Where Speed, Service & Value Come Together
www.netfutures.com
NETFUTURES
Online Futures Trading

Phantom's Gift

Contents

Foreword
Preface
Phantom's Insight
Your book
A Little History
Preparation for Trading
Rule 1
Rule 2
Trading with Rules 1 and 2
Day-Trading
Options
Cloud Hopping
Behavior Modification
A Wink Is As Good As a Nod to a Blind Horse
Quicker Than the Eye
Your Comeback After a Big Drawdown
Is the Market Always Correct?
Rule 3, You Say?
The Third Rule
Tie Ribbons on Your Trading
A Few Questions for Phantom
Trading and Three Aircraft Accidents
My Order Was Filled...Where?
Your Trade Program

Phantom's Christmas Gift
Time to Reflect on God's Rules
Addendum:
When We Lose One of Our Own
By Harold B. Simpson
About the author

Phantom's Gift

Foreword

When *Futures* magazine started the "Futures Talk" forum on its web site in the middle of 1996, it attracted some good interest initially -- nothing too spectacular but just traders talking to other traders about markets and comparing notes. But beginning in the Spring of 1997, it became increasingly clear that one participant had unusual trading wisdom and insight and experience, although he sometimes wrote in a vague, mystical way that forced other traders to really think to get his point.

His posts became so popular and attracted so many responses and followup questions that separate threads were set up just for his comments. He was willing to share what he knew about trading exclusively on the *Futures* magazine forum, yet he did not want his identity known under any circumstances and he did not want the money or accolades that he might have gotten from revealing his ideas. Thus was born the "Phantom of the Pits."

From his participation in the forum and the acceptance of his ideas by a growing number of loyal followers came this "book" summarizing some of his thoughts. "Phantom's Gift" is not a print book in the traditional sense but is actually a work in a progress, continually being updated or added to online as a result of interchanges among the Phantom, associate Art Simpson and forum participants. A new chapter may be added to the middle of the book to expound on Rule 1 at any time, for example, so the "book" you see today may not be the same tomorrow.

The book is presented as a conversation between the Phantom and Art Simpson and is "printed" here essentially as it appeared over a period of weeks on the Futures Talk forum, with some comments from other forum participants included. The unique process for writing this "book" means thoughts or ideas may be restated, they may seem a little disorganized in places or they may even appear mysterious at times. Some chapters may be more rambling or personal than will appeal to many traders.

But most traders will find some real nuggets throughout these chapters. Accept the Phantom's gift for what you can glean from it that will make you a better trader. And, better yet, participate in the **Futures Talk** forum yourself and share your questions and ideas so everyone can learn more about trading.

P.S. We still don't know who the Phantom is.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

Foreword

When *Futures* magazine started the "Futures Talk" forum on its web site in the middle of 1996, it attracted some good interest initially -- nothing too spectacular but just traders talking to other traders about markets and comparing notes. But beginning in the Spring of 1997, it became increasingly clear that one participant had unusual trading wisdom and insight and experience, although he sometimes wrote in a vague, mystical way that forced other traders to really think to get his point.

His posts became so popular and attracted so many responses and followup questions that separate threads were set up just for his comments. He was willing to share what he knew about trading exclusively on the *Futures* magazine forum, yet he did not want his identity known under any circumstances and he did not want the money or accolades that he might have gotten from revealing his ideas. Thus was born the "Phantom of the Pits."

From his participation in the forum and the acceptance of his ideas by a growing number of loyal followers came this "book" summarizing some of his thoughts. "Phantom's Gift" is not a print book in the traditional sense but is actually a work in a progress, continually being updated or added to online as a result of interchanges among the Phantom, associate Art Simpson and forum participants. A new chapter may be added to the middle of the book to expound on Rule 1 at any time, for example, so the "book" you see today may not be the same tomorrow.

The book is presented as a conversation between the Phantom and Art Simpson and is "printed" here essentially as it appeared over a period of weeks on the Futures Talk forum, with some comments from other forum participants included. The unique process for writing this "book" means thoughts or ideas may be restated, they may seem a little disorganized in places or they may even appear mysterious at times. Some chapters may be more rambling or personal than will appeal to many traders.

But most traders will find some real nuggets throughout these chapters. Accept the Phantom's gift for what you can glean from it that will make you a better trader. And, better yet, participate in the **Futures Talk** forum yourself and share your questions and ideas so everyone can learn more about trading.

P.S. We still don't know who the Phantom is.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

Preface

I've been asked over three decades to present to others just a few of the secrets of trading. I am not one to want my picture front and center. I am not one to want my name a household word. I am not one to face the 5% of those who would cry foul in giving to others what has been given to me. If I can save the grief of some of the trading torture to those who search out the knowledge of trading, then I am in a position to acknowledge my debt.

Most traders think the important element in success is knowledge. In my trading career I have found that correct knowledge and the ability to change behavior are the most important parts of successful trading. Correct knowledge without behavior modification projects improper execution of an otherwise perfect trading plan.

In three decades of learning correct trading knowledge and behavior modification, I have included in my trading plans two rules that present me with the ability to change my thinking and behavior. Both rules are required for successful trading. Upon urging from a long-time trading friend, I shall share my insight on these rules.

By trade, I am not a writer nor is Art. We are both traders, but it is my desire to present insight into what is required in successful trading. This project was agreeable to me if we would do it on my terms. We came to an agreement on my terms of how it would be presented and that it would be presented as I wished.

Our agreement was that I would remain in my own privacy. I would not give my name but only my approval in writings about my insights of trading. You may call me "Phantom of the Pits." Your success in trading shall be at your own hand and direction. You shall know me as Phantom, a shadow in your success. That is how I wish it to be.

"Phantom of the Pits"
(As narrated to Art Simpson)

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 1: Phantom's Insight

It had to happen, I thought to myself as I took a walk to the top of a small hill just behind my home.

There isn't a single trader who wouldn't give half his trade equity to know how the big guru did it! Knowing his thoughts could be worth thousands of dollars in a single trade. For decades traders have wondered what is so special about perhaps the best trader ever.

It was six months ago that we had talked about giving something back. And why shouldn't he give something back? We're talking knowledge, and you can't put a value on knowledge or experience.

He had both. We agreed that, to give back, it would have to be without expectations of any recognition or rewards. He came up with a plan just as he always did. We would go on the "Futures Magazine Traders forum" and sneak information onto the forum and see how well the reception would be for the new knowledge.

First, he called me every name he could think of calling me, other than my name, to be listed as the author of the information. I wasn't happy with any of the names until he asked, "How about POP?"

His agreement to give back (knowledge) to other traders was really important to him at this stage of his life. I could hear it in each breath of his voiced words. I could see as his face mirrored the concern in his heart. I could see he was taller than usual that day in the spring.

It was almost 30 years ago that I had first met him. I didn't see him as a tall man until years later. Over the years he had grown taller than I had imagined possible -- not in height but in his confidence, his manner of thought, his gestures, his speech and all the characteristics you would expect of a hero. I met him in the pits in Chicago on even ground. We were trading the same futures. I got the best of him that day but just one lesson he taught me by week's end showed that the market is more than a day!

The name "POP" sounded like a setup for me. He stopped at the top of the hill and looked to the sky as he urged me to agree on always keeping his identity confidential. He said, "I will not accept the credit for my good fortune and do not want recognition for my insights on trading."

He looked me in the eye and said, "From now on, you may call me Phantom Of the Pits!"

Yeah, "POP," I thought to myself.

As you progress from page to page, you'll see the importance of Phantom's insight on trading as I have over the years. Trading is not as we all thought. Few have ever approached is methods in trading. "How do you measure the worth of a man or woman?" I still ask myself after that short walk to the top of the hill. Here is a trader who is the best trader I have ever known and perhaps the best trader in the world. We will measure his worth by his deeds and insights into trading!

Yes, that's how we will size up Phantom of the Pits.

Phantom is dedicated to giving knowledge to those who have open minds and a desire to learn. Your part is knowing that, in trading, you can do it, too! It is not an untraveled road . . . only a lonely one!

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 2: Your Book

(Or "Why Give Everything Away?")

To reiterate the points I made in "Phantom's Insights," the following chapters in "Phantom's Gift" are based on interviews with one of the most important and best traders I have ever known. His purpose in agreeing to these interviews is to help those who have the ability and desire to become the best traders they can possibly be. There is no claim to fame, so to speak, but only the honest effort to bring to other traders the insight of a very difficult business of trading for a living.

Art Simpson (ALS): Phantom, why do we start this book without knowing who you are for others to admire and thank?

Phantom Of the Pits (POP): I remember being on a train after one of my first trading days and thinking about how I had doubled my account in that one day. I looked around and was so proud of what I had done, but not one person on the train knew or would even care if they did know.

At that point my direction was self-driven in seeking out what was possible in trading. I know more now than I knew then. The markets have humbled me as a trader more times than I wish to remember. It's always easier for an observer to put their finger on a problem than the one who is wrapped up in the situation.

That is who I am! I am the observer, and I wish to point out the line in the sand. I don't know who puts the line in the sand, but I clearly see it. Who remembers who points out the line? You may call me Phantom of the Pits from here forward, and we shall remain as the shadow of your writings.

ALS: After more than three decades of trading, why haven't you written a book sooner?

POP: I have, but they have all seemed to become outdated because knowledge is quicker in coming than in writing. I always wanted to have it exact. I have made mistakes, and to give my mistakes to others seemed to be admitting I was wrong often. It has taken years to understand that being wrong is what trading is all about.

ALS: Surely there are those who know you and appreciate what you have accomplished in your trading career. Why don't you accept their recognition?

POP: I have always believed that there are two sides to a coin. In fact, I find there are times when you could argue a third. I won't take credit for what I have accomplished. There are no guarantees, and I have been put on notice a few times. My success is nothing without putting a bucket full of water beside the pump to prime it for the next trader, the other side of the coin. There will always be those who drink the water from the bucket (the third side of the coin). Why shouldn't the thirst of others be fulfilled when it can be done so easily?

ALS: To you, what is the most important aspect of trading?

POP: Behavior modification, without doubt, is the key to trading success -- not only in how we think but also how we act in certain situations. We must adapt to changing situations over which we have no control. We must change the situations over which we do have control.

ALS: Let's start your writings and insights into successful trading from any background you can give us of your trading! Is there any important point you wish to make about your trading background.

POP: My only point is that I am no different than any of the traders who will read this. How I got started or who I am makes no difference in trading. Let us not dwell in such trivia, which has no significance in how your readers will succeed. What was is and what is was but a breath after the markets close.

ALS: Okay with me if it is okay with you that we get started with our behavior modification for trading!

POP: Okay with me. But a little history on my first access to behavior modification as a child. My brother was on a tour of a blacksmith's shop in his youth and watched the blacksmith take channel lock pliers, hold a horseshoe, hit it with a ballpin hammer a few times to shape it and then put it into a fire to temper the metal. Upon removing the horseshoe from the fire and dipping it into water, a tempering process, he laid it down.

At that point, my brother picked it up and threw it down on the ground. The blacksmith looked at my brother and said, "Hot isn't it, son?"

Well, my brother said, "It don't take me long to look at a horseshoe!"

That taught me more about trading than anything else: Trading is not taking long to look at a horseshoe. Don't ever forget that!

ALS: What do we call the next chapter?

POP: It's their (traders') book. Why not ask them?

NOTE: *Phantom has observed and participated in an internet forum sponsored by Futures Magazine in an effort to pay his debt, so to speak. Many sharp traders, as well as beginning traders, frequent the forum. Often in posting replies, Phantom uses a sort of firewall to protect his identity. Some of his remarks get posted through the author's efforts. One remark of interest that other traders made Phantom aware of was how effective knowledge can travel today compared to the late 1960s and early 1970s. It is Phantom's thought that those who have the most toys will not win but those who have the most knowledge and can change their behavior to what is needed will take it home.*

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 3: A Little History

Art Simpson (ALS): Let us get into a little of your background without breaking the rules here. How did you come upon the name of Phantom of the Pits?

Phantom Of the Pits (POP): It all comes from the respect I have been given in the pits. I started pit trading in the early 1970s after some early off-floor introductions to commodity trading.

ALS: Why did you decide to trade on the floor instead of up above (off-floor with quote machine) as most traders do?

POP: I really liked the challenge and excitement of floor trading. The appeal of being in complete control at all times seemed to be a dream of all traders. I certainly felt I could do well on the floor by being in total control. I had a few friends who advised me to buy a membership and get on the floor. It happened so fast.

ALS: We both know you are Phantom at showing up on the floor over the last several years. Can we get into some of your experiences on the floor?

POP: You know we all had so-called offices on the floor in the pits. Each day prior to the market open we would all go stand in our little 3-foot by 3-foot office. Every day there was this trader named Cindy who would make her office one tier in front of mine. I remember her name because her career start was as a math teacher. Her husband was a general manager at the FM radio station I always liked to listen to for easy music. I actually knew more about her than she ever knew.

Each day she would wait until she was sure where the market was headed and positon. It happened that I was strong into taking profits on the 3rd wave of buying or selling. It apparently was her breakout indicator. She would always take my offer below the last trade for selling, and before she carded it she would say, " I hate trading with you because I always lose when I take your trade."

I never forgot that statement she would make. Losing never stopped her from staying with her plan as she knew how to lose small and go with her program. I am sure she has made lots of money over the years. I sort of felt bad when she would say what she said, but it started me thinking about losing. Her mind was set correctly in trading. Funny how little incidents shape our belief in trading -- some good and some bad.

ALS: She was never afraid to take your trade, even though she felt she lost from it most of the time?

POP: She had convictions. A lot of the other traders would shut up and back off whenever I would make an offer. I was starting to pick up a reputation for being correct, and the traders would start to follow me. It actually would hurt my execution, and that is where I discovered that EXECUTION is critical. If you can't EXECUTE in getting in, you sure can't execute to get out. It wasn't a mental thing but a hindrance in my trading plan.

ALS: So what did you do to overcome this execution problem?

POP: I started to play games with my trades. Actually the funds do it now. It is so artificial but they fall for it. It worked like this: If I had a position and I wanted to take profits, I would pretend I wanted to add to my positions. So I would bid the market instead of offer. I had enough people following me that they, too, would bid the market. Then I would turn and, instead, hit the bid and sell my positions.

ALS: Seems like a good strategy. Did it work most of the time for you?

POP: Well, I felt bad about getting the other traders out of position by using this little game so I decided to just hit the bids when I wanted to get out. If there weren't enough bids at the last price, I would let the market work itself down to a point I was out.

Today the funds must use fades because they must go at the market to position. This is a problem if they don't know the liquidity at the time. In the long run, it won't make much difference as short-term influence isn't what you would think. I also learned to not stakeit all on one price. A long-time friend taught me the range strategy. It works for me.

ALS: What did you usually trade at first?

POP: You know the only answer I am going to give you! Anything that moved! By that I mean movement has less risk. You wouldn't think so ordinarily, but in a move you can have a smaller position and make a better return. In a dead market you tend to position too large and then, wham, a news story runs the market and you weren't prepared.

ALS: But don't moving markets chop you around more?

POP: There is integrity about the chop as trends that develop give you a good range to work with if you don't get emotional about it.

ALS: Maybe we should elaborate on that statement in a later chapter. How did the other traders treat you when you first hit the pits?

POP: They would yell at me to take my profits and to step off of first base. I didn't mind their remarks except for one. They would say, "Well, it is only money," and that made me mad as I took it personally when I would throw money away. I started out with such a small amount of money, and I couldn't stand to lose money at first.

I got even with the other traders for that remark. I would watch them, and when their shirts would expand and their ties were too tight and, finally, when their face would turn red, I would yell at them, "TAKE YOUR LOSSES!" It wasn't long before we had an understanding.

I actually was doing them a favor in telling them to take their losses. To this day, I call this out to myself when the market isn't working my position correctly -- the big start of my behavior modification, I suppose.

ALS: How have your pit friends and your recent friends treated you over your trade life?

POP: You know, I have just really found out recently how loyal my friends can be. If you do something they remember, it is without fail that they will be loyal to you. They respect me more now than at first. That respect is not just out of trading but knowing that true friends look beyond your face into your heart and soul to find you. It is very touching.

ALS: You don't seem to floor trade much anymore. Is there a reason?

POP: You look on the floor and you see it is a young person's game out there. I am not saying that is the route to success now because it is more than youth in this business that makes you a successful trader. I trade upstairs because I understand the markets better at a distance and can trade more markets.

Being on the floor is limiting as a trader. A floor trader is more of a scalper than a position trader is. I like the latitude of being able to set up various criteria for different markets and not depend on my own execution in the pit to position.

ALS: Would you advise other traders to start on the floor?

POP: I am asked for advice often, but I don't like to ever give advice. I only like to give guidance, as all traders must make their own bed. They must make their own efforts to learn. It is their decision as to how they will make their plan on trading. I can help guide them away from bad behavior, but it is their own determination that makes them a success.

ALS: Phantom, can you remember the first advice you ever heard from another trader?

POP: No, I can't ever remember any advice. I don't mean to be ungrateful to all my many friends and colleagues, but I really don't remember any advice. In fact, that is part of the reason I want to pay a debt to other traders. I don't think anyone ever gives much advice because they feel it is putting them at a disadvantage. Of course, it isn't the case but most traders' behavior is determined early in their lives. That is why I feel behavior modification is critical.

ALS: I can see the critics already starting to line up to point out your big point of trading is behavior modification! Are we going to write an entire book on behavior modification? If so, we will have to give this book away. Not only that but also what credibility does Phantom of the Pits have to anyone?

POP: Nothing would please me more than to give the books away. Or perhaps we could ask *Futures* Magazine to sponsor it for all the publicity they would receive. Accurate insight is what we are going to give every trader who reads this book. It isn't enough to point out requirements. I want to give them guidelines so they can choose their own destiny.

ALS: Sort of like change your thoughts and you change your destiny, huh?

POP: This is exactly where we want to be. No promises, no requirements, no false hopes and no undue influences. Exactly the way it should be. Traders must make their own millions. I only need to be responsible for keeping them in the game forever.

ALS: Phantom, I don't make my money from writing so how about making it a little easier in writing this book for me? Guide me a little in what you want to convey to the traders in this book.

POP: I have an idea, which presented itself when I viewed some of the other traders' questions on the forum I frequent. They don't know the important questions other than from their own experiences in trading. Eventually they will come upon all of the situations I want to protect them from getting into.

However, I don't want to give specific trading advice or any outdated information like the writings I wrote in the 1970s. So why don't we call upon the traders from the forum to guide us in this book?

ALS: Great idea! I am rather impressed with this one trader and know he will respond. But we don't want to exclude any of the others so I guess we kind of make them Phantom of the Pits, too!

POP: That certainly is okay with me. I like the idea. No loss to throw out is what I enjoy.

ALS: Okay again! You win! You are right!

POP: Funny, I have had years to hear what you just said. I really don't hear that anymore. I mean the "You win and you're right." Trading is not those statements. A trained trader understands success as "You lose good and you're wrong small." Trading is called coming out on the small losers' side and being rewarded with knowing how good you have been wrong.

It requires a balanced life to sustain the meanness of the markets. Traders never plan for the bad days, and there are bad days. It is when it affects their lives that they must make a new choice. Either change their behavior or go down in defeat.

ALS: There's our subject again. Are we going to get tired of hearing the truth of trading?

POP: Traders have a choice: Either face the truth of trading or look for the nearest exit.

ALS: Have any of your associates over the years given you a difficult time in your trading?

POP: Only through ignorance! I can forgive all that. Those who don't learn are their own enemy.

ALS: What must they learn?

POP: Most important, they must learn that they don't have to make SELF-LEARNED mistakes. They are always better off to learn from OBSERVED MISTAKES. It can be pretty costly to make mistakes in this business. You cannot really tell someone what to do, but often if you guide him or her, they will be more receptive to making the right decision.

ALS: How do you differentiate between self-learned mistakes and observed mistakes?

POP: Let us say you go to an eye doctor, and he asks you if you can see better out of lens A or lens B. You make a choice, and then he goes to the next step by asking you again if you can see better with lens C or D. This continues until you have the best lens criteria for your eyes.

Well, any mistake you make is a self-directed mistake, and it will hurt only you . No one can teach you not to make this self-learned mistake.

Now, if you tell the eye doctor you are blind in your left eye when he says cover your left eye and he then says cover your right eye, then you have an observed mistake. You wouldn't make that mistake, and because you were affected by that mistake, even though it wasn't your mistake, you will remember better.

It is better to learn from a mistake that affects you directly when it is made by someone else. You have to be mistake-aware in trading because there are so many lessons.

ALS: I see. I mean, it is clear what you mean on mistakes. Learn from others' mistakes, and it is cheaper than learning from your own mistake?

POP: I think you have it.

ALS: Do you ever go into the pits much anymore?

POP: To sharpen my thoughts on a market and to re-enforce the proper behavior, I often do go back. There is always something to learn from it.

ALS: What happens when you walk into the pit?

POP: At the end of the trading day there are those who come up to me an say, "I knew it, I knew you would be selling today. I should have known the market was going down."

ALS: So you move the market?

POP: It seems to be their thought, but it isn't the case at all. You see, if I am selling to take profits, I am aggressive in doing just that. It is that I have a position to get out of, and it so happens there are others doing the same thing. Maybe they have a signal close to mine. It is inaccurate to think anyone moves the markets. If they could, I wouldn't trade! The truth is that the BEST LOSER is the long-term winner.

ALS: One of the traders (on the Futures Talk forum) had some good suggestions on phases of this book. He calls step one "preparation." Let us continue with that suggestion from the forum.

POP: Suits me fine.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 4: Preparation for Trading

When several traders who use the *Futures* Magazine Talk forum learned there would be a book by Phantom of the Pits, they made suggestions. We are going to start this chapter with an anecdote from Ulrich Eckardt, a young trader who was born around the time Phantom was learning his first behavior modification about trading.

When Ulrich was in the States as a youngster, his uncle wanted him to paint the staves on his roof. Excited as any child at a young age to earn money, he was eager to start. He grabbed the paint and a brush and decided to hurry onto the roof. His uncle stopped him and gave him his first lesson in trading -- or life, for that matter.

His uncle proceeded to tell him the requirements for completing a job. First, you must be properly prepared. Second, you will do the work and, last, you will do the cleanup. It seems we can follow that train of thought just fine. First, we must be prepared!

It's a step everyone must go through to get to where traders want to be in trading. To prepare oneself for trading is just as important as any aspect. Without it, a trader does not have the foundation to continue in trading. Where does a trader start to prepare to be a successful trader?

POP: Too many beginning traders -- and established traders as well -- take the easy route and expect the markets to be cut and dry of what is required of them in their trading careers. They will paper trade and have fairly good success.

This in no way prepares them for trading. They must be prepared in every way. That means mentally as well as physically and emotionally. Priorities must be in the proper place including family, friends and environments.

ALS: Where do you suggest they begin?

POP: Get your office ready! Pick out your office where it is comfortable for you to have quiet time and a proper place to relax. Trading is going to be an all-out effort if they expect to climb the mountain in front of them.

The first thing is to get a comfortable chair. It must be a proper chair in order to start behavior modification immediately.

ALS (laughing): I really have heard strange things but really? The readers are going to think this is a joke book! A chair?

POP: I'll tell you the reason for the remark about the chair being so important. There is significance in what I am going to tell you about the proper chair. You see, some traders think the market is to position yourself and lean back and wait to get stopped out or take their winnings.

It's not. That is where your chair is going to save you more than it cost you. Don't get one of the lean-back easy chairs as they will be too comfortable. As with the markets, you must be reminded daily that you can never let yourself get too comfortable in your market positions.

Don't get a standard rocker, especially if you have a cat with a long tail, as it moves all over the place. What kind of chair do you think I am talking about?

ALS: I'm supposed to ask the questions! I know your chairs so that is an easy one to answer.

POP: Okay, I'll give you the answer anyway. You want to get what is known as a slider-rocker chair -- one that rocks back and forth over its own base without moving over the floor. Even get yourself an ottoman. The big reasons are as follows:

First, in your trading career you will find that the markets go back and forth without going anywhere a lot of the time. Your slider rocker chair will remind you of this every time you use it. That step is important to drill into your thinking. Your chair will not move around the room but will rock back and forth.

Second, in your trading you will find you do not ever control the market but only your position. Your chair is the same way as you can stop your position wherever you wish. I want you to drill that into your thinking also.

I will repeat what I just said because it is important. You can stop your position wherever YOU want! You wouldn't think of letting the chair oscillate if you didn't want it to. Same in trading. You can stop the market's oscillation any time you wish. Simply stop (remove) your position.

ALS: I knew you had a good reason for the proper chair. Do you really believe this helps?

POP: How much easier can it be? No one has to remind you to stop your chair from rocking back and forth. You will do it without thinking. Your trading position will oftentimes need to be stopped. It must become second nature to automatically do it at times. This simple symbolic gesture for your office will save you lots of distress in your trading.

ALS: Okay, we are now prepared with an office and a chair. What next?

POP: Next, we want a clock with accurate time -- a battery-operated clock so you don't have to reset it often. The most important part about the clock is to get one that actually talks to you and gives you a reminder of the time by talking. Instead of looking at the clock for time, it will remind you what time it is.

It's another symbolic point to start behavior modification. You see, we remember things well when we associate them with something else. Memory experts will tell you this also. When the time announces itself, you must realize you are required to work with your positions and not let the market work on your positions. You must always act promptly and deliberately within your plan. The clock can be used to reinforce your thinking and behavior.

ALS: Aren't you making an assumption that traders are going to be free while the markets are open? Doesn't this leave out the poor trader who works two jobs and seldom has time to kiss his wife, let alone trade your way?

POP: So it seems. But, no, I am not making that assumption. My concern in preparing a trader to trade is to make behavior modification immediate from the beginning. The chair is to be used whenever any trading plan is developed and thought is given to what the market possibilities on your position might be. The clock is to be there to remind you of promptness every time it announces.

The office setup is to give the trader the message of importance to be in control of their positions and not delegate it to the markets. Your office is important because you must be in control. Remember, we used to have our small space in the pit and what did we call it?

ALS: Your office.

ALS: We have our office with a chair and a clock. What's next?

POP: You must establish a routine to set up the environment of each trading day. Allow at least one hour prior to the opening of your market. In this hour you should exercise from 10 to 20 minutes. This really does keep your mind sharper.

The next thing after your shower you should spend one or two minutes giving thanks to your higher power and explain what you are going to do with the funds you earn. Don't be selfish about it. This actually gives your subconscious a reason for being a successful trader.

Last of all, face the north and acknowledge you actually know which way is up. This gives you a better sense of well-being by confirming to yourself that you are in total control. You will need that total control when you follow your trading plan.

ALS: Not everyone can do or would want to do as you suggested!

POP: I know! Some will be at work or on their way to their work, but they can still do those things as they commute. It is important to acknowledge the reason for trading, regardless of your situation or reason. Thirty years ago I would have thought it very strange to take these steps.

ALS: Do you do these things?

POP: Yes, in my own way I do. Every trader, whether beginner or established, should set up a routine to follow as I suggested. There is more benefit from it than can be seen at first thought.

ALS: It all seems like a lot of work, and we haven't started our learning process yet.

POP: The most important person in your trading is yourself. Take care of the minor details early, and you will have your routine. It is more of a positive reinforcement of what you are expecting from trading.

ALS: Are we ready to start yet?

POP: A couple of more items. You need to acknowledge your reason for trading each day. If you can't afford to buy the chair and the clock, then you should postpone trading until you can, the reason being that you need every aspect of trading in your favor. If you do it all right, there will be better times ahead.

The next thing I suggest is to get a favorite book to read.

The last thing I suggest is to pick out a person you admire most in your life for their accomplishments.

ALS: What would your favorite book be?

POP: I shall tell you of a suggestion from a very brilliant trader. His suggestion is "The Art of Warship" (the U.S. title might be totally different) by Sun Tzu. The book was written about 2,500 years ago and forgotten for a long time. Because it was in Chinese, there are different translations.

The best one is with a word from James Clavell. He based his noble house saga characteristics on that book. The book discusses rules for war in ancient times but can be translated into business-life, private relations and even trading. Sun Tzu's rules have been alive for 2,500 years now and still fit perfectly.

ALS: Why is a book important?

POP: On bad days, instead of coulda-woulda-shoulda, you must expel your feelings of defeat as soon as possible because, if you don't, it will affect your next day's trading. Read that book if just for 10 minutes. Make it a routine.

(Sidenote: Phantom and I have taken note, thanks to Futures Magazine Online, that Dean Lundell has re-authored "The Art of Warship"and titled it "Sun Tzu's Art of War for Traders and Investors." Both Phantom and I actually feel this is the best book on Sun Tzu to date, especially as it refers to trading.

Futures Magazine insert note: This 220-page hard-cover book is available from Futures Learning Center for $19.95. Order No. B2085. Call toll-free 1-800-601-8907 or fax 802-864-7626.)

ALS: I guess I have a few things to learn myself. You said to pick out the one person you admire most. Why? Whom do you admire most?

POP: There is a great deal to be learned from the person you admire most. You will need to understand your ability to become an admired person if only in your own mind. I have changed my most-admired over the years, and now that person is younger than I am.

There are many reasons I admire my choice. I'll give you the most important reasons. She gives and gives of herself each and every day. She is not selfish, and she truly cares about her fellow men, women, children and all life on this planet. I admire that so much. I hold her responsible for showing me the light. She is the only Oprah I know.

ALS: Does she know you feel that way?

POP: No, but it is important to let your most admired person in your life know they are indeed most admired. It goes right to the positive example you need in your trading life. Do it! Let them know, even if there is no time for their acknowledgement. You have done your part at that point. It is good mental food.

ALS: Are we ready to start learning to trade yet?

POP: I would say that for me I am prepared now for the job.

ALS: I guess preparation for trading is a different process than most imagine. I really thought we were going to get into the learning process of how to trade and setting up a program to trade. Are we going to get into the specific ways to trade?

POP: Keep in mind we want to guide and not give specific advice on trading. There are basic requirements that determine a winner from a loser, and that is what I am after in this insight. There are as many ways to trade as there are traders, but the basic fundamentals required are seldom presented to the trader. It is important to present a plan that keeps the trader in the game over their lifetime.

Let us expound on that subject in your book. We can address trading methods in detail in later writings. I have been trying to give some examples on the fourm to help traders understand where I am coming from in my rules of Phantom trading.

We will answer some of their specific questions on trading later. I read a short book called "Notes to Myself" several years ago; it was but a self-diary that had been published. It was a small book, but it really had great insight. I like the idea. We can all learn from other people's insight on subjects that we are investigating. It in no way is advice, but we can make up our own minds by knowing those thoughts.

This is more of my purpose in answering your questions for this book. It puts the traders on a one-on-one basis for understanding the complexity of the markets and helps establish a criteria for an overall plan with the most important points at the front of a trade program. More often than not, these simple thoughts are not used or known by most traders. It's sad that everyone feels they have a great fortune hunt in front of them and there isn't a lot of thought required in how trading actually unfolds.

What subject do you want to discuss next?

ALS: It's beginning to be a surprise to me and knowledge learned new again.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Book

By Art Simpson

Chapter 5: Rule Number 1

When the subject of why it was so important to write this insight, Phantom's remark was always, "Catch me at the right time for that answer." I remember as a child playing out that situation. It was always better to get my Dad to agree to something when the mood was correct. When gathering Phantom's insight on the reasons for this book, it wasn't clear until I caught him at the right time. It was after a big move in the grains in early October 1997.

Art Simpson (ALS): Phantom, I see you agree on the subject today. I need to know just why is this particular time the right time to give your reasons for this book?

Phantom Of the Pits (POP): This day is an example of the reason for this book. The grain market did a total surprise on most traders. Oh, there were those who were fortunate to be on the right side, but most of them took their positions off too soon. I wanted to discuss the shock most traders get on a day like today.

A great number of traders got what we call "killed" today in the grain market. Most all of the new traders are now wondering what they did wrong today. There isn't anything they did right today because they most likely don't know what the right thing is. I don't mean that all traders are in the dark. I am talking about those who fail to understand what to do and, if they do, don't carry out that requirement.

I am going to express the importance of doing the right thing from the beginning of a trade and at the right time.

Many traders -- and most new traders -- aren't even aware the market can do what it did to them today. I have often said the BIG money is on the surprise side. I should perhaps have said the BIG LOSERS are on the familiar side or the popular side of a trade. I call that the expected side.

Today gave us several reasons for a surprise -- harvest pressure is strong and this is a day you expect there to be more selling by the producer than normal. Expecting prices to be pressured by hedging and seasonal influence is the correct way to trade in most minds. You can't argue with probabilities. It is not what the trader does with his trades until the market starts a big move like today's. That's what separates the big winners and big losers. There were more big losers today than big winners.

There are traders who, because of today, can't make their next month's car payment or their house payment now. It just didn't ever occur to them that what happened today was even a possibility. They were over-positioned, even though they thought they had a good protection plan. They used stops okay, but they forgot to tell the broker to place the order.

Everything they did was based on their thoughts of how much they could take out of the market today. Their trades are designed to lose but not because of the good traders or the way the market works but by their own hand. The worst part is they don't even know it was at their own hands.

It is sad anytime a person's heart gets pulled from their dreams but even worse when they lose money, too. Sometimes they lose a fortune in such a little period of time. It has happened to every trader. It happened to me when I was smarter than the market. Why does it happen? Mostly because a trader's plan doesn't consider, "What if I am wrong?" Their thoughts are always expecting to be right.

Herein is the key to being a successful trader. I have learned this over and over again in my trading career. I haven't found one trader to tell me I am going to tell you. The reason for our agreement to give something back is that all of these big losers are doomed from the start unless they are given the knowledge of what the market can do to them. The blame is within their own responsibility and not anyone else's fault.

Six months ago we started our journey in presenting one of the most successful sides to a market strategy. On the *Futures* Talk forum there have been exceptional traders who have read the information I gave and did not understand the simplicity of what I said. We will have a better exposure of presenting the same information in this writing.

I never want to see a homeless person and always wonder how they became homeless. If traders aren't aware of what the market can do against them as well as for them, they will head in that direction. Many homeless people I have talked with have had bad luck. In most of our lives we will experience an evening out of luck.

In trading, if you have bad luck, you will eventually have to stop trading. To be prepared for that bad luck is a requirement in trading. You will not survive if you do not plan for bad luck. My first steps in trading remove the bad luck altogether.

ALS: I know what you are going after here. Should we put this in red letters and double the size of the print here?

POP: Yes, I think that would be appropriate, but traders must discover for themselves what I am telling them. It will save them from an outcome that they never discover until it is upon them. So let us not over-emphasize the most important point of any trading plan here as we will drill it into their plan until they survive at all costs in trading.

There are those who, in a modified way, do exactly as I suggest but may consider it more money management than a plan for trading positions. Every broker tries to limit a customer's exposure and protects them, but the key word is "limit." Putting a limit on something infers that you actually can put a limit on exposure when having a position established. You really only have a ballpark limit in most cases. It seems to be worse than you thought in looking back.

I shall present two main rules in trading. Both are required to be successful. Every trading plan must start with the understanding of these rules. Before I give the first rule, it is important that what we say is understood correctly. Next, it is important to have this rule become second nature in all of your trades. The second rule I shall state and explain after the first is adapted into behavior modification by the traders reading this.

I need to ask you a few questions to better present my Rule Number 1. When the walk light comes on, assume there is traffic that will run the red light at each intersection you cross. What do you do now before you cross the intersection?

ALS: I would double-check and look both ways before crossing.

POP: Of course, that is the correct answer -- you know what I am after. Now, just because you looked both ways before you crossed and each time you cross you looked both ways and each time there wasn't any traffic that ran the stop light, is there any reason to stop looking each time you cross the intersection? Your answer, of course, is no, you won't stop looking.

What kind of limits did I just give you? Are they life-saving limits before you cross the intersection? Yes, they certainly might be, but you will never know that if you follow the restriction each time you cross the intersection. You can't know if it saved your life for you prevented finding out by looking each time.

But what if you don't look and you lost your life. You certainly won't know you should have looked either.

Does the restriction tell you that, if you look, there will never be any traffic running the stop light? No. Does your experience of crossing and looking tell you what the probability of someone running the light will be? You can make an assumption based on your knowledge at this point. What does an assumption do? It actually presents criteria based on proven facts that are a possibility. It in no way gives you a high probability or low probability but the best answer you can present.

I don't want to lose you in this thinking but to point out that it's the same in trading as in crossing an intersection. We need to make our best assumption of what is possible. We must plan for that assumption in trading as long as it is a possibility and not just when it is probable. This is a very important point in understanding Rule Number 1 correctly!

If you were never to look at the intersection until proven wrong for not looking, wouldn't it be too late? It is the same in trading. You must protect yourself from any possibility in trading and not just protect yourself when the probabilities are high.

This will be the surprise side in trading The surprise side is a possible outcome but not a very high or likely probability like today's grain trade. When someone gives you a gift, you are surprised by it. Getting that gift was not a high probability. However, you are prepared for that surprise because you say, "Thank You!"

Most traders plan only for the probability side and that, to them, is always what they consider the winning side. This is the biggest mistake you can make in trading. Instead, you must plan for the losing side.

How you understand your plan is how you will react to a situation. You must learn that, when you are told not to do something in trading, it is not ever the same thing as saying you must do the opposite.

I often get feedback telling me I told someone to do what I never said. As an example, I will tell you not to sell beans today. Would you tell me I told you to buy beans today? It's not funny because most traders would. This is what I mean by "correctly."

We have covered "assumption" and "correctly" in my terms . . . what I expect you to understand in the first rule and second rule. If you don't have those correct, you will not be able to fully understand and accept the two rules for trading required in all plans.

ALS: Let me get this straight! When you say to not do something, you are never telling me I must do the opposite. Seems simple enough. Thanks for making that point by example.

On your meaning when you say "assume," you are telling me there is a possibility or probability based on some fact of the situation that requires me to acknowledge and always have a plan for the possibility or surprise side in trading. Your meaning of the surprise side of trading is the side that presents the possibility but not the highest probability. Am I correct on this?

POP: It really is quite simple. After our dialog, it will be more clear to the traders as to how to interpret our rules. I don't want any misunderstanding. I say with a high probability that the readers will read our dialog again.

We often don't understand how news stories get out of context, but it can be done pretty easily. Lack of proper assumption is routine by lawyers a lot of the time. They'll ask someone something like, "Who is in the picture?" and when they find out it was the defendant, their next question is, "Were you there when the picture was taken?" In their case, it might be proper for information-gathering, but you as a trader must have proper assumptions as you cannot know exactly how a market is going to react each day.

Trading is not a favorable game in most circumstances, and that is what we must use as our assumption in trading. The big mistake made by traders is thinking and expecting trading to be a favorable game.

You have execution costs or slippage when getting in and out of a position as well as commissions as a cost factor to be subtracted from your winnings or added to your losses. The market spends much time in an unpredictable mode. Trends both short- and long-term do exist but not 100% of the time.

The correct way to control positions is to only hold them once they prove to be correct. Let the market tell you your position is proven correct, but never let the market tell you that your position is wrong. You, as a good trader, must always be in command of knowing and telling yourself when your position is bad.

The market will tell you when your position is a good one to hold. Most traders do the opposite of what is correct by removing positions only when proven wrong. Think about that. Your exposure and risk is much higher if you let the market prove you wrong instead of your actions removing positions systematically unless or until the market proves your position correct.

Let me give you an example before we state the first rule. Today let us say you sold beans just like your plan said to do at $6.30 on the open. If that position did not prove you correct, you must remove it to reduce your risk. You decide what is correct according to your plan.

Let us say you expected hedging to come in early and the price to drop from 5 to 8 cents in the first hour. It didn't even drop 3 cents so you remove the position. Say you removed it at $6.29. Just because it showed a profit of 1 cent when you got out did not declare it a good position. However, your exit is a better exit than if you made the market tell you the position was wrong.

When you remove the position because the market proved you wrong, it is always a higher loss, and with stops it also is usually with higher slippage. This is not the same as removing the position because the market proved you wrong -- say, buying back at $6.45 on a $6.42 stop. By making the market prove you correct in order to hold a position is acknowledging that trading is a losers' game and not a winners' game. If you only remove your position because the market proves you wrong, you are acknowledging that trading is a winners' game.

You never want to be in a position that is never proven correct. If you only get out when the market proves you wrong, it is possible to have higher risk due to the longer time period required to prove your position wrong. We will further clarify these thoughts for you further into the book.

So here is Rule Number one:

In a losing game such as trading, we shall start against the majority and assume we are wrong until proven correct! (We do not assume we are correct until proven wrong.) **Positions established must be reduced and removed until or unless the market proves the position correct!** (We allow the market to verify correct positions.)

It is important to understand that we are saying the one criteria for removing a position is because it has not been proven correct. We at no time use as criteria for removing a position the fact that the market proved the position incorrect.

There is a big difference here as to how we treat all positions from what most traders use. If the market does not prove the position correct, it is still possible the market has not proven the position wrong. If you wait until the market proves the position wrong, you are wasting time, money and effort in continuing to hope it is correct when it isn't.

How many traders ever hoped it wouldn't be proved wrong instead of hoping it was correct? If you are hoping it is correct, it obviously wasn't ever proven to be correct. Remove the position early if it doesn't prove correct. By waiting until a position is proved wrong, you are asking for more slippage as you will be in the same situation as everyone else getting the same message.

What makes this strategy more comfortable is that you must take action without exception if the market does not prove the position correct. Most traders do it the opposite by doing nothing unless they get stopped out, and then it isn't their decision to get out at all -- it is the market's decision to get you out.

Your thinking should be: When your position is right, you have to do nothing instead of doing nothing when you are wrong!

I don't mean to repeat and repeat but, in this case, you will better understand the rule the more you read it. It is very critical to your success in trading. Over time it has proven to be the rule which keeps the losses small and keeps a trader swift and fast to take that loss.

A person's thinking when the market proves a trade to be bad is counter to what is productive. By using the rule properly, you are productive and don't have to face the demoralizing effect of the market when you have a proven wrong position. This enables you to continue to trade with the proper frame of mind. You are more objective in your trading this way than letting a negative reinforce your thinking. This way you only let good trading reinforce your thinking and actions.

ALS: Phantom, not everyone is going to agree with your first rule. There will be traders who don't feel this is a good rule for them.

POP: Look at it like you would buy a new car. The dealer says you can drive the car you think you want for a month and we will give you credit toward another car if you don't want to keep it. Okay. After a week you decide you don't want this car because it just isn't right for you. You take it back and the dealer says you only owe $80 for rental.

You don't buy the car and keep it until it proves to be the wrong car for you, which could be months from now. If you did, you would lose more of what you would have to pay for the car.

Most traders keep their position until it proves to be wrong for them. I say don't keep any position unless it proves to be correct.

ALS: Yes, but who is to say a position that was not proven correct turns from a bad position to a correct position?

POP: That is the kind of thinking most traders have. They fear being wrong when they get out and that the market will show them they should have stayed with the position. If they don't take early losses, it becomes more difficult to take a loss as it gets larger. However, the market assumption you must make is that big losses will eventually take you out of trading.

My Rule Number 1 is to address the swiftness needed in keeping your losses as small and quick as possible. It won't always prove to be correct, but you will stay in the game this way.

Which would you choose? You have an opportunity of a 10% probability of making money in the long run if you take a position until you have lost 10% of your equity or made 10%. Or take the opportunity to have a 90% probability of making money if you only keep a position for three hours unless it has proven to be correct by that time. It is pretty clear which choice you would make.

Most traders don't know what their choices are when it comes to assumptions about what is possible in trading. Keep in mind that traders are usually unaware that trading is a losers' game. He who loses best will win in the end!

Why not make a time-proven decision to change your behavior to trade the method that gives you the best long-term outlook. Trading is not gambling! Treat it as a business where you only want the best merchandise for the shortest possible time in order to have the maximum profit with the least possible chance of failure. That is what Rule Number 1 does for you.

ALS: I can see the need for much discussion and review of your first rule.

POP: It's critical to have Rule 1 in force by next surprise day. The one thing that teaches most traders to take a small loss is a big loss.

ALS: Yes, but that is expensive behavior modification. My wife, Karen, just gave another parallel example of your Rule Number 1. She points out that you don't go buy clothes, take them home and wear them until they prove to be wrong for you. Instead, you try them on and make sure they have the proper fit and look before you buy them. I like her thoughts along this line.

POP: You can see in ordinary life you try to spend the least amount of money and have the least amount of waste. Why should you do it differently in trading?

ALS: The answer is surely that in trading human elements take over. Everyone knows them and most likely have come face to face with them. They are fear and greed.

POP: We must remove the emotional element as quickly as possible in trading. If you can do it before you put on a position, you have a good start.

Note: To give some insight on Phantom's Rule Number 1, several traders have indicated their experience with it as presented on the Futures Talk traders forum. The following is a copy from one such trader, M T:

I've read Phantom's postings about Rule Number 1. The price action must confirm the position or get out quick. What I have done in trading is to enter a position and have a chart position that is a good spot to exit if the price moves adversely. This would usually either be the previous swing point, which, if violated, would be a signal for a possible new trend and would definitely be the signal for me to exit my position or it would be the first 15-minute high (resistance) and low (support), if it were violated adverse to my position.

So that meant there were times when I entered a position and the price action was flat or slightly adverse but not so adverse as to violate my predetermined chart exit position. I would stay in because there was no violation. I thought this meant I was following Rule Number 1.

I was staying in not because the price action "confirmed" my position but because the price action did not "confirm" my stop-loss chart signal. I was thinking this is what Phantom means. I have to tell you that with this strategy I was keeping my losses small, just by the nature of my plan.

But I was unwittingly violating Phantom's Rule Number 1. I thought I had modified my behavior but, in reality, I was "behaving" incorrectly. It's a very subtle thing, I believe.

Then last night, in a restless sleep thinking about my trading, an inspiration came to me (don't laugh too hard). A lot of my losses had come after I had been in a trade for an hour or longer, where price action was mostly flat but my stop point was never touched. I realized I would have been better off if I had just gotten out in the first 15 minutes. It would have been a loss, but it would not have been as much of a loss as my chart stop point would give me.

Then I realized that is what Phantom means. My position was not confirmed in those first 15 minutes! It wasn't violated according to the nuances of my plan, but it also was NOT confirmed. Get out.

Well, lo and behold, I went back over the last three months of trading and, using the exact entry points (fills) that I used every day, reviewed what would have happened if I had followed this 15-30 minute confirmation rule. Let's just say it made a huge difference. I know back-testing is not completely reliable, but it was significant.

Anyway, thanks Phantom. I'm still learning. I'm still here trading. Started with only a 5K account, day-trading, and I'm still alive without even following your rules. I'm below breakeven. Let's see if I can change that. I'll keep you filled in. Once again, many thanks. You once asked for Rule Number 1 stories. Well, there is mine.

Note: The following is an excerpt from a message in the Futures Talk forum that Phantom presented to help understand Rule Number 1.

Behavior modification is knowing the limits. Let us use basketball shooting as an example. Say you shoot 1,000 times and make an average of less than 50% of your shots. This means you have a better chance of missing than hitting whenever you shoot. After practice, let us say you are able to hit 55% of your shots. You would expect to say that, now when you shoot, you have a better chance the shot will go in than not.

Same in trading. You must know what the limits are! In trading most of you have a greater chance of being wrong than right! Trade accordingly . . . which means expect the limit (being wrong more likely) in your trading.

How can you come out ahead? In the short run, you can only with luck. But in the long run, luck tends to even back the other way. You must trade in the long run!

So what is a trader to do in a losing game? You must trade in the long run! How can you trade in the long run? Only way I know is that you must keep your losses small and take more small losses than small winners to come out ahead. This often means washing a position for the sake of being able to keep in the game.

The theorem now is to assume your position is wrong until the market proves what you positioned is correct. Keep your losses quick and small. Don't ever let the market tell you you're wrong. Always let the market tell you when your position is correct.

It is your job to know you are wrong and not the market's job.

The other side of the coin is that you will get positions that are correct. You must be bigger at that time. This will require a Rule Number 2, which is designed around adding to winners in an unfavorable game to come out ahead in the long run. When you are correct, you must continue to use Rule 1 to keep losses small. It's okay to be wrong small but never okay to be wrong big if you expect to trade in the long run.

Trading is not easy. Most traders just let the market do its thing. The correct way is that you do your thing and control your positioning. You control your positions by using rules that keep you in the game.

Rule 1 is the most important rule in any trade plan. Rule 2 will be the other side of the coin, which must be dealt with if you are expecting to remain in the game in the long run.

Learn to be wrong, fast.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

by Art Simpson

Chapter 6: Rule Number 2

Art Simpson (ALS): Phantom, do you want to continue on Rule 1 or is it time to move on to Rule 2?

Phantom of the Pits (POP): There will be lots more on both rules so let's get to Rule 2 and see the other side of the coin. We will need to get to the qualifier of Rule 2, but we will do that later. We'll state Rule 2 right now:

Press your winners correctly without exception.

Sounds pretty elementary but correctly is the key. What you hear quoted most of the time is "cut your losses." Cutting your losses is the other side of the coin. Without Rule 2, you will find that trading still isn't even a 50/50 game. Without a correct method to press your correct winners, you will never be successful. Without correct winner pressing, you will never be in a position to have a bigger position when you are correct. You always want a larger position when you get a correct move or more accurate stop-loss position when you are wrong.

There certainly will be debate on how you know when to add to a correct position and on how you know can turn a correct position into a losing position. Many ideas are conditional in nature. First, let us get the rules and reasons established; by knowing what is expected in Rules 1 and 2, we can later discuss the conditions and exceptions to proper execution.

Rule 2 does not mean just because you have a position in your favor that you must now add to your position. Rule 2 does not state that the market must be moving in your favor before adding to your position. Rule 2 states that the proper criteria for adding positions depends on your time frame of expectations in your plan.

You might be a day-trader just trading back and forth in a sideways stock market, or you might be a position trader. Rule 2 states that the rules for adding will be different for each trader. The important point of Rule 2 is that the rules for adding to positions must be made in advance of the trade with the least drawdown expectations. You must also use Rule 1 proper.

Rule 2 is important for it keeps you in a good position as well as impressions upon your mind regarding about having a correct position. Many traders are conditioned to wait to take a profit to prove to themselves that they are right. Being right does not, in itself, make the most amount of money.

Most traders also want to get out before the market turns and takes away any profit they may have. Certainly, they want to be out before they give back any profit they have already made. This is just simple human nature when having a market position. Human nature in trading is the greatest enemy of the trader.

Always a good reason for adding to a winner is because traders usually tend to doubt the correctness unless they have the confirmation of a good position. Adding to the correctness of best does this.

The other good reason is that you must be larger when correct on a position than when your position is wrong.

Correctly adding to a proven position must be done so that a pyramid isn't established that will hurt the trader in a minor reversal. Each add onto an original position should be done in proportion to the size of the original position. If you are correct on an up-or-down-trend position, you should use four contracts for your first add and two contracts for your next add. This gives you a larger average position in your original position and still, Rule 1 is in effect. Rule 2 is establishing three levels of positioning.

The reason that Rule 2 is important is the important Rule that 1 be in your plan. This includes when you are adding to your positions to protect your trade from any major reversals, which often happen.

Your plan for adding positions could be as simple as using each buy signal for longs and each sell signal for shorts. Many traders use Bollinger retracements for adding.

Without exception the rule indicates it is not an arbitrary decision on the trader's part whether to add. Keep in mind that the rules for adding will be different for each trader. The important point of Rule 2 is that the rules for adding must be made in advance of the trade with the least drawdown expectations. You must also use Rule 1 proper.

Rule 2 is important for it keeps you in a good position as well as impressions upon your mind

Phantom's Gift

By Art Simpson

Chapter 7: Trading with Rules 1 and 2

Art Simpson (ASL): Phantom, your required rules seem pretty simple. Let's use some practical application to illustrate trading.

Phantom of the Pits (POP): In trading, rules are not meant to be broken for your own sake. The rules bring you to a no participation condition. You design your trade program and approach to trading by keeping the major choice of positions within your program while maintaining your approach to the market. You can't do that if you follow your trade program while breaking Rules 1 and 2.

The rules take away the need to decide while the market is open what to do during the trade day, you will have made those decisions in your trade plan and will be prepared for anything that may arise in actually going to take place with your positions. You will either be proven correct with your positions or you simply get out of the position. You don't stick around to get hurt with exposure if the market is not proving you correct.

You are in the market with positions that are in direct opposition with you and what the markets are doing. This will be a minimum problem, as the rules will keep you in the trading game for the long haul. Without the rules, you will be in the market with positions that are in direct opposition at bad entry levels. Even if you make a simple mistake such as chasing markets, Rule 1 will keep you from being in a position opposition to the market for long.

ASL: I notice a few questions coming up (on the Talk forum) about excessive commissions and slippage. Is this a problem?

POP: Today, as an example, I bought the DJIA after a 30-point rise and expected to see continued upside. Commissions and slippage cost me 50 seconds I lost, but I was not in it just on the trade. The market continued to drop against me, and my loss would have been 30-40 points without the rules, but with the slippage and commissions it was 50.

Now you can't tell me that it is better to stay in and wait for the market to come back than it is to get out on a small loss and wait for a better time. Commissions and slippage are a minor standing after a simple Rule 1 trade is a lot better and allows me to have sanity about my next trade.

Most traders think it is bad for them to be wrong and, when they are, that's it for the day. Well, being wrong is the best time to make a decision on well your trade program is working. It certainly can trade again. If you keep a trade that never proves to be correct within your program, you will be in a position that will cost you more than just the initial loss and will have a tendency to cause you to stay in the market when it is worth a lot more than just the initial loss when you are thinking well.

What I am getting at here is something usually learned not by observation but by making the assumption itself. *Most of your money from trading is going to come from trades that take place in the middle of the trend, not at the beginning.* Most people, when they are beginning, look at most starting trends and the good runs you have once a market turns. The chop-chop markers and trading range markets are killers.

While it is true that being in control of your position in the market rather than the market being in control of you is something to think about your program, the market is dangerous. It also greatly enhances your ability to make good trades. The main reason is that you know what is expect of the market and what to do when it does what it is not supposed to.

If you supervise building a house and you have several trades working on the house, you know what trades are supposed to be done in the beginning and what trades are correctly placed you walk away and let the foundation be completed. Building a position is the same in trading and, if you have a trade program, you know what trades are correctly placed in a position and what trades are not.

Stat, at any time the prior work finished could create a problem. Let's say the foundation contractor cracks the concrete. Would you continue on the foundation? No, you would stop and wait. No, you will continue with a trade that proved correct but now shows problems.

You can never let your guard down in trading. You must always know what the next step is for the market. Rules 1 and 2 will keep you in the game, but you must know what the market is and just like driving a car becomes a subconscious effort for you when you are proficient at it.

You can't say, I'm not going to drive today because I'm not in the mood to drive. You can never control what the market will do or how the orders will enter the pits. You cannot tell me when a trade will come. You can only be prepared and have a program that is ready when the trade does come.

You can do is build your criteria or trade plan to take every angle that is important into account. I can give you a plan that will catch every move, but you will catch moves that are wrong, too.

Along with that plan to never miss a move, I can give you the big drawdown and the rules that will keep you in the game. Rules are important because, if you don't follow them, you will be in very small profit trades and very large losing trades. Without the rules, you will not last long to have a profit.

Now, I have added the usual trader is about. He is not in this game to earn a few extra bucks for his vacation. He is always after a better return than most would consider fair in any other investment. The rules are not meant to hold you back. You are competing in a game and need fail to see the big risk that faces you at first. Somewhere along the way you must face the market and win.

Trading is a loser's game. You must learn how to lose. The biggest loser who loses small will continue in the game.

Obviously, the small trader who loses big will quickly go to the sidelines. Sometimes the beginner who loses small will go to the sidelines, but, if he learns how to lose small, he will have seen them. It is the saddest thing in the world to take away someone's dream – more so when they never have a chance to make it a reality.

A trader must know and accept what the market can do along the damage side to equity, to make a good decision on a trade. Every day is a new day and, if you have a good trade, it is no surprise from the time you put your position in place. The big surprise can sometimes be a friend, but you must be prepared for it.

Why do I say the market is going to give you a surprise? Can you tell me exactly how far a friend, but you must be prepared for surprises? Or if it will come?

What you can do is eliminate your reactions to what the market does to you. You do this by having a trade program that is control your position and not the market control your moves. You start out expecting the adverse market moves and plan your action based on expectations.

Rule 1 is the rule that keeps you in control at all times when that position is in place.

Attractive modifications come to your program, but you need a rule to show what that must be done at all times. One trader suggested the rubber band method. Each time you took a profit, you put a rubber band around your trade program. Rules are rubber bands – that is, you remembered to do it. I don't like this method, but it is better than a lot of others.

Just because you are in a good trade, you must know what to do if it turns out to be a position on and lose big money, that is when you can feel very bad.

Rule 1 is the rule that keeps you in control of the situation. You put the trade on based on the trade plan. The market either confirms and you now have a good position, or it doesn't confirm and you get out with a small loss and wait for a better time.

Simple! Only a big deal if you don't get out when it isn't confirmed as a good position. No need to worry about the big drawdown. Rules that don't interfere within a trading program are always going to look bad sooner or later. Why not take the sooner?

ASL: It's beginning to look like it takes more thought to put a trade on than the time you're going to be in it. Is that true? ... or I mean should it be in a correct position?

POP: The logical step is to have the plan in place for the next step before you put on the trade. I would guess that most of the time the trade will be in a good position if the market proves they have a bad position. Even if the position is correct, their next step is wondering what to do if it proves wrong. Rule 1 and 2 will keep you in control of the situation and keep you in the game.

ASL: Human nature is as you say. I know you did some research on human nature of traders and non-traders. Perhaps we can talk about some of your data.

POP: I'd rather you let me refer to it, if needed. I don't want to just suggest some of the experiments and let the readers come to their own conclusions. Let's keep that the behavior modification book.

ASL: There were some questions on when to get out of a position. I realize this is out of order but, can you give a few comments on that?

POP: That's okay, as a common question is when do you know when to get out of a position. Actually Rule 2 addresses this very well because it says to press your winners correctly. Pressing your winners correctly means that you have a good position and you want to press it correctly. Pressing your winners correctly means that you want correctly pressure them.

The time to get out of a position is not when the market is proving your position to be a correct move. You have the market proving to be wrong as that is the correct, but when you are already proven correct, this is certainly the time to step off first base.

We have two rules to keep us protected from our lack of certainty and enhancement of profitability. Rule 1 keeps us from being in a position at all times, but it also allows us to pressing that the market is proving to be right or wrong.

Well, this is just absolutely not true. Rule 1 doesn't allow us to pyramid! Why say it so strongly as I should still have an open mind. I have to put this in the category of thinking a statement that says not to do something because it is not in the rules is a bad statement.

Too many times I have watched a fund bid the market so they can sell the market. It's a plain fact that, when a fund is bidding the market, it is not in a position to sell the market. Rule 1 keeps us out of this type of trading. Rule 1 keeps us from being in a position to be wrong.

The easiest way to make money is to be on the right side of the market. Rules 1 and 2 are the rules that keep us from being in a position to be wrong. Rule 1 keeps us from being in a position to be wrong.

Rule 1 keeps

Phantom's Gift

By Art Simpson

Chapter 8: Day-Trading

***"In day-trading when the last trade is made, you expect to be out of your positions. You are letting the clock decide if you win or lose. That, to me, is a nothing."* Phantom of the Pits**

Art Simpson (A.S): Today the title of the chapter, Day-trading, is a picture being painted by an artist. Hundred traders standing with notebooks, bow and arrows, darts ready to be launched and no bids in the pit quiet sets in.

Phantom of the Pits (POP): Yeah, and I can tell you the artist.

A.S: Who would it be?

POP: Leroy Neiman! I'm impressed with his work. It is something he would paint. I can't help but put him in the class with Oprah, MJ, Don Gibson, LeAnn Rimes and . . .

ALS: . . . and Phantom of the Pits!

POP: Phantom of the Opera maybe but not the Phantom of the Pits! You must remember that no one knows who the Phantom of the Pits is. In fact, I know a guy that there will be bet this one book! Only this one!

ALS: Now wait a minute. You said it depends on the reception of the traders when we started this project six months ago. Are you telling me that it's not?

POP: That is something I want to discuss with you. There is no big profit in writing unless you can really write. I can't and don't want to write except for my own keeping. You can make more money trading than writing.

This brings me to my point of insight in trading. I wouldn't do this insight on my own for it would be a waste of my time. In fact, I am sure this reason is the primary cause of lack of knowledge generated by traders based on experience. Theory is great but not a learned behavior. Behavior is the key.

ALS: Phantom, you forget easily as it was YOU who came to me about giving back by helping other traders. You were as sincere as Michael Jordan is on the court. You don't fool me! I know what your plan is!

POP: Yeah, perhaps, but I know you won't tell anyone unless I let you.

ALS: I am going to tell without your permission right now! You are going to cut your losses, if any, in this project, and you certainly will not profit from your gain, if any, from this insight give-back.

POP: That's good. Wish I had thought of that.

ALS: I would like to know in day-trading if you should use the same rules as in longer term trading. Are there times when you shouldn't use Rule 1 for day-trading or any trading, for that matter?

POP: Never, in trading forward from now. Looking back, you could say there are certainly times when you would have been far better off to forget the rules. But that is looking back and that is how you lose. You must plan for what will eliminate you from trading in the long run and protect yourself.

ALS: There are going to be times and trades you will want to tell anyone about.

POP: Let me point some things out here. Many years ago when I first started to use computers and their speed was slow, I had so much to do that I had to get outside help. I had this one program that I could have written but it would have taken too long. I didn't want to write it in assembly language because I wanted to see every step of the execution of the program. I contacted newly established programmers and some not so new to help me.

It was sort of an experiment within itself. I narrowed my choice down to about four or five qualified candidates. I asked each one of them to solve a problem and I gave them the given access to a computer and a basic programming language. The question I asked first was what is the answer to every number from 1 to 100 added up.

Think about how you would solve that problem for a minute before you see the final conclusion to it. One programmer used the computer and came up with the correct answer. It took him all of three minutes. One candidate put down his paper and computer and said the answer is 5,050 within 10 seconds.

I asked the individual who only took 10 seconds how he came up with that answer. His remark was, "I don't see or think in things the way everyone else does. I see and split the numbers into pairs such as 1 and 99, 2 and 98, 3 and 97. When I am done, I have 49 pairs that make 100 and two numbers of 50 and 50 left over. If you multiply the 49 pair times 100 , you get 4,900. Then add the 100 and 50 you get 5,050 as the answer.

Well, that made an impression on me I still remember.

Now, I want you to understand about day-trading the same way. WE DON'T ALL SEE OR DO THINGS THE SAME WAY. We all can get at the correct answer. My answer is to keep you in the game for the longest possible time.

ALS: Who gave you the quick answer?

POP: You know very well who it was! I didn't say I wouldn't give you credit in these insights, just that I wouldn't take any. And wipe that big smile off your face.

That impression was a start, but I wasn't done with my experiment. Next, I asked each of them to write me a computer program to see if they could add up the numbers for all numbers added from 1 to 10,000. They were all able to give me a program to do what I asked of them in Basic language. I judged their success on how quick the computer would give the answer and not by looking at the program. I ran the three programs and timed them with a stopwatch.

All of the programs came up with the correct answer but at different speeds. Because we were using Basic language, it was slower than I wanted for my particular program, but I was pretty well decided I wanted to understand the logic behind my own problem. The speed of speed were from 48 seconds to 3 minutes for all but one.

The last one took less than a second done in Basic. That surprised me so I took the fastest two programs and included in the programs a timer. The 48-second program ended up with a loop: N=0; for N=1 to 10,000; N=N + 1; next NN. Print N.

The time of 48 seconds was still slow as far as what I wanted. The fastest program was: N=N square + N divided by 2: Print N.

Just as each programmer came up with a different style and program, not everyone was looking for what I wanted. It is the same in day-trading. The common ground that we are all after the ability to not ever having to stop trading, and we are all after the ability to make more than we lose.

You see, there are variables in all of our trading styles. It is just that my Rules 1 and 2 are designed to give you the longest answer when it comes to trading longevity (Rule 1) and the shortest time to get to your goal of return (Rule 2). You need them both.

ALS: You've made a good point!

POP: Let the debate continue for we all benefit from knowledge brought forth with each different situation. The only time I have a closed mind is when there is total lack of understanding of what is required of a trader. That part of a program is not a control front program but the required execution by the trader.

ALS: Day-trading. Where do we begin?

POP: We'll start with the reason for day-trading by most traders. It is a function of my Rule 1. And it is a function of my Rule 2.

ALS: You mean you are going to take credit for day-trading? I thought you said you didn't want any credit!

POP: It is the traders desire to be able to trade and not worry overnight about their positions. Risk and exposure of positions beyond a short period of time while expecting to eliminate this possible gain in the quickest possible time. Actually, the desire to have Rules 1 and 2 in a profit time frame is a perfect profile for a day-trading.

ALS: Okay, we'll buy that. A day-trader often is doing just what your rules imply.

POP: There are advantages in day-trading but not many because restrictions come into play. In day-trading you are more apt to lose than win due to the time limit being a restriction that creates a situation of whoever is ahead at the buzzer wins.

In basketball, when time runs out in the fourth quarter, the game is over. The high score wins. In day-trading, when the last trade is made, you expect to be out of your positions. You are letting the clock decide if you win or lose. That, to me, is a nothing.

I did a study on day-trading and came up with some very interesting findings. The first thing I learned in the study was that you could use the day-traders to your advantage in trading by knowing that they would have to trade in a short time.

Second, I learned that day-traders actually do a better job of keeping ranges smaller than do scalpers whose purpose is to trade small moves for quick profits.

Third, I learned that day-trading did afford traders a way of keeping risk smaller and allow them to work larger positions in the market without being exposed to large prices in the long run.

Without going into the next 10 learned points, we will concentrate on the first three. The first three are probably the most important, but they all have merits.

Day-trading is good for some traders, but it is not for those who they know to keep risk smaller because of shorter time frames. There are those traders who do not want to put up the margin to carry overnight positions and have the risk (better known as under-funded traders who don't have the money in the first place and who should not be trading such size). Whatever the reason for day-trading, it is a valid method of expressing my Rule 1. The only exception is that they actually expect their positions to last.

A scalper is quicker to take a loss but tends to let profits run a little less than a day-trader's ability to take losses. In other words, a day-trader tends to lose on average more than a scalper makes. This leaves a scalper with a better chance of being in the game for not, guess who picks up that extra loss that day-traders make? It is usually the position trader.

So that, to me, is the edge. You must know when you have the edge and just what it is. It is not in exact thing, but it is in the tendencies. Numbers are not as clear as we would like to ability to execute as scalpers. A day-trader would do better if execution became a market order on stits – especially in falling tokens.

ALS: You're going to discourage a lot of day-traders.

POP: Not at all, as the day-trader is a more disciplined trader. It you take Rule 1, which is the assumption of being wrong until proven correct, you will have the other side of the coin for day-traders. They could become disciplined traders if they were to use Rule 1. Day-trader's odds are lower because of their limitations on overnight carries.

Another big drawback is delayed reactions on what the market prices have done. If they use criteria such as opening range breakouts, they have to be fast to take the trade and place stops in the pits. On the type of trade they are better to take a position on the open and protect it than to take the opening range breakout. But they want the position proven before they take the position and wait until the breakout.

As a day-trader, they would do better if their trades were within criteria, executed and protected by Rule 1. Instead of the delayed reaction to the market, the anticipation. They must pick the points almost exact. This is another drawback for them. You put yourself at the mercy of what the orders enter into the pits as well as the execution. It is almost impossible to be exact in your estimate of price. A better situation is to be able to pick a range instead of a price on execution.

Same with exits. This all reduces your potential profit from day-trading.

So what is the answer? A day-trader can do better by averaging, but you never want to average in an established trend. The trend will tease you into bad entry positions if you don't do your research on market characteristics. Experimenting with a trend is a game for fools because there will always be those weak positions that turn into profit-taking. This is a day-trader's nightmare to be avoided.

ALS: How can you be so certain on day-trading?

POP: The best traders will take what I have to say, study it, research it and decide how exact it is. They will judge accordingly and make their own trades based on improved judgment of day-trading.

That is what we want them to do. It is too easy to think day-trading is everyone's game and a good one. It is a good one for some but not most. It can be improved by understanding the drawbacks. All trading has drawbacks so it is critical as to how they view their trading probabilities.

ALS: You said day-trading could also be compared with your Rule 2. How so?

POP: A day-trader tends to take bigger positions because they know they will exit quicker than most position traders. This will give less risk long term and affords them a way to over-trade . . . or I guess I should say gives them a way to trader bigger.

In Rule 2, the idea is to be bigger after proven correct, and I suppose that is what the day-trader is thinking in trading bigger as a day-trader. Right or wrong, it is correct in being bigger within correct criteria. The bad side is they tend to be wrong as often as right. This keeps it more of a 50/50 game than an advantage they would have if only being larger on correct moves.

Being larger on correct moves as a day-trader is difficult, at best, due to limitations of the day's price requiring the action be quick. Day-trading is a relative game. Position trades, day-trading will not allow more than one add, if any add at all. Often, too, the profit side gets taken off sooner, restricting the large even more.

ALS: Is there a better way to day-trade?

POP: You bet there is! Now I have every day-trader's attention. For a price I will be glad to give that information out.

I am just kidding, of course. The answer lies in their research. Look at what causes the most losses in day-trading. Look at what causes the most profit and criteria which decide what does work. Look at the other side and assume a day-trading criteria does not work and expect it to be wrong. Next, devise a way of removing positions until they prove correct. There you have the answer.

Can you incorporate it? Not in all situations, such as we said previously. Trends and counertrends tend to do a number on day-traders due to their not caring what a trend does.

Next, set up a criteria for removing your positions. You must not allow the clock to dictate when you get out.

Most important in day-trading, you must never play everyone else's game. Say, for example, play the opening range breakout. Everyone does that. You will wash in the long run, even though you just want to day-trade.

You set your criteria differently. Let us say you trade the third move through the opening range. Why? The market tends to be a trading market if you get the third move through. That is what you are, a day-trader. You can now expect the market to be on your terms as a day-trader. You expect to come out of the market, but if you are wrong? Well, then you will make your profit instead of being prepared to break even on a swing trade.

As a day-trader without an existing trend, you can also fade the market. Let us say the last 10 days' range averages 8 cents in soybean meal over the last 10 days. Your criteria could be the old Fibonacci number of 5. Wait for a 5-cent setback to buy or a 5-cent rally to sell. I am not saying this works in your particular market, but you can study it and establish your criteria in a non-trending market.

I know some day-traders who take the day off until they have had two days in a row of a non-trending market in the same direction. The next day is theirs, as they will wait until it looks like the reversal is about to take place and then counter the two-day move.

Day-trading is a psychology study of the last few days. If you use Rule 1, you stand a better chance of being up in the long run. It is not exact, and as long as that is understood and losses are kept low, it is a possible moneymaker in the long run. If you like the odds, you can be satisfied if you do everything correctly, regardless of the outcome.

A critical point in day-trading is not to just use the prior day's high, low, range and close as inputs to your criteria of signals to use. Point-and-figure charts are closer to the market as P & F charts don't restrict prices to within a day's range.

Remember, you are staying away from the same methods used by most day-traders in order to get the edge on them, as well as the position traders who most likely only use bar charts.

Last of all, don't just take someone's word on day-trading. Check out your particular market and see the characteristics in action during the day. Many you think is a good trade might not even be possible when you try to place the position. Use market orders to make sure you get a position but do not let the market control the entry price.

ALS: Phantom, I have a question and sort of a remark from a successful day-trader. Using a volatility breakout system and using a stop after a series of consecutive losing trades, can you use Rules 1 and 2 correctly?

POP: I can tell you whose idea that is and what course it is in, but I don't want to disclaim or endorse the data. There are some markets in which this is an excellent method for day-trading. Not all markets will be good candidates for this method. I am sure traders who use this method know which markets to shy away from by experience.

Yes, you can use Rule 1 correctly, as it is saying that you assume your position is wrong until proven correct and, taking a position reversal after a series of losses, you assume that you are going for probabilities of a turnaround. If there is no turnaround, you certainly were expecting to pay the piper. Naturally, the market will have to prove you correct after your entry with your established criteria.

On one of our examples of an onion trade earlier, we used end-of-day criteria as an example of what some would consider the last reasonable time to place a trade. It is the end-of-day criteria to get out. Day-traders tend to be or get out by the close. To watch a market go against you all day and not get out until the close is certainly a challenge in trading criteria, but sometimes your criteria will require this situation to be the case. The market may come well be out on the close but does not prove out. This alone keeps from carrying a loser overnight.

On using Rule 2 in your question, would you say the odds of increasing the position after a series of indicated losses would be in your favor compared to the odds of the initial position is taken after those losses? Only if the position proves to be correct.

The swift would be able to determine if the position had proved swift and at that time adding a removal stop would take place without the fade to zero. I would agree that, with this plan, if your data feed is quick and your line to the broker is quick, you would certainly be in a position to minimize your pause. What I like in this idea of Rule 2 is that you are required to do either one of two things at a certain point – either add or remove.

Keep in mind that Rules 1 and 2 do not negate a successful trading system at any time. They are to keep you from a catastrophic situation that a particular system may not recover. There could be additional protection outside the plan or could be incorporated within the plan itself. I appreciate that question and understand the concern that trader has in his career. It sounds like proper research for the proper criteria in his style of trading is paying off. It's good to hear about that happens. It proves that trading is not easy but is behavior modification and knowledge.

You can learn from other traders, but you never learn to be them. Just the other day on a Phantom chat room the announcement came that a particular trader had made a million dollars and the question was why they would sell now. One of the answers was correct: He was offending his position.

I remember one day when I bought all day and at the end of the day when the market was down on the close, one trader asked me why I went long all day. He didn't know I had orders place as large selling after every buy order.

My point is that you don't know what a trader did; you only know what you have seen him do at the time. You see, my plan was to establish what the market was going to do that day. Every time I bought, I had a broker with my exit double the other way. I would try to offset my new short position and getting out was wrong so we doubled it the other way again. At the end of the day I had a position twice as large as I had intended and the opposite way I intended to go. I only knew that the day I had to be swift.

Sometimes your criteria may be that you must be swift to take any possible loss -- especially when a certain Fed chairman speaks.

ALS: Is there a way to plan for such surprises?

POP: Yes, there is . . . by not ever over-trading at any time.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@iquest.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 9: Options

***"An option can get bigger than its original size if all goes well for the trader. It can also melt with predictability."* Phantom of the Pits**

Options trading presents many more possibilities to vary your trading plan than do just futures, bonds or stocks. There are as many ways to trade a position or scenario as there are ideas, it seems. Phantom uses options for various reasons, as do most traders who understand them.

The purpose of this chapter is to give insight to all traders and not to narrow the insight just to the experts. There is much to be learned about trading options, and good research is needed to become properly prepared in trading them. Keep an open mind as to what the market can present on both sides of the ledger.

Art Simpson (ALS): Phantom, I know you don't see or do as most traders when it comes to options trading. How can we better understand the proper trading of options?

Phantom of the Pits (POP): Most traders know what options are and how they work. I view them as ice cubes, which can either melt or get larger when the water around them also freezes. When water freezes, it will take up more volume than the water did in the original state. An option can get bigger than its original size if all goes well for the trader. It can also melt with predictability.

I like to weigh each of my option positions against a futures contract. By this, I mean that each position or combination of positions has a weight. To impress upon you my view, let us use a balancing scale. You know the kind I mean -- one that has a platform on each side of a balance indicator. Put an ice cube in the glass of water, and I consider the weight of the ice cube as a call that has been purchased. I consider the weight of the water as a put that has been sold.

Regardless of how large the ice cube (long call) or how much water is left (short put), the total weight of that glass will remain the same. The ice cube can become larger when the temperature drops below 32 degrees, and the water becomes reduced liquid.

It is the same with the call and the put. They can and will change size. I call the size of each ice cube the delta and also the amount of water a delta. Any time you add the long call delta and the short put delta at the same strike price you will get 100 in theory, excluding the interest rate factor, volatility and time element.

Using this as a rule of thumb for our understanding, we will assume positive 100% delta in this case. You can consider the opposite as negative 100% delta -- the ice cube as a call sold and the glass of water as a put bought.

On the other side of the balancing scale you will have an equal futures position of some size and bias that will equal the option side and balances the scales. Your glass of water with an ice cube (long call, short put at same strike) is equal to short one contract of the futures you are trading. You will remain balanced and have no risk as long as this position is in place. We call this a conversion. The option side of the scale is the synthetic future. You would be either long or short a synthetic future, which can be offset with an opposite futures contract.

Pretty simple at this point. You start to throw variables in, and it changes dramatically. Each glass is going to be a different size, depending on the strike price. In other words, even though the delta of our initial position will be 100%, regardless of strike price, the size of the glass will be different. I consider the size of the glass as the value of the water and ice cube added together. It will be different at different strike prices. The delta remains at100%.

You may be getting into this description and even a little ahead of me. If you have had geometry, you can have some good fun with this approach.

We can now think of throwing out the futures contract but still wanting to balance the scale! We put on the other side of the scale the opposite option position, and we still have our balanced position. But guess what? What we have really done is to offset our position, and no position exists on either side of the balanced scale. We can only make money in certain situations, but we must know what we can do to move our position around when required.

Now we get into the ifs. There is no limit to what we can do -- almost no limit, I should say. What we want to do is to come up with a plan to make money in almost any situation. We must also find a way to include Rules 1 and 2.

We discover we can balance the scale by using different strike prices and not just the same strike price. We also can tilt the scale to one side and leave it biased to the long or short side. Pretty simple still.

Now add a balanced scale on each side of the existing balanced scale. You have three balanced scales to work with. You can add four more balanced scales to the last two on each side. You see, you now have the possibility of each of the balanced scales giving you an opportunity to move positions around but still keeping it balanced. It becomes trickier with each set of balanced scales you place in use. You can even add as many balanced scales as you wish, but you are out of control trying to stay balanced. This is what happens to some option positions not well thought out.

I hope I didn't confuse anyone with the balanced scales and ice cubes, but it is critical to understand what each move can do to your overall position. My option model is a combination of balanced scales as data input to the program, which determines what each variable will do to my position. You can make money when you know how to use volatility, time decay and price movement. The criteria research becomes a little more intense and expanded.

Without getting into specific programs, we'll discuss the fact there are certain option positions that work with my rules. Extensive options understanding is beyond the scope of what I am trying to teach you. I only want to show you how you can incorporate options trading into a good method of trading while using Rules 1 and 2 to protect your drawdown.

ALS: I know you use vectors, weights, volumes and angles as part of your computer program to establish criteria of balance as well as the usual research of option evaluation. I also know you developed your own evaluation of options' worth, which is different from most programs. Is it because you don't want to play someone else's game?

POP: It's like a basketball, which retains the same shape but has a different bounce when the pressure changes. Same with options. I consider an option evaluation in a bull market different than in a bear market. The market just considers the volatility different. It is how you can best work with options.

If I gave you a notice that from now on we would consider bearish options and bullish options and not just change the volatility to fit the price, you could better understand what is expected of your trade instead of guessing the changing volatility every day. This has all been debated before, and we aren't going to change what is believed to be the best method. In fact, sometimes when you are trading with a different view, you are better off.

I am going to explore some option possibilities that use Rule 1 to start. Because we are going to assume we are wrong until proven correct in options also, we will put a fairly protected position on to start. Let us say we have a bull market started as we see from our criteria platform. Okay but we could be wrong so we will not go long an option. We will instead put on a bull spread. A bull spread is buying a lower strike and selling a higher strike price. This leaves Rule 1 in use.

Options experts are going to say we only put a smaller options position on. Yes, that is correct for the purpose of requiring the market to prove us correct. Let us say we bought a 1000 strike when the future was at 990 and we sold a 1010 strike just for an example.

If we had bought a 1000 call outright, we would have paid more for the call than we would by also selling a 1010 strike. We have limited our potential loss at this point to the debit we paid out. Let us say we had a debit of 3. An outright call bought without the bull spread would have cost us, say, 5. We have already started to use Rule 1 by reducing our possible loss to 3. Our maximum loss is 3 at any time.

What can now happen? Three things can happen. One of them isn't going to happen as the price never remains the same very long. So prices are going up or down. What else can happen to our position? We can lose time value as the ice cube melts, and we can lose volatility as the interest in trading falls.

We have used Rule 1 so we are slightly protected from time decay because we don't have as large of a position as we could have with an outright call. We are also slightly protected form falling volatility because we are not with as large a position as we could have had with an outright call.

Okay, but the experts are saying we did all this at the expense of potential profit. Yes, indeed, right again. But isn't Rule 1 to keep our losses as small as we can? Isn't the name of the game to stay in the game forever? Yes, so we need Rule 2 to make our money!

Rule 2 actually works better in options than futures. The main reason is that volatility can increase and decrease. With futures, sure, the market may go limit up or down, but options move that value as expected and then some extra because of what the experts call volatility changes. I call it changes form liquid to solid! Water freezes with higher volume as a solid.

At any time you are not risking more than 3 in our example and you are long a 1000 call and short a 1010 call (bull spread.) Let us say that our criteria for being correct is that the market moves at least 15 points. So at 1005 we accept being correct at this price.

We will make our position larger at this point. How? We have many option possibilities but the best option is to buy a higher strike than where our current position is due to the increase in volatility. We want a delta (position size) that can more than double. A delta of 50, 60, 75 can only go to 100. A lower delta gives us a possible double plus, triple plus, etc. Also we are risking less equity.

Okay, we buy a 1020 strike for example purposes. Let us say we pay 6 for it due to increased volatility. So what do we risk now? We risk our original 3 but, because of volatility increase and price movement, we have a value of, let us say, 6 on our original bull spread. Okay, because we paid 6 for the 1020 strike we still have only 3 at risk or do we? We have a value of 6 (1000/1010 bull spread value) + 6 (1020 call purchase price) or a value of 12 and have only paid out 3+6 or 9. We show a profit of 3 at this point and can work with our Rule 1 and have no additional risk on our position by using criteria here forward, which protects us from negative drawdown. To do this we remain after the last 1010 call at 20. That means we have -3+(-6)= -9 paid out and +20 received. We are up 11 points. Okay, the experts say you could have had more if we had just offset the positions. Okay, so we're bad! We still have 367% profit so far. That isn't bad, is it?

Two weeks later the market is at option expiration and the price of futures is at 1009. Oh, darn, we forgot our butterfly position! Well, let us salvage what we can!

What is the butterfly worth now? The answer is 9. Okay, so we offset it and take commission charges or we don't offset it and let it offset by our exercising the 1000 call. In the end, by leaving the butterfly on, we set up a payday provided the market was within 1000-1020 at expiration. We made anywhere from 11 to 21 (depending on where the butterfly is offset) on the trade.We made the 11 from the sale of the 1010 call and anywhere from 0 to 10, depending on where the butterfly is offset. Don't take all your profits but let leverage work for you in options.

Our maximum risk was our original 3 and never more, using Rule 1 correctly in options by having a limited risk. We also added to our position and used Rule 2. But, wait, there is more! Once we put the second short call on to establish the butterfly, we were never going to lose anything because we bought our butterfly by being given 11 to take the total trade of four options over the range of movement. We can options long at 1000 and 1020 strikes and short two options at 1010 strike for a butterfly legged into. In other words, as soon as we neutralized or balanced the scales on each side, we could never lose.

The experts again say, "What if the market had gone to 980 instead of up to 1005 and then 1030?" Well, we would have lost 3. So what kind of ratio did we set up for our trade in options? Risk 3 to gain 20 equals 6.6:1 (slightly less with commission and depending on where the market price established itself at expiration).

ALS: It looks easy. Is that all there is to it?

POP: I don't want anyone to think it is that easy because you must be aware of what is required in exercising options and the effects of increased volatility and decreased volatility. This is a start to give you the desire to learn more about options.

One of the big keys in options is the hidden secret of putting on no-risk or low-risk trades and working the positions into a no-risk trade with the potential of a big payday toward expiration. If you are to trade butterflies, you must learn that the proper time to buy them outright is with a long time out when the liquidity may not always be good to put them on. You can often put them on with bull spreads and then a bear spread. Commission costs are a concern if you are at a full brokerage. You must figure all of the costs to reduce the ratio of payout.

ALS: Do you want to go into some other strategies?

POP: Let us put this on the back burner and see what the traders want?

ALS: Okay.

NOTE: There are so many good books on options trading and, because it was not the purpose to show different strategies here, we will leave you to further research. The main point Phantom wanted to make is that you can and should incorporate Rules 1 and 2 in options trading as well as futures only trading.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 10: Cloud Hopping

***"I believe if someone important can have faith and expectations in those around them, it will make a difference in their lives."* Phantom of the Pits**

"Cloud Hopping" is dedicated to the memory of your and our friend John Denver, who died in his experimental airplane on October 12, 1997. John touched our hearts with his songs, and his touch of kindness reached out to all living things. Our memories are stronger than death as we search the clouds and share past laughs. Far out, our Brother in Mankind.

One of the most-used tools in trading is perhaps the chart. Charts not only show high prices, low prices and current prices but also other data that can be used for derivative information generating. Each trader has their own way of using and interpreting their charts. Some make up their own charts; others buy them from a commercial vendor.

When it comes to their use, Phantom remembers when charts were charted on a big graph in the pits themselves for all to see. We continue our insight with Phantom on charting.

Art Simpson (ALS): Phantom, sometimes I wonder how organized traders can be with all of the charts around their offices. I always thought the less information you had to research during trading hours, the better you would be able to react to the current market situations. What do you view with your charting?

Phantom of the Pits (POP): First of all, you mean "Cloud Hopping!" On a Sunday afternoon I would go out to the park and do my charting. Let me reach over and turn this old radio on with this funny-looking knob here. This big radio is an oldtimer, and it takes me back 30 years or so. As I turn it on, you will hear WGN and the Eddie Hubbard show with his theme song, "Poor People of Brooklyn," playing in the background. I think his theme was a spoof on "The Rich People of Paris" but I don't know that for sure.

I doubt that many oldtimers will be reading what we say here but, just the same, the past is certainly worth a view once in a while. A look back is good if, for no other reason, just old time's sake.

On my Sunday afternoon charting, this is what I would see with my charts! I would look to the sky and see all of these kites flying. My chart would show this as volume. All of the kites on the ground, not in the air, and the flying kites would be the open interest. The clouds in the sky would be my price on the charts. I would chart all of these with a connecting line from all of the clouds in the top part of the chart and volume and open interest on the lower parts of my chart.

As I saw the movement of the clouds in my sky market, I would place another chart point either higher or lower, depending on whether an existing cloud moved higher or a new lower cloud formed. Any time I could get a divergence from the clouds' highs and the open interest of kites and volume of kites, I would get a signal to sell sunshine futures.

My father would ask me what I was doing, as he would always pick up the trash from our picnic when the wind would blow it away. I would answer him, "Dad, I am CLOUD HOPPING!"

I got pretty good at cloud hopping and sunshine futures as I could predict when it was going to get cloudy again. I think I was all of 13 at the time. That was my first introduction to charting.

I tell you this little insignificant point of my early charts because I have seen just this week examples of the same things in trading signals from traders. It may not make much sense most of the time to most of the people but if it works, who am I to argue. My cloud hopping worked for me!

There are advantages and disadvantages in charting. When you use charts to look back to get signals, you are setting yourself up to believe you can actually be more right than wrong. It is possible, but you must never forget Rule 1, regardless of how accurate your chart indicator shows over the past. Just because it worked nine out of the last ten times does in no way suggest that it will stay 90% accurate. Protect your positions at all times.

I think the main advantage I see in charts is that you can plainly see what will be dictated to other traders for them to think at certain points. You will remember I said I don't totally agree the market is always right at all times, but that is what we must trade with or against. How many times have you seen public sentiment be a massive majority of opinion one way or the other? What happens? More times than not the thinking was wrong.

In charting I have to say my strongest signals are when support or resistance is broken and thinking is in the majority against what is happening to that support or resistance.

I don't want to go into specific types of charting and indicators as there are so many of them and so many ways to interpret them. I will try and point out what I think is useful to all traders the most. I could explain each type of indicator and charting process, but that serves no purpose. Each trader must decide his or her own criteria for charting.

My charting is based on knowing what the signals of each type indicate to other trades more so than to myself. I am always looking to find what is the edge to me. I don't care about what the charts indicate if they are not my tools, but because others do use them, I must be aware of those indicators. I need to know what other traders are thinking.

I don't position opposite to my signals ever, but that doesn't mean I don't position opposite to my fellow trader's charts and indicators. My criteria takes into account the other signals, though not directly a signal indicator to me.

There are many trading plans based on various charts and indicators, which can be accurate over a period of time. The biggest problem with the dependable plans is that Rule 1 and 2 are not a part of the plan, and the traders never get to trade in the long run. The trade plan may have what they call money management, but that is always a weak point in the plan. Drawdown eventually demoralizes the traders. In the end all is lost.

ALS: Do you have any specific advice on using charts?

POP: Yes, when you see what most charts give you, it is clear that everyone is looking at the same data to establish a method of being the most accurate.

The key to usefulness of charts, as far as I am concerned, is that you take everyone else's chart with a grain of salt and establish your own charting to be reflective of data not usually known to others. All bar charts show the same things. It is a daily chart of high, low, close, open, volume, open interest and other moving averages or indicators. This is one reason I prefer a chart like a point-and-figure chart. It removes the daily bar graph points as the most important for that day.

Let me ask you what would you think of a chart that takes the same parameters as a standard bar chart but your daily high, low, close and open data had a time frame different than daily? You would laugh. I like that laugh! It tells me I have no competition with the idea.

I will give you an idea and an example here. Let us say you make a chart that starts one hour and fifteen minutes prior to the close of a market. We will justify this by saying that the most important trading data for a day is in that last part of the trading day. We will call this the opening for your next day's chart. One hour and fifteen minutes of today's trading is already on tomorrow's chart. We will call this tomorrow's support and resistance. We continue to chart tomorrow until one hour and fifteen minutes prior to the close. This closes out our day's trading chart.

Okay, I think you see what I am getting you to think about. Now keep in mind I am not giving you my way of charting but using this as an example of how to change your behavior when it comes to charting. Most traders will never chart this way for several reasons and that, to me, is good. They can't get the data this way as they may only get it out of a newspaper, delayed or through a broker. Other reasons exist that prevent them from getting a different outlook chart.

I feel you need a jump on tomorrow's trading to get the edge. The edge to me is important but not as important as execution. It is just that, with the edge, you can get better execution. You are ahead of the game because you are in front of the day-traders, funds, scalpers and position traders because you are not using their data to follow them. Instead, you are using your data to look beyond their view. By using Rules 1 and 2, you can establish a plan that is a little more remarkable than anyone would think.

You will have to do back-testing and research and most traders can't even come up with that data yet, even today. I guarantee in the future there will be those who look at what I have done lately and say it is time to make the computers earn their keep. You see, the frontier is just now opening! The sharpest trader with the most intuition will win here. I want you to remember where the idea of "Different Outlook Chart" came into play. It started with me when I was 13. It can start with you today.

Do your research! Do it again! Learn what different outlook charting can do for your trading plan. I have given ideas of what my criteria is in trading certain situations so that an understanding of where I am coming from shows up. Vary your data times. Use 15 minutes, half an hour, half day, first hour and other time frames.

I am giving you a gift here and someday it will hit you. Just don't take too long to see what is behind all three doors. I still want to point out that we will see different outlook charts as the years go by, and they will get better and better. There will be a day when they are followed closely enough that they no longer have the same value.

In trading you need to change the odds to your favor. By using Rules 1 and 2, you are moving in the right direction. By using your own mind, you are doing what that computer programmer did many years ago. You are looking at a different view. An artist will view his subject material from all angles. Shouldn't you?

ALS: Aren't you making it a little dangerous by telling traders to go find your own plan and make your own charting system?

POP: I believe I am only making it a little more difficult in showing that trading is complicated when it comes to getting the edge in trading. I don't expect them to take entry and exit signals they devise without using Rule 1 for protection and Rule 2 for enforcement of their new knowledge.

I believe in the small trader! I know what the potential is because I know every trader started out as a small trader. Not one big trader started just big. You must start. There is no better place to start than at the start line. Only then can you say you went the entire course.

I want to impress upon you the importance of my belief in the small trader. I believe if someone important can have faith and expectations in those around them, it will make a difference in their lives. A good mentor knows that their guidance will grow up one day in those who benefit from their convictions of belief.

This story I am going to tell you was told to me by a very brilliant mind. I like the story better the way I like to tell it but will tell it the way it was told to me.

One year a math teacher in the geometry class had more students that usual. Thirty-eight students were just too many to have the time to give one-on-one guidance as required. Not only were there too many students in this particular class but the teacher also had more bad students than usual.

One particular student had never gotten grades above Ds in all his school years. His name was Robbie, short from Robert. Robbie was the class clown and had been his entire life because that is what the other students expected of him. He had no interest in school and would brag he would quit school at the age of 16 in a few short months.

The teacher had three Robert's in his class: Rob, Robbie and Robert. It was pretty easy for the teacher after two weeks to keep the Robert's clear, as the one who went by Robert was the top student in math.

Five weeks into the school year the first PTA meeting was coming up. The teacher told each of the students to have their parents come to the PTA meeting. That night only about a third of the parents showed up. The teacher knew by how well the students were doing just which parents would most likely show up at the meeting. The teacher took three to five minutes with each set of parents to chat and find out a little about them.

The last parents were a little backwards and shy, but the teacher shook their hands and made them feel at ease. The teacher never got an answer when they were asked their name so the answer was never known. The parents asked the teacher, "How is my Robert doing in class?"

The teacher thought and then answered, "I have never had such a good student in my class who takes so much interest and is a delight to have as an example to my other students. Why, your son is a living example of those who will be leaders in our future. It's just wonderful to know that in our lifetime we will see youngsters like Robert grow up to make us all proud to have known him!"

The parents of Robert stood a little taller and smiled as they left the PTA meeting that night.

Over the next three months going into the end of the first semester the teacher noticed his students doing better than he had expected up to this point. Trying to comprehend how his teaching had improved and what he had done differently, the teacher spent more time trying to improve. At the end of the school year, the teacher was in his own glory as no student had failed -- not even the class clown Robbie. In fact, Robbie had gotten all his assignments done, taken a math scholarship exam and finished with the top score nationwide. He had won a math scholarship as a sophomore. The teacher was really proud to have taught so well.

The last day of class, Robbie waited until everyone had left and then headed to the teacher's desk to talk. Robbie held out his hand and said, "My Mother told me what you said about me! I have never had anyone ever want me in their class before or even cared if I learned. Thank you for giving me insight into my life!"

The teacher began to cry as all the efforts to improve as a teacher reflected back to the PTA meeting at the beginning the year. You see, the teacher thought that, when the parents asked how Robert was doing, it was Robert's parents and not Robbie's parents. The teacher had made the biggest mistake of his life at that PTA meeting by assuming he was talking about the right Robert. Not only was it the biggest mistake but it also was the best mistake of his life.

Can you imagine a grown adult crying? Isn't it refreshing to know we as adults can learn from youngsters and it's ok for us to cry! At one time or another in life we see a flash of light in thought looking back and realize what we have just been given.

ALS: Pretty touching. You say you like to tell it differently?

POP: I like to substitute Robbie's name and instead use "a brilliant trader." You must understand that somewhere as a trader the light must come on for you. There will be a point that the biggest mistake of your trading career will be the best mistake you have ever made.

I personally want that student to come to me and say, "Phantom, no one has ever wanted me in their class before or even cared whether I learned about trading. Thank you for giving me insight into correct trading."

I do care and I have only one thing left that I wish to become: A better teacher!

ALS: How do we go on from here? I think your pep talk has caught me by surprise. I don't know what to ask right now.

POP: I'll go over point-and-figure charting next. Go and enjoy a walk to the top of your hill with your wife.

ALS: Okay, I would like to reflect upon what you have just given as insight -- not just for the book but I also want to reflect for my own personal evaluation right now. Thanks.

The next interview:

ALS: On point-and-figure charting one question I see often is what size to make the boxes?

POP: The fact of P & F charting is that the smaller you make the boxes and retrace criteria, the closer you will see the market characteristics and order flow. To learn the nature of trading and each market, at first I suggest the smaller box sizes. Keep in mind for the retrace that it must have some significance beyond a normal bid-and-offer slippage.

Each market can be a percentage of daily expected moves. I would say that, as an example in soybeans, if the daily range is usually 9 cents, I would use a 1 by 3 box -- each box is 1 cent and each significant retrace has to be at least 3 cents. This pretty well says to take 10% of the daily expected move as the box size and 30% of the daily move as the retrace requirement.

As time goes by, you will want to extend the sizes to larger sizes. You may even keep multiple P & F charts to compare. Today computers can do this for you if you are set up for it. It is important to realize that, at one time or another, each trader will try and improve his trading office.

Is it good to improve your data before your success or after your success? The answer is a catch 22 as you will improve your trading as you improve your understanding of how markets work. Most traders do not want to extend the costs at first due to limited funds. What really can you do with your data if it is based on someone else's criteria and information? You can only be a derivative trader of that restriction.

I am not going into how to specifically use P & F charts, but many good books on the subject will be a good library add for you. Learn the highlights of support lines, resistance lines, three wave recognition and breakouts. You will be able to see what the trade does each day within the market parameters. This is important to see first-hand, and P & F charts are the perfect way to do it.

You are better off if you do your own charting rather than using a computer until you understand and see what important data is available on these type charts. I also suggest that, if you had to use only one chart, it should be a point-and-figure chart.

I don't mean to be weak on giving knowledge on on charting, but it is critical that each trader come up with his own thoughts and ideas. For someone to give you their thoughts just limits a trader's horizon of what is possible for them. Do your own homework and decide what your charting shows.

On some of my programs on charting and signal criteria, I narrow it down to inputs of importance. I could have as many as 64 inputs. I can weight each one according to how important they are, or I can have them in one of two states only. Some of my criteria input is qualified by going through several doors first. In other words, if the criteria is met, that input must go through the next set of criteria. It sort of ends up like an eye examination as you expect one total answer in the end.

Charts and criteria are nothing more than the best set of eyeglasses at the end of the examination. You will wear those glasses after your exam. Same in trading, you will use that data after your criteria is set. Why argue with it?

Many traders are always making exceptions. For example, the last time they used their criteria signal they lost money. They won't make the next trade. The big one! If you lost money last time and aren't happy with the signals, you must go back over your program or criteria and reintroduce the correct data that you expect to be required. If at any time data is excluded that you require, your signals are useless. Get the total picture on your plan and not just the pieces. Have a definite signal and not a maybe signal.

There are times when nothing you do seems to work. When things continue to go bad, I can say to you that you have violated another known fact. Diversity helps reduce risk but only in the long term. In the short run we are talking about luck, both good and bad. Believe me, if bad luck comes first, you are finished if you only depend on luck.

Charts are not an answer alone and have no use if your trades can't be executed promptly. Any time you can't do what is required as a trader to get the position on, you will take the scales the wrong way. Remember, you must be in before you can get a correct move.

ALS: What kinds of charts do pit traders use mostly in trading?

POP: I have seen P & F charts, bar charts with half hour, ten minute, down to 1 minute used. I have also seen several of the new popular volume based price charts as well as different color charts with indications of momentum along with price.

ALS: What type do you use when you are in the pits?

POP: I never use anything but mental graphs when in the pit. The mental charts are more point-and-figure charts. They are really easier as I am looking for the third wave to position against the public on the third wave in my desired direction. It works well for add-on positions and keeps my entry cleaner for protection requirements.

I don't go to the pit often anymore unless it is to be an exceptional day indicated by my signals. I will go to the pits when I have an unusually downward bias indicated, as gravity seems faster to me in those markets that reverse to the downside.

Most of my charts are kept on computers, but that doesn't mean the computer gives me my signals during the day. I like to have them before the day begins. It is more mechanical and not ever emotional that way. That is an important point in trading -- remove those human elements as best as possible. Only then can you truly be objective.

Look at it this way. When it is no longer your money, it is easy to do the right thing. But, when it isn't your money, you can also be careless. Just follow the rules and your signals without exception. If they don't work in the long run, you are not using the correct system or you're not using my two rules first and foremost.

ALS: You are still going to have arguments about your two rules as to whether they work for all traders!

POP: We wouldn't have markets if everyone agreed on a plan. We would have nothing but limit day moves everyday. We really need various ideas and concepts. I just want one that will work over time and keep my drawdown smaller than when I first started. I must have a rule that allows me my freedom to know, regardless of what happens today, I will be here tomorrow and the next day and next year and next decade if I wish to be.

Don't ever think that no one ever cared whether you learned anything in trading. I do care and I insist you take full responsibility to learn the correct knowledge. That knowledge must be not only criteria for trading but also the correct method of changing your behavior to that which is required to be successful in the long run. Your trading career should be a long-term expectation on your part. A short time frame is not acceptable in trading. I am not saying that short-term trades are not acceptable but that you must look beyond one day in your trading career.

Some of the best traders started out broke! And then they got more broke. Until success!

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 11: Behavior Modification

Phantom has indicated it is a combination of knowledge and behavior modification, which he learned over his trading career, that are the important elements in correct trading. We will go into some of the observed behavior modification insights Phantom has seen and used over the years. Phantom liked the approach of a professional on behavior modification but felt it was important to present the unique situations that trading presents to traders. Phantom is a professional in behavior modification and wanted to make sure that was known before we began any conversation on the subject.

Art Simpson (ALS): Phantom, you and I know that we are on some thin ice when we talk about behavior modification. You are qualified to give examples of what you have seen and used over your career in and out of the Pits!

Phantom of the Pits (POP): Yes, thank you for being alert on that point. Your point is important, as my methods are unscientific, to say the least.

ALS: Where do you start in changing your behavior to proper behavior for successful trading?

POP: It goes back to history class. Not everyone liked history, but it was a way of understanding prior behavior and events in order to plan for the future. It is the same in trading. We must understand our prior behavior so we can judge what we need to do to make changes in our trading style, if any at all.

A person will make the same mistake again and again if there is not a properly learned reaction to a particular consequence of an event. We must know the right and wrong reaction before we can make any judgment as to what is correct for the situation.

Most situations are pretty obvious as to what a proper reaction should be. Most traders assume their reaction is proper in the consequence of what the market has done. Some traders are better at knowing the correct reaction than others. The correct behavior is a learned process and not one that is always obvious.

Animals are easier to study than humans, and I think that perhaps is a good reason for studying animal behavior. Take a simple action-reaction event for any animal and see what results come about.

Let us say your family dog has never known what hot meant. In the old days when stoves burned coal and cobs, my Grandfather would pick up the stove lid to put corn shucks and cobs in the stove to get the fire to flame a bit. This would ignite the other coals better. He would lay the stove lid down on a fire pot when he was finished on the floor-stove board.

Well, because the dog liked warmth, it would come over to lie near the stove. When the dog lay on the stove lid, he let out a yip you could hear on the trading floor. The dog learned behavior modification by instinct. The dog would never lie on a stove lid again. Now, was this correct behavior modification?

ALS: I've heard this one before. The dog never would lie on a cold stove lid either. I suppose it saved the dog from getting burnt again. In the dog's case I would say it was proper learned behavior. It is the same when your brother threw the hot horseshoe on the ground. He would never pick up another horseshoe again.

POP: Yes, but, you see, traders learn that way, too. They take a big loss and, they will never take that signal to position again or perhaps just won't take it the next time. Now, that is not proper learned behavior. It is learned behavior by instinct due to a consequence of an event. This is just one of the examples I mean when you do understand when I say behavior modification is one of the most important aspects in becoming successful in trading.

How can a trader expect to be successful unless the trader knows the proper behavior to react to an event, especially unexpected events, which a trader seldom is expecting? I think that, along with my two rules of trading, a trader must have a good inventory of what behavior they need to survive and succeed in trading. Something that has been missed on my rules up to this point by traders (in the Futures Talk forum) is that the two rules incorporate behavior modification within the rules.

ALS: Explain how behavior modification is in your first rule!

POP: Look at what the rule states! **In a losing game such as trading, we shall start against the majority and assume we are wrong until proven correct! Positions established must be reduced and removed until or unless the market proves the position correct.** (We do not assume we are correct until proven wrong. We allow the market to verify correct positions, not incorrect positions.)

Rule 1 incorporates behavior modification by expressing the truth that trading is a losing game and that we start against the majority and assume we are wrong until proven correct.

ALS: Sort of like the IRS, huh?

POP: (Smiles) I think their behavior modification is going to be changed, but that is another example. I am not sure we even want this example.

By stating that trading is a losing game, we think differently each time we position. By also stating we shall start against the majority and assume we are wrong until proven correct, we also change our thinking. We should not trade under false assumptions for if we think most everyone wins in trading, our behavior is going to be based on winning protection rather than losing protection. In other words, our focus will be on when to take our gains without thought on taking a loss, much less a quick loss.

We need that correct assumption to be able to correctly incorporate the proper behavior when we have positioned. With the proper assumption we can now include the proper behavior. We are going to concentrate on protecting what we have rather than what we expect to make first. That is behavior modification. This, above all else, is just as important in trading as any plan for entry and exit.

Next, we know from the rule the proper behavior for protecting our positions is to remove them unless the market proves them correct. This is the proper behavior instead of letting the market tell you that you are losing money.

When the market tells you that you're losing money, your reaction to get out is not by instinct because nothing really physical happens to you except that maybe you get a sick feeling in your stomach. That sick feeling as your body chemistry changes doesn't teach you anything about the proper behavior. It is a fact that you will become braver when your body chemistry changes as that is a protection, which is natural. This is not the behavior you want to learn.

Actually, you never want to get to the point of a market move making you sick. It is destructive, and you won't react properly without learned behavior modification.

Rule 1 is designed to protect you from ever being in a situation of distress. In distress you will decide the wrong decision in trading most of the time. There are always exceptions but not all first. Because all traders must start somewhere, why not learn properly as soon as possible?

ALS: I can see some psychology majors challenging you on your thoughts.

POP: Yes, they are the experts on psychology and not on trading. I am not expert on either subject. I am only an expert on myself. That is what I trade with today -- expertness of oneself!

I could give you the reasoning behind Rule 2 with the behavior modification incorporated within the rule but let us leave correct behavior for the readers to think for themselves.

ALS: Okay, let us leave Rule 2 open to interpretation and reasoning for better understanding of one's own expertness, as you put it.

It's really strange how we start with this cheat sheet of an outline and never get to most of the points, and the ones we do, they seem out of order. It goes to show that we really don't have a behavioral plan in such a widely misunderstood field such as trading. I don't think you are stepping on anyone's feet, as you were concerned about earlier in your efforts. How about discussing some examples of observed behavior and behavior modification?

POP: There are so many possibilities, and every trader could come up with better ones than I can going to use here. I will start with the elevator behavior modification.

It was my desire to learn how most people thought in certain situations. It was important to compare ordinary people and then traders. I wanted to see if they thought differently and reacted differently to situations such as getting on an elevator -- pretty simple but yet complex enough that we had enough variables to group data. It was not scientific, but it did give me good insight. Rather than give the exact results, I'll just give the particulars and let readers decide for themselves.

We took an observation at a building away from the trading district at an elevator on the top floor of the elevator ride. We watched those waiting to get on the elevator to see what the behavior would be. We had two criteria: They would try to get on the elevator immediately or, second, they would stand back. This gave us a better-computed programming input by using binary input of one of two states.

The second group we observed was in the trading exchange at the top elevator floor. We assumed most were traders but did not know, without trading jackets, which were off-floor traders. It was important to find out about would-be traders also so we included a third group, which we took to the top floor to observe without their knowing our reason for the tour at that level.

The results were rather surprising. Most of the people would approach the elevator as soon as arrived on the top floor. They had to know if there could be anyone getting off the elevator. Some would even get on the elevator before all the people on the elevator got off. This was strange, but most who got on the elevator before those on the elevator got off apparently did not recognize the situation of the elevator being on the elevator. Those that all who were on the elevator would get off on the top floor. Others blocked the door when the elevator arrived.

A small minority of people would stand back and anticipate the elevator would not go down before all were off-loaded, new people back on and the door closed. They would wait to get in last, and they were the first to get off on the way down. I won't tell you which group did the best because you will have to decide for yourself how you would react.

This little experiment was important because trading is not so different from the elevator. Markets go up and down and trends take off, stall and fall. And then they do nothing for a period of time. Behavior modification for the elevator riders didn't occur to most of the people. It is the same with trading. Who would teach you this?

Okay, we watched behavior and next we would tell the group of would-be traders they would have to stand back because the elevator would be packed with people getting off. They became so good they didn't even care to anticipate which elevator would be up first. Now, we had our behavior modification, but was the elevator behavior modification for the would-be traders? In this case it worked for them because it is what they were told.

Again, not to repeat myself but it is necessary to say it is the same in trading. Traders mostly change their behavior by what they are told. Is this the proper behavior modification for traders? The answer, of course, is no. It is not. A trader must learn from research what the proper behavior modification is in all possible situations. This takes lots of inner soul searching and market data to understand what behavior takes them to the threshold of successful behavior in trading.

You are most likely seeing my reason for stating that knowledge and behavior modification are required for successful trading. It never is an addressed issue in trading, when a trader opens an account, as to what their behavior might be. They are qualified as being financially fit to trade and understanding the disclosure documents that explain the risks but nothing occurring to the trading public flags them to learn about their behavior in situations.

You see, behavior modification is your responsibility and no one else's. You cannot dictate behavior to anyone. All I can do is tell you I feel it is not possible to succeed in trading at all without some sort of plan for proper behavior modification. I could never have survived without it.

Behavior modification can take many directions for traders and can be defined differently by experts. All successful plans have some sort of behavior modification built into the plan. I feel the best plans are those that address the proper observation of trading and the proper reaction of trading.

ALS: I have other examples we have jotted on our sheet here. It might be interesting to give the readers ideas for their own research.

Maybe I don't really think we could give them ideas greater than their own. But I understand they might be interested in some of mine. If we get to a few, that is fine. We have really made the point of behavior modification to the readers, I feel. That is my concern. We can give them a total book on it, but that is not going to help them search their own souls for their trading.

ALS: I hear what you are trying to say. Is there any people in the field of behavior modification who you regard as impressive?

POP: Yes, there is this one genius whom I have always admired and have felt is the only one who I can honestly say has every point in successful trading covered. If I were to tell you who it is, it would disappoint a lot of deserving people who are pretty close to being exact -- especially when exact is almost impossible to maintain for long.

Changes mean changing behavior in trading constantly. I don't know everyone's trading characteristics and, besides, whom am I to judge. I am but an observer and only an expert at observing my own trading.

Really wish I could give you his name, but it isn't fair. I shall tell that person some day. In fact, I have a diary in which I include the accomplishments of great people, and that person is certainly in it. I am not even in it. I don't think I will ever be.

ALS: I think the readers are interested in your view on how they can imitate or change their behavior to be a successful trader.

POP: You are going to get me into trouble with someone. I'll drive around the outside of the track here with another good story and example.

In a basketball camp about 30 students were trying to improve their shooting. Half were taken outside and told to sit down and practice shooting free throws. The other half stayed in the gym to practice real free throw shooting.

This went on for three days of practice. On the fourth day all were given a chance to shoot 100 free throws. The outside group actually did better, even though they had not actually been able to shoot prior to the fourth day.

This was astonishing to the main coach, and he asked the outside group coach why his group had so well. He remarked, "Most of my boys were shooting at the basket and not above it so I called out their name each day and told them to shoot the ball higher above the rim instead of at the basket. My boys improved on the last day as they never missed a single shot in their own minds."

Now, I am not going to paint a picture of the head coach's face, but you can imagine his mouth hanging open and shaking his head. It didn't make sense that this could even occur to the head coach.

It is the same with trading. You cannot rule out any possibility but must have proper behavior to address any situation once it happens. This takes forethought.

You see, what the outside basketball coach did was to incorporate his knowledge of why most free throws are missed. It is usually because the ball never clears the rim getting to the basket. He told his students to shoot the ball higher above the rim. Even though they had not shot a single basket, they were able to improve their behavior through knowledge. They go together, knowledge and behavior modification.

I want to give you a well-known statement, and it is effective in trading, too: "You have to think it before you can act it!"

I am a believer in the small trader. We just need to point out they must shoot higher above the rim to have better odds. Behavior modification learned from knowledge is what they must research in their trading careers if they expect to succeed.

It shall happen in the future that the small trader will learn they can move more quickly than a big trader, and that is oftentimes an advantage provided they know how to use it. To make it happen, they have to know the rules -- not my rules specifically but their own interpretation of what is required.

ALS: What is the most important point of this chapter on behavior modification, the point you want traders to remember?

POP: There are several but the one that is often missed or misunderstood is this: **Trading is a losing game, and the best loser is the winner!**

ALS: Thanks again for your insight, Phantom. I know it's meant as a gift and you are not selling anything or trying to show up the experts. Surely you are expecting some kind of reward here?

POP: Every day I am surprised by a reward. Today an editor whom I consider the greatest editor of all times and whom I have had great admiration for over the years humbled me by pointing to others as the reason for success. I cannot say that about myself and that bothers me.

I cannot point to others yet in my life and say that. It is not because I am selfish. It is because, to be a successful trader, we must stand alone in our days and do it alone. I feel it's very sad until you actually can point to others as your reason for success. It says a lot about a person who can expand his or her horizons by including others.

Trading isn't that type of business. It's almost a solo flight at all times. It's you and the markets. I shall look forward to my day that I, too, can say I owe my credit for whatever I did belongs to a lot of people." When that day comes, I can walk taller and I can reach the heavens! Until that day I can only pass along my insights of trading.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 12: A Wink is as Good As a Nod To a Blind Horse

"There are few things in a child's life that allow a child to play as an adult while allowing an adult to play as a child." **Phantom of the Pits**

Many subjects of interest seem to intrigue Phantom on trading but seldom is there time in a person's life or career when the time to smile and have nothing but fun exists. As a child we all experienced the great fun of a Sunday afternoon filled with surprises and anticipation of newly found fun things. As an adult we often miss the point of a balanced life in most respects and none more than to take the time to be happy, regardless of the current situation.

It seems fitting that Sunday could be one of those days for traders. With electronic trading now and world markets, it is more difficult to have the old days of limited hours of trading through the week and have weekends free.

Still, Phantom wanted to give a smile upon the serious adventures of trading. Today we start with a blank sheet of paper on the so-called cheat sheet so we can convey the thoughts of fun in trading as well as respect the seriousness of the business required. We never know the road and the turn this project is taking until we come upon it. Fitting, since this is written as Phantom's view as a trader's insight into reality of trading . . . nothing more than his presentation into your thoughts in order to generate your own ideas as to what the possibilities are.

Sometimes a question of how to approach any situation can usually be reduced to a series of qualifications of one of two states before going into the next priority of thought. Phantom indicated that, as we grow older, it seems to be natural to oppose change of any kind. Because change is the one thing we can count on, we must learn to use it to our favor even more so as we grow older or we fail to grow at all. This is true in trading and is usually magnified as change takes place.

Phantom's explanation of how the opposition to change is directed was explained as a percentage of the whole. He indicated that, as a child of maybe 6 or 7, we would judge change based on our new adventures of discovery. Over the next year as a child we would grow much more than the additional year of 12.5% from age 7 to age 8 -- mainly that, in that additional year of growth as a child, we would find change an adventure of new-found knowledge and not put restrictions on ourselves.

As we grow older, say from 49 to 50, we have increased our new-found life knowledge by a smaller percentage of, say, less than 2%. Our new knowledge is now not new frontiers of adventure but more of an uncomfortable reality of unfamiliar situations. Because 98% of our known knowledge is more comfortable than the 2% of new knowledge, we tend to oppose any change created by the new knowledge for we strive for the simple, comfortable life as we grow older.

We tend to feel that our effectiveness of making changes ourselves is reduced as we grow older because the percentage of the whole of new knowledge is smaller and smaller each year.

Phantom feels when we reach the point of not caring about change any more, we have severely defeated our most powerful thought process of creativity. Creativity can enhance our ability to accomplish great things and make great trades.

One point Phantom felt about the question of change was that it is important to expand the creativity process best by doing the fun or new thing, which gives us a sense of adventure in our lives. To be young again is not a lost thought if we could decide to be young today in our thoughts and our motivation toward being creative again.

But how do we proceed with our creativeness to overcome opposition to change? Phantom is no expert on such a subject, so he feels as long as we could put a fun smile on the reader's face, it would serve to put on notice anyone who failed to come up with their own excellent ideas or their own answer.

Art Simpson (ALS): Phantom, I know that "A wink is as good as a nod to a blind horse" is one of your favorite sayings. Why is that so great a statement to you?

Phantom of the Pits (POP): My Grandpa was one of the last people to have horses for working the fields that I knew. It really wasn't that long ago, but to younger people it seems like long ago. When I was a small child, my Grandpa would take his workhorses to the field to plow. I would get to sit on the big workhorses, as they were very gentle. Being gentle horses had drawbacks, as they also were at times very stubborn. When Grandpa couldn't get them to do what was required, he would say, "A wink is as good as a nod to a blind horse."

Well, that stuck with me whenever I knew I was correct on something and couldn't convince anyone of it.

Trading is full of situations where that phrase is fitting. There are traders who are as stubborn as the horses my Grandpa had for working his fields. Still, we loved those horses until they died. We never gave up on them, and they proved to be great memories of wonderful efforts of a great team of my Grandpa and the horses.

Today if I take interest in any particular trader's view and I see that view as very narrow or perhaps close to an opinion set in cement, I will use the phrase. It is meant only to provoke thought as to all possibilities rather than leaving a narrow and fixed opinion. There are often times when it is obvious to me that the particular trader is wrong in their fixed and narrow view. I am not making a judgment that the view is wrong but that it is too narrowly based or insufficiently thought out. I will use that phrase to provoke the important re-thinking process to search out new knowledge.

ALS: You must be careful with the statement because there are traders who will immediately think they are wrong and go the other way.

POP: Yes, that is a mistake newer traders will make. To verify an order, a broker will say, "Are you sure you want to place this stop?" The trader will doubt his plan at that point and say, "No, let's hold off on that."

I don't mean to be responsible for changing a trader's mind but only to change their horizon of knowledge and thoughts. I especially will see it as an important statement when a dramatic change is starting to flag our indicators.

A common thought is, "What if I miss the move?" So what? Is there no tomorrow? Okay, you put the position on anyway and you are wrong! So what? You expect to be wrong if you are thinking and trading correctly. It is a big problem only if you don't properly protect your trade as required.

My statement is to prepare a trader for looking and being prepared to act on any possibility rather than being convinced beyond doubt.

ALS: You said we would talk and explore fun things that provoke creativity. Let's just start with being a child again and playing games on Sunday.

POP: Okay, you have given me good thoughts when you said to start being a child again. I can remember when just our family would play a game on Sunday called "Pit." I don't think many folks knew of it that many years ago, but I just recently saw a deck published in the 1920s and that brought back memories of a game that has been around for a long time. It was a game based on trading. Now that I think of it, I can take my introduction to trading back even further.

It isn't my intention to sell the game, but I know there will be a run on it now. Perhaps we should talk *Futures* into licensing its own version for marketing as a courtesy to their readers. The game was an exciting game then and still is today. We would get as many as four decks together and have 32 people at a time yelling and screaming. What fun that was to everyone from 6-year-olds to 80-year-olds.

By expanding the players to four decks, we were being creative. To be creative, it is easy to improve upon anything that inspires your interest. That is what we all need to do to grow, as we grow older.

ALS: Why was the game so much fun?

POP: The game was rather simple and, though not well-publicized, became an adventure of newly found fun for anyone who discovered the game. It was a deck of cards with different commodities on the face of the cards. I remember there were commodities such as hay, rye, wheat, corn, barley, oats and I believe two others. I will leave the two others out to let the readers fill in the blanks as we get them to being a child again. Each commodity had, I believe, eight cards. There was a bell like the one you would see on the counters at motels; you ring it by hitting the top of the bell.

The idea was to deal eight cards to each player, and the first player who had all eight of the same commodity would ring the bell and say they had won. At that point the game was over. Each player who had never played the game before would be shy and say this seems a bit far-fetched. As the game progressed by the rules, the shy player would start screaming the loudest.

Each player could exchange any number of their cards with any other player up to three at a time. If you had five wheat cards and were trying for all eight wheat cards, you could get rid of the other three cards based on the number of other commodity cards you had. For example, if you had two corn cards, you would yell, "Two!" Anyone else who had two cards to trade would trade with you. You wanted to trade all of your cards away except the ones you were trying to get eight of the same kind.

You wouldn't think much of this game without seeing the action it created. All the players would start screaming at once as they got into the game. I remember we had a visitor come by one day when we were playing, and they thought there could be a war going on when we were playing.

"Pit" is the closest game to true trading emotion and adventure to this day. I haven't played it for decades but still remember the fun it gave us all.

If I were a magazine or broker, I would put my advertisement on the cards and give that game to all of my clients at a discounted price. It's a fun game anyone can play within minutes of hearing the rules, and it takes less than 15 minutes for each game. We found it was the best way to bring strangers into a conversation at a new meeting or reunion.

ALS: You're going to start a run here! I am sure lots of people remember the game and would like to get a game or two.

POP: Okay, I know we have the readers thinking and being creative now. They can improve the game and the cards, as an example of showing them the nature of how being creative will overcome opposition to change.

ALS: Why don't you put your picture on the cards and call them the "Phantom of the Pits" game?

POP: Why didn't I think of that? You see, you are very creative, too! Sure, we could do that and give the game to each person who bought a book. In fact, I know you have two artists working on the trademark now.

I realize we are getting a little away from what the traders want to read. Do you think they will forgive us and understand the importance of the Sunday fun point we are trying to make?

ALS: To use your phrase, "So what?" I know you are going to cover it all eventually and interactively with the traders. How can we deny you the smile on your face as you think back as a child would and enjoy the pleasures of being creative. I know the readers and traders whom you have so much faith in are enjoying this as much as you.

POP: Yes, it is important to me. There are few things in a child's life that allow a child to play as an adult while allowing an adult to play as a child. I don't regret bringing up the game I remember best as a child. "Pit" is a game that will sharpen your awareness of your surroundings and interaction with other people without requiring much of a task on your part. Do you remember the game?

ALS: Yes, and a few others, too, more recently. I remember playing drop the clothespin in the milk bottle with a 101-year-old lady. Now, how much younger thinking can you get! If a 101-year-old can go back and enjoy the childhood memories, then why wouldn't a trader be able to understand this importance, too?

Phantom, it looks like you're on a roll here. I remember a well-known writer saying that he felt the books with less in them were sometimes better books. We certainly are giving less in this part anyway.

POP: I know whom you are talking about. I don't know whether he would want credit for that statement or not. I think I know what his point was. It was to express that it was important not to overwhelm readers with too much data, which could do more harm than good.

ALS: I think so, too. Could that be the true Phantom of the Pits who said that?

POP: You're not going to get me to admit or narrow the field, but why don't you ask yourself that question? I guess we can narrow the field, can't we? That is pretty clever on your part. By knowing who POP isn't, I guess you do narrow the field some. But why is it important anyway?

ALS: Okay, I'll drop it. I was just trying to think from the reader's point of view in asking. I am just being creative. Can you be more creative in front of a warm open fire on a cool fall day or cold winter day?

POP: Relaxed, maybe, but I think serenity sets in with comfort. That, too, is important in a trader's balanced life. I really see trading as driving a car around the Indy 500 track at 200+ and having to always be alert at every turn.

That is why it is so important to wink at a blind horse sometimes. You don't need to operate at 100%-plus all the time for you lose some sharpness that way. Come down and go a different direction on thoughts. We are kind of doing that now.

One of the ways a trader can be creative is to just pick up the newspaper on a Sunday and ask how a story they read could be expanded for more information. I like to do this, as very few times do we happen to see the followup story of something that is a question for which we want the ending answer. It is easier to research further today with the news updates on the Internet news posts. Oftentimes, we read news on different trading stories, and we must keep in mind that the view is not ours but the writer's view.

I don't want our discussion to be taken as my views but my effort to provoke traders' views and ideas.

ALS: Yeah, and I know your draft chapters are just a beginning in getting feedback to complete the process of interactive feedback so you can continue and complete each chapter. You have presented ideas, which have generated other ideas, and questions to which you want to respond for the benefit of the readers.

POP: It's part of the reason I wanted a light part in our discussion here before we get into trying to narrow down the needed answers to questions that will or already have been presented. We have many subjects yet to draft before we turn the car around.

ALS: I remember reading an article about motivational speakers recently. Do you see your insights as doing that?

POP: Not at all! Who would want to replace their own intuition of what they see as success with someone else's? It is important to have your own thoughts and ideas. You can't be someone else so why would you want to be totally guided by someone else's idea on what is best for you? Motivational speakers have a place and it is important to be motivated, but most that follow forget one of the most important truths: You are the one who motivates yourself. It must be you. As in trading, it is you who must make the trades, not someone telling you to make a trade.

I see my insights as a guide to knowledge that the trader may not have had otherwise. This always leaves open the interpretation of their own ideas and thoughts. In fact, that is what makes markets. In trading we make assumptions based on known knowledge, and we use theory to prove or disprove our expectations being correct. I am trying to take away the feeling that a trader usually has the advantage when they do not. I am trying to take away the feeling that there is no way to succeed in an unfavorable game.

My insights are not anyone's ideas but experience in my trading career. When I was in junior high school, I and the class were asked to select one of two stories to write. The first one was, "Clothes don't make the man;" the second one was, "Clothes make the man." I chose "Clothes make the man." It was the worst grade I ever got.

The teacher was biased toward clothes don't make the man. Well, I chose the one I felt would be the hardest to prove with theory and assumption. I had good arguments, and I think to this day that I did the best piece of writing in that class. The teacher had her mind made up: Anyone who chose what I chose would be wrong. "A wink is as good as a nod to a blind horse" was what I thought of the teacher's grade.

I have proven that I was right in my lifetime, and I think that story is part of my success. You see, a person must believe something and then proceed to either prove or disprove their theory. My theory proved out over the years. My theory of clothes make the man built my character and my determination that I would someday be able to prove in fact that it was, beyond theory and assumptions, true in my case. Now, that does not mean it would be true in all of the classmates' cases. This is what the teacher missed.

ALS: How did you prove you were right by fact?

POP: My assumption was that how a person feels affects their actions and reactions to situations in their lives. My main point was that someone who had good clothes and was dressed well would have a different feeling about themselves than someone who would be wearing, let's say, just shorts in important situations. The key was "important situations." Can you imagine being at a funeral in just shorts? How would you feel? Wouldn't your actions and reactions be more agreeable with your feelings if you were dressed in good clothes? Of course, they would.

My fact proof came as a parallel to that article. I considered the well-dressed person and the well-knowledgeable trader as a parallel in points of feelings. In the pits trading with good knowledge (well-dressed) I felt more confident in trading. When well-dressed in correct situations such as meetings and important events, I felt better confidence and my effectiveness was much higher. True, I am the same man, regardless of how I am dressed, but I am not the same person if I have not prepared my knowledge before I trade.

For the traders, I want to impress in their minds the same parallel. If you trade with lack of proper knowledge and behavior modification in situations the market will present you with, you are only wearing shorts at a funeral. How does that makes you feel? It certainly won't say to you, "Clothes don't make the man!" It will strike you to know that being prepared properly is the same as having the proper clothes for any situation.

ALS: Okay, did you ever want to get back at that teacher?

POP: I don't think I was smart enough to know what getting back at someone even meant as a child. I had lots of stars in my eyes. I still do, for that matter. It is a waste and non-productive of time to have anger or greed or regret or fear.

ALS: How about hope?

POP: Hope and love have a place in my life. Hope must be tied to action and plans. Love is my reflection of what I have given or am willing to give.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 13: Quicker Than the Eye

"You really are looking at it reverse image. Sometimes it is important to see things differently than others." Phantom of the Pits

Usually a newly placed trade in any particular market is placed with the greatest optimism and with human elements of hope for its correct movement. Perhaps the hope for the correct movement is what keeps new traders interested in trading the market's inability to carry more times than not. Can it be possible that it is easier for a trader to do the wrong thing, or is it that, when a trader makes a trade, all the other information comes out two minutes later?

We will explore Phantom's insight on why things seem to change rather quickly when a new trade is established. Why does the market seem to know when we have placed a new position? What does it take to expel this type of thinking and reaction to our newly placed position?

At what point do you feel that it is the other traders against you in trading? Why should you feel that someone who is playing against the market is now your enemy and in the drive side after you have just positioned yourself? Doesn't everyone?

Is it possible to do just the opposite of what we think is correct and come out ahead because we seem to do what we think is right and we are the ones who are wrong? We are thinking instead here, and that is the one element that no one seems to have at the time of researching a position or entry. Once a position is placed, it becomes an element you have to be able to deal with. We get excited when the position moves our way but become complacent far too often and not totally prepared our hard-earned money position for positioning.

Art Simpson (ALS): Phantom, I know you have said you are not an expert on anything except on your own trading. I also realize we are only talking about your insight and that you have said it is important for each trader to have their own develop his or her own ideas from insights they formulate from observation and research.

Sometimes it helps other traders to know other points of view on a subject. We know that everyone has his or her own ideas and insights on the marketplace. Why do you think it is important to view other people's insights as a way of understanding our own behavior?

Phantom of the Pits (POP): I've read good books on the adult-child theory in trading. We are not as the child, the traders other people are against at that point. Our thinking must become adult in trading, and that is from understanding and knowing what is correct. As a child, we don't need a reason for what the rule. As an adult, to be effective in trading, it is important to know why and not just the rule.

It is difficult to convey to someone an insight of what happens when a position is placed because the person you are trying to convey the information to has the same position on and effectively has the same environment.

Just a simple thing as changing a flat tire is a good example of what I mean. If you are not the person who had to change the flat tire, the feeling of frustration is not there. In the absence of this, you are going to be more removed from the important feelings of such an event. Trading does have the same type of removal from a situation of a particular point of view as changing that tire.

Most traders are placed with good reason and backed with good research. If the trader didn't feel that it was the right time to be successful with that trade, they would never want to have made that trade. That feeling of better-than-average probabilities is self-defeating because, with that feeling alone, it is possible to miss the big moves by being wrong first.

Have the nature of wrong positions a tendency to be wrong, and that is a key in better trading. It is not natural to feel other than optimistic about a trade. What must be done is that the optimistic view must be positioned beyond the initial position.

The most important point of a newly established position is to understand that the initial entry of a trade is only a small part of the expected process of trading your position. Look at it as if you are going to make a series of trades anytime you get a signal. You must have the latitude of knowing and doing what it takes to position yourself with a position that reaches to your goal. Your goal is the important part and not the trade you have just entered.

It were to tell you that your signal to enter a market has the criteria that you must stick with protecting that initial position and adding to that position as quickly as you can, would you be able to reverse your position as many as three or four times. You would be more agreeable and prepared to have the ability to do that than to reverse your original position. That thinking would make it easier for you to make the needed adjustments to your position. This is what you must do when you enter a position. You must know that the initial entered position is just the beginning of your trade.

Rather than taking a position and letting emotion enter the picture, you must understand that position does not justify emotional involvement. Emotion is a very strong feeling because before emotion even enters the trade by removing the position. You can re-enter the position correctly again and again and not have the emotional effect that position. If your position brings emotion into the picture, it is usually wrong or the wrong way.

The market will seldom comply with your position at first, but that in no way says not to trade correctly. A lot of times your entry is at the place where many think the same as you. Don't ever feel bad about this because you're not alone in your thinking. It is that you seldom can be right at the right time.

The edge you have over everyone else's thinking is that you know you are quicker than the eye. You can remove your positions quickly because you are alert to the idea of knowing you can re-enter immediately or quickly. You can do this as quickly as you can, would you be able to reverse your position as many as three or four times. You would be more agreeable and prepared to have the ability to do that than to reverse your original position. That thinking would make it easier for you to make the needed adjustments to your position. This is what you must do when you enter a position. You must know that the initial entered position is just the beginning of your trade.

Rather than taking a position and letting emotion enter the picture, you must understand that position does not justify emotional involvement. Emotion is a very strong feeling because before emotion even enters the trade by removing the position. You can re-enter the position correctly again and again and not have the emotional effect that position. If your position brings emotion into the picture, it is usually wrong or the wrong way.

The market will seldom comply with your position at first, but that in no way says not to trade correctly. A lot of times your entry is at the place where many think the same as you. Don't ever feel bad about this because you're not alone in your thinking. It is that you seldom can at the right at the right time.

The edge you have over everyone else's thinking is that you know you are quicker than the eye. You can remove your positions quickly because you are alert to the idea of knowing you can re-enter immediately or quickly. You can do this as quickly as you can, would you be able to reverse your position in the correct way. You are going to always do the correct thing. Be swift! You can stop this emotional feeling of always getting in at the wrong place immediately, and it will soon become second nature to you.

If you find that you feel you are wrong as soon as you enter, remove that position because you are right (in removing that position!) Why do I know this works? I know that some of my best days and trades are when I simply remove the position. Learn to understand that an existing wrong position is the best excuse to get a good position.

So what if you are wrong and wrong and wrong again. The best part of being wrong is that you are going to do the right thing when you are wrong. Learn to stop your position. Listen to your inner thoughts on being wrong, and when emotion becomes an element, remove the position. It really works. Emotion is the enemy of a position in a very, very, very, very, very, very position.

ALS: It seems easy to say but how about executing the idea of getting out when emotion shows its face in your trade?

POP: You must make it a mechanical thing. It can be done in various ways. Most new traders don't have enough funds to diversify property so they have several positions, which gives them the opportunity of throwing out the bad and keeping the good with lower overall risk proportionally.

There are other ways of making the removal of emotional positions mechanical such as when you use Rule 1. You are not going to become as emotional when a position proves correct as when it proves wrong. Rule 1 gives you the ability to listen to yourself without emotional distress of knowing that you and not the markets are going to tell yourself that you are wrong in a position. Your emotional distress is what causes you to remove the position immediately. Do that without hesitation, and it becomes mechanical to you.

Isn't the purpose of Rule 1 to also listen to yourself and not the market on telling yourself when you are wrong. If you do that and not the market, you will be more mechanical in trading, which now will affect your judgment and decision to remove a bad position properly. Because we will allow the market to tell us when we are wrong but only when we feel we know that we have something tell us when we are wrong. What do you think that is? There is probably not a better signal to you than the beginning of emotional involvement in your trade.

I know it take practice and a method of behavior modification, which you must devise to help you work with the implications of emotional elevation when wrong in a trade. You can do it as well it is habit after a little practice. It is not difficult to learn if you can learn to be a stranger each day and say good day. After a period of doing it, you would find it second nature.

ALS: Aren't you going to give us your methods or suggestions for helping with the behavior modification on getting out of bad positions?

POP: If you have unbuttoned your top button on your shirt, you had better get out. If the phone ringing irritates you, you had better get out. If you are beyond your reasonable time limit to hold a position and you are not comfortable with it, you had better get out.

We know a broken clock is right twice a day. You could assume that when you don't know the position is correct, you just as well reverse as you still won't know, but you can be sure you will soon know one way or the other. Of course, this isn't a very good assumption so it will actually keep you on your toes more than anything else will.

This can also be a dangerous way to position but, believe it or not, I have seen day-traders position this way to establish a position when their mind is not prepared. I do not personally recommend it, but I don't advise against it if you do it with good research of non-trending markets. Sometimes you can be very successful when you have the correct market and trade. The opportunity is that you correct a bad position and profit from that wrong position being corrected. It happens more than not if you are alerted to this thinking.

Death is all I can see by impressing on the reader the importance of stops. The surprise is often the other side of our current position. Just because we have the expected side of a trade does not prevent us from going with the surprise side when we know our position is wrong. In a recently proven position, we never go against that position, though.

Keep your loss small and quick; act early while you have the opportunity, otherwise you will allow bigger losses to affect your loss taking and thinking. This is why I call entry the conscious time of a position. It is your first time to make a decision on that trade. The first opportunity to keep losses small is your best opportunity. What you do immediately upon entry of a trade determines whether you will be successful or not in the long run or even at all.

ALS: I have often heard traders make the statement they should just do the opposite of what they think and they would trader better. What do you think of that statement?

POP: It also have heard that remark. I know my Dad thought that was a good strategy in my early trading days, but it does have merit. Don't get this wrong! The market is not that it is good thinking to have a plan for acting upon that thinking. Plan to know that what you do has a good possibility of being right and have the ability to be successful as soon as you know you don't have a proven position. This works better in non-trending markets.

Isn't a say you know a big news item is going to come out or you have just been given data that it's big news, I'm sure you would like to be long or short in that market, but you don't know any more. Most traders will trade accordingly and, when wrong, get out and that is that! Well, doing the opposite is the correct way to do it. It is correct because you are now allowed to be bigger with after the data. It is important to avail yourself to all sides of a market in certain situations such as reports.

So you must admit the merits are true in a sense of that statement. You can do the opposite of what you think, even though you did something that was wrong at first. Isn't that the same as doing the opposite of what you thought was right? It is a foundational idea.

ALS: I have another question that just recently became pretty important. On a news channel, an interview with a particular expert was like throwing gas on a fire. The traders who were mentioned counter on a remark made that the interviewer was making the market move and by making such a statement. Is this appropriate to have such remarks made, and is it destructive relative to let it affect our trading?

POP: It happens all the time. That is the first assumption you must make for it is true you will be more sensitive to a person's remarks that are counter to your position. And I suppose that is okay to be sensitive as long as you keep your position out of it. But remember that it is when you see a big slide or big runaway market is hard and almost impossible to ignore.

The true test of such remarks is what the market does in reaction. I have found over the years that markets do react to such remarks. But, that is the key. You must see what the market in reaction. You can use those reactions to your advantage if you remain swift in your market moves. In fact, you must be swift, and you must use what the market gives you for your advantage to position for profit.

Here is why you will tend to have more than one reaction. The local traders will see the news or even a report of data first. Their reaction will be as a professional, and they will position according to their beliefs. At first it won't be in unison but it will pick up a cadence of sorts, and you will see some kind of trend in pricing early. That is usually your first wave of buying or selling.

Next come the orders into the pit from those who have just gotten the news, and you see a further reaction to the news. The third wave of news is the customer (public) who has been held the news and has contacted or been contacted by their broker. The third wave is usually by the strongest because the willingness to fade the news is less prominent when they have to reach the pit. This is when you have your thinnest market and when markets make new highs or lows.

After all three waves of orders are filled, you still have your strategists who take positions upon learning the news. They will take a long time and will tend to enter the market. The news is seen on TV, heard on radio and read in the newspaper after the market is closed. That is part of my weekend-a-half course on news items and their effect on markets. Remember that it is a half of response and reaction to data or a critical news remark, the market usually comes to a balance of understanding and pricing.

The second part of your question is that it is not constructive to become emotional about a news remark, but you should recognize the opportunity of such a remark being a mechanical reaction you can make to capitalize on profits. Don't allow yourself to emotion from such a remark. This sometimes will take a couple of days to play itself out.

It is important to understand that this can change the continuing trend, counertrend, non-trending or ranging trade and overall strategy of trader's signals. The market, the news seen on TV, heard on radio and read in the newspaper after the market is closed. That is part of my weekend-a-half course on news items and their effect on markets. Remember that it is a half of response and reaction to data or a critical news remark, the market usually comes to a balance of understanding and pricing.

ALS: With a slide of the hand and quicker than the eye, we seem to get back to the same things in successful trading: knowledge gathering and behavior modification. Isn't this most everyone's theme in trading?

POP: You know, I don't really know. I only know what I have learned over my years of trading. If it isn't most experts' theme, I would venture to guess it soon will be. I know there are those who well-read this to improve upon their trading into successful results. I know they can understand the problems of trading better because of what we are doing. I am not out to disprove any successful method by presenting my views on trading but only to enhance the possibilities.

ALS: I think there will be critics of your views.

POP: Do you really think so? I disagree with you. I am wrong in the markets a lot of the time, and I don't think you are right with that statement. I'm sure I'm going down one of two roads. Unless you go down both of them, you cannot say you chose to take the wrong one for the better view along the way.

Pick the same in trading. I have presented a view along the way. It is just that I have been down both roads, and I can accurately express which road I feel is the better one to take. I am presenting an opportunity to expand knowledge and improve upon trader's minds. I am not presenting a limit or restriction to improved thinking on trading systems or criteria.

To be a critic, it is important to look at things from all views. You look in a mirror and you don't even see yourself the way others do. It is important to see the other side. Maybe you must be able to see as others see. You must not rule out the reverse image as a correct view.

ALS: Is that what you consider your rules, reverse image?

POP: Very interesting observation. I suppose you could call Rule 1 a reverse image rule from what others see. It is just the opposite of most people's understanding of what is necessary in trading rules.

We do make the market prove it right rather than wrong, and that is the reverse of common thinking. We do assume we are wrong and let the market prove us differently and correct. That is also reverse image. In Rule 2 we do press our winners, and that is the reverse of taking losses or the other side of the coin.

Yes, I guess that by looking in a mirror you could easily understand why others do not see as you do. You really are looking at a reverse image. Sometimes it is important to see things differently than others. I have learned that it is trading to be different. You never need to conform to anyone's view but your own trading. Don't forget that! Use your own ability to improve your behavior in trading.

Futures Magazine home page
Other learning opportunities

E-Mail: artsimpson@aol.com

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved.

Phantom's Gift

By Art Simpson

Chapter 14: Your Comeback After a Big Drawdown

"You want to establish your position prior to the increase in volatility. This will be your entry of the fourth day when the market breaks above the prior four day's highs."
Phantom of the Pit

Art Simpson (AS): Is it true that you have saved the best until last in your implicits? (NOT: Phantom of the Pit was written, but this chapter was not!) Implicits (NT: however, due to market response and questions, the Phantom elaborated on some insights and presented other thoughts in additional chapters.)

Phantom of the Pits (POP): You will see as clearly as anyone can see that what I am going to tell you is the most important information in the book. Some of it you have read before. Much of it you have read before. Much of it you have read, you have read, I will send back many thoughts to the cleaners.

There are great coaches, great advisors and great traders in the world of trading. There are great editors, great reporters and great teachers of trading. They all have a reputation. They are well known and well respected. Some of them are very, very good at what they do. Some of them are very, very good at what they do and they have a reputation that is well deserved. Some of them are Gibson, Oprah and my brother. They have learned how to carry such heavy baggage in their lives.

Who I am is always going to be more important to myself than anyone else in the field of trading. I am the person who has to live with the results of my trading. I am the person who has to live with the mistakes I make in my trading. I am the person who has to live with the rewards I bring in your life for it to be possible for you to become the trader you know you are capable of being.

I am the person who has to take the time to take the time to be the person who can be of value in your trading to think that your success is because of you.

I am the person who has to understand that I am the person who the events that have taken place. I am tell you that my birth in the small trader is no when. As I read your brother's memoirs to John Gibson, I realized that I am the person who has to understand that I am the person who has to be the person who I am. I am the person who has to be the person who I am. I am the person who at the moment just coincidentally more for my imagination to make it as I will, or was I supposed to make it as I will, or was I supposed to.

I am figure theorists pretty well from the facts I am given, and I can assure you that you and I are the same person. I am the person who has to be the person who I am. I am the person who has to be the person who I am. I am the person who could imagine a trader who has the ability to understanding I have received over just the last two weeks (NOT: from Futures Talk forum discussions and questions) and I am the person who has to be the person who I am.

I have it calculated we could put no less than a 1,024-page book together of those we can put together. I am the person who has to be the person who I am. I am the person who has to be the person who I am. I am the person who has to be the person who I am.

I can tell you that our experience has opened our eyes and unlocked our hearts because we have seen the results of our trading. We have seen the results of our trading. We have seen the results of our trading. We have seen the results of our trading. We have seen the results of our communications, the markets are quicker today and my rules are even more appropriate.

I can tell you that our experience has opened our eyes and unlocked our hearts because we have seen the results of our trading. We have seen the results of our trading. We have seen the results of our trading. We have seen the results of our trading. We

Phantom's Gift

By Art Simpson

Chapter 15: Is the Market Always Correct?

Nov. 28, 1997

Everyone knows the market is always correct and correct, and there isn't reason to even dispute this belief. Most of our beliefs have been previously written or have been stated to us over decades by experts.

Phantom has hinted his feeling as to how he felt about the market being correct. He made the statement that he didn't always agree. We felt it would be an important insight into trading plans by looking at his view on the subject.

Art Simpson [AS]: Phantom, do you feel the market is always correct?

Phantom of the Pit [PP]: Art, I'm surprised you don't know I get pissed at anyone who proved that to be a correct statement? Or can anyone tell me who proved it? This statement is the biggest crutch traders are buoyed against. It's bullshit.

AS: They're going to put you away with that kind of statement. They're going to lock you up. You are going to lose all of your credibility unless you can make a good case for you statement Phantom. You are going to have to explain yourself.

PP: I guess I appear to be bad with that statement. The experts seldom know or understand what they are talking about. A trader expected to be a winning gamer. It is the same with the statement that the market is always correct. Whoever thinks it is possible that there could be wrong in the market? Who is the fool who made up that one? Who believes? I see the market as a continuing image of liquidity. A liquid market reacts differently to news than a market with liquidity problems. Is the market liquid? Is it fair all, which is the purpose of floor traders in the pits of different markets? It is to provide liquidity.

Markets are the most fascinating, interesting game. Traders and investors tend to be sloppy in price determination. We have the reason for different markets and the creation of new markets. We have new markets like AUTUCKATS price discovery.

If a news item is bullish or bearish in a non-liquid market, the bid and ask spread is usually wider than in a liquid market. Now, are we to believe a wide spread on bid and asked price is a correct market? Is it correct? Is it fair? Is it fair to the buyer? Is it fair to the seller? Is it correct? We have seen those wide spreads. I tell you the spread is not always a sign of a bad condition of demand and supply a lot of times. Not having an offer to sell is not the same as not having any product available. Sure, it can have an effect on pricing, but it is an artificial condition.

These artificial market conditions don't mean that it is a good trading plan to chase. Sometimes it can be. It can be a good trade. It can be a bad trade. It depends on different market conditions. Human emotions. Every trader knows what I mean. Fear and greed is always correct. The market is always in a process of moving away from what it currently says about a price. Does that say it is correct? Perhaps it is more correct in more than a day.

AS: Yes, that is the first lesson you taught me in trading. I didn't even know why you were there. I learned that from you. It didn't take me long to respect you and watch you in your pit. I watched you make a lot of money. I saw you lose a lot of money. I saw you get out of your pit when there are those wide spreads. I saw you take a loss by the emotion driven spread. You once began this pattern that locally corners from the reflected image of the market. Do you agree about that?

PP: A simple statement about markets being more than a day can change a person's thoughts and lead to a different outcome. It says the market is changing every day, and what it knows now is never the same as what it knew yesterday not correct for today.

You often see larger market moves in thin markets. Those who direct a fund know new prices are coming in and they are willing to pay whatever the price is because they are willing to be in the direction of their indicators? This does happen.

Is it wrong to say the market is correct when it is not clear in thin markets at all times? I am telling you to look at both sides of the coin in thin markets. Why? The thin market move is not always correct. The market is in a process of building or unwinding when liquidity enters the market. The fund positioning in a thin market is going to see a slight advantage on thin days. The fund that requires a large position in a thin market is sometimes forced to pay more than it wants.

When funds take profits in a thin market, it hurts their average price fill because the market will move farther than in very liquid markets. So it is a double-sided edge where there is a good trend and a bad side. The bad side is when the market is ready to reverse and the fund is caught in thin markets. It is important to have the knowledge of the difference of thin and liquid markets. Most traders don't know or care most of the time because they are caught in the middle.

Markets are more than a day! This alone tells you not to believe the markets are always correct! This is a good reason to use Rule 2. Not all of your position will be established until or unless the market proves you correct.

AS: Isn't this a conflict to make the market prove you correct while not always believing the market is always correct? Isn't that a conflict in your statement and in your trading?

PP: Isn't this the same conflict most traders use to get out of a position by getting stopped out? Even the market even thin on the day they get stopped out? This is what traders think when they get stopped out. Isn't it correct? Isn't it fair? Isn't it the truth? Isn't the market only a day? Isn't it better to be stopped out of a good position.

Why shouldn't we turn this situation to our favor by using another rule in trading? Yes, there are those who use trailing stops and other methods of protecting profits. In the past, I have had my position I kept and then looking for a limit rule, they have come close but not exact to Rule 3. They wanted to get out of their position at the close of the day. Yes, I understand that but they all have agreed they just could not justify a criteria for Rule 3 telling them when to take a profit.

You see, my Rule 3 takes into consideration both sides of the market instead of just taking profits. It also gives them a reason to take position off when the market moves in their favor. Rule 3 profits and other times it will be to offset any position when the market's criteria says to do so.

Rule 3 uses the criteria of the market not always being correct.

AS: Do you want to explain Rule 3?

PP: No, I don't! I want the traders' input now that they know they have been on the right track of Rule 3 but not quite getting to the important point in the criteria. I want them to think about it and give me a report. I'll tell you this much. They just state Rule 3 without a lot of thought on their part will make the rule a little less useful to them. We need more information for them to understand the rule and how it can be used in their trading.

I have indicated on the *Futures* Talk forum the importance of several aspects on offsetting positions. There have been several questions and comments on it on sights. Some would read my posts to the forum are picking up on it. You'll be surprised at how punctual and accurate I am with the ideas. I'm still receiving mail from people who have contact about a Rule 3 or other ideas.

We have traders for years and decades saying they see the market reflects all the market conditions by just looking at the last price. They continue to trade based on that fact. They ignore their trading program because they feel they know what the market always being correct. Why shouldn't I use that to my advantage with a Rule 3? Why shouldn't traders take advantage of that knowledge? Shouldn't traders use that knowledge to their advantage?

I want to state again. "It just never occurred to most traders the market could be wrong" They don't want to hear it. They don't want to see it. They don't want to be wrong. They don't want to be right. They don't want to see there is so much conflict in their trading plan. I'm saying the market is not always correct and that liquidity and timing are important to understand in order to make good decisions.

In making this assumption, wouldn't this help in positioning and exits? It is not complicated but another rule to keep the advantage of a situation from being unfavorable at all times. My rule looks at the liquidity and timing of a position and uses that knowledge for the trade.

Let us further explain our position on this thought? To review the statement,"Is the market always correct?" Most traders have proved that they could take the market always being correct. Why shouldn't I use that to my advantage with a Rule 3? Why shouldn't traders take advantage of that knowledge? Shouldn't traders use that knowledge to their advantage?

I want to state again. "It just never occurred to most traders the market could be wrong" They don't want to hear it. They don't want to see it. They don't want to be wrong. They don't want to be right. They don't want to see there is so much conflict in their trading plan. I'm saying the market is not always correct and that liquidity and timing are important to understand in order to make good decisions.

Say, for example, a report came out that the orange crop was the smallest in history and the night before the report we had the worst freeze in history in the Florida crop area. Based on fundamentals, the market would open up the limit the next day. Based on technical indicators, let us say the market shows a bullish trend being established. Before the open, the market is up the limit. Based on the news, the market opens lower than yesterday's close and the market never comes back to trade at not one trade in minutes.

Now, the market is open and no trading is taking place and OJ is limit offer two hours into trading. The experts and the reports in the news make the following statement: "Well, we see the market is correct in opening lower. It is always overpriced."

How can you say that the market is correct when there are no buyers willing to buy? Any trader who is willing to buy back from the shorts? Is it fair to force the market to be right in my book! It only shows me there is no liquidity in the market at this time.

Say the market closes limit offer. Now, are we to believe that from close to tomorrow's open the market is always correct? Is it correct when there is no correct during the time it was closed and there is no market? How can the market be correct when there is no trading?

Now, we have a very good chance of a gap open and all are wrong and we get stopped out the entire day. No additional news is available except the news reports stating, "The market proved to be correct today in the fact it was lower at the open."

The only thing the news reports did for the last two days was to state the market was correct. Yesterday, the market was up the limit move and the news reports stated it was a good thing that had an hour. Is the stock market right because of the halted trading?

What is it we are to do? Do we just sit there and let our position ride our equity and balance our accounts, other criteria must be used to understand if the market is correct. I am not sure you understand what I am saying but we need to have another example.

AS: When we say "markets", are we talking about the price of a contract currently or does "market" mean what is or has happened over time in a market action of a contract?

PP: That is a very good question. Yes, and the question should be answered. You have reports the market moved up today. Is the market correct in moving up? Say it opened lower and closed higher. Is the market correct? Is it correct to say the market is right in the direction this day no change in open interest exists at this point. The only two left in the pit are the two traders.

All of a sudden someone bought wheat, and it went limit up within 10 minutes. Now the pit traders in the broad pit are willing to sell wheat. Yesterday, it could be bought back at the close and now bread is bid limit up at 76 cents. The locals are eating lunch, and the position traders are willing to sell. The locals are willing to buy back what they can. Is it correct to say that the market closes limit bid.

Is the market always correct and correct now in bread future? I still only see the market is not liquid. I don't see this as being a market that is correct. Okay, the experts say that, yes, the market is always correct and the market is correct because demand exceeds supply.

No one wants to sell, but this may not be correct just because the wheat market went up. Traders think this way, though, and that is why I always look to sell the weakest market in a group of markets. I want to see a similar thinking toward the bread market that is bid at the goes limit up, bread should go.

Other, there are unrelated unwind the positions are or can be filled. At that point the true market takes over when there are now no buyers. There are times the markets are not correct, there are unrelated unwind of great positions in the market.

You would never think of this side of trading if you only see the market is always correct. The experts are going to tell you the market is always correct and there is no reason to even give the opportunity of the surprise side is often because of the market not being correct.

There are times I do not consider the market correct. I feel it is useful in questioning the market and its correctness. Yesterday, I had two different time situations where I expected the market to be correct, then there is always a possibility the market is incorrect, and I must be prepared for it.

Some days when we are seeing a topping action and the market makes several moves up and then back down, the market is not necessarily bullish anymore. Is it correct to say the market is correct? With good liquidity, I consider the market correct. With poor liquidity, I do not consider the market is always correct because of liquidity disorders.

Anytime I consider the market distorted, it is my judgment as to whether I consider the market correct, and I do not always do what the market says.

AS: Isn't that just another technical indicator you are using rather than debating the correctness of the market?

PP: If a market moves limit one way or the other and no trade takes place and you have both a gap and lack of liquidity, you can call the gap a technical indicator, but the lack of liquidity is a different thing. It is not a technical indicator. It is impossible to trade without liquidity, and those times are flagged as not fit for trading and a not-correct market.

You could have several days in a row of limit moves without the ability to establish a position. Which day do you want to pick as the one where the market is correct? Would you pick all of them, none of them or any one of them?

Art, let's go back to the traders for input on whether the market is always correct. They now know there is a Rule 3 to take advantage of the market is not always correct. We shall state Rule 3 some time.

AS: Okay, we now wait for input is the market always correct?

Part II: Is the Market Always Correct?

There are great traders and many great ideas. You usually can tell the great ideas from the mediocre, and in our search for new ideas we have received from Alfredo A. Ramos very worthy indeed. We felt the following post by Alfredo A. (on the Futures Talk forum) important enough to put in this section.

Alfredo A.'s post:

PhantomAnvil at Was traveling the past two weeks. Am excited by your concepts and developments of an eventual Rule Three relying heavily on volume/open interest/liquidity. I think you are definitely on the right track.

I personally don't like and stay away from illiquid markets. We have all seen OJ go limit up for three days and finally trade at the end of the fourth with no liquidity. Who in their right mind would you want even have a chance to implement Rules 1 and 2. (This is OJ, never mind pork bellies.)

I like to watch DIV (on-balance volume) and be wary of major divergences. But a market (OJ) that consistently closes on the bid, DIV is useless. Its absolutely meaningless. Yet I see volume price fluctuations, not to mention eventual attempts at manipulation, resulting in impairment of liquidity.

As for the markets being "correct," I daresay they are never correct, and that that's where you have a chance of making the money. The only "correct" market I can imagine is the SPIT market, where someone actually stops and the other side actually tenders the merchandise.

Even the date of expiration of a gold contract, the last contract tendered is, say, at US$380 per ounce, then that perhaps is as "correct" a price as you can get. But as for futures, the very futures contract itself represents an infinite series of future prices. Perhaps, especially for traders; for a market to be "correct," there would have to be, by definition, unanimity. I think of Orwell's Animal Farm and the phrase "unanimously incorrect." (Dogs, the proportion of being proven correct.) But I also guess this "incorrectness" adds to the fun of the game.

But, yes, I myself prefer to trade very important markets, both as indicators of liquidity as well as giving us inklings about where prices might be going. It's a shame the exchanges can't get their act together and do with volume, but I suppose that would be an operational impossibility.

Best regards and good trading.

Alfredo A.

Phantom felt Alfredo has lots of great ideas, and when we are fortunate enough to be associated with them, we should listen closely.

We need another chess piece on the board, and many of you have ideas and feel open interest and volume are very important. Alfredo A. believes, they are important in determining liquidity and give good feedback about where prices could be heading.

I believe we can have room for another more useful piece to improve our trading. Phantom took note of Geoff Hughes' thoughts as they show some interpretation of the importance of volume and liquidity.

Geoff Hughes' view:

PCP, what I think you are telling us is that Rule 3 pertains to volume. Volume = Liquidity. If a market rises on low volume, the market is incorrect, and a short order would be the best way to enter. The opposite is true if the market falls on low volume, the market is correct, and a long trade would be the best route. This pattern would be reversed on a market that goes down. Open interest is also important. Rule 3 = Rule 2 + Rule 1 + Open Interest. Volume is an up-market, shares are covering their losses. I think that's right . . . not quite sure . . .

Phantom liked seeing Geoff's excellent interpretation of questioning a market with price and volume. David Fisher had good input.

David Fisher's post:

Phantom, ALS and all, Thanks for stirring the creative juices on this forum. I'm certainly a beneficiary of the effort. On the subject/topic/thing Rule Three, I remember reading a while back that Phantom had mentioned he looked to take profits within 3 or 4 days of high-volume days. Pits must be profit taking.

After reading the last posts, I attempted to build an indicator that would show me current volume relative to recent history. What I came up with was current volume divided by 60-day moving average of volume. I then smoothed the resulting ratio with a 10-day moving average. Then I plotted the ratio on a chart. The result was smooth in all but one way.

Then, using Phantom's 1/3 theory, I put alerts at 67% and 33%. Tell me if I got out on a brain fart. This could be interesting if it proves to be indicative of the price-discovery process. Anything in the upper third of the range could be considered "correct" price discovery, and anything in the lower third would definitely be suspect. Nothing special about the exact numbers used.

This seems to make sense. Any thoughts on this, anyone?

What do you think of David Palmer's ideas? Phantom was impressed and indicated, with good testing, even if the results are not perfect, it would be a very useful tool. Phantom felt you will call it the Palmer indicator after David Palmer. Think this one over and put your thoughts on paper.

Randy Hogan always gives his thoughts plenty of time for accuracy and they are always well thought out. Take a look at his thoughts on Rule 3

Randy Hogan's post:

Art, A thoughts . . . how often are markets thin? Can you tell a thin market as it's trading or does Rule 3 criteria get us away from the effects of making a trade in one?

Phantom's thoughts on Rule 3 are very interesting. Do you have a feeling that the market moves in your favor (near high of day on a long, for instance). If the market doesn't follow through immediately (the next day) the market is probably not in your favor. Phantom's offers, a.k.a. the position is "offset." Is this Rule 3 protection?

Can a thin market be considered correct more than 1 day? Rule 3 criteria changes daily so the market must continue to prove, eliminating the possibility the position was taken and added to in an "incorrect" market.

That was a stab in the dark (with maybe a little light on the background)!

Thanks . . .

Phantom's thoughts on Randy's ideas were that Rule 3 should do as he asked in getting away from making a trade in illiquid markets. Thin markets certainly can last more than a day. Alfredo had a good idea in OJ.

Ulrich always questions both sides of a situation and has good insight. Phantom wanted to include all of his thoughts in this post enough to place the market is not always correct, a very big and unpopular stand. Here are a couple of Ulrich's ideas:

Ulrich's ideas:

I stated the market is always correct before. I meant it in the way that your equity runs will always reveal the truth. If you lose, YOU lost. Not the market, the broker, etc. It was you putting on the trade, no one else.

The market itself is wrong most of the time. This is what gives opportunity to trade. If the market were to be right today, why should I trade it? I wouldn't expect a move — would ??.

Ulrich usually hits the nail on the head because he never gives up his search. That is a characteristic that leads to great success.

Phantom appreciated all the input and didn't want to leave anyone out of the input process as he feels it is very useful. How often do you come face to face where the market is close to your entry price and you are questioning yourself? Phantom felt many of these ideas of the past are in preparation to be discussed on the futures forum.

I asked Phantom if he would want to expand on the input he received. His comment was that, yes, indeed he would. We shall come up with what will be known not as Rule 3 (his rule) but THE TWELFTHS RULE, or WHEEL of FORTUNE.

Thanks for your input and thoughts on improving a knowledge and behavior search beyond Phantom's Rules 1 and 2.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@netzero.net
Art Simpson

© 1997-2001 Art Simpson and Phantom of the Pit
All rights reserved. October 1997
Contact webmaster for permission to use.

Other learning opportunities

Chapter 16: Rule 3, You Say?

By Art Simpson

"It's all the traders, you and me, who will be satisfied with Rule 3 at its conclusion."
Dennis of the Pits

I've noticed a lot of arrows drawn on pieces of papers, a few triangles and other strange ditos. I thought they might be new flow charts for another one of Phantom's computer programs. It's not unusual to have scribbles that turn into verbiage on pieces of paper shortly after the markers are closed and are tossed out to the circular file.

These particular scribbles were different, more organized, and that made me more interested in them. Because they didn't make any sense to me, I decided to ask Phantom just what they were. He was a bit uneasy about them and didn't want to detail any of them.

I decided to try and figure this out myself. Here is what I saw. In his first set of scribbles, there were arrows and triangles. The triangles were numbered and labeled. The first arrow pointed to the top of the page, and the second pointed to the right of the first arrow. The last two arrows pointed from the other two arrows and pointed to the bottom of the page. The last arrow pointed to the left side of the paper. In other words, what we had here was your old ordinary 'to turn left, make three rights' dito.

The next set of arrows had two arrows. One pointed to the top of the page and the other to the left side of the page. The triangles were all in the top half and the bottom half.

To the left of both sets of arrows was a triangle, indicating one of two choices. It still looked like a flow chart for a program to me at this point.

I asked, there is it one or two arrows at the top of the page. In very small letters are the words "rule three." Great, I thought, Phantom is going to give us Rule 3 just like everyone had asked.

Traders on the Futures Talk forum had asked Phantom to give them Rule 3 to tell them when to add a position. Rule 1 tells them when to initiate a trade, Rule 2 tells them when to exit. Traders were begging for a rule that would tell them when to add a position and whether to keep the position established. They were also beginning to understand Rule 2 and how it works. Rule 3 would tell them when to add a long to current position and how to do it.

Could it be that Phantom has had a Rule 3 all the time? Did he just not want to share this rule? I wasn't sure about Rule 3 in his trading career as I thought I knew reasonably well how he traded. I was sure that Rule 3 was a long-term goal for him, and that Rule 1 and Rule 2 were questions ran through my mind.

Around the papers over, I saw it was a little disappointed in what I saw. Nothing other than a big question mark was on the other side. There was nothing written on the pages except the scribbles and "rule three" at the top of the page.

Art Simpson (KLS): Phantom, about Rule 3, what can you tell me so I can pass your insight on to traders as we have been asking for a rule to add a position?

Phantom of the Pits (POP): I am afraid I have let them down, Art! I don't have a Rule 3 such. What the traders are asking of me is more automatic for me than a rule. When to take profits is not an easy rule to write down.

You see, my rules have been set up to address the nature of trading as a losing game and to keep losses small. I have a long-term perspective and I have a rule for every decision I make when correct. To have a rule on taking profits is to have a rule that is second nature most of the time.

I can understand the point of view that profits should be more correctly also. Thought might be second nature to me, I am learning that important insight one expect is just as important to our traders.

Art wrote back, what is Rule 3. Did you expect said "no"? If the traders, we are who are not satisfied with Rule 3 at its conclusion, it is not clear yet at this time, but we shall do what we discussed.

If you take a breaker of dirt and water, what do you get when you stir it up?

Phantom of the Pits (POP): I am afraid I have let them down, Art! I don't have Rule 3 such. What the traders are asking of me is more automatic for me than a rule. When to take profits is not an easy rule to write down.

You see, my rules have been set up to address the nature of trading as a losing game and to keep losses small. I have a long-term perspective and I have a rule for every decision I make when correct. To have a rule on taking profits is to have a rule that is second nature most of the time.

I can understand the point of view that profits should be more correctly also. Thought might be second nature to me, I am learning that important insight one expect is just as important to our traders.

Art wrote back, what is Rule 3. Did you expect said "no"? If the traders, we are who are not satisfied with Rule 3 at its conclusion, it is not clear yet at this time, but we shall do what we discussed.

Art Simpson (KLS): Phantom, about Rule 3, what can you tell me so I can pass your insight on to traders as we have been asking for a rule to add a position?

Phantom of the Pits (POP): I am afraid I have let them down, Art! I don't have Rule 3 such. What the traders are asking of me is more automatic for me than a rule. When to take profits is not an easy rule to write down.

You see, my rules have been set up to address the nature of trading as a losing game and to keep losses small. I have a long-term perspective and I have a rule for every decision I make when correct. To have a rule on taking profits is to have a rule that is second nature most of the time.

I can understand the point of view that profits should be more correctly also. Thought might be second nature to me, I am learning that important insight one expect is just as important to our traders.

Art wrote back, what is Rule 3. Did you expect said "no"? If the traders, we are who are not satisfied with Rule 3 at its conclusion, it is not clear yet at this time, but we shall do what we discussed.

Art Simpson (KLS): Phantom, about Rule 3, what can you tell me so I can pass your insight on to traders as we have been asking for a rule to add a position?

Phantom of the Pits (POP): I am afraid I have let them down, Art! I don't have Rule 3 such. What the traders are asking of me is more automatic for me than a rule. When to take profits is not an easy rule to write down.

You see, my rules have been set up to address the nature of trading as a losing game and to keep losses small. I have a long-term perspective and I have a rule for every decision I make when correct. To have a rule on taking profits is to have a rule that is second nature most of the time.

I can understand the point of view that profits should be more correctly also. Thought might be second nature to me, I am learning that important insight one expect is just as important to our traders.

Art wrote back, what is Rule 3. Did you expect said "no"? If the traders, we are who are not satisfied with Rule 3 at its conclusion, it is not clear yet at this time, but we shall do what we discussed.

Hmmm, I guess I'm not very quick on the uptake. I thought Phantom was being very polite and was trying to tell us that he wasn't ready to give us Rule 3 yet. I guess I was wrong.

Phantom's Gift

By Art Simpson

Chapter 17: The Third Rule

"Find the positive in taking small losses rather than getting wiped out. Find the positive in the simple rules we have given you to use. Decide what you want to do with the guidance you have been given!" **Phantom of the Pits**

Art Simpson (ALS): Phantom, you have indicated you used Rule 1 and Rule 2 in your trading career to allow you to change your thinking and your behavior. Why do you now state a third rule?

Phantom of the Pits (POP): The third rule has not been a written rule for me but has been a second-nature type of rule over the years. You know I strongly disagree that the market is always correct. From experience I have concluded that to be the case. I use this assumption on my part to protect profits and eliminate new positions in illiquid markets.

I'd like to point out that the third rule is not my rule, and the credit goes to the traders who have convinced me there certainly is a third rule to be used after Rules 1 and 2. I was very reluctant at first, but I see they are correct in this request. Let us look at everyone's rule here and not my rule.

Almost every trader who read my Rule 1 and 2 felt there is a third rule. They really are sharp and more observant than I am. Even though I have used a third rule more as a rule of thumb, it is indeed a third rule. Our traders thought it should be a rule on when to take profits. It extends beyond that point because our true focal point is to keep loss possibilities as small as possible and retain as much profit as we can. That implies taking profits at the correct time and properly outside of Rules 1 and 2.

Although Rule 1 does address taking the quick loss when the position has not been proven to be correct, we do need Rule 3 to tell us something about our trading plan that is very valuable in trading. That rule tells us when we must question the liquidity in the market and the place that indicator has in our trading plan. I feel it is better to have that in a rule outside of the original trading plan to give us our criteria in illiquid market times for not losing much money.

I also feel the time to take profits is clear within market conditions when we have our extreme volume days. This is usually a turnaround indicator in most cases. But let us get out on those indicators. Why? Because we can re-enter any market as soon as we get another signal from our trading plan. Even if we were to miss part of the move at the expense of being early, we still will be better off in the long run. It is the long run we plan to trade in our careers.

ALS: Do we need to qualify the third rule?

POP: No, we do not. We will state it now!

The Third Rule

We shall go against the majority and assume the market is not always correct (those times being when liquidity is poor). At those times we shall question all signals and wait for future signals for positioning.

We shall use the converse of poor liquidity and remove our existing positions when extreme liquidity takes place in two steps and within three days of extreme high volume. Half of our postion shall be removed immediately the following day after an extreme high-volume day. The other half of our existing position shall be removed within two additional days. We shall wait for further signals in those cases for future positioning.

The first part of the third rule addresses the situation of thin or illiquid markets. It states that we shall question our trade program signals and wait for further clarification of signals in those thin markets. At illiquid times the market is not a valid indicator for taking positions. Because most signals are generated by price, you can see the importance of the third rule allowing you to have an exception of questioning your signals. Some trade programs address this situation very well. Not many programs use volume and open interest such as moving average indicators in generating signals.

I am not questioning various systems but only saying that with the third rule we must put an illiquid relief valve somewhere in the plan to preserve equity at those times.

The second part of the third rule gives us criteria for taking profits or removing any previously established position. We do know when to take profits. Although we take all the profits and may miss some of the move, we shall await further signals at extreme high-volume days. Additional signals develop quickly after high-volume days, and we want the benefit of that by not being positioned incorrectly prior to additional signals.

Don't forget that a good plan will continue to give you signals based on market conditions. We are using extreme liquidity to our advantage by knowing that huge volume is the prelude of further correction possibility. Many times huge volume days are the very reversal days in bull markets. At any one time there could be an event that causes extreme volume. It usually takes several days to play out when this happens. We also use that to our advantage in the third rule.

When we say we shall take the last half of our position off within two additional days, it is important to note there will be times when we will do it very quickly and not extend to two additional days. The two additional days gives us the outside limit allowed for our rule.

The third rule is a good rule, and it stresses the acknowledgment of trading in the long run and not the short run.

ALS: Many experts are going to argue with your Rule 3, as it will surely interfere with their professional trade programs. Most systems say to trust them over a valid time to allow them to work properly in the long term.

POP: My trading experience has told me to have enough integrity to bail out when I see that everyone starts putting on their parachutes. Why stick around to see who leaves their seat belts on? Trading is a run-run game. There are times you have to run before they run. That way there is less chance the market will out-run you.

Do you think the experts ever buy insurance for their homes, cars and health? Surely the experts have a plan to protect positions at critical times. The third rule just places another double-check in a good trading plan.

Traders must never be complacent when the market is at extreme volume, whether high or low. These times are to be flagged, and I don't know a better way to flag them than to remove existing positions. How much can you lose after removing a position after a market volume extreme? Why not make your plan give you another signal before you re-enter the market?

ALS: Do most traders have the same kind of thinking on this liquidity situation?

POP: We are either at the first floor (bottom) or approaching the 18th floor (top) of the elevator. Few traders watch the floor indicator. They wait to get off. I say just don't wait long! Liquidity is giving us our floor information so we know where to get off the elevator.

I've seen what waiting can do to people. It was back when the Hunt Brothers had too many bean positions in place. They were told they would have to get out. I had just put a position on and within seconds the market was practically all sellers. I lost money that day within 10 seconds and I got out. The volume was extreme, and the market went limit down very quickly. Sure, this was a short time frame and few knew to get out until it was too late, but many situations do flag you that you are looking at a special price level.

We have all heard "when in doubt, get out!" I think a poet made that statement, and it took hold. It makes sense to this day and always will. You don't ever lose when you are out. There are times to be out.

ALS: It looks like the third rule is more of a rule to keep from losing money and to keep from losing profits previously made in the market. How often do you foresee a situation in which market conditions present these criteria of either high or low liquidity? Or should I call it volume?

POP: Yes, you could associate liquidity with volume in most cases. We are talking normal and abnormal market conditions of liquidity, and we measure liquidity by using average daily volume as our reference. But don't forget, we are only talking about extreme conditions of liquidity that are abnormal.

Traders will see the validity of watching for extreme volume days. Their use of the third rule will become second nature. They will see the thin markets better and know what not to do in those situations. The third rule is a good rule!

We would normally expect the conditions to be a possibility at trend-reversal times and at certain events that cause lack of interest in trading a particular market. At times in front of critical reports you could see the situation develop.

ALS: In front of reports what do you usually do with your positions?

POP: From experience I have learned that, if you make a mistake, you pay heavily with being wrong after the report. You have to have a big lead and then it takes it back sometimes. I must consider always cutting back in front of a report unless I am given a big edge. There are times you cannot control your position the next day so why not cut back? Most traders should remove their positions to allow longer views of their trading careers.

I just recently had a new trader ask me about a sugar position, and my guidance was to look at what the market had done the prior four days -- we had three higher lows in a row. The opinion was that sugar would go down. That day it made a contract high. Rule 1 and Rule 2, with the help of the third rule, allows all traders a long-term outlook in trading.

First, behavior modification must be adapted to the rules to have any expectation of trading long term in a trader's career. Many shall have to face the aspect of human nature to oppose any change. Change is required, and you are the only one who can do it. Your trading career depends on it. Don't take it lightly.

If you must, rehearse your behavior daily until you have it down correctly. Behavior modification requires positive reinforcement, and trading often is not positive. Find the positive in taking small losses rather than getting wiped out. Find the positive in the simple rules we have given you to use. Decide what you want to do with the guidance you have been given!

Unless you go down the defeat road, you will never have to endure the hardship of knowing you didn't make a good attempt to change your behavior in trading.

I would like to leave you with one last thought: Trading is not as we had all thought. The sooner you learn that what you imagined about trading is far from reality and that you must change your thoughts on that reality, the better trader you shall become.

Good trading to all of you! I shall watch you trade and shall always be your shadow.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Chapter 18: Tie Ribbons on Your Trading

Just when you know you have everything covered to start your trading career or to continue the one you already have started, you find you have a few more questions you would like to have answered. We will get Phantom's view on a few of those important questions yet unanswered. Questions like a few of the following are perhaps in your minds:

- When you spill a soft drink on your mouse pad, why does it always soak in, but good trading methods take forever to soak into our brains?
- What kind of system should I use to trade?
- Should I buy a good system or come up with one of my own?
- How do I trade to not chase the market all the time?
- Why do I always end up with the bad positions but seldom get the good positions and the big moves?

Other than your questions, we should ask Phantom some of the questions he first had and has now in trading. Answers are usually from different views. It helps to get other views for our questions. A good decision is one that can be made from having good choices.

Isn't trading a lot like picking out a Christmas tree? Do we just take the first one we see? Or does that apply only to the first house we buy? How about when we buy a different car: What approach or plan do we have? Do we buy the same car everyone else wants to buy? Or do we make the trade that no one wants?

There isn't really an end to questions we have in our trading careers. We'll try to touch upon some of the most important ones without writing a book about each one. These are Phantom's views and are not in keeping with everyone else's ideas at times.

Art Simpson (ALS): Phantom, since this was your idea after reading the Sunday paper, what questions do you think are important points that should be answered in trading?

Phantom of the Pits (POP): A point I would like to make is that sometimes the most brilliant minds cannot trade correctly. They don't always have all the answers. When they don't have the answers, we are disappointed. Many times the correct answers for someone else does not mean they are the correct answers for us.

It shows that, to be taught by someone else or by being self-taught, there is an important aspect of gathering the correct information. And then the remaining part of learning is the behavior modification after learning correct information. This conclusion has been stated previously.

The point I want to make is that, when we don't know the correct answer, so what? Admit it and use the channel required to find the answer. We can't know all the answers, and we can't be expert at all things. The smartest person doesn't know all the answers.

ALS: I've known some people who know it all!

POP: They don't trade long, do they? Having all the answers is still an incomplete process in trading. Often in trading we know the logical answer but don't know the intuition answer. There are situations in trading when we don't want to take the logical answer but the intuition answer. To know which answer to take is the most difficult decision for most traders.

I believe at least 90% of the traders lose money and that close to 80% of traders are logical in their trading and not intuitive. What do you now see about trading? Wouldn't you now look more at the intuition side of trading and do more research on intuition?

Do you remember that many times I say "second nature?" What I mean is intuition when I say that. Intuition can come from known logical reasoning but with the emotional part removed. It is a feeling we have. Sometimes we can't explain the feeling with reasoning or a logical plan.

Does this make trading seem more scary or open more thought in you mind? Many traders don't want to miss a move so they buy regardless of the intuition they may have. Other traders see a market move and refuse to jump on because intuition says they are buying a top. Who is right?

Is the intuitive trader a better trader than the logical one? How do you know? How would you prove it?

Those are questions I had when I began to trade. I found the correct answer for me, but it may not be the answer for others.

I guess you will want my point of view on the logical or intuitive trader answer. I don't expect all of you to agree with what I have found to be my case. There is one word I have dropped on you at times in these writings, and that word is a very important one in the answer to the logical or intuitive trader question.

I'll give you the word and let you use it to give some thought to the question. We'll answer that question as I see it along the way in this part. The word E X E C U T I O N is our key to the answer.

I saw an advertisement pointing out you would never have to worry about buying tops and selling bottoms again. There are times when you can make an exception about any statement, and you need a filter system in your trading program to help clue you in on these times.

There are, of course, times when you should buy tops and sell bottoms. I do it all the time when I expect a market to reverse. Why? Because I use a method I call the best of a bad position theory -- my theory being a learned one that my best trades are usually after correcting a bad position and getting correct in a market. This happens to me more at tops and bottoms than any other place.

Some of the biggest moves take off from a reversal, and if you miss the entry, it causes you to be hesitant to position as the move gets stronger because you missed the entry. A worse case is when you had a plan and didn't get filled. Why does it happen you got filled when it went against you but a good position never got hit? There are good reasons for that to happen.

I've always said to pick a range and not a price. The exact price cannot be done with consistency. A range is easier to pick and position when you have your signals. Most people think the position of getting out is the most important. You know what? It is important but the most important position is actually the entry. How many times have you put an order in at a price and got the price but not the fill? Many more than you think! It happens to most traders.

By knowing that most traders have put orders in the market and never gotten filled, what does that tell you? Inexperienced or uninformed traders are great market supporters and market resistance builders. Now, just why should I say that? The locals lean on the orders, as it is only natural. It works like this: You want to buy 10 December corn at 268 because that is where the support is. Sure enough, that is support. Tomorrow on the way to 275 you ask yourself why is it you only get filled if it continues to go down.

Do you have any clues? E X E C U T I O N! You must guarantee that you are filled with every signal you get. Any signal you get and you don't get your position is going to be your money position. The market never waits for you. If you trade millions of bushels a day, then you should worry about the extra quatrer-cent.

Even so, execution is still the most important step in your positioning. Your plan is the most important part of your trade, but execution is what validates your plan by giving you a position.

When you learn to use Rule 1 properly, you will never worry about or hesitate to take your signal and position with the utmost execution. You will see you must take all signals and make sure the market lets you in. How do you think the best way to enter a position is? The answer is based on how close you are to the market, how accurate and timely your quotes are and how quick your orders to the floor are.

You must guarantee you get all your positions on at all times! I can't stress that enough! The unfortunate thing about that statement is that it is completely true. The unfortunate part of positioning is that most trade programs or systems use price action, and positions are usually taken on strength or weakness. This causes buying tops and selling bottoms at the thinnest part of the trading day at times.

How are you going to make sure you have all your signaled positions in place? I could give you a way or you could come up with a plan of your own. Which would be the best plan? It has to be your plan. It is only my job to tell you what you must do!

You must position according to the market characteristics. Sometimes you will have to buy the high and sell the low. How do you know when to buy the high and sell the low? You must have two plans in place at all times. I would guess most traders have one plan, and when they miss their position, that is it for the day. You must be smarter than those who only support the market with their orders and never get filled. They can never make any money but you can. You see the market order support the orders waiting to get filled but never will be filled until they are wrong. Same thing on the topside! Why would you want to position this way, too?

One of your entry plans will always be a market order. The other order will be an intelligent order based on the nature of market you are trading. We know that each day there is a high and low and a range throughout the day. You seldom buy the low and sell the high so don't even consider it. Your second plan for entering positions will be based on the fact that better liquidity tends to migrate toward the middle of a day's range.

You don't want to chase the market if you can prevent yourself from doing so. This is the reason for your two plans. Your market order plan is your plan to execute upon failure of your first plan -- same as "get me a soda" but if no soda (sometimes they are out), then "get me a glass of water" (lots of water around). This is all pretty elementary to most traders.

What is not elementary is always having two entry plans. Some of your systems will ask you to enter a position on a stop. Okay, it is a market order. Throw out your other plan if the system is that accurate to expect you to enter on a stop. Other systems may ask you to enter on the close. Okay, execution is important and you have no choice but one plan at that point.

I usually know within the last hour of the market what I am going to do. This allows me more time than to just enter on the close. The reason most entries are poor is because the systems are based on how you get your market prices and information. It can't be a system that gets data that you don't have the possibility of obtaining. That is your big disadvantage.

As an example, if there are 1,000 day-traders in a market, you can almost be certain they have positioned by the last hour of the day. If the market is up, what do you think their position is most likely to be? Same if the market is down. What is their most probable position to be? Long or short?

Okay, you get my thoughts here. The point is that, when they offset, there will be some kind of wave action. You want to use wave action to your advantage when positioning.

You don't want to chase the market, but you don't want to miss it either. So your two plans cover all the bases with your input of market characteristics. If each day the market tends to give you a range of, say, 15 points, then you surely must be cautious when the market is already up 15 ticks. But only be cautious for a short period of time. Don't miss the move and use your "at the market" plan after a period of time. Sort of like a stop and I must say the best use of stops I know.

How does it work? Today at one hour into the trading session you get a buy signal. Your two entry plans are now valid to be used. The first one says to buy at the market, but you want to use that one last. Okay, so you hold that one because what you are doing is holding your own stop order to buy. The second plan is to buy as intelligently as your input allows for the particular market you are trading.

You know the signal to buy is going to be based on strength and stops are hit going up when it kicks in. More times than not, you will get several waves of buying, and this can be to your advantage. Sometimes you do just plateau but that is okay, too. Use your second plan for entry and price based on your criteria, but do one thing more! Add "MIT" (market if touched) to that order and add two ticks! It will be the best money you ever threw away. You must guarantee you are in your position but with intelligence. That is exactly what you are going to do.

After a short period of time, if your position is still not filled, you will use your first plan to go at the market to get filled. So be it! You still acknowledge that you guarantee you are filled and in the market at all signals.

Keep in mind if you don't get positioned, you are acting like you only want positions when you are guaranteed wrong immediately. This is one time the market can give you an emotional letdown if you didn't get positioned. It will always be the time the market takes off without you. Stop! Stop yourself into your entry signal at last resort but absolutely do it if necessary.

Take a survey! How many of you have missed your entry? Don't let it happen again!

Now we have your position established after you have a signal. Good and well so far, but what happens now that the position just isn't acting correctly? You have the old "oughta get out" signal. So what is so important about the bad position, now that it isn't correct?

What is important about a bad position -- one I consider not proven correct -- is that it gives you the greatest opportunity to get a correct position. This happens often at tops and bottoms. It must come from a trade program you develop that allows you to reverse your position at certain times but not all times.

Most of the time a good position, other than the bad position, is being out of that position. Other times the best position is to reverse the prior position. Your trade program should address this.

How do you know when to reverse? We watch effective ranges in bull markets. We expect a bull market to continue to build range during most up days as long as bull markets are strong. When markets are getting into topping action, you often see what is known as a large effective range.

Effective range is nothing more than a broker's dream. The market will go to a level, reverse, go to a level, reverse and so on until you have a very large number of price swings within a small range. Buying gets met with selling and selling gets met with buying which swings the market back and forth many times in compact ranges.

In bear markets your effective range may just go dead and not swing at all for lack of interest. A normal bear market will eventually have bottom-pickers cause upswings even though you are in a bear market. When all interest is lost in trading, you can look for a possible reverse of a bear market.

I find the positions that I reverse are usually the ones I have the intuition of not wanting to place in the first place. It works so well for me because I know my answer to what I disagree with in my positioning. This allows me to take all signals, even when I disagree with them, because I know that my true thoughts will allow me reverse if the first position isn't proven correct.

I saw some posts (on the Futures Talk forum) that the most difficult positions to place are usually correct. That is true in most traders' situations. That is why you must take all your signals and be prepared when you disagree with the signal to have a strong counter-plan due to your intuition. Intuition is your friend as it is your caution flag but not to the extent it takes you out of your plan.

Logical plans are usually what a system is developed around. Intuition is often left out. To me, the intuition side of trading is the surprise side of trading. You must always have your intuition plan along with your expected logical system.

You are starting to get my answer on the logical and intuition trade question. I did not prefer one to the other. They both have their place. What the true answer is to me is in the trading system or program I develop for my trading. Perhaps this is an answer for you also. I must have both covered in my trading plan. There are times the intuition plan comes out ahead, and these are usually at tops and bottoms. Be swift! The intuition part of my program is swift. It prevents large drawdown.

It's not exact but you see you must let intuition be your surprise side plan. How many times have you said, "I just knew it?" That is right! You did know it. Learn to use that intuition and when to use it. I cannot tell you because I am not you. I can only tell you how important it is. I know you have all felt it was important and have learned that it is important.

You know now how to put the good positions on and not just get stuck with the bad positions. EXECUTION when you get your signals is a must!

ALS: I thought you would go into more detail on how to enter with the two plans than you have. Would it help if you did?

POP: The point of execution has been made, and I think reflection of a person's trading is more important at this time. The positions must be entered to have a fairly good chance of having the good positions on as well as the positions that are never correct.

ALS: What kind of trading system should a trader start with for the early part of their careers?

POP: First, it must be one they totally understand. They cannot take a system they are not familiar with and expect to trade it correctly. There will be too many conflicts if the signals and how they are obtained is not fully understood. This can be a problem at times for some systems, which may not properly disclose the criteria on entry and exits of the trades.

The trader should error toward simplicity at all times unless they have a better understanding of a more complex system. With my rules, the system is going to be easier to judge, and simple systems can be just as effective as long as execution is never in doubt. The system they choose will be a tradeoff most of the time. I always want the system with the least drawdown and the maximum gain in the shortest period of time.

ALS: You don't want much, do you?

POP: I don't mean to be cavalier about it, but it's easier with my rules to look toward that goal. You will have to make sure you can use the rules successfully with the particular system you choose.

The other terms of a good system are the liquidity filters but with Rule 3, thanks to our traders, it won't be as critical as without the rule. To confirm the move, of course, the system should have some kind of volatility figured in and open interest.

On suggestions as to whether to purchase a commercial system or design your own, I would say your first purchase of importance is price data whether it is included in your system or outside of it. You need price data and chart data. Without those two elements, you have a very large handicap to overcome.

ALS: I've seen systems where they say "just 10 minutes each day." What about systems where you only need a short amount of time each day?

POP: I don't rule them out! I am saying you need the data to verify the validity of any system. Without it, you cannot be a good judge of any system.

ALS: What about long-term trade suggestions by various individuals or vendors?

POP: I don't know if you can remember my remark about not being able to carry a reputation. My reason for that feeling is that I know what has happened in the past is no guarantee of the future. I also know I change my mind more often than the experts. It is extremely difficult for expert traders to convey with confidence to their customers that they know what they are doing if they change their minds often. I like the luxury of changing my mind. They don't have that luxury.

I remember one day when I got at least six reversal signals in one day. How do you think a trader you are trying to help would understand your changing direction every time they saw you in a day?

That is another reason I say it is not an impossible road but a lonely one. It is out of necessity. You must have the courage to do what is correct at all times. A good advisor is perhaps good at advice. There is conflict between giving advice and also trading. I do not accept conflict. Some can but not me. Most new traders are better off without the conflict of advice.

I could tell you what I am doing every trade, and you would not trade the same way. You could never be at my point in time when I execute my trades. We must always have the latitude of changing our positions based on our systems. My rules allow this thought for doing the correct trading.

Good advisors are often trading funds instead of giving individual advice. Advisors have a harder job than I do. Think about how you explain to more than 80% of traders that they have lost and been wrong in their trading.

I am not saying anything against advisors, for I know the cards are stacked against them. You take the best advisor, and there will always be those who are upset with them for one reason or another. It's the adult-child thing in trading. I admire those who stick to the field and move beyond the difficulties of being leaders in their field.

The same also holds true of systems vendors. They are only as good as their data used for back-testing, and often it is past data being used for future prices. Any one event can change the entire picture. I guess that is why stops are so important in most systems.

I think to not overtrade is more important than a good stop system, but most traders don't have the discipline to trade small enough that stops won't much matter. Everyone is in this game to get rich. Why, it's the farthest thing from my mind. Can you imagine trying to get rich by trading? There is only one way to trade and get rich.

ALS: What way is that?

POP: Trade your program signal, protect it with Rule 1, add with Rule 2 when the program says to add and take profits or offset with Rule 1 or Rule 3 when required. And then do it all over again and again and again until you have the confidence you need. At that point you can think about getting bigger but not until you have complete confidence in your trading.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

Trading and Three Accidents

The phone rang in the middle of the night. Not knowing if it was important, I got up to answer it just as everyone else would. The voice at the other end was a familiar one.

"I believe John Denver's biography is going to be the most important biography of this year. If not the most important, surely one of the important. Art, I was just doing some thinking on John Denver's accident. He touched millions of lives as well as yours and mine. I can relate to that accident," Phantom told me.

"You called me in the middle of the night to tell me this?" I asked.

Phantom explained, "I know how our traders can relate to John's accident, too. Of course, there are those people he never touched or who didn't even know who he was. This is so important to me. Maybe it is more important to me than anyone. It is important because I always have had timing as my friend in my trading career.

"Traders will have to face in their trading career what John had to face in his last flight," Phantom continued. "I just don't want our traders to ever have to face that last flight in trading. I have to make them understand one very important point in their trading. Somewhere along their path they will face an unexpected event that can take them out of trading if they don't prepare for that eventuality in their trading."

Phantom continued to convince me, but I already knew Phantom was expert at timing. When you get a phone call at 2 a.m. in the morning, you can almost know it must be from a friend. Why else would someone call at that hour and awaken you from deep sleep? As I answered the phone, I could see this call from Phantom was not just to me but also to Phantom's trader friends.

"Art, I must ask you to address three aircraft accidents! It's John's, the latest one in the article your brother sent you (about a December 1997 accident) and the one I was in. I never could make anything out of the aircraft accident, but it has to do with life and in trading, too. It is important that we warn our traders of needing to be prepared for all possibilities.

"I have searched for some kind of answer from John's accident and my accident in the past. Not until I read about the last accident -- the doctor whose aircraft landed itself after carbon monoxide poisoning in the cockpit -- did I realized the similarities to trading and how it is important," Phantom continued. "It does have to do with trading, Art! When you wrote about God's rules, you never really understood fully why it was such a difficult time for me. I went through the same process in my aircraft accident as with John's. We survived and we had altitude to recover and to make a decision. John didn't have that altitude and couldn't make a decision. He had to take what was given. The doctor wasn't even in the decision process because of his condition.

"Three accidents, and they all had different results. The doctor had no choice, and when he lost consciousness because of the carbon monoxide in his aircraft, he still survived because he ran out of gas. John had what appears to be fuel and a fuel valve problem and he lost his life. Our engine failed, and we had time to work the fuel tank valve and get the aircraft on the ground where we wanted because we had altitude. We were able to make a choice of where to land. John didn't have a choice. The doctor's aircraft landed by itself and he survived. These three accidents are all the same accident with different circumstances.

"Can't you see what I am getting at, Art?" Phantom exclaimed. "Trading has the same conditions"

I remembered seeing Phantom's post on the *Futures* talk forum to Randy about the fuel valve over a month ago and had thought little about it until now. I began to see Phantom's thought on the three aircraft accidents. There are times when the market hasn't given you enough altitude to be able to recover. At other times you have enough altitude on your position to make a good landing choice when the market goes wrong. And there are times when you have no control over where you are going to land or how because it is out of your hands. Yes, it makes sense that Phantom would call at 2 in the morning.

Phantom never pulled rank on anyone and never considered himself better than anyone. He has always been a gentleman and perfect example of what you would expect of a hero. Why should I hesitate to let him impress his thoughts on his friends? He wishes to save as much grief of trading to his trader friends as he can. I cannot question the unconventional thinking about the accidents and trading as my thinking is pretty unconventional at times, too.

We shall convey the insight for you on the three aircraft accidents and allow you to question if you feel it appropriate.

Phantom rarely ever said anything about an aircraft accident in his life, but it always bothered him. In John's accident he was presented with an aircraft accident not easily accepted. Now, out of the blue sky, an accident where there is no logical reason the pilot, a doctor, could have survived but did. Phantom surely has gathered reasoning for all of this. He has been right in his useful insight on events over his trading career. Why not now, too?

Events in life have a lot to do with trading. Could it also be that trading has a lot to do with survival in life?

"Okay, Phantom," I said. " We can start the chapter while it is most importantly on your mind at this early hour. Where would you want to start?"

Phantom indicated he would just tape his thoughts and let me make out of them what seemed to be the message as we had on his insight in this project. I agreed and went back to bed.

You can know that Phantom didn't sleep that night and kept the midnight oil burning. I guess there is a time and place for all thought. We must let it flow and not restrict thought at those times. That point is another Phantom has taught me.

Phantom felt the three airplane accidents reflected clearly similar uncontrollable events in trading just as in the accidents. We'll see just how they compare.

The three accidents Phantom was talking about were John Denver's, the doctor/pilot's and Phantom's accident. The doctor's aircraft landed in Missouri on its own when it ran out of fuel while the doctor was unconscious. The aircraft accident Phantom was involved in was at greater than 5,000 feet altitude when the aircraft engine quit.

In John Denver's accident, two pieces of information about the accident disturbed Phantom. Before the flight took place, John had borrowed a pair of vise grip pliers to turn the fuel selector valve. The fuel selector valve was not in the correct place below his right hand on the floor of the aircraft but over and above the left shoulder behind him. This required him to take his right hand from the flight stick to turn the valve, which was difficult to maneuver.

The most disturbing aspect of John's accident was that his problems occurred at less than 500 feet of altitude. Thought time in the emergency situation didn't exist, as actions had to be second nature. Because John had few hours in the aircraft, second-nature reaction with such little time wouldn't have allowed recovery in time.

The doctor's accident happened when he was overcome by carbon monoxide, which entered the aircraft because of a faulty exhaust system. The aircraft was on autopilot when the doctor lost consciousness from the carbon monoxide. He was flying to Topeka, Kan., from the west and, instead of a 150-mile trip, made more than a 300-mile trip to the Moberly, Mo., area as the plane ran out of gas. Surprisingly, it landed with the autopilot engaged and the pilot unconscious.

The doctor walked away with only a broken arm. Had the fuel onboard been enough to fly another half-hour, the carbon monoxide level in his blood would have been 50 parts per million rather than the 35 ppm he had. He would never have lived. Had the terrain been different, the aircraft could have crashed instead of landing on its own.

The third aircraft incident occurred to Phantom, and he never wanted to talk of it before. At about 5,500 feet altitude, the aircraft engine stopped. Phantom's explanation of the accident was that it required an immediate decision, and that was where to land. The altitude gave comfort in allowing a good amount of time for a good decision on where to land.

In two of the three accidents everyone survived. Two aircraft made landings without loss of life. While the two aircraft had control in landing, one pilot wasn't conscious but still survived. In the other airplane accident, in the safest aircraft, John lost his life. The loss of life was in the aircraft that had the lowest altitude and least amount of time for reaction and corrective action.

All three accidents were unexpected, and all had different outcomes because of circumstances beyond control of what the pilot could do. It was these situations and different outcomes that Phantom wanted to discuss as it relates to trading.

Phantom never had any value of learning from the accident he was in as he always wondered what reason or purpose it pointed him to in his life. He always felt other people's thinking of a person who is in an accident is that somehow they are to blame. As I see the way John was treated in the news media when he lost his life, I understand Phantom's view. Others do often look for blame rather than answers.

Phantom has always looked for an answer in his airplane accident. He has found some answers to uncontrollable events in life and in trading. To relate the three aircraft accidents to uncontrollable events in trading, Phantom gave me his explanation.

In our lives and in our trading lives, we come upon a situation sooner or later where we have little or no control. We must at all times plan for that time. When a pilot learns to fly, they are always practicing emergency landings. In trading we must practice those same landings.

Depending on the exact situation, we shall at times end up with entirely different results, even though the situation may repeat itself again and again. We, of course, want the best result, but there are times we don't control the result.

In your first situation as you take a trade, there is a time when it is just as if you took off from an airport and don't have a comfortable altitude. This is the time when the trade has not really been proved to be a correct position yet. At this time an unexpected event can have its worst result in your trading. You have to take what you can get for a landing spot due to the lack of altitude.

The second situation is when a trade becomes a proven correct position. It is similar to being at a higher altitude in an aircraft. If an unexpected event takes place, you have a more comfortable choice and can make a better decision due to the extra lead, which is also similar to picking out a better landing spot. In this situation you are in control of keeping the trade from being a total disaster. You land in a clearing.

The third situation for a trader that parallels these three aircraft accidents is that you are on your way with comfortable altitude and are on autopilot. There are no problems with your position. All of a sudden your trade is taken out of your control. Several events can cause this . . . your phone line goes dead . . . you get delayed on your transportation and can't get communications to your broker . . . your quote machine goes dead . . . a big report comes out and the market locks limit before you can even get an order into the pits.

All of these are the same as losing consciousness due to carbon monoxide in the cockpit as you fly to your destination. Nothing you can do will change the result as the result is going to deal you what it will.

The trades with the best altitude or lead allow you the best opportunity to recover from a bad or unexpected event. A lot of traders expect their trades to show this lead and do nothing when they don't show the lead they need. They allow the market to take them out and prove that they are wrong. To be taken out by the market when proven wrong opens up much more disaster than many traders ever imagine.

At all times you must understand that the surprise and unexpected event will create a worse situation than you are prepared to face. You must practice your emergency landings. You can recover from good positions. You will not recover from bad positions in unexpected situations.

Just as the doctor's airplane landed itself, you will have times when you luck out. After all, a broken arm is much better than a lost life. Traders are in the only profession I know where they are happy when the market gives them back half of their loss. When you get back half of your loss, you have just seen your airplane land itself on autopilot as it ran out of gas.

Phantom indicated the most critical time of a trade is immediately after you have just entered the position. This is the time you must be most sensitive to news and events. How many traders are most comfortable upon entry because they know they are protected by stops? How many surprises are there in trading? How about the time the unemployment report was a surprise and your stop gave you the biggest slippage you ever thought was possible? Listen to Phantom! It happens. Don't let an unproven position set you up for a downfall.

Phantom asked why is it so difficult for traders to understand that bad trades get worse? They get worse until the unexpected takes place. The unexpected is always your downfall in a bad position getting worse. Get a lead on your trades or throw them out.

Phantom wanted you to understand part of his distress in John's accident and death. He wants the best for you. Can you relate to the three accidents and your trading? Make out of it what you can. Phantom intended it as a way to ask his trader friends to be prepared for any possible event in your trading career.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

By Art Simpson

My Order Was Filled . . . Where?

"This shall be the ending post of "Phantom's Gift" but not the end of Phantom's attempt to give to you!"
Art Simpson

Phantom has always been anxious to address what the traders questioned in trading. It was with great hesitation that the subjects of order placement and fill prices were finally addressed. He felt more research on his part was necessary. There are so many different situations for traders when they put in orders for their trading.

Some of the questions appeared over the months on the *Futures* Talk forum. Many traders would get what they felt were bad fills for one reason or another. Phantom knew it was mostly misunderstanding of how a market works in volatile situations. This lack of understanding due to little known knowledge on the subject disturbed him in these situations.

It seems there is a vast opinion by most traders that the brokers are to blame on most of their bad fills. This misunderstanding is a great handicap to traders unless they are aware of what causes bad fills in volatile markets. We shall present some of those situations with the explanation in order to improve order placement by traders.

Little research is done individually by most traders, and Phantom felt this is a big mistake. Phantom has always done his own trace of order placement, execution and reporting of orders to and from brokers in order to know the integrity of his placement. It gives him the ability to know what the edge can or cannot be upon an order placement.

Logging and tracing placed orders early in a trader's career affords the opportunity of knowing just how exact an order must be placed. An order placement for market orders, price orders and stop orders will have different urgency and slippage at various times due to current volatility at execution. Understanding changes in volatility is critical in knowing when and how to place each type of order.

I asked Phantom to give some insight on order placement before we got into particular experiences and results of traders. His insight is based on experience and knowledge of his many orders in his career. Phantom is the only trader I know to have been stopped out limit up and limit down in the same day. It was early in his career, and he takes full blame for not knowing early in his career the situations that can cause such slippage and fills.

Some of the important points on order placement and price fills are seldom talked about or considered. Phantom felt many misconceptions were important to address as well.

Art Simpson (ALS): Can you tell us some of the most important insight you have observed in your trading career on order placement and market prices?

Phantom of the Pits (POP): Let's just start with a normal day and look at an opening, daily range and closing. Regardless of what your order is to be, you will find that there are times during a day that liquidity will be better than at other times. That is really the reason for different ranges each day.

I remember in the early 1970s watching a trader bid the high of the day consistently at each new high. I asked that trader why he would buy the high of the day. His answer was that there would be many highs during a day but at the end of a day only one true high of the day.

If you think about that answer, you'll realize it is true. Each time you buy a high, it is possible that, sooner or later, there will be another new high for the day. To use his method of buying new highs, you would have to be a floor trader to use my rules but it has merits. A reason I say it has merit is because the thin part of markets is at highs and lows. You'll see this if you look back on volume at the end of the day. When the markets are thin, they can be pushed further until liquidity once again enters the markets. Even though markets are thin at the high and low of a day, during the day there will be many new highs or lows that are not the high or low showing at the end of the day. We can never know for sure which high or low during the day is the true high or low for that day.

I got a kick out of some posts on a forum as one was headlined something to the effect that the locals were gunning for the stops. There are some misconceptions in that thought. Locals don't gun for stops; it is just how they trade. If you knew the market was thin at highs and lows and were positioned the wrong way, what would you do if you were a floor trader? It is the traders who are wrong who push the stops before the stops are hit. In other words, you don't want to have to buy many ticks higher if you are wrong and approaching the high of the day. That is what the public tends to do by putting their stops above the high for the day.

I certainly don't think the forum participants were wrong in their thinking but only having fun with the way the markets tend to act on their positions at times. They have really hit the nail on the head, and it just takes some understanding as to why it seems to be that the locals are gunning for the stops. Locals are good at taking the smallest loss possible and going with the flow. It is an advantage over the public traders.

To understand why markets act as a system that tends to prove the most people wrong in any one day is a good start in correcting bad entries when trading. Traders are correct in thinking that the stops will get them out, and then the market will just turn around and go the way they had thought prior to being stopped out. The fact that it happens is reason enough to devise your trading plan accordingly. This idea is especially useful upon planning entries.

I never really liked stops but trading off-floor creates a problem for the public because they certainly need protection from being hurt from extreme moves. Stops do not protect well in choppy markets. Trading plans can be improved by knowing how stops work and what happens far too often.

If I get my signals for what I want to do, often I can see a new high for the day in the last hour of the day. If I have my signals telling me to sell, it oftentimes will say to sell the new high in the last hour, with the requirement of proving that position correct being that the market must spend little time at or above that new high. This is not saying to take a loss on a stop but saying that the new high is a move created by day-traders, locals getting out or bad buying creating the stop run toward the end of the trade day. For the position to be proven correct, the market must prove that the reason for the new high is just as I previously described.

Markets slip through stops on the bottom toward the end of the trading day also because of the day-traders, locals and bad selling that push the stops that build up below the markets. This is natural in trading and is not recognized often enough by traders, especially new traders.

Another big disadvantage of stops, as I see them, is the feeling by traders that they are protected from adverse moves. When the market is liquid, stops work fairly well. Too often, however, when an important report comes out -- the monthly unemployment report, for example -- markets such as bonds and currencies will do the long jump. There is no liquidity sometimes for as much as several support or resistance points. This means huge losses in a matter of minutes until the stop order can be executed.

Keep in mind a stop order is a market order whenever the price is hit. Most traders blame the broker for not getting the stop order filled at the stop price. How can they, if the market has no bid at your sell stop price? How is the broker to fill your order on a stop when every order he has is the same stop order price and there are no traders or orders willing to take the other side? Everyone sees the same chart. Stops are grouped in the same place.

After a big report, the stops are free game for anyone who wants to squeeze as much profit as they can. If I am correct, I know it will often take three waves of effort before I have to worry about the market reversing and taking my profit back. Why shouldn't I bid the lowest price possible after a report my way? If the market didn't fall substantially on a big report, I would be adding to my position until I see the bad selling. The bad selling is the stop selling after a report. Same on bad buying as the bad buying will be the stops buying at the market.

By understanding the drawbacks of stops, you can come up with a better-suited trading plan to protect yourself. Rule 1 does just that. Your criteria must include getting out if you don't want a flip of the coin at times. Big reports are those times.

Another aspect of getting your order filled way out here is when you go at the market on the open. Order fills look bad to some traders just by the way some of the quotes get reported. Some quote machines show the open price as the price that was the night trading open price. The next day the open may not be anywhere close to the night trading open.

Many trade systems signal a position to take after the previous day's close is used as data in the program and position on the open. This alone can skew the opening price by good margins of price difference. If you are buying and you are on one side of the pit, you may get a good fill. However, a large order may bid above your order in another part of the pit. The broker's job is to buy the offer when it is a market order on the open. They don't have time to look for the cheapest price when there are numbers to do. They take what is offered.

If you wanted to buy a computer and you did, you bought at the offer price. Why didn't you wait six months until the price was half as much? It is because you wanted it now! It is the same in trading. Your market order on the open is saying you want it bought now, not after it went down or went limit up or tomorrow after a selloff.

Just because the opening call was four cents lower and you put a market order in on the opening, are you going to get the low of the day? You might get the high of the day but most likely never the low. You may even be filled five to ten cents higher on the day if news changes quickly enough. Or in orange juice, you might have no sellers at all on the open for several minutes.

Orders are entered poorly more due to lack of understanding of how the market works at certain times in getting orders filled. It is seldom because of a mistake on the order placement by the broker or executing broker that you got filled way over there.

Another misconception of being filled in left field on an order is the thought that the broker is trading for himself. I watch this myself and can attest that what I see has never been beyond providing liquidity by a broker in poor liquidity times. Brokers are position traders. They cannot attend to being day-traders or scalpers. It is their primary job to fill your order first. The brokers I have seen do just that! They fill your order first.

One more aspect of being filled at what looks like huge slippage is the delay in quote prices and the delay in getting your brokerage runner to get the order into the pit in timely manner. They are allowed a certain amount of time to get your orders into the pit as it takes time to go to the desk, take the order to the pit and hand it to the broker who is filling other orders already. Repeat the process again as the runner looks for your order to report your fill price back to you.

Sometimes you don't know you were filled because the runner can't find the filled order before he has to run another order to the pit. Let me give some insight on this situation. If you must know if your was filled, CANCEL the order! This way the runner must require the broker to pull the order from the
deck. If it was indeed filled, it won't be there and the runner will have to look for it. Sometimes new runners don't know to look over in that pile for the filled order. Every runner starts a new career and is not good at it until experience becomes the teacher.

There are times when runners are seeing so much volume that the floor managers will tell them to do the most important aspect of their customer business -- that is, getting the orders into the pits and worrying about the fills later.

Often, confidence of customers and a new trader in the way orders are routed and filled is never above a "1" on a 10-point scale. You owe it to yourself to see the flow of orders and understand the strict method that must be -- and is -- followed by the commission houses and the brokers. Believe me, integrity is as good as it has ever been.

I remember when beans had gone above $4.44 for the first time in history, and I fed orders to the floor to sell out my longs as they hit $4.44. My fill was at 4.32. I did my research and checked all time and sales and price quotes that day. When I get a bad fill, I know why today and everyday. It has never been because of the broker not being alert. It has always been because I was not in the pit and did not know what was going on for anywhere from two to ten minutes before my order was filled.

Art, I know we want feedback on this so we can address the input from the *Futures* Talk forum. I never really had my heart into this chapter as it seems so cut and dried for me, but I know it is important to the traders. They must understand their fate when blame is quicker than answers in difficult market times.

ALS: Okay, traders, Phantoms, paper traders, brokers, newcomers and us old folks alike, let us have it! Your questions and observations, please!

Note: Within a few days after posting the message above, we had some good feedback from R.H. and it seems fitting to put it in this writing.

R.H.'s comments:

Phantom . . . thanks for another insightful chapter. Unless you've been there or had much experience, you tend to follow the notion that the little guy always gets the short end of the stick. This chapter explains the process of the markets for better understanding.

No specific comments other than paraphrasing my understanding of your words.

On tracing orders, is there other info or stats that one can request other than time and sales and price?

On "gunning for stops" it's my paradigm and others that running the stops creates a quick bounce and, once hit and expanded, the locals offset and is done as a tactic in itself. Your explanation seemed to be that it was not necessarily a concentrated effort to run the stops but rather floor traders positioned wrong, and as they offset near the thin areas, the market pushes through the stops.

On markets proving most people wrong and hitting their stop and heading in the way they had thought, Rule 1 was made for this action. If you position and the market goes against you, Rule 1 offsets the position, allowing for re-entry (in the last hour, in this instance) rather than positioning once with a stop just beyond the daily extreme. So Rule 1 allows us to use these areas to re-enter again or enter (e.g., on the 1 1/2-day move) rather than lose the position and see it go our way shortly afterward.

On stops and a big report, any other ways to see the bad buying or selling other than looking at the same chart everyone else looks at?

Thanks again for providing us clarity on the true workings of a market. R.H.

ALS: Phantom, a couple of questions from R.H. we should answer. His question on tracing orders: Is there other info or stats that one can request other than time and sales and price?

POP: The best way to trace an order is to know by name the phone clerk who takes your order and to identify the runner who takes your order into the pit. For me, this is pretty easy to know because I am pretty well known for requesting all the information I need to keep the integrity of my orders going into the pit.

I like to have the information because I like to prove to myself that the myths of what happened to an order are just that -- myths. Most of the time other traders who put orders into the pit are not aware of what has happened because of fast markets or newly reported information. They only know they got a bad fill.

Well, bad fills all have a good reason. Every time I check to see the reason for my bad fill, I have verified the circumstance that it has indeed been at my own hand that I got a bad fill. I didn't know at the time when I placed my order that I didn't have the timely news or what the liquidity was at the time. How can we always know the situation at all times? We can't!

You see, it is easy to use a crutch in blaming some reason other than a fact that we don't know at the time. It is wasted energy to think our fill was other than with the highest integrity. Even though I could fill all of my own orders, I know I can do a better job giving the order to the professional broker. Now, most traders don't know that.

On tracing orders, most of the time you can get time and sales, but the true event is that your order, if a market order, can be filled anywhere within a time limit of say two minutes. Now, have you ever seen a market move in two minutes? Of course you have! A market can move quite a lot in two minutes.

How do you win the game? If you put enough orders in, you will find it tends to even out. If you put few orders in, you will find you tend to get the short end of the stick as Randy suggested. The short end of the stick is that you will put your orders in just as the market is changing direction and starting to go against you.

You know what the market is going to do, and it has already done it by the time your order reaches the floor and you got the slippage from the market reaction. The quotes you receive are not the same as the bid and offer in the pit when you put the order in. There is always a lag. I can stand in the pit and watch the tape and be behind as much as minutes at times. I bid and offer according to what is going on around me in the pit. The public cannot do that. At times you are better off with resting orders, but execution is always the most important part of order placement if you don't trade large amounts.

Okay, time and sales is it, and the rest of your research is on your shoulders to check your broker, runner and phone clerk. A good commission house will do this for you but not always when the market is open. Do it when the market is closed and keep your own records. I consider it as if I am hiring the people who work my orders both into the pit and in the pit.

ALS: What do you think of R.H.'s ideas on his interpretation of running the stops ideas?

POP: I don't mean to remark lightly, but R.H. has a good handle on the correct interpretation of what I meant. I can't really add anything to his correct ideas.

ALS: Another question for you on stops and a big report: Any other ways to see the bad buying or selling other than looking at the same chart everyone else looks at?

POP: I see the reason for R.H.'s question on the bad buying and selling. In the pits it is pretty easy to see what is going on. Off the floor it is a sense we have to be alerted to in our thinking. We must know the possibilities of why things happen the way they do in markets. People will trade like herds at times and when the herds have finished their positioning, the market takes a breath and the move starts to fade.

It is the lack of followthrough that tells us when we have seen bad order placement. When we are away from the floor, we must be aware of lack of followthrough. It happens at the highs and lows because of momentum trading, which causes the moves to be quick and sometimes causes artificial moves.

My suggestion is to be alert as to how quick a move happens and then to watch for the followthrough in a proper amount of time. Each market is going to take a little different reaction to such conditions. R.H. has my idea on Rule 1 and the way I trade correct. It is the criteria of followthrough with the combined knowledge of what day-traders have done up to the last hour that I use to help generate a trade during the last hour or two. It is more powerful for me to get the bounce in positioning.

In fact, I have a chapter or two or even a book on the systems I use in trading. Of course, I would not give all of the inputs but enough to help most traders establish a game plan that would match mine.

ALS: Do you want to address any other situations on order fills?

POP: No, I don't as I think it is research that every trader must make on their own, and I cannot give them the results of their ideas of bad fills. They must slay that situation themselves to have the confidence of putting it behind them.

ALS: You've been generous in helping me write "Phantom's Gift." I know the traders do appreciate it and wonder what are the plans from here?

POP: You know I have been rewarded, and as I watch posts of forums, I see the effect this project has had.

Art, I think it is time to see how Robbie does in his trading. We must step back and be the observers again.

ALS: Does this mean this project is completed?

POP: Art, you know the project is not completed. I see the CD on your desk, and I see "Phantom's Gift" in red on the cover. I also know we have the best for last. Now, who wouldn't suspect that? We want our traders to make it big. So far, they have had lots of insight to interpret on their own.

You know the respect and expectation I have for the small trader. It shall happen that they are the winners. For how long I don't know, but they will be the unexpected winners.

The next step is to point out where the pot of gold is. I have a little surprise of a grand trade that is going to happen in the first full week of the new year. Unless you have seen Darrell Jobman's new internet video, you will have to search out the clue yourself. It is somewhere in the internet within your reach. You had better have it two-day delivered and in your hands by Thursday (Jan. 8) unless you want to search clues out yourself.

ALS: I see you can get the tape free with Darrell's book. I haven't seen it. What do you think of it?

POP: First class, just like Darrell!

ALS: Do we go ahead with "Phantom's Gift" on CD with the rest of the story chapters? If so, what will it cost?

POP: Only if our traders want it! Production and distribution will have a cost. It's up to our traders as to what they think it is worth to them. That will be the cost. It has to meet cost of production and distribution. It is all up to our traders!

ALS: What is next?

POP: I am a good observer. I know our traders. Some know me already! It shall get better for the small trader. To keep my mask on makes me pretty obvious, but the small trader has the best advantage this way. Let's keep it that way. Offers are offers, but I want to see my little Phantoms grow up.

ALS: So be it!

Thank you sincerely,
Art & for Phantom

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom of the Pits

By Art Simpson

Your Trade Program

"Let's look at some of Phantom's writings and his updated notes as to his ideas on your trading plan." **Art Simpson**

Phantom indicated it was time to conclude the *Futures* talk forum part of *Phantom's Gift* and move to the sidelines to complete the final phase of his gift to the back project. There were a few hesitations on the forum but only because of not knowing the further plans that Phantom intends to complete.

The project has been very successful and well-received, which pleased Phantom and exceeded his projections. Several comments were made to the point of wishing for a never-ending dialog between Phantom and participants on the forum. Phantom felt it was time for him to stand on the sidelines to see the results of his efforts.

Trading is an extremely difficult business, and research is always a demanding part of each trading day. While Phantom needs to concentrate on his own other projects, none are as important to him as the efforts he has given on seeing the small trader compete successfully with the big traders.

There are so many turns and new frontiers in trading, and only a few have been covered up to this point. For a trader to know what is required to stay in the trading game for a long period of time is most important and above other things. But without other aspects such as a trading plan and a system to generate trades, trading cannot be completed properly.

There are so many trading plans and systems; while one trader may be able to be successful with a system, another trader may have to adapt to master the same system due to different entry and exit points. It can be a very fine line.

With Phantom's rules, it is one more card with the same system. This is what Phantom intends to see in presenting his trading plan. Phantom's rules are to help traders learn and improve the standing somewhat due to the quicker actions required by the rules than actions of the deep pocket traders in an improved edge for the small trader.

The small trader cannot survive unless equity is preserved first and foremost in trading. It can be done but must be done with the skill required. This requires following closely the rules and learning oneself. It is difficult to learn the rules without a trader having an honest understanding the need for the rules, which require the trader to run like a coward to survive in the long run.

It isn't too much different than a professional football game in that, if you don't protect your chin you are running to defeat at the other end of the court. You know you will have another chance if you can continue to keep the opposing team (the market) from running up the score against you.

It must be instinct, and practice is required to make it a reaction trained by your practice. Knowing the rules is just not enough. No one is perfect in following the rules, and it must be your own thought to properly follow the correct rules. Same at getting out of positions that have shown to be correct.

Be proceed with a trading plan after we feel our behavior and reaction to market conditions is in our total control. As long as we are prepared for any outcome and adapt our behavior to all possibilities, we can start to follow a good trading plan.

Phantom wanted to give the important step beyond the critical starting rules to give traders a better outlook in their trading. We include some of his writings over the years of his trading on his things as how he looked for an entry and improve the edge upon entry. We shall look at ideas on system entry and trade signals.

All traders feel there is a system that is best. The best system is going to fail at some time or another, and that is why we need Phantom's rules. Bad systems can turn into good trades and be correct at opportune times. Many of these systems have drawbacks.

Many systems assume you will have the funds to cover what the back-testing indicates is required to margin your trades. Phantom has included these assumptions and will give ideas as to the difficulty of using back-testing as the criteria of system creation.

The best system is not to see the entry requirement everyone seems to focus at least on the team bench. This absolutely will defeat the system. What system is best? Phantom has thoughts on which system you might use to better survive. Which ones are they?

Most of the book has required a course of thought and study to interpret a lot of what Phantom has indicated in his insight. It was no accident that his insight prompts your own questions and wondering. You are what you are, and you have your own important ideas. You can use your own thinking. From here forward it will be a little easier for you. It is discouraging to have a market take funds away from you and your family. The more soul-searching you do about what the market is waiting to show you, the better prepared you will be in using the rules properly.

Take a break, have a favorite drink or refreshment and get your note pad ready to make your own notes. You are going to draw your trade plan according to your goals. Phantom will have some good suggestions about your trade plan.

It is easier to look greed and fear in the face with the proper frame of mind. You have to be your own motivation expert in your trading. The motivation must be tilted toward the rewards of receiving big losses out of your account. Who is responsible for your trade? You must look at a big loss the same as you would a personal bad habit. It is undesirable to ever have a big loss show on your statement.

Phantom is going to look at your statements. If he sees big losses in your account, you will have to answer to him personally. It is his business when you have a big loss because he is trying to see it in your face. You've let down the dojo, your teacher and you will have a miserable day. POP wants better treatment for you in your trading. He cares and you must treat each minute your trade is in the market.

Can you make that good fortune in trading? Only if you lose small and never let turnaround markets take you for a ride. It is your question to answer. Phantom has no one to answer to for anything to prove to anyone. You must answer to yourself. Let your performance speak for you. It should not take you more than six weeks to know for sure.

You can expect to be on your way not because you made some money but because you don't lose your money day-trading from you. We have to know some big winners to be successful for them. The only thing they forget or never knew was that, though it isn't difficult to make money, it is difficult to keep it. There is a difference in the two.

Okay, if it isn't difficult to make money, why don't you understand before you make money that you must keep all money at whatever cost you can create with the word small. The biggest lesson I ever saw was a trader who had a good understanding method of trading in the cash market. You may have heard of the Hunt silver slide. It can happen to anyone who does not respect the reward of a SMALL LOSS! You must see the reward of a small loss. Don't let it be your forgotten advice.

Let's look at some of Phantom's writings and his updated notes as to his ideas on your trading plan.

Art Simpson (AS): Phantom, I'll transcribe these into our book and have you verify the details that I don't fully understand. Phantom, I have known you very many hours and years, but I don't know everything about you. When you put thoughts on paper, it seems different for me than when we talked answers back and forth.

I'm more like the readers now, as I must read what you wrote instead of what I wrote from your spoken insight. Do you think this will make it easier for the readers by doing it this way?

Phantom of the Pits (POP): You bet, Art! I am exact in my thought when it comes to making a trading plan for traders. You go ahead and put it in the book.

ALS: Okay, here we go!

POP (from his writings): In every trading plan there must be an element that gives you the edge. It is that edge that can change the outcome of your trading career. In the pits it is the edge to locals get for putting on the market that is to their advantage that allows them to trade for a longer term than if they had not gotten the edge.

Not all rules are equal, but the rules are the ones that have a plan that will work. To me, the rules are the most important part of giving me the confidence I need to know that I can and will survive in my trading. Survival is the most important point of any plan. If I know I can survive, then my plan can be much easier to develop.

While my plan may seem advanced to others, there are only three ways for a market to go. I know you are going to ask me about the rules. But, nevertheless, there will always be a situation coming up in a few days, and every trader off the trade floor is not thinking the trade but writing points out a third way the market can move.

I don't want to put the rules on the *Futures* talk forum because I didn't want to confuse new traders with my thoughts on this point. I am not going to ask you to interpret what I am trying to say; I am going to tell you what I want to know.

A good trading plan must have the third way a market can move which is the unknown. It is the third way a market can move the surprise side move. No, not exactly!

The third way a market can move is the edge we want in our trade plan. A market that goes from trade and then breaks sideways is a third way. Good trend-day trade traders to get out of cause them to get stopped out, will turn into your friend. The most powerful signals in a plan are the ones where the market has moved two ways in a trend and are showing reversal to the big bullout of trend-followers. I know of a couple of funds that have been proven winners due to this one impact of their trading. Some have other criteria, too.

Oh, you say, but you are the great trend-follower of all time. What is wrong with throwing in the towel early in a trend? I'll tell you what is wrong! Not throwing in the towel early is what is wrong. Big losses are the reward when you don't have the edge of a reversal signal or resistance. You got it, the market trips and you must take it. You need not only to take the profit but also to head the other way. You need to make criteria for this situation in your trade program.

In your trade plan we now have two situations that can give you the edge. The first is the surprise side and the second is the third way the market can move. The surprise side is an event that takes place during the day and, unfortunately, seldom allows the public to benefit from entries -- mainly because they are on the other way when the surprise hits.

The public seldom reverses their position because they seldom get out at the right place in the first place. You must use this knowledge to your advantage and not be caught up in the same situation.

I don't care how bullish or bearish a position you have established appears to be, there is a place in every day when it is going to be wrong for the public and the position. The odds are won't hit the place most days. You'll find it seldom happens when expected in trends. That is why you must have that exit planned during every day. You must be prepared when your trade plan to use the rule of needed.

How do we put this into our plan? If you are using point-and-figure charts, you can often see a 45-degree line of resistance or support. A good trend will give you several attempts at the support and resistance lines. After several attempts, a reversal day will break through the line. At that point you will have stops, and the stops can generate more orders coming into the pit. At the price moves through, it will generate more orders to exit.

You don't want to stay around long after the first move through the line. Even if it does reverse back again, you really will have a good clue that you did the right thing by offsetting as consolidation starts to take place if the line holds.

Some of your biggest trends and moves come from the breaking of support and resistance of a strong established trend. Put these points into your market can move. Even if you were to only trade this edge, you would be making the best moves of your program.

Let me qualify this for you a little more. This is the third way a market can move. The market must have moved in the direction of the trend and then hit support or resistance. It is not the same as the surprise side moves. The surprise side move is different in that it can be caused by a reversal of a market after going out of the open, it is a surprise side move. The surprise side also can be when opinion is one way and the market has no more traders to reinforce the opinion with positions in the market before the open.

You must have a surprise side plan in your trade program at all times also. The surprise side, over years of research for me, has always been the opposite way the market opened in all markets except one. It is up to you to develop your own plan for this. Some traders think about taking a diversified trade plan by spreading your trades over several contracts. If you trade two different futures and one is a loser, you have the one I expect to be a surprise side in the direction of the open, you have the odds in your favor in your thinking.

I don't want to mislead you on the surprise side. What I mean is that, if the market opens and closes higher for the day but was lower for the open, it is not a surprise side. The surprise side also can be when opinion is one way and the market has no more traders to reinforce the opinion with positions in the market before the open.

You must have a surprise side plan in your trade program at all times also. The surprise side, over years of research for me, has always been the opposite way the market opened in all markets except one. It is up to you to develop your own plan for this. Some traders think about taking a diversified trade plan by spreading your trades over several contracts. If you trade two different futures and one is a loser, you have the one I expect to be a surprise side in the direction of the open, you have the odds in your favor in your thinking.

Oh, you say, but you are the great trend-follower of all time. What is wrong with throwing in the towel early in a trend? I'll tell you what is wrong! Not throwing in the towel early is what is wrong. Big losses are the reward when you don't have the edge of a reversal signal or resistance. You got it, the market trips and you must take it. You need not only to take the profit but also to head the other way. You need to make criteria for this situation in your trade program.

In your trade plan we now have two situations that can give you the edge. The first is the surprise side and the second is the third way the market can move. The surprise side is an event that takes place during the day and, unfortunately, seldom allows the public to benefit from entries -- mainly because they are on the other way when the surprise hits.

The public seldom reverses their position because they seldom get out at the right place in the first place. You must use this knowledge to your advantage and not be caught up in the same situation.

I don't care how bullish or bearish a position you have established appears to be, there is a place in every day when it is going to be wrong for the public and the position. The odds are won't hit the place most days. You'll find it seldom happens when expected in trends. That is why you must have that exit planned during every day. You must be prepared when your trade plan to use the rule of needed.

How do we put this into our plan? If you are using point-and-figure charts, you can often see a 45-degree line of resistance or support. A good trend will give you several attempts at the support and resistance lines. After several attempts, a reversal day will break through the line. At that point you will have stops, and the stops can generate more orders coming into the pit. At the price moves through, it will generate more orders to exit.

You don't want to stay around long after the first move through the line. Even if it does reverse back again, you really will have a good clue that you did the right thing by offsetting as consolidation starts to take place if the line holds.

Some of your biggest trends and moves come from the breaking of support and resistance of a strong established trend. Put these points into your market can move. Even if you were to only trade this edge, you would be making the best moves of your program.

Let me qualify this for you a little more. This is the third way a market can move. The market must have moved in the direction of the trend and then hit support or resistance. It is not the same as the surprise side moves. The surprise side move is different in that it can be caused by a reversal of a market after going out of the open, it is a surprise side move

Phantom's Gift

By Art Simpson

Phantom's Christmas Gift

Phantom's Journey

Phantom remembers those people he meets along his journey in trading and those he has met since he started giving his insight back. His remarks were that he felt he could serve you much better than he has. Phantom felt that he is the beneficiary of what you have given to him.

The best compliment I can remember Phantom ever getting was when he was at an important meeting. The wine steward had just poured a glass of red wine for the host and, to be polite, Phantom also accepted the gesture. As the wine steward poured Phantom's glass to the brim, the last few drops spilled onto Phantom's white shirt and suit.

The wine steward turned to Phantom and said in a loud voice, "Sir, a lesser man I could have served perfectly!"

Phantom turned to the wine steward and said to him, "It is I who must serve mankind better! I am
grateful for your reminder."

Phantom wants to serve you better and is grateful to you for the thought you provoke within his reach. Some of the great traders are often overlooked. Great traders are not just those who have been fortunate enough to make it big in trading but also those who have made great trades in their lives.

It was Phantom's request after seeing a simple kindness of others toward a dad and his son in their loss of a long-time family friend. The family dog had just passed on. To see the pouring of kindness of others toward the man and his son touched Phantom's heart.

It is not just this random act of kindness that touches his heart but powerfulness of wonderful thoughts that can be extended by others. Traders in their time and atmosphere of intense trading are still human in a cold and harsh environment.

Phantom wanted us to write his journey in an effort to balance the scales of trading and living as partners within the soul along the way. Trading at times can reach out and grab your soul with cruel implications, but your living can repair your touch of kindness within your soul. Phantom wants you to see his insight of you.

It is true that much of the human element has nothing to do with trading and that most see no need to study human behavior. Or do they? In researching the lost dog incident, it is clear that around 90% of traders involved tolerate such thought along their trading route, and actually those opposed
also contribute.

Phantom starts his insight to your journey. There is something to be learned. Or is there? He starts with his Christmas Gift.

Arthur L. Simpson

Phantom's Christmas Gift

By Phantom of the Pits (POP)

Along my journey of trading, there have been great traders I shall always remember. To my surprise, it is not the big success stories I remember but the great trades (events) those traders have made in their lives. Often, it is a helping hand in exchange for their precious time; other times it is dedication in their lives toward mankind. The brotherhood shown by those great traders is what my journey has shown most to me.

I want to share some of my insight on you, the great traders in our world. The strongest thing in the world is love. It is stronger than death. What guides us to gather strength even when touched by death? This is just one of my questions in an effort to balance my trading career with the living side of the scales. What I have found out about you continues to give me answers. I want to share that with you.

The wife of a trader conveyed to me one of the great trades made by a person whom I consider a great trader. In our journey, we shall identify that person only if that person wishes us to do so. In this case, the person has not decided to do so at this time.

It was Christmas Eve in 1979 and two men had just finished their work shifts on a United States
Navy ship tanker. The ship was anchored in Ulsan, Korea, and unloading fuel a distance from shore. Because the two men didn't get to be home with their loved ones on Christmas Eve, they had plans for the evening. It was 8 p.m. and the two men took a boat launch to get to shore.

Both men were carrying large bags ashore. One of the men questioned whether they should be taking anything ashore for fear of being thought to smuggling. The other man pointed out this was surely the time to take that risk as it was indeed Christmas Eve, and understanding might be easier if an explanation were required of them.

After getting off the boat launch, the two men walked about two miles, and the sacks were really getting heavy by this time. It was a cold winter night in a country foreign to them, but they had a plan and carried on with their heavy sacks.

The two men arrived at a building and entered, as it was unlocked. A lady came and met the two men from the ship and asked them to have a seat. A short time later a group of children came into the room and spoke in Korean. It seemed to be with great excitement that the children were pleased to see the two men. They had seldom seen others and especially these two men.

One man's name was Preston, and the other man was my trader friend. The youngsters were laughing at their broken Korean language. Because the youngsters could not speak English, it was the only chance for communications.

My trader friend, according to his wife, had caught the eye of two children. One was a boy about 10 years old, and the other was a young girl about 6 years old.

The only word the children were trying to convey to the men was the word "Wahn" or "Waan" or "One." The men thought that perhaps they were trying to show they could count in English. The young girl would stare at the two men, and the older boy would not stop talking, as he was very excited to meet Americans on Christmas Eve.

"What is in the sack?" the housemother asked.

The two men said you shall see in time. Let us get the children something to drink. At that point they were given something to drink.

Preston pulled out a sack within a sack, and the children's eyes got wide as they thought it was a trick of sorts. The little girl was questioning with her eyes as the two men pulled out pieces of fried chicken, which was left over from the ship's Christmas dinner that night. The men started eating a piece of chicken in front of the children, whose eyes were sad as they seldom were able to eat as much as they wanted.

The children had never seen or eaten fried chicken in their entire lives. Chicken pieces were being passed around to the youngsters as they learned the tasty smell of the new-found food. The full sacks of food were more than enough for it didn't take long for the children to get full.

The oldest boy motioned to the housemother and asked several questions. It was Christmas Eve and getting late for the children, but they were allowed to stay up late this special night.

The two men had to be back at the ship soon because it was to leave at 3 a.m. as the tide was going out, and it was the only time the ship could leave safely. About midnight the two men left on the launch for the ship. As the two men arrived back at the ship, the crew made ready to depart as their unloading of fuel had been completed.

My trader friend had tears in his eyes as the ship left, and he thought of the starving children and his small participation on Christmas Eve. He had just been presented with a gift for trading his time in this event. He would see many years later it was one of the best TRADES he would ever make.

Fifteen years later in October 1994 my trader friend was once again on a ship, and his wife had just been in a life-threatening event. Being on a ship and away from family presents impossible resolve in helping anyone.

My trader friend searched the ship for a Bible, and for some reason none existed on this ship. The ship made weekly trips from Puerto Rico to New York and was in New York on a Saturday. After the ship had been properly secured to the dock, a man walked on the ship with permission to do so and approached my trader friend.

The man held out his hand and said, "My name is Mr. Wohn. Here is the Bible you wanted!"

Why, my trader friend was astonished as he had not mentioned this to anyone. How could this be? A stranger walks aboard a ship and hands out a Bible after my friend had been looking for one earlier in the week.

Having just finished lunch, my friend asked Mr. Wohn if he would stay for lunch. Mr. Wohn asked, "What is your meal on the ship?"

"Today it is fried chicken," my friend informed him.

Mr. Wohn indicated it was his favorite food, but he had already eaten lunch. At that time Mr. Wohn started to explain just how fired chicken became his favorite food.

"I am in America from Korea," Mr. Wohn said. "I promised God I would give mankind what they are in need of in their lives."

My friend asked him how he had decided to dedicate himself to helping others.

"I was 10 years old and my sister was 6 and the only family I had. We were both orphans and lived in an orphanage in Ulsan, Korea. I first met God in my life on Christmas Eve in 1979. It was a cold Christmas Eve, and it was a sad time in our lives for we never had enough food to eat and we would always be hungry when we went to bed.

"At about 9 or 10 that night, our housemother awakened us and told us to come with her. We went to our lunchroom and sat at one of the tables. It was cold so my sister and I sat nearest to the stove to get warm.

"Two men were in the room, and I thought we would see a magic trick as one of the men pulled a sack out of bag. The men started to eat a piece of food, and it looked strange to us. They gave us some and motioned for us to eat the same way as them. One man put it up to his mouth and took a bite of the food. So my sister and I did the same. It smelled good and really was wonderful. It was fried chicken. It was the first time we ever ate fried chicken.

"Well, I remember the kindness of the two men to this day, and that is how I decided I would help
others.

"On that Christmas Eve, our housemother let us stay up late as this was different from the other nights. I was the oldest in the group of children, and I wanted to know who brought the food for us. I asked our housemother, and she said God and Jesus had brought us the food. My sister looked at the two men and wouldn't take her eyes off of them when she heard the housemother's explanation of where the food had come from. She had heard of them and wanted to know more. My sister asked how they had gotten to their orphanage, and she was told they had come on a big ship in the water.

"The two men left before we went to bed, and all the children talked about the wonderful food and happiness of that night. Our housemother told us it would soon be Jesus' birthday the next day.

"I was excited the next morning, and my sister was more excited as she wanted to go down to the ocean to see the big ship that God and Jesus had come on to give them food.

"I will never forget the disappointment in my sister's eyes when there was no ship. Can you imagine that? We had just seen God and Jesus in our eyes, but there was no ship there at all. How had they gotten to us?

"I began to lose faith that it was God and Jesus who had brought us food. My sister said yes, it was them and she knew it was and wouldn't change her mind. She was so dear to me and all I had in life. So I let myself have the same faith, and I promised God I would spread the same kindness to man.

"My little sister talked of meeting God and Jesus when she died and of living with them. She would ask me if I would come with her. I would cry at nights because I knew I would soon lose her."

Mr. Wohn told my trader friend of his sister's death when she was eight.

Mr. Wohn indicated that perhaps he had seen God and Jesus that Christmas Eve in 1979. As he walked down the gangway, my trader friend called to him but didn't know what to say. He could only think of that Christmas Eve away from home and loved ones when he had walked a cold night's walk with heavy sacks of food from the ship to an orphanage in a Korean town.

My trader friend yelled to Mr. Wohn, "Mr. Wohn, God uses people to accomplish his wishes at times."

Mr. Wohn yelled back, "Yeah, I know! Would you thank your friend for that Christmas Eve in '79 for me?"

Talking to my trader friend's wife, I have found a deep gift. She says it is one of the most powerful gifts her husband cherishes. To trade a part of his life and to see it come back everyday when he looks at that Bible is the greatest Christmas gift he will ever need.

It was a great trade my friend made in 1979, and to see it come back amplified 15 years later is what I consider a great trade of a great trader. There are great traders among you, and I see this of you, too!

I hope you can see the true meaning of being a great trader. This one Christmas story of a ship's chief cook and an officer is just the beginning of your great future in your trading career. There shall be more along the journey, and I wish to share them with you. It's all about YOU!

Phantom

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved, October 1997

Phantom's Gift

By Art Simpson

Time to Reflect on God's Rules

***"Our farewell and God's flight to our friend, John Denver."* ALS**

This chapter is as important as any chapter of any book written in modern times to Phantom. I don't mean to take a platform, but today I have discovered many reasons for *Phantom's Gift* being written.

Today (Oct. 13, 1997) Phantom was given some very sad news. I have never in my life seen Phantom defeated in his entire career. Today Phantom is on his knees. He is in pain and distress to understand what has happened in his life. He has been prepared for most any possible outcome by being able to protect his positions.

Today is much different! He can only reflect as to ,what the importance his life is to others in this world and what his purpose has been for presenting his insight into trading and methods of trading in order to make repayment of his life at this time.

I can only pass along to you what some of his views today included and why. Many of you who have read my efforts to convey his thoughts to you in my own unfamiliar writings perhaps understand my difficulty as I write with tears on my keyboard.

Phantom is not one you would consider extremely religious, but today has shocked his thought on reality of what is beyond! Phantom's heart has finally been torn from him -- no matter how prepared he has been to protect and defend his chosen world.

Today Phantom learned that John Denver was killed Sunday (Oct. 12, 1997) in his experimental aircraft when it crashed off the coast of California. The aircraft plummeted into the Pacific from about 500 feet of altitude. Trading has been Phantom's life, and singing has been John's life. The love of flying has been in both of their lives. There has been common ground by so many of John's family, friends and fans.

Phantom knows the hardships and difficulties of being a public figure and of the struggle of public figures like John. We keep Phantom's identity confidential for that reason. I can only request that you understand and respect Phantom's request.

John had given a big part of his life to others by being in the public's eye. This always takes a big part away from family over the years. This causes Phantom to reflect how trading is such a very small and minute incident in our lives. Who do we turn to when our world is voided of one of our familiar lighthouses in life?

Several months ago Phantom indicated it was time for payback, and he really didn't know why it was so important now or what the true reason was. We both agreed to find reasons or wait for the answer. Today we understand more of the reasons.

You must understand that Phantom today cried and pointed to when he was asked what his favorite book was that he failed God's test. You see, his favorite book is indeed the BIBLE. Phantom felt no one would understand a different direction than a trader's highest goal. He set out to explain and guide traders to the best possible outcome in their trading lives. It is clear as to how this guidance was meant to point. Phantom actually pointed out the reason for the book and the word, which was to be understood by all traders and everyone in their lives at one time or another.

Phantom tried to point out his Rules 1 and 2 for the purpose of helping you survive in trading. He has given you the ultimate choice of following the correct path, as he wanted to help guide you away from the rocks and storms. He always will offer his guidance. But it is you who must make the correct choice.

It is my interpretation that this following statement is the truth of trading and the reason for the book: "If you do not use proper rules in your trading, you will lose everything you had hoped to gain." Phantom has been the messenger but not the judge of your survival in trading!

The Bible, which is Phantom's favorite book, also gives us a choice. We are given the choice of believing or not believing what is written. The Bible indicates those who believe in what is said in Bible and accept it shall have everlasting life.

What Phantom has missed about his favorite book is that we all must make the choice, but there is only one correct answer. Our decision, according to the Bible, can be based on what will happen IF WE DO NOT BELIEVE or it can be based on what will happen if WE DO BELIEVE! Just as trading must be based on the correct choice, so must our choice for everlasting life.

Phantom's Gift has another message, I believe, in addition to Phantom's insights. The most important part of our lives is what is in our lives. Our family and our friends are above all material gains from trading and must, at all times, be the most important reason for our struggle in being a good trader. Your God must be the ultimate and supreme in your life to have any meaning to those who love you and want you to be their sunlight in life.

Let us learn from what has just happened to Phantom in his life! Phantom cares and he needs to understand. His distress is not easily overcome. I think Phantom had to face the reality of mortality or lack of mortality in his life. Phantom is determined to work harder at giving back as long as it is welcomed.

Our farewell and God's flight to our friend, John Denver.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom's Gift

When We Lose One of Our Own

By Harold B. Simpson

"Love is why I came here in the first place,
Love is now the reason I must go,
Love is all I ever hoped to find here,
Love is still the only dream I know."

John Denver, *Seasons of the Heart*

It has taken me awhile to get my thoughts together after what has become one of the most eventful trips of my life. We arrived home in time for Allan to make a 7 p.m. class on Monday evening. He had to mentally shift gears from vacationer to student in a matter of moments. We dropped him off for his class in Danville, and we waited for him to get out before we came home.

Our trip out to Lake Powell went smoothly. It's always a great joy to drive through the Rocky Mountains. Through the World Family of John Denver, I met some wonderful people named Virginia and Sam Allen. Sam is a writer and has written a number of excellent woodworking books. Virginia is a self-described "arch seeker." Knowing that we were going to be passing through their town of Moab, Utah, they invited us to tour Arches National Park with them and share a few John Denver notes as well.

We met in the welcome center parking lot, and with Virginia and her son in our van and Mom in their 4 by 4 with Sam and their other son and Cathy driving the station wagon, we formed a caravan of three vehicles. Virginia and Sam turned out to be extraordinarily knowledgeable about the park.

I didn't know it at the time but found out later that Virginia and Sam had written the guide book that is handed out when your enter the park! Virginia has spent much of her time exploring the far reaches of the vast park and has discovered some of its arches. When you find and cataolg a new arch, you get to name it. One of her sons just recently found one and had the honor of naming it. He called it "Hideout Arch" because he said it was very difficult to locate -- high up in a very inconspicuous place. They took us to the cave used in the Indiana Jones *Last Crusade* movie. They also pointed out Arches Park's most famous arch of all, "Delicate Arch."

As we traveled along from one place to another, Virginia and I had some wonderful conversations about our mutual enjoyment of John Denver's talents. I happened to have a new four CD set of John's music called *John Denver . . . The Country Road Collection*, that Virginia didn't have. She put a disc in the van's CD player, and we listened to his music as we traveled through the beautiful park.

Our time went much too quickly, and we said our good-byes around 3:30 or so. We were heading to Lake Powell via a different route (to us), which meant a long drive through some of the most desolate and awe-inspiring scenery in the United States. With me leading in the van and Cathy following in the wagon, we made our way winding back and forth, up and down some spectacular red sandstone formations that were seemingly not of this earth.

At one point, a little more than an hour and a half after leaving Moab, I went over the crest of a mountain that gave me a startling, fearful feeling unlike I'd ever felt before. The sun was low on the horizon, and we had been traveling on the shade side of the ridges for quite some time. Just as I reached the sun side, the glare was so intense that for a few moments, I could no longer see a thing . . . I was completely blinded! Not knowing what lay before me, it seemed an eternity before I could catch a glimpse of the road again.

Those few moments were some of the most frightful moments I've ever experienced. I quickly called back to Cathy on the CB to slow down because you'll be blinded by the sun at the top of the hill. We have all experienced the similar effect of the sun momentarily blinding us as we drive into it. Cathy and I both agreed this went far beyond that sensation. Along with this blindness came a fear the likes of which I don't recall having experienced before. We made it on to Halls Crossing at Lake Powell, our destination, at sunset. We had an evening to relax before boarding our houseboat the next morning.

Rising early and feeling about as happy as ever with the way things were going up to that point, I headed off to an early morning shower. I could hear that someone had turned on the TV, and I was happy they had. Perhaps we could catch the weather forecast for the coming adventure. Then, with a heartfelt cry that I knew meant something horrible had happened, I heard Cathy exclaim that John Denver was gone!

The next moments were filled with immediate denial. It took me into a world of hearing the words but somehow not registering in my mind the reality of it all -- at least not fully comprehending the reality. I went through anger, I argued with mom when she wanted me to get going and pull me away from the news bulletins. I wanted to stay glued to the TV to get every last detail that was known at that time before we just had to leave for the boat.

I've always known that it doesn't matter how experienced the pilot, how safe the airplane, aviation is at the same time the most unforgiving and, yet, the most rewarding activity one can ever participate in. I know John was aware of that, but life is not worth living if we live in fear.

When I met John Denver a few years ago at the Experimental Aircraft Association convention in Oshkosh, Wisconsin, I asked him if he would sign my pilot license. He looked at me and asked me if I was sure I wanted him to do that. I said, "Absolutely!" I was embarrassed by the fact that I couldn't find a pen, and a lady standing close by offered us hers. The way he said "Are you sure?" makes me think I might have been the only one who ever asked him to do that.

A year or two after that he starred in a made for TV movie called *Higher Ground* about a bush plane pilot in Alaska. That was enough to inspire me to go for my seaplane rating. It was some of the most enjoyable (fun) flying I've ever done. I learned to fly a Maule Rocket 235 floatplane in the waters of Lake Monroe near Sanford, Florida. In the process of obtaining my new rating, I had to surrender my old license for the new updated one. Good-bye, JD's autograph.

Somehow, I thought that was his gift to me in exchange for his autograph. I later was able to obtain another of his autographs at a book signing in Chicago of his autobiography, *Take Me Home*. (By the way, thanks to my brother, Art, for letting me know about the event and enabling me to see him again.) John Denver has meant a great deal to me for many years, and there will be an empty space for him for the rest of my life.

We had been told we might be asked to upgrade to the highest class houseboat should the need arise. As I began the checkout procedure, I was told we had lucked out and had drawn the best houseboat on the lake. *The Admiral* was luxury houseboating at its finest. You should have seen the smiles on my crew's faces when they realized what they were in for. The ship can only be described as awesome!! We were loaded and away in a couple of hours.

Each day on the lake was warmer than the last. It just kept raising our spirits higher as we floated along this most unique jewel among the earth's treasures. There just isn't any place I have found that gives me the feeling that is Lake Powell. Simply put, I love the place!

The days were all sunshine, and the night was filled with the full moon and bright stars and planets. We located an ever-elusive Anasazi Indian dwelling in Cottonwood Canyon. They were experts at hiding these things from their enemies. We hiked for two hours trying to find it, only to find it was where we had looked the moment we arrived in the canyon, yet we couldn't discern it from its surroundings! Great fun!!

The swimming off the back of the houseboat was refreshing, to say the least. I never did get the courage to go down the slide. Seems kind of strange such a thing should give me pause, when jumping out of an airplane in my younger years didn't bother me in the same way.

Disembarking from the houseboat following this greatest of adventures wasn't going to be something we wanted to do but offload we did. Our watery travels were not over, though, as the path back to civilization included a ferry boat ride across the Bullfrog Basin to a quicker path back home than we had come. As we headed towards Colorado, it occurred to me that it might be possible to attend John Denver's services, which would likely be in his hometown of Aspen, Colorado. A phone call to my brother, Art, confirmed that he would indeed have some type of service on Saturday in Aspen.

The timing could not have been more precise for us. We would be in Glenwood Springs, Colorado, by the evening, and that would be an easy 35-minute drive to Aspen the next morning. The service was to be at 2 p.m., and it was to be held at the music tent in Aspen.

We arrived around 10:30 a.m. I stopped at the Pitkin County Airport where in 1976 John Denver learned to fly a Cessna 172 with his dad as instructor. From beneath the tower, looking to the east, one can see the mountain on which John Denver lived in Starwood. There were many more jets sitting on the ramp than I thought would be usual. I suspected this was due to the number of important people who were no doubt here for the services.

One particular small craft caught my attention. I was parked right behind it. It was a Burt Rutan designed aircraft called a Long Easy, the very same type of craft that John Denver had lost his life in. How ironic, to be standing by this aircraft, at this airport, looking at that mountain, on this day. Was I somehow meant to be here? Was this moment just coincidentally mine for my imagination to make of it as it will or was I supposed be a part of all this? I was awestruck . . . no one else was aware of what I was feeling. Something magical was sparking my thinking.

The day before a formal service was held at Faith Presbyterian Church in Aurora, Colorado, where his mother and brother, Ron, Lives. Today, Oct. 18, 1997, was to be a final farewell from his family and friends in the setting that John would have been most comfortable with -- his hometown, Aspen.

Cathy and I were about the ninth or tenth people in line. It was a joy talking to those around us in line. We all told each other of our connections with John and his music. The couple ahead of us in line had flown from Minneapolis that morning. They had left on 45 minutes notice, just barely making the only connections that would have allowed them to make the trip. They were both married but not to each other. They both knew of each other's love for John Denver and were friends through that. Their spouses, knowing how important it was for them to be there, were understanding enough to let them travel together.

Another lady flew from Nashville, Tenn. She had been waiting since early morning and was asked to leave so that sound systems could be set up and wires safely strung, etc. She left and came back a short while after Cathy and I got there. By the time she had come back, the line had grown considerably. She came to me and told me about the fact she had been the first one there. After I explained what she had told me to everyone around us -- by now all friends -- I brought it to a vote to allow her and her friend to join us at the head of the line. It was unanimous; we let her in. She turned out to be a lawyer -- a good lawyer, she said, and there is a difference!

We passed around addresses for each other, promising to get in touch again. The music tent holds 1,700 people. The lower section was reserved for relatives and close friends. We had the best seats available for the "public."

The stage was set up as though a concert was about to begin. John's guitar was there, his microphone was there, his band members from the past and the present were there as part of the audience. The whole thing took on the look of a concert, but we all knew this was no concert. This was the last time we would gather together in such a way to celebrate the life of John Denver. The music tent was overflowing by the time the ceremonies began.

At about ten minutes until 2, a group of small planes flew over in trail, spaced about 15 seconds apart, each containing a pilot expressing in his own way a tribute to a downed flyer. One was a Christen Eagle Biplane like the one John had owned and what he had flown solo to Oshkosh the day I met him there. Another flew over so as to allow his plane's shadow to pass over the assembled mourners.

High overhead, a beautiful white sailplane, possibly John's, was released to soar in the blue heavens above. I know that John's ashes were to be released over the mountains of Aspen on this day. Was I watching this final act of releasing his remains back to the earth without knowing for sure it was happening. I somehow didn't want to know but had to smile at the thought of how beautiful a way to return our physical body back to the earth -- the most dramatic of ways to end the most dramatic of lives.

In one of his songs he sang: "I can see you in singing skies and dancing waters, laughing children, growing old, and in the heart and in the spirit, and in the truth, when it is told."

All those things were present at that moment.

With the help of Tom Crum, one of John's best friends, Zak, Anna Kate, and Jesse Belle Denver put together a tribute to their Dad that was at times almost unbearably sad and at others some of the best laughs I've had. They were all there, all of John's family. His mother, Erma; his brother, Ron, and his first wife, Annie. His second wife, Cassandra, all of his aunts and uncles, cousins and friends he had amassed over the many years. His long-time producer, Milt Okun, who vowed to use his remaining years to somehow make John's works accepted on the higher level that it deserves.

The stories were told in a way that made us feel very much closer to the John Denver that they had come to know by their close association with him over many years of friendship. I learned many things about him that were intimate insights, precious tidbits of the life of someone whom I really knew little but on this day was very much privileged to be allowed to be a part of.

During the service, one of his secretaries told a story about a moment she had with John. I think it was Stephanie Ryan, who said John had asked her if she believed in astrology.

She replied that she believed in just about everything (with a laugh).

John then said his astrologer told him this year and this time in his life is so important and that he has a chance to be out in the world like never before.

Stephanie just said, "Great, I think that's amazing. I'm so happy for you."

He said this chance only comes about once in a lifetime.

Stephanie said, "Even more than in the 1970s?"

"Yep, just once in a lifetime,"John replied. "Pretty exciting, don't you think?"

Stephanie said, "I think that's great, and you are so deserving of it."

As she reflected back on this conversation, she couldn't help but wonder, although she didn't take it that way at the time, if this had been what he'd meant. His spirit just exploded into the universe!

The day was as perfect a day that only God and John Denver could have made. The aspen trees around us glittered with the light warm wind, the sun was gently shrouding us all with a perfect warm glow, and the sky . . . the sky, I've never seen the sky more beautiful -- a shade of blue that perhaps can only be seen from the 8,000 feet of altitude at which Aspen lies. The day was one in which not a single person there wanted to leave behind. What was to be a two-hour celebration of music intermixed with the sharing of eulogies turned into a much more relaxed atmosphere of the sharing of stories and feelings that lasted more than three hours.

My new friend, Virginia Allen, and another friend of hers named Patty, who had flown in from Michigan, made it to the celebration. I was able to greet them as they arrived. Some of the people around us were people that I had met at one time many years ago through various fan clubs. It seemed the people to which it mattered the most somehow had made their way to this gathering. I don't know exactly how it all works, but somehow we all felt that John had a hand in all that. Maybe so.

It may seem strange to call this gathering a celebration, but that is exactly what it became. That is what he wanted it to be thought of. He celebrated life and lived it to the fullest.

At the end of the day, we were asked to bow our heads and close our eyes and to think of John Denver as being there with us at that moment. To think of him as being in the wind, in the mountains around us and in the sky above. It wasn't hard to imagine that for me. They played the last song that John recorded, *Yellowstone (Coming Home)*, as we watched hundreds of white helium-filled balloons drift upwards into the blue sky.

It was a kind of closure for me. We left Aspen.

We may never know for sure about the exact timing, but that flash of light that rendered both Cathy and I temporarily blinded from bright sunlight and brought with it a feeling of complete fearful helplessness occurred at approximately the same time that John Denver crashed into the Pacific near Monterey, California, on Oct. 12. At most, there could only have been a few minutes' difference.

My mind can make what it wants to of that. We'll never really know.

Peace,
Harold and Cathy Simpson

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997

Phantom of the Pits

By Art Simpson

About the author

Arthur L. Simpson is an independent trader and has been a member of the Chicago Open Board of Trade and (now) the MidAmerica Commodity Exchange continuously since 1971. He is a registered floor broker with the National Futures Association.

Art is a licensed Merchant Marine Officer by the United States Coast Guard and is licensed as a pilot by the Federal Aviation Administration. He also holds licenses issued by the Federal Communications Commission as a first class radiotelegrapher, general radiotelephone operator, GMDSS radio operator/maintainer and an amateur extra radio license. He has worked assignments with the United States Information Agency Military Sealift Command.

He has served as chief engineer at CBS radio in Champaign, Ill., and has served as a consulting broadcast engineer and been instrumental in construction of broadcasting stations.

Art lives in Indiana with his wife Karen and their family of pets. His interests include trading, flying, amateur radio, computer programming, music and world travel.

Futures Magazine home page
Other learning opportunities

E-Mail: asimpson@csinet.net

© 1997 Arthur L. Simpson - Phantom of the Pits
All rights reserved. October 1997