Tactical Trading Method – Day Trading And Trading Indicators

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Day Trading And Trading Indicators

Indicators And Learning To Trade

Learning to day trade as an indicator trader is very typical. After all, how are you supposed to initially learn how to trade? Trading indicators are available to anyone who has a charting program, and simply using line crosses, or histogram color changes, provide 'easy' signals to understand.

However, being an 'indicator as trading signal' trader only, becomes what I have seen to be one of the primary 'sticking' points in the progression of learning to trade, as you come to find out that you are unable to profitably trade indicators as signals only.

Indicators can be very useful for trading. If you will also take the time to learn the basis behind your indicators, and learn what each indicator is specifically intended to do, not only is this a logical way to begin, it is also a good 'step' in your learning progression. Doing this will increase you understanding behind the WHAT-WHY of trading, -vs- simply attempting to create 'canned' indicator only trading systems, without any regard as to a reason that you are trading this way.

Indicator Types

Amongst all the indicators available in your charting program, there are essentially 2 basic types: (1) those intended to trade with price direction or what could be called 'trend following' (2) or those that are intended to trade against price attempting to pick tops and bottoms, or what could be called 'trend fading'.

Moving averages, either where price crosses the moving average or where 2 moving averages cross each other, along with momentum type indicators, are two commonly used 'trend following' indicators. Stochastic and price bands are two commonly used 'trend fading' indicators.

Particular Indicator Weaknesses

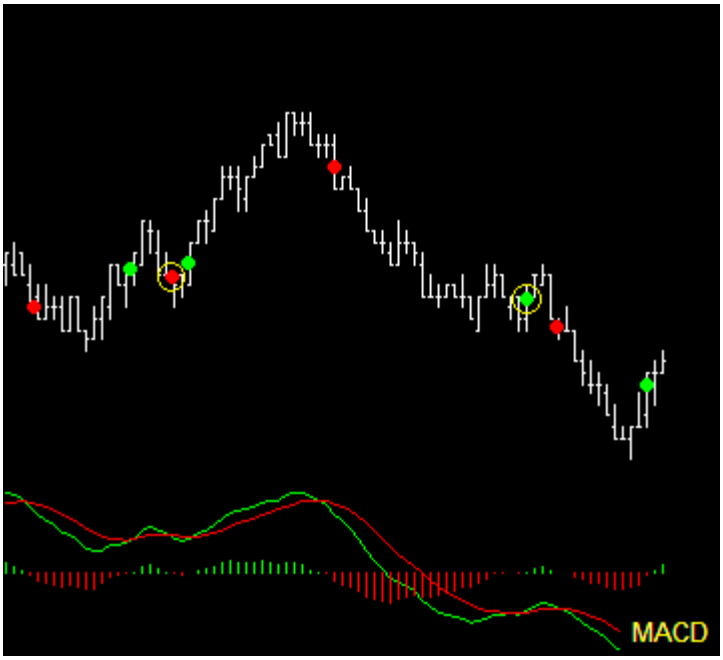
Indicators are time frame dependant - meaning that your indicators will trigger simply because of the speed of chart that you are using AND there may be little correlation with that speed and swing direction. This is especially the case when 'fast' charts that should be used for entry timing are also used for direction, but have no directional relevance.

Indicators are essentially useless in congestion and/or pauses in price movement - see weakness notes with the charts below.

MACD

This is a momentum type indicator, where a concept that momentum leads price is used for 'trend following'. The red-green lines are moving averages and the red-green histogram is the difference between the moving averages.

The moving average cross, or the histogram red-green 'flip' gives the signal - the dots on the charts are the corresponding trades.



Weakness

The specific weakness in a momentum indicator, or any indicator that triggers on a zero line cross or moving average cross, will be that it overtrades in congestion or pause in price movement.

You can see this on the chart AND the dots with the yellow circles, where a trade triggered during a pause in price movement and quickly reversed back - this will continue during an extended congestion period.

Stochastic

This is an oscillator type indicator, where a concept of overbought-oversold is shown by the red-green lines moving above-below the horizontal lines - this intended to show the top-bottom of a price swing and thus used for 'trend fading'.

When the lines move to overbought-oversold AND then cross and come back above-below the lines, the signal is given - the dots on the charts are the corresponding trades.

Weakness

There are 2 specific weakness: (1) when there is a pause at an extreme which causes a cross but no reverse, and direction resumes (2) when there is a reverse that doesn't move to the opposite extreme AND thus there is no re-entry for the 'bigger' move - see the yellow circles on the chart where there is a cross but not from an extreme.

Tactical Trading Indicators

WHY Use Indicators For Day Trading?

I have no inherent problem with trading indicators, nor do I feel that trading is diminished because indicators are used. Depending upon how indicators are used, and how they 'fit' the method being traded, using indicators as part of a trade setup have a number of important benefits.

The trading method is that of directional trading, a method that 'believes' that tradeable price movement starts from the 'center' AND with a build in momentum that leads to momentum expansion, moves to the 'outside' BUT when this is 'extreme' is reached, a reverse is not imminent. Instead, price can hold a retrace to trade support or resistance, stall, and then resume the previous move by building-expanding momentum again, leading to a higher-lower swing 'extreme'.

Trading indicators, as a component of trading method setups, give specific information while reading a trading chart - information that allows the chart to be read faster and more accurately than could be done without the indicators. The trading indicators being used have been developed and/or customized for this method of trading, and thus are an important component of the trading setup, again because of the specific information that they provide. As well, the indicators help give the right side timing or trigger to a setup trade.
BUT the indicators are NOT viewed as trading signals.

Tactical Trading Indicators

This chart is the same as the charts above with the MACD and/or stochastic indicator on them.

Notable differences would be those that may have been added to the price bars: trading bands -vs- price channels, and possibly moving averages which we don't use. Regarding the indicators below the chart, although we use an 'extreme' type indicator like a stochastic, the indicator itself is different, and the usage of the indicator is especially different.

Indicators On The Price Bars

9 period high-low price channels

direction-congestion indicator

Indicators Below The Price Bars

slow momentum - fast momentum

slow momentum flow - fixed range oscillator of slow momentum

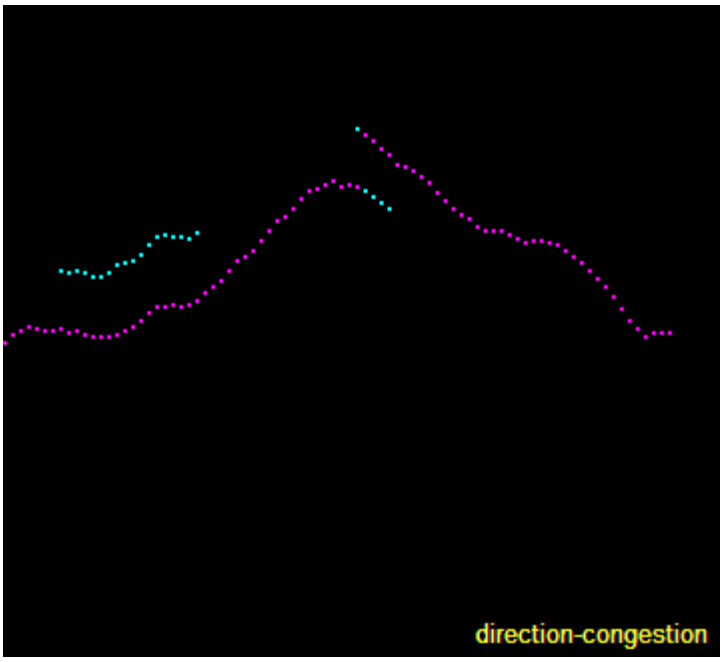
Direction-Congestion

The purple-blue dots have been located in the area of the price channels - the difference between using actual price and a channel indicator based on price.

The dot colors and whether there are single or double dots above or below price is not an arithmetic formula, but have been determined by a number of different 'conditions' that have been written in an attempt to define price continuation or price congestion.

The 'strongest' combination of conditions for directional trading gives single purple dots - on the bottom for long, and on the top for short.

This particular combination is similar to that of the price channels, but adds the congestion conditions to the indicator, in order to help 'filter' trades during this period.



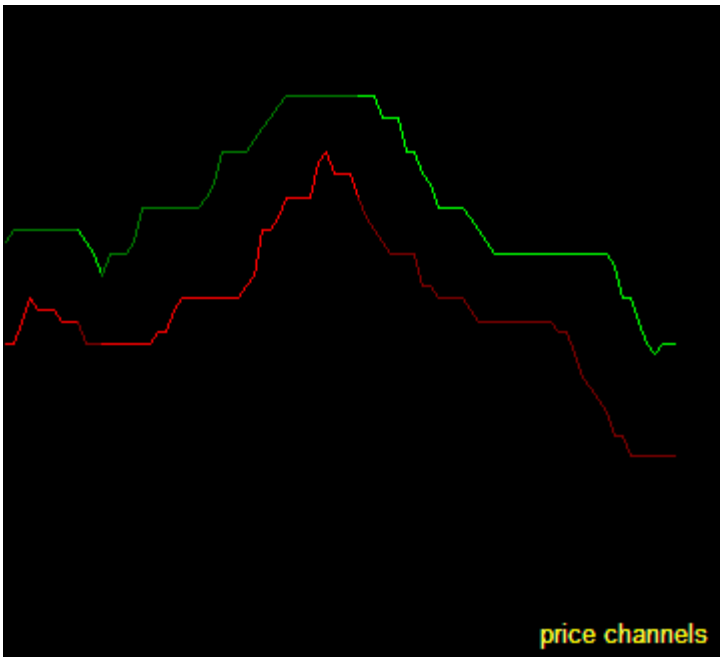
9 period high-low channels

The channels have been coded so that they are bright green on top after the bottom channel breaks and slow momentum is red - bright red on the bottom after the top channel breaks and slow momentum is green.

If this was traded as a mechanical system, I would be long when the channel was bright red and short when the channel was bright green.

As I am what I would refer to as a directional trader, this would work very well in markets that are a combination of longer continuation swings and shorter congestion periods, but would 'overtrade' and typically get chopped up during periods of extended tight ranges and congestion.

Consequently, I trade a method and not a system, in an attempt to eliminate certain trades during the periods that are the weakest for this 'base' indicator mode.



Fast-Slow Momentum

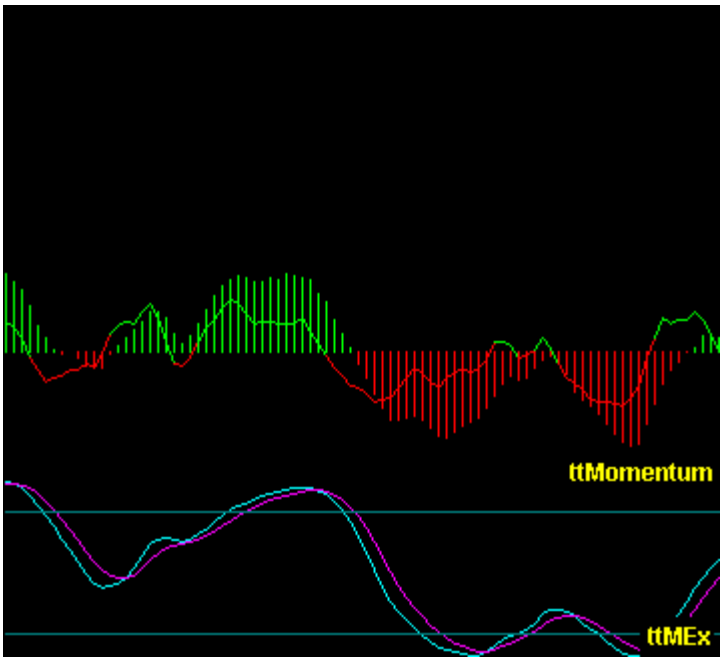
ttMomentum: I have used used the difference between moving averages instead of the actual macd or 'canned' momentum indicator. The histogram is the difference between a 23 period and 4 period, and the line is the difference between a 10 period and 3 period.

Remember that a momentum indicators is the 'worst' indicator that you can use in congestion as it will keep 'flipping' during what is clearly meaningless price moves.

Slow Momentum Flow

ttMEx: the purple-blue lines, and the indicator has been coded to 'force' slow momentum into a fixed range oscillator.

When I refer to momentum flow, I am looking at two things: (1) what is momentum doing when price is retracing (2) when does momentum resume and start to 'build' again during sideways or congestion periods.



Learning Through Trading Indicators

As mentioned above, trading with indicators is the typical way that most people start trading and/or continue to try to trade. Indicators are available through the various charting programs, and they are the easiest to 'see' trigger-signal a trade.

However, when I consider learning about trading through trading indicators, this isn't meant to be about learning when the indicators trigger. That is a 'simple' definition, for instance look at the paint bars on the charts below, they show when the indicators on the chart - trigger in combination. Instead, I am talking about learning the indicator strengths and weaknesses, and thus why all indicator signals shouldn't be traded. As well, I am also talking about learning how to combine the indicators 'into the trading method', for use as market-trading information, and for use as a base setup component - attempting to maximize the strength while minimizing-avoiding the weaknesses.

Initial Indicator Trigger

In order to get started doing this, I would suggest that a trader paper trade every initial indicator trigger BUT do so making notes about the market conditions-market type at the time of the trade. It is important to do this so the trades will have a different evaluation basis than simply win-loss. Instead, you will be evaluating the trades by win-loss as a function of the market conditions-market type, and by doing so start understanding trade discretion, and a repeatable reason for eliminating certain indicator trades.

Indicator Mode

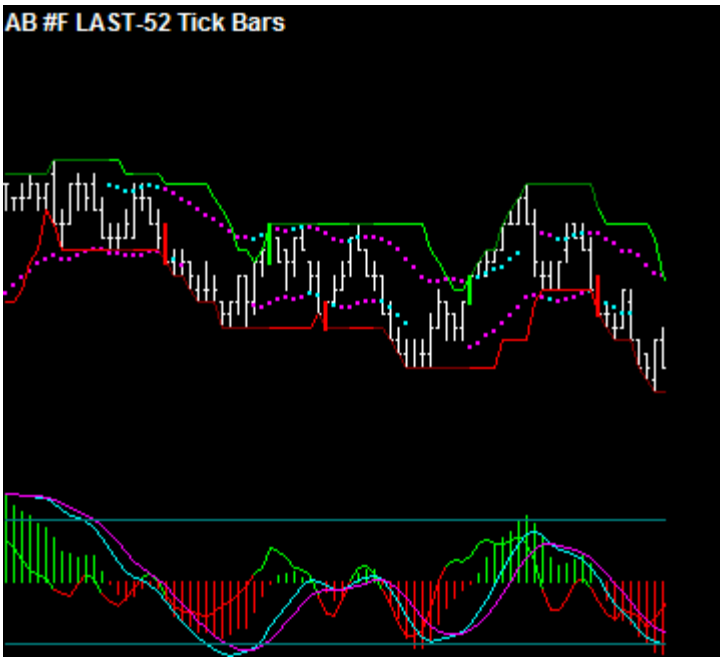
Another thing to do, in order to get away from viewing indicator triggers as signals, is to start viewing indicator triggers as indicator mode - where a sell trigger is 'sell mode' and a buy trigger is 'buy mode'. Once you have an indicator mode, you realize that your 'next' trade is going to be in the direction of the mode BUT only if additional defined trade setup components occur. This is a step intended to start viewing trade setups -vs- indicator signals AND in understanding the method concept of trade setup-trade trigger.

The first thing you will learn about indicator trigger trading is the trading problem-indicator weakness during congestion periods.

This will be a time where the indicators will continually trigger inside of very little movement.

The tighter the range AND slower the market - the worse that this trade 'flipping' problem will be.

consider: is there a way to combine the trading indicators with additional trade setup definitions - specifically related to the market conditions at the time AND avoid the overtrading?

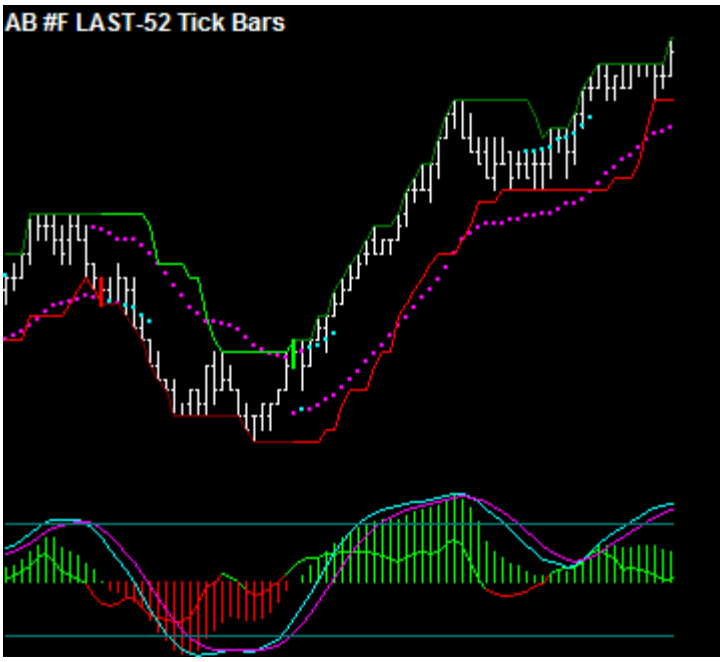


The second thing that you will learn about indicator trigger trading is the trading problem created when you don't take every indicator trigger.

Just as soon as you go through a period like the chart above where you take a series of losing trades AND stop trading - you will get a trading period like this where you would have had a small winning trade AND a very big winning trade.

What if you took every trade on these 2 charts, would you have been profitable? Yes, but unfortunately the profits came after a series of losers AND after a period where it became just too hard to retain the confidence in your 'indicator trigger trading system' to keep trading.

consider: is there a way to combine the trading indicators with additional trade setup definitions - where all indicator triggers will not have to be taken in order that the 'best' trades are not missed?



Indicator Setup Component

Consider the chart from above with the 2 winning trades - 2 trades that may have looked similar at the time as the chart with the congestion trades.

Neither the sell or buy were traded on the initial indicator trigger BUT neither of the gains available from the trades were missed either. This was a function of using the indicator mode as an indication of current trade direction BUT only if there was a base setup-trigger that occurred

.

In the case of this chart there was a base setup that occurred after the indicator trigger - in the case of the first chart there wasn't. NOTE: before you suggest that the first sell from the 'congestion' chart was a base setup - a triple break with a ttmf hook and mex flow down on the retrace - that trade was during consolidation after a big up move and 'shouldn't' have been done.

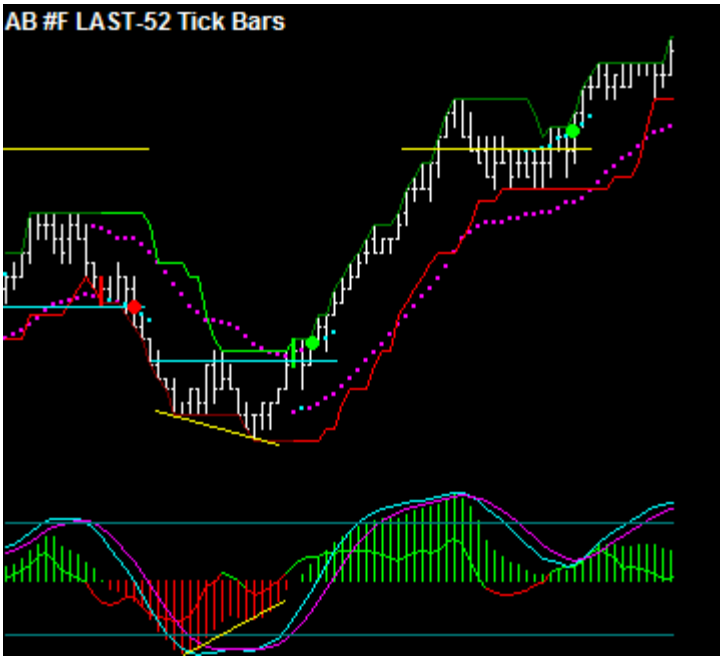
Price lines: (1) yellow line = left side resistance (2) top blue = centerline (3) bottom blue = support under the centerline AND key to shift to resistance if a sell was going to continue.

Market conditions-type: 2way period in an up market after there was a consolidation period that broke into a counter sell - the period low was a pmd in the area of left side support.

red dot: indicator reverse at the centerline - retrace to lower high WITH mex flow down - sell the blue line break2.

green dot1: pmd low then indicator reverse at left side sup:res - higher low with mex flow up BUT unable to trigger at the blue line.

green dot2: the buy break went to the area of the yellow line AND 'straddled' trying to hold as resistance-shift to support. the green dot was an addon timed as a break back above the line into the swing high - a trade with swing direction AND market direction.



Trading Indicators As Trade Setup Components

Trading Overview1

Compare this chart-trades with the same charts above using MACD or stochastic. Particularly note: (1) the indicators as a setup component -vs- a trade signal (2) the fewer trades during 'pauses' where MACD got whipsawed (3) the losing counter trades on stochastic which also didn't have a re-entry signal for the directional trade -vs- no losing counter trade + addon trade.

yellow circle: at this time the only indicator component that indicates a sell is momentum - dc is still purple dots on the bottom AND with regards to price - you can see the double bottom with the left channel. the actual situation is a hold of a left side buy.

green dot: the indicators have reversed back 'into buy' - since i am long any next trade would be an addon to that long AND to do an addon i want to be more selective - i want indication of breakout-continuation. i get that with a combination of: blue line break2 - with mex flow up on the retrace and the ttmf hook - into the 2 dark blue dots as the breakout setup.

red dot: this is an initial indicator reverse - there are no additional setup components involved in terms of price or pattern. i did this trade because the high into the trade was left side resistance that had rejected AND even though there was a buy that included an addon - this 'ended' at resistance of what was actually a bigger move down.

red dot2: this is one of our base addon setups - what is referred to as a right side reject/matched price failure - these prices are identified from the left. as well this includes a basic method concept that double hold - the 2 yellow dots AND triples break - the entry into/through the 2 dark blue dots. the entry is located at the matched price break AND is done with the ttmf hook.

particularly note the 2 dark blue dots WITH the yellow rectangles - these depict the very important method concept of trading into/through a breakout. key for continuation AND an important component of any addon trade.

Trading Overview2

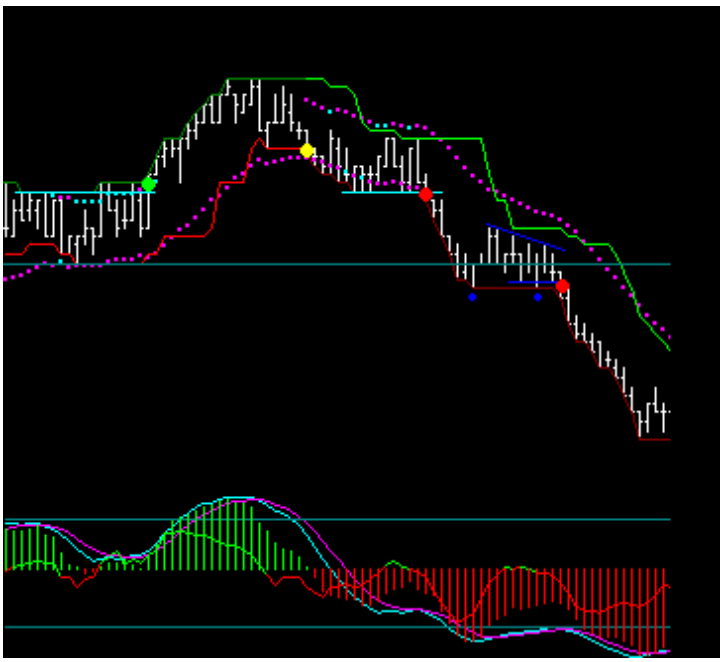
This chart begins with the market 'congesting', I can see this from the overlapping price bars AND I can see this from the direction indicator 'double dots'. The location that this is occurring at is significant to me, as the dark cyan line on the chart is the floor pivot trying to hold as support AND the blue line which keeps hitting as resistance, is a price line that I have seen from the left of this chart that has been both support and resistance, what I refer to as a price specific.

green dot buy: You can see the line has broke on 3 bars, and you can see that the histogram has gone green-red-green while in this sideways period - WHY is the green dot bought? While momentum is green there is also 2 bars which are higher lows AND then the flow indicator 'rolls back' - this becomes the timing of this 'ledge' breakout buy.

yellow dot sell: This is where the trading indicators reverse 'into sell' BUT at this time I do not have a sell setup coupled with the indicators - I might exit the buy if I don't chose to hold it back to support, but I do not have a sell yet.

red dot1 sell: The indicators have reversed, and price hits the blue line now as support, and then retraces to a lower high. I am now getting a sell setup to combine with the indicators - this includes the hit of the res:sup price into the lower high WITH the flow indicator continuing down, a double hold of the price channel [our method has a concept that doubles hold and triples break], and a hook of the fast momentum indicator - the red dot was then sold.

red dot2 sell: After short, price moves back to the floor pivot and stalls - actually it probably was bought by a trading method that I refer to as a mixed method, meaning that this method's typical setups are counter to our method - buying a pullback to the floor pivot would be one of these trades.



very significant in the decision to do a trade addon which will risk the gains of the initial sell, is a failure of the mixed method trade, meaning that there will be additional selling pressure as their counter buy is 'stopped' out, and the momentum of the directional trade resumes.