Trending vs. Volatile Markets
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its run until the trend weakens or time begins to run out on our option. During a volatile market, we need to be prepared to take money off the table at the first sign of weakness, or even sell into strength.

When trading short-term trades, I like to use a short-term moving average on my charts to help me know when it's time to get out. I typically use an eight-day moving average (MA). If the stock is going to close below its eight-day MA, then I will exit the trade before market close. Usually this decision is made in the last hour of the trading day.

You can also use the highs or lows of the day to determine if the momentum is slowing. If you are in a call or bullish position, the stock has run up and the intraday highs continue to be higher each day, you may wish to stick with the trade until the intraday high of the current day will not exceed the previous day's high. This is a sign that weakness is creeping in. When trading puts, or using bearish strategies, the opposite is true. If a stock cannot reach a new intraday low that is lower than the previous day's low, then it may be time to exit the trade.

Stop losses should be set for calls just below the intraday low of the day you entered the trade. Stop losses for puts should be set just above the intraday high of the day you entered the trade. If the stock is going to close below or above these figures, exit the trade. No questions asked. Move your money into a better trade. Cutting losses is the one thing that all profitable traders do well.

I read a quote from a famous trader named Ed Seykota in *Market Wizards* by Jack D. Schwager. Ed Seykota said, "There are three elements to good trading, and they are: (1) cutting losses, (2) cutting losses, and (3) cutting losses." He said if you follow these three rules you may have a chance. I guess he thinks cutting losses is pretty important. If a trader had ten trades, lost on five trades, and won on five trades, is it possible to make money? Yes. If you had even dollar amounts invested into each trade and cut your losses at 20% on the five losing trades, one winning trade that doubled in price could take care of all five of the losing trades. Hence, the remaining four trades would be pure profit.

Here is an example of a short-term momentum trade that I recently placed on Broadcom (BRCM). On May 5, 2000, I watched BRCM hit a resistance level of approx $182.50 and then roll over to the downside. The resistance level was a prior support level for the double top that formed in mid-March. I purchased May 180 Puts at $10.75. The stock was trading at $178.75. My mental stop loss was placed at $185, just slightly above the resistance level. After falling for three days to the $144 range, the stock bounced up slightly and I sold my puts for $24 7/8 on the morning of May 11, 2000, with the stock trading at $147.50. Less than five full days and I more than doubled my money!

So, to take advantage of volatile markets, shorten your trades to approximately one to five days in length, select in-the-money strike prices, take profits at the first sign of weakness, and cut losses short. Remember, trading requires concentration. Stay focused; be patient and selective with your trades. Preserve your capital so you can take advantage of better trading opportunities. Remember, longevity in the market is the mark of a good trader!

Sean attended the Wall Street Workshop™ 14 months ago and has attended several of the SUPPORT™ classes. Sean recently left a 13-year career in the automobile industry and is now trading for a living.

Chart for trade reference.
BRCM. Telechart. Zoom #4. Horizontal resistance line drawn from mid March to early May at approx 182.50 level. Chart also shows 20 day and 50 day Moving Averages. I normally use Volume as the only other indicator in the lower window of the screen. Bar style chart.