

My Approach to Trend Trading

By

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Equity Market Theory

- Dow Theory
- Elliot Wave Theory
- Efficient Market Theory
- Random Walk
- As many theories as there are traders
- Most traders trade using a system
- A system is not a market theory



Why Develop a Theory?

- Is market theory a waste of time?
- It provides an insight into what may happen in the future
- It is not a guarantee that it will happen
- It provides a probabilistic frame to interpret market behaviour
- Theory can be applied to a trading system



My Theory

- Markets do behave in patterns
- Each market is different
- Equity markets do display certain characteristics
- Short term versus long term
- The wise and experienced versus naive and reckless
- Many traders in the market may not necessary have a lot of market experience especially given the 'booming' equity markets
- There is a distinction between traders and investors



My Theory

- Wise and experienced accumulate knowledge
- Theory evolves from observations over time
- Time and Measurement Factors
- How long is long enough?
 - Days, Years, Decades, Centuries?
- Schumpeter studied long term economic cycles
 - Decades or longer may be required to observe repeatable cycles
- Visit [Harry S Dent website](#) for a snap shot into future

My Theory

- Data availability
- Data consistency
- Long term consistent series – DJIA, ASX...
- Analysis of the data series
- Linearity versus non-linearity
- Semi-log chart scales to adjust for non-linearity
- What observations are my observations based on observation of DJIA 1900 - 2007



My Theory

- Complex Adaptive Systems...not mine BUT
- Markets are never constant but always adapt and evolve like colonies of ants
- Price activity forms channels
- Complex phases are sustainable and relatively stable eg. Examples ASX & DJIA
- Transitional phases are volatile and unsustainable and are by definition dangerous and difficult to exploit

CAS Trading Techniques

- During boom phases
 - Speed/resistance fans
 - Trend lines
 - Channels: regression, Pitchfork etc
- During transitional phases
 - Elliot Wave Counts?
 - Why take the risk?



My Trading System

- Support and resistance
- Moving average band
- Price and volume break out
- Momentum based
- Fibonacci trading levels?
- Primarily just price and volume
- Can be applied to long/short trending and non-trending markets?

My Trading System

- Weekly system
- Money management
 - 2% capital at risk
 - Maximum of ten trades at any one time in any one trading system portfolio
 - Trailing stop loss

My Trading System

- Entry on Monday's when:
 - Price above Entry Band (Cameron) and
 - ROAR (Hull) greater than 10% or either of the two

Plus:

- Initial High (Wilson) within last month
- But must be supported by higher volumes than normal
- Not convinced that sophisticated entries are much value
– keep it simple

My System

- Exit on Monday's open when
 - Price falls below trailing moving average stop
 - Profit target?
 - Let your profits run confirmed by back testing
 - Cut your losses quickly not necessary confirmed by back testing in trending markets but only for the brave
 - Setting stops too tight significantly reduces the profitability of the system



Application of BullCharts

- Development and optimising of custom moving average band parameters
- Weekly scan to identify trending stocks
- Watch list used to monitor
- Extensive back testing using Tradesim to establish significant parameters and then optimise
- Refine and simplify system
- Presentation and colour seem are important to me BUT may be a waste of time to others

Application of BullCharts

- Monte Carlo simulation
- ROR >40% over 5 year period using ASX300
- Winners greater than 65%
- Average winner to average loser ratio \$5:\$1
- Minimum capital draw downs
- Sampling technique (ASX300) is self fulfilling
- Filtering the All Ords to remove bias in sampling technique may be problematic



Application of BullCharts

- Yet to test on consolidating markets
- Tested for short trading and looks promising except key parameters need to be modified
- Test more sophisticated profit exits (Tradesim expertise?)
- Line studies based on similar framework and perhaps more elegant (Standard error channel, Regression channel and Andrew's Pitchfork)
- Systems that match your own personality, what does that mean???