The following S&P day-trading strategy was related to us by Steve Kane, who was a fellow speaker at Fred Brown's Technical Analysis Conference in Austin, Texas, in 1990. When we returned from the seminar, we started watching the system and we have been encouraged by its effectiveness over recent data. Here is how it works:

1. Determine the trend using one-hour charts. Trade only when the hourly chart has made a higher high or lower low within the last two hours. When the trend is up, look for buy signals only. When the trend is down, look for sell signals only.

Entries: Use a five-minute chart with a 12-period slow stochastics.
Buy when the %K (the faster moving line) goes below 20 and turns up. Sell short when the %K goes above 80 and turns down. (Don't forget to trade only in the same direction as the hourly trend.)

3. Stops: Use an initial stop of 100 points, or put a closer stop just beyond a recent trading range. When the trade is 100 points ahead, it is a good idea to raise the stop to break even.

4. Exits: Take profits when the %K hooks in the opposite direction from +80 or -20. Another strategy is to watch the one-minute stochastics and exit whenever there is a divergence against the current trend. (See Exhibit 5 & 6.)

Steve had a few additional comments worth passing along. He has observed that, when the %K entry signals are also divergences from the price action, the resulting moves are particularly strong. He also suggests that, when there is a very sudden profit move of 100 points or more, it is often a good idea to take the profit immediately. Finally, he cautions that, whenever there are two consecutive losses in a day, it is time to stop trading and try again tomorrow. This is good advice for almost any day-trading method.

We like the idea that this is a method that buys dips in an uptrend and vice versa. We also like the idea of buying when
Hourly chart is trending up at time of signal.
ONE-MINUTE HARTS
WITH STOCHASTIC

This is a day-trading method developed by Humphrey Chang, a trader and former futures broker in California. Humphrey explained that the method works best for day trading S&P futures, but mentioned that he sometimes uses it for day trading yen and Swiss franc futures. Here is the method:

1. Use one-minute bars for the S&P futures and a 21-period stochastic.

2. One of the most important rules is that entries are done only in the first hour of trading. After the opening, wait until both stochastics lines go to an extreme level (above 80 or below 20) and then cross. Enter as quickly as possible after the cross. Ignore all other stochastics signals after the first hour.
3. Trail stops using swing patterns. Look for patterns of higher lows, or, if you are short, look for patterns of lower highs. Humphrey cautioned not to have any stops at the exact high or low of the day. He has observed these are points that the floor traders are watching and seem to raid as frequently as possible.

4. The trade is left on until stopped out by the trailing stop or exited at the close of the market. (See Exhibit 7 & 8.)

Humphrey suggested that the method can be made more reliable by trading only in the direction indicated by the half-hour stochastic with 14 periods. For example, if the half-hour %K is above the %D, you would use the one-minute stochastic for buy signals only.

EXHIBIT 7

1-Minute S&P

Initial Stop

Enter

Trailing Stops

Stopped out at $s_6$ for a nice profit.
21-Bar Slow Stochastic

Crossover Signal

Remember, enter only if the signal occurs in the first hour.

8:45 9:00 9:15 9:30 9:45

0 25 50 75 80 100
As we have explained in our previous chapters, we don't believe in the general practice of forecasting specific prices. However, if enough people use exactly the same method and wind up looking at the same forecasted prices, perhaps they do start to have some predictable impact on trading.

We suspect that the popularity of these pivot points is causing them to act as self-fulfilling prophecies. The formula for figuring pivot points (or support and resistance levels) was explained to us by one of our newsletter subscribers, Neal Weintraub, author of The Weintraub Daytrader and a floor trader in Chicago, who conducts some unique training seminars for traders, which he calls "Commodity Boot Camp." Neal explained to us that the formula is very widely followed, particularly by many floor traders who make a note of the
pivot points before entering the pit each day. Neal suggested that knowledge of the calculations might be especially useful for S&P traders.

We start the pivot point calculations by adding together the previous day's high, low, and close. Then we divide by three to get an average price. Example:

Yesterday's high = 365.30
Yesterday's low = 361.30
Yesterday's close = 364.40
Total = 1091.00 divided by 3 = 363.66 avg. price)

Now to find today's pivot point high (or resistance level) we simply take the previous day's average price, multiply it by two, and then subtract the previous day's low. Example:

363.66 (yesterday's average price) x 2 = 727.32
727.32 - 361.30 (yesterday's low) = 366.02 (expected pivot point high)

Next, to find today's pivot point low (or support level) we simply take the previous day's average price, multiply it by two and then subtract the previous day's high. Example:

363.66 (yesterday's average price) x 2 = 727.32
727.32 - 365.30 (yesterday's high) = 362.02 (expected pivot point low)

These numbers represent the nearby support and resistance levels that for many years have been very widely circulated among day traders and floor traders. Since they are not chart points but are calculated numbers, the chartists will probably see them only after the fact, while the floor traders have the numbers noted on their trading cards.

Neal goes on to explain that we can carry the calculations another step further if we want and calculate a "highest high" (or extreme resistance point) as well as a "lowest low" (or extreme support level).

To calculate the highest high, we take yesterday's average price of 363.66, subtract the expected pivot point low of 362.02, and add the expected pivot point high of 366.02.

Our answer, 367.66, might be a good target on the upside if the resistance at 366.02 is broken. It would also indicate the next possible resistance level as the market advances.

To calculate the lowest low, we take yesterday's average price of 363.66, then we subtract the difference between the expected pivot point low of 362.02 and the pivot point high of 366.02 (a difference of 4.00).

Our answer of 359.66 represents a possible target or low point on the way down if our first support level of 362.02 doesn't hold.
We used real numbers for our examples, so we couldn't resist checking the S&P after the close to see how we did. The low of the day was 362.10 versus our projected pivot point low of 362.02. Not bad. (Sep S&P 6-21-90)

Again we caution that we think these points only work because they are popular and that popularity may be short-lived. If they should stop working for a while, because of some more important factors, they may never work again and you can throw this method away forever. On the other hand, if more people follow them, as time goes on they will work better than ever. In the meantime, we thought they were an interesting phenomenon worth passing along. We would be inclined to give more weight to the nearby numbers than to the "highest high" or "lowest low" calculations.
PRICE GAPS ON OPENINGS

At a meeting of the Technical Analysts of Southern California in 1989, Bruce Babcock, Jr., was the guest speaker and described a day-trading strategy that he was developing. Bruce is the publisher of Commodity Traders Consumer Report and author of several commodity trading books. His book, The Dow Jones-Irwin Guide to Trading Systems, which has been referenced here many times, contains a great deal of useful information, and we recommend both his book and his CTCR newsletter to our readers.

Here are the highlights of the day-trading strategy that Bruce described to us:

1. Trading nearest month S&P futures, wait for an opening price that gaps noticeably from the previous day's close. You will then be looking for a trade in the
direction of the gap. If the opening price gaps up, look for an entry on the buy-side. If the opening gaps down, look for an entry on the sell-side.

2. Tack on a few points above or below the opening price range and enter the market on a buy stop or sell stop as the market begins to trend in the direction of the gap.

3. Use a stop loss of about $500 and exit the trade on the close. (See Exhibit 9.)

Bruce was probably intentionally vague about defining some of the instructions in specific terms. His gap strategy can be tailored to suit your individual trading style. Bruce indicated that he had done a considerable amount of testing with various gap and follow-through parameters. Generally, the bigger the gap and the more points you tack on to the opening range, the more likely you will be to have a winning trade. However, waiting for bigger gaps and more follow through means fewer trades.

Remember, profitable day trading requires high volatility, so we advise keeping the parameters toward the higher side, rather than the low side. That way you will be trading only after the market has demonstrated some volatility. As a starting place, try waiting for gaps of 75 points and tack on 25 points for follow through, if you want more trades make the numbers smaller; if you want fewer trades, make the numbers bigger.
RSI DIVERGENCES

Here is a simple day-trading method that uses a short-term RSI to find potential tops and bottoms in the S&P market. It is a logical approach that should work in any market and could be modified to use in longer-term trading as well. It is one of our favorite day-trading strategies for someone who does not need a trade every day. This method may go several days between trading signals, but, when the signals occur, it has a better winning percentage than some of the more active strategies. Since it doesn’t trade every day, it could be a supplemental method to be followed in addition to a more active system. This method works best when trades are signaled in the direction of a longer-term trend. When there is no prevailing trend, the signals can be taken in either direction. You might want to review the use of ADX as a trend-measuring tool. When the daily ADX is rising, the day trades should be