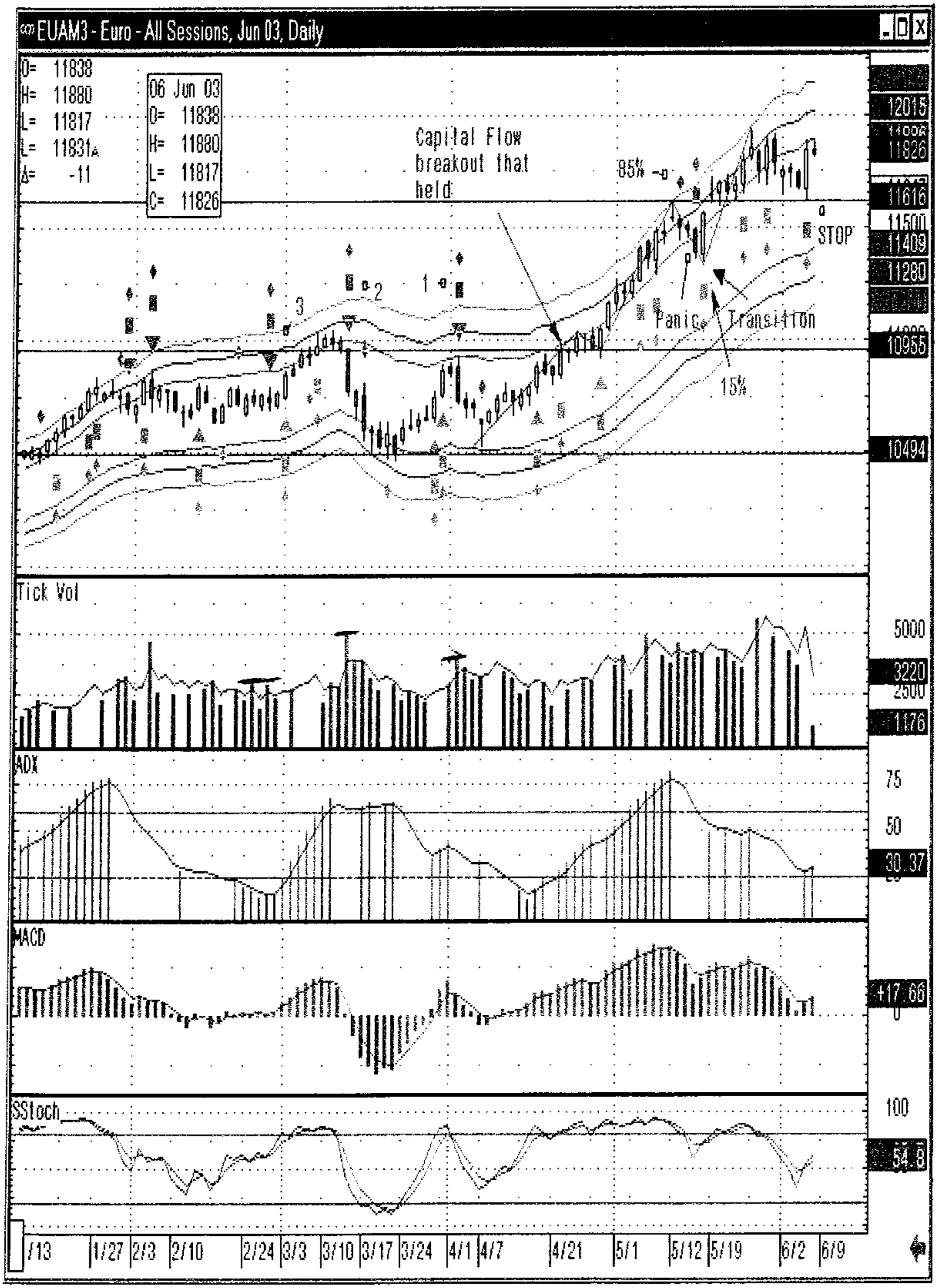
MARKET TRENDS, CAPITAL FLOWS, TRADE EXECUTION AND PROBABILITIES V7

If a trader is going to succeed through time it is important that most trades are placed with the prevailing trends, macro capital flows and directional probabilities. Traders must evaluate the directional probabilities through multiple time frames and make sure that a long or short position is supported by those probabilities. In theory, most trends should continue to proliferate and when they don't a significant reversal is probable. An external trend in motion will with a high degree of reliability continue to stay in motion. Time tells the trend. All traders need to be aware when major highs and lows are being penetrated indicating potential directional trade. When a market moves outside of 50 or 100-day new highs or lows there is probably a strong economic justification for that macro market strength or weakness. As E.S. stated, he does not understand why anyone would trade against the trend when it is already a difficult enough game trying to trade with the trend. Panic liquidations force traders out of the trend over and over again. In actuality it is these corrections that fuel trend continuation. Lets explore this concept more fully.

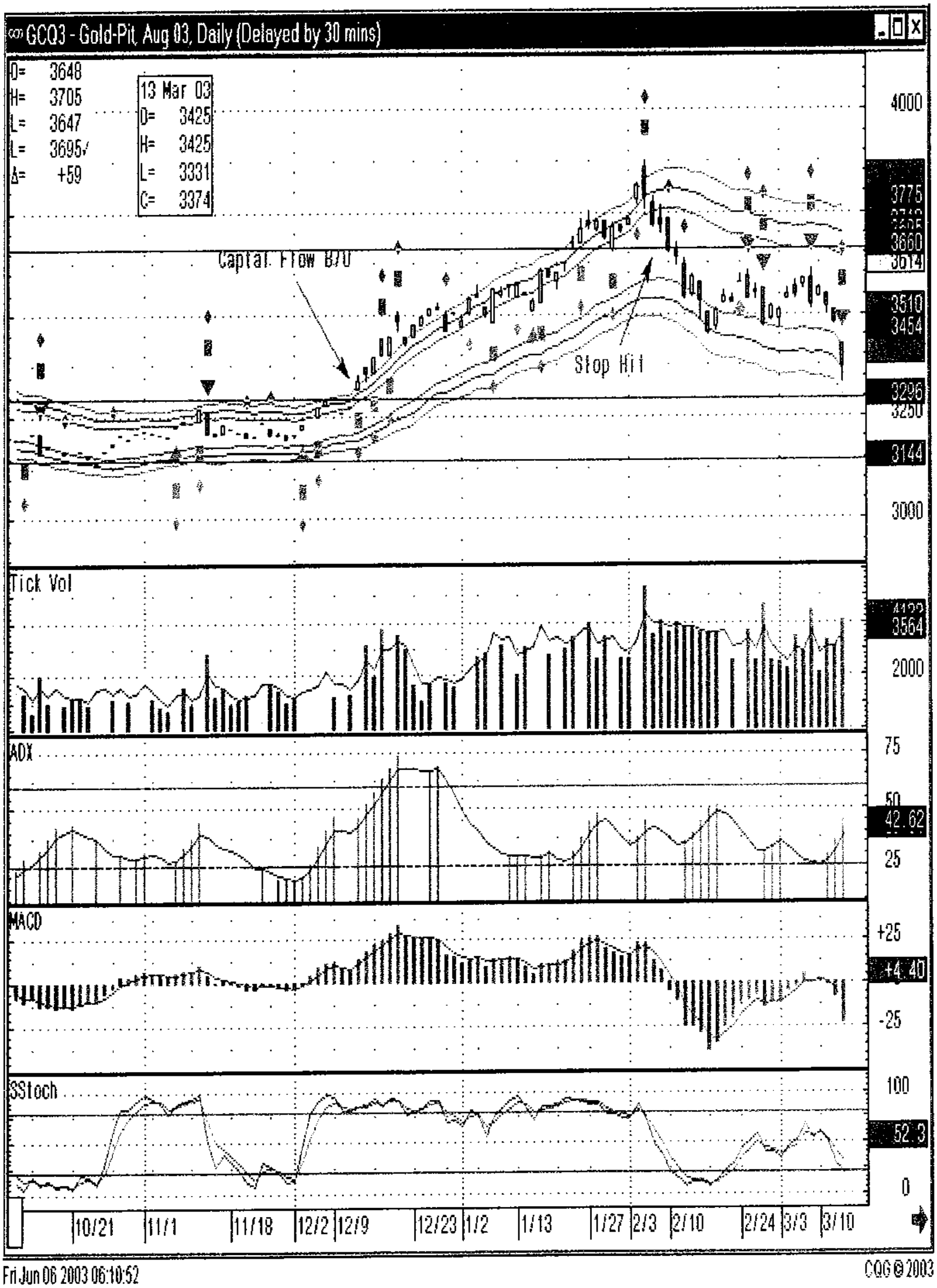
Directional probabilities are based on predictive price patterns and capital flows. Given strong directional range expansion patterns on high volume what is the probability that price will continue to reach specific predictive price levels thereby continuing to perpetuate prevailing trend. Any time the market exhibits strong directional thrust activity whether it is a 5 minute price bar, daily, weekly or monthly range expansion bar or an expansionary swing line there is an 85% probability of price continuation and only a 15% chance of taking out the opposite extreme. This is known as the 85-15 rule. Every major trend has 3-7 pullbacks. Average price levels are important support and resistance levels and are used to gauge the probability of trend continuation. **As long as the 20 EMA and 50% level holds on a pullback during external momentum based wave structure there is an 85% probability that the trend will resume and make new highs or new lows in the direction of the prevailing trend.** In order to determine the future direction of price, all a trader needs to do is evaluate bar to bar and swing line directional probabilities from multiple time frames. Up or down range expansion through multiple time frames will help a trader determine market odds and reward to risk ratios. When corrective price activity holds the averages, swing line structure and individual range expansion price bars there is an 85% probability of trend continuation following a trend resumption price transition. This is when traders should let open positions reach their price targets. Traders should try and initiate positions as close to low probability rejective price levels (15% levels) as possible allowing for the use of tighter stops. Intraday traders should try and initiate positions when high volume range expansion bars are retested on pullbacks.

High volume is required to move a market and overcome the inertia associated with neutral markets. When a dynamic trend is underway it is extremely difficult to create a sustainable imbalance against macro directional capital flows that will reverse the prevailing sentiment and macro volume flows of the market. This is why range expansion bars and external expansionary swing structure are more likely to perpetuate directional capital flows than reverse direction. It is only late into a directional auction sequence or late into a multi thrust campaign that directional volume flows breakdown and counter trend imbalances develop that can potentially arrest a trend. Protective stops should be placed outside of multi swing structure that trails at least 2-3 prior high volume directional thrust bars. **When both bar to bar probabilities and swing line probabilities are at 85% favoring the long and short side of the market with a rising ADX let position run.** Traders must define key support or resistance levels and define where a market is most likely to go with an 85% probability and also specify the 15% probability levels where the market should not go. The market will reject these levels 85% of the time. These are key risk points that need to be identified. Whenever the market fails to move in the direction of the probabilities and penetrates low probability price levels that should not be penetrated a big move in the opposite direction is probable. Counter trend directional imbalances can stress open longs or open shorts and arrest a prevailing trend. Those stressed open longs or shorts will then be forced to rotate out of their positions as they lose directional price control. Therefore markets that move outside of these 15% levels tend to trigger big moves. There is also a very high probability that this 15% breakout level will be retested after the initial penetration prior to a big move occurring. As you can see it is very important to know all key structural price levels, the macro capital flows and the probabilities associated with these highs and lows so a trader can determine which strategy to implement with the highest probability of generating a successful outcome.

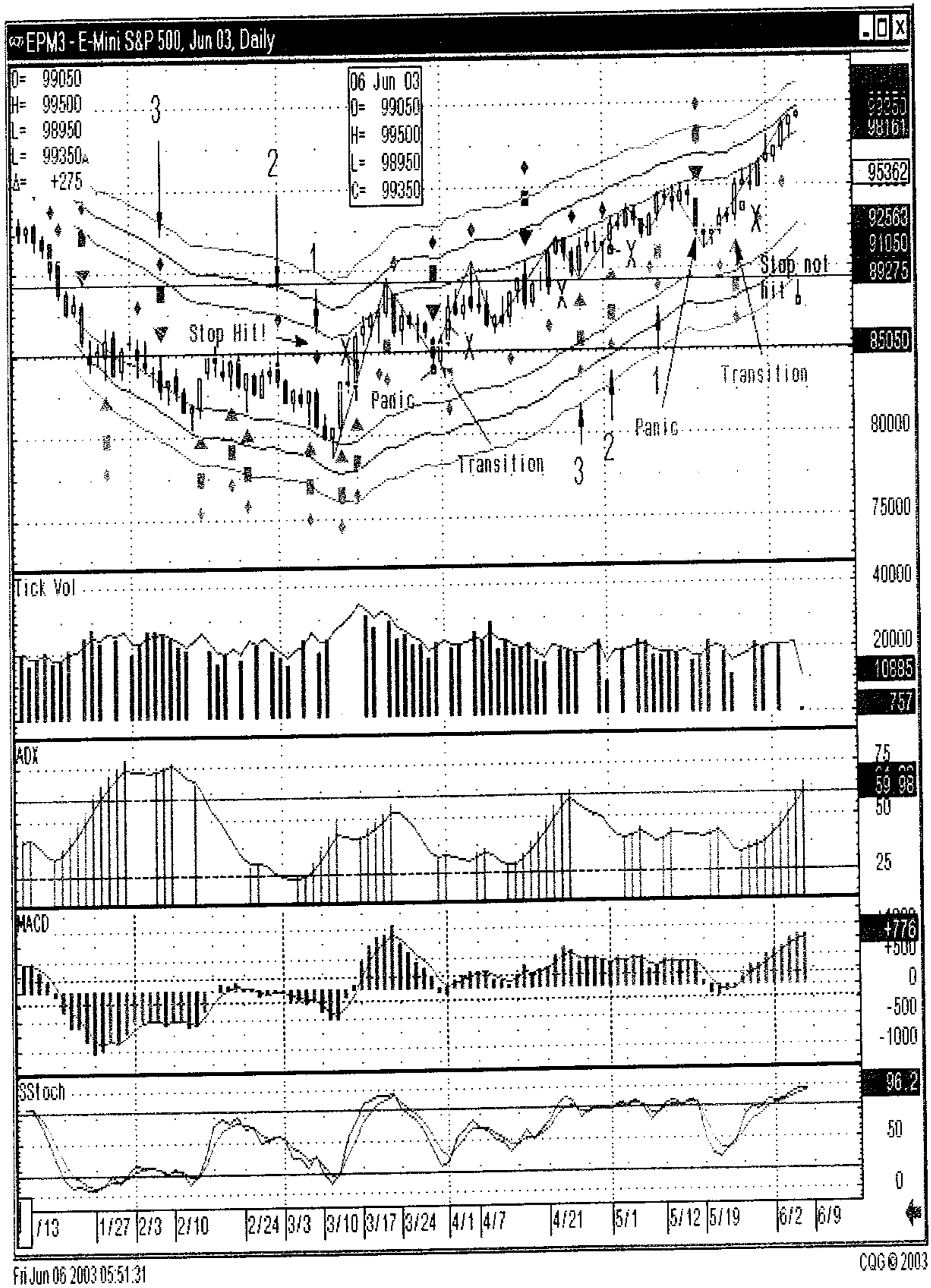


Fri Jun 06 2003 06:07:22

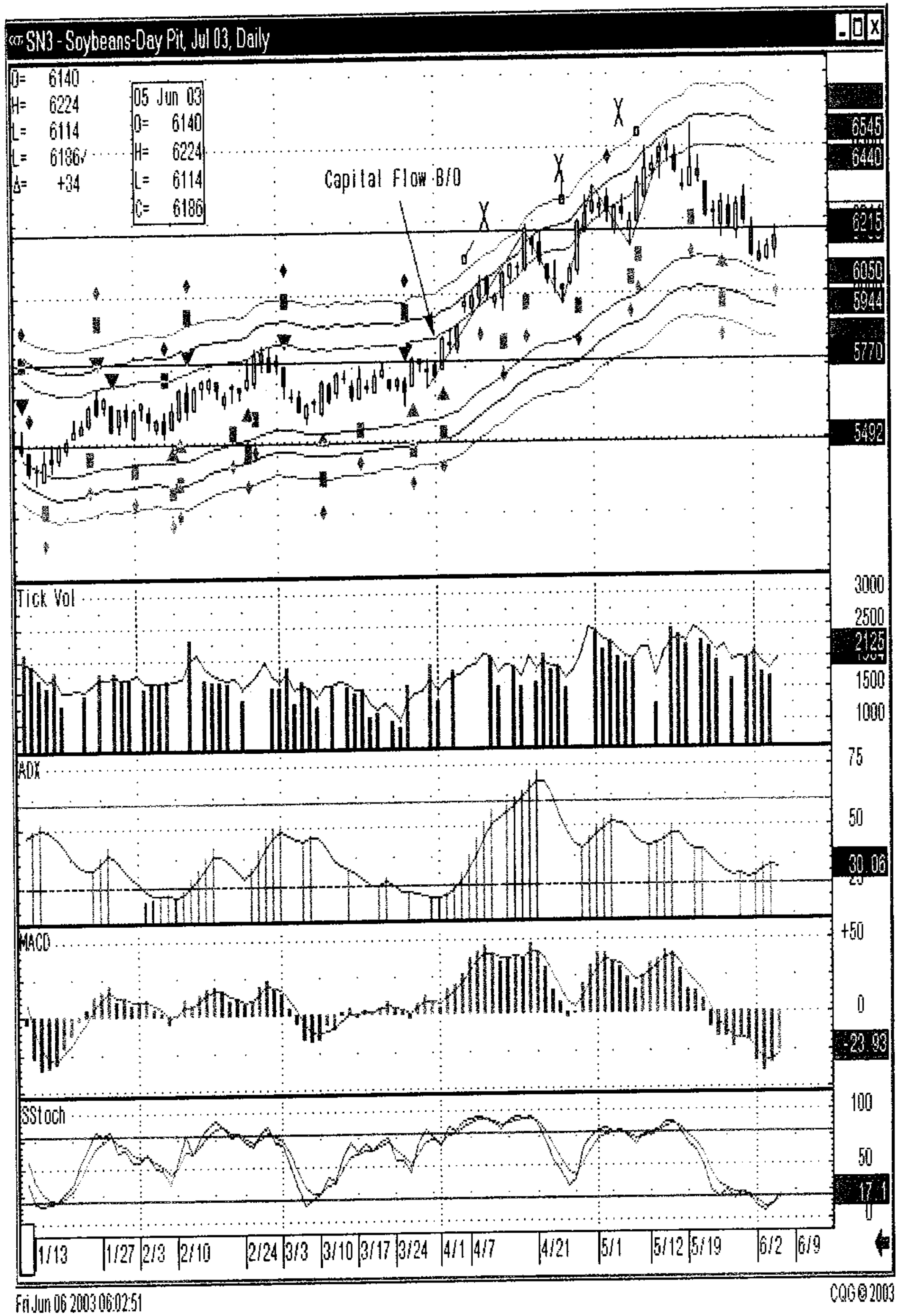
CQG © 2003

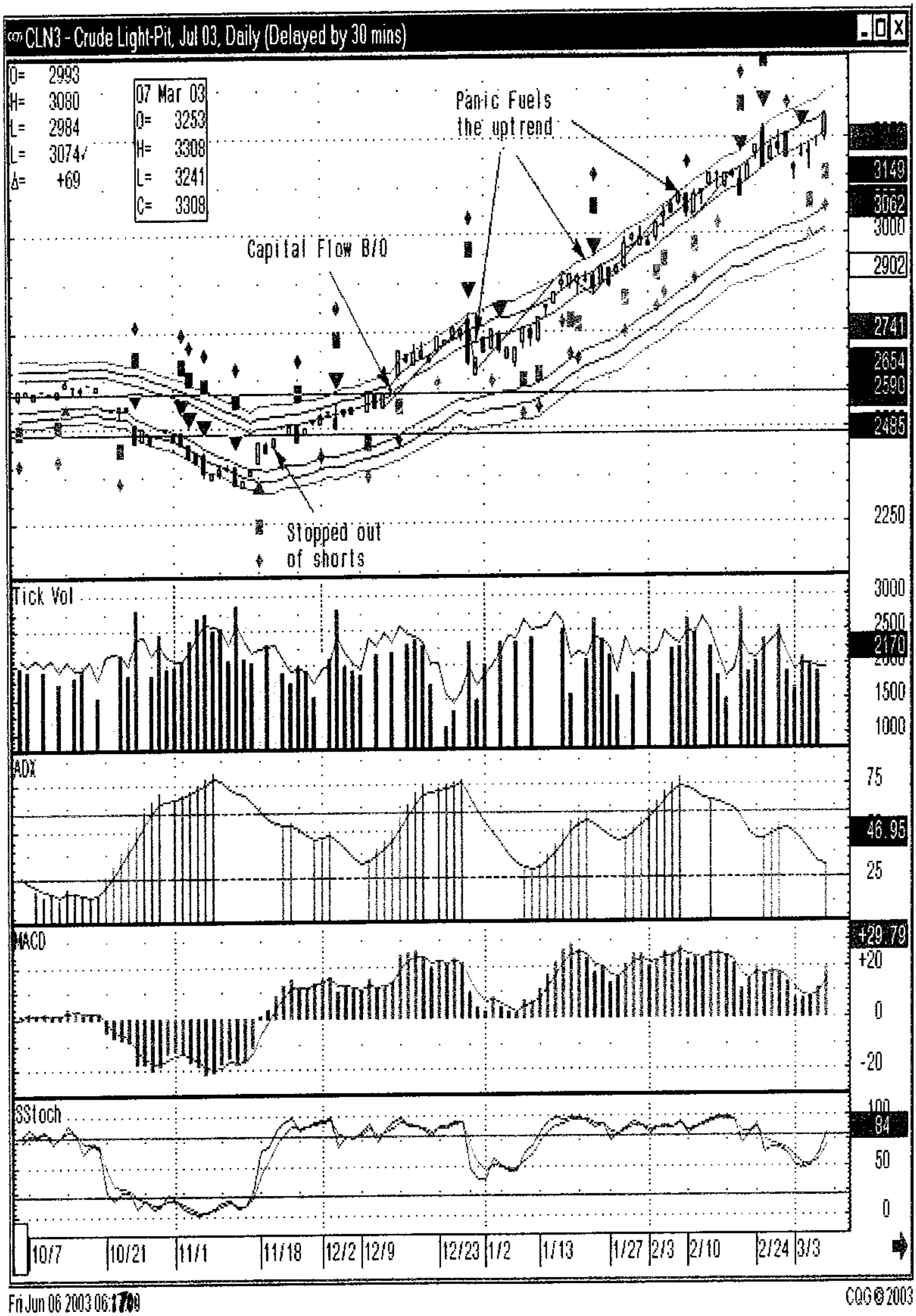

GCQ3 - Gold-Pit, Aug 03, Daily (Delayed by 30 mins)
O= 3648
H= 3705
L= 3647
L= 3695
Δ= +59
13 Mar 03
O= 3425
H= 3425
L= 3331
C= 3374
Captal Flow B/O
Stop Hit
4000
3775
3660
3614
3510
3454
3296
3250
3144
3000
Tick Vol
3564
2000
ADX
75
50
42.62
25
MACD
+25
+4.40
-25
SStoch
100
52.3
0
10/21
11/1
11/18
12/2
12/9
12/23
1/2
1/13
1/27
2/3
2/10
2/24
3/3
3/10
Fri Jun 06 2003 06:10:52
CQG © 2003

Learning to read capital flows and then gauging the levels of prevailing sentiment is integral to this game. **The essence of price movement is defining who controls the market, where they are exerting this control and where price control is lost.** Traders must be able to define precise price levels where a shift in the balance of power could take place possibly reversing a trend. Trading confidence comes to those who are able to properly evaluate market sentiment. It is extremely important to define capital flows and then trade in the direction of those flows. The first auction failure at a prior trend pivot point may indicate a breakdown in the trend and kick off neutral price structure with down trending volatility. When neutral structure dominates a trader should identify the last three high volume transition bars above and below the market. When all of these bars are penetrated with a rule of 4 high volume breakout from a low volatility environment a multi thrust campaign will manifest from this breakout. There is an 85% probability of trend continuation as long as pullbacks hold equality with other corrections and the 20 EMA and 50% retracement levels continue to contain corrective activity during external wave structure. A retest of the prior capital flow breakout level is probable prior to a strong directional thrust. When a trend develops trail macro price structure by trailing swing line pivot points.

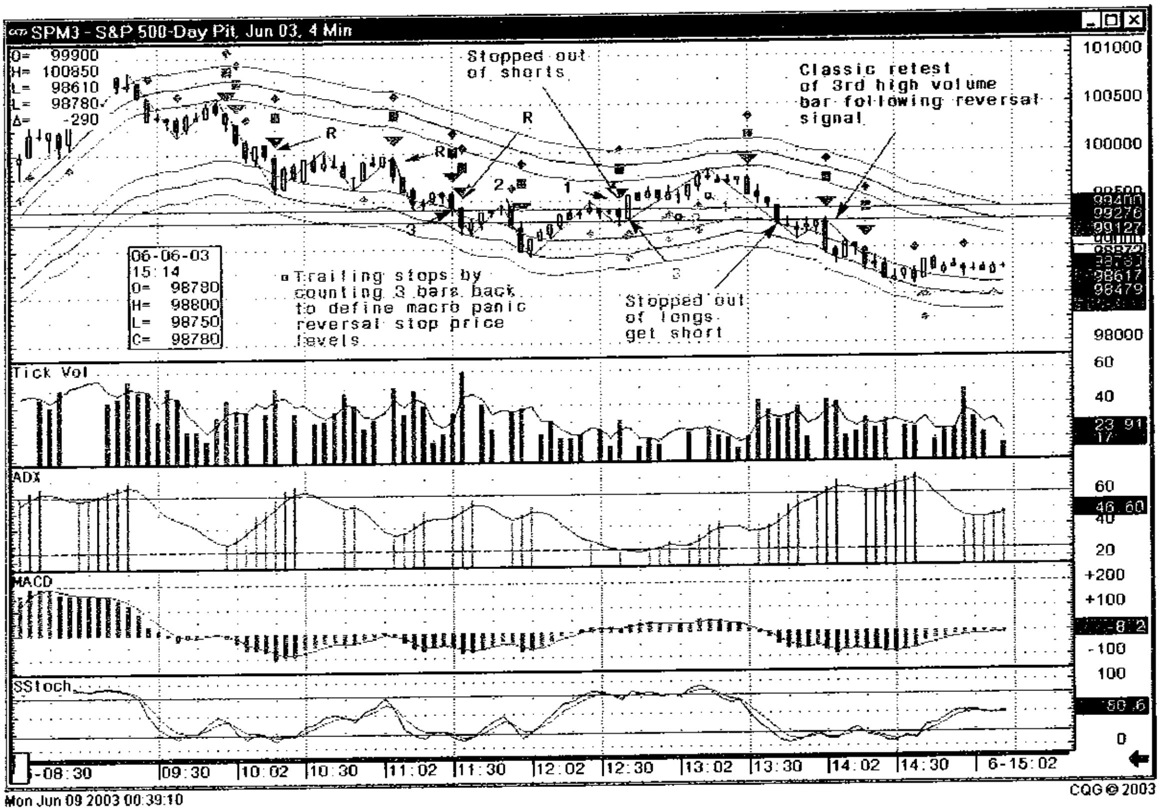


EPM3 - E-Mini S&P 500, Jun 03, Daily
O= 99050
H= 99500
L= 98950
L= 99350
Δ= +275
06 Jun 03
O= 99050
H= 99500
L= 98950
C= 99350
3
2
1
Stop Hit!
Panic
Transition
3
2
1
Panic
Transition
Stop not hit
Tick Vol
ADX
MACD
SStoch
1/13
1/27
2/3
2/10
2/24
3/3
3/10
3/17
3/24
4/1
4/7
4/21
5/1
5/12
5/19
6/2
6/9
Fri Jun 06 2003 05:51:31
CQG © 2003


SN3 - Soybeans-Day Pit, Jul 03, Daily
O= 6140
H= 6224
L= 6114
L= 6186
Δ= +34
05 Jun 03
O= 6140
H= 6224
L= 6114
C= 6186
Capital Flow B/O
6545
6440
6215
6050
5944
5770
5492
Tick Vol
3000
2500
2125
1500
1000
ADX
75
50
30.06
MACD
+50
0
-23.93
SStoch
100
50
17.1
0
1/13
1/27
2/3
2/10
2/24
3/3
3/10
3/17
3/24
4/1
4/7
4/21
5/1
5/12
5/19
6/2
6/9
Fri Jun 06 2003 06:02:51
CQG © 2003

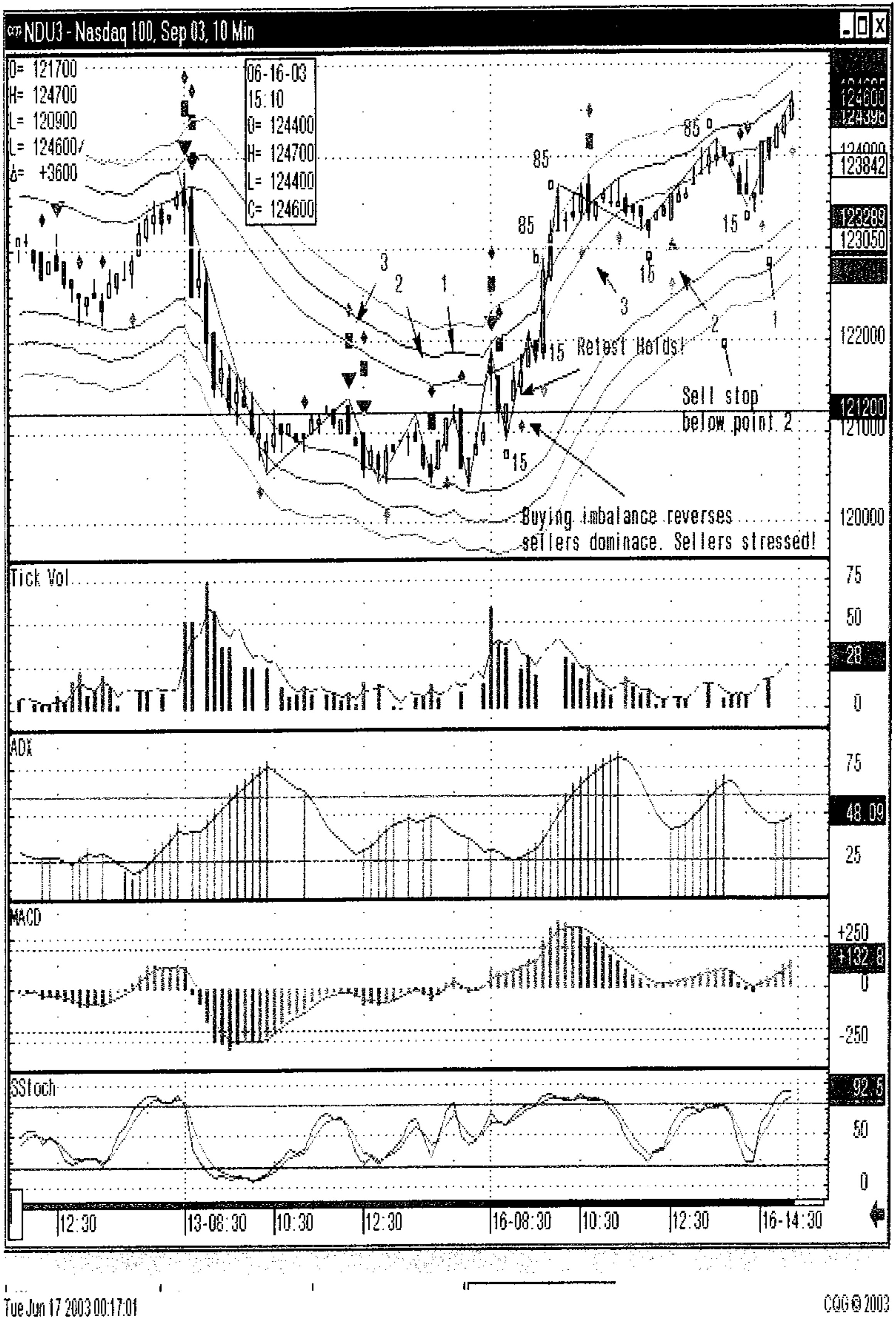

CLN3 - Crude Light-Pit, Jul 03, Daily (Delayed by 30 mins)
O= 2993
H= 3080
L= 2984
L= 3074
Δ= +69
07 Mar 03
O= 3253
H= 3308
L= 3241
C= 3308
Panic Fuels the uptrend
Capital Flow B/O
Stopped out of shorts
Tick Vol
ADX
MACD
SStoch
10/7
10/21
11/1
11/18
12/2
12/9
12/23
1/2
1/13
1/27
2/3
2/10
2/24
3/3
3149
3062
3000
2902
2741
2654
2590
2485
2250
3000
2500
2170
1500
1000
75
46.95
25
+29.79
+20
0
-20
84
50
0
Fri Jun 06 2003 06:17:09
CQG©2003

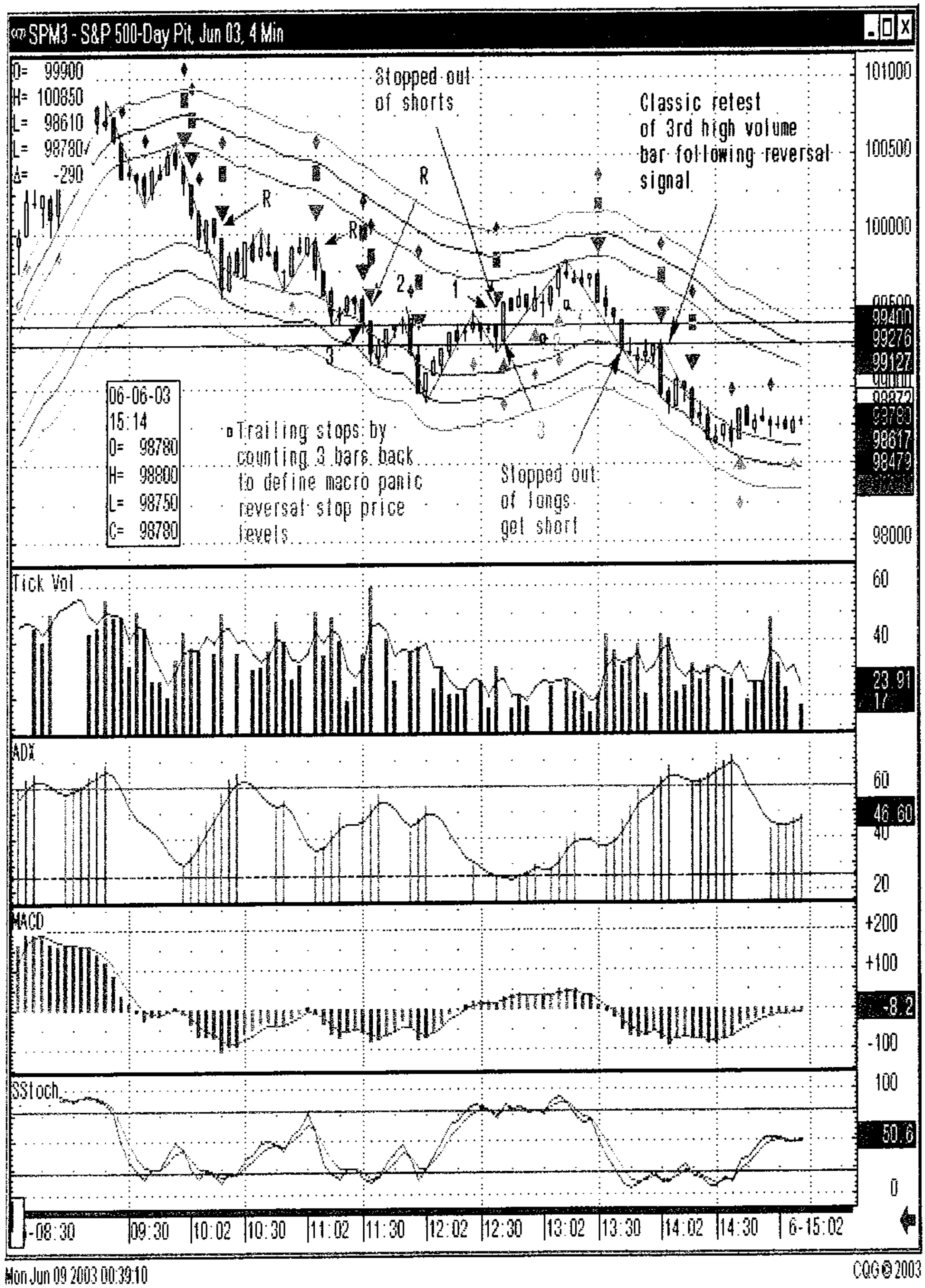
All traders need to utilize capital flows and probabilities to make better trading decisions. They need to eliminate inefficient trades to become more profitable. Traders must first scale up and down in time and price and evaluate swing trends, capital flows, MA filters and then determine which side of the market has the most favorable probabilities. Traders need to count back 2-3 high volume range expansion bars to accurately determine directional capital flows as well as identify those price levels that will seriously stress open longs or shorts if violated indicating a loss of price control. **A violation of corrective equality, penetration of the third high volume bar back and/or penetration of 2 or more swing highs or swing lows confirms a trend reversal seriously damaging prevailing trend.**



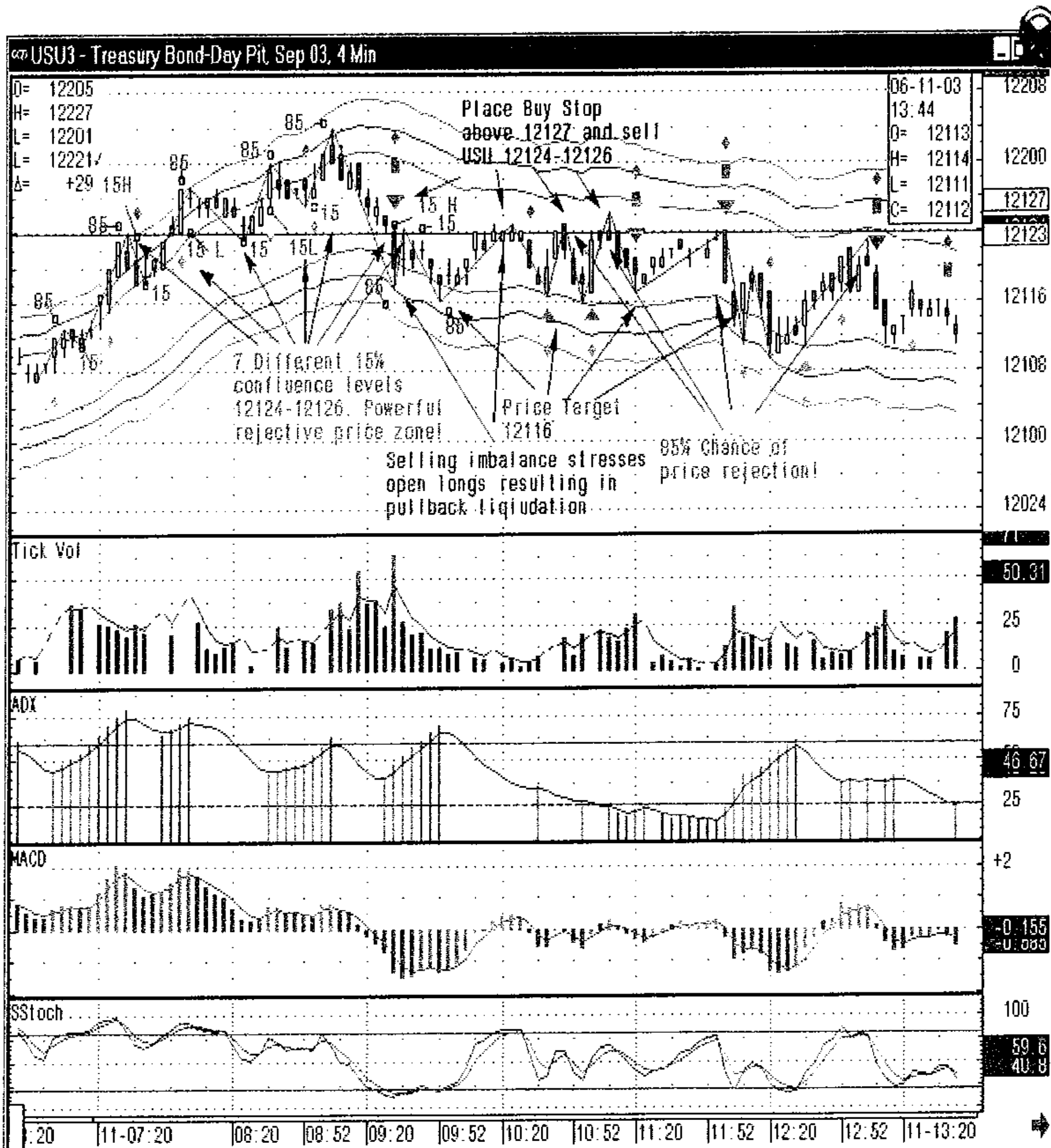
The next step would be to determine the most advantageous price levels that favor a long or short position by first evaluating multiple time frames and identifying all the 15% swing and range expansion high and low price levels. These are the highs and lows that have a low probability of penetration and a high probability of rejection, There is powerful rejective tendencies at or near a confluence of these 15% levels. Learn to trade against these levels free of fear. These price levels will continue to reject price until these levels stop repelling price. During pattern or price structure development with down trending volatility highs and lows should be assigned 15% probabilities. These are the price levels where the market should not go! So these are the price levels that give a trader outstanding trade location. Protective stops are to be placed outside of structure allowing for very tight risk control. **The most important question that needs to be answered prior to initiating a position is where to place a stop that truly identifies where a position is proven wrong.**

These are the macro price zones that can arrest and reverse a trend when penetrated. Traders are then to patiently wait for the market to test and then transition away from key price clusters with down trending volatility. The market will with a high probability reject this price cluster and seek random more stable pricing. These entry price clusters should be as close to predetermined 15% structural stops as possible. These stop levels will then determine a proper and legitimate execution price zone with tolerable risk limits. Only take those trades that have minimum reward to risk criteria in relation to the correct stop.


NDU3 - Nasdaq 100, Sep 03, 10 Min
O= 121700
H= 124700
L= 120900
L= 124600
Δ= +3600
06-16-03
15:10
O= 124400
H= 124700
L= 124400
C= 124600
85
15
3
2
1
15 Retest Holds!
Sell stop
below point 2
Buying imbalance reverses
sellers dominace. Sellers stressed!
124600
124396
123842
123289
123050
122000
121200
121000
120000
Tick Vol
75
50
28
0
ADX
75
48.09
25
MACD
+250
+132.8
0
-250
SStoch
92.5
50
0
12:30
13-08:30
10:30
12:30
16-08:30
10:30
12:30
16-14:30
Tue Jun 17 2003 00:17:01
CQG © 2003

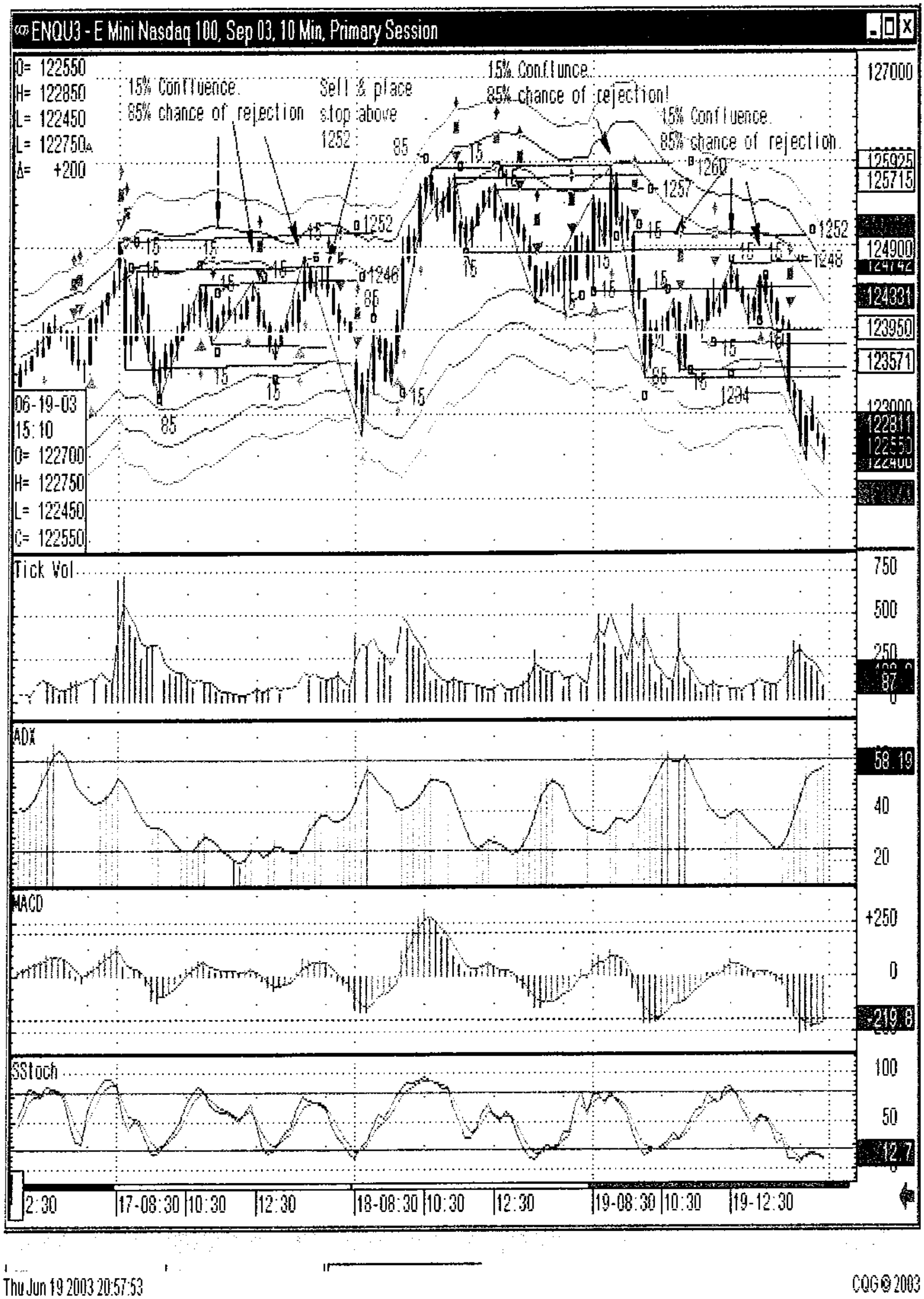

SPM3 - S&P 500-Day Pit, Jun 03, 4 Min
O= 99900
H= 100850
L= 98610
L= 98780
Δ= -290
Stopped out of shorts
Classic retest of 3rd high volume bar following reversal signal
R
1
2
3
06-06-03
15:14
O= 98780
H= 98800
L= 98750
C= 98780
Trailing stops by counting 3 bars back to define macro panic reversal stop price levels
Stopped out of longs get short
Tick Vol
ADX
MACD
SStoch
08:30
09:30
10:02
10:30
11:02
11:30
12:02
12:30
13:02
13:30
14:02
14:30
6-15:02
101000
100500
100000
98000
Mon Jun 09 2003 00:39:10
CQG © 2003

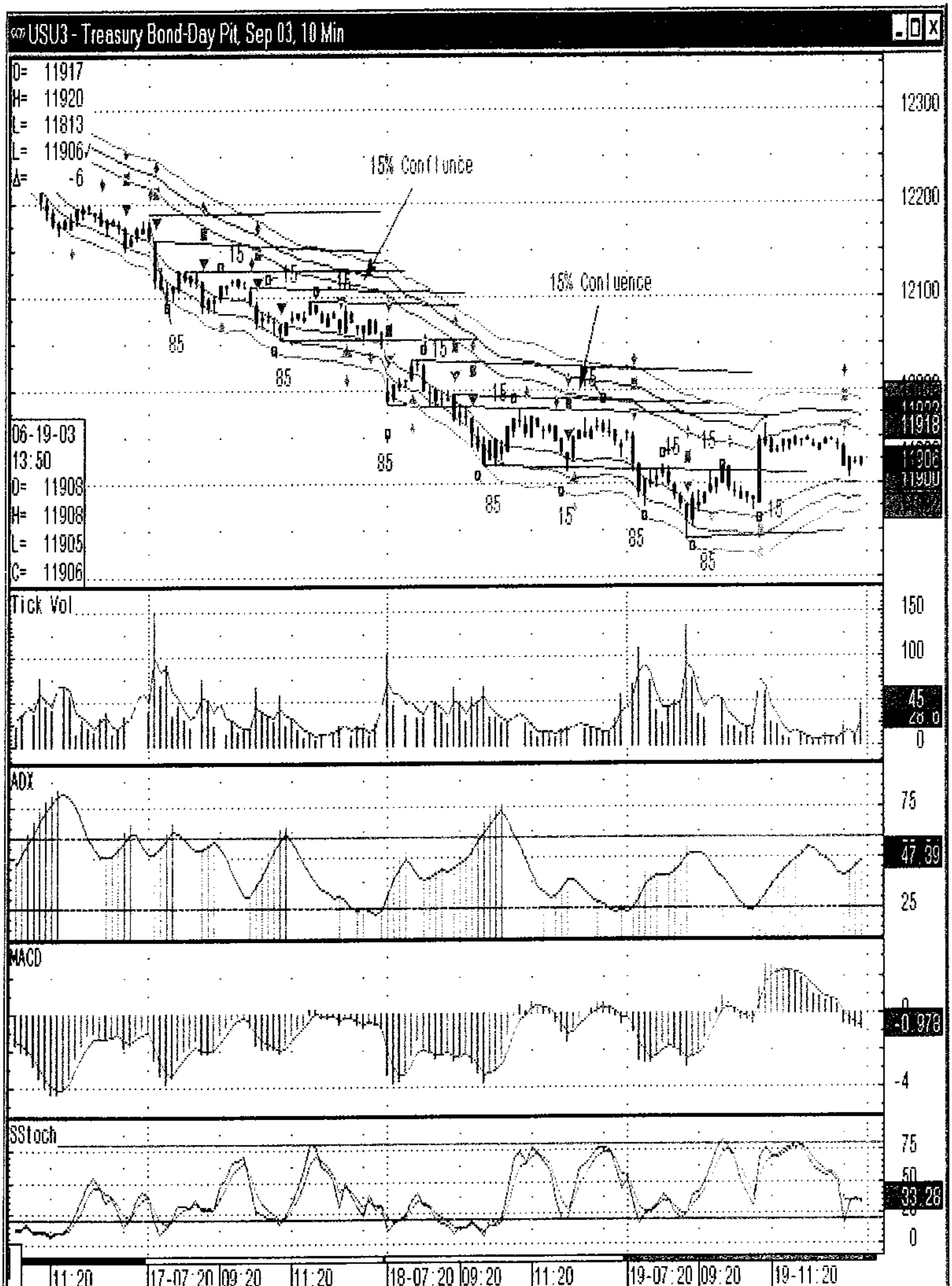
If a trader is going to expend emotional capital on a trading decision it should be on a high quality trade rather than a low probability trade. **Get your price as close to low probability 15% confluence stop levels as possible. Traders need to concentrate first and foremost on entering positions with superior trade location using the correct stop.** Getting better trade location will clearly determine a trader's staying power and mitigate market risk. The most advantageous trade location would be to enter a position on a retest of a prior swing high in a downtrend or against a prior swing low in an uptrend. The goal would be to enter as close to this price level as possible. There is only a 15% probability that a protective stop will be hit outside of this counter trend high or low while there is an 85% probability that price will retest the last trend high or low.



Mon Jun 16 2003 05:16:29

CQG © 2003


ENQU3 - E Mini Nasdaq 100, Sep 03, 10 Min, Primary Session
O= 122550
H= 122850
L= 122450
L= 122750
Δ= +200
15% Confluence.
85% chance of rejection
Sell & place
stop above
1252
15% Confluence.
85% chance of rejection!
15% Confluence.
85% chance of rejection.
06-19-03
15:10
O= 122700
H= 122750
L= 122450
C= 122550
Tick Vol
ADX
MACD
SStoch
17-08:30
18-08:30
19-08:30
19-12:30
Thu Jun 19 2003 20:57:53
CQG © 2003



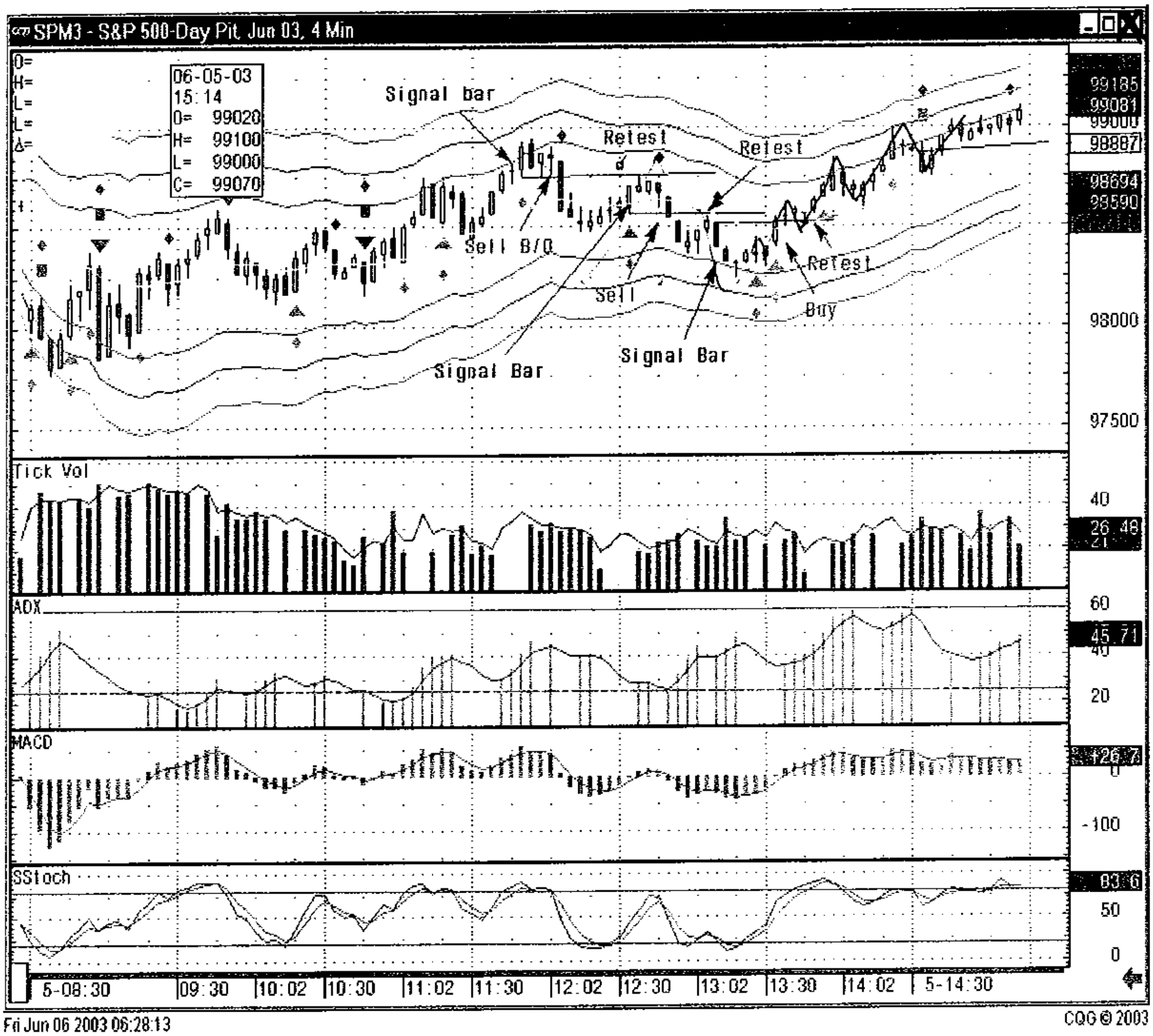
Thu Jun 19 2003 21:23:49

The next best entry technique would be to establish a position on a pullback into the 20 EMA, the 50% retracement level and a symmetrical price cluster. During a strong external momentum trend this will be the most probable entry price level. Risk points are determined by identifying the 15% counter trend swing points and high volume price bar highs and lows through multiple time frames. As noted earlier there is strong rejective market tendencies at or near these price levels. **Therefore legitimate stops must be placed outside of these price levels if a trader is going to avoid being rotated out of a position by random noise. Avoid establishing positions in between 15% rejective price clusters. These are inferior trade setups.**

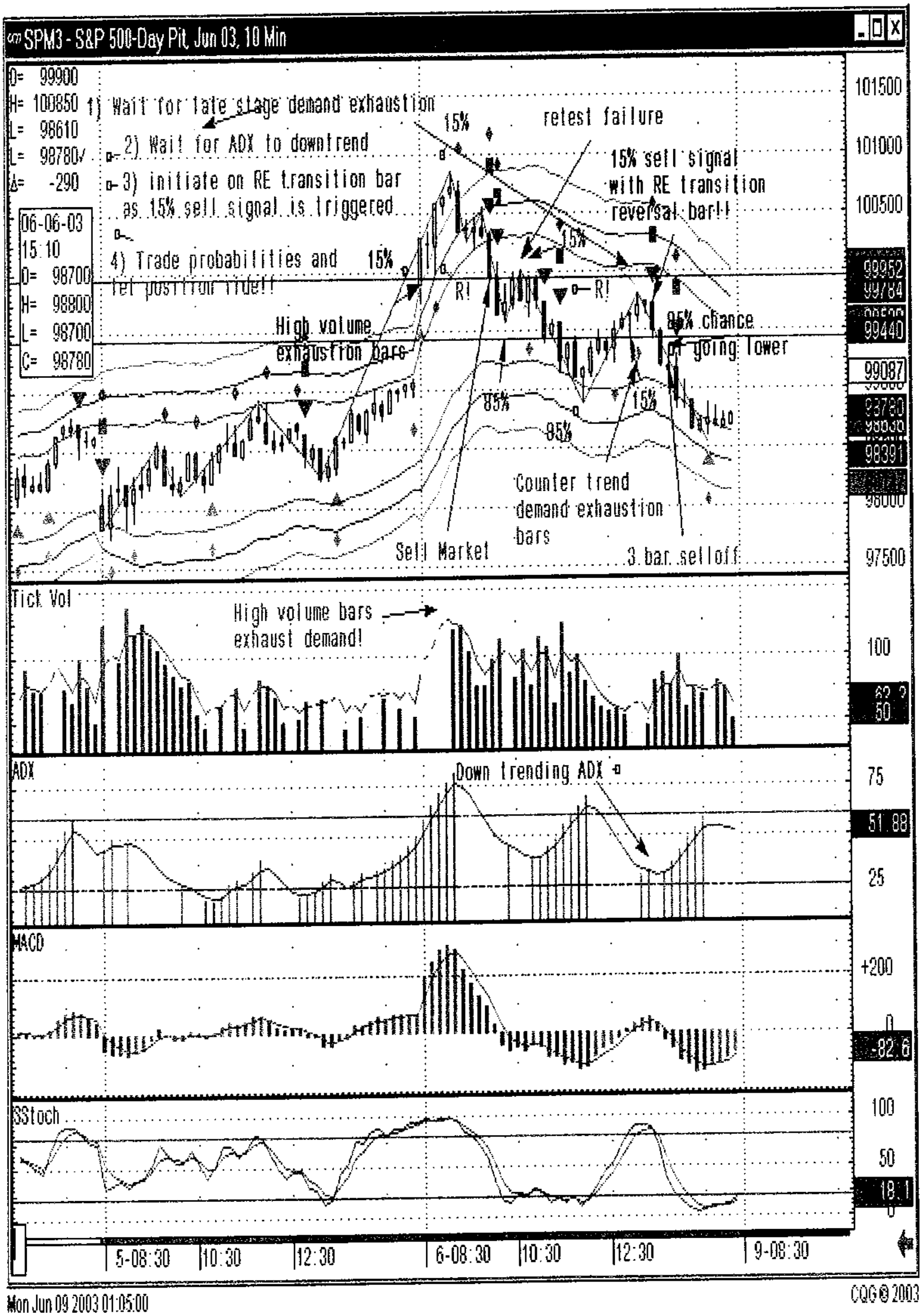
The last and least favorable entry level would be to sell a high volume range expansion thrust through the last swing low in a downtrend or to buy a market on a high volume range expansion thrust through last swing high. Volatility is an important consideration when choosing to take this trade. The higher the ADX reading the greater the snapback risk. Price stops should be placed below the low on upside breakouts or above the high on breakdowns. These trades work best on rule of 4 low volatility breakouts. Most of the time these turn out to be nothing more than low expectation thrust exhaustion setups. The market should go linear immediately upon a breakout or exit position quickly. Unfolding market activity and volatility will differentiate an exhaustion thrust from a valid thrust breakout.

Anytime a thrust bar moves into new high ground or new low ground followed by immediate range and candle body contraction with a failure to move at least one execution time frame ATR market failure is high. Range contraction and candle body contraction will most likely jeopardize this trade setup. This is indicative of exhaustive weak hand activity rather than strong directional activity. Market will most likely rotate against the trader quickly. Open longs or open shorts have very little staying power so be proactive with this strategy. **It is best that a trader decrease the number of these types of expansion trades through highs and lows because this is precisely where most of the weak hands like to establish positions so the failure rate is high.** Weak fearful hands will be rotated out of the market quickly as they buy into resistance and sell into support. If short-term volatility is high (ADX >60) a rotational snapback is very likely.

Once a trader has determined the optimal trade location to establish a position, the next step would be to patiently wait for a counter trend exhaustion thrust excess to shut off a directional up auction into 15% resistance with new sellers or shut off a directional down auction into 15% support with new buyers. ADX should be down trending increasing the probabilities of price rejection. **Panic green up bars into 15% resistance sets up rotational short sales and panic red bars into 15% support sets up rotational buys.** The more violent the corrective process the greater the price vacuum left behind. Let's review how and why this process sets up superior trade locations and discuss how best to exploit these pre- transition dynamics. This will help a trader who is really trying to trade with very tight risk limits.



The closer a market is to exhausting supply or demand in the late stages or a directional auction or multi-thrust momentum campaign the closer the market is to snapping back potentially creating a market imbalance in the opposite direction. **Late stage panic that exhausts supply into support or exhausts demand into resistance precedes supply or demand transition.** Supply/demand transition precedes a rotation in sentiment and a volume transition. A downward auction into support that exhausts supply and finds buyers shutting off further selling provides a pricing anomaly that sets up an upward rotational transition. **Selling exhaustion when combined with a demand surplus allows buyers to easily take control of the market.** An upward price auction that exhausts demand into resistance and finds sellers shutting off further buying provides a pricing anomaly that sets up a downward rotational transition. **Buying exhaustion when combined with a supply surplus allows sellers to easily take control of the market.** The weak hands are always forced out of the market at market extremes. This can reverse prevailing market sentiment. Sentiment transition that is corroborated with a transition in volume can reverse market direction.


SPM3 - S&P 500-Day Pit, Jun 03, 10 Min
O= 99900
H= 100850
L= 98610
L= 98780
Δ= -290
06-06-03
15:10
O= 98700
H= 98800
L= 98700
C= 98780
1) Wait for late stage demand exhaustion
2) Wait for ADX to downtrend
3) initiate on RE transition bar as 15% sell signal is triggered
4) Trade probabilities and let position ride!!
High volume exhaustion bars
15%
retest failure
15% sell signal with RE transition reversal bar!!
RI
85% chance of going lower
85%
95%
Counter trend demand exhaustion bars
Sell Market
3 bar selloff
Tick Vol
High volume bars exhaust demand!
ADX
Down trending ADX
MACD
SStoch
5-08:30
10:30
12:30
6-08:30
9-08:30
Mon Jun 09 2003 01:05:00
CQG © 2003

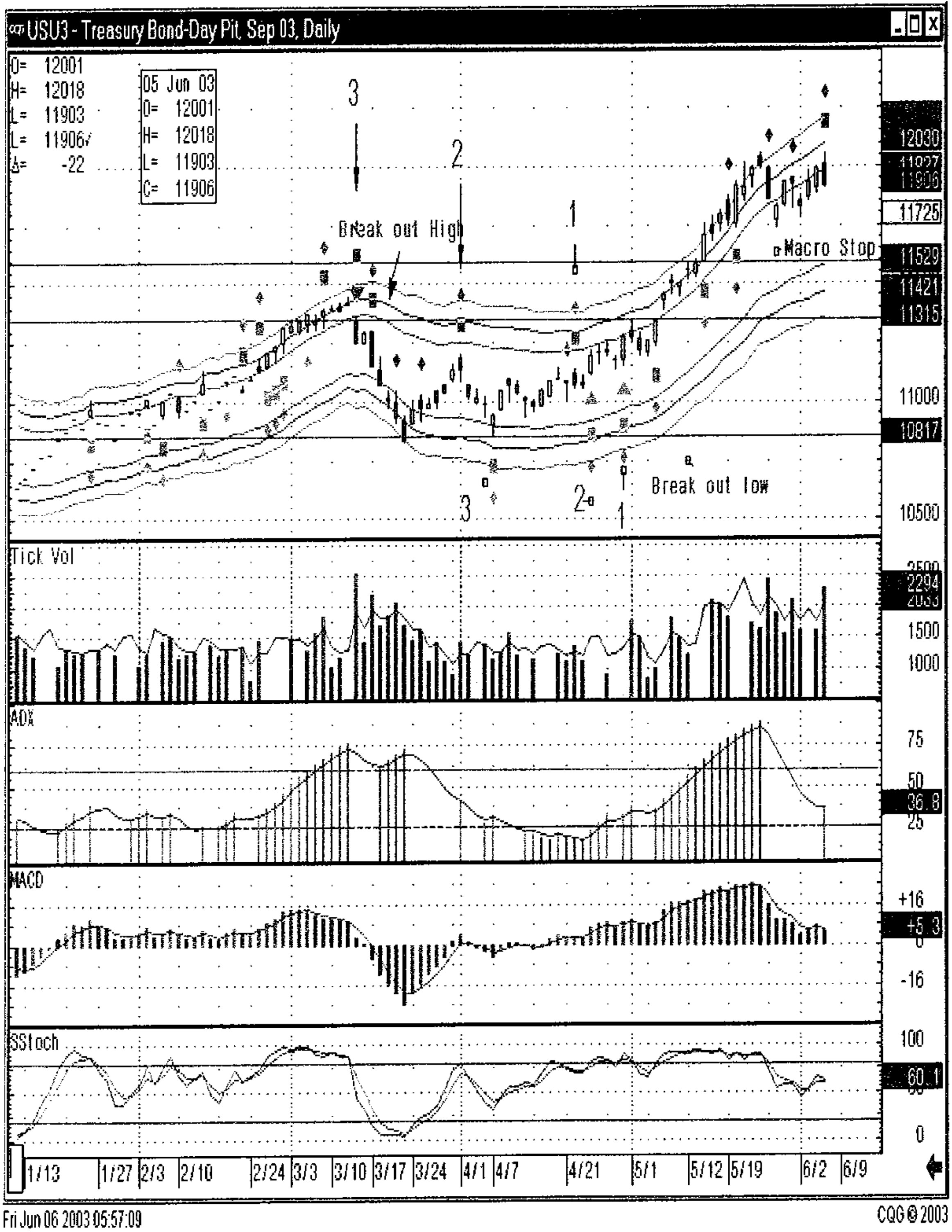
Successful trade execution then boils down to a series of simple steps. Traders must condition themselves to patiently wait for panic exhaustion price bars or high volume ~~price bars~~ to manifest into rejective support or resistance with down trending volatility. These weak hand panic exhaustion price bars precede virtually every price transition. Price transition will reverse a market and define a future risk point. The emotional, under capitalized, risk adverse weak hands are responsible for most of these pre-transition panic bars and will be quickly forced out of the market.

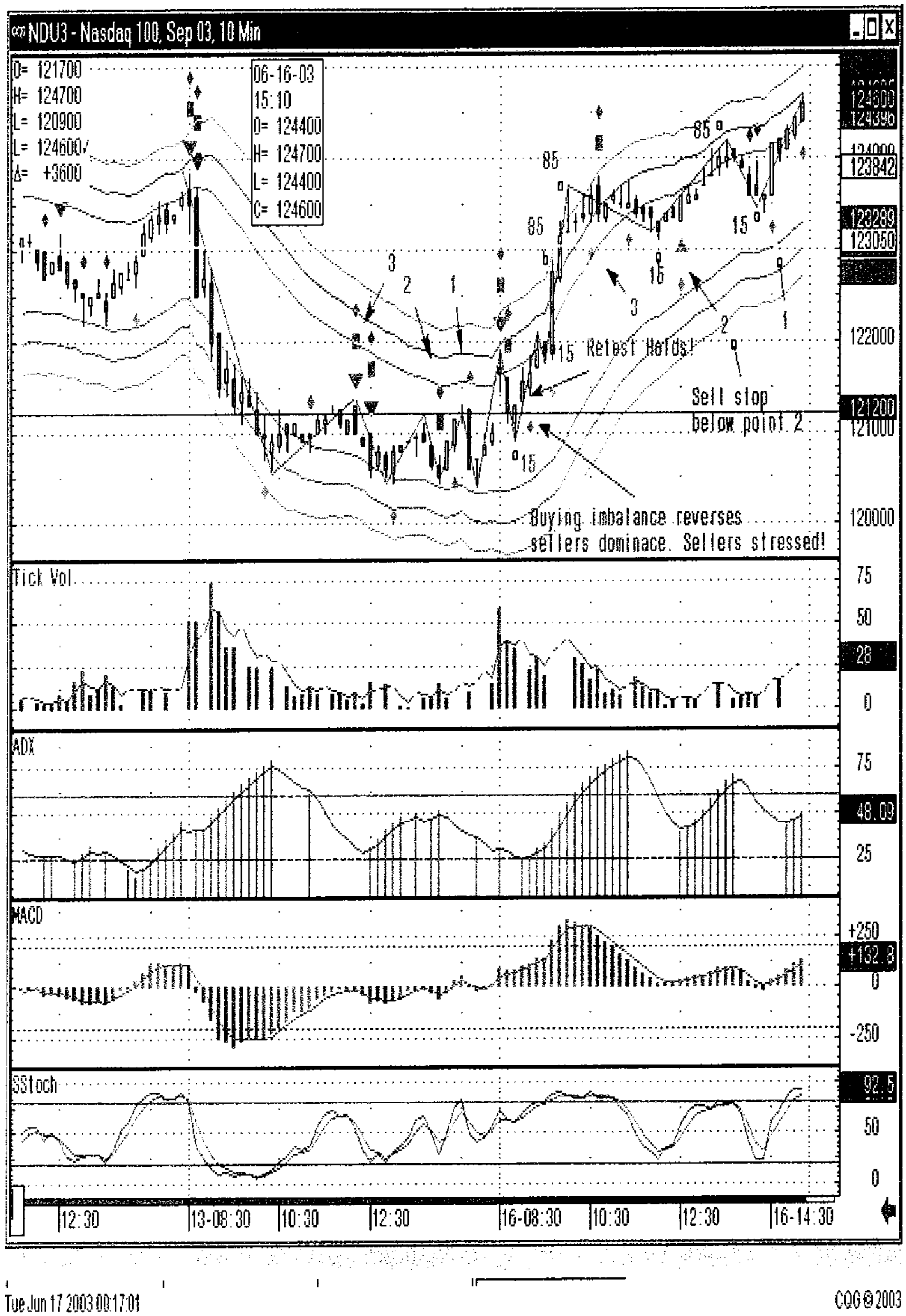
These panic or chump exhaustion bars perpetuate themselves day in and day out at key price levels. Weak hands consistently enter late in a trend and then panic when the market corrects. Weak hands also consistently front run breakouts by buying into resistance or selling into support only to be quickly rotated out of the market on a price reversal. These weak hands have absolutely no staying power so they will be easily stressed and forced out of the market. These panic bars precede market rotation or price transition ultimately providing the fuel for trend continuation.

Corrective panics that fail to reverse a trend provide the fuel that perpetuates a trend. **As stated earlier it is difficult to break capital flows or an existing trend. The very best traders have learned how to exploit panic liquidation rather than fear panic.** They have learned to read prevailing sentiment and have learned to fade the weak hands into high probability 15% rejective price zones by establishing positions with superior trade location.

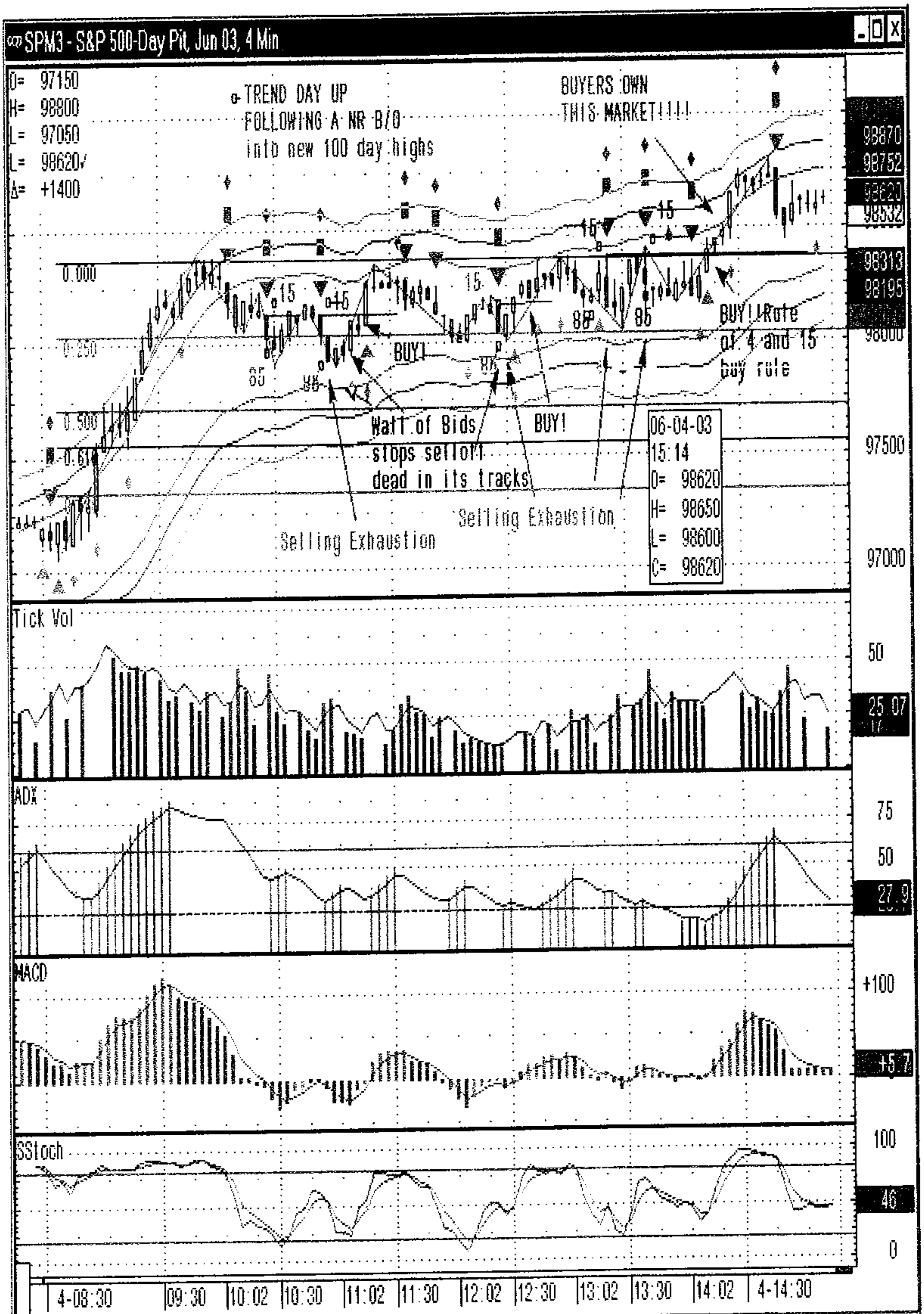
The bottom line, price is always chasing high volume prices. The market will reject low volume exhaustion into support or resistance and rotate back toward the higher volume prices in the direction of the macro capital flows.

Successful trade execution requires the exploitation of panic against those price levels that have a high probability of price rejections. **Protective stops must then be placed outside of these 15% price confluence levels.** Only use those stops that clearly indicate that a shift has taken place in the balance of power. The following charts will better clarify this discussion.

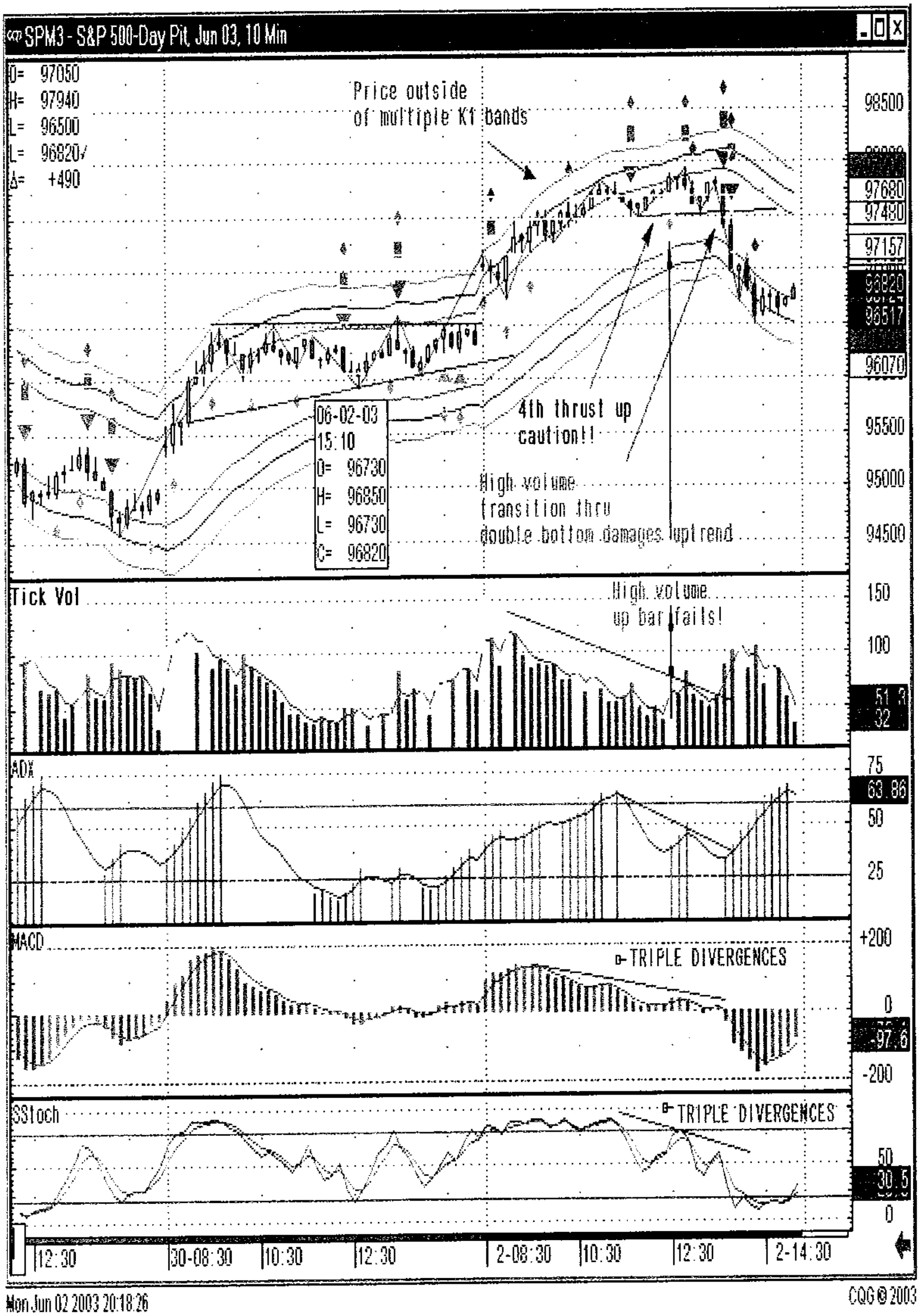

USU3 - Treasury Bond-Day Pit, Sep 03, Daily
O= 12001
H= 12018
L= 11903
L= 11906
Δ= -22
05 Jun 03
O= 12001
H= 12018
L= 11903
C= 11906
Break out High
Macro Stop
Break out low
Tick Vol
ADX
MACD
SStoch
1/13
1/27
2/3
2/10
2/24
3/3
3/10
3/17
3/24
4/1
4/7
4/21
5/1
5/12
5/19
6/2
6/9
12030
11725
11529
11421
11315
11000
10817
10500
2294
1500
1000
75
50
36.8
25
+16
+5.3
-16
100
60.1
0
Fri Jun 06 2003 05:57:09
CQG © 2003



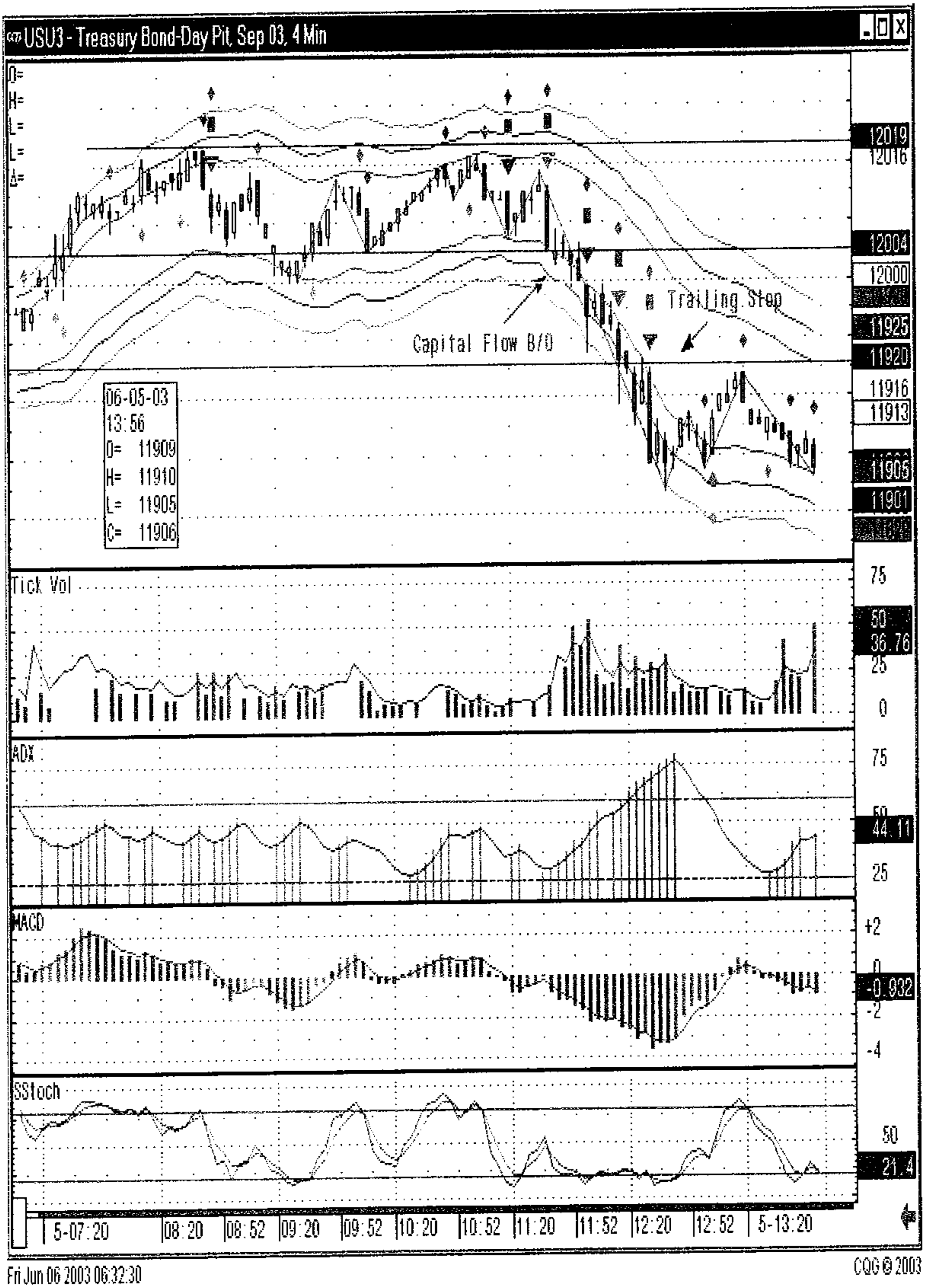
NDU3 - Nasdaq 100, Sep 03, 10 Min
O= 121700
H= 124700
L= 120900
L= 124600
Δ= +3600
06-16-03
15:10
O= 124400
H= 124700
L= 124400
C= 124600
85
15
3
2
1
15 Retest Holds!
Sell stop
below point 2
Buying imbalance reverses
sellers dominace. Sellers stressed!
Tick Vol
ADX
MACD
SStoch
12:30
13-08:30
10:30
16-08:30
16-14:30
123842
123289
123050
122000
121200
121000
120000
Tue Jun 17 2003 00:17:01
CQG©2003

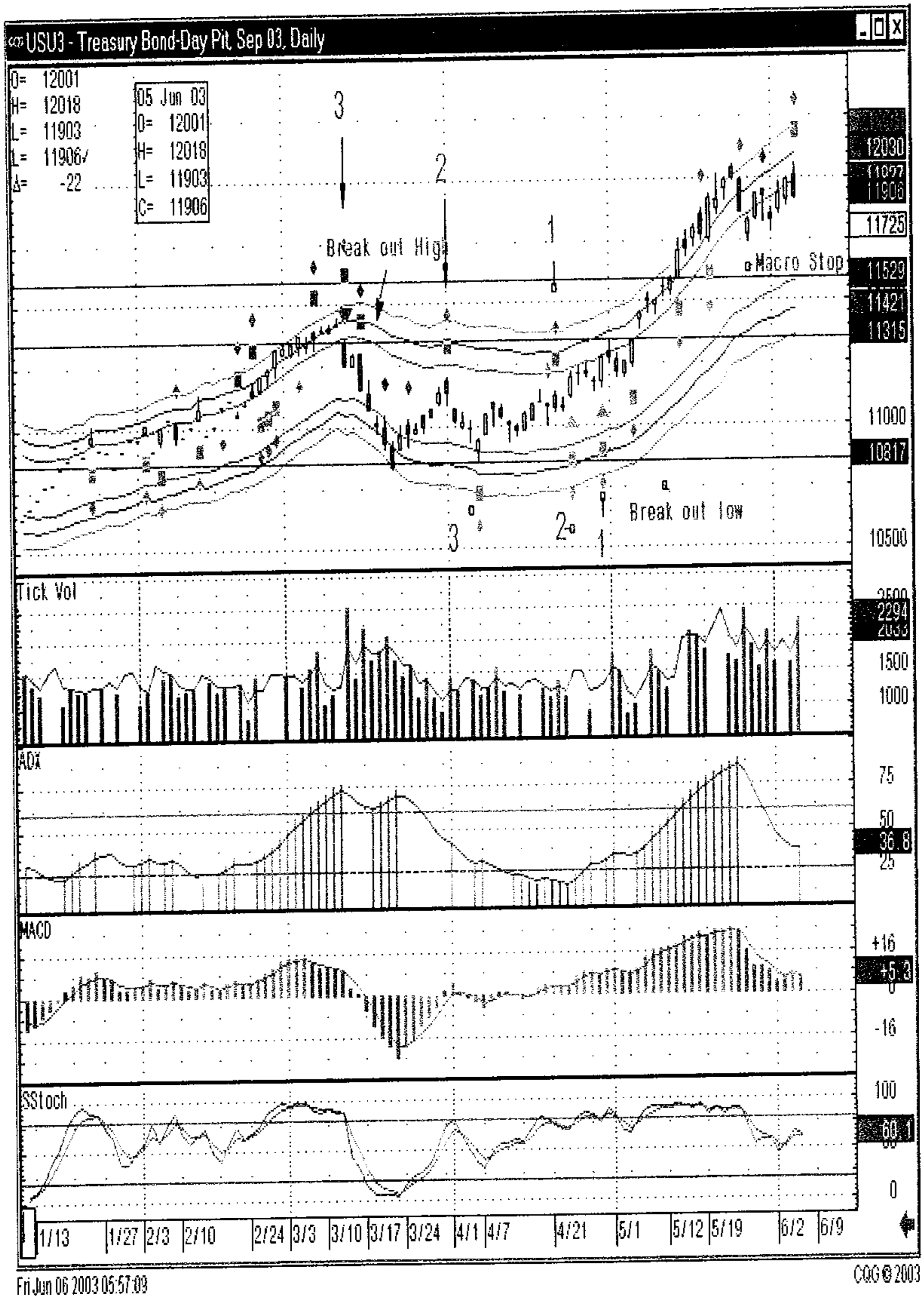


Wed Jun 04 2003 20:41:43 CQG © 2003



SPM3 - S&P 500-Day Pit, Jun 03, 10 Min
O= 97050
H= 97940
L= 96500
L= 96820
Δ= +490
Price outside
of multiple Kt bands
06-02-03
15:10
O= 96730
H= 96850
L= 96730
C= 96820
4th thrust up
caution!!
High volume
transition thru
double bottom damages uptrend
Tick Vol
High volume
up bar fails!
ADX
MACD
TRIPLE DIVERGENCES
SStoch
TRIPLE DIVERGENCES
12:30
30-08:30
10:30
12:30
2-08:30
10:30
12:30
2-14:30
Mon Jun 02 2003 20:18:26
CQG © 2003


USU3 - Treasury Bond-Day Pit, Sep 03, 4 Min
Trailing Stop
Capital Flow B/O
06-05-03
13:56
O= 11909
H= 11910
L= 11905
C= 11906
Tick Vol
ADX
MACD
SStoch
5-07:20
08:20
08:52
09:20
09:52
10:20
10:52
11:20
11:52
12:20
12:52
5-13:20
Fri Jun 06 2003 06:32:30
CQG © 2003


USU3 - Treasury Bond-Day Pit, Sep 03, Daily
O= 12001
H= 12018
L= 11903
L= 11906
Δ= -22
05 Jun 03
O= 12001
H= 12018
L= 11903
C= 11906
Break out High
Break out low
Macro Stop
Tick Vol
ADX
MACD
SStoch
1/13 1/27 2/3 2/10 2/24 3/3 3/10 3/17 3/24 4/1 4/7 4/21 5/1 5/12 5/19 6/2 6/9
Fri Jun 06 2003 05:57:09
CQG © 2003