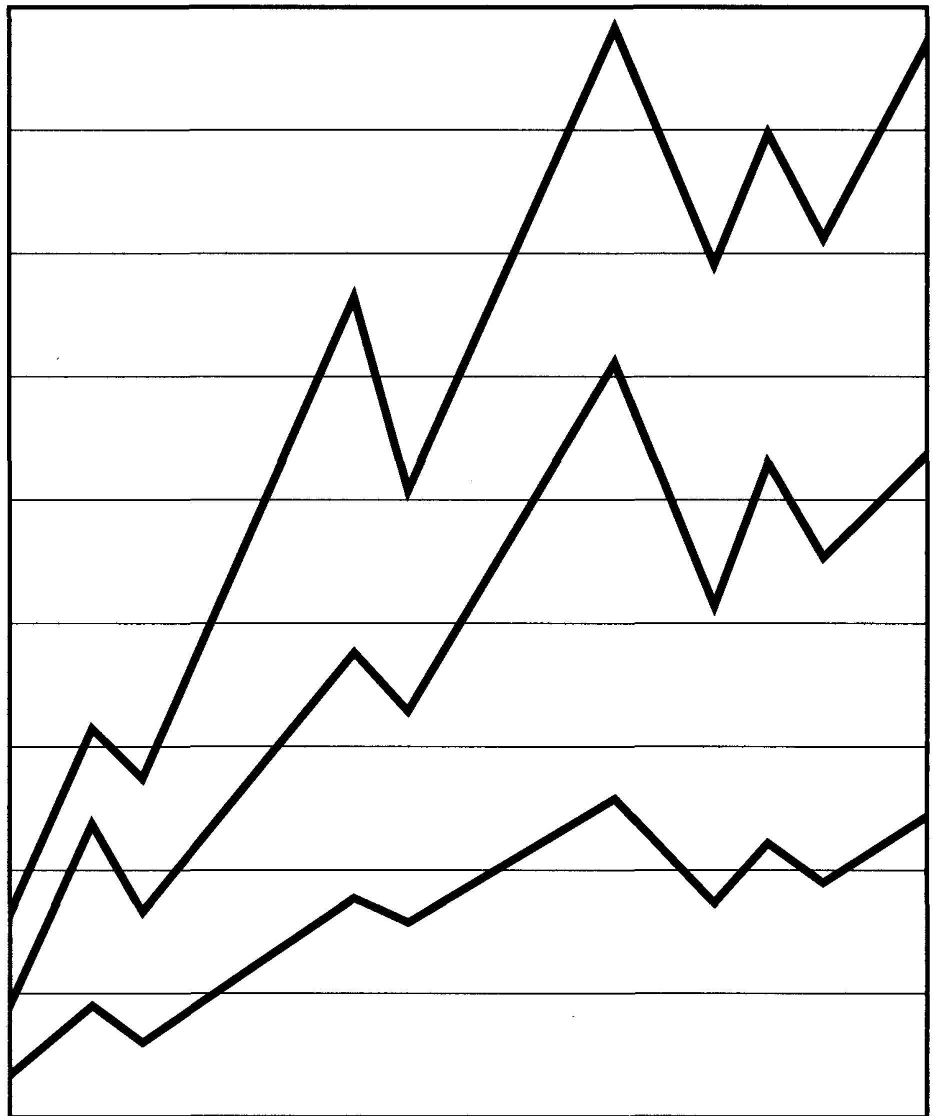
Trader's Notebook 1

by R. E. McMaster, Jr.



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TRADER'S NOTEBOOK
#1

by
R.E. McMASTER, JR.

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FOREWORD

It is indeed ironic that in an arena such as the commodities markets, where success is heavily dependent upon objectivity in decision making, that there is so much froth. The half-truths, mysticism, witchcraft, jealously guarded "Holy Grails", and rampant subjectivity that pervades the markets is a tribute to the omnipresent ruling emotion of man. Emotion, money, and security are all linked in the same harness, and are sparked by the pursuit of the illusion of "any easy way", if not "THE easy way".

It is hoped that this work will shed a ray of reality on this fascinating market arena, and in so doing, convince a few that the road to meaningful success is marked by persistent learning and personal growth.

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PART I
PSYCHOLOGICAL SECTION

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A CHANGE IN ORIENTATION

It is an observation that men who are continuously successful in their field are in love with their work, stimulated by it, and are psychologically suited to it. One wonders, then, since men do best what they like doing, would it not be a better approach for schools to develop the individual, emphasize talents and differences, rather than mass produce academic drones? We'll chase this rabbit another time.

Another attribute of success is a willingness to change and grow with new information and wisdom. The best type of change comes slowly with added information fed into the system until all the pieces fit together. At that point, the change is easy. It is a natural step.

The Commodity Comments in THE REAPER are about to make a major change. It has come naturally. It is a change that has been building since this letter began. It is in your best interest. From now on, the emphasis in the Commodity Comments will be long-term position trades. Yes, there will be short-term and intermediate-term recommendations for those so inclined. But the emphasis will definitely be on the long run. Here's why.

Reviewing my total trading history in the commodity markets, far and away, I have been most successful with trades that I have watched develop over time. They come together slowly and naturally, and they went a long way, in both time and price. The odds of making money in commodities also supports the longer-term perspective.

Commodities are a zero sum game. For every winner there is a loser. But there is a catch. The commodity broker always wins, always. Thus, there is less money for the winners, right off the bat. As soon as a trader enters the market, he is an immediate loser due to commission cost.

This can and will eat the short-term trader alive. Short-term traders generate between 60% and 100% of their account balances in commissions yearly. Now, just what does this mean? It means in a $10,000 commodity account, one may pay out, in hard dollars, between $6000 and $10,000 a year. Let's put it another way. In a $10,000 account, a short-term commodity trader must earn between $6000 and $10,000 a year above his original $10,000 account before he pays himself any profits. How easy is it to earn 60-100% a year, just to break even? Not very.

Next, let's say the trader is looking for a 10¢ ($500) short-term profit on a silver trade. He tries to buy silver at $4.60 with the intent to sell out at $4.70. He puts his order in the market. He is filled at $4.61. Oh, oh, there goes one cent. Price rises to $4.70. He exits the trade, filled at $4.69. Oh, my, there goes another cent. Plus, he pays a $50 commission. Therefore, his net profit is $350., not $500. He paid $50 commission, (12.5% of gross profit) and lost $100 in and out on the execution. This is not unusual. What if his stop loss was $4.50, and he had been wrong and was stopped out. His loss could be $650. Enter market at $4.61, out at $4.49, plus commission cost. Thus, a 50%-50% shot is really a $350 W vs $650 L, a poor risk reward. A trader must be right better than 50% of the time if he is to show a net profit trading short-term. But there is a kicker. It is called emotion, mental wear and tear.

Have you noticed there is a rhythm, a grace, an ease with which the most successful athlete moves in his speciality? The snow skier is a good example. He flows down the hill. Short-term trading is a rag-tag affair — highly emotional and unrelaxed. It does not flow. Over a period of time, only gifted hunch traders and locals on the floor win as short-term traders.

Intermediate-term trading is not much better. If one plans to trade short or intermediate-term, do it on a computer. Remember, however, that most computer systems are based on trending markets, and markets usually trend only ¼ to ⅓ of a year. Thus, one must be lucky when one enters the market based on a computer program. Get in after a long losing period. One might make 15%-75% a year, if lucky.

Long-term traders maximize their odds. If one pulls $4000 out of soybeans, what is a $50 commission? Patience is a must. Expect to miss some major moves. Risk is greater. The stop loss is farther from the market. A good long-term trader will only be right one of three trades. But one good win, coupled with correct money management, more than makes up for the losses. Plus, it is not nearly as hectic. The broker won't like it, but one can, for once, with a little luck, profit. I believe this is the best way to trade for most folks. The exceptions are: (1) Geniuses who have a "feel" for the market, or (2) Men who are lucky, or (3) The likes of W.D. Gann, who probably came as close as anyone at understanding the mathematical keys of the universe as they apply to markets.

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A MOST DAMAGING MISCONCEPTION

Most Americans are a product of the public education system. Most believe that their instruction in economics has been of the free market variety. What a surprise to learn upon studying the Austrian school of economics (Von Mises — Human Action) that the public school system teaches "socialized economics," whose operating assumptions are quite different.

For example, "self interest" is taught as being in the same family as selfishness. This morning 11 typical Americans (high school and college graduates) were asked about "self interest" in the economic sense, and they too put it in the selfishness "family tree." Interesting, yet dangerous. Acting in one's self interest can only be damaged by concomitant selfishness according to free market principles.

A consumer's needs can be viewed as biological, safety, social, ego, and self-fulfillment (Maslow's hierarchy). In the free market, the businessman who meets the needs of the consumer best will profit. The businessman serves the public . . . service! The businessman gives in order to receive. Success is built upon satisfaction of needs of others, successful giving! Being others oriented benefits self. Think back. The individuals who have meant the most are those who have given of themselves. The successful salesman heeds the needs of his clients. The successful doctor listens to his patient's complaints. The successful parent fulfills the needs of his children, not his own, if the relationship is to endure.

David Ricardo's Law of Cooperation and Association showed clearly the benefits of human interaction and sharing of tasks among equally unequal men under voluntary contract, free of coercion, where each benefited. One of the best illustrations of this is found in Frederick Nymeyer's Minimal Religion. Adam Smith saw the advantage of division of labor in his Wealth of Nations. Meaning in life comes from association with others.

WHAT'S THE POINT? SELF INTEREST IS BEST SERVED BY GIVING, NOT BY BEING SELFISH. It doesn't matter if one is giving his labor, individually contracting, selling, producing goods, or being a parent. There is more to the statement, "It is more blessed to give than receive," than meets the eye.

Does the principle apply to market traders? Of course, Self interest is best served by the sharing of ideas, promoting mutual growth. Sadly, most traders are about the most independent, selfish, suspicious, untrusting, and secretive rascals around. And they deserve their miserable lot in life. They are contrary to natural law.

Let's look at it in a slightly different light. In business management, if one division in a chain of production selfishly works only for itself (suboptimization), the entire system is negatively affected. Synergy — the concept of 1 + 1 = 3 states that the whole is greater than the sum of its parts. Or, stated differently, benefits are maximized by cooperation — each person giving. One of the best examples of synergy in action was the NBA championship victory of the Portland Trailblazers over the Philadelphia 76'ers — the coordinated whole (Portland) was greater than the individually superior parts (Philadelphia).

When does the principle of service as the best means to self interest break down? (1) When there is a one-time shot, no continuity of relationship, and (2) When communications between members of society are broken down, so that word of poor service cannot be spread.

Example: The Gyp strip at carnivals.

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THE LAW OF EXCESS

Watching the 1978 NCAA Basketball playoffs brought to mind a principle which this trader had temporarily forgotten. It is called, for lack of anything better, The Law of Excess. Basically, the Law of Excess states that when all is going well, in one's favor, resources tend to become utilized inefficiently to the point that the epitome of performance slips down to the point that new energy and effort is required to again reach peak performance in excess of the amount of energy required to maintain the level of peak performance. Boy, was that a mouthful. Some examples are as follows.

In basketball, a team will play precision ball, let's say, for the first half, and build up a 15-point lead. It seems they are invincible. Then comes the second half, and the seemingly invincible team relaxes mentally, takes poor shots, & passes the ball carelessly with the result being an increase in turnovers until the point that momentum shifts to the losing team, who close the point spread, and again make a game out of it. How many times have we seen this in sports?

And, in business, a company will sweep the field against its competitors, sit atop the heap, and then, in the twinkling of an eye, excess will set in. A new corporate headquarters is built with excessive interior finish. Expensive stationery is ordered. Too many company cars are available. The staff becomes excessive. Competitors pick up accounts, and finally, the result is that earnings drop and percentage of market share declines. The company is forced to retrench, regroup, and again struggle to regain its superiority.

The government is exactly the same way. Federal programs become excessive as does spending, personnel, and fringe benefits. But government has no competition. It has a monopoly (in effect) so there are no competitors who can challenge it (initially) and so cynicism, graft, corruption, as well as more excess sets in until the point when the ultimate in regulators come in, in the form of revolution, riots, or invasion from other governments which are superior and more efficient.

On a biological level, the human body functions the same way. When one exercises regularly and is in good shape, less sleep is required. The mind is more alert, less food is eaten, and health is improved. Contrarily, when one's body is not running efficiently, and one becomes overweight, one tends to sleep more, eat more, gain additional weight, and develop health problems along with a sluggish mentality.

Machines operate under the same Law of Excess. An automobile that is properly tuned with new "points and plugs" will run efficiently, use less gas, get more miles to the gallon. By contrast, an automobile that is poorly maintained will guzzle excessive gasoline. It then requires increased effort, money, and attention to bring it back to the peak of efficiency.

In the markets, inefficient buyers will enter the markets when all seems well, when prices have been continuously rising. They will be joined by those who are pyramiding their position, in an attempt to increase profits. Now, when there is an excess of buyers, smart and efficient sellers will come in and take profits and go short. The inevitable reaction will take place and the inefficient purchasers will be washed out of the market with losses.

Along the same line, two or three times a year the markets allow a trader to make a lot of money in a hurry. The markets of March 1978 are a case in point. After the fast money-making opportunities, after the account equities have increased, then traders, instead of sitting back and withdrawing from the markets and again waiting for optimum opportunities, do exactly the opposite. They become careless in their trade selection, overtrade, and generally squander their hard earned funds which were accumulated during the good markets. They let their discipline and their efficient trading system go to pot, just like the basketball team with a good lead, just like the business which sits atop the heap, just like the individual who decides it is time to quit exercising, just like the motorist who refuses to have his regularly scheduled tune-up, just like the government which becomes oppressively obese and scandalously spends its constituents' funds. And, the trader, just like each of the above, must work harder to regain the efficiency that brought him the earnings in the first place.

Oh, how sad it all is, this recurring cycle which adheres to the Law of Excess. The Law can be and has been broken by a few. But it requires awareness, vigilance, and discipline. It is much easier to maintain a level of peak performance than to lose it and attempt to regain it.

The John Wooden's of this world have learned to be constant watchdogs, to stand apart from the sleeping and indolent pack, and as a result, they earn their just reward. They have beaten one of the laws of human nature, the Law of Excess.

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PRICE: ABSTRACT TO ABSOLUTE

Price is the abstract transformed into the concrete. A buyer has an idea of value (price), a seller has an idea of value (price). When they consummate a transaction, price becomes an absolute at that point of time for that transaction. The next second, price again becomes a variable, an unresolved psychological/mental concept in the mind of the buyer and seller. Each has an idea of "value or worth." There is no natural law of price. Price requires the meeting of the minds, which is a psychological phenomenon.

Logically then, it is important to recognize in markets the existence of a mass mind — moved by mass psychology which establishes price. Given that discipline is individual in nature, and rare at that, we should expect the mass mind to be undisciplined, emotional in nature, and easily manipulated, but at the same time possessed of immense power to move markets due to its size alone. It is a tidal wave of emotion. Thus, it is most important to gauge the mass psychology of the market, for the mass will move the market regardless of the logic or irrationality of price direction.

We cannot fight the mass mind. We must flow with it — surf on the wave, so to speak. We know, however, in the back of our mind, while we ride with the wave, emotion is in control. When the emotion plays out, as it always does, it will be at some extreme. Then the adjustment will come. The trick for the trader is to be able to judge the exhaustion of the emotional wave and profit from it. The mass emotional mind will be wrong at the extremes, when it appears to be most powerful.

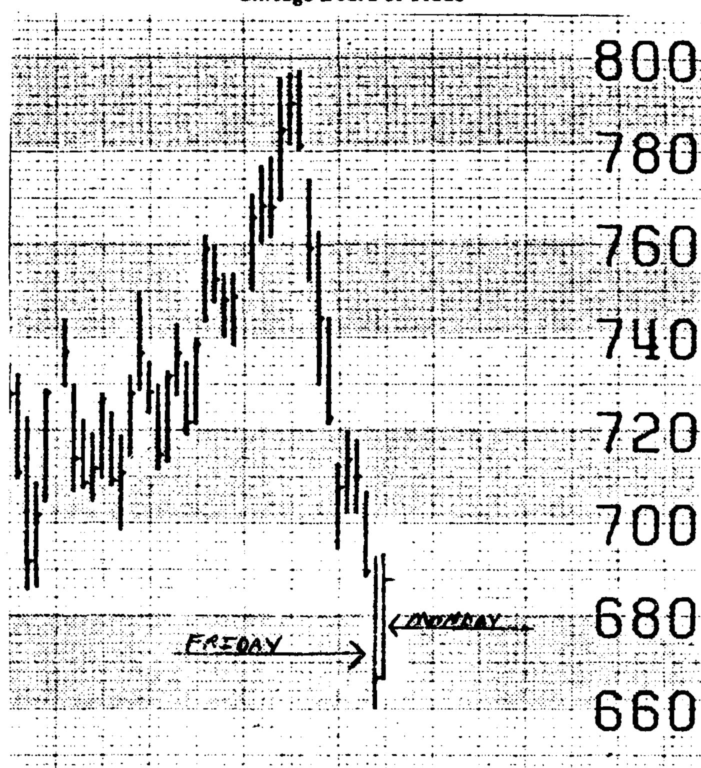
Let's summarize:

1.) The establishment of price in markets is essentially a psychological phenomenon dictated by the emotional whims of the mass mind of the market.
2.) The mass mind is the most powerful force in the market, and, as such, must be discerned and accommodated.
3.) The emotional mass mind moves to excesses, is wrong at the extremes, at its apex of power.

Technically, analysts attempt to ascertain these extremes using such indicators as contrary opinion and overbought/oversold oscillators. For now, let's think through the psychology of a decline as we witnessed on Friday, June 17, 1977, in November Soybeans.

During the first week in June, November Soybeans went to a high of 797, formed essentially a triple top and then collapsed. The psychology of the market was bullish — rain was needed, subsoil moisture was insufficient — the trend was up! When the market cracked downward, it was met by disbelief. The emotion was — a correction was due! Confidence/optimism was still apparent. As prices declined further (720), concern set in. Optimism, however, was not yet replaced by fear. The open interest had not yet declined. Thus, new buyers were replacing old buyers. Commercial users, watching the price decline, were content to "sit on their hands" and wait for lower prices. The second week of the decline (June 13th) fear set in. Lower exports than expected. (The news, as usual, FOLLOWS the price action.) Rain in the Bean Belt. Pessimism takes over. The 700 support level gives way. More bad news, this time Brazil. Finally on Monday — panic! Commercials sell out in large numbers. The news hits the floor. The locals get short, disillusioned speculators sell out — they have lived with this decline for two weeks! New short sellers enter the market — the Bear market is going through the floor. Finally, there is liquidation of the

SOYBEANS
NOVEMBER
Chicago Board of Trade



open interest — a clue — Sellers are taking profits while Buyers are exhausted out of the market. It is emotionally burdening to carry a position over the weekend. On Friday, new buyers won't come in. Old longs will liquidate. Locals liquidate. No buyers. Sell, Sell, Sell!

Now comes Monday, Who is left to sell? There are no stops under the market, the market has been lower three days in a row and two weeks in a row. The locals have no incentive to press the short side. The

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commercials sold out on Friday. The speculators and commission houses, who were long panicked (fear carried to extreme) and liquidated on Friday, and commercial buyers sat on the sidelines. ONLY A FEW INTREPID BUYERS, STANDING ALONE, SAW THE OPPORTUNITY AND BOUGHT. Most buyers decided to wait until Monday. Why think about the trade over the weekend? Shorts sat on their profits.

In short, the market became sold out! That created a vacuum. The market could go no lower. There were no more sellers. A market bottoms when there are no more sellers. The emotional tide had run out, when it seemed most powerful. There was nowhere for the market to go but up.

(Editor's Note: This was written after the close Friday, June 17th, before the rally.)

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MARKET OBJECTIVITY

The market is objective. The market is amoral. It just exists. To put it in the vernacular, it just doesn't give a damn, about you, me, your mother-in-law, my sick kids, our hang over, or Uncle Dan's lumbago. It is THE Laissez Faire market in the U.S. Those who are right are rewarded with profits. Those who are wrong are rendered losses-objectively, unemotionally. (Makes ya mad doesn't it?) Frustrating! Really frustrating! Who do we blame when we lose? Oh, for a market confined in a punching bag! Unfortunately, there is the mirror. Look in it. There stands the defeated foe, whipped by the entity that is truly a total reflection of life itself.

The market has no character flaws. It has no character. But count on the market to bring forth every flaw in our character. See, there it is — our impatience on display under floodlights! WE MUST CHANGE! We must flow with the market. We get nowhere fighting it. Many successful men have come to the market and left in defeat. Why? They refused or were unable to change, to grow, to leave behind their culture, group norms, parental influence, pride, fear, impatience, greed. They, in their other successful endeavors, did not have to first deal with their own weaknesses. The market requires one to deal with one's flaws first. It will find every chink in our armour, our protective shield, until we become flexible, open and change.

Is there a progression, a sequence or checklist of growth? Yes. First, frustration. One's "shell" is challenged by the market. The market won't give. One loses, is angry, frustrated.

Second, realization of the need to change. A little light comes through. Now, one doesn't have to "get even" with the cocoa market for that last loss. Maybe there are some things to be learned.

Third, one becomes receptive to change. Principles from other disciplines become evident in the market. From each trade, lessons become learned. One looks carefully at one's hangups, make-up. Inductive and deductive processes kick into gear. The losses still hurt, though, with emotional hangover.

Fourth, one embraces change, growth. Growth is no longer painful. At all costs, learn, grow, change. Ruthlessly, excitedly root out the flaws, the faults in both systems and self. Separate the wheat from the chaff. Now, moving from break even to profits. One learns from the profits, as well as the losses. One can even reverse positions intraday if necessary with no emotional turmoil. Tension is eased. One can become relaxed, patient, content. Meaningful change has taken place, slowly, as it must, to be meaningful. Profits become a means to an end. The end — personal growth. Being right or wrong is met with equal neutrality. Pride is minimal. There are men in this fourth category alive today who simply take just what they need from the market, nothing more.

This fourth area is never completely mastered. But in the fourth arena comes the joy of life itself. For on this fourth battleground real freedom is felt and then embraced. The shackles of "other-imposed" norms, faulty upbringing, and misconceptions are tossed aside, easily, continually. Freedom under natural and divine law and consistency with self are realized with objectivity as a result of emotion being subordinate to mentality. One rejoices with the works of great minds of ages past. Now a full vessel, the capacity to give, to share, is natural, unforced. Peace is natural with all peoples with intelligent discrimination. In this fourth arena comes the personalization of the phrase, "You shall know the truth, and the truth shall set you free."

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MANIPULATION IN THE MARKETS?

The question continually arises among commodity traders, "Are the commodity markets manipulated?" Irascible old Ted Warren in Southern California, who has made a fortune in commodities over the years, works with the BASIC assumption that the markets are manipulated. Lefevre's classic work, Reminiscences of a Stock Operator, contains blow by blow accounts of market manipulation. The December 1, 1977 issue of International Moneyline discusses the "box" theory — a theory which holds that markets are manipulated — "actions deliberately designed to make money, or prevent other people from making money." There are primary power groups which exercise such an influence over the markets, that they can manipulate them for their own self interest, or so the "box theory" goes.

While this writer does not have any final answers, it can be safely stated that large moneyed interests do attempt to manipulate the commodities, and have/are able to do so in the short-run, from time to time. Government actions have manipulated the gold and interest rate markets. The large commercials in the industry, such as the grain giants, can move the markets. However, the financial trouble in Cook Industries, as well as Simplot in the potato market, points to the dangers of attempted manipulation. The legendary activity of the Dallas gunslingers, the Hunt Brothers, has left their brand on the gold and silver markets.

Undoubtedly, the markets have and can be manipulated short-run, by big money, or by leaking false news (USDA reports?). However, the bigger the market in dollar volume, number of participants, and world-wide interest, the less effect any attempted manipulation will have. Therefore, to avoid potential manipulation, trade only the markets with large open interest. Avoid thin markets — eggs, plywood, cocoa, and the like.

Next, technical analysis usually allows for manipulation in the sense that the movements made by the manipulators can be picked up by the technician. Walt Bressert (Hal Cycles) and I picked up Simplot's potato shenanigans very early. (A word to the wise. Short-term technical analysis can be whip-sawed to death by manipulation. Longer term analysis? Not likely.)

It is helpful to think of the markets as being manipulated, particularly from the perspective that the market price action is geared to manipulating one's emotion — fear and greed. Traders buy when they should be selling, and vice versa, based upon the emotion of the moment and/or the herd instinct.

One of the grand masters of technical analysis in this country is Edson Gould. After many years of study, he concluded that the action of the mass, the crowd psychology, is the most important consideration in investment analysis in markets. The thundering herd always takes price movements to extremes of optimism and pessimism. A commodity market millionaire stated in COMMODITIES magazine that it was most important to figure out which side of the market the public was on. The public will be right for a while in a trending market, but will lose its shirt at important market turns.

So, in summary, whether markets are manipulated or not really doesn't matter if one assumes that the market will always work to separate the masses from their money.

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ME, . . . AND FEAR!

It has been established that the average human being utilizes 4% — 10% of his mental capacity. Psychologists have shown that the majority of thinking that people do (some 90%) is about themselves when they are not concentrating on some specific activity such as solving a mathematical problem. The useless activity called "worry" stemming from inaction, and focusing on "me" has been well documented and shown to be a cause of many physical ills. In light of this, the November 1977 issue of "Psychology Today" gives some insight that should be useful to both a commodity trader and any individual in day to day activity, business or otherwise.

In the Newsline article "The Happy Laborers and the Sad Professionals", Charles Weaver, using partial correlation (a statistical technique), discovered that laborers were found to be far more satisfied with their jobs than professional and technical workers when the effects of occupational prestige (pride) were removed. Pride, which is best manifested through occupational prestige, is a "me" factor, and results in such things as fear of changing occupations, fear of failure, fear of loss of face, and generally inhibits productivity.

Another article in the same issue of "Psychology Today" — "Reflections on the Dawn of Consciousness" stated, "In consciousness, we always see ourselves as the center of a story." Thus the "we," in this case, translated from "me," is again a focal point.

Now we get down to the nitty-gritty of how the focus on "me" results in fear and lack of growth and utilization of maximum capacities. W. Timothy Gallwey and Robert Kriegel, in the article "Fear of Skiing" noted that there was a "Self One" and a "Self Two."

"You can hear 'Self One' chattering within your head, criticizing, judging, worrying, and pontificating about things it doesn't really understand. It distorts perceptions and blocks the expression of the natural potential of the body, which we call "Self Two." It is interesting to note that Fritz Perls, the father of Gestalt Therapy, observed that human beings are members of the only species that possess the capability to interfere with its own growth."

Therefore, it should come as no surprise that most of us perform well below our potential.

Gallwey and Kriegel also had two categories of fear, "Fear One" and "Fear Two."

". . . 'Fear One,' distorts our perceptions and tends to paralyze us and decrease our confidence. The other kind, which we call 'Fear Two,' heightens our perceptions, and gives us energy to perform beyond our normal capabilities."

"Fear Two" is a natural process that prepare the body for peak performance, coexists with courage, and often is present in athletes, race car drivers, soldiers, etc. Under "Fear Two," the body prepares for increased activity by increasing the flow of adrenalin. Breathing is stimulated, the chest expands, the throat relaxes, pulse and blood pressure increases, volume of blood sent to the muscles increases, the liver manufactures glucose which effectively fuels the tissues of the body. The pupils of the eye dilate, which sharpens vision.

"Fear One," on the other hand, inhibits our ability to perform at our potential peak, magnifies whatever dangers are perceived.

The authors continue, ". . . so many of us have been conditioned for so long to measure our self-worth according to how we perform . . . that loss of self-esteem . . . seems a matter of great importance."

"The key to overcoming fear of failure is breaking one's attachment to results. Whenever we convince ourselves that results are all that count, we fall into anxiety that paradoxically limits our ability to achieve results . . ."

Another fear, the fear of letting go, of achieving beyond one's expectations, is another vulnerability. When an individual breaks through to a new level of performance he is often so absorbed with the task that his conscious mind is put effectively into neutral. When he begins doubting, thinking, fearing, self-instructing, analyzing, then he is liable to return to low levels of performance. The authors note that the quieting of the mind, peace of mind, helps performance considerably.

What does all this have to do with commodities? First of all, fear of failure, fear of loss, often prevent many traders from initiating positions that, in hindsight, would have been profitable. This fear is usually associated with going against the crowd's opinion, of being alone, or of being wrong — much like the fear of failure described above. Secondly, it should be noted that these authors, who are ski experts, discovered that the quieting of the mind is important to successful skiing. This is also the case in successful commodity trading. As mentioned in earlier REAPERS, where was discussed the importance of long-term trading, one can best analyze a trade over a considerable period of time and then quietly reflect on it and then, in a very relaxed manner, enter the market. It is a building of thought processes to a climax where the trade is entered.

Finally, results are a by-product of doing an activity correctly, in other words, results take care of themselves. Relating self-worth and fear of failure to how we perform can only detract from focusing on the activity, and isolating the "me."

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PAIN

It has long been a personal belief that the background of military training — the discipline and instantaneous decision making of flying, plus the personal limit testing and emotional turmoil of land and water survival schools — have been excellent preparation for trading the commodity markets. However, the concept is much more clearly stated in the phrase, "Train for Pain."

Most folks will go to extremes to avoid pain, either emotional or physical pain. It feels good to eat. So, overeating is not uncommon. It hurts to diet. Has anyone ever commented that dieting is fun? A five degree change in temperature upward in an office environment causes irritability and a reduction in job performance. The emotional pain of a loss in a trade can lead to the unwillingness to cut the loss short. The physical exhaustion and mental anxiety of a move puts marriages on the rocks.

And yet we know that pain and testing is a real part of life that all will experience. How much better is it to change our mental attitude, recognize and accept the fact that one will have to deal with pain as a normal part of life? This change in mental attitude, from a fear based avoidance stance, to a positive problem solving approach is healthy. Accept pain. Expect pain. It is part of life. Accept losses. Expect losses. Don't expect too much from the market. One can deal with it.

Now, to minimize the effects of pain, one must train. The athlete — boxer, football player, mountain climber, tennis buff — all expect to confront pain in his respective arena. His performance is enhanced and pain minimized by mental discipline and physical training.

By remaining mentally open to new ideas, by making the conscious decision to change and grow, by reading the wisdom of the ages and applying it to one's own life, by focusing on the task and/or others rather than self, by expecting losses in the normal course of things in the market, one can effectively fight pain. As the market is a microcosm of life, it stands to reason that the benefits of training for pain mentally and physically is doubled for the commodity trader.

A trader who had made in excess of one million dollars in the commodity markets stated in an interview with COMMODITIES magazine that he had to be at 90% efficiency just to break even in the markets. As the connection between mental and physical training is now well documented, how much more evidence does one need to realize the importance of "training for pain."

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AVERSION TO RISK

Men seek security. Maslow, in his hierarchy of needs, noted man's basic need, following the satisfaction of his biological needs, is his need for safety or security. It is a well established psychological principle that people resist change. Change threatens status quo security.

As civilizations age, they become more security conscious (social security?). The freedom and tolerance that characterized the early stages of the culture are now replaced by established sanctions, regimentation and bureaucracy — agents of security.

(Thus, there is a conflict between freedom and security. Personal security carried to the extreme can be found in a hospital or in solitary confinement in a prison. Obviously, freedom in either of these situations is nonexistent.)

The entrepreneur has a very high security need. The risk that the entrepreneur takes is due to a deep felt need to control his own environment, to feel important, to feel secure. Wealth, or the drive for wealth, is often the result of a very high security need.

Just what does all of the above have to do with the commodities market? Each of us needs to objectively evaluate our own security needs, for the greater our need for security, the greater aversion we will have to risk. A high degree of aversion to risk is deadly in the commodity markets and leads to loss of capital.

Look at the overall business investment (speculation) community. The rewards, financially, are reaped by the successful assumers of risk. The entrepreneur who successfully speculates on the needs of the public in the future reaps maximum profits. The most highly paid members of corporations are those who make decisions that involve risk in environments of uncertainty. All business is involved in markets, and thus all businesses face risk. Unfortunately, most businessmen have a very poor understanding of the cyclical nature of markets and the associated psychological swings of optimism and pessimism.

EXAMPLE: The banking community, ironically, has probably the poorest understanding of how markets function. The bankers traditionally want to make loans when all systems are "go," when all risk is removed. The banker has a high aversion to risk. When cattle prices are high, and feeders are operating on very profitable margins, the newspapers are filled with articles on what a "killing" cattlemen are making. New clients are applying for loans for cattle operations daily. Then, the banker wants to lend to present and prospective cattlemen. The banker assumes that the risk is minimal. No so!

When a maximum amount of information is available so that a decision seems "easy," real risk is present. The banker is operating under the illusion of no risk. Thus our friendly banker, with his high aversion to risk, will be faced with some troublesome loans down the road in the future as the market responds to oversupply. When he feels most comfortable loaning to cattlemen is when he should be most on guard. The banker is not a risk taker, and, in keeping with the principle of risk assumption, he will not be rewarded for his efforts.

It is an easy step to take this example and apply it to the commodity markets. A trader who has a high aversion to risk will wait until a trend has been in effect for a considerable length of time, until all systems (moving averages, point and figure, etc.), are confirming the direction of the trend. He will wait until the news is confirmed, for purposes of example, that soybeans are in a bull market and supply is running far under demand. He will have no negatives left in his decision making process. All questions will be answered. Then he will enter the market. Then he will be wrong and lose money. Why? Real risk has been assumed by others at lower price levels who did not have the high aversion to risk, the high need for security. Those who purchased at lower prices acted contrary to their emotions. Obviously, the opposite is the case during a bear market. The trader with high aversion to risk will sell the market short when all the information is in and no risk exists in his mind, when, in reality, risk is maximized. Each of us needs to look at our life, our method of operating on a day to day basis, and objectively evaluate our desire for security, our degree of risk aversion. The simple truth of the matter is, regardless of how well we manage our capital or how good our technical or fundamental trading system is, if we have a high aversion to risk we will consistently lose money in the commodities market.

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ON BEING WRONG

"I hate being wrong. It just kills me inside. But what is worse, I hate admitting I am wrong." How many of us have felt this way at some point in our life, or still feel this way. It is difficult to admit that one is wrong. The ego/pride is hurt. It is easier to forget it and hope others will forget it too. Where is that hole to crawl in for a while and let some time pass?

The market doesn't forget. Our trading statements don't forget. Our tax return doesn't forget. The record is there. Being wrong is a part of life, of being imperfect, of not enjoying the attribute of omniscience. The greatest hindrance to admitting error is pride. And pride is a killer in life, the market, and in relationships. The salve of "I'm sorry, I was wrong," has saved many a marriage, business and personal relationship.

In my college years, I had a professor who was trained in Cuba as a communist cell block recruiter for black cell blocks in Houston, Texas whose purpose was to prepare for the next U.S. Revolution. She had developed "the debater's technique of admitting error" to a fine art. In attacking the American system, she was often caught in warped statements, and sometimes outright lies. But they never did her any damage. None whatsoever. WHY? Because she never argued. She simply admitted her error, and thanked the correcting student for helping her grow and clear up her own thinking. She turned an enemy into a friend by her humility and appealing, in some cases, to his "fine mind" (his pride). She also used the technique of saying, "Good point, we'll come back to that later." We never did.

We never win when we argue with the market. It is as much use as fighting the tide. It leads to our loss, financial or physical, maybe both. In the market a break-even trade is a win; a no-lose situation is a win. A win is a win. Hey! That is three out of three. We win! (Yes, a loss is still a loss.)

The point is this. None of us will always know the future exactly. It is an unknown. We can only guess in sophisticated ways what it holds. So, like the situations in life, we should say to ourselves, in the market, we will be wrong. Period. Accept it and expect it. It is a law of the market and life. And when we admit our error, and learn all we can from it, we grow, and lessen the chance of having it happen again.

There is an old saying that people make their own misery. That is probably 90% correct. Therefore, the logical thing for each of us to do is to first put the blame entirely on ourselves whenever anything goes wrong in any area of life — the market, our business and our personal relationships. It is amazing how much we can learn out of every situation if we first assume that every problem is our own fault. If a problem is our fault, we can move to solve it. If it is partially our fault, we can solve our end of it and be more understanding and gracious toward the errors of others. If a problem is not our fault at all, by looking to ourselves first, we have a "reflective basis" to solve the problem in a thoughtful manner.

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A BIBLE THUMPING TRADER

Several months past, I had the pleasure of visiting with Larry Williams in his home in Kalispell, Montana. The topic of discussion was his tentative decision to run for Senator of the State of Montana. Now, I'll have to hand it to Larry. He has always been one to spot an opportunity. But this trader had other fish to fry, and the idea of running a political campaign left me cold. Frankly, it was my advice to Larry to wait about four years, until things became more unsettled and the home folks were suffering a bit, angry, and ready for a real change. It could be dangerous to be identified as a politician in this era, prior to the Great Awakening. All that happened that evening is water under the bridge, and now Larry Williams has a bustling campaign underway.

As the conversation that evening shifted to the markets, as it inevitably does when two market addicts get together, I again asked Larry who the best commodity trader he had ever known was. He again quickly answered (as he had done four years previously) that the best trader he had ever known was a Bible thumping, Bible studying, commodity trader who lived in Nevada. Nevada, I would believe. Bible thumping in Nevada? Well, if Billy Graham can do it . . .

In any case, Larry's quick comments again set my mind in motion. Why would a trader be such an avid student of the Bible in order to improve his trading? The central theme of the Bible is salvation for mankind through Jesus Christ. What does that have to do with trading?

For months now that question has intrigued me. Here are some of my observations:

1. Besides being a religious book, the Bible is a book of principles, rules for living. The market requires one to adhere to rules if one is to survive and profit.

2. The Bible speaks of the nature of man — his lusts, passions, failings, greed, and fear. As such it is a book on psychology. Well, well. An article several years ago in Commodities entitled, "The Market Millionaires" quotes a market millionaire who stated that the person best equipped to trade the markets would be a psychiatrist, or, stated differently, one who had a firm grasp on the nature of man and all his weaknesses.

This writer has long held that one of the primary reasons that speculators fail in the market is that the markets REQUIRE one to deal with oneself first, BEFORE dealing with the markets. Money is so tied to a sense of security that it brings out all the frailties in man. The market will find every chink in a man's armour. A successful trader must learn how to adequately deal with himself — self-discipline, self-control before he can succeed in the markets. This is not true in other occupations. A salesman, an attorney, a doctor, a banker, a construction worker, an engineer — men can be successful at any and all of these professions and have a personal life which is in shambles.

This trader has long held that, with rare exception, men make their own misery. Principles of life for successful and abundant living are as consistently in tune with the nature of man as trading principles are in harmony with year after year of market action. The Chalcedon Foundation in Vallecito, California has done the best job this trader has ever seen in explaining and "nailing down" in a logical manner correct rules for living.

3. It struck me as curious how God dealt with his saints. Jonah, Moses, and David, for example, had to wait their time for God to work through his plan for their life. At the risk of generalizing, the church saints were put through tremendous testing, were battered around, left in despair, humbled, and finally upon submission to a higher power, it was then that their character was rebuilt. They became the two-edged sword through whom God could work out his purpose. In their state of humility (When I am weak, then am I strong), they could listen, learn, respond, change, and be patient until the time was right for them to move into action.

It struck me that this same exact process is what is necessary for one to be successful in the markets! Was this the Nevada trader's secret? Yes, yes, I think so! The market is nothing more than the result of the thinking of the minds of many men — disciplined, undisciplined, arrogant, humble, rich, poor, righteous, self-righteous, and reprobate men. The market is a mental melting pot. Just like with the church saints, traders lose when they initially come to the markets. They do not know the rules. New traders are tested, battered around, left in despair, humbled and THEN THEY EITHER CHANGE AND GROW (SUBMIT), OR LOSE AND LEAVE THE MARKETS. Mankind has never been known for its humility. It is no surprise so many are devastated by the markets.

With the change, however, comes a rebuilding of character, painful growth, but then, as time passes, growth is embraced as the trader starts to see the markets and the world as it really is, through the objective training by the markets. The trader loses the puffery of his own importance, becomes an enlightened child of the universe, able to respond objectively to life's situations. He becomes patient and waits for the markets to tell him when to move. He IDENTIFIES the few points the market gives for real moneymaking opportunities, and he is content to take a chunk out of the middle (no greed) year after year and wind up wealthy. So did the church saints wait for guidance. They became open, they listened, and they responded when the Lord led and the time

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was right. Our ability to respond correctly to the markets is dependent upon our make-up, our character. The Nevada trader found the mother lode!!!

The greatest blessing in my life are my children. As many of you know, my book, CYCLES OF WAR, was dedicated to them. I tell my son, "Look around you. See all these people on this earth. Read about all the folks who have lived down through the ages. Study their history. Their concerns, hopes, fears, desires, and passions are no different than ours. Human nature has not changed. Man is the same animal he has always been. Are you any different? No! Certainly our form of government may be different, our climate better, and our technology more advanced, but we are still fragile men. Now my son, that being so, doesn't it make sense to say to yourself, 'Since I am little or no different than those who went before me, I should, in light of the fact that men make their own misery, study the wisdom of ages past, learn from wise men who have gone before, in order to not repeat the mistakes which brought them misery and suffering. Would not such an approach enrich my life and make it more productive, abundant, and happy?' " I tell my son too, "If anything happens to me, and I am unable to fulfill my role as a father to you, I have drawn up a list of books for you to read which are deposited in the safe deposit box. Read them! They will guide you through this life. And there are two things in particular I want you to learn. Learn the principles of the Bible and the principles of the market. Apply what you learn from the Bible to the market. If you can learn to do that, and are successful, I shall rest peacefully. For then I shall know that you have all the equipment necessary to deal with any and all of life's challenges. If you remember nothing else, remember this . . ."

I have the great pleasure of dropping off in Las Vegas occasionally. Being the trader I am, I cannot resist the challenge of the casinos (in moderation, of course). Without fail, when I am there, the desire to seek out the Nevada trader arises — to sit down and discuss with him the tremendous insights that he has gained over the years. But those discussions are not for this life. And with the comfort of that reality, I whisper a prayer, and let the dice go, and watch them roll, and roll, and roll . . .

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URGENT OR IMPORTANT?

One of the outstanding management consultants in the nation is Robert D. Weber of Marietta, Georgia. At a lengthy luncheon one day, Mr. Weber discussed what was to him the most critical principle that must be adhered to by management if management is to be both effective and efficient. The principle is, "If it is urgent, it is never important. If it is important, it is never urgent."

This catchy principle, Mr. Weber noted, applies to management of affairs in all aspects of life — business, family, personal organization, and relationships with others. Let's look at a few examples: (1) A production supervisor who spends his time keeping his desk neatly arranged and answering telephone messages is doing things that are urgent, at least to him. But they are not important. He should be supervising the men involved in "on line" production. (2) A grandmother spends her time remodeling her home while her granddaughter is in the hospital having an operation. She is doing the urgent thing, but not the important thing. If the granddaughter dies, the foolishness of the priority system will become evident. (3) The top business executive, who is responsible for leading the company in the future, spends his time putting out administrative fires. He is doing what is urgent, but not what is important. What is important is planning for the future, being creative. (4) The parent who works late at the office every night building a successful career soon discovers that his children have grown up. He has lost their precious youth which he could have shared. He did what was urgent, but not what was important. (5) The Congress spends five months a year away from its work, tending to small matters while the legislative function of the country is assimilated by the executive branch, negating the historical check and balance system. The Congress did what was urgent but not what was important.

Jim Mckeever in MISL #143 did an article similar to this entitled, "The TYRANNY of the URGENT", in which he stated, "The urgent things in life absorb all of our time and keep us from doing the important things. The urgent things in life always have a deadline while the important things never do."

The application of this principal is direct to market traders. When a trade is urgent, when it seems as though the market is about to run away and leave one behind, when a trader feels great anxiety, tension, and must be in the market, then he should avoid the trade because it is not important. In fact, it will probably lead to a loss. Contrarily, the trades that are important are the trades that a trader can watch build and unfold. They are the ones that give him time to get on board and are the result of careful planning and patience. It seems as though the market gives the trader too much opportunity to enter this potentially profitable trade. So, if there is an urgency to trade, re-examine. The urgency may be a trap door to a loss. If the trade is important, it should be one that has developed relatively slowly (excluding hunch trades) and one that will flow quite naturally when the time is right.

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PATIENCE

Patience is as vital to a commodity trader as the black bag is to a country doctor. Even if a trader has a good trading method, meshed with an adequate money management system, lack of patience can ruin him in the market. Americans, by nature, are impatient. It is our tendency to get something done now, never later. It is the tradition of the "go get 'em" attitude. Also, the concept of man controlling his own destiny lends itself to impatience. If I control my future, why wait, let's "get on with it."

This attitude is contrary to the philosophical base of cycles, and the idea of everything in its own time. Finally, living in an inflationary world only complicates matters. Inflation is like drugs to an addict or chemical fertilizer to a plant. It speeds up the metabolic rate tremendously. How can a trader be patient when the monetary environment says, GO! GO!

But the history of successful traders is a history of patience. Trading commodities is like guerrilla warfare. A trader must wait to pick his own time and place in order to have a chance of winning. If he does not, he loses. One cannot cross swords on an equal basis with the market. The market has far more strength, wisdom, and years of experience at saber rattling. Plus, the market has an ace in the hole; it's called leverage.

A trader must be right on his timing, and right the first time, or he is a loser. It makes little difference if one is right in the long run if one has lost all his risk capital prior to the move. That is why pure fundamentalists have so much trouble in the commodity markets.

So then, what is the best way to view the markets? First of all, it is important to view all the markets objectively. Each of them either moves up, down or sideways. It is important not to fall in love with gold, or silver, or pork bellies. That can only intensify emotional involvement which will lead to losses if not just a horrible trading disadvantage. What is important is to look for opportunity to profit, for that is the name of the game.

Perhaps it is helpful to look at the markets from the perspective of a tourist who is in Monte Carlo and trying to decide which bus to catch. There he is, Mr. Tourist, standing on the corner. Every 30 seconds a new and exciting tour bus comes by. Which one to catch? "Gosh, I want to catch them all!" By so doing he runs himself ragged.

Better to have a plan, watch the markets, wait, and BE CONTENT TO CATCH AN OCCASIONAL MOVE IN ANY COMMODITY. NO ONE CAN CATCH THEM ALL, OR CALL THEM ALL, OR WIN IN THEM ALL . . . NO ONE! The market is endless, just like the tide. There are many good surfing waves day in and day out at the "Pipeline" in Hawaii. The very best surfer waits; he picks his day and his wave. He recognizes his own limitations and that he is no match for the ocean's boundless energy. He is patient, humble, and he profits.

The long history of successful traders is a history of missing many potentially profitable moves totally. So what! The lesson has been learned that "each dog has his own day." The chance will come. It cannot be forced.

It is wiser to buy a market at a higher price when one can pick his entry point and stop loss and know what he is in for, than to "buy blind" at a lower price and be in limbo. Buying blind is a sure road to eventual ruin.

Impatience, due to pride, envy, greed, or fear is a financial killer too. It is the playground of the foolish. And finally, it is important to recognize patience in the old market adage, "When in doubt, stay out." (Capital conservation)

NOTES

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PRIDE OF OPINION

One of the most invaluable habits to be developed in commodity trading is the ability to think contrary to one's position. For example, let's say after consideration of the fundamental and technical factors influencing soybeans, a trader buys soybeans. At this point the average trader becomes defensive of his position. He looks for reasons to support his previous conclusions — buying beans. His mind is closed to input. Far better that the trader says to himself, "What would have to happen for me to be wrong? What would it take to neutralize my previous evaluation? At what price level will I close out this position, admit I am wrong?" These questions are just as important as, "Where do I add to my position?" — for they plant the seeds of flexibility.

The mental attitude here is key. The ability to think contrary to one's position requires an openmindedness, a willingness to change, the flexibility to alter one's opinion quickly. Stated another way, it means admitting one is wrong, having no pride of opinion. Pride of opinion is ruinous in commodity trading as it is in life. In commodity trading, it can lead to large losses as well as to missing profitable moves. In life, it means smallness, no growth, rigidity. It's roots lie in insecurity, further evidenced by hostility toward those of differing opinion. Whether in investments, politics, religion, economics, commodities, friends, or family, those who claim to have all the answers are dangerous leaders.

In the investment arena, the environment is constantly changing. New input always. A good trader will form new conclusions based on the evidence, and many times admit "I don't know," or "I was wrong." It is important to become comfortable with the humanness of being wrong. A great help here is David Seabury's The Art of Selfishness. His comments on "No ego satisfaction" and "Never compromise self" are must reading.

One caveat. Changing one's mind based upon input from others requires discrimination, discerning evaluation of the motivation as well as the intelligence and expertise of the opinion giver or writer.

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CUTTING ONE'S LOSSES SHORT
(In the market and life)

Every commodity trader who has ever lived has heard that the old market adage, "Cut Your Losses Short" is the key to success in the commodity markets (along with a few thousand other old "saws"). Well, so what? For purposes here, we'll assume it is true. But one would not be far wrong venturing that the interpretations of that proverb are as numerous as there are traders.

It is axiomatic in the commodity markets that one's first goal is to survive, to not be wiped out. Then, one can worry about winning. So, consistent with preserving capital, one must cut one's losses short, take small losses, if one is to survive. The trick is how to do this without being endlessly whipsawed in the market with the result being that it is the commodity broker who gets rich.

Cutting losses short is keyed to timing of entry into the market. As this writer sees it, there are only three safe times to enter the market when one can safely cut his losses short without the likelihood of being whipsawed.

(1) The market is coiled like a spring, ready to explode. Just prior to the explosion, or during the explosion, one can safely place a stop on the other side of the launching pad because the probabilities are small that one will be stopped out, and if so, the loss will be small.

(2) If the market is on bottom and trading slowing in small ranges with relatively no trading interest, then one can enter and put a stop "X" dollars away from the market and wait. Of course, this means one's patience will be tested. It also means that capital will not be available for other upcoming trades, But, the ability to cut losses short is there.

(3) A third approach is to buy a heavily oversold market that is in an uptrend or hitting support, or sell a heavily overbought market that is in a downtrend or bumping its head against heavy overhead resistance. Here a stop can be placed on the other side of the support or resistance, as the case may be, or "X" dollars away from the market. The dollar risk is usually small.

Notice that the principle of cutting losses short implies heavy probabilities that the market will move in one's favor shortly (timing). So, maximizing the principle of cutting losses short requires solid judgment, a trading plan, and the expectations that prices will move in one's favor.

Otherwise, cutting one's losses short is an invitation to getting endlessly whipsawed and eventually wiped out.

These prime opportunities do not exist very often. That is why patience is required. Those traders who wait until a trend is clearly established, or buy on the breakout, with a stop placed the other side of the trading range or under some distant low are assuming huge risks, dollar wise. And good long-term traders are only right one of three trades.

(Sure, the short term trader may hit 75-80% of his trades, but this type of activity is usually confined to "Johnny on the spot" day traders and floor traders. The short-term trader just has more entry points and expects less in profits from the market.)

In life, as in investing, one should condition oneself to cut one's losses short. That means constantly attempting to correct one's faults and improve on one's weaknesses. It also means realizing the importance of listening, learning, and being sensitive to input. It means never rationalizing any difficult, unpleasant, or unprofitable situation or relationship, but rather, dealing with it head on — facing the music so to speak, and getting on with life.

When one enters the market it is imperative that one have a plan for exit (stop loss). Staying with a losing position, hoping it will come back with the leverage working against the trade is the road to financial suicide. In life, in business, in the family, with friends, the same principle applies. Cut the losses short. Face the music.

There are tactful ways to discuss difficult subjects. One may wonder how many cases of cancer are the result of staying with, tolerating unnecessary and unpleasant situations needlessly. It is mental slavery.

Why is it that the important things in life go unsaid, undiscussed? Listen to conversations among friends, business associates, and family. How many of them are really meaningful? Remember how good it feels when one "clears the air." Think how much easier it would have been to clear the air earlier. The longer one lets losses ride, the harder it is to cut them off.

Situations which illustrate the point are: 1. Stop smoking. 2. Failure to admit error. 3. Holding a grudge. 4. Not speaking one's mind over a group decision. 5. Letting a bad loan ride (New York Banks). 6. Letting a conflict simmer.

It is much easier all around to cut a loss short than it is to let one ride.

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WHEN IN DOUBT, STAY OUT!

Even the most novice trader has had some market savant tell him, "When in doubt about a trade, stay out of it." The young trader gobbles down this advice as he would a fresh batch of Grandma's homemade cookies and goes on his way never pausing to reflect on exactly how this gem of wisdom is to be applied.

All trades, all entries into the market, are shrouded by a certain amount of doubt. When all factors are known, and a trade seems easy, and the news confirms, and the public is "wild" over a trade, stay away. The market is being set up for a correction. The expensive and valuable Chase formula, which is used primarily in stock trading, basically identifies all these "knowns" and then goes contrary to all the confirmations.

So, it would seem that if one is to avoid a trade which is wallowing in good news, one should take a trade where there is doubt. Not necessarily! "When in doubt, stay out" refers to a situation when a trader has no inkling of where the market is headed. He can flip a coin and look at contradictory evidence with no clear-cut direction. A random gambling situation is not for speculators. In this type of situation, "When in doubt, stay out."

Does this mean that when one is in a trade, and doubt enters the mind, one should exit the trade? Not usually. The market will dance with spiked toes over a trader's emotion. If one enters the market with a solid plan and stop loss procedure, more times than not, one is better served by sticking with the position, particularly near the beginning of a trade. Only as a trade progresses, and the evidence changes, is one best advised to make adjustments.

This writer finds the best trades are those which, while they do not contain the element of doubt as above discussed, do instead contain an element of fear. This fear usually stems from acting contrary to the prevailing opinion. Being human, by nature a gregarious beast, this is always difficult.

One final comment on, "When in doubt, stay out." This adage applies to all other businesses and areas of life.

Also, never assume something when the information is available. It is unprofessional, and intellectually lazy. It is incredible — the number of people who will assume this or that fact, rather than check it out, who will act on the opinion or action of another rather than investigate. What a lousy basis for decisions in life. These folks are operating in an arena of doubt and error. Avoid this folly. The mere refusal to assume something when the information is available will thrust one far ahead of the thundering herd which kicks up so much needless dust.

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TIME'S ROAD

The following is taken from Brad Steiger's A ROAD-MAP OF TIME (Prentice Hall, 1975). It deserves pondering, for it is true.

"Speculation is carnivorous in the truest sense of the word. The spider that eats a fly, the cat that eats a bird, the Stone Age man who eats the flesh of another man — one and all are eating meat to get the energy that the meat contains. Money is another form of energy. It cannot be swallowed . . . but the 'money paper' can be taken to a bank and there exchanged for currency which will buy many a dinner."

"One of the essentials of speculation is that what one man gains, some other man must lose. The accounts always balance just this way. When one man becomes rich, another man, or more usually a group of men, must become poor. As might be supposed, this scheme of things does not make a successful speculator a much beloved man. In fact, the speculator is cordially hated, with not a little bit of envy and jealousy mixed in . . . Every man jack of the crowds on Wall Street and La Salle Street would strip his fellows of their last dimes if only he could."

"The Street is filled with men who keep 'charts,' financial records of what has happened, and one and all try to predict the future. It is enough to be thrown out of some brokers' offices to so much as take a chart out of the pocket. Beneath the surface contempt for charts and chart players, there is a deep fear of charts."

"They say on the Street that of the people who come there, 98 percent go broke, 1 percent breaks even, and 1 percent makes money. Most novices at trading do not last long. No one willfully robs them: they cheat themselves. Professionals seldom outrightly lie to the novices, but they fill the air with half-truths — which in trading are often as bad as downright lies and harder to detect."

"No sooner does a man start trading than psychological laws go to work to alter his mind. A loss right at the start is often the best thing that can happen, for a thumping loss may knock the inner conceit into a cocked hat and thus save the man. To win opens the floodgates of conceit, and in place of the usual gamut of emotions — love, charity, idealism, kindness, fondness — there in time grow to be only two, fear and greed."

"When trading, thoughts of women, love, home, are positively poisonous; and they will cause losses. The successful trader keeps thoughts in mental compartments where they cannot hurt him; and after a time, they wither. The successful trader gets to be a true miser. Unless fear and greed are rampant in his soul, he will never be successful at winning other men's money."

At the 1978 Hawaiian Investment and Economic Conference, an astute subscriber asked me how I "squared" Steiger's comments with my own philosophy. He was referring to the last paragraph of the "Notebook" which is as follows:

"When trading, thoughts of women, love, home, are positively poisonous; and they will cause losses. The successful trader keeps thoughts in mental compartments where they cannot hurt him; and after a time, they wither. The successful trader gets to be a true miser. Unless fear and greed are rampant in his soul, he will never be successful at winning other men's money."

It is quite interesting that this particular section of the "Notebook" would be brought to my attention, for Steiger's words have been nagging and haunting me since I presented his piece. Some personal reflections will (I hope) clarify your own thinking in this area.

First of all, Steiger's words put me in tremendous conflict because I think he is essentially correct. When one is trading, one MUST exclude thoughts of all else from one's mind. If one does not, one will most probably lose. At least two years ago, I made it a policy to never trade if there was the least little thing bothering me. As a result, I found myself, and still find myself, out of the market personally a great deal, missing good moves, because I am distracted, or otherwise preoccupied. Sometimes, it seems as if one must literally sell one's soul to the market if one is to maximize profits. Problems at home with sick children, other business ventures, lack of sleep, too much work, and temporary dislocations from routine operation can drive one crazy when one is trying to trade the markets.

One of the mixed blessings of the market is that it teaches one to keep thoughts in mental compartments where they cannot be of harm. The blessing side of this picture is that one learns, and must learn, if one is to survive — to see life, situations, and circumstances objectively. One must flow in harmony with the market if one is to succeed, and the market is coldly objective, COLDLY OBJECTIVE! One literally bleeds out all the hang-ups, prejudices, subjectivity, and EMOTION as the price to be paid in order to succeed. A huge amount of scar tissue is built up, shielding one's emotion from one's perspective of reality. And it hurts. It is contrary to human nature, and sometimes, one will wonder if it is worth the price. Why? Because, as Steiger puts it, "they wither." One literally dies inside. One subscriber said to me in Hawaii, "The reason I like your writings is because they conform to the Chinese adage which states that a wise man has died many times." Now, I had never heard that before. And I consider myself always a student in search of wisdom, knowledge, and understanding — first and foremost, which is in and of itself a hindrance to maximum success in the

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markets. But, I can say this. I identify with that statement, about dying inside. There are times, in my painful history, as I am sure there are in yours, when we felt that the "pain" could not become any worse. But we recovered. However, when one is in the market as a critical part of life, the dying process continues. Stated differently, the change is constant and relentless. The market seems to demand total submission and humility, which are at least two of the qualities we all share in common after we take our last breath.

One can and does become able to turn one's emotions on and off like a stop watch, particularly when the human emotion of HOPE dies. Then one can see things as they are, and accept things as they come, coldly, in an inhuman way. Now, I know all this is harsh, but it is important, and I know so from bouncing these thoughts off of several of you.

Back to the blessing. By isolating one's emotion, one has enhanced capacity to let them loose and appreciate the important things in life to an enhanced extent if one is so inclined. The emotion is subordinated to the intellect, which means it is controlled. After all, is not the emotion the appreciator of the soul, which gives it a responsive and feminine quality? The danger and trap into which many old successful traders fall is the one where the heart is hardened for all time, and true inhumanity sets in, which brings us to Steiger's last point.

I know what Steiger is stating when he says, "Unless fear and greed are rampant in his soul, he will never be successful at winning other men's money." Men like these are the most successful in the markets, and in other fields as well, but they can be tyrants to work for. Steiger here is referring to an all consuming greed, a total, personal, mental, and emotional involvement with making money, to the exclusion of all else. Please, do not confuse this type of greed with the game-winning desire of the typical emotional investor. The type of greed Steiger is talking about is a killer's game, the type you find among the most professional of poker players. You know the type. It seems nothing can move them, and, in reality, little or nothing can.

In conclusion, what we have looked at here are the requirements (a better phrase might be total commitment) if one is to maximize profits. The price of selling one's soul comes high in exchange for the greatest of financial reward in the speculative markets where there is a loser for every winner. Remember too, that what has been discussed here is not true for the most part in free enterprise, where the essence of good business is where both parties to a transaction benefit and profit, hopefully for the good of society.

My personal conclusion? I'll trade off the total commitment to the markets for some of the "BEST THINGS IN LIFE ARE FREE" items. Now, I know that means, that all things being equal, I shall not be as successful as I know I can be financially, unless I'm lucky. Or, unless the work I've done with the weather is correct, in which case, the protein complexes in the next 6 years will make us fabulously wealthy.

NOTES

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TIMING IS EVERYTHING

"It's Better to Be Lucky than Good" is usually the sibling phrase of, "He was just lucky" — from the parent named Sour Grapes.

The American work ethic states, "Work hard, and you will succeed." OK? Industrial psychologists, as well as estate planners have noticed the large number of "bungling" individuals who have made a great deal of money. They have also found there is a whole unwritten story of how many have lost the fortunes they made. Is there something to, "It's Better to Be Lucky than Good?" Is "Work hard, and you will succeed," a myth? Yes, to the first question. Yes and no, to the second. It all depends upon timing! Timing in life is everything, as it is in the market.

Being at the right place at the right time, fulfilling an economic need consistent with the flow of the economic need tide is handsomely rewarded. True, it generally takes hard work to be successful even if one is with the tide. The principle is consistent with competition in a free market. But, to beat one's head against the wall, working hard against the tide, is often an exercise in frustration. Just ask the mountain land salesmen in Colorado who, in 1971, made $10,000 a week-end, and in 1974-75, worked hard and starved to death. Or, the gold stock millionaires of '73 and '74 who worked the mines in '76 and '77. The year (time) made a real difference in income.

The reason fortunes are lost is men fail to realize that good timing, not their own brilliance, is a major factor in success.

The application is direct to the markets. Timing is everything. The tide is the trend! It is relatively easy to make money trading with the trend. It is hard work to make money fighting a fast moving trend, up or down. This reciprocal principle of life/markets is both important and humbling.

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CYCLES

Cycles, when properly understood, are shunned by the academic establishment. The doctrine of the educational establishment is humanism — man having the power/ability to totally control and rule his own destiny, a law unto himself, so to speak.

Cycles are deterministic, the anti-thesis of humanism. Cycles say, in effect, the efforts of man, in the end (and on the way), are predestined. The event will occur to fit the cycle. Cycle says thumbs up — "thumbs up." Cycle says thumbs down — "thumbs down," as it were.

For purposes of this discussion, cycles in the natural order are absolute — those cycles not involving man. The laws of chemistry, the theorems of geometry, the law of gravity, the laws of thermodynamics, etc., work consistently with absolute reliability. Some of the principles of this realm (science) apply to men, but not in an absolute sense. For example, as the ancients say, nature hates a vacuum. Thus, molecules expand to fill a vacuum — a law from physics. The human application is "The job to be done fills the amount of time allowed for it" — Parkinson's Law. But here's the kicker. The vacuum example has absolute reliability. Parkinson's Law does not apply to all human beings, albeit sadly to most. Why?

Men have free will, volitional choice. That is why cycles, as applied to human action, are probabilistic, subject to interpretation. (There are reliable guidelines for inciting a riot.)

The word "generalities" might be applicable here, too. Just as principles are gleaned from past human action by historians for future predictability, and, as Spengler astutely observed, civilizations cycle, so too are there cycles in shorter time spans that apply to human action.

One familiar example is found in the commodities markets. There are cycles in various commodities. But, following the above reasoning, cycles contract, expand, and vanish and thus are subject to interpretation! Matters are complicated in the markets by the fact that many different cycles affect (simultaneously) the commodity.

Cycles thus remain a useful trading tool if one does not take them as an infallible tool.

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TRADING ON HUNCHES

The novice to the most seasoned professional has, upon occasion, experienced the almost overwhelming desire to make some particular trade just because it is "right." In the vernacular stolen from the financial supporter of many televised sports events, "When it's right, you know it."

What about the hunch in trading, the inclination to make a trade when one can't put his finger specifically on the logic behind it? Where does this stroke of "genius" come from?

Basically, it wells up from the subconscious mind, the subordinate mental storehouse/computer that has a perfect memory. The hunch is the conclusion synthesized from all the data entered into the subconscious concerning commodity trading. As the subconscious works, it eliminates the irrelevant factors and forces into consciousness the logically correct conclusion.

Most traders, upon careful questioning, express anguish about correct hunches they have had but refused to follow. In fact, most traders lament that their hunches are almost always right. If so, why didn't they "follow their noses"? FEAR! Fear causes uncertainty, and makes the trader discount the hunch. Once the hunch is questioned, the conscious mind is again in charge and the salt has lost its savor.

Well, then, should one always trade on his hunches? Are there any guidelines so that one does not confuse a hunch with a forced opinion? Fortunately, yes. Successful Speculation noted the characteristics of the trader who was successful trading on hunches. The hunch trader had an immense mental storehouse of information on trading commodities from which to draw. In short, he had paid his dues. He was calm, conservative, reticent, and self-contained. He neither sought nor gave advice. He was a true professional.

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HOW TO SURVIVE A SPASTIC ECONOMY

I just finished reading David E. Rhoad's book "How to Survive a Spastic Economy." I highly recommend it for any investor who seriously wants to make an attempt to understand what is happening in the financial markets today. Rhoads points out clearly that all investments today are pure speculation. He lays down some principles of speculation under the following headings: (1) Know what you are doing. (2) 90% of the time you don't know what is happening. (3) Know where your profits come from. (4) Big winners make big losers. (5) Sometimes bulls make money in the market, sometimes bears do, but pigs always lose. (6) You will go broke trying to call a market turn. (7) Most of the big pots in poker come in the last hour of the play. (8) Keep good current records. (9) You can't really tell how good you are until you have been through at least one entire business or market cycle. (10) Don't trust anybody. His comments under these particular headings are must reading.

Likewise, his economic overview on the monetary climate in what he calls "Book I" is quite excellent. For hard core analysts, the meat of the book starts with Chapter 8, page 91, "Checking the Economic Weather." From there until the conclusion of the book, Rhoads gives guidelines on how one can judge what markets will do based upon the Federal Reserve's monetary moves. Having personally utilized much of what Rhoads discusses for some time, I find his analysis quite thorough. Those of you not familiar with Federal Reserve Bank of St. Louis' publications will have a real eye opening experience.

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LARRY WILLIAMS: A PERSPECTIVE

It's Tuesday, August 30, 1977, 3:45 p.m. A stimulating 2½ hour lunch has just been concluded with Larry Williams. Larry is probably the most famous/infamous individual in commodities today. After considerable high exposure, writing his own commodity advisory letter, selling the notorious Trident system, and his subsequent battles with the CFTC over his registration as a Commodity Trading Advisor, Larry has withdrawn to Montana, his home. His life today is much simpler. He says he doesn't know what to do with all his free time. Yet, he is edgy and nervous, ironic for a man with an abundance of free time. His eyes reflect the terrible psychic pain that he has endured over the past four years. His restlessness perhaps is the residual manifestation of his pace of life in years past. In any case, one would suspect that Larry Williams' best years are ahead of him. At 35, he is running 15 miles and more a week, and plans to run in a 26-mile marathon in Hawaii. He is into health foods, handball, back packing, and enjoying life. His understanding of the markets now is far superior to the days of How I Made One Million Dollars Last Year . . . Trading Commodities.

Gone is the "look at me, I'm just 32" attitude. It has been replaced with a simplistic approach to the markets that is almost alarming, particularly when one considers the tremendous mathematical research this man has done.

On the markets. Amazing! Separately, we have made almost the exact discoveries in technical analysis, arrived at independently no less. The philosophical base is sound as it must be, for ideas precede action.

Larry notes philosophically that American culture focuses upon being right or wrong, as opposed to making money in the markets which is the real measure of success. He is now content with probabilities, comfortable with being wrong in his trading. He loves to be wrong. He just reverses position. He sticks to his system. He notes that Americans love to deviate, and that is detrimental, if not deadly, in trading. He recognizes the overwhelming challenge in the markets is the ability to deal with mental pain from losses. He thus trades more or less mechanically, insulating himself. He only follows 6 markets, and only holds two positions at a time. He says that is all he can handle mentally.

Larry hopes to be remembered for his work in money management. He states that any "fair" technical system can make money if the money management techniques are correct. One senses growing wisdom in Larry Williams.

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PART II
TECHNICAL SECTION

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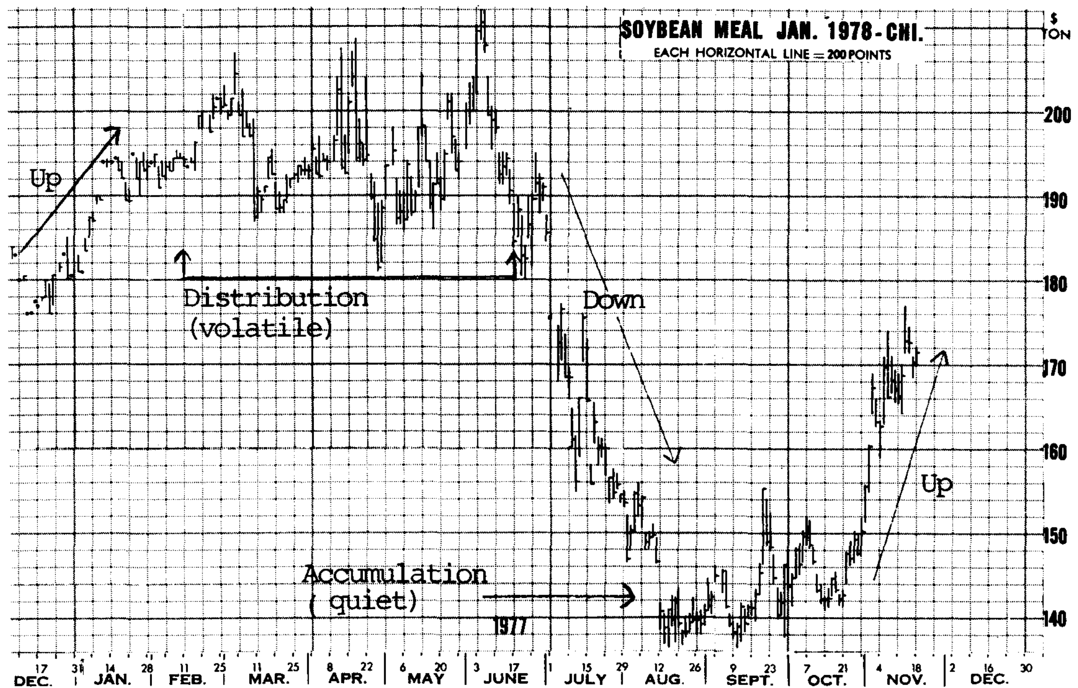
A SIMPLE OVERVIEW OF COMMODITY PRICE MOVEMENTS

Commodity price movements follow a very simple similar pattern over time. They form a base (accumulation). During this time they are in what is known as a trading range. Next, they move up with intermittent reactions occurring during the price rise. The price rise is followed by a topping out period (distribution). Once the distribution is complete, prices fall with intermittent rallies until a new bottom area is reached. Then it is back into congestion (trading range) until accumulation is complete and prices rise.

This is the normal recurring cycle of commodity price movements: Accumulation — up — distribution — down. If one will keep this simple overview in mind with an eye to seasonals, probabilities, contrary opinion, and where the market has last been, over the long-term one can profit. Notice the Soybean meal chart. The price cycle is obvious. Up — Distribution — Down — Accumulation — Up.



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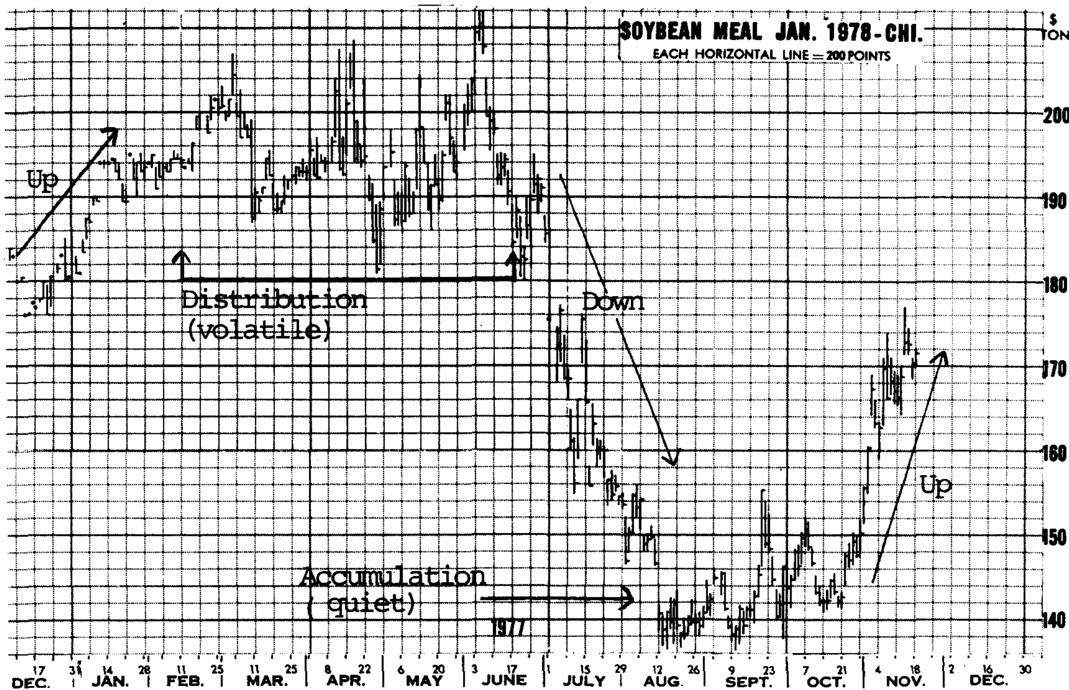
IT IS EASIER TO BUY THAN SELL COMMODITIES

It is much easier to buy a market after a base building period than it is to sell a market in the process of topping out. Why? First of all, at lower price levels, during the base building, trading range process, markets are generally quiet. The public is not in the market. Price action is not volatile, and one can comfortably take a position with minimum risk and exposure. Emotion is absent.

Conversely, during the time when a market tops out at higher price levels, commodities swing more wildly. The action is much more volatile. The public is in the market. Emotion is rampant. It is more difficult to position in such a market. The risk is much greater, due to the whipsaw action of the market. Stops are usually necessarily placed farther away from the present market price in order to avoid whipsaw losses. Also, it is difficult to judge how long the distribution process will take place. False news can be leaked into the market to drive up prices. This aids those distributing.

It is fair to say that the risk in going short a market in distribution is often three to four times the risk of buying a market which is basing prior to an upmove. However, there is compensation for the risk assumed by those going short in a market that is about to break. Often, a bear market will move down three times as fast as prices previously moved up. One can therefore make money three times as fast in a bear market as one can during a bull market. It is the old law of risk assumption. The greater the risk, the greater the potential reward.

Notice the Soybean meal chart. The wide price swings during the March — June distribution make it difficult to sell short safely. Now notice the accumulation period in the meal that took place between August and October. The price swings are not near as volatile. A trader could have positioned in October on the long side, with stop losses below the August and September lows and profited nicely with manageable risk.



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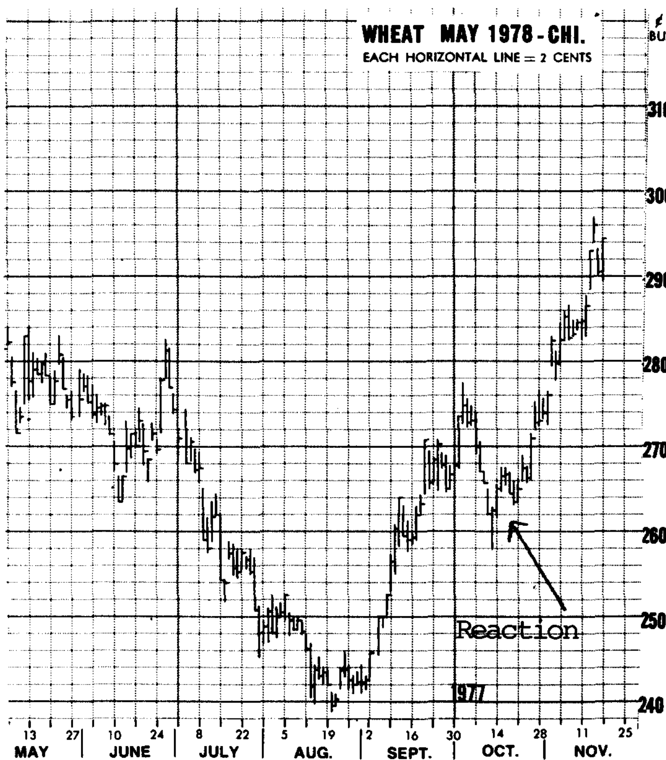
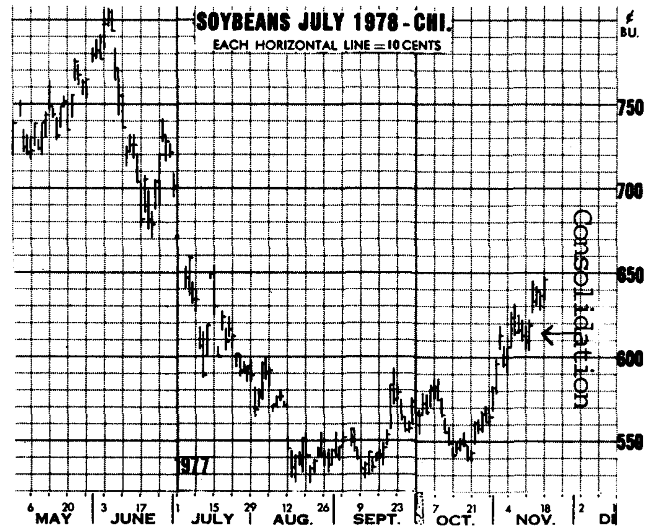
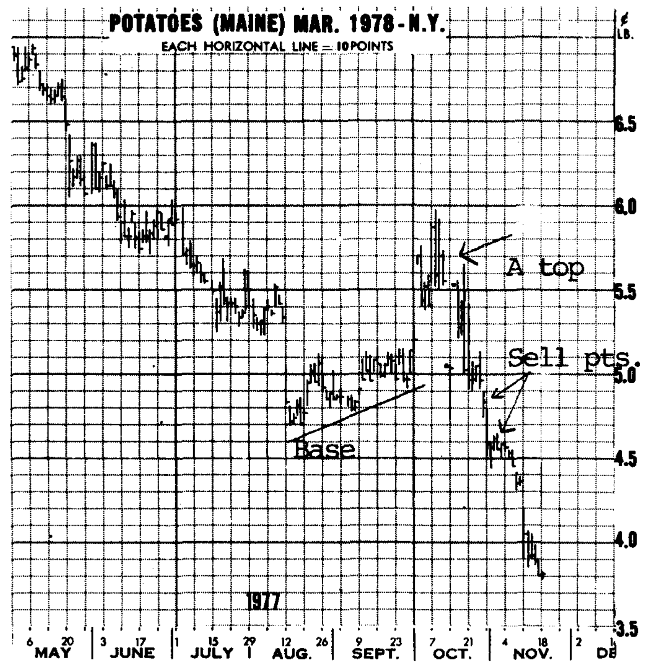
NEW BULL MARKETS

After an extensive decline (bear market), a market will form its base and then move higher. Nearly always, the first leg up following the base will have a reaction or a consolidation. SELDOM is this first reaction or consolidation a top. The first reaction or consolidation following an up move from a bottom should be viewed as a buying opportunity! Notice the May Wheat chart. The first reaction in mid-October was a buying opportunity. Notice the July Soybean chart. The consolidation in mid-November was a buying opportunity.

There are always exceptions. The March Potato contract was one. The price rise following the August — September base was followed by a congestion which broke down. But, as in every exception, there is an opportunity to turn misfortune to one's favor. Toward the end of October, the market returned to its August — September base. Nearly always, when a market breaks out upside from a base, returns to the base, and then breaks the base to the downside, it is going a lot lower. Witness potatoes. The arrows indicate two days when one could have gone short. Another example of a base breakdown following a breakout to the upside, was sugar in June of 1977.







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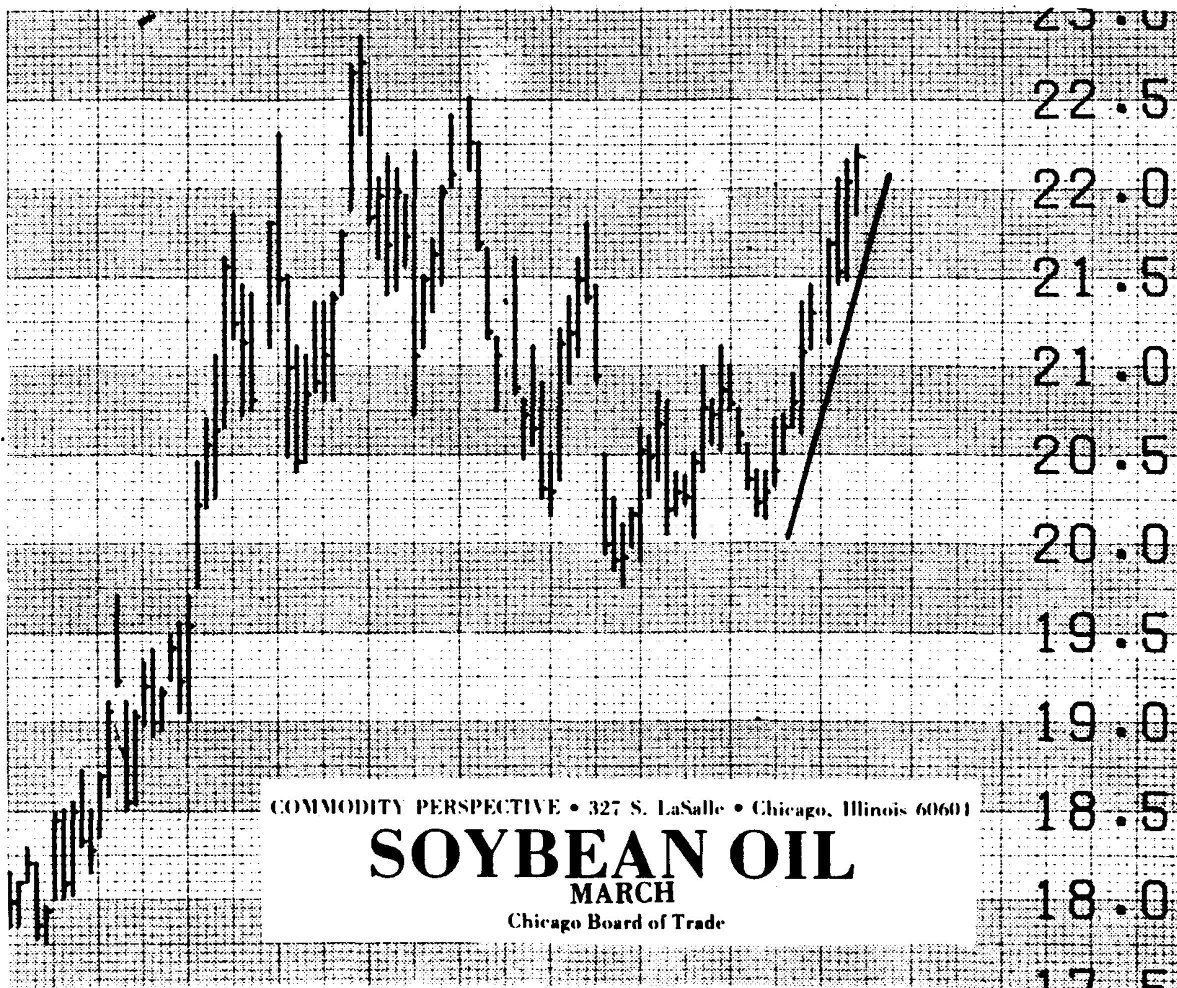
Nearly all commodity traders keep daily bar charts. Traders in the pits keep charts, or at least notes that are the equivalent of daily charts. Most commission house traders keep daily charts. The brokerage community keeps individual charts on daily commodity price activity. The plain old-fashioned bar chart is probably the most pervasive tool in the commodity trading spectrum.

Why is the bar chart so important? It is a simple bookkeeping record of price activity that not only gives a graphic presentation of this human activity, but also is utilized to a great extent for TIMING PURPOSES — determining entry and exit points. While the weekly and monthly charts provide a trader with a broad perspective on market price action, it is the daily charts which "fine tune" price action and market entry and exits.

As a large percentage of traders focus on only the daily charts, and thus "fine tuning" as it were, they often wind up with whipsaw losses and large commission costs. They are too close to their subject and lose their perspective. One chart service which tends to exaggerate the importance of daily price movements is Commodity Perspective (327 S. La Salle, Chicago, Ill. 60601). Notice the Commodity Perspective chart of daily price activity in March Soybean Oil. Just from viewing the C.P. chart, the recent uptrend in prices from 20.0 to 22.0 seems to be one whale of a move up, and prices are approaching old highs. One might conclude that the Soybean Oil move is about out of gas and ready for a correction. This perspective, however, is myopic.



Now, take a look at the Commodity Research Bureau chart of May Soybean Oil. (One Liberty Plaza, NY, NY, 10006) Wow! Does the perspective ever change. The recent uptrend which looked so breathtaking on the Commodity Perspective charts is simply a minor rally in the price action of the past

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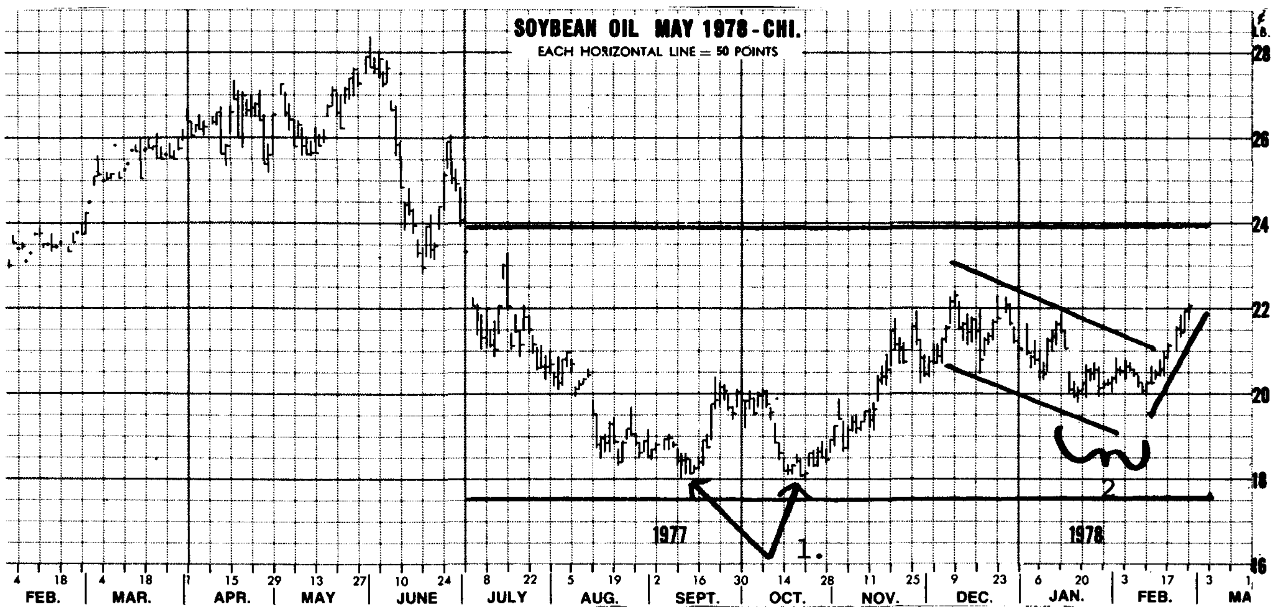

year. And, in fact, with the big double bottom formed in September and October of 1977 (1), and the major higher bottom (2) formed in January and February of 1978, one gains the perspective that the Soybean Oil market may be preparing for a significant up move. A substantial close above 22¢ would send the market to its highest high in 7 months, a bullish signal for a market which had been in an extended base building process. Therefore, the correct use of the daily charts is to view them after the monthly and weekly charts have been analyzed, and then, in this writer's opinion, focus first on the Commodity Research Bureau charts in order to receive a broad perspective of daily market action, and next analyze the Commodity Perspective charts for real fine tuning.

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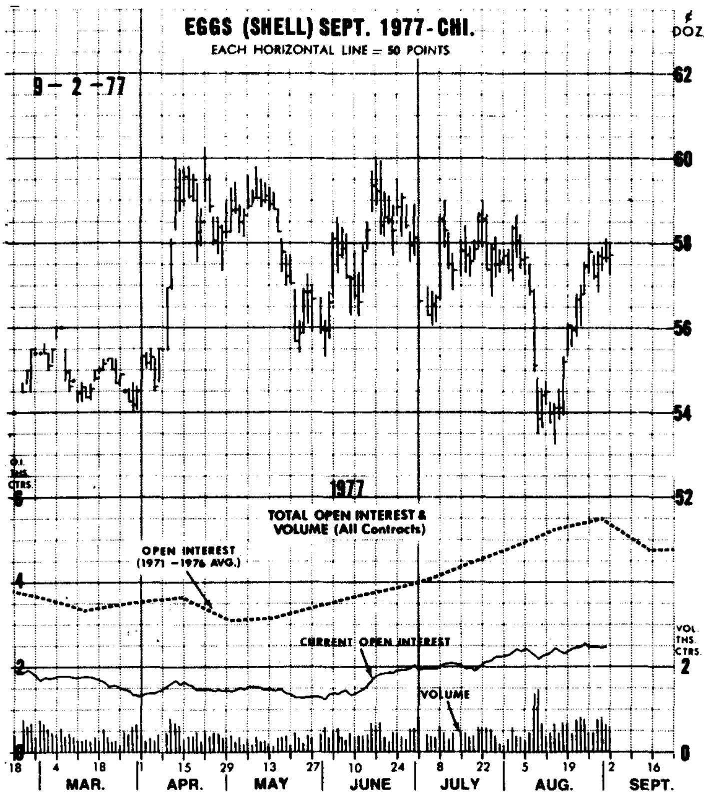
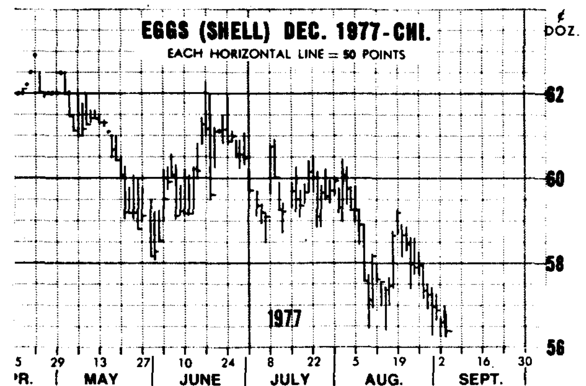
TWO CONTRACTS

The action in the September Eggs vs. the December Eggs illustrates the importance of watching two contract months of the same commodity.

The September Eggs made higher highs for two weeks in a row (August 15th - 26th) while, during the same time period, the December Eggs worked lower. Usually when a nearby contract moves up, the deferred will also rally in sympathy. Thus, if a trader was looking to short September Eggs into resistance, he was best advised to short the December contract, the weaker of the two contract months.



Additionally, a position trader would have observed that the seasonal tendency is for eggs to peak in September and go lower into December. Thus odds favored weakness in the December option versus the September. Positioning on the short side of the December Eggs between 58¢ and 59¢ with a stop close only at 60¢ made sense. The trade had a low dollar risk and was favored by both seasonal probabilities and market action.



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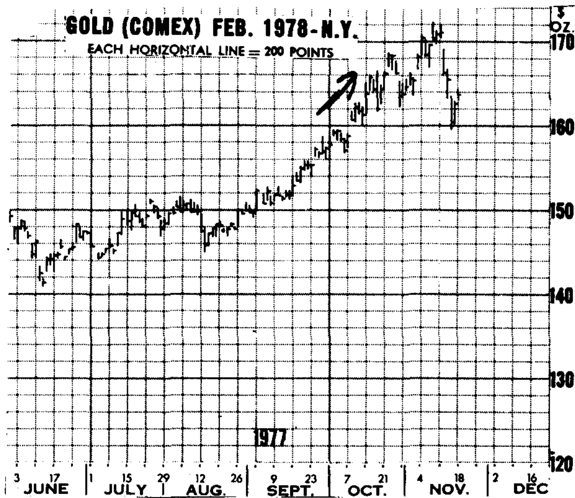
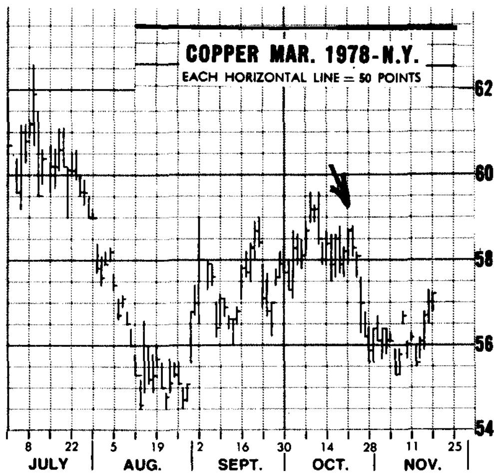
RELATIVE STRENGTH

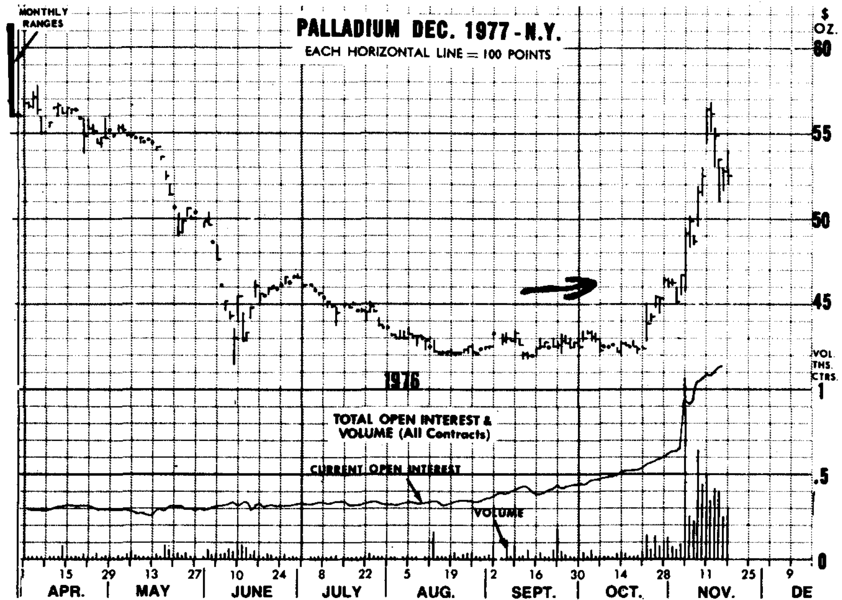
There is such an "animal" as "relative strength" in commodities. By this is meant that certain commodities tend to move together and some members of the complex are stronger than others. For example, gold, silver, copper, platinum and palladium tend to move together. Soybeans, soybean meal, and soybean oil are inclined to move as a unit. Corn, oats and wheat tend to trend in the same direction.



Let's take an example. The gold market starts to trend up. It moves for several days, or maybe even a week or so, without a commensurate rise in copper. Traders will look at the market and say, "AHAA!! — since I missed the gold rise, I'll catch the copper before it starts up." With this logic, the average trader then buys a contract of copper in expectations of a rise to match gold's ascent. That is usually faulty thinking. The market does not make many mistakes. It leaves very few loopholes. There is probably a very good reason why copper did not rally with the rise in gold. Therefore, a trader is best advised to stay with the primary strength in the index. In this case, staying with the primary strength would mean buying and trading the gold market rather than the copper market. The rise in gold and the stagnation and drop to lower prices in copper illustrates this perfectly.

There are, of course, exceptions to this rule. When a relationship gets way out of line, such as occurred in the gold versus the palladium market, then there may well be some "catching up". A rise in open interest and increasing volume often indicate such a situation. A solid chart formation will also usually confirm. Then, when the "rubber band" effect takes hold (gold in this case pulling up palladium prices), one can catch the rise in the weaker of the commodities within the index. But aside from this exception, a trader is advised to trade the primary strength in hope of making profits as opposed to trading the weaker commodities within the index.





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Looking at two contract months of the same commodity offers a trader an expanded perspective which he does not enjoy by just zeroing in on one contract. Look at the Sept. and Nov. Plywood contracts, for example. Here, we have a nearby contract (September) and a relatively deferred contract (November). Notice that the contracts had moved up pretty much together until the second week in July. At that point, the Sept. contract began moving up faster than the Nov. Possibly, this was a temporary squeeze situation in the Sept. But another possibility was that the gain in premium (Sept. over Nov.) indicated a potential bull move.

By following both contracts, it could have been observed that three bottoms (1, 2, 3) had been formed at the same relative levels. The rally following bottom number 3 was the first indication of divergence in chart patterns. But then, the higher bottom at point 4 alerted the trader to a bull move, particularly since the point 4 bottom was so much higher in the Sept. contract than the point 3 bottom, particularly when compared to the Nov. situation. The point 4 bottom had another point of interest. In the Sept. contract, the market just dipped low enough to take out the protective stops below the lows of the previous week. In the Nov. option, the market dipped to point 4 and gracefully ate up the stops below the logical stop placement points, the lows of two previous weeks. When the November exploded up on good volume and range through the downtrend line, and confirmed the September breakout, an all-clear was issued for a buy with protective stops below point 4.

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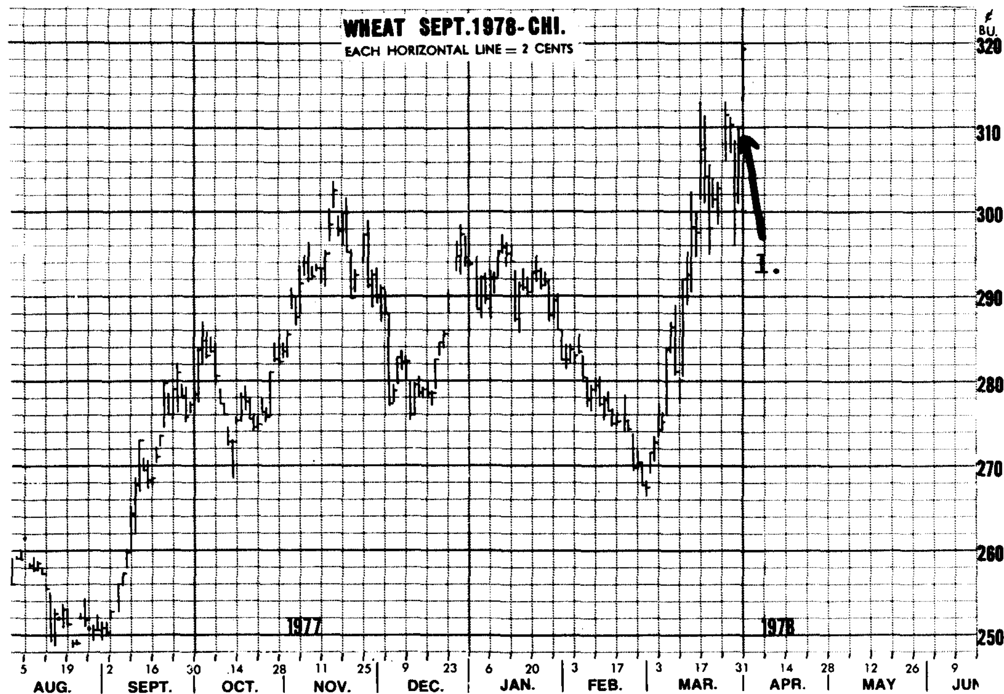
THE MARKET TIPS ITS HAND

A great deal has been written in this publication about patience, about waiting for the right opportunity to enter the market, about it sometimes being "cheaper" to buy at higher prices than at lower prices, about WAITING FOR THE MARKET TO TIP ITS HAND!!! On Thursday, March 30, 1978, the wheat market tipped its hand (which is why the weekend tape recommended buying wheat).

The grain complex (wheat, corn, oats, soybeans) tend to move as a unit. In fact, they are tracked as an index. When the emotion at the Board of Trade (where the grain pits are located) gets out of hand, and there is rampant bullishness or bearishness, this whole protein complex tends to get into gear together, either to the upside or the downside. Therefore, a trader can sit and wait for any VARIATIONS from this pattern in order to ascertain relative strength or weakness. Thursday, March 30, 1978 the wheat market tipped its hand. It told the observant trader that it intended to work higher. How?



On Thursday, March 30th, the mood of the Board of Trade was one of pessimism. Soybeans (the King of the Commodities) were under tremendous pressure downside. In fact, they broke down over 30¢. (Day 1). The Meal and the Oil, likewise, were weak. Sympathy selling should have appeared in the wheat. But no! Wheat rallied (Day 1) and, in fact, closed near its high of the day at 310. By so doing, the wheat market tipped its hand that it was going much higher. The place to buy wheat was on Thursday, March 30th, Friday, March 31st — the breakout day, or on the first correction which occurred on Monday, April 3rd (not shown here). Wheat quickly moved up another 10¢ from Friday's close, presenting the excellent opportunity for a quick profit.

A trader who is patient can wait for such opportunities for they will periodically appear. Why guess? Why take poor risk trades? Over time, the market will tip its hand as to real opportunities.

(Please see soybean chart on next page).

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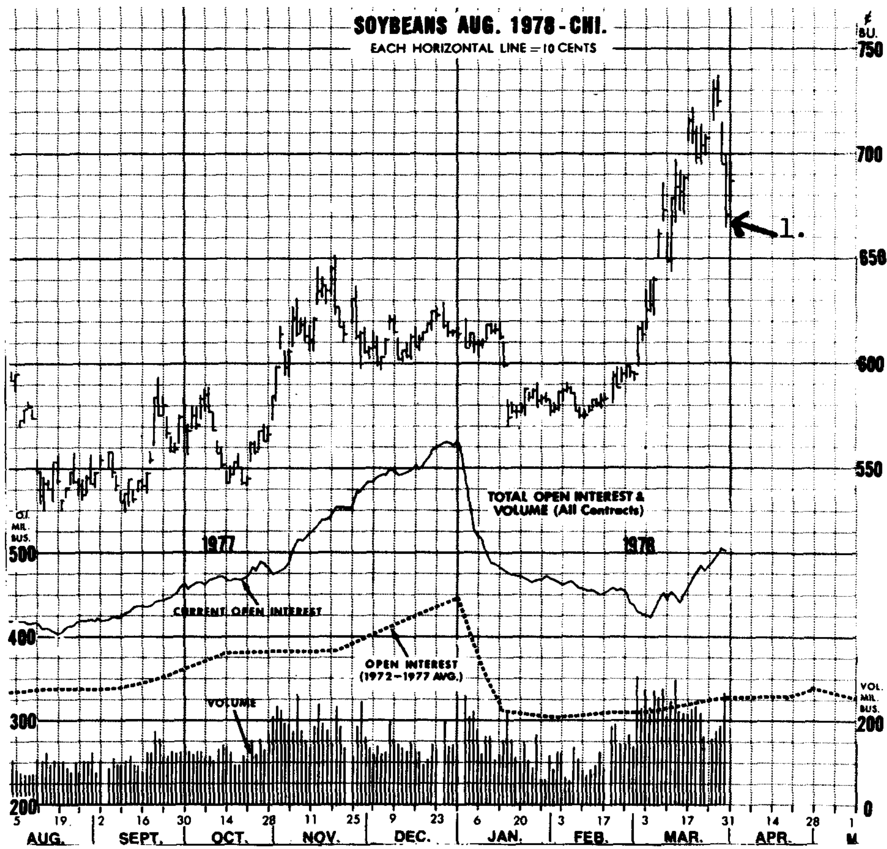

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SELLING SHORT

In the Reaper, Vol. 1 — XXIII, we correctly called the decline in the soybean complex. Some readers were confused, however, on how to judge the rally, and thus position in the market prior to the next decline.

There are various ways a market can rally for one or two days after a severe sharp decline. In fact, a pause may well suffice as a rally. Below are several of the more common ways the rally can occur.

1.) A sharp decline (2 days) followed by an inside day prior to the next decline. This was a pause. Short positions could have been taken below the low of the inside day, or below the low of the second down day, or on close below the inside day. Notice that the second down day is a low surrounded on either side by a higher low.

2.) Here we have a reversal day up the third day with a higher close. No follow through the next day upside and the market declined. Short positions could have been taken on close with protective stops above reversal day or fourth day.

3.) A two day rally with a narrow range higher highs and lows, and low volume fails on the last (6th) day. Sell below the low of the second rally day or on close the last day. Stop is placed above the rally high.

4.) A reversal, a one day rally (gaps on both sides) followed by the decline. Sell on opening the fifth day or on close. Stop above the high of the last day.

5.) Reversal day, two day rally with narrow ranges and big break down. Sell below low of the fifth day (high point of rally) or on close the last day. Stop above rally high.

6.) Tricky, and difficult to position. Market went above the high of the second down day and then reversed down. Once, on the third day, the market rallied above the high of the second day, a sell stop could have been placed below the low of the second day. Stop above last day's high.

7.) When the market went above the high of the second day, the rally was under way. The lower close the third day was the point to go short. Stop above high.

Generally, the rally or pause following the first severe breakdown from a top will begin when:

1.) A low is surrounded on both sides by a higher low, or

2.) The high of the previous day has been penetrated to the upside, or

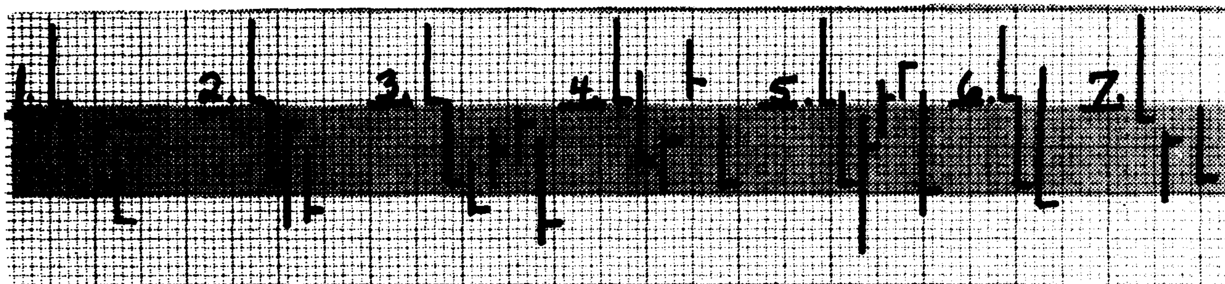
3.) There is a higher close than the previous day.

Generally, the correction upside will be over when:

1.) The previous day's low is penetrated to the downside, or

2.) A high is surrounded on both sides by a lower high, or

3.) A close is lower than the previous day.



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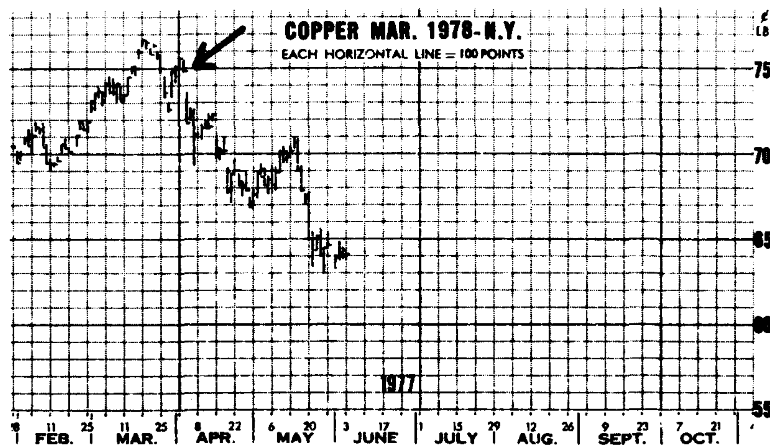
SELLING BIG BREAKS

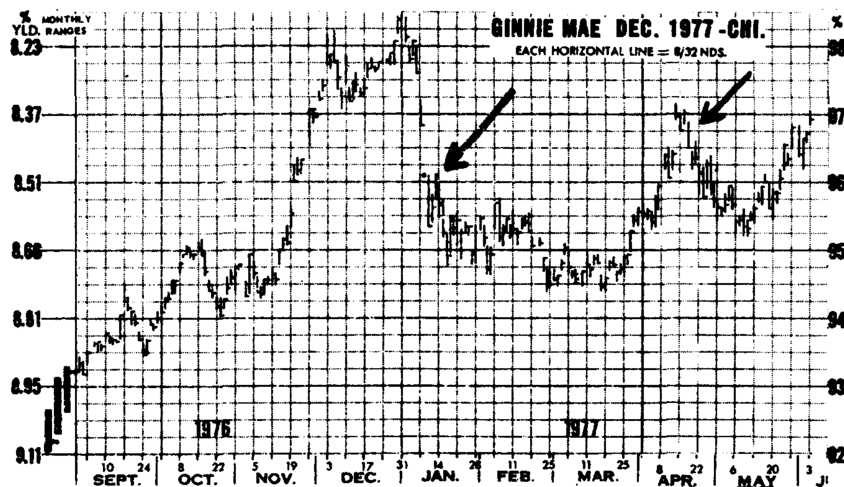
When a market: a) Breaks sharply for two or three days with, b) Heavy volume, c) Wide daily ranges, d) Low closes, e) Below the lows of a top formation, usually, a) The first corrective rally is for no longer than two days, b) On a bulge to the upside, a trader can short the market, c) Expect the next decline to at least break the recent low that followed the initial break. Should the rally after the initial market break last for three days, be on guard for the next decline may well not carry below the recent low. The best place to short the market is on a fast run up the second day after the low of the initial break. Stops should be placed above the high of the first break day, and, as soon as the low of the highest day of the upside reaction is broken to the downside, stop should be moved down to above the high of the rally. For the more cautious trader, a sell stop can be placed below the low of each day of the rally. Once "stopped in" on the short side, protective stops can be placed above the highest high of this latest rally. Profits can be taken after the market breaks the recent low, or a trailing stop can be used. REMEMBER, nothing works all the time. Use stops for protection. The probability is, however, some 80% of the time, following a fast break, a market will have a weak rally and then make new lows.

For additional confirmation, the rally following the break should be no more than 61.8% of the previous decline. Rally should terminate at or below the lows of the top formation.

EXAMPLES:

1.) August 1977 Soybean Meal (end of April — 1st week of May)
2.) October 1977 Sugar (end of April — 1st week of May)
3.) December 1977 Ginnie Mae (2nd week in Jan. 1977 and mid-April 1977) See chart.
4.) March 1978 Copper (end of March 1977 — Note the 3 day rally. However, the daily ranges were narrow the 2nd and 3rd days.) See chart.
5.) September 1977 Silver (2nd week in July 1977)
6.) August 1977 Pork Bellies (mid-Sept. 1976, mid-Jan. 1977, mid-May 1977. Note: At the end of February 1977, the market rallied for four days before another break. It, however, retraced the decline approximately 50%, did not rally back to the lows of the top formation, and did not make a lower low until the big second break. See chart.





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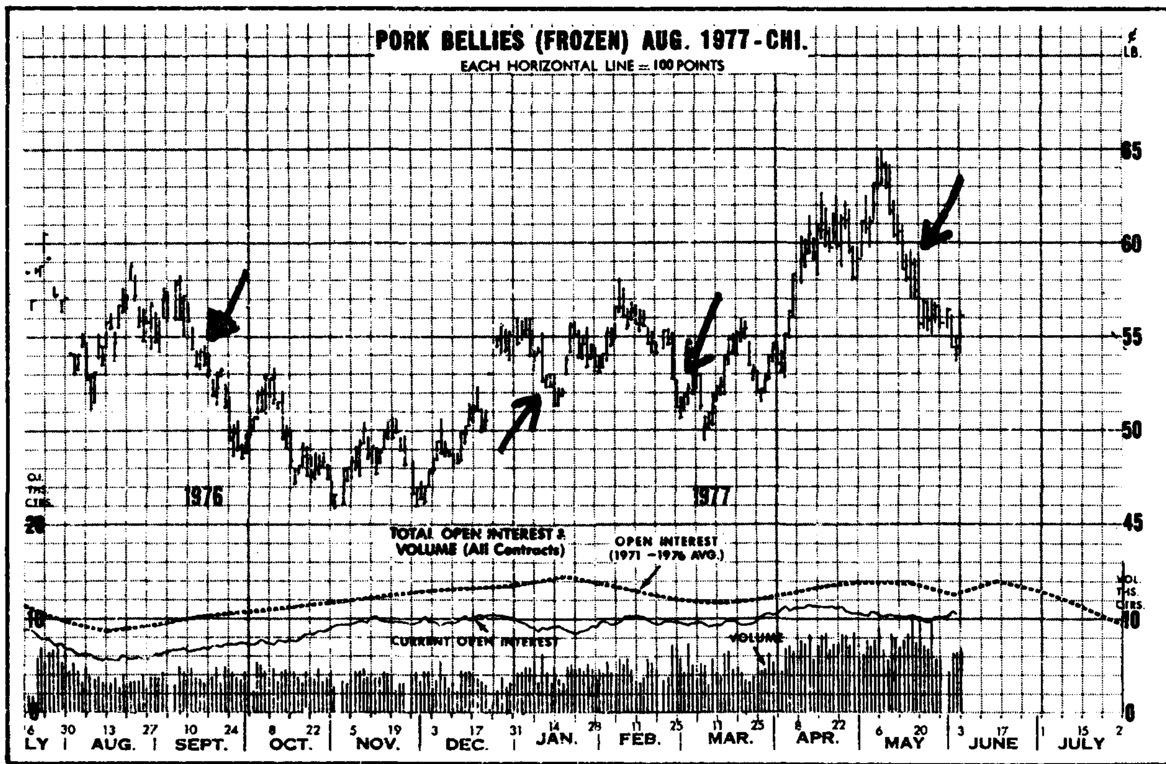

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There was a good indication that copper had bottomed the week of June 6th. The key to the market turn — the much maligned technical tool — OBV — On Balance Volume.

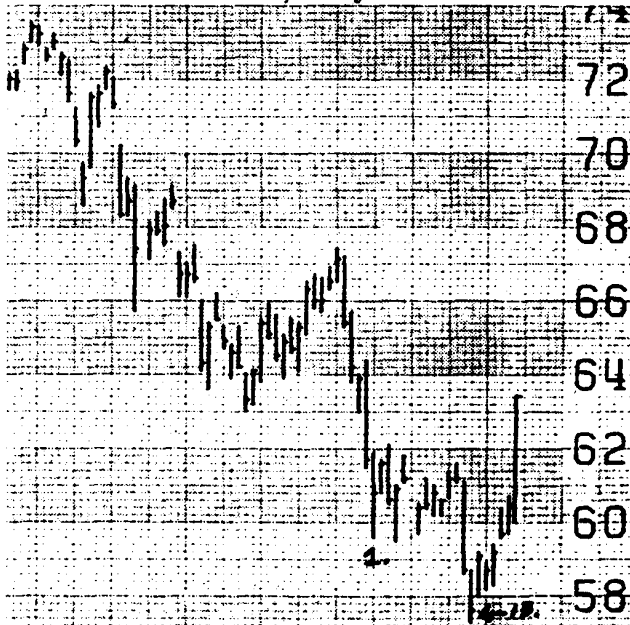
Good friend and owner of Lambert Gann Publishing Company, Mr. Billy Jones, puts considerable faith in this tool. Notice the following:

1.) On Trading Day marked #1, Copper went to a new low for the price decline. OBV confirmed (new low).

2.) On Trading Day marked #13 on the July Copper chart, Copper made a new lower low in price than it did on Day #1. Notice, however, the same day on the OBV chart, Day #13, OBV did not make a lower low. Divergence! A non-confirmation. Volume favored the bulls, even with price making a new low! Accumulation was taking place in Copper! On Friday, June 17th, came the upside explosion.

OBV is simple to compute. Use the following columns. Ex: July Copper.

Date	Commodity's Closing Price	Volume	OBV
6/9	57.6	− 740	− 740
6/10	59.1	+3613	+2873
6/13	58.7	−3370	− 497
6/14	59.2	+5777	+5280
6/15	59.7	+4412	+9692



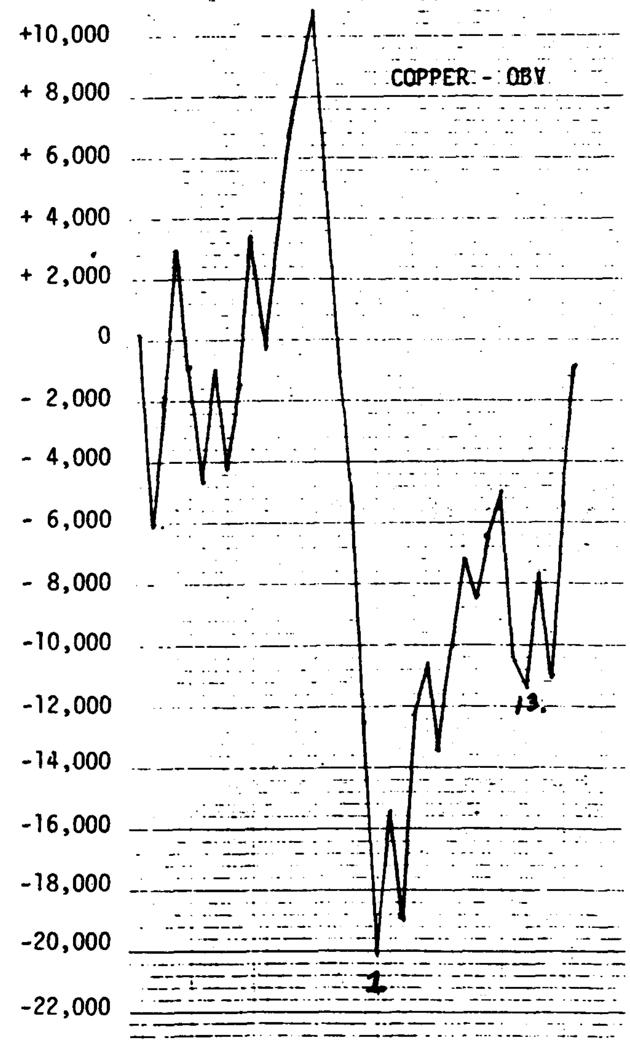
Step 1: Record the commodity's Date, Closing Price, and Volume.

Step 2: If today's close is greater than yesterday, put a "+" in front of the volume #. If today's close is less than yesterday's, put a "−" in front of the volume #.

Step 3: Add or subtract today's volume from yesterday's OBV. Thus, you have a running total — OBV.

Volume figures can be obtained from the Wall Street Journal or the Journal of Commerce. Be sure to correctly match volume with correct closing price and date.

Although this tool may be of little value most of the time, when the market is going to turn in a big way, OBV will often clue you in. Incidentally, it recently gave clear warning of the gold top in mid-March, 1977.



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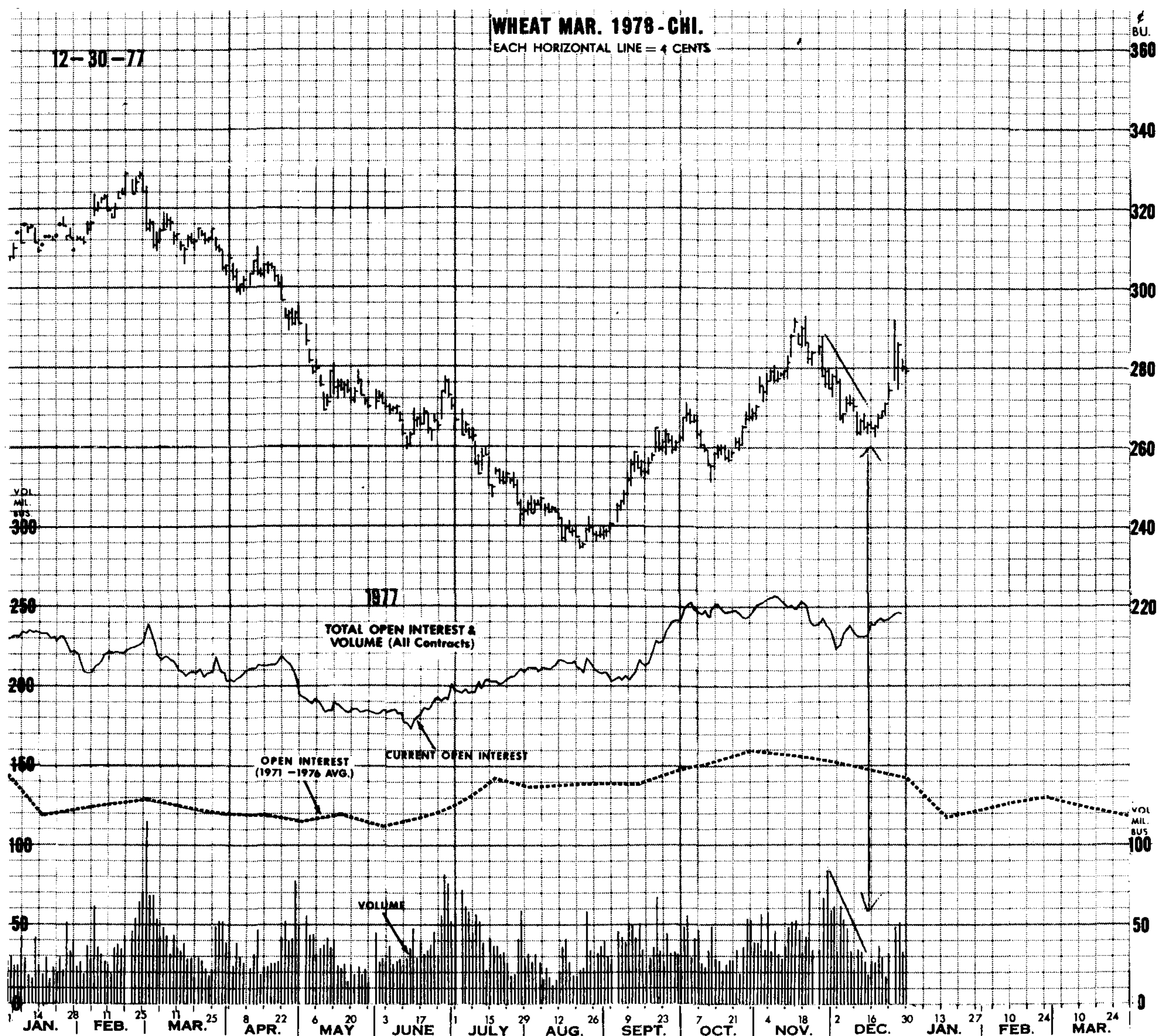
Wheat formed its bottom in mid-August 1977. Next, it moved up, delineating its uptrend through mid-November 1977. A four month uptrend had occurred. The market then declined for four weeks in a row. Question: Was the uptrend over? Certainly, after four months of bull market, the question could be rightfully asked. Also, it is unusual for a market to make lower lows 3-4 weeks in a row if the uptrend is to continue. Support came in where expected, at the 264 level, basis March. What would be next?

Since only 2 or three major highs occur each year in a commodity, it made sense to expect wheat to make some attempt to challenge the November high. It did so, in a convincing manner. One of the clues as to whether the wheat market would challenge the high, and when it would test the high, came from the volume indications.

From the high volume day at the end of November, throughout the decline, volume continually decreased. The decrease in activity was so consistent, one could draw a trendline across the top of it. The primary trend was up. The assumption was made that the primary trend would continue. An excellent indication that the primary trend will continue, or at least retest the recent high, is a drop-off in volume on the reaction. This is exactly what occurred in wheat. Therefore, a low risk trade was recommended on the long side, with a close stop, playing the probabilities for a retest of the November high, which occurred.



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THE CYCLICAL OSCILLATOR

Walt Bressert (HAL Community Cycles, P.O. Box 2275, Evergreen, Colorado 80439) had dedicated his life to the study of cycles. He has made a contribution to market theory. In my opinion, cycles work best when, as Burton Pugh stated, there is no other overwhelming influence on the market. Historically, that is between the months of September and May for the grains. Other times, when there is no news in the markets, and trading is quiet, one can expect cycles to be most useful.

There is an indicator I use that is a combination of Walt's "Trading Cycles" and a well-worn oscillator that has been called %R, %A, %C, etc., depending upon who is laying claim to it at any particular time. I call the indicator a "cyclical oscillator."

Here's what's been done. The oscillator formula is as follows:

$$\frac{\text{Highest High of Last "X" days} - \text{Today's Close}}{\text{Highest High of the Last "X" days} - \text{Lowest Low of "X" days.}}$$

Walt's "Trading Cycles" days are used for the "X" days. For example, the "Trading Cycle" days are Copper-18, Silver-25, Wheat-31, etc. So, if the formula is being used on December Wheat on Monday, October 17, 1977, the formula would look like this:

$$\frac{261.5 - 249.5 = 12}{261.5 - 230 \quad = 31.5} = .38 = 38\%$$

261.5 is the highest high of the last 31 days.
230 is the lowest low of the last 31 days.
249.5 is Monday's close.

The 38% is how overbought or oversold the market is. Here wheat is slightly oversold, but not in a danger area. When the percentage drops to between 90-100%, the market is really oversold. When it rises to between 0-10%, it is quite overbought. Thus, a trader can judge when a correction is due (overbought), or when it's time for a rally (oversold).

The indicator will work better than 76% of the time. (When the oscillator is between 0-10%, 76% of the time, the market will correct down.) Obviously, when the market does not correct, it is time to take notice. What does not happen, in this case, is more important than what actually occurred. A high probability has been violated. Therefore, a trader will want to look at the market. When a market will not correct, when the cyclical oscillator calls for a correction, it is usually going a lot higher. A recent example is the 1977 Gold market from September 5th through the following six weeks. The cyclical oscillator called for a correction between $150 and $151, between $156 and $158, and at $160. No correction came. After watching this tool for some time, I have discovered that when a market acts like gold acted, it is going much, much higher, or forming a top. It seems to be a black/white situation.

Take a look at the wheat oscillator. The percentages are plotted from 0 to 100% along the left axis. Each line on the horizontal axis represents a particular day. The dots are then connected. In the wheat example, 38% would be plotted on Monday, October 17th.

Here's how to use the oscillator. When a market has been fluctuating between 90-100%, it is oversold. Thus, when one is looking to buy a market, look for a "W" with the second leg higher than the first leg. Notice circled example (W). In a trading range, or a reaction in an uptrend, this tool comes in quite handy for finding a buy spot.

The reverse is true in a downtrend. Notice the T-Bills chart. Inverted W — (M) and down! Use this procedure when looking for a point to go short during a downtrend, or during a trading range.

The "W" or "M" is also good with contrary opinion. If Wheat is 15% (contrary opinion) and a "W" appears — expect a rally. If the contrary opinion on T-Bills is 90% and a "M" appeared, expect a fall in prices.

Every tool has its problems. The cyclical oscillation is no exception. If one goes short, using it against a major uptrend with a head of steam, expect to lose money. In steep up or downtrends, or powerful markets, it does not work!

Why does it work at all? First of all, as Walt has discovered, there are trading cycles that occur with probabilistic regularity in commodities. Thus, one is in tune with the market's tendency. Secondly, markets tend to oscillate from overbought to oversold conditions. So if the wheat market, for example, is oversold, and cyclically it is time for a bottom, double confirmation is housed in the same indicator.

Oh, one final use. I find trendlines drawn on both the bar charts and the cyclical oscillator to have added strength when both confirm a "break" simultaneously.

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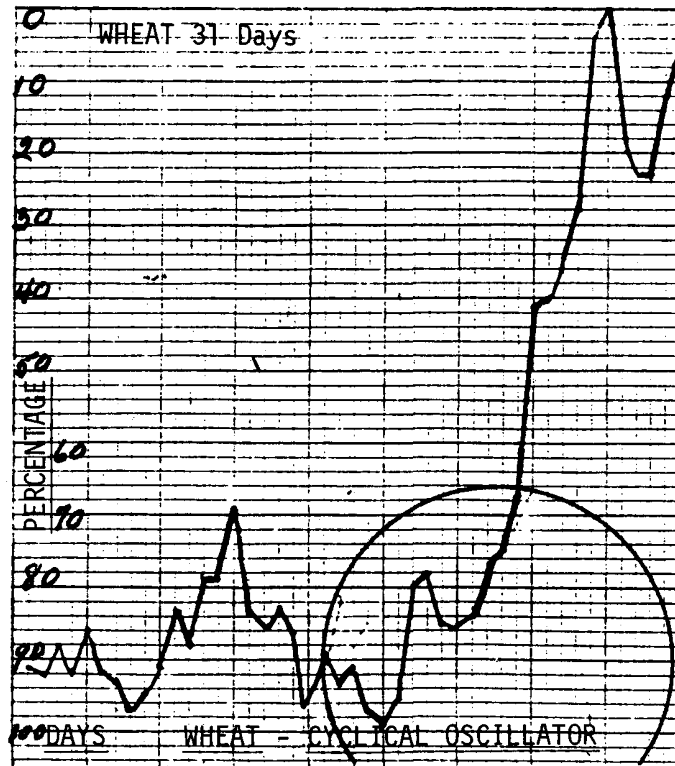

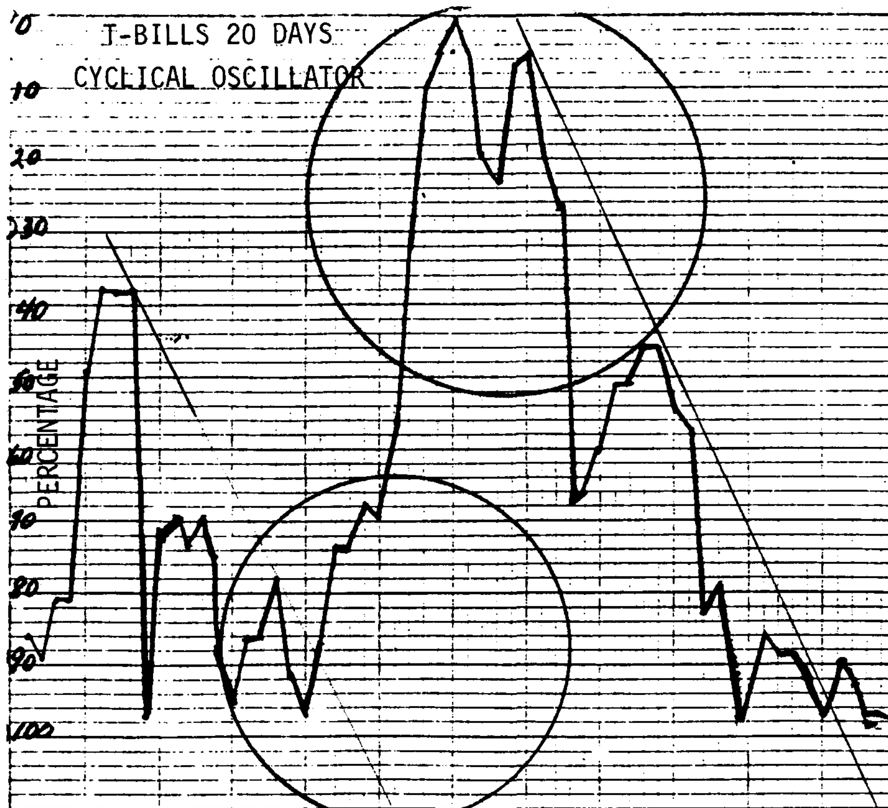

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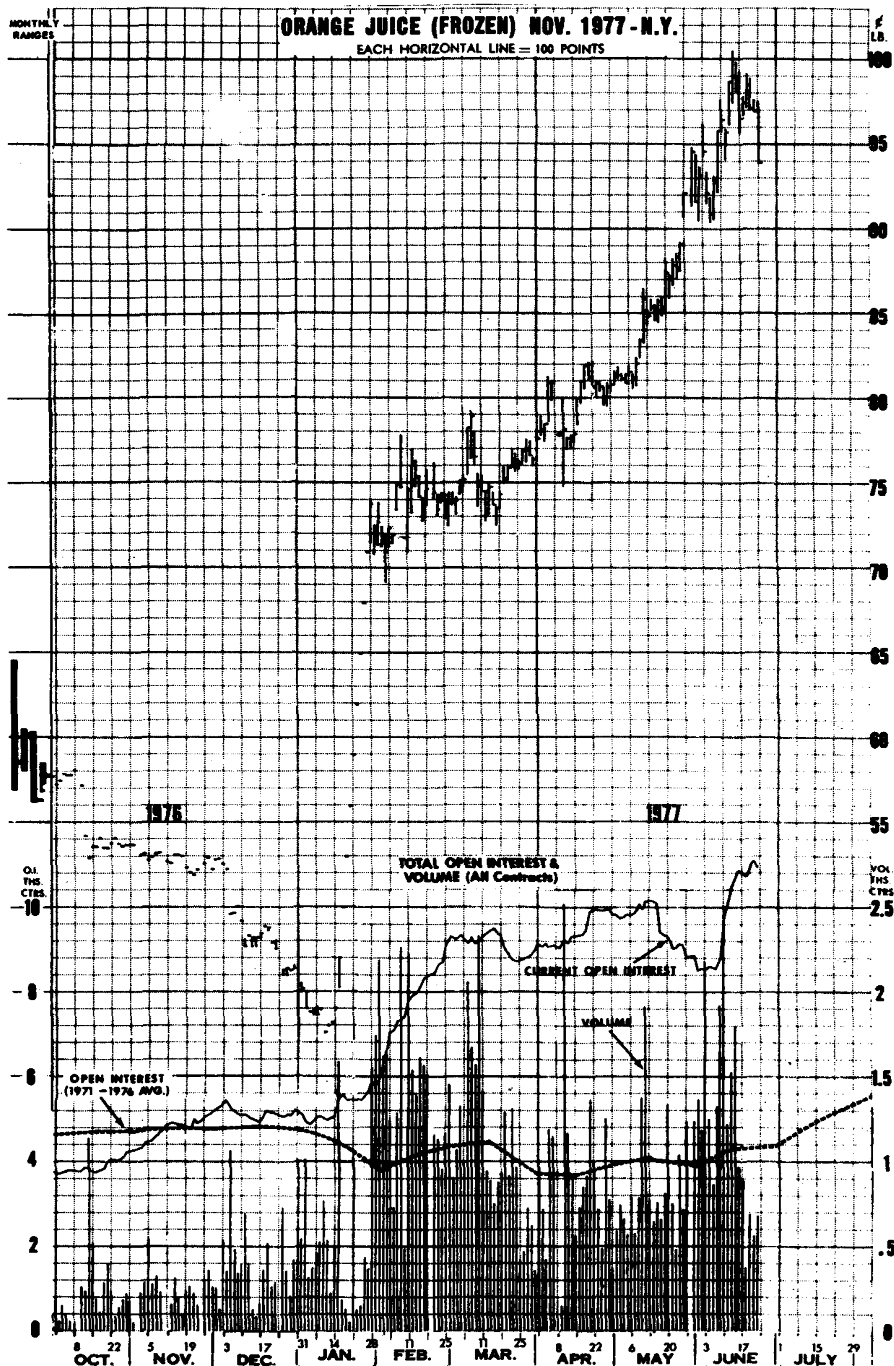
VERTICAL OPEN INTEREST

Orange Juice was a "natural." Even if that conjures up images of Anita Bryant skipping and singing across your TV screen, and milks your intelligence as well, take notice of the charts of O. J. anyway. For, you see, the run (up) was at the end and ready for a short sale!

Normally, O. J. is too thin to trade. However, flipping through the charts on the week of June 20, 1977, the short sale in O. J. stood out like a sore thumb. LOOK AT THE RISE IN OPEN INTEREST. IT IS VERTICAL! As baseballs, markets, oranges, and open interest become vertical in ascent, watch out. Momentum is about to turn, and turn sharply, down! Let's think it through.

In open interest, for every long there is an off-setting short. The O. J. market was going up, a bull wave. Beginning in mid-June, the open interest started climbing dramatically. Who was shorting the bull move? The clue was to be found in contrary opinion. The commission houses and advisory services were bullish; they were buying. The contrary opinion was running week to week in the 70's. So, some 70+% of



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the public was buying O. J. Who went short? The trade, the commercials! They know their business, and at the $1.00 level felt enough was enough. Hedge time. Additional clues confirmed. The week of June 13th the market broke sharply on heavy volume, a warning signal. The early part of the following week, the market attempted to rally. It went nowhere, and the volume was less than 50% the norm. Open interest continued to rise to record levels with no improvement in price. Something had to give. Who was left to buy when prices could not advance under present new buying? Thursday, June 23rd, the O. J. report came out. It was bullish. The next day, Friday, the market opened lower. The market had tipped its hand. On close Friday, O. J. was limit down. It collapsed under its own weight.

There were other signs of confirmation. The bull market was six months old — an aging bull by most standards. The market had advanced six weeks in a row. The O. J. was overdue a correction. The market had also hit the key price of $1.00, a level of "natural" resistance.

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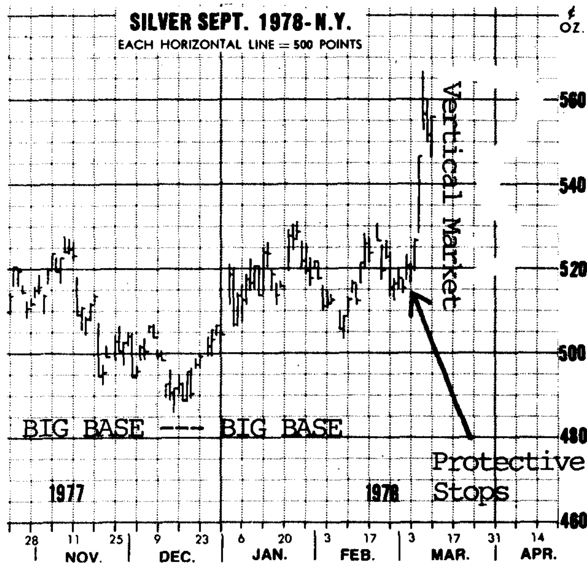
VERTICAL MARKETS

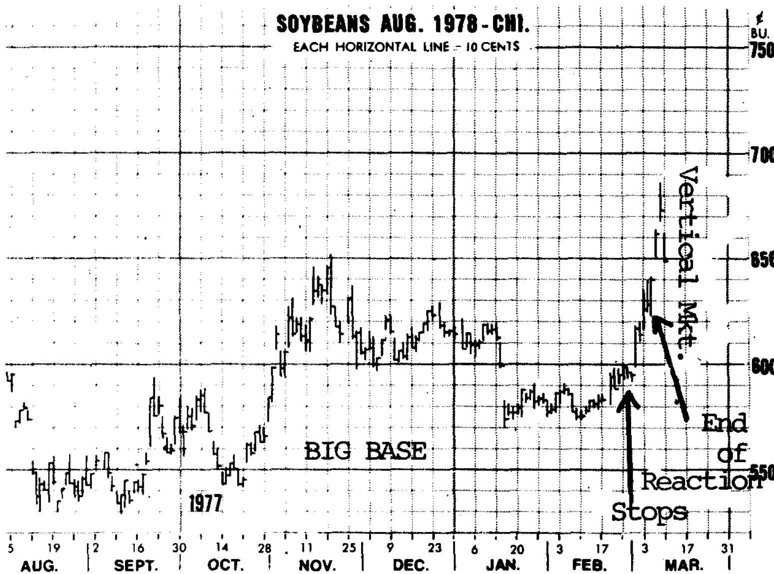
The week of March 6, 1978 we saw vertically rising markets in soybeans, soybean oil, soybean meal, wheat, corn, pork bellies, hogs, cattle, silver, and copper. First of all, a vertical rise in markets is unusual. When a vertical rise does occur, it usually is a hallmark of the culmination of a long bull market, a blow-off top so to speak. Obviously, in such a case, a trader wants to take profits during the blow-off or use close trailing stops.

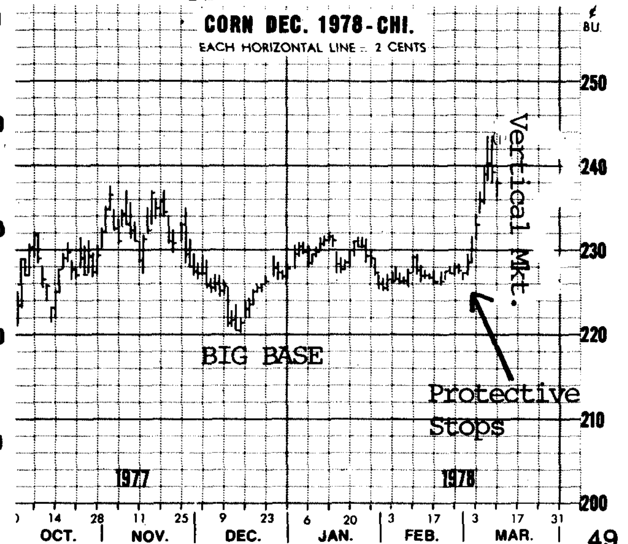
Was the action we witnessed the week of March 6th a blow-off top? Probably not. While the vertical rise and the island reversals might well be a temporary top, to be followed by a week or two of backing and filling, or congestion, it is unlikely to be a blow-off top. Why? Simply because the markets had just moved up, out of long strong base formations. Such a situation usually forecasts much higher prices. The markets literally exploded out of the bases. With that much power coming out of the bases, the probabilities are that eventually the markets will move much higher. After all, TIME must be considered, and it is very unusual for a bull market to terminate in one week. A good bull market can last from 3 to 6 months. Therefore, one must assume that we are in the early stages of a bull market. Analysis of the individual indexes confirms such a perspective. Also, the overall index has been in the process of bottoming, and with the recent sharp breakout upside it is unlikely to work considerably lower for any time in the near future.



But, what if one missed the entry, missed the vertical rise in the markets (which is easy to do)? What is one to do? How should one approach these markets? First of all, vertical markets are very difficult to position in. The market can do almost anything — explode higher, react sharply, or go into congestion. All entry plans are high risk. Therefore, there are only two entry plans which make sense. One can wait for a market reaction, and buy the second day of lower lows or the first higher close after the reaction, and put one's stop below the lowest low of the reaction after the reaction is completed, and hope the market will work higher. With this close stop, risk ($) is minimized.

The second option is to say, "OK, these markets are going a great deal higher. This bull market is young. Therefore, I will take a position here, heavily margin the position, and sit through those teeth chattering corrections, and place my stop where I think the market will never return to before it runs a lot higher. Time is on my side." This second approach can be best implemented if one trades multiple contracts. One can feed in one's line slowly into the market at different price levels in the vertically rising market.





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For example, if a trader decides to trade 3 contracts of silver, he may buy one contract now, one contract on a 10¢ dip, and another contract on another 10¢ dip. He is averaging down, not a good idea usually, but a solid approach in a vertically rising market in laying on ONE'S ORIGINAL LINE! Or, if the market works higher, the trader could feed in a contract with every 10¢ rise in price, and follow up with close stops on the latest purchased contract.

As in most things in life, commodity trading is situational. Judgment and common sense mixed with trading rules will reap the greatest return over the long haul. This approach to vertically rising markets is a case in point.

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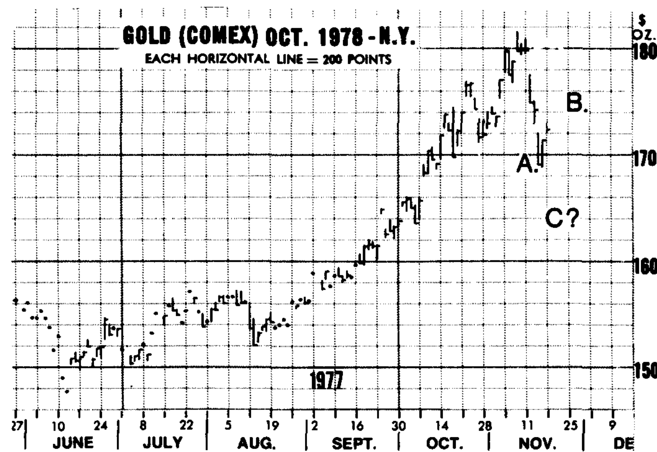
WHY A REACTION MUST COME

The week of November 14, 1977 Gold's contrary opinion hit 88%. Some 88% of those who traded gold felt the price would work higher. Fine. All the bulls bought gold. Once they had bought all they could buy, price could not go any higher. Exhaustion had to set in. Thus, there was a vacuum of buyers. For lack of support, the price of gold fell and with the fall in price, fear set in. Buyers took profits. That drove the price lower. Previous buyers had protective "stop losses" below the market to take them out at a profit. The lower prices ran the "stops" depressing price more. Thus, the reaction was fully underway.

The best way to play such a situation is to figure out where all the stop losses are (usually below some low) and wait for the market to run them. Then one can buy, put a stop loss away from the market, and wait. Almost always once the reaction is completed, the market will rally and test the high. Thus, the trader can move his stop up to breakeven once the market rallies. With 88% contrary opinion, however, one must be careful. Buying power may still be near exhaustion and the 88% figure often occurs around a top. Thus, the trader should be prepared for an ABC correction downside — a reaction from the high, a retest of the high, a failure, and then a drop to a new reaction low.



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CONTRARY OPINION

The week of November 15, 1977 had exceptionally high contrary opinion numbers throughout the grain and metal complex.

Platinum	—	96%
Silver	—	84%
Gold	—	83%
Wheat	—	89%
Oats	—	84%
Soybeans	—	82%
Soybean Meal	—	75%
Corn	—	77%

When the market leaders overall become exceptionally bullish, as was the case here, caution is warranted. Buyer exhaustion is imminent, which means a correction is near at hand. (Additionally, the market had advanced 3-4 weeks in a row.) If the primary long-term trend is up on a weekly and seasonal basis, then only intermediate and short-term traders should go short. Long-term traders should prepare to sit through a reaction or exit the market and pick the position back up at lower prices. Normally, when such widespread bullishness as this exists, the correction will last between 1 and 3 weeks. At some point in the reaction, expect negative news. The termination of the 1-3 week reaction usually occurs one of two ways. Either there is panic climax selling after enough time has passed for the good folks to forget the nice high prices, or prices drift down and all the old longs become discouraged and sell out. In this latter case the market becomes quiet — low volume and few traders.

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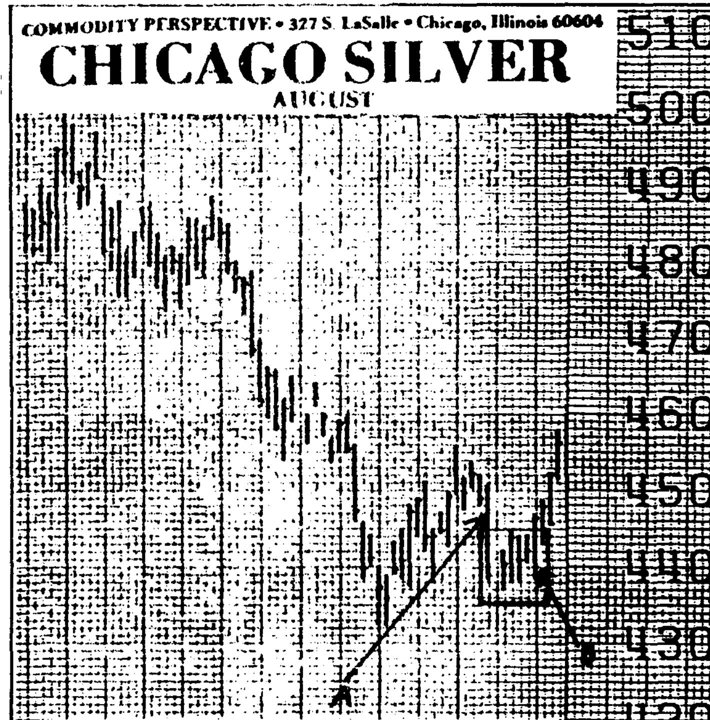
A CLUSTER OF CLOSES

A group of closes (5 or more) act as support or resistance in price action analysis. In the chart of August Silver the closes within the box, withir 5¢ of each other, are an example. Of particular significance is the fact that this group of 5 closes followed a down day characterized by wide range and heavy volume (Day "A"). Notice Day "A" also broke the minor uptrend line. Normally, following a trendline break of such force as this one ("A"), the ensuing rally will be minor and the decline will then continue. The very fact that this did not happen alerted the trader to a possible change in trend. Day "B" was the



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tip off. The market opened lower, declined and tested the lows at 438.0. Sell stops were built up between 437 and 438 below the series of lows. The fact the market could not take out these stops, and instead reversed to the upside on wide range and volume with a close above 445 was the key to buy. (The Reaper had a recommended buy stop at 445.) The close above 445 confirmed a higher bottom (437-438) and probably a move at least above the recent high (456), which did occur.

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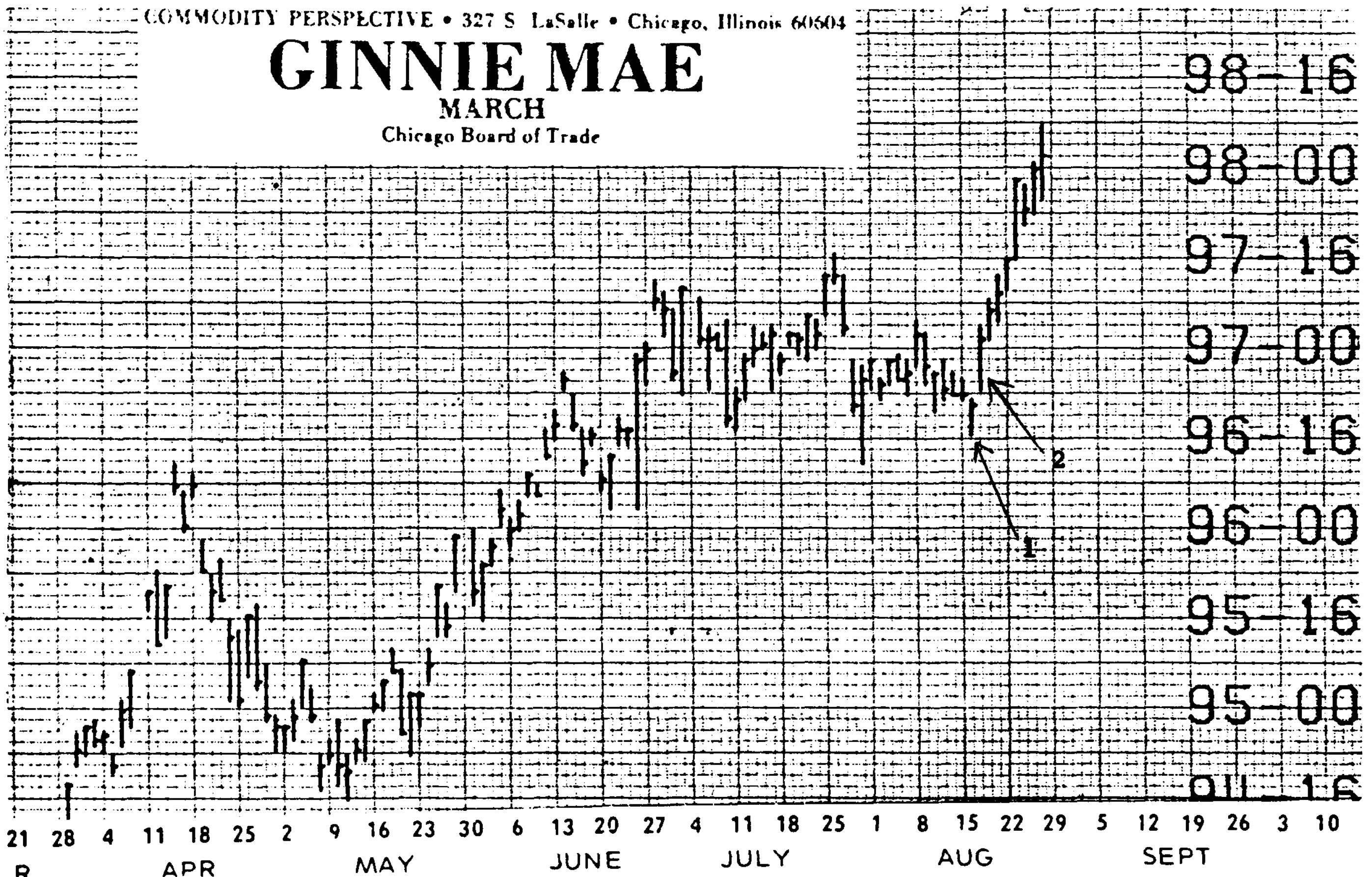
FIVE UP DAYS

On August 16, 1977 (Day 1) there was no indication of direction for March Ginnie Maes. What ensued the next eight days, however, was highly significant. Beginning with August 17th (Day 2), the market made higher highs, higher lows, and higher closes for five days in a row. The probability of that occurring is very rare (less than 3%). Thus, when it happens, it is time to pay attention to that market. Added to the strength of the move was the fact that the 5 up days ripped right through the extensive overhead resistance of the past 7 weeks.

What does it mean? What does one do? First of all, it usually means that a market is incredibly strong and will work higher. However, it can also be an indication of exhaustion. The best way to play the market, if the contrary opinion is moderate (55-78%), is to buy the second day of the dip, or after a reaction, the first higher close. Why? With such strength in evidence, the market will almost always retest the high. Thus, the trade is low risk. On the other hand, if the contrary opinion number is very high, 85-95%, and after the first reaction the next rally is sluggish, a trader can: (a) Short the third day of the rally on close and put a protective stop above the recent high, or (b) Wait and sell the sharp break following the rally if the recent high is not exceeded.

In either of the above cases, fast action and profits are the norms.



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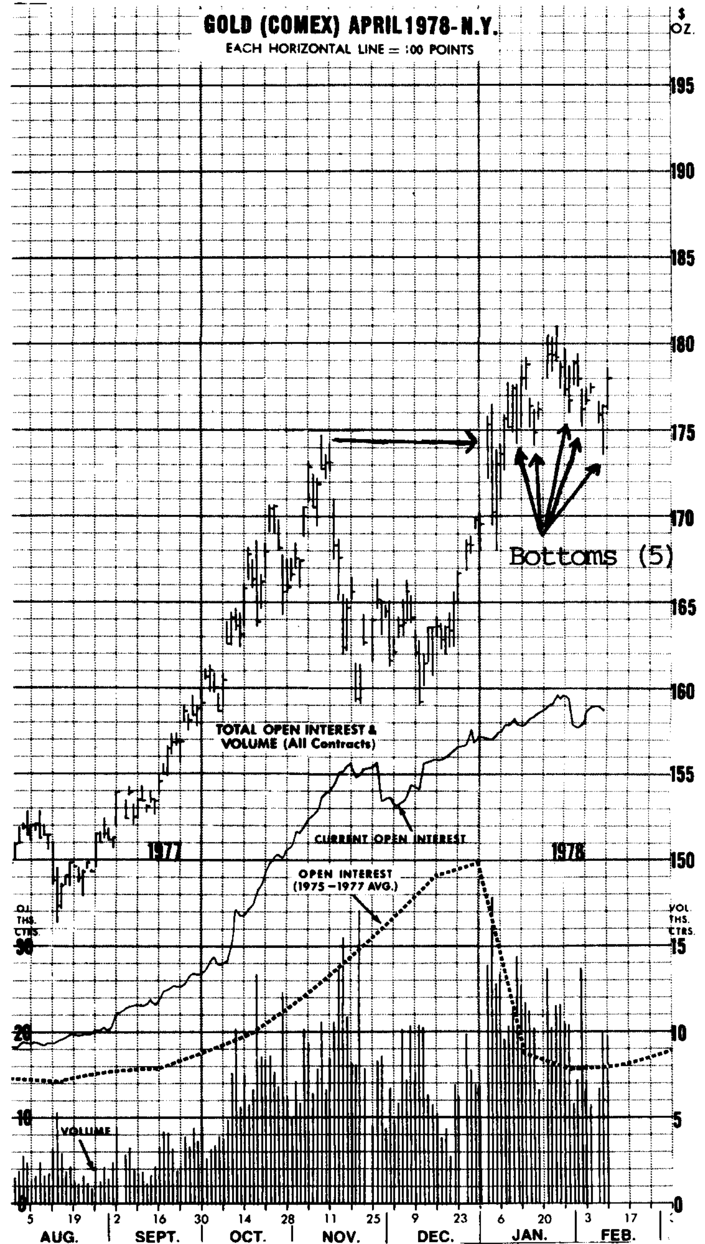
BOTTOMS

One can make a great deal of money in commodities if one is just patient. Waiting for a market to tip its hand as to its next major direction and having the courage to take a position is often all that is needed to profit. The gold market is a case in point.

From its August 1977 low, gold was in a bull market (from the perspective of this April 1978 chart). Prices were trending higher. Therefore, the correct assumption was that prices would continue to work higher. In mid-January when gold ran into resistance at the $180 level, the question was rightly asked, "Is this the top?" The $180 level was an area of historical resistance. However, one must remember that a major top is only formed once or twice a year. The probabilities favored higher prices. And there had been no change in fundamentals (no major reason the dollar should become stronger). The market corrected downward for two weeks, a normal amount of time for a correction. The correction was slow and sluggish (very apparent from watching the tape), and the correction kept wanting to hold at approximately the November highs. Very bullish. (See the 5 bottoms on the April Gold contract).

Now please look at the March Gold contract (on the next page). At each of the first four bottoms, gold had closed in the lower half of the daily range. Therefore, there was no indication that gold would move higher the next day, as it did in all four cases. From observing bottoms 1, 2, and 4, it became pretty obvious that a large number of sell stops had accumulated just below $173. Therefore, after bottom 4, it became critical to watch the next drop in prices. What would the action be when the March Gold dropped below $173? If the bull market was still intact, time was up for the reaction. Would buying overcome the tremendous selling pressure located just below $173 resulting from sell stop accumulation?

Bottom 5 resolved the problem as the market dropped just below $173, picked off the stops, and transferred ownership of gold contracts to strong hands. The ensuing strong rally on the day of bottom 5 (key reversal) with the close at the high of the day gave a trader a position to enter the market (on close) with a small risk of less than $200 per contract in hopes of higher prices.



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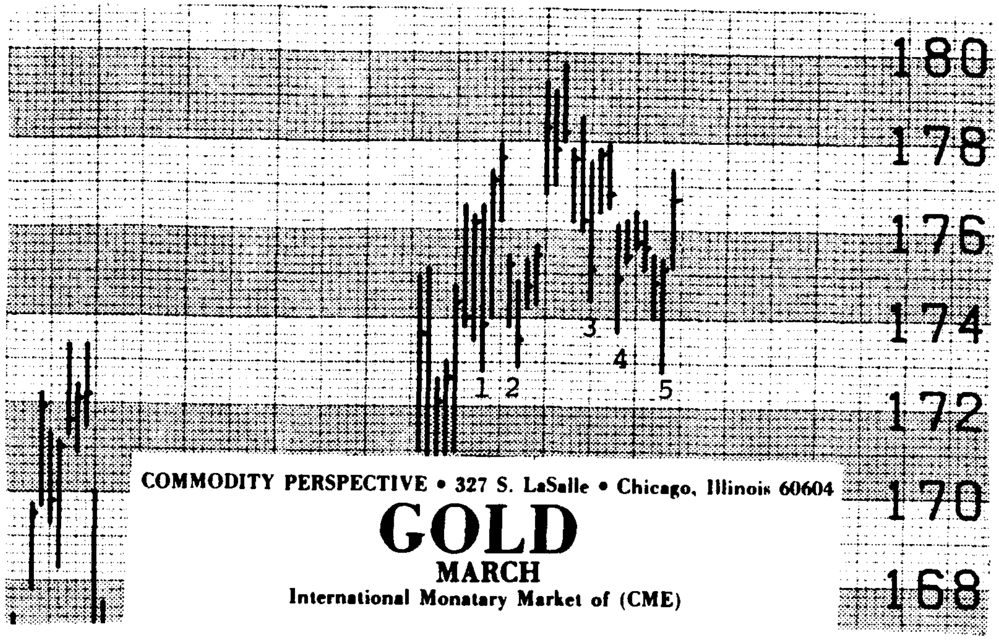

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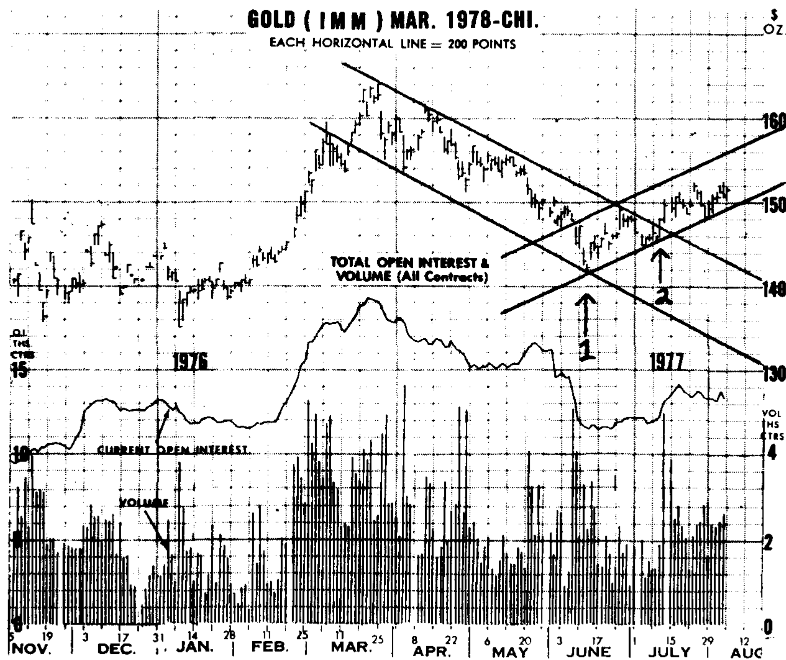
INTERSECTIONS

Just as automobile traffic is most active at road intersections, so too is price action volatile at the intersections of trend lines. Volatility is increased when the trend lines' intersection is also a channel confrontation.

Notice the chart of March IMM Gold 1978. From mid-March 1977 through early June 1977, prices trended down in a channel bounded by an upper downtrend line and a lower parallel. On June 14th, gold made an island reversal bottom. (Point 1) This served as an alert to a potential change in trend.

Following the reversal, gold trended up, forming two higher bottoms which composed an uptrend line. The upper parallel was above two tops which completed the upward channel. The stage was now set for the channel confrontation. On July 12th, (point 2) gold exploded up through the downtrend line on heavy volume and good range. The higher close, reversing the closes of 22 of the last 23 days was the point to buy, with the stop below the low at point 2. Thus, once the intersection conflict was resolved, gold worked higher within the now dominant upward channel.



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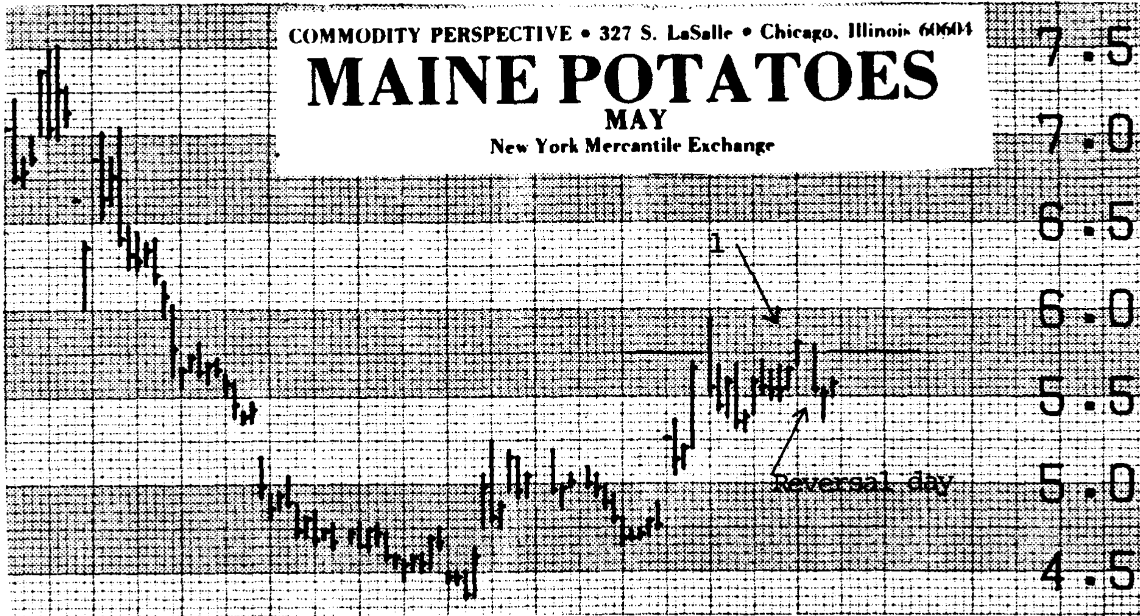
FALSE BREAKOUTS

May Potatoes gave a false breakout signal when the market closed above 5.8 on day 1. The correct technical play was to buy the breakout on close and then tighten up with a stop at 5.5. If prices moved higher, one could ride the move. If prices broke down, then one had a close stop and could absorb a small loss, which is what occurred in this case.



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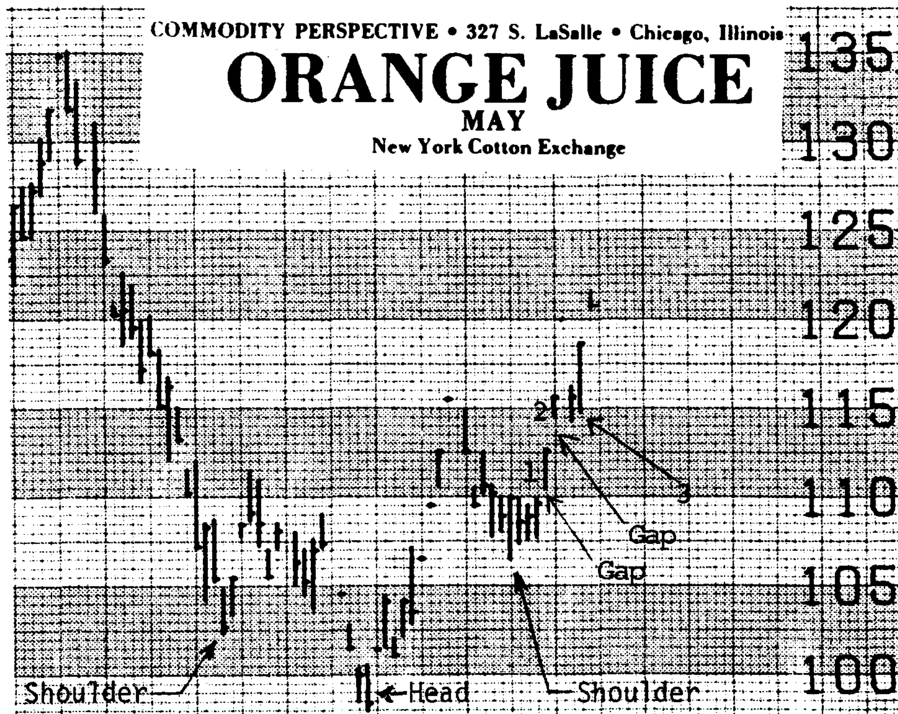
GAPS

The May O. J. gave traders an indication that higher prices were in store. On day 1, prices gapped up from an inverted head and shoulders formation and closed at their high of the day. The next day prices gapped up again (day 2) indicative of even greater strength. The small correction on day 3 which partially filled the gap and then reversed to close in the top half of the daily range was a sign of significant strength. Technically, the best place to have gone long was on close day 1 or on close day 3.

There was one other indication of strength which is not obvious from the chart. Day 2 occurred on a Monday. Price action during the entire week did not fill the gap between day 1 and day 2. Therefore, on a WEEKLY CHART, the market gapped up. It is very rare to find a gap on a weekly chart, but when one does occur, it almost infallibly forecasts higher prices.



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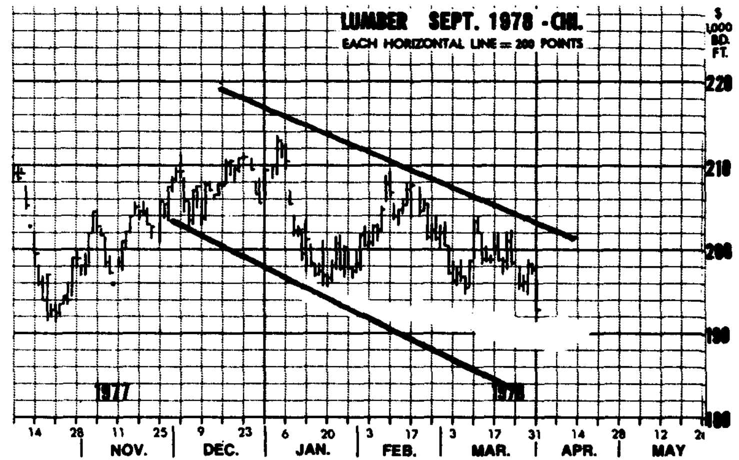
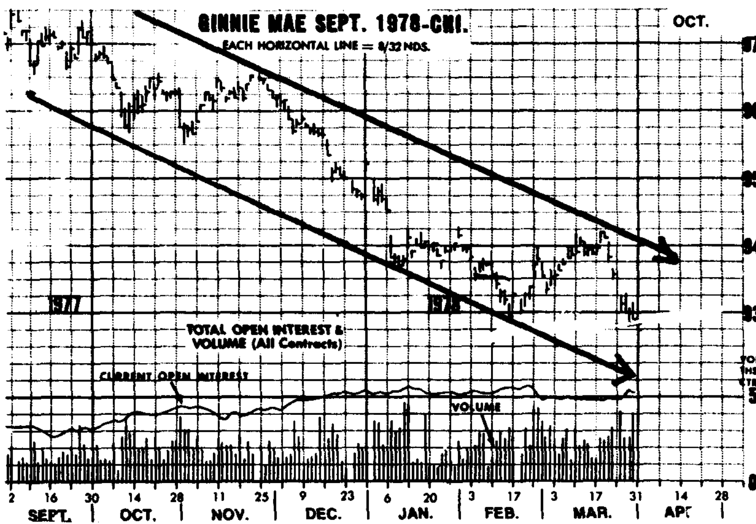
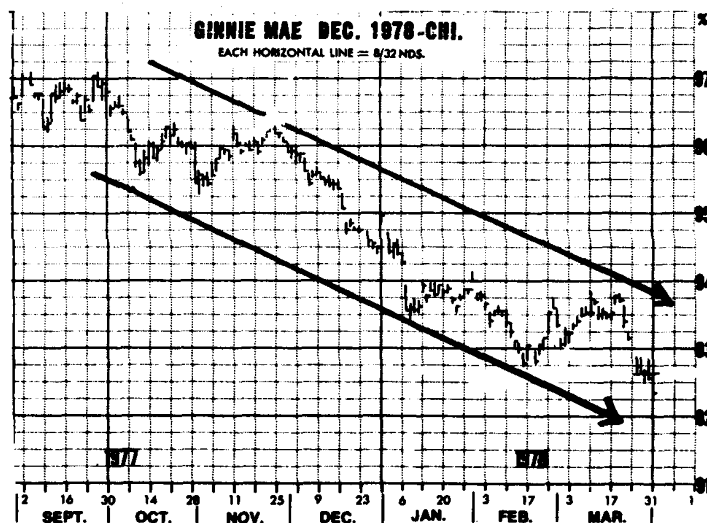
Please notice the September 1978 Ginnie Mae contract and the December 1978 Ginnie Mae contract. They are both moving along nicely in down channels. True, the December Ginnie Mae contract is at a lower price level than the September contract, meaning that the markets are anticipating higher interest rates later this year in the mortgage markets. But, the point here is that both contracts are working lower.

Now, notice the September Lumber contract. It too is working lower in a channel, not unlike the down channels in the Ginnie Mae contracts. The Ginnie Maes started working lower in December and January. The Lumber prices broke in January after a December peak. For the most part, February and March were unsettled months in the Ginnie Mae contracts. So too, during the months of February and March, Lumber was unsettled. Is there a relationship between Ginnie Maes and Lumber? Of course.





Lumber is used for construction. Nearly all construction in this country is financed. Higher interest rates discourage construction. Therefore, with higher interest rates (lower Ginnie Maes) less lumber is required for less construction. So the demand for lumber falls, and the price falls as well. Pretty simple. A trader just needs to remember that when he is considering a trade in either Ginnie Maes or Lumber, it is worth a few minutes time to check the "other" commodity to see if there is harmony of movement. If harmony does not exist, then one might be well advised to reconsider the trade.



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FLOOR TRADERS' PERSPECTIVE

The February 1978 COMMODITIES had an interesting interview with some floor traders. For those of you who have been infatuated with the pit activity, a copy of this issue is highly recommended. Some points made by the floor traders that have been emphasized in previous REAPERS bears repeating: 1. The opening price is important. Where a market opens compared to the previous day's close is critical, and often determines the day's direction. For example, when a market was up the previous day (higher highs, higher lows, higher close) and then opens below the range (lows) of the previous day, watch out downside. There may be a gap filling rally, but then the market should work lower the rest of the day. 2. Floor traders are scalpers. They don't care if they are trading a soybean or a tomato, or what the difference is between them. They just want in and out. They trade numbers. Good point. The only fundamentals most commission house traders really need is just a broad overview of the situation. If one considers all commodities the same, numbers if you will, he is better off, less emotionally involved. 3. It only costs the floor traders pennies to make an in-and-out trade, while it costs commission house traders $40-50. Conclusion — in-and-out trading will financially ruin the commission house trader. 4. Trade with trend. If the market is moving higher, buy. If it is moving lower, sell. One must keep a clear perspective on what one is trading — a short-term, intermediate, or long-term trend, and where the two will come into conflict if at all. Example. The major trend may be up and the intermediate trend down. Knowing where one stands is critical. 5. Trade against the commission houses. When all the activity (buying) is done by commission houses that is bad buying, bad company. Floor traders will trade against this crowd and often make good money (80% of the time). 6. Traders are their own worst enemies. The greed and fear of trading brings out the worst in people. Personal faults lead to destruction. That is why the market is so difficult. One must deal with oneself before dealing with the market. Consistent with this strain of thought, one's trading method must be consistent with one's personality. 7. The number one thing in commodity trading is discipline, and that means primarily not getting stubborn, and instead, taking a loss when one should, and not letting the loss get larger. The flip side of the coin is to be a defensive trader, go the guerrilla warfare route. Hit the market and if things go for you, fine. If not out. Gather up the marbles to play another day. 8. Let the market do the work. Follow it. Don't try to pick highs and lows. Sell new lows, or buy new highs, or buy reactions after new highs. 9. Only trade the number of contracts that are comfortable. When one is in too heavy, one's judgment becomes distorted and then the market has won. When a trader stops seeing the market as a game to be played correctly, but instead, as dollars per tic, the market has won. 10. The 50% correction point is important. If a commodity rallies from 20 to 30, the reaction usually carries down to 25 before the rally is continued. 11. Count on losing money on 7 out of every 10 trades. Count on it. By taking bigger profits than losses, one will make money. 12. Always use stops to get out of the market. If that stop is not in the market, the emotion of the moment will overwhelm most traders and lead to larger losses. The best decisions are made at home, or when things are quiet. 13. Money management is critical to success. Never reverse pyramid, that is to say, never buy 3 contracts after earlier buying 1. Instead buy 3 first, and 1 later. 14. Don't try to get in and out of the market quickly. That is the scalper's game, and they will win the contest. 15. Be patient. Wait for the good trade. 16. Leave stops in the market. 17. When the story is on the front page of the WALL STREET JOURNAL, the move is over. It is the old story, "Buy on rumor, sell on news." 18. Once a bearish report is out, and all the selling has been done, if the market rallies, expect the trend to then be up. 19. Bear markets are easier to trade and safer. The public doesn't know how to sell short. Bull markets, where the public is heavily involved, usually have a good many reactions, sharp reactions downside (panics). Bear markets erode and only have a few sharp rallies.

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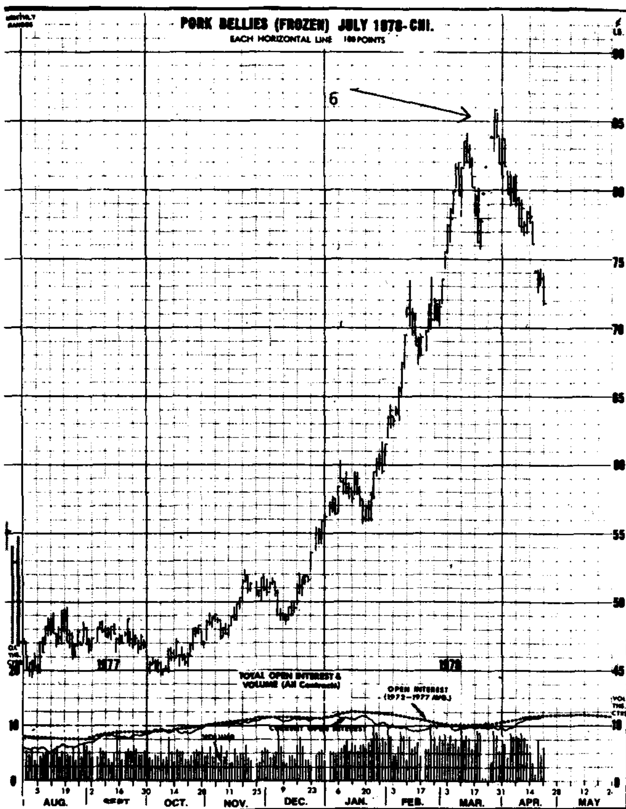
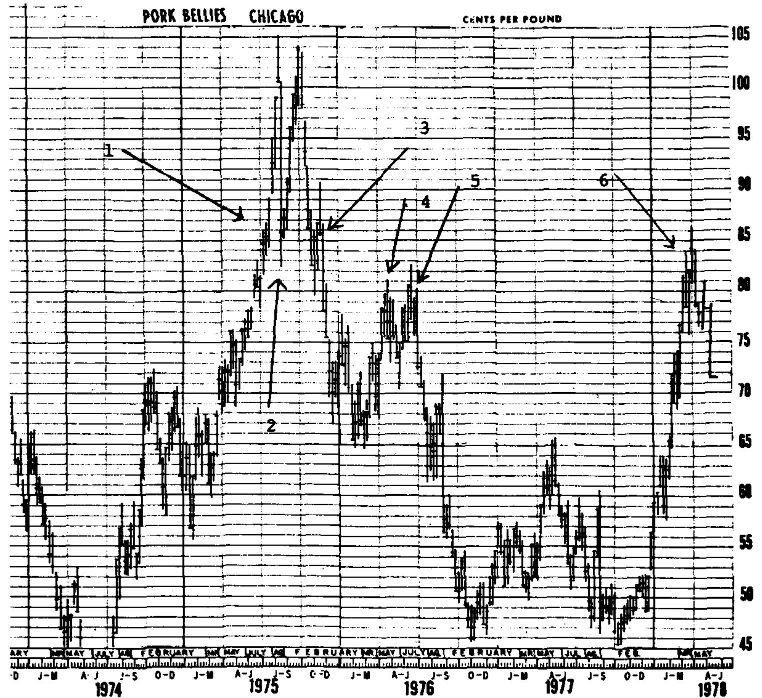
ANTICIPATING PROFIT TAKING ZONES

The March 3, 1978 REAPER projected an upside target in Pork Bellies of 80¢. The March 10th REAPER projected the target to be 80-84¢. The last week in March, Bellies topped out at 86¢. The Commodity Research Bureau Weekly Futures Charts aided one in anticipating the profit taking zone.

Pork Bellies are an extremely volatile trading market, a technical market too. Therefore, historic support and resistance is more meaningful in the Bellie market than it is in some of the more "cash sensitive" markets. From the Weekly Futures Chart (6 arrows), it is obvious that during 1975 and 1976, the last time Pork Bellies traded at this level, the 80-85¢ level was critical to the price action. Arrow #1 — 85¢ was the break away level. Arrow #2 — 82¢ was a significant low. Arrow #3 — 85¢ was a level of important congestion. Arrow #4 — 80-81¢ was a significant top. Arrow #5 — 80¢ was again a level of significant resistance. Arrow #6 — The level of the latest price action, again showing resistance between 80-86¢. Sure enough, the market backed off from this important resistance level as can be seen on the accompanying daily bar chart of July Bellies (Also labeled Arrow #6.)

Therefore, if a trader had been long in the Bellie market, by looking at the Weekly Futures Chart and the confirming double top on the daily charts, one had good sound reasons for taking profits between 80-85¢.





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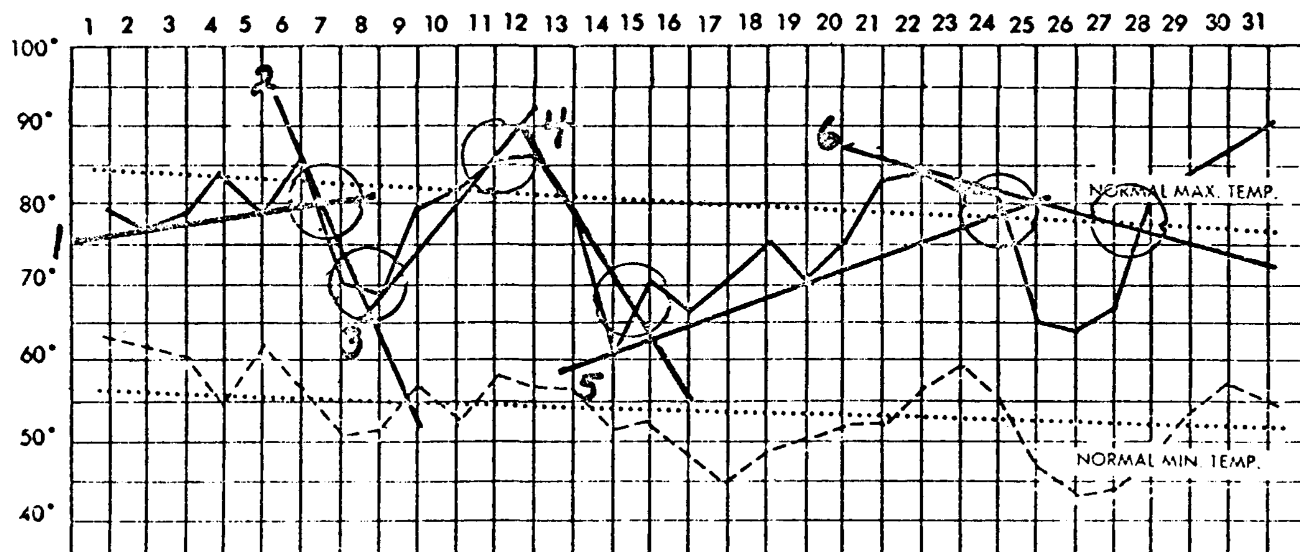
JUST FOR FUN

Once one is a captured student of charts and technical analysis, it becomes automatic to do a quick overview of almost any presentation made on a "time/price" graph. Notice below the temperature graph for the month of August 1976 in Spokane, Washington. Using a simple trendline analysis (Trendlines are numbered 1-6), one could have bet on temperature changes and bought and sold on trendline breaks very profitably. (The circled areas are where one buys and sells.) It is interesting to ponder who would be the better forecaster of temperature change — the "fundamental" meteorologist or the technician? That should be an interesting study someday.

By the way, technical analysis works with wood grains, and profiles of mountain ranges also. One other study was particularly interesting. Linda Banks, a pseudonym, is the wife of a good friend in Denver, Colorado. Thank goodness for her sense of humor. Invited to her home for dinner one evening, I was immediately attracted to a graph on her refrigerator — a time/weight graph. Linda was on a diet. She had judiciously reduced to the 117 lb. level but had absolutely no success breaking through 116. A technical analysis was made of her graph. To her alarm, it was noted that she should expect a gain to the 119 level, then shortly breakout at 120 for a run up to 128. Long term upside projection 140-145 lbs. That was the abrupt end of the analysis!

Two weeks later, Linda gained to 119, and then rushed through 120. The next week she went to the doctor, and to her absolute surprise, discovered she was pregnant. After all was said and done, a year later, Linda confirmed her peak weight was 143 lbs.



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