The Secret to Day Trading – How to Use Multiple Time Frames for Pinpoint Entry and Exit Points

Now I'm not going to advocate day trading. That isn't what this report is about. But there are some principles used by successful day traders that can help you make better entry points whether you are a long-term investor or are trying to take advantage of short-term (3-8 month long) swings in the market.

The stereotype of a day trader is someone who is sitting in front of their computer all day long and watching his Level II screen for temporary order imbalances to take advantage of. This indeed was what many people attempted to do in the late 1990's, but the change from fractions to decimals by the exchanges on the bid/ask made such tactics almost impossible to succeed with as if they weren't difficult enough already. Most day traders blow up, because as a general rule of thumb the shorter your time frame the more difficult it is to succeed in the financial markets. In fact most who try to trade on a minute by minute basis are pure gamblers handing their money over to the market makers and floor traders.

The successful day traders are few and far between, but all have one thing in common – they analyze the market in multiple time frames to make their entry points. For instance one of the most famous day traders is Marty Schwartz who wrote the book Pit Bull: Lessons from Wall Street's Champion Day Trader. He traded options and futures and in his first year as a trader made $600,000. A year later he made $1.2 million. And these figures were made in the later 1970's and early 1980's when money went further than it does today.

Schwartz made most of his money day trading S&P 500 futures. He would take a position against the market or with it right on the

open and sell out at the end of the day. However, the secret to his trading was that he didn't do this every single day. He would use the trends on the daily chart to look for overbought or oversold conditions and then look at an hourly chart to pinpoint his exit and entry points. He could wait a week or longer for his trade to line up.

What he in effect did was use the daily time frame to determine whether to go long or short in the S&P 500. He would then use the hourly time frame to make the timing on when to actually enter the trade.

Although I didn't explicitly talk about multiple time frames in my lesson about timing the trade when it came to short-term trading I applied the concept. My first step when it comes to short-term trading is to figure out what long-term stage the stock or market you are following is in by looking at the 150 and 200-day moving averages. I then looked at the shorter-term trend to find oversold conditions by using the more short-term oriented daily stochastics indicator.

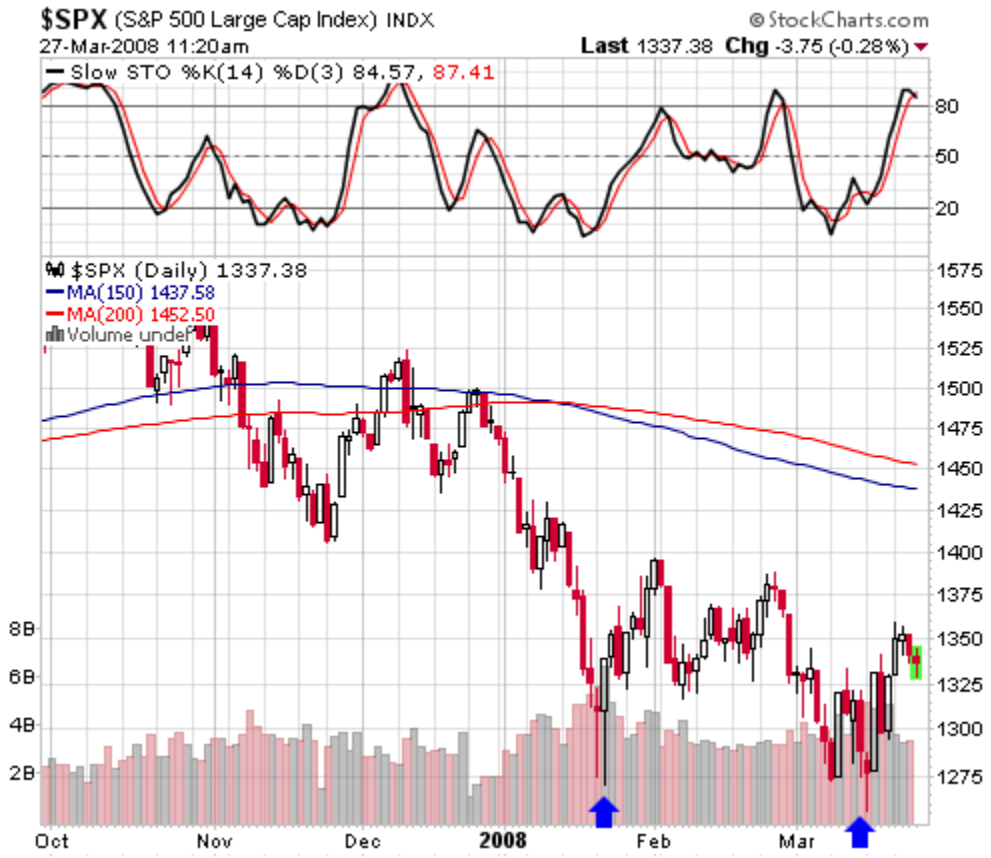
All successful investing and trading uses this concept of multiple time frames. When it comes to day trading, though, many people enter that arena totally unaware of this concept, because they get glued to their screens and obsess over the minute by minute fluctuations. Those few who are successful day trading are because they apply the concept of multiple time frames. This is the secret to day trading.

Anyone can use multiple time frames. An investor can use weekly charts or the long-term moving averages to determine the overall market trend and then daily charts and indicators to make his entry points. A more short-term trader who looks for 2-8 day holding periods can use both of those times frames in addition to an hourly time frame as I'll demonstrate in this report. And a day trader can use 15-minute, 60-minute, and daily charts to make his decisions.

The choice of time frame depends on the individual trader and how long he plans on holding his positions. Ideally he will choose the time frame they like to position in and then watch the time frame above and below that to complement their main time frame. The longest time frame is used to define a trend

and then the smallest time frame to further refine entry and exit points.

Let's look at some examples.

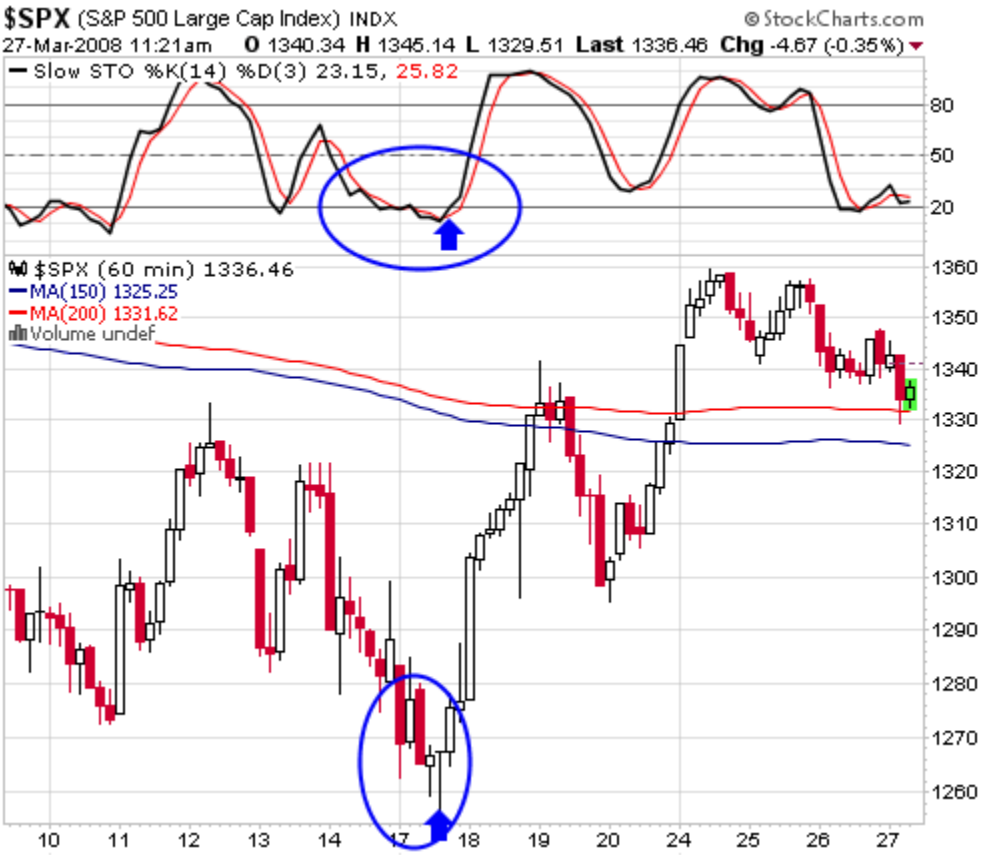


In March of 2008 many people were looking for a stock market bottom to buy back into. The market had been falling since October in a confirmed stage four bear market. Notice how the S&P 500 remained below both the 150 and 200-day moving averages while both of these moving averages were sloping down.

Despite the overall bear trend people tried repeatedly to buy bottoms on days that the market was up or there seemed to be a glimmer of good news or Federal Reserve action that brought hope.

A very short-term oriented trader could use multiple time frames to make an entry point. The S&P had support at the January lows near the 1275 level. At the beginning of March the daily stochastics became oversold. If someone wanted to take a

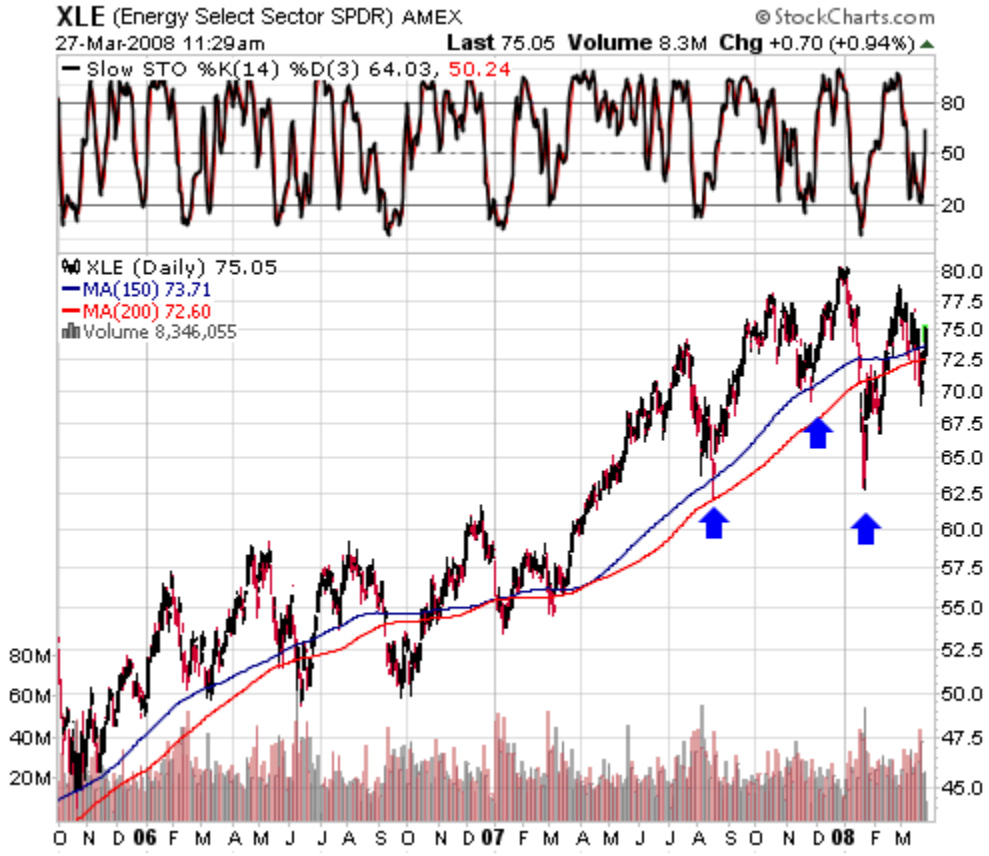
position the thing to do would be to now switch to an hourly chart.



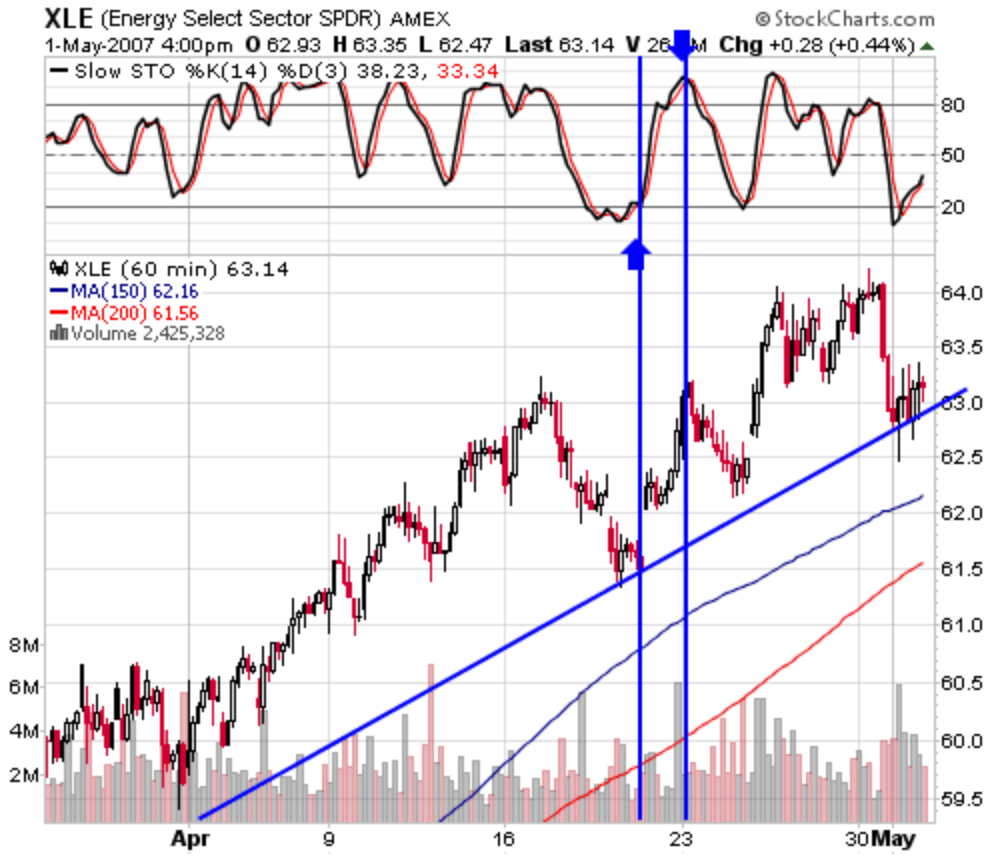
Once the daily stochastics became oversold the hourly stochastics became oversold on March 17 and then crossed up to give a buy signal. At that moment one could have bought an S&P 500 ETF to take advantage of the move.

However, since the market was in a confirmed downtrend I would not advise that most people try this. Only the most disciplined short-term traders should attempt to trade against the overall trend. One would be better to abandon the S&P 500 at that time and look for long entry points in markets that remained bullish at the time.

What I want you to gather from this though is that you can use support levels and oversold readings on a longer time frame and then use a shorter time frame to pick your entry point.



For example in 2007 the daily stochastics for oil stocks became oversold three times. An investor could simply start to buy once this happened, but he could make more exact entry points by using the 60 minute chart to pick his entry points. This is suitable for someone planning to hold for 3-8 months.



For instance if you used the 60 minute chart to find an entry point in the energy spider in April of 2007 when the daily stochastics became oversold while the XLE got near its 150-day and 200-day moving averages you would have had a virtually perfect entry point.

A day trader would have bought then and simply sold a few days later when the stochastics on an hourly chart became overbought and have made two points for a 3% gain. Short-term traders who are looking to hold for several months could have sold when the daily stochastics became overbought six weeks later with the XLE in the mid-70's for a 20% plus gain and long-term traders could have simply used this pullback to position themselves with a profit/loss sell stop placed below the long-term moving averages.

Note though that if one did this you would have probably gotten stopped out at below the price a short-term trader would have sold out. This is often the case when a market or stock is deep in a stage two advance as was the case with energy stocks, which

had been going up since 2003. As a general rule of thumb longer term positions works better at the beginning of a trend while it is more prudent to be more short-term oriented as a trend matures.

I think you understand the basic concepts behind using multiple time frames. Many people jump into day trading without considering anything more than the minute to minute trend and get blasted out of the market. Successful day traders use multiple time frames in their trading strategy. The concept is a cornerstone to making successful entry points in the stock market no matter what your holding period is. To me the two keys to successful positioning in the stock market is to understand the broad trend through stage analysis and then to use a combination of the 150 and 200-day moving averages as long-term support areas and oversold conditions to time entry points in a stage two advance.

Different trading tactics and holding periods are suitable for different stages of the market. For instance the identification of buy points when a market is transitioning from stage one to stage two is different from when the market is in a stage two advance, in which the usage of multiple time frames becomes key.

At the same time one should never try to buy when a stock or market is in a full blown stage four decline. I've provided one example of this in this report, but insisted that such buying attempts are suitable only for people equipped to do day trading.

Most people lose money in the stock market and they do so, because they hold during stage four declines or try to guess bottoms all of the way down. People think because a stock is falling it is cheap and that it will go back up. But the problem is during a stage four decline you don't know where the bottom is and can get wiped out if you try to hold all of the way down, because you refuse to admit a mistake. Only traders can even attempt to buy and investors need to wait until the end of stage one to take their positions. Unfortunately few know to do this. You have become one of the few who do.

There is money that can be made during stage four bear markets, but it is made by betting against the market. In a future

lesson I'll apply the techniques of using multiple time frames to bet against the market or individual stocks during stage four declines. In fact I have found that using multiple time frames is even more important when doing this then ever before.

There are two main ways you can bet against the market or a stock. First you can buy many of the reverse-ETF's on the market that are designed to rise when the market drops. You can trade them just like a stock, but they go up when the index they are linked to drops. For instance the SDS ETF is designed to go up at twice the rate that the market drops, but if the market goes up it will fall at twice the pace the market rises.

The second way is to sell short stocks. When you make a short sell you borrow the shares from your broker and sell them on the market. You then repurchase the shares back – called buying to cover the short sale - from the market at a future date and return them. If you repurchase them at a lower price than what you short sold them at then you will make a profit, but if you cover your short position at a higher price than what you sold it at you will take a loss.

It isn't as complicated as it sounds. You just put in a sell short order with your broker and they take care of everything for you. The stock shares come from another one of your broker's customers or from another brokerage. The shares are sold and the proceeds are credited to your account. Most of the time you can hold the shares for as long as you want, but you can be forced to cover the position if the broker needs the shares back if many of its customers who have the stock start to sell. Since you are being loaned the shares you are buying on margin and need a margin account to short sale.

Just think of it as selling first and then buying later instead of buying first and then selling. Your objective is to make money when the stock drops instead of when it goes up.

In the next lesson I will explain short selling strategies and tactics I use to profit during stage four bear declines. Even if you aren't interested in short selling you should watch this next lesson, because in it I will bring together many of the principles explained in this report and earlier ones with more concrete examples to help you build on your learning.