

Factor Update, May 15, 2016

Administrative note: This Factor Update is being issued early on Friday morning (U.S. time). Friday's price behavior may negate or modify some analysis herein.

The picture to the right is the famous Wawel Castle complex in Krakow, Poland. I will be addressing a group of equity and forex traders in Krakow on Saturday, just down river from Wawel.



Market Review

Candidate Factor Moves are currently ongoing in:

- Platinum
- Nifty 50 (SGX)
- Medtronics (MDT)
- Crude Oil
- Silver
- Japan Mothers Index (proxy is SCJ)

A candidate Factor Move was terminated in the British Pound. Candidate Factor Moves are developing in Cosmo, Eurodollars (interest rate) and U.S. Dollar Index. This issue of the Factor also comments on 10-Yr T-Notes, NOK/SEK, Soybean Meal, Soybeans, Gold and global stock market indexes.

General market commentary

There is almost a completed lack of "late-stage" developing classical chart patterns. I anticipate little trading activity in the near future. In my experience, there are "times to make money and times to keep it." I have a sense that we are entering a "time to keep it."

The focus of my attention

This issue of the Factor Update may contain charts for some markets that are of "charting interest" only and not subject to "trading pursuit." A trader can have all the opinions he or she wants – but what matters are the order that are entered. A trader has NO control over the outcome of a trade. A trader's only control is over the processes of analysis and the subsequent entry of orders. A trader is nothing more than a glorified order enterer. Markets in which I am holding or considering orders include:

Existing positions

- Medtronics – protective stops
- Silver – protective stop and target
- SCJ – protective stop and target
- U.S. Dollar Index – protective stop

New positions

- COPN.S – Entry order with protective stop
- Eurodollars – Entry order with protective stop
- 10-Yr. T-Notes – Price alert
- British Pounds – Price alert

Candidate Factor Moves in Progress

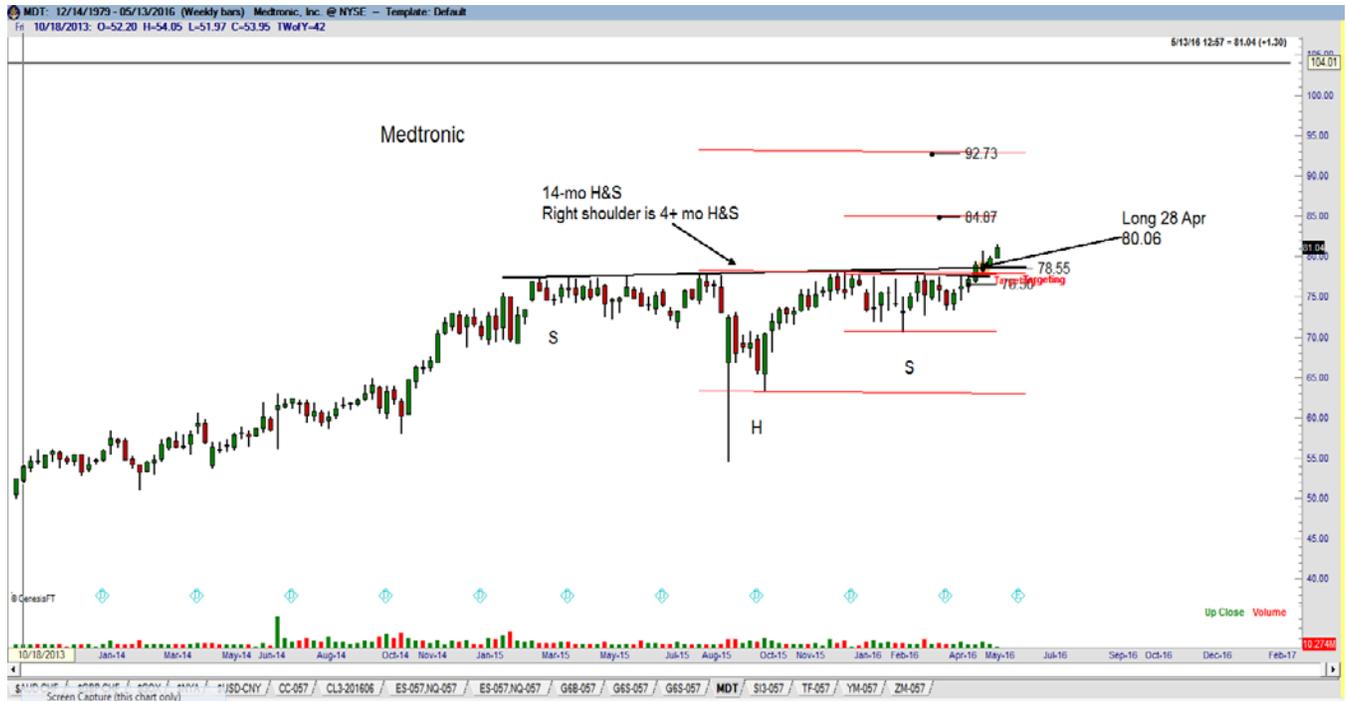
Crude Oil (weekly and daily charts)

WTI continues to grind higher within the boundaries of an advancing channel. The dominant chart construction remains the completed falling wedge on the weekly graph with possible targets ranging from 51.40 to 62.20. I have no position in Crude – and lacking the formation and completion of a recognizable chart configuration I will remain flat.



Medtronics (MDT) – weekly and daily charts

The dominant chart construction in this stock continues to be the completed 14-month continuation H&S formation on the weekly graph, wherein the right shoulder formed an independent H&S pattern. I remain fully long with protective stops split at two levels below the market.



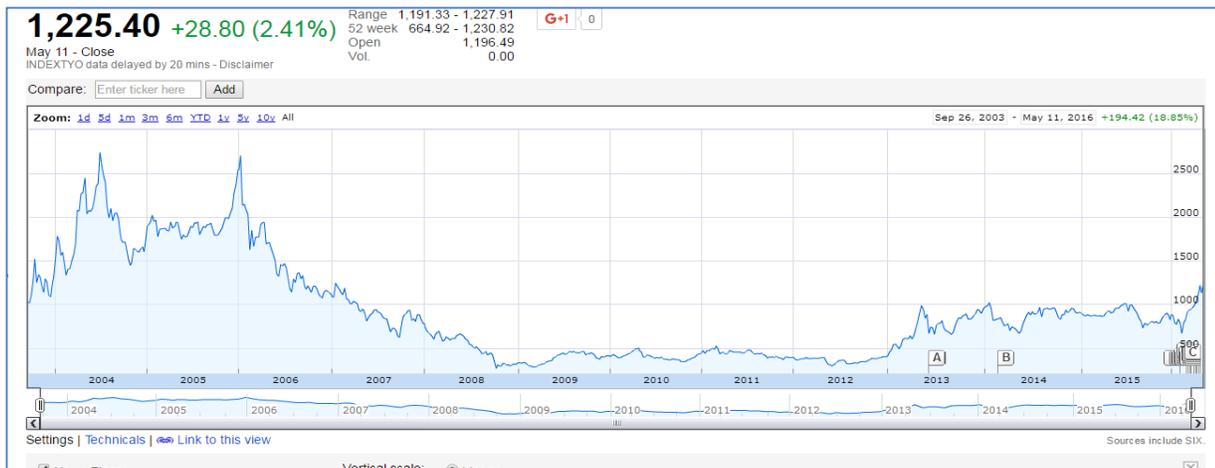
India SGX Nifty 50 (daily chart)

The dominant pattern remains the completed multi-year ascending triangle on the weekly and monthly graphs (not shown). I am monitoring this stock index for another buying opportunity. The WBB advance on Monday was a "sign-of-strength" day (SOS), an indication that last Friday's low will stand as the retest low. I could have used this SOS to establish a long position, but choose not to. During periods of travel I only want to be in extremely liquid markets. If the daily chart forms a continuation pattern I will re-enter the long side of the Nifty.



Japan Mothers Index (proxy is SCJ - iShares MSCI Japan Small Cap Index)

The first chart below shows the Japan Mothers Index (representing growth and emerging stocks) dating back to 2004. The second chart (top of next page) shows that the trading range from 2013 through early 2016 has been decisively completed by advancing prices. The late Apr low is now a very well defined risk level. I am long SCJ (U.S. ETF), a proxy position. I am eager for the Osaka Exchange to introduce a Mothers futures contract.





Platinum (daily chart)

The dominant chart construction remains the completed underlying 9-month H&S bottom pattern. I jammed my stop on 40% of my position based on the 3-day trailing stop rule (3DTSR) even though the markets had not reached 70% of its indicated move. This stop advancement was purely a discretionary over-ride of my trading rules. This stop was activated on May 4. I retain a 60% long position in Platinum. The target remains 1179.



Silver (daily graph)

The dominant chart construction in Silver remains the completed underlying H&S bottom with a target of 1863. For discretionary traders, decision-making is often a “damned if you do, damned if you don’t” process. I chose to jam stops in Platinum based on the 3DTSR even though the market had not reached 70% of the expected advance – and was partially stopped out. Platinum is probably the metal I most want to be long. Silver has reached 70% of its suggested target. While I jammed stops on half of my position (exited on May 2), I retained the other 50% of the long position. I probably should have jettisoned the entire position – but did not. Sometimes a trader’s judgement is correct, sometimes incorrect. Welcome to trading. The daily chart is forming a small H&S top. I remain constructive on Silver prices. The small H&S top pattern, if completed, will most likely morph into a yet-to-be-determined continuation pattern.



Other Markets

Cosmo (COPN.S) – weekly chart

This stock is struggling at the upper boundary of a massive symmetrical triangle pattern. A decisive close above CHF170 is required to complete this pattern and launch the next leg up in this stock. Factor is flat with buy stops above the market. U.S. Interest Rates (Eurodollars and T-Bond daily charts)

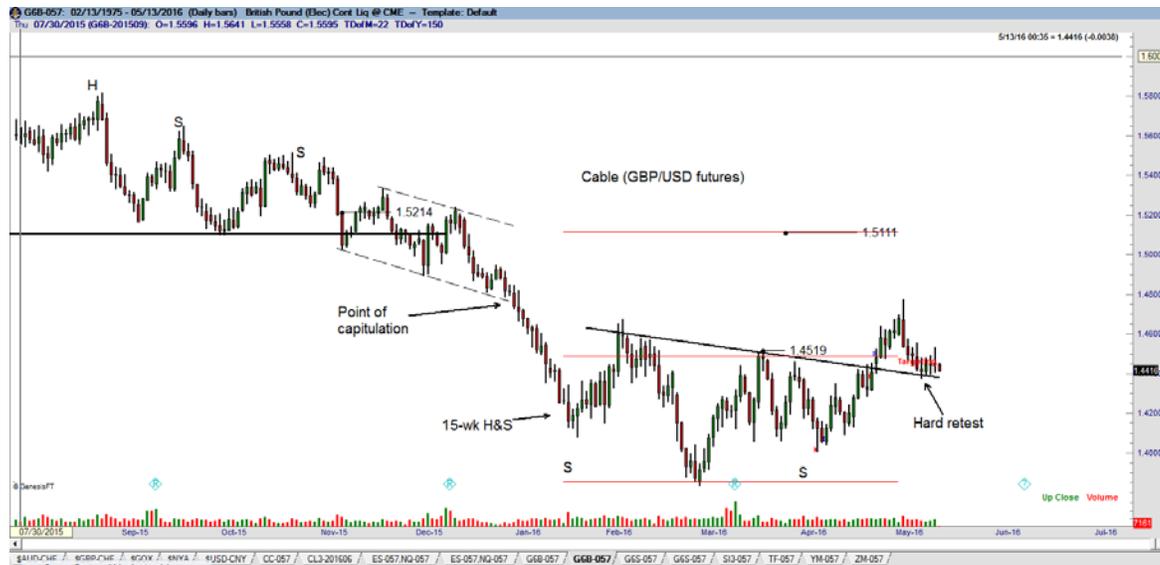


The dominant chart construction on the daily graph in the Dec 2019 contract is a possible continuation H&S pattern. I am willing to buy a breakout and close above 98.58. It should be noted that the target of this trade would only be 40 points (\$1,000 per contract). If the pattern is completed, I will likely purchase three or four contracts per \$100,000 of trading capital. June T-Bonds are forming a 15-week congestion. Using the Feb 11 orthodox high, this pattern appears to be a possible descending triangle with bearish implications. I prefer to ignore the Feb 11 orthodox high and view the congestion as a rectangle. The rectangle pattern can serve either continuation or reversal functions.



British Pound

The dominant daily chart construction in this currency is the H&S bottom completed on Apr 25. I bought this breakout, but jammed my stops – and exited on May 4



and May 6. The market appears to be retesting the neckline of the H&S, but the burden of proof is on the bulls. I am willing to reenter the long side, but only if the daily chart can show an indication of a bottom.

NOK/SEK

The advance in this crossrate on 12 May completed a 4-month ascending triangle – this is a constructive chart pattern. I did not take this signal for a couple of reasons, including:

- Non-USD crossrates have not been kind to me in recent months.
- This cross involves two non-global reserve currencies, thus, a lack of liquidity. I have no desire to be in a trade of two secondary currency units when my phone (text messaging) could be out of cell range.
- The upper boundary of the ascending triangle lacks clarity.



Gold daily chart

Two charts are shown. The first is the daily chart with price and volume. The second chart displays the CFTC COT data as well as price.



From 11 Feb through the present:

- The net long position by the large spec (hedge funds) has grown from 98,400 to 271,600 contracts, a 2.76-fold increase.
- The net short position by commercials has grown from -104,900 contracts to -294,900 contracts, a 2.8-fold increase.
- From the 11 Feb close through the 12 Feb close, price has increased from 1247 to 1265 – a 1.4% advance in price.

Draw your own conclusions from this. I have my own opinion as to what this means. Opinions are cheap – and that includes my opinion. Personally, I think that if price cannot begin to accelerate, the Gold market is in for a time of trouble. Factor is flat. I remain long a 50% position in Silver and Platinum. As I have previously stated, my preference is to be long the strongest members of a group when long – and the strongest precious metals have been Silver and Platinum.



U.S. Dollar Index (monthly and daily charts)

I have held a strong bullish bias in the U.S. Dollar Index since Sep 2014. My opinion has not changed. I view the shake-out decline on 3 May as a bear trap on the daily chart. I went long DX on 6 May. My thinking was that the full green bar above the lower ice-line on 5 May was a confirmation of the bear trap. Is my interpretation correct? Probably not! But the reward to risk profile in being long DX near the lows of this 14-month rectangle are extraordinarily asymmetrical. I love asymmetrical trades whether they end up working or not. The bear-trap low should not be penetrated – otherwise my entire interpretation of the USD is incorrect.



Soybean Meal (daily chart)

Last week's Update identified the period ending Apr 28 as a half-mast flag on the daily chart of Jul Meal. The chart below shows how half-mast targets are established – in this case, 374.4 is the target of the half-mast flag. The advance on Tuesday also completed a flag – although I would not identify this second flag as being half-mast in nature. Factor is long meal from Apr 28 – and I am not willing to let the market retrace much of the current gains before covering the long position. The daily chart of the new crop Nov Soybeans appears to have completed a running wedge. My hunch is that sharp set-backs can be used to establish long leverage.



Factor Member Q&A

Question:

What changes, if any, have you made in your trading since you wrote "Diary of a Professional Commodity Trader?" -Neil Jackson, U.K.

Answer:

Even though I have based my trading on classical charting principles since 1980, the tactical aspects of my trading have evolved over time. There are several areas of my trading today that are modified vs. 2011 – the year "Diary" was published.

Trading frequency – Back in the 1980s and early 1990s I typically made 25 to 30 trades per month. At the time "Diary" was published, my monthly trading frequency had declined to 15 to 20 trades per month. My present goal is to enter no more than 10 trades per month.

Pattern selection – My focus is on horizontal patterns. While I will trade an occasional symmetrical triangle or wedge, these patterns must meet additional criteria.

Pattern duration – At the time of "Diary," I considered patterns of 4 to 10 weeks in length. My focus now is on patterns 10 to 20 weeks in duration. I will trade a smaller pattern if it is part of a larger pattern – either as a launching pad or continuation pattern.

Trade management – I am much less likely to retain my initial stop levels. I make every attempt to as quickly as possible move a trade to a breakeven proposition.

Question:

Have you ever thought about only looking at weekly charts? I guess this could include using a last week rule instead of the last day rule. – J. Sevard, France

Answer:

In all honesty, focusing exclusively on the weekly charts for trade identification, entry and management is superior to the combined use of weekly and daily charts. Because I have a public presence I probably pay closer attention to the markets than I should. I can easily envision myself trading only the weekly charts once I retire from a public presence. Trading only the weekly chart would result in far fewer traders and larger Dollar risks per contract or forex unit. As a result, trading only the weekly charts would require downsizing leverage. My educated guess is that trading only weekly patterns would increase the win rate by 5 to 10 percentage points.

Question:

Do you place stops to enter and protect trades in the night hours? – Frequent question

Answer:

As a rule – NO!!! That band of thieves know as HFTers prowl the night sessions looking to rob traders by running stops that would not usually be threatened during daytime trading. I ran the risk of overnight gaps for more than 30 years prior to the invention of overnight markets. I would rather run the risk of an overnight gap than the risk of being raw meat for the HFT robbers. I will enter overnight stops in the most liquid markets – USD/JPY, EUR/USD, Crude Oil, etc. There was a great example this past week of the "ne'er-do-wells" of the NFTers in Silver. The Tuesday night low in the 5,000 oz. contract was 16.925. The HFTs ran the stops in the 1,000 oz. contract down to 16.60.

Global stock markets

It is with some discomfort that I am always pointing out potential tops in the U.S. stock market indexes. But, I must call them as I read them. The S&P daily chart has made ZERO upward progress in 18 months. A possible complex H&S top formation is under construction. Also note the appearance of a 7-week H&S top pattern. I am willing to short this smaller H&S pattern if given a well-defined risk point. I will give up on a bearish interpretation of the S&Ps if a new high is made – but this does not mean I would have any interest in being long in new high territory. The Nasdaq is tracing out a possible broadening top, although as I have pointed out in recent updates, the rally from the Feb 2016 low has exceeded the normal construction of a true broadening top. Outside of the Nifty (India), the Dow Utilities (dividend play) and the Japan Mothers Index, I have a hard time finding a futures market index I am willing to own.





Be happy you're not in the Mexican-bottled-water pit.



Look, I'd love to open the account for you, but I'm afraid there's no such thing as a market for marijuana futures.

Coming soon to the Colorado Commodity Exchange – A state where there are more marijuana stores than Starbucks and McDonalds combined.

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