number is kept while the stop price is changed.

Price Limit: The stop order may have a price limit that will prevent the order from being executed at a price that is considered too high or low. The above buy-stop order may have been "buy at 55.10 on a stop, 55.60 limit." The typical time you may want to include a price limit with a open stop-order is when you don't want to enter the trade if the market gaps open far above the stop price. Another circumstance when you may want to use a price limit with a stop order is if you are anticipating a very short-term trade with a small profit objective and it is important to buy within a specific price level. Price limits should never be included with a stop order that is a protective stop-loss order.

In most cases, you will not want to use a price limit with the stop-order. Keep in mind the objective of a stop order. You want to buy or sell when the market is moving in the anticipated direction. If the market is moving so strongly in the anticipated direction that it gaps through the stop price, do you really want to limit the price for entry? In most cases the answer is no. The market has confirmed your outlook and confirmed the trend direction. You want to be in the market.

Stop Close Only (SCO):

The stop-close-only order will be executed if the market trades at the specified price in the last few minutes of trading. The typical use of the SCO order is if the closing price is your signal to want to enter the trade. For example, let's say you believe a bull trend is at or very near then end of the trend and you want to enter the market on a reversal day. In a bull trend, a reversal-day is when the market makes a new high during the day and closes below the prior day's close. Before the day begins, you know what is the prior day's closing price and high. If the market makes a new high during the current day, the first condition for a reversal day has been met. You can then place a stop-close-only order one tick below the prior day's close. If the market trades one tick below the prior day's close in the last minutes of trading, the order becomes a market order.

The SCO order is used to enter a trade whenever a specified closing price is the key to a daily reversal signal. Let's say the market is in a bull trend and has traded into a price zone where you believe the market has a very high probability of making a trend reversal. You want to enter on the close if a reversal day is made. Yesterday's high was 55.00 and close was 54.60. If during today the market trades to 55.10, one tick above yesterday's high, you will place a "54.50 stop-close-only" order to enter a short trade. Depending on the volatility of the market in the closing minutes of trading, you may or may not be filled at 54.50 or lower. You may even be filled a tick or two above the prior day's close, as trading may become frantic in the final minutes.

<u>SCO As A Protective Stop-Loss</u>: The SCO order may be used as the protective stop-loss order for an open position if a closing price at a specific level is the signal to abandon the trade. The big problem with using a SCO order as a protective stop-loss is the market may have a very wide range day and close far beyond a price level when you would have wanted to be out of the market. Stop-close-only orders that are used as a protective stop-loss are often combined with a

straight stop order to prevent this from happening. When the two orders are combined, they become a one-cancels-the-other (OCO) order. If the straight stop order is first elected, the stop-close-only order is canceled.

Let's say you are in a long trade and you determine that you want to abandon the trade if the market closes below 54.60. You want to keep the open long position even if the market trades a few ticks below 54.60 during the day and only want to exit on a close below 54.60. However, you may feel that if the market traded as low as 54.10, you would also want to be out of the trade. You could place the order "sell at 54.50, stop-close-only or sell at 54.10 on a stop, one-cancels-the-other." If the market trades during the day to 54.10, the sell order becomes a market order and the trade is exited. At the same time, the stop-close-only order is canceled. See more about one-cancels-the-other orders below.

I recommend that if you use a stop-close-only order as a protective stop-loss, you always combine it with a straight stop to prevent unacceptable losses in the event of a run-away move against your position during the day.

Or Better Order (OB)

An or-better order instructs the broker to buy or sell at a specified price or better. The or-better order is the most typical type of price-limit order. The or-better order is usually used to buy or sell on a retracement against the trend. Let's say a market has made an advance and you want to enter the market if it makes a 50% retracement, which is at 55.50. You are willing to buy at a price of 55.50 or lower. The order would be "buy at 55.50 or better."

There are two risks that may be unacceptable with an or-better price order. You may be deadly accurate determining the high probability retracement level and the market bounces right off that level. Your order may not get filled if only a few trades were made at or below the or-better price. I strongly suggest that you make the or-better price slightly above what you consider the beginning of the important retracement level. Markets often make a sharp reversal off of the Fib retracements of 38.2%, 50% and 61.8%. If you want to buy or sell at or better than these levels, place the or-better order price slightly above these levels for a buy order or slightly below these levels for a sell order.

A better order to use to buy or sell on a retracement is the market-if-touched (MIT) order. However, some exchanges will not take an MIT order so an or-better order must be used.

If an or-better order is filled during the day when you are not watching the market, how do you immediately protect yourself with a protective stop-loss order? In this case, you must give the protective stop-loss order at the same time you give the or-better order to enter the market. Let's say you have determined that 55.70-55.10 is a retracement support zone. You want to buy if the market declines into this support zone but want to be out of the trade if the market continues to decline to below 55.10, the bottom of the support zone. You would give the broker two orders. The first would be to "buy at 55.80 or better" (one tick above the support zone). The second would be to "sell at 55.00 on a stop" (one tick below the support zone. You would be happy to be long if the market retraced to the support zone but you want out of the trade if the market continues to trade down below the support zone. If you are filled on the 55.80 OB order and the market reverses and begins to rally as anticipated, be sure to cancel-and-replace the 55.00 sell-stop order and bring it closer to the market.

Market If Touched (MIT)

A market-if-touched order to buy is placed below the current market price and a market-if-touched order to sell is placed above the current market price. This is just the opposite of a buy-stop or sell-stop order. If the market trades at or through the MIT price, the order becomes a market order.

MIT orders are usually the best orders to use if you want to buy or sell if a market reaches a retracement zone. Some exchanges do not accept MIT orders. When this is the case, the or-better order is used.

When placing an open MIT order, the position may be protected by also placing an open stop order to protect the position if it is filled as described above with the or-better order.

Stop and Reverse (S&R):

A stop-and-reverse is not an actual order given to the broker. A stop-and-reverse order is given if you desire to reverse the position if the protective stop-loss is elected. The protective stop-loss order is for twice the number of contracts as the open position. If the stop-loss is elected, the position is reversed from long to short or from short to long.

A S&R order is often used when a market is in a relatively narrow trading range and you are not strongly biased for a trend developing in one direction or the other. The market may break out of the trading range and quickly reverse to break out from the opposite extreme of the trading range. You may place a stop-and-reverse order to take advantage of a false breakout followed by a sharp reversal.

In the *Dynamic Trader Weekly Report*, I often recommend a stop-and-reverse order on an inside-day breakout trade-entry strategy. If a trade is entered on the break above the day prior to the inside-day, an S&R is placed one tick below the low of the inside-day. If the S&R is elected, the new protective buy-stop for the new short position is then placed one tick above the high of the day prior to the inside-day. See the *Dynamic Trading* book for more details on the inside-day trade-entry strategy.

The initial stop-and-reverse order protects the initial position. What if the S&R is elected? The new position is open without a protective stop-loss in place. If you are not available to receive a fill-call from the broker when an S&R order is made, you probably should not give an order that will reverse a position. You will be exposed for at least part of the trading day to an open position with no open protective stop-loss. A trader never, ever should have an open position that is not protected by a stop-loss order. If you are paying the premium for a full service (full priced broker), you should be able to give him or her any series of orders to place under specified events. While the broker may not be able to place the order with the exchange, their job is to watch the market and place the order as you have instructed when a certain market event occurs. Just hope the broker is not in the bathroom or making a quick trip out of the office for lunch or to pick up the kids when the event occurs that should trigger the new order to be placed.

One Cancels The Other (OCO)

An OCO order is really two orders given at the same time. If one order is filled, the other order is canceled. One example of an OCO order was given above where a stop-close-only order was given with a straight stop order.

Another example when an OCO order may be useful is when a market is in a narrow trading range and you want to buy a breakout above the trading range or sell a breakout below the trading range. Let's say the trading range is between 55.60 and 54.80. You want to be in the market on a break above 55.60 or below 54.80. You would give the order to "buy at 55.70 on a stop, sell at 54.70 on a stop, one cancels the other." If one order is filled, the other order is canceled.

If you use this type of OCO order, be aware that the position will be unprotected until you place the protective stop-loss order after the trade-entry order is filled.

Keep It Simple

There are other orders that may be given, but those described above are the most typical. Beyond the typical orders, a broker may accept any order that you will give him or her, even if the exchange will not accept the order. You are then relying on the broker to place the contingent order if a certain event unfolds. Usually only full priced (full service) brokers will provide this service. If you want to make atypical orders that the exchanges won't accept and rely on the broker to place them at the appropriate time, you open yourself up to potential mistakes. You have taken your destiny out of your hands by relying on the broker's alertness to properly execute your atypical order. My recommendation is to keep it simple. Use the typical exchange accepted orders.

Before calling the broker with the order, write it down. Be sure it is the exact order you want to accomplish your objective. Read it to the broker and make sure the broker reads the order back to you. Make sure there is no chance for misunderstanding. When the broker has read the order back to you and given you the order number, write the order number down and always repeat it the broker to ensure you and he or she has it correct.

Order Log

Keep some sort of order log so you can quickly and easily review all open positions and open orders. Along with the order given, include the date, time, order number and name of who took the order. I find the best way to track orders is to enter each order on a separate small piece of paper. I have a small file on my desk where the order is placed. One slot for open/unfilled orders and one for filled orders. Each sheet with a filled order also includes the protective stop-loss order for that open order. Every time the protective stop-loss order is adjusted, the new order instructions, date, time and person who takes the order is noted. I know that if I have a slip in one file slot, I have an open/unfilled order. If a slip is in the other slot, I know I have an open position with an open protective stop-loss. If I am traveling with an open order or open protective stop-loss order, I carry the slips with me and don't have to carry an order log notebook.

I've made many mistakes giving orders over the years. The mistakes have always come about because I wasn't organized and didn't have the order clearly written down before calling in the order. The most common mistake is to tell the broker to buy when I meant sell! Don't make this mistake unless you are convinced you live a charmed life!

What Are You Trying To Accomplish?

Whenever you decide to place an order, ask yourself, what are you trying to accomplish with the order? What order is most appropriate for the trading strategy you want to use? Use the order that will best accomplish your objective.

What If You Are Not Available To Receive The Fill?

Most traders have day jobs and are not sitting in front of a screen during the trading day. If your open order is filled, how will the open position immediately be protected? I teach in *Dynamic Trading* that before a trade is considered, the trader must identify what market action will invalidate the trade. In other words, a specific position is only considered within the context of the protective stop-loss. Never, ever have an open position without an open protective stop-loss in place. Typically, the protective stop-loss order is given when the fill for a new position is called to you by the broker. What if you are not able to receive the fill-call because you are at you day job? How will the trade position be protected?

I have described above how some protective stop-loss orders may be given at the same time the order to initiate a trade position is given. If you are not able to receive the fill-call and not able to give a protective stop loss order at the same time the initial trade-entry order is give or when the fill-call is received, do not give the order.