OPTIONS MADE SIMPLE

Sang Lucci's Approach To Options Trading

by Sang Lucci

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Learn more information at www.sanglucci.com

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INTRODUCTION

I'm Sang Lucci. I'm an avid stock market trader who specializes in high-risk, high profitability options trades. My strategy combines market timing and simple options plays to capitalize on short-term moves. These short-term moves could be anywhere from a couple of seconds to a couple of a months.

I started my career as a Financial Analyst; a career I soon felt unsuited for. So I decided to take the plunge into the markets and come up with a way to avoid the nine-to-five lifestyle. I traded stocks for two years at a proprietary trading firm - barely making a dime - all the while learning what strategy suited me best: swing trading. I made some good money at the prop firm but I was never allowed to take any huge positions, which totally hindered my profits. So, I decided to go at it on my own with my own money. I remember a fellow trader begging me to try options and once I saw that you can double your money in less than a day, I was hooked! I soon took about $50,000 I had made from the prop firm and a ticket brokerage firm I started years prior, and quickly flipped it to almost $2 million. I even posted all my trades for the public to see.

This book is a collection of some of the early articles form my website, Sanglucci.com, to help you get started with trading options. Many new visitors to my website and traders interested in my classes have asked for a quick guide that they can read at their leisure to help them get caught up before diving into the options world.

I hope this book does just that. Whether you're an experienced trader or one who has NO clue about anything stock market related, you can benefit from this book.

Enjoy.

MY TRADING STYLE

My trading style involves combining the lost art of “Tape Reading” and market timing with basic options strategies.

Tape Reading is a method much less used today than in previous years. It has been replaced by modern day technical analysis which involves advanced charting tools, widely adopted chart patterns, complex technical indicators and of course indicators of the indicators that indicate what the indications are.

Simplicity is at the forefront of my trading style and any strategy that attempts to complicate that simplicity gets thrown out the window. A Level II, a time and sales, and a simple chart are the only tools that I need in order to make profitable trades.

There is, of course, a method to my madness.

Tape reading, in it’s most basic form, is the practice of analyzing the price and volume of a particular stock in order to assess short-term action. Traders who use this technique assess the size of stock orders, order speed, order price, and order condition (at ask, at bid, between ask and bid) for the purposes of identifying trends in trading behavior by insiders, professionals and the general public. These trends help a trader recognize good times to buy or sell a particular equity. I learned this supposedly lost art at a proprietary trading firm where I worked for close to three years. Most prop firms promote scalp trading and actively teach their new trainees this method simply because it generates the highest dollar amount of commissions for the firm. The ability to tape read is necessary to profitable scalp trading but it can be used for far greater purposes.

Price action is and will always be king. Being able to pick up on the actions of a large buyer or seller can result in substantial profits. In reality, all forms of technical analysis generally come to the same conclusion as the next but picking up on a pattern in the tape will alert you to possible trades long before any chart or technical pattern will. The hybrid market, however, has changed tape reading drastically. Previously, large bids and offers were actually REAL. Nowadays, because of high frequency trading systems and lightning fast executions, many are able to place “fake” orders, which add to the manipulation of many stocks. This leaves the retail trader at even more of a disadvantage. A good tape reader, however, can decipher what is real and what is fake.

Now, instead of taking a position in the actual equities, I seek to make trades in the options.

Why the options?

Options in high-volume equities have larger percentage moves. The volume in these specific equity options also allows a trader to commit the same amount of capital as he/she would in the stock. This, of course, increases risk considerably but, as a result, increases a trader’s profit/loss potential ten-fold.

MY APPROACH

Learning how to trade the stock market is by no means an easy task. The problem with becoming a profitable trader is that it requires effort, persistence and patience. Most people who attempt this game have none of these qualities. The information age we live in has allowed for EXCESSIVE resources to "help" people learn whatever it is they desire to. Unfortunately, the over-saturation of information has caused a lot of confusion. This theory holds true in Finance, Economics, Politics, and just about every other industry.

Competition to earn the attention from readers who seek that information is now at an all time high. This leads to sales gimmicks, get rich quick schemes, pyramid schemes and an overall lack of honesty. Most products and services sold by anyone in the Finance industry are sub-standard at best.

The concept is simple. Pitch someone the dream of getting rich and that dream all of a sudden holds an inherent value. People will pay big money, even put themselves into debt, if they believe they can change their lives for the better. It's become the foremost practice in the Finance world to sell you the information and to sell you that dream.

Now, with so much competing information, anyone looking to enter the industry finds it difficult to figure out how. That, usually, is enough to turn most new participants away. The ones who do end up sticking around seem to be seeking out that "golden nugget" or guru who is going to lead them to profitability.

This brings us to Sang Lucci's approach to education in the stock market:

The only way to learn is to get in that ass!

The fact of the matter is, unless you put things into practice for yourself and become an independent trader you will never become profitable. Sure you may have some profitable trades here and there but your discipline will lack and that will get you into a lot of trouble.

This game is 90% mental. It's all about managing your losers. Anybody can pick winners, but do they actually book those winners and do they manage their losses? Most do not.

Traders often times are so bombarded with ideas that they lose focus and try to make use of every single one. This of course leads straight to disaster.

The stock market is unforgiving and doesn't care about you or your ideas. Learn the basics and adapt/create your own advanced concepts.

Seek knowledge and information but do not live by it. Craft and mold that information into something you yourself can understand and manage.

Becoming a profitable trader is as much about finding yourself as it is about learning the mechanics. This is why many times it's better to learn about the psychology of trading before trading itself.

WTF IS AN OPTION?

OPTIONS BASICS

Taking it back to basics!

I actually did a Google search to find out how others explain what an option actually is and found the same ol' complicated rhetoric:

An equity option is a contract which conveys to its holder the right, but not the obligation, to buy (in the case of a call) or sell (in the case of a put) shares of the underlying security at a specified price (the strike price) on or before a given date (expiration day). After this given date, the option ceases to exist. The seller of an option is, in turn, obligated to sell (in the case of a call) or buy (in the case of a put) the shares to (or from) the buyer of the option at the specified price upon the buyer's request.

To tell you the truth, I don't even understand this shit. Who can??? Lucci is here to simplify the situation and assign his own definitions.

So WTF is an option?

First let me paint a little picture in your heads so you can get the juices flowing. (This is an embellishment of an example I stole from Investopedia.)

Let's say you want to buy a house and it costs $200 G-packs (G pack = $1,000 in Lucci's world). So $200,000. You don't have the money to buy the house right now but you know you are going to have it in three months. So the owner gives you an option to buy the house within three months FOR $200 G-packs. The price of this option though is $3,000, non-refundable. So you give the dude $3,000.

Now in two weeks, somebody finds out that freaking Michael Jackson lived in that house. The appraiser says hell no this house is worth a million bucks!

Now, you have an option to buy that house now for $200,000 OR you can sell that option to someone else for just as much. Remember, the owner of that house is OBLIGATED to sell you the Michael Jackson Moonwalk house for $200,000. So you basically made an $800,000 profit if you end up buying the house.

Here's the flip side: let's say after further inspection of that house, you find it to be in need of serious maintenance. You've bought an option for $3,000 but that doesn't mean you are obligated to buy the house! You walk away with just the $3,000 loss.

Now let's tie this into equity options. If you bought the house in the previous example, you've exercised your option by buying the underlying security (house). If you decided to let the house go, then you let your option expire worthless and did not exercise your right to buy the crib, thus, taking your $3,000 loss.

You dig?

The stock market is a messed up place. It's a place where new derivatives (financial investment vehicles) are created everyday. The exchanges, banks, and other large organizations create these derivatives to further juice commissions and money out of the herb investors (a.k.a. me and you). Swaps, futures, options…these are all instruments to "help" an investor stay more flexible in today's rapidly fluctuating markets. In reality, they can be just another novel way of luring uneducated investors into the markets to trade securities they don't *really* understand.

Having said that, options have been around for hundreds of years, often to help businesses hedge their risk. Farmers may have bought contracts to make sure within a specified amount of time they could lock in the price of whatever they were selling or buying. Derivatives are used by corporations to combat future interest price fluctuations; let's say a company borrows a crapload of money but they're afraid that interest rates will go up after a period of six months. They can buy a forward rate derivative, which locks in the interest rate so the bank takes the hit if the interest rates rise.

At the end of the day, for properly educated investors that don't have businesses requiring the use of such derivatives, options are just a means of either making money (like a stock) or protecting the downside risk in your portfolios.

CALL OPTIONS

Most every stock in the market is "optionable", which means you can buy and sell options based on that particular stock.

Every option has a specified strike price and an expiration date. I'd rather use pictures to teach you newbies this instead of bogging you down with financial terminology and definitions, which you may or may not understand. Regular taxonomy on options is sometimes convoluted and can be extremely confusing at times.

Let's get into it!

In order to understand what a call option is you must first look at an equity that you want to buy an option on. So let's just rock with Bank of America (BAC) for this post.

We'll be using this chart periodically through this example.

Now, for most options, the strike prices will start at the whole numbers. So, for this particular stock you'll get a $13 call, $14, $15 and etc. A call option generally goes UP in value as your stock moves higher. Now, I say generally because there are times where that actually will not happen. I'll explain those examples in further detail after getting through the basics.

Call Options						Expire at close Friday, January 21, 2011	
Strike	Symbol	Last	Chg	Bid	Ask	Vol	Open Int
2.50	BAC110122C00002500	11.75	+0.14	11.70	11.80	6	4,196
2.50	BAC1110122C00002500	8.75	0.00	9.65	9.90	40	6,231
5.00	BAC110122C00005000	9.00	−0.61	9.20	9.30	21	35,590
5.00	BAC1110122C00005000	7.40	0.00	7.15	7.40	5	729
6.00	BAC110122C00006000	8.43	0.00	8.20	8.30	5	205
7.50	BAC110122C00007500	6.65	−0.35	6.70	6.80	116	49,038
7.50	BAC1110122C00007500	5.00	0.00	4.70	4.80	13	767
9.00	BAC110122C00009000	5.25	−0.15	5.20	5.30	177	4,570
10.00	BAC110122C00010000	4.25	−0.20	4.25	4.30	1,840	65,577
10.00	BAC1110122C00010000	2.07	−0.09	2.24	2.29	3	2,290
11.00	BAC110122C00011000	3.28	−0.12	3.25	3.30	3,045	93,895
12.50	BAC110122C00012500	1.82	−0.13	1.78	1.81	58,641	369,043
12.50	BAC1110122C00012500	0.19	−0.12	0.23	0.25	174	26,022
14.00	BAC110122C00014000	0.54	−0.11	0.54	0.55	116,896	270,242
15.00	BAC110122C00015000	0.16	−0.04	0.14	0.16	66,245	345,805
15.00	BAC1110122C00015000	0.02	0.00	N/A	0.02	150	16,163
16.00	BAC110122C00016000	0.04	−0.01	0.03	0.04	23,841	142,517
17.50	BAC110122C00017500	0.01	0.00	N/A	0.01	542	356,131
17.50	BAC1110122C00017500	0.01	0.00	N/A	0.01	20	6,288
19.00	BAC110122C00019000	0.01	0.00	N/A	0.01	10	93,750
20.00	BAC110122C00020000	0.01	0.00	N/A	0.01	8	444,918
20.00	BAC1110122C00020000	0.01	0.00	N/A	0.01	386	10,151
22.50	BAC110122C00022500	0.01	0.00	N/A	0.01	25	121,768
22.50	BAC1110122C00022500	0.01	0.00	N/A	0.01	0	2,819
25.00	BAC110122C00025000	0.01	0.00	N/A	0.01	1	217,186
25.00	BAC1110122C00025000	0.01	0.00	N/A	0.01	20	2,744
30.00	BAC110122C00030000	0.01	0.00	N/A	0.01	4	258,657
30.00	BAC1110122C00030000	0.05	0.00	N/A	0.07	30	3,025
35.00	BAC110122C00035000	0.01	0.00	N/A	0.01	0	30,608
35.00	BAC1110122C00035000	0.04	0.00	N/A	0.01	0	1,758
40.00	BAC110122C00040000	0.01	0.00	N/A	0.01	2	45,002
40.00	BAC1110122C00040000	0.03	0.00	N/A	0.07	0	639
45.00	BAC110122C00045000	0.01	0.00	N/A	0.01	0	8,557
45.00	BAC1110122C00045000	0.01	0.00	N/A	0.07	0	168
50.00	BAC110122C00050000	0.01	0.00	N/A	0.01	1	6,321

Here is an option chain for BAC January expiration. Every stock has an option chain. We call it a “chain” because it basically gives us the information for all possible options of the stock for a specific expiration date.

Looks confusing as hell I know, but with a few details and some repetition, you’ll be reading these chains like a superstar in no time.

The first column is the “Strike Price”. Think of the Strike Price in terms of where you think the stock will go. So, for example, if I think BAC will rip to $16 next week, then I’d want to buy the $15 or $16 strike.

The “Last” column shows the last transaction that went off in the option and the “Chg” column shows the change in price during the market that day. The “Bid” and “Ask” columns show where the best bid and offers are for the option (Bid and Ask is something I’ll explain in further detail in future education posts). The “Vol” shows the volume, which means the number of contracts that were traded that day. The “Open Int” is the Open Interest, which is the total number of contracts that people are still holding on to.

One last thing to remember is the Expiration Date.

All monthly options expire on the third Friday of the month, NO EXCEPTIONS!

Now, a simple way to understand the pricing of Call options is to ask yourself, “How likely is it that an increase in the stock price will occur by the expiration date?”

Take a look at the BAC chart and you can see that stock is currently (as of January 8th, 2011) at about $14.25. January expiration is on the 21st so let’s take a look back at the chain and find the $16 strike price. You can see that option is trading at $0.04.

Why so low? Because the likelihood of this shit happening is extremely low. Therefore, people are not willing to pay up for the right to buy the stock at $16, so it’s trading pennies right now. If the stock were to, say, hit $15 on Monday, then there would be some renewed interest in this option and people would maybe pay up to $0.10 for it.

The important concept here is will said event happen BEFORE the expiration date. If you buy into the $16 Call and BAC is trading at $15.99 by the end of trading Friday, January 21st, your option is worth ZERO dollars.

Let’s do one more example.

The $16 Call is what we call “out of the money” because the stock is below that strike price. Let’s take a look at an “in the money” option like the $14 Call. Now the $14 call you can see is trading at $0.54. Key thing to notice here is how much MORE the option price is above the current value of the stock. If you take the option price and add it to the strike price ($0.54 + $14.00) you find out how much premium they’ve still tacked on to the option. So $14.54 is how much over the current stock price of $14.25? That’s $.29, and that’s how much premium is still in this option. I read this pricing as saying, “People are still assuming this stock could go higher to about $14.54”.

As the value of the stock goes up or down, so does the price of this option. People are constantly re-assessing their position and valuing their option as they go along according to what the stock is doing. So, on Monday, if the stock tanks to below $14.00 then you'll see almost ALL the premium go away in this option. The LESS time that's left before expiration the QUICKER you lose premium in your option. So if it's at the beginning of the month, your premiums on monthly options will stay high.

Let's say for example tomorrow is expiration day. How much do you think this $14 Call would be worth assuming the stock was currently trading at $14.25?

That's right folks! Exactly $0.25! Why is that? That's because there's no premium left in the option. Time is up! These options expire tomorrow soooooo the option directly correlates with the stock price.

You dig?

PUT OPTIONS

Calls, in basic strategies, are used to capitalize on the upside movement in a stock. Puts aim to capitalize on the downside movement.

Same deal here with the Put options; they all have a specified 'strike' price and an expiration date.

I'm going to again use pictures and charts to explain how to use these things instead of hitting you up with definitions and more shit that you won't understand. In the previous section with the Call options we used Bank of America (BAC) as a stock that we want to view the options on so we'll stick with that. Again, most U.S. equities are "optionable" and have an option chain containing both Calls and Puts.

So let's get right into it! Why would you buy a Put option? Look at it as an inverse to the Call option. If you think a stock is going to go down in the near future then you may want to buy a Put to capitalize on that movement. Another popular use of Put options is for getting "protection."

Protection? Protection from whom? The stock bandits?

Nah reeeellllaaax. Let's say you have twenty stocks in your portfolio and you really want to hold on to them for longer but you feel the market has gone up too far too fast. Instead of selling your stocks to lock in whatever profit you've accumulated, you can buy some Put options to offset the losses you think you'll take once the market pulls back.

Let's explore Puts in more detail.

Here is the chart of Bank of America (BAC), you'll be coming back to this often throughout this section.

For most Put options, the strike prices will start at the whole numbers. So in Bank of America (BAC) you'll have the $15 Put, the $14, the $13, etc. Once stock values get higher in price they may move to strike prices every $5 or even $10. Stocks like Priceline (PCLN) have strikes that have a $10 difference between strikes.

Let's take a look at the January Puts for Bank of America (BAC) and then we'll go through some examples to assist you in understanding the concept of a Put option.

Put Options Expire at close Friday, January 21, 2011

Strike	Symbol	Last	Chg	Bid	Ask	Vol	Open Int
2.50	BAC110122P00002500	0.01	0.00	N/A	0.01	0	51,325
2.50	BAC1110122P00002500	0.03	0.00	N/A	0.07	0	898
5.00	BAC110122P00005000	0.01	0.00	N/A	0.01	200	56,928
5.00	BAC1110122P00005000	0.06	0.00	N/A	0.07	0	1,142
6.00	BAC110122P00006000	0.01	0.00	N/A	0.01	503	936
7.50	BAC110122P00007500	0.01	0.00	N/A	0.01	100	77,194
7.50	BAC1110122P00007500	0.01	0.00	N/A	0.01	1	7,008
9.00	BAC110122P00009000	0.01	0.00	N/A	0.01	100	68,755
10.00	BAC110122P00010000	0.01	0.00	N/A	0.01	187	214,664
10.00	BAC1110122P00010000	0.01	↓ 0.02	N/A	0.02	40	2,682
11.00	BAC110122P00011000	0.01	0.00	N/A	0.01	1,485	167,167
12.50	BAC110122P00012500	0.05	↑ 0.02	0.04	0.05	10,552	349,545
12.50	BAC1110122P00012500	0.47	↑ 0.07	0.47	0.50	262	7,418
14.00	BAC110122P00014000	0.28	↑ 0.05	0.28	0.30	64,395	138,847
15.00	BAC110122P00015000	0.89	↑ 0.12	0.89	0.90	9,518	233,404
15.00	BAC1110122P00015000	2.87	↑ 0.30	2.72	2.76	10	6,706
16.00	BAC110122P00016000	1.81	↑ 0.19	1.77	1.79	4,119	24,542
17.50	BAC110122P00017500	3.25	↑ 0.15	3.20	3.30	319	94,202
17.50	BAC1110122P00017500	5.10	0.00	5.20	5.30	20	249
19.00	BAC110122P00019000	4.75	↑ 0.15	4.70	4.80	76	1,510
20.00	BAC110122P00020000	6.05	↑ 0.50	5.70	5.80	38	80,043
20.00	BAC1110122P00020000	9.45	0.00	7.50	8.00	3	191
22.50	BAC110122P00022500	8.00	↓ 0.05	8.20	8.30	180	9,523
22.50	BAC1110122P00022500	12.80	0.00	10.00	10.50	0	250
25.00	BAC110122P00025000	10.95	↑ 0.35	10.70	10.80	5	18,765
25.00	BAC1110122P00025000	12.95	0.00	12.35	13.15	0	12
30.00	BAC110122P00030000	15.80	↑ 0.20	15.70	15.80	151	7,872
30.00	BAC1110122P00030000	18.50	0.00	17.35	18.15	0	133
35.00	BAC110122P00035000	20.55	0.00	20.70	20.80	37	3,522
35.00	BAC1110122P00035000	25.30	0.00	22.25	23.25	0	94
40.00	BAC110122P00040000	27.30	0.00	25.60	26.00	3	2,020
40.00	BAC1110122P00040000	30.45	0.00	27.25	28.25	0	168
45.00	BAC110122P00045000	32.75	0.00	30.20	31.30	0	1,557
45.00	BAC1110122P00045000	32.90	0.00	32.25	33.25	0	214
50.00	BAC110122P00050000	34.00	0.00	35.30	36.45	0	10

Now, a simple way to understand the pricing of Put options is to ask yourself, “How probable is a DECREASE in the stock price is by the expiration date?”

Take a look at the BAC chart above and you can see that stock is currently at about $14.25. January expiration is on the 21st so let’s take a look back at the chain above at the $12.50 strike price. You can see that option is trading at $0.05. (In the chain above you’ll actually see two options with a strike of $12.50. I have no clue myself why they got two but always go with the one that has more volume that’s the one that you can physically buy and sell.)

Why so low? It’s trading pennies because the likelihood of this event happening PRIOR to the expiration is highly unlikely. Therefore, people aren’t willing to pay more than $0.05 for this option and I’m even surprised they’re willing to pay that much. So unless this stock has a wild move to the downside next week towards $13, this particular option will stay trading in the pennies. Remember that these Put options generally increase in value if the underlying stock (in this case BAC) goes down. I say generally because there are instances where that is not the case. If you buy this option for $0.05 today and it closes at $12.51 on Friday, January 21st, then this option will be worth ZERO dollars.

Let’s do one more example.

The $12.50 Put option here is currently out of the money. With Put options, strike prices are OUT of the money if they’re below the current value of the stock. So all options that are below $14.25, are considered “out of the money”. Options with strike prices ABOVE the current value of the stock are called in the money. The $15 Put is trading at about $0.89. When looking at option prices it helps if you use the stock price to provide context. With Put options, take the strike price you’re looking at and subtract its price ($15.00 - $0.89). So in this case we get $14.10. That’s basically where people are assuming the stock could get too after evaluating what the stock has been doing lately. Now take the current stock price and find out the difference between what people are saying in the option ($14.25 - $14.10). You get about $0.15 and this is what I view as the premium in the option or how “expensive” the option is at the moment. I use this as a gauge on whether I will be able to make money on this option if I choose to buy into it. If I pay $0.90 for this option, I better be damn sure the stock is going down well before the expiration date because if it doesn’t, then I lose a lot of that premium.

With this particular option, if the stock closes at $14.50 on the day of expiration (Friday, January 21st), what do you think the value of this option will be? Remember, at this point there is no premium left, so this option will be directly correlated with the stock price.

Figure it out yet? The answer is $0.50! Instead of the $0.90 I paid for it, I now have lost all of that premium and the price of my “in the money” option is exactly the difference between my option strike price and the stock. ($15.00 - $14.50).

You can buy or sell your option at any time you want prior to the expiration date. Remember folks, people are constantly re-evaluating their positions in options which shows through on the price of whatever option that you’re in and how much added premium there is at any given time.

Again, in order to fully understand these concepts, pull up options chains frequently. If you can get real-time data that's even better because then you can watch during the day how changes in your stock price affect the option that you're watching. It's all about repetition. You look at this stuff enough times you'll pick it up quick.

TIME PREMIUM

Undoubtedly the most important part to any options trade is Time Premium, and its essential to understanding how to actually make money in a damn option. And since that's what we are all out here to do, then yeah, ya might wanna understand what it is, right?

Now, time premiums are built into the price of any option you happen to look at. Some options have high premiums and some have low premiums. Again, think of an option trade as a bet on your stock hitting a SPECIFIED price within a SPECIFIED time frame. To go even further I introduce a very simple concept that indirectly determines the price of any option. The more "time" you have to see your bet come into fruition, the more "expensive" (premium) your option will be. Vice versa for less time.

That's basically how the price of all these options are calculated.

Conventional wisdom will preach to you mathematical formulas in order to understand how an option is priced; Black-Scholes models and implied volatility. All that may work but it's too damn complicated for me.

In Lucci's world simplicity is everything. I need to adapt things to my own language in order to understand it.

Let me give you some examples. In our previous section, we've used Bank of America (BAC).

To give you a clear picture on the concept of Time Premium, we're simply going to compare the price of an option that expires in January to the same 'strike' option that expires in February.

So let's say you think Bank of America (BAC) could easily go above $16 in the next week. You say to yourself, "I want to buy the $16 Call but I don't know which month I should buy, January, February or March". If you're positive the stock is going higher but are unsure of the time it will take for the stock to do so, that's when Time Premium considerations need to be pondered.

Let's take a look at what the current value of the $16 Calls are for January and February. I'm confident you will instantly understand what I mean by Time Premium.

JANUARY							
16.00	BAC110122C00016000	0.05	↑0.01	0.04	0.05	7,147	161,438
FEBRUARY							
16.00	BAC110219C00016000	0.19	↑0.03	0.19	0.20	2,218	37,258

So these are your two options with the same strike price – $16. WTF? Why is February's so much more expensive?

C'mon son! Have you not been listening to a word I've been saying? TIME PREMIUM!

So for the same strike in February you're paying around $0.15 more than what you're paying in January. That's because the more time until expiration the more premium you will see on your option. Let's get a little more advanced though. Don't be scared now…

Everyday, the Time Premium on your option is being constantly re-assessed by all the market participants. Bank of America is currently trading at $14.74. Can you take a guess as to why the option is only $0.05?

The option closes in about eight trading days. For a stock like BAC, that doesn't normally put in big, big moves, it's going to be hard for this to get OVER $16. Therefore, people aren't willing to pay up quite yet for this option. Now for February, they're willing to pay a lot higher. Why?

Duh! There's a lot more time until the option expires and the odds that BAC will climb up over $16 are much in all that time that's left are much higher. So the market is willing to pay a lot more because of the longer time period.

That's the basics of Time Premium folks!

CHOOSING THE RIGHT OPTION

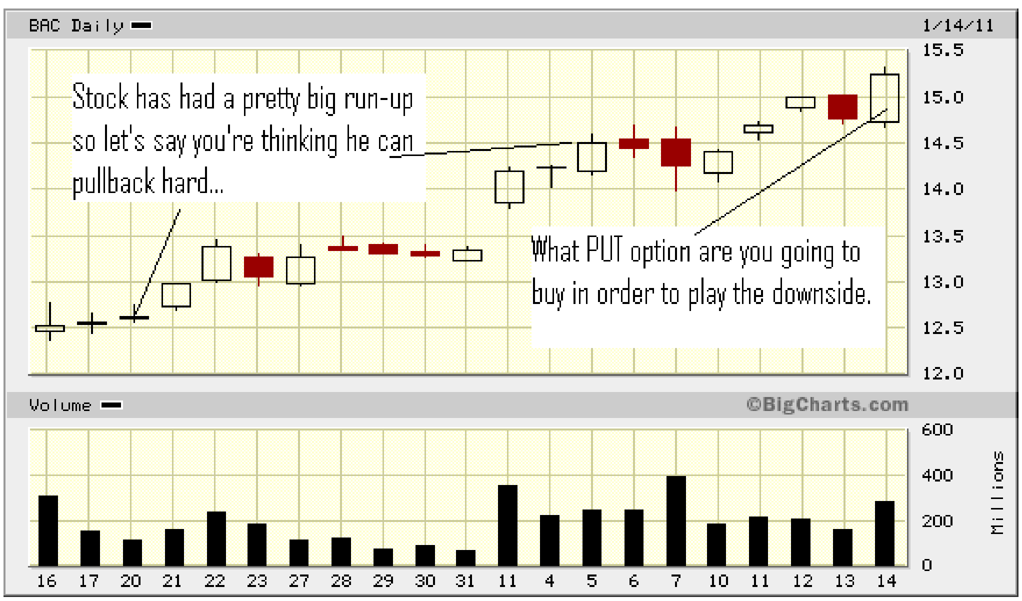
As we continue this particular series, we are going to get into further detail about different strategies one can pursue when attempting to trade options. There's a lot more to consider when trading options as opposed to the actual underlying stock.

For a stock like Bank of America (BAC), if you think that shit is going up then buy however many shares you want, set a simple stop area (the point at which you'll sell and take your loss if you were wrong), and then just "lean wit it rock with it."

To play the same move in an option, you have to assess what the stock will do in a given time period and then select which option you feel will gain the most in value. This is no easy task folks. But not to worry you newbie options traders!

To understand options all it takes is repetition. If you see a big move in a stock you have been watching, just pull up an options chain and look at the action in the Calls or Puts both in and out the money. After you do this over and over you'll understand which options to go for instinctively.

We will continue to use Bank of America (BAC) as an example for this series.



Clearly, this stock has had quite a big run-up. For this lesson, we're going to assume you guys want to play a possible pullback on this stock by buying some Put options. Which option do you buy? What strike? What month do you buy? This is a partial option chain for the January Puts in BAC:

10.00	BAC110122P00010000	0.01	0.00	N/A	0.01	35	214,598
10.00	BAC1110122P00010000	0.01	0.00	N/A	0.01	40	2,704
11.00	BAC110122P00011000	0.01	0.00	N/A	0.01	9	164,090
12.50	BAC110122P00012500	0.01	↓0.01	N/A	0.01	2,764	349,730
12.50	BAC1110122P00012500	0.09	↓0.09	0.07	0.09	53	8,319
14.00	BAC110122P00014000	0.04	↓0.06	0.03	0.04	11,491	154,754
15.00	BAC110122P00015000	0.22	↓0.26	0.21	0.22	56,004	247,183
15.00	BAC1110122P00015000	1.98	↓0.22	1.92	1.96	87	6,724
16.00	BAC110122P00016000	0.87	↓0.42	0.85	0.87	4,142	24,245
17.50	BAC110122P00017500	2.33	↓0.42	2.28	2.29	2,540	94,633
17.50	BAC1110122P00017500	5.10	0.00	4.40	4.45	20	249
19.00	BAC110122P00019000	3.95	↓0.10	3.75	3.80	23	1,322
20.00	BAC110122P00020000	5.18	↓0.07	4.75	4.80	51	79,873

There's a simple process that one should go through whenever trying to select which option to play. General questions should be asked such as, *"How many days do I have left until expiration? What's the likelihood of this move happening within that time period? How expensive are the options? What's the open interest and volume looking like?"*

Let's throw an example out to give you guys some more insight.

You think the stock is due for a MAJOR pullback and the bulk of the move could happen in one or two days. You have $14.50 in your head as the area where BAC can get to.

The first thing you need to consider is how many days you have left until expiration. January expiration is on Friday the 21st; that gives you four days until expiration. Four days is not a long time in the options world. Out of the money options, in this case $15 or $14, drop in value VERY quickly if the stock isn't heading in that direction before expiration. This is something you MUST keep in your head at all times if you decide to play the out of the money option here.

So now let's say you theorize that buying the out of the money Puts for January is too risky. You decide to play IN the money instead so you're thinking about the $16 Put. The $16 Put costs $0.87. The stock itself closed at $15.25 which means there is about a $0.12 premium in the option ($16.00 – $0.87 = $15.13… If you don't understand this go back in the previous sections). Now if the stock does actually go down below $15 this option will start getting a lot of action BUT, percentage wise, you ain't gonna knock it out of the park with this because the option is already so expensive (in the money). For example, if the stock gets to $14.80, by expiration your option will be worth $1.20. You made a little less than 50% on your money. That's obviously not bad, but in options you can make far more than that if you play your cards right.

How do I know when the stock will pullback?

Well that's the trick of the game folks. If you knew that then I wouldn't be sitting here writing this post because you wouldn't need me. This is where "tape reading" comes into play for me. Tape reading allows me to make a good prediction on what will happen in the short-term future of my stock, more so than just a shot in the dark.

Let’s go back to our example. Most of the time, buying out of the money options will pay you out GINORMOUSLY if you are correct in the move. If you’re not, you lose just as big. Many times it is not safe to buy these options unless you truly understand the risks. You must be able to watch constantly and take your losses VERY quickly if you feel you are wrong in the move. Therefore, you can save yourself a really bad day by cutting the trade short right away. Many people get crushed with this particular strategy because they have blind faith in the stock following their thesis. What they don’t take into consideration is HOW LONG it will take their stock to do that. If you’re unsure of time periods, buying a month out may work well for you. That will allow you to buy something out of the money and get the percentage gain without having to worry TOO much about losing premium in your stock. Of course, you’ll still have to worry BUT it won’t be as wild!

WEEKLY OPTIONS

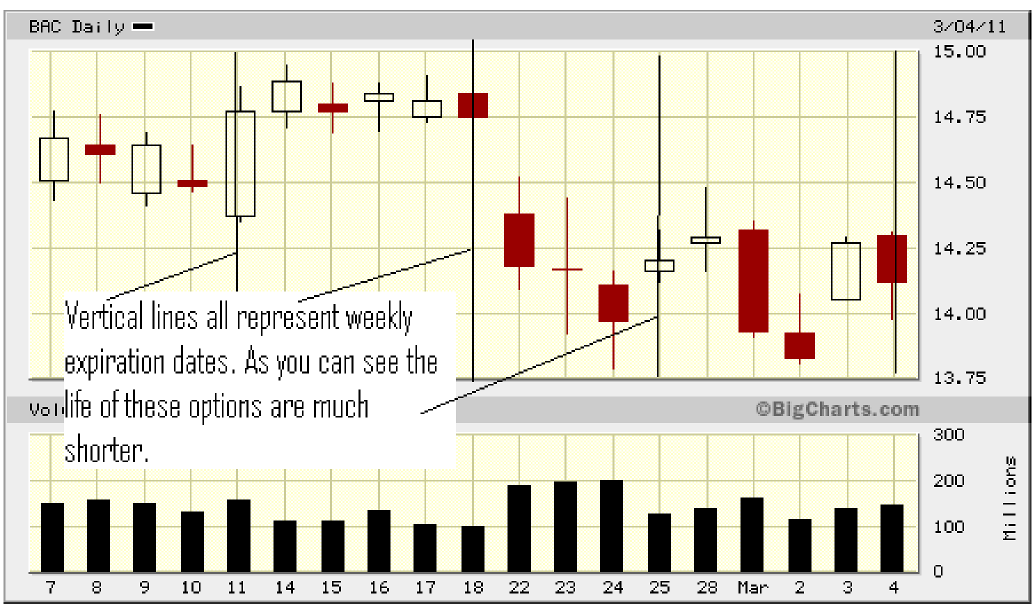
I pride myself on helping others out with the type of language that is not convoluted and filled with financial jargon; the jargon that so often confuses the common man and makes him fear the stock market. You'll see no use of thetas, betas, gammas or any confounding Greek symbols.

My theories rely solely on common sense and practical applications. This lesson will be to discuss a fairly new concept in the stock market: weekly options.

Weekly options were introduced into the stock market by the CBOE (Chicago Board Options Exchange) in order to further capitalize on increased options volume trading in the past couple of years. Looking at weekly options from a market maker's perspective, it's a no-brainer for pulling in even more commissions from millions of market participants. The more instruments there are to trade, the more trading there will be and the more money flowing into their pockets making those trades happen.

A highly subscribed new derivative equals SICK fees and commissions for all brokers! And to say that weekly options are highly subscribed is a freaking understatement because the volumes seen on contracts traded with weekly options many times EXCEEDS the volume traded now on the regular monthly options.

We have used Bank of America (BAC) in all of our previous examples so we'll continue to use it for this series.



The above chart shows the last month in the price action of BAC. Vertical lines have been drawn to show you the expiration days of these newly created weekly options. A weekly option now has a life of seven trading days. New weeklies are added every Thursday for the following week. Here are the March weeklies expiring next week for BAC:

Calls								Puts						
Contract Name	Last Trade	Change	Bid	Ask	Volume	Interest	Strike Price	Contract Name	Last Trade	Change	Bid	Ask	Volume	Interest
BAC\11C11\10.0	4.15	0.00	4.05	4.15	10	n.a.	10.00	BAC\11O11\10.0	n.a.	n.a.	n.a.	0.02	n.a.	n.a.
BAC\11C19\10.0	4.08	-0.12	4.05	4.15	45	2,509	10.00	BAC\11O19\10.0	0.01	0.00	0.01	0.01	8	19,575
BAC\11C11\11.0	3.22	0.00	3.00	3.15	10	n.a.	11.00	BAC\11O11\11.0	n.a.	n.a.	n.a.	0.02	n.a.	n.a.
BAC\11C19\11.0	3.10	-0.15	3.10	3.15	127	9,762	11.00	BAC\11O19\11.0	0.01	0.00	0.01	0.01	22	28,940
BAC\11C11\12.0	2.04	-0.13	2.09	2.12	55	10	12.00	BAC\11O11\12.0	n.a.	n.a.	n.a.	0.02	n.a.	n.a.
BAC\11C19\12.0	2.11	-0.16	2.11	2.13	380	17,363	12.00	BAC\11O19\12.0	0.02	0.01	0.01	0.02	135	53,381
BAC\11C11\13.0	1.13	-0.12	1.10	1.13	2,278	82	13.00	BAC\11O11\13.0	0.03	0.01	0.01	0.02	325	274
BAC\11C19\13.0	1.16	-0.16	1.15	1.18	4,042	74,928	13.00	BAC\11O19\13.0	0.07	0.03	0.05	0.07	3,105	106,830
BAC\11C11\14.0	0.30	-0.11	0.28	0.30	6,015	3,220	14.00	BAC\11O11\14.0	0.19	0.04	0.17	0.19	8,905	3,820
BAC\11C19\14.0	0.39	-0.10	0.38	0.39	10,258	175,592	14.00	BAC\11O19\14.0	0.28	0.05	0.28	0.29	7,977	176,727
BAC\11C11\15.0	0.04	0.00	0.03	0.04	3,687	6,701	15.00	BAC\11O11\15.0	0.95	0.18	0.91	0.94	905	438
BAC\11C19\15.0	0.06	-0.03	0.06	0.07	28,358	205,187	15.00	BAC\11O19\15.0	0.98	0.15	0.96	0.97	2,951	61,538
							16.00	BAC\11O11\16.0	0.00	0.00	0.00	0.00	0	0
							16.00	BAC\11O19\16.0	1.84	0.05	1.90	1.92	128	23,574

Strikes are not duplicate they show both the monthly and the weekly option.

You may be asking yourself, why are there two different options for each strike price? That's because in most options chains you see today they show the current weekly option and the regular monthly option. Take notice of the difference in the option values and the open interest between the weekly vs. the monthly. For example, let's take a look at the $14 Call. The weekly option has a current value of $0.30 and about 3,000 contracts open (interest column), while the monthly $14 has a value of $0.39 with over 175,000 contracts traded. Now, considering Time Premiums, the monthly is obviously more expensive because it has another week left before expiration. The weekly has literally just been opened for trading this past Thursday so that is why your open interest is lower. But take a look at the volume for the day--this shows the number of contracts that were traded in the last trading day and you can see they're pretty similar, the weekly traded about 6,000 while the monthly traded about 10,000.

If you are a short-term trader, choosing which option to go with for a certain trade can be a crucial decision. I've compiled a list of things to keep in mind if you decide to play the weeklies in the future. Keep in mind, these are things I've picked up from experience and simply from just trading these on a daily basis.

* Time premiums erode EXTRA fast with weekly options in general.

* Buying next week's weekly options before the weekend is dangerous because you immediately lose those two days of premium even though the market is not active during the weekend.

* If you expect a gap up or down in a stock the next day, playing weeklies can be much more advantageous than the monthlies.

* Weeklies should generally be used to play a move that you expect to happen

immediately and not to be held overnight. Overnight holds in a weekly option can really kill you because everything is about sentiment. If there is a chance your move will not happen, your weekly will dwindle in value MUCH more quickly than a monthly option would.

* Thursdays and Fridays are generally ideal times to play weeklies. It is not at all surprising that it is also a risky time to play them. The percentage gainers are sometimes enormous if you can time your entry when a stock is about to make a major move. The Time Premium may have eaten away at an option and taken it to nearly zero, and a strong move in the stock will send that same option to $1.00, $2.00, etc. THAT is buying low and selling high.

* Weeklies are freaking bananas, so grab ya' balls. There is no rationality towards the pricing of a weekly. None whatsoever. The sooner you accept that, the better off you will be.

* Since the advent of weeklies for many stocks, the options market has changed a great deal, in my opinion. Monthly options premiums are now generally much higher than they were before. Prior to the addition of weekly options, OPEX days (options expiration on the third Friday) were always pretty crazy. Now, the action has moved away from the third Friday towards the weekly expirations.

Weeklies have also caused outrageous pricing inconsistencies. The pricing of options is totally irrational. Anyone who uses mathematical models to price options or to plot out expected future values of those same options has no clue what's going on in this market.

For the newbie traders, I would recommend paper trading these options before using real money so you can get a feel for how they move in conjunction with the underlying stock prices.

Selling, or writing, these weekly options has also become a lucrative game as well for the investor who is strapped with plenty of capital.

There is plenty more information regarding these strategies on Sanglucci.com, so checkout the site to dig a littler deeper.

THE PSYCHOLOGY OF TRADING

LUCCI'S PSYCHOLOGY

Instead of recanting the things I've learned thus far from reading up on this material, I'm going to try and explain to you what I feel is the most important way to keep your emotions in check.

Trading is said to be 90% mental and 10% strategy. You've heard me say plenty of times at Sanglucci.com that making money is the easy part. The toughest part about trading is how you manage your losers.

There are many dynamic forces going on in your mind while you're trading stocks. Both positive and negative forces work together to pull you in different directions and towards different decisions.

All of this is going on subconsciously in your head and it's important to be AWARE of and to pay attention to what's going on up in that brain if you're going to overcome the challenges of this game. I've read many books on this topic and if you're a trader and reading THIS book then I can safely assume you have as well. Most of those books come to the same conclusion: one must conquer the mind before they can conquer the market.

When I was younger, my father always told me psychology is total bullshit. It was his way of making sure I never got interested in things that wouldn't make me money. It was either an Engineer or Doctor for me in his head. He'd say people use psychology to make excuses for why they couldn't get something accomplished. In reality, the man is right to some extent but at the same time, psychology plays into everything we do.

Everything we do or don't do takes place first in our heads. Character traits such as confidence, arrogance, fear and desire all drive us towards the decisions we end up making. As a result of those decisions, our lives are shaped and mapped out into different paths. Sometimes we take wrong turns and have to work twice as hard to get back to the main path.

Sometimes, we only need to realize one major thing that changes the way we think about anything in particular. It's called a paradigm shift.

As much as you think you're different from other traders, you ain't! We all wear the same emotions on our sleeves and we all fall prey to the same shit, plain and simple. Some have a little more control than others, but for the most part, the same factors are going on in our heads causing us to make bad decisions as much as the next guy.

So what is the root of it all?

This is a principle that holds true in all activities we partake in. Bluntly put, humans complicate every fucking thing there is to consider. You are your own worst enemy in this game and just about anything else you do. Your stupid mind is overcomplicating the way you read this damn book!

Drilling down on trading specifically, we complicate things by asking ourselves an infinite amount of questions. How come this guy is doing better than me? Shit, how can I make enough money so I don't have to work all I have to do is make $1,000 a day and I'll be good right? Crap, I'm down a thousand in this position but it'll come back I should hold this right? I can't take another loss can I? Damn, I should take my profit on this but what if goes up more then I'll miss out? Did I miss that trade? It's not too late to get in is it?

No doubt you've all been guilty of overdosing on mind blasting questions. My policy on my own mind and how to control it is quite simple.

And it is as follows: WHO THE FUCK CARES!

Who cares if someone makes more than me on a trade? Who cares if I didn't get the whole move? Who cares if I sold out and the stock ended up doing what I thought it was going to do? Who cares if I missed a banger? The answer to all these questions and anymore you can come up with is: NOBODY CARES, ONLY YOU!

The market is the market and there are opportunities every second. If we get a couple moves we're closer to where we want to be. If we don't WHO THE FUCK CARES? More are on their way. Do yourself a favor and tell your ego to go screw itself tonight!

THE BEAST

Why does your mind always seem to get the best of you?

Sometimes no matter how hard you try at staying focused and uninhibited by the constant and repeated battles going on in your head, you just can't control it. Ultimately, your mind gets the better of you every time.

Why is that?

Are our minds, in effect, vile beasts that lurk in our innermost chambers, waiting to thwart all of our actions and desires? Or is it that WE complicate every situation by luring that '"beast" out ourselves?

Your mind is a beast, no question about it. Your mind will cause issues to exist when in reality there are none. And I'm talking about everything here, people, I'm not just talking about trading. I guarantee right now if you thought about all the conflicts you're currently having right now, you've made up more than half of them in your own head because of your biased and misguided assumptions.

We make assumptions to explain shit we just don't understand. This allows us to put the blame on something other than us and sets our minds at ease by attaching reasons as to why we stress out.

Meanwhile the monster still lurks in the shadows waiting to blow your assumptions further into reality, thus the saying "reality is perception".

Let's bring it back to trading now. The reason why psychology plays such a big part in trading is because emotions run much higher in this particular line of work. Higher stress levels come with the territory there is no possible way to avoid it unless you're a robot. Second guessing your intentions, your method, and your actions when you're on a losing streak is inevitable.

I think for me folks, the answer really is simple. I've had enormous success before and I can do it again. Being wrong in the stock market is simply a cost of doing business and instincts are still what guides us. I have plenty of instinct and I have blind faith in myself.

So at the end of this monologue I come to the same conclusion that I arrived to in the first part of this series. Who the fuck cares about losses?!

I still have my instincts and they're currently firing on all cylinders. A couple tweaks and I'm good to go!

REALITY VS. POTENTIAL

How many times have you seen a big move happen and you weren't in it? You saw it coming and even planned for it but you still didn't "get in that ass."

Or how many times have you said you were going to take your profits or minimize your losses only to watch your stock blow past your "planned" exit and you find yourself STILL in your position?

Better yet, how many times have you been in a wild move that gives you no reason to sell but you do and consequently leave an obscene amount of money on the table?

After trading for several years, I've realized there really is a fine line between "holding" or "folding." Everything is situational. Unfortunately, I know that's not what you want to hear but it is "reality" and not what you may perceive. Our episodes of "Wall Street Porn" get many folks excited and at the same time extend the perception that these scenarios are very plausible, but the simple fact is it's a lot easier said than done.

I've gotten several wild moves in my day, left hundreds of thousands of dollars on the table, and also failed to take profits many times. All of this shit comes down to your understanding of "reality" and "potential."

Your mind will constantly reaffirm your blind conviction in holding a trade for more profits while the tape or charts are telling you, "What are you doing? I'm bout to stab you in the eye! SELL ME NOW BEFORE ITS TOO LATE!"

Price action never lies and the fact is for the veteran traders out here we all know when we should sell something or hold on. That gut instinct is most of the times indicative of reality setting in. Your mind is what puts you in la-la-land waving the perception and allure of "potential" and grandiose stock market debauchery.

It's a difficult task discerning the two worlds and, in effect, walking on that thin line. I can't tell you how to do this folks, 'cause I got no clue myself either! All I can tell you to do is be aware of it. I'll leave you with a joke that I heard explaining the two concepts in detail.

A son asks his pops, "What's the difference between reality and potential daddy-o?" Pops says, "alright son you wanna know the difference? Go ask your mommy if she'd sleep with Usher for a million bucks." So the son goes to his mother and asks her. She replies, "Ya know I would be cheating on your Father, but we could really use the money, soooo, yeah, I'd sleep with Usher for a milly!" The son goes back and tells his father and pops now sends him to ask the same question to his sister. So the son goes to his sister and asks her to which SHE replies, "FUCK yeah I'd sleep with Usher! He is too fine AND I get a million??? Hell yeah I'd sleep with him!" So the son again goes back to his father and his father says "OK, son here's the difference between reality and potential. POTENTIALLY, we sitting on $2 million dollars son, but in REALITY we just got a couple of hoes living in this house!"

This is trading folks. This is what we do and these are the situations we have to deal with on a daily basis. Sometimes you'll overcome it, sometimes you won't.
Realize though, that most people who fail at this game almost never think in reality.

BIASES

I really dislike psychology. I don't like thinking about thoughts. If I spend all this time thinking about my damn thoughts and how they're encouraging me to act in certain ways, I'll never get anything accomplished.

Psychology is like that woman/man you wish you never met. They never go away and they're always lurking in your subconscious causing your wishy-washy side to come out. Since we can't get rid of them we may as well understand how they're fucking up our lives, no?

Now to address the nasty biases you have and how they affect your trading.

Bias is dangerous. A bias will always cause you to discern a situation from the incorrect perspective. What you've effectively done is premeditated your reaction to the problem or event. Most of the times we do this without even realizing it.

No matter what aspect of life we're talking about, if you are biased or partial to one side of an argument or situation, you'll never see the error in your ways, if in fact there is one to be seen.

Most often people are too stubborn or too late to realize that their bias lost them the chance to address the problem correctly.

So how exactly is this bias affecting my trading? In trading, you pretty much have three choices. You can go short, you can go long, or you can do nothing. Now, you go about choosing which way you're going to play a stock based on however the hell it is you decide and you hop in the trade.

If you're wrong about the trade and the direction you believe is going, what happens? Hopefully you're quick to get out and take your loss as soon as you possibly can. But what next? Do you reassess the trade and ask yourself if you were in the right direction? Or do you to continue to hit the stock again and again on the same side? I'll tell you right now most traders stick to that one side until it beats them up SEVERAL more times. It's almost like we continue to attack it from the same angle in the hopes that eventually it will head in that direction when in fact, the stock has no desire to do so at all. The price action continues to tell us that we're wrong yet we still lay siege repeatedly with the same misguided biases.

The market must always be looked at with an open mind. Folks, the market is not rational. It does not want to be rational and it never will become rational. There is no rhyme and reason to this shit there's just you and your thoughts. Those who believe the market is a rational place and that stock prices are in fact TRUE valuations are smoking some high quality, grade A marijuana that's flown in from the Philippines and grown with special light from a different sun than we currently have in our solar systems. If you think the market is rational then you have psychological issues beyond my control or comprehension and you should seek assistance ASAP.

In an irrational environment, I hope you see how holding a bias just doesn't make sense logically. How are you going to add the soundtrack of your mind to something that really doesn't give a shit about it? In the market, you have your opinions and you make trades based on those opinions. That is it. There's nothing more than that.

You’re not right or wrong you’re simply in at the right moment. Holding biases, however, causes you to forget these things and bring about those useless human emotions like pride and stubbornness.

STYLE

When it comes to fashion, everyone's got his/her own tastes. The movie star wears Versace dresses, the skater wears paint-on jeans, and the housewife wears sweatpants and a hoodie. In fashion, who you are determines your style.

Trading is no different.

To be a successful trader, you must develop and practice a trading style that matches your personality. The myth that there is only one way to make money in trading is, well, a myth. It's bullshit. You could hear the best stock tip ever given and STILL lose money in the trade simply because you couldn't handle it psychologically. Maybe it was a volatile move and the pressure caused you to exit the trade too early. Or maybe it was a slow developing trade and your failed patience made you leave money on the table. Just because the stock tip ends up making money, does not mean YOU can.

If the trade does not match your particular style, you have no business trading it in the first place. Trades come in all shapes and sizes, so do traders. As far as trades go, they're a dime a dozen: Netflix (NFLX), Bank of America (BAC), calls, puts, 10 contracts, 1,000 contracts, 500 shares, a couple minutes, a few days, etc. It's the same for traders: hot head, shaky hands, action junkie, intellectual, quants, street tested, newbie herb, white collar, blue collar, working stiff, and the list goes on. All types of traders and similarly all types of trades have the potential to make money.

So then why do so many trades fail? Why do so many traders wind up broke? Because they've got the wrong style!

You have to ask yourself, "Am I a movie star, or am I a housewife? Maybe I'm a skater?" Think about it, if a movie star decides to wear sweatpants and a hoodie, People Magazine will end their career. And if a housewife is seen wearing paint-on skinny jeans, her son gets the shit kicked out of him at school.

If you're a nervous person and can't handle big swings, don't trade Netflix (NFLX), Apple (AAPL) or any other four-letter ticker with a three-digit stock price. If you're a tweaked out adrenaline junkie, don't trade Citigroup (C), General Electric (GE), or any other low-dollar, blue-chip, high-volume stock.

The trade must fit the trader.

Even when you're right in the move, if the trade doesn't match your style, you'll get smoked every single time! Determine who you are. Develop the appropriate style. Make money.

NUMBERS

Do you believe every number you see or hear?

Most of you probably don't even think twice when you hear numbers being thrown around to validate statements. We hear numbers describing everything from baseball statistics to quarterly earnings reports.

What if I told you that 90% of those numbers are complete bullshit. I said 90% right? Where the hell did I get that number? Clearly, I just pulled 90% straight out of my ass.

Numbers are magic and if you know how to use them, then you are in actuality, a magician!

We all live and die by numbers. When we're kids we think once we get to eighteen years old we're free. As adults, we stress about the price of a gallon of gas and pour over numbers displayed in bold on our IRA statements. Advertisers use crafty numbers to swindle dollars out of your wallet everyday by plastering the covers of magazines with utter nonsense like, "YOU CAN DROP FIFTY POUNDS IN TWO WEEKS!"

You think there was really a million people protesting at the "Million Man March" in 1995? You think our unemployment rate is really below 9%?

Watch CNN during the presidential elections and you will be force fed more numbers than you can even shit out in your entire lifetime. New polls are conducted by the minute with the sole intention of persuading your vote.

The psychology behind numbers has a big presence in the stock market as well. Traders fixate themselves on specific numbers and technical levels that indirectly place limits on their game plans. Whether it's max position sizes, expensive option values, or percentage gains/losses our minds hold us back from trades because we BELIEVE in the numbers. Let me give you a perfect example of where belief in numbers can hurt. It takes $25,000 in the United States to secure margin and not have to trade under the confines of the dreaded Pattern-Day Trading rule. You grow your account to $24,000 and now you want to lighten up in order to make sure you get to $25,000 as smoothly as possible. What you don't realize is that you've put that $25,000 on a pedestal and you're now about to go on an extended losing streak. THEN, you'll get so pissed at yourself you'll go on a tailspin ensuring your inevitable death in the market. Catch my drift?

Again, what if I told you those numbers were totally bullshit and arbitrary? Would you believe me?

It's time to take dose of Lucci's Reality people. This is a special medicine only available at SangLucci.com. This medicine will flip your world upside down.

DRIVE

"Stay thirsty, my friends."

You know who said those words? None other than the most interesting man in the world. Goddamn right.

For all those out there who interpreted this message simply as encouragement to drink beer, particularly of the Dos Equis flavor, you got it all wrong. It can allude to an entire array of different philosophical meanings – none of which we'll be discussing here because I don't know shit about philosophy and I don't want to impinge on the statement from a man of such caliber. Plus, let's face it, Dos Equis is piss in a bottle.

We just want to tweak his message a little. And, here it is: *"Stay hungry, my friends."*

Now this phrase goes without explanation, but nonetheless it is often overlooked in the realm of trading. To be successful long-term, you have to stay hungry, you gotta have that drive. Two things happen to traders: we get beat, and we triumph. You all know this, of course, but it is important to examine the effects that arise after the two instances. When we get beat, depression and regret set in a little, and there is a tendency to go looking for the first shoulder to cry on to comfort the blow. When we triumph, elation fills our skull, and there is a tendency to want to bathe in that moment of glory.

Before I go further, let me say this: the best traders out here, the super traders, don't go through any of this shit. They don't display either reaction. The super traders take the ups and the downs in stride like it's always just business as usual. No emotion. However, unless they were born with ice in their veins at some point early on in their life as a trader, they too rode the roller coaster.

Drive got them off it.

You may think that it is more important to have drive in those situations when you get beat, but this isn't the case. Both situations are equally important. The reason is complacency – the complacency that later leads to fear – the fear that comes from the mindset of "I don't want to lose again after having just lost," or the converse: "I don't want to lose what I've just won." Both trains of thought will get you nowhere in trading.

If you don't have the drive to push yourself after a loss, or the drive to motivate yourself to find the next trade after a nice gain, you might as well leave the table. The market isn't going to serve up anything to someone who's not hungry.

Win or lose, it's all about what's next.

CONFIRMATION

Patience is a virtue.

Is it true that good things come to those who wait? In the business of trading, yes, this is true. It is important to have patience long enough for the best trade set-ups to come to you, as opposed to trading everything that has even the slightest whiff of making money. Overtrading is the fastest way to decimate your account. Just sit on your hands and wait for the opportunity to present itself. Otherwise you'll churn and burn.

However, when those perfect trade set-ups do come your way, you better throw patience out the window. Among rookie traders, but also with some veteran traders alike, there exists a fear of being wrong. Because of this fear, inexperienced traders, and of course bad traders, wait for confirmation of their trade ideas before entering a trade. The fear of being wrong creates a hesitancy that causes many traders to miss a good entry or at times to miss a move entirely. Identifying a good set-up means nothing unless you get in the trade, and you better get in early.

This market doesn't show money to those who wait. Too many traders want to wait until they see what it is they're looking for before making the decision to pull the trigger. This is not the way to make money. In fact it might as well be the exact opposite. It is the surest way to buy tops and sell bottoms. One cannot be timid and require reassurance. You must anticipate the impending move and act accordingly prior to it occurring. Confirmation must come AFTER you've entered the trade. This will allow you to let your winners run longer and provide you the ability to identify a losing trade much sooner.

Second-guessing and over-analyzing a good set-up while waiting for the confirmation of your idea will certainly cost you in the long-run. You must be confident about your trade idea early, get in, and let the price action affirm whether you are right or wrong. This eliminates the coulda-woulda-shoulda mentality and leaves no room for hindsight. You're either ahead of the move or you already missed it.

Do not concern yourself with missed trades that you have not been previously watching – they are a dime a dozen and it's outside your control. Besides, plenty more opportunities are on the way. Do, however, take great concern with trades you HAVE been watching that you let slip away. Along with it will go potential profit, and also your potential as a trader.

THE PSYCHOLOGY OF NOT TRADING

Psychology is in everything we do, every action we perform, and every thought we have. Even when you're NOT doing anything, psychology is there mixing chemicals inside of your brain determining your next move.

They say money never sleeps? Psychology NEVER sleeps. I want to address a psychological issue that has plagued many traders as of late, because of the current see-saw action prevalent in today's market environment.

Let's first address the life of a day-trader. A day-trader wakes up every morning expecting to find the action and find the money. He/she generally doesn't come to the conclusion that the day may be a "churnbox" unless they put some money to work and figure it out indirectly by losing money. Typically, a trader goes into everyday assuming the day will yield money-making opportunities.

It's only until after a trader has done enough damage to his/her accounts that they take a step back and realize the big picture. At the end of the day, the majority of us all trade break-outs and break-downs of levels that we feel are pertinent. We create these levels from watching price action, watching charts, or watching the paint dry on the walls. How you come up with the levels is irrelevant; the point is many times during changes in the ebb and flows of the market, those break-outs and break-down entries simply don't work. Coming up with a reason as to WHY they don't work, however, is not an easy task. Manipulation is often times the easiest explanation. We're humans. We naturally play the blame game in order to explain why something didn't work. North Korea and Venezuela blame America for just about everything, man blames woman and vice versa, and Democrats blame Republicans.

Well, traders blame the market makers.

Regardless of what mechanism caused your trade to fail, the point is that the trade DID fail. Now, traders are not going to assume that because one trade failed, the rest will follow suit. A trader is, by nature, quite stubborn. As a young Thundercat back in 2006, I wouldn't learn the lesson until I erased my whole months gains.

The psychology of NOT trading is even more difficult to learn than the psychology OF trading. Imagine that shit?

Again, traders feel the urge to be in a trade at all times. If you don't believe me, think back to the times where you're away from the markets. How many times do you refresh your phone for prices? How many times do you rush through other activities to run back to your computer only to find your stock has gone absolutely nowhere. Better yet, how many times have you neglected your body's needs and foregone a meal to watch your stupid positions?

Learning how NOT to trade is one of the most important lessons in trading you can learn. Gut instincts tell you exactly when to pull the reins back, the problem is we seldom listen to the gut when emotions are running high. I urge any one of you to comprise your stats for the last five years and figure out where you made the most money. Chances are it's a few weeks or months out of the year. The rest of the time you're just trying to stay alive and not lose too much.

So take a word from a bird in a fuzzy herb tree and try to NOT trade if the market isn’t paying your strategy out at the moment!

OVERTRADING

Traders, do me a favor and smash your keyboard if you often fall victim to overtrading!

Now, I'm venturing a guess that about 99% of you now have to pick up the pieces of that dismantled keyboard off the floor. If you did NOT have to smash your keyboard, well then chances are you're simply not honest with yourself.

Overtrading is a problem blocking many traders from entering a better and more confident place with their trading. However, to look at overtrading as a problem would be the wrong way to go about it.

Overtrading is simply a response. Any number of events can cause this type of response, meaning trading in and out several times more than you usually would. The market could be choppy. You may have recently taken some losses and are struggling to recoup the damage. You may have recently taken a bunch of winners and you keep trading off sheer adrenaline. You may subscribe to three different alerts services and you want to make every trade possible.

As you can see, there a number of causes resulting in the effect of overtrading.

The key thing to realize about overtrading is that one never notices what they are actually doing until it has become to late. This is the same predicament you'll find yourself in when dealing with many other weak human emotions. Whether you're in love, you're scared, you're depressed or just insane, certain bad habits are the natural response. These habits soon become routine mechanisms that automatically initiate in order to "deal" with all of that emotional stress. The problem is that they take away from dealing with the ACTUAL problem.

The solution here is a simple realization: you don't HAVE to be "in the market". You don't HAVE to do anything. Many traders can't even wrap their minds around such concepts because it's contrary to everything they've been taught, but cash is a position.

Less is more, especially in the current market environment. Overtrading is a clear-cut characteristic of a trader who hasn't found his/her true strategy yet. There are very few traders who know what they can handle and know what they simply can not tolerate. Being aware of what you are NOT good at is at the root of the solution to overtrading. The statistics that claim 95% of traders fail exist for a reason people.

Trading is more about understanding oneself than it is about making money.

PERSISTENCE

Folks, it's time to dust off our old inventory of educational material here at Sanglucci.com and breath life back into one of the most penetrating and relevant subjects of this book.

When it comes to trading, persistence is a trait that can be applied to many aspects of the game. One of the most common applications is continuing to trade in the face of losses and tough times. Back in the prop firm days as a young buck, the turnover was through the roof. New traders would funnel through the office and back out within a month. Working with no guaranteed salary is a difficult thing to grasp for many people, especially those unable to make sacrifices.

Trading can only be done successfully when you sacrifice your current lifestyle, to some extent, in search of a better one. Thus, persistence becomes the determining factor whether or not you will make it in this business.

I was just a kid when I started around the age of twenty-three and had recently just had a completely "unplanned" child. My girlfriend and I moved into the shittiest, illegally converted, one-bedroom apartment you could possibly imagine. Rent was about $600 and our landlord took it in cash.

There were mice. Oh, there were mice.

We lived off of her school loans for a while until she had to bail & started working full-time. Ticket scalping wasn't bringing us steady money so I took a job as a Financial Analyst to make ends meet. We were comfortable, until I decided to quit and pursue what I felt at the time to be a great opportunity for my new family and I.

Of course, she didn't see it that way…

As you can imagine, the arguments were plenty. I hustled ten times as hard doing whatever I could to pull in extra cash on the side. I was obsessed with making my new venture in trading work so I put every dollar I made back into my prop account, often foregoing paying bills or for basic necessities.

I eventually lost her in my self-proclaimed pursuit of happiness.

I studied every night, going over plays made by the head-traders in the firm. I took notes on EVERYTHING. I watched recordings of the tape to hone my skills. Finally something clicked and the persistence paid off.

Now, I'm not advocating for you to go through the same process that I did, but I am trying to convey the simple notion that sacrifices must be made. Not everyone will understand these sacrifices and many of your friends and family will think you're just wasting time, doomed to fall into the pit of failure like everyone else who has tried.

Fuck them.

Persistence is a dangerous weapon.

STOMACH TOLERANCE

What do you think of when you hear the words, "Stomach Tolerance?"
Do you think of how much Indian food you can consume without having to hit the bathroom shortly after? Do you think of how much of your wife's shitty casserole you can eat without giving in and telling her it's horrible? Do you think of how long you can listen to your co-workers ramble on about their mundane lives before throwing ketchup packets at them? Or do you think about how much denial you can take before falling into a deep depression?

Although these would all be valid examples for displaying one's stomach tolerance, in trading stomach tolerance alludes to your ability to take a loss as well as your capability to push it to the next level.

Think about the last time you took a loss when exiting a trade. For many of us, this reoccurring phenomenon should be fresh in our minds given the current market environment. How did you feel after taking that loss? Did you feel regretful? Did you feel like you've completely forgotten how to trade? Did you tell yourself you should have known that outcome was going to happen and subsequently shouldn't have taken the trade in the first place? It's natural human behavior to question decisions that resulted in a negative outcome. It's only natural because, initially, that same decision had no definitive outcome.

It's similar to mulling over a failed relationship or a missed job opportunity, agreed?

You realize that you loved her after she left you for not being ready to commit. You opted to stick with your current job instead of pursuing your desires of a more fruitful & fulfilling career. The proverbial "coulda-woulda-shoulda". When there is no guaranteed way to win or succeed at a particular endeavor, humans resort to psychology to offer up solutions for all of these unknown variables. Unfortunately, second-guessing, indecisiveness, and remorse are all byproducts of this same thought process.

Your stomach tolerance is what dictates how you will come out of these mental struggles with yourself. Let's face it, if you have a weak stomach tolerance, life will beat you down and you might just stay down. The greater your stomach tolerance, the further you can push yourself towards achieving what others simply don't have the stomach to handle.

Let's bring this back to trading.

No trader likes to lose. Yet trading requires accepting the responsibility of losing.

Pointing the blame at the markets will get you nowhere. It will only solidify your inevitable demise and your inability to build your stomach tolerance. Thinking about the concept of losing money as a responsibility, a cost of doing business, instead of a negative outcome is paramount if you really want to become a professional trader. If you were to dig deeper into the actual psychological effects of a losing trade you would undoubtedly find an overabundance of misguided emotions. If a mind loses itself to these emotions, then it has already lost the battle. For a person with a weak stomach tolerance, the mind will produce those same debilitating emotions before they even make their next trade, thereby hindering a trader's ability to reach his or her full potential.

Stomach tolerance also is a major factor when a trader is attempting to “size up” and amass larger positions sizes, which in turn results in larger swings to his/her trading account. The stomach and mind have to get accustomed to this change in the status quo. Books and systematic traders will tell you that it's all relative and there is no change that needs to be made to a trading style. Although in theory this may be true, psychologically it's a crock of shit.

For example, say you are a trader that usually takes 10 contract positions in a majority of your trades. Now let's say you feel great about this one trade you've been waiting on for a while and you decide to throw 100 contracts at it instead of the normal 10. The position goes south on you and you freeze up after looking at how much your account is down. You are unaccustomed to the feeling, therefore, you just can't react quick enough to what is happening on your computer screen. Your stomach has DROPPED.

Advancing in your career as a trader requires that you pay attention to your stomach tolerance and constantly test it to assess it. The inability to mentally accept losses or an increase in position size sits as a barrier to your natural progression.

Don't be complacent!

CONCLUSION: IN THIS BRIGHT FUTURE, YOU MUST FORGET YOUR PAST

People say history repeats itself…

Some say the same theory applies to the stock market. I, for one, don't believe that.

For us short-term traders the market changes almost daily. The good traders last because they see and feel the changes and are able to adapt. They develop new strategies and are constantly one step ahead of the pack.

Am I one of those traders??

I'd like to think so.

Past performance for a trader is NEVER indicative of future performance. Anybody that comes to you and pitches you a hustle BASED on historical results CANNOT guarantee you a damn thing in the future, despite what they may say or how good they make it look on paper.

I'll give you a perfect example. I had a buddy I used to trade with at the Prop Trading office I was at from 2006-2008. We called the kid the *'Flux-Capacitor'*. He was the *Flux* because the kid just knew everything about everything. So, periodically if any of us needed some information we'd yell out "YO *FLUX*?! Wtf does this mean?! Or hey *Flux!* What's the fundamentals behind XYZ?" This kid had answers for everything I tell you. He had a good heart, that boy, but he could never make money trading. I felt bad but at the same time I knew why. Those that can't stand being wrong or don't know how to 'deal' with being wrong can never make money trading much less do anything that requires risk-taking. People like that are SUPPOSED to become analysts in whatever career-paths they choose. You will never get a person with that type of brain to admit they're wrong about even the smallest little detail.

Anyways, I had already struck out on my own prior to that office being closed down. Once it did go under, the Flux came to me with a Forex (Currency market) trading system. A system that his math-wizardry and analytical mind created with a buddy of his from college. They thought they had everything figured out. They showed me back-tested data that proved they would make 4% a week, doubling/tripling my money inside of a year. The draw-downs shown of course were minimal. My friends and I thought to ourselves, "shit this is our ticket out!" We put much faith into the *'Flux Capacitor'*.

I mean it's the fuckin *Flux* how can we go wrong? !

They were so sold and confident on this deal that they advocated for a 50-50 split on the profits. How's a start-up going to take half the profits with no ACTUAL past performance data? My boys and I didn't care.

Remember, this is the fuckin *Flux*, how can we go wrong?!

So we pooled together about $45K collectively and signed a contract with the Flux to get started immediately. We started off on a good foot and then took some losses that were WELL BEYOND what was put forth to us in all the stats. After asking what the problem was or if the program needed to be tweaked, we got the standard response we'd soon get very used to: "Weeeellll uhhhh what had happened was the indicators of the indicators didn't account for the indicators that were indicating the indications of that plunger being stuck up our ass."

I mean, that's what it sounded like to me …

The system just didn't perform as they showed us it would. If the Flux had approached me and just said, "Hey listen, try this shit out and give me a shot" then I wouldn't really care so much. But to show me all that jazz and then say nothing to me when it doesn't perform how you said it was going to?

SHAME ON ME! Not shame on him, shame on ME!

My boys and I wanted to believe it was possible SO BADLY. I mean we were ready to give the Flux the rest of our money too. The $45K was just to test it out. Then I was going to sign over my life savings.

Again, nothing against the *Flux*, he's a good kid, but if you talking past performance in the stock market? That shit does not mean you can do a damn thing. It would be best for you all to remember that fact.

This finally brings me to my point. No matter what scale you're talking about, the past is the past. Five years ago, five minutes ago, it doesn't matter. This goes for both your personal performance and the market's behavior. If you aren't focusing on how to adapt to the current market and how to trade to the best of your abilities, right now, you might as well walk away.

Introduction to tape reading

THE LOST ART OF TAPE READING PART 1 – INTRO TO OPTIONS

The term 'tape reading' gets its name from the old method of displaying trades. Information on bids and ask prices were printed on paper by a ticker tape machine. Investors would crowd around these machines and read the tape numbers to try and capitalize on the behavior of the market. The basic premise of tape reading involves evaluating the size of stock orders, the frequency of orders and the price at which orders are taking place (at ask, at bid, between ask and bid) to identify trends in trading behavior by insiders, professionals and the general public. Profiting from understanding these trends is what tape readers seek to do.

Today, everything is done electronically and within fractions of seconds. The tape has evolved to display it's information through several tools readily available in most broker platforms. These tools are the 'time and sales' and the level 2. These two tools compile all the necessary information for the savvy tape reader. Gimme those two with a simple chart and I'm good to go!

Over the years, tape reading took a back seat to 'Technical Analysis'. Ironically, technical analysis is just a derivation of tape reading and seeks to transform bid and ask prices into charts and categorize specific price action into common chart patterns. This particular analysis also adds in the use of many 'technical indicators' that introduce even more patterns to the game.

Personally, I think the whole concept of technical analysis was designed for the simple purpose to attract more investors. More investors means bigger markets. Bigger markets means more cash money for the market makers. Technical analysis EXPLODED and new ideas were constantly being created. The more people followed the same patterns the more technical analysis became the foremost way to trade the markets. Candlestick charts, bollinger bands, cup and handle formations, inverted hammer sex positions are all examples of terms used by the avid technical analyst (Maybe I exaggerated on that last one, but tell me that doesn't sound like a sex position?)

To tape readers, the only two terms we really need to be concerned about are BID and ASK.

All the technical analysis in the world is just a simple recreation of price action (BID and ASK). Price action will always show you the way before any chart or technical indicator. That is a fact, not an opinion.

Alright Lucci, so how does one read the tape?

THE LOST ART OF TAPE READING PART 2- THE BID AND ASK

Folks, we continue this much anticipated series by bringing back another classic. This post breaks down the fundamentals that set the groundwork for this forgotten trading methodology.

'Bid' and 'Ask' are the two most important terms you'll ever hear a true tape reader talking about. Understanding these two basic tools will allow you to analyze what's happening on that Time & Sales so you will no longer assume it's just random numbers running down your screen.

So without further ado, let's get crackin'!

The 'Bid' is the best price you can sell your shares/contracts at this exact moment. Vice versa for the 'Ask', which is the best price you can buy shares/contracts at this exact moment.

Starting out at the prop firm, I always got the two confused and it took me a couple months to truly grasp what was going on logistically between the two. Normal rhetoric will describe the 'Bid' as the price that someone is willing to buy a security and that the 'Ask' is the price at which someone is willing to sell a security. Even the actual words themselves imply the action to be taken: 'bidding' suggests you want to buy whereas 'asking' or 'offering' implies you want to make a sale.

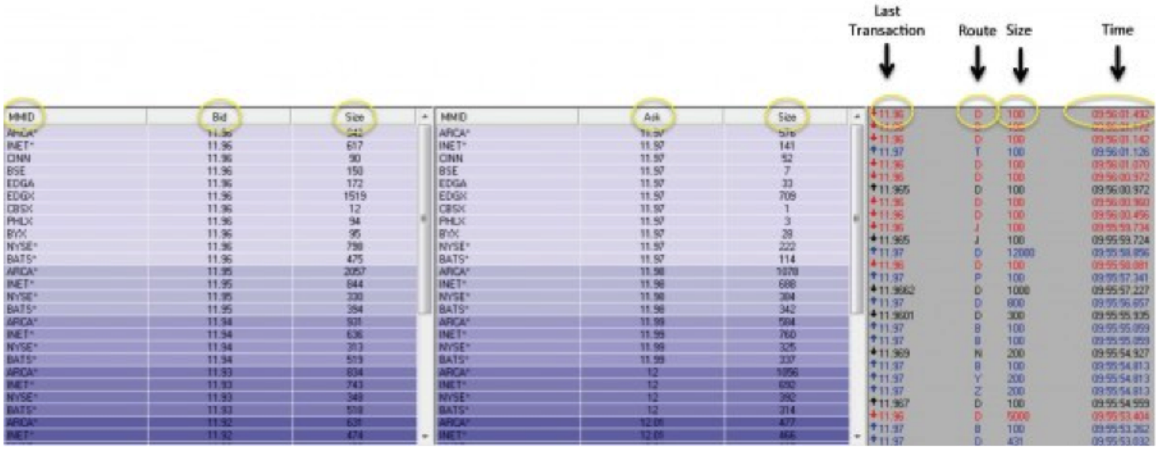
While this seems obvious to experienced traders, it added a lot of confusion to me starting out in this game. I remember sitting at my desk, staring at my screens looking at the 'Bid' and 'Ask' prices fluctuating sporadically and continually asking myself the question, **"So is that someone buying or selling?"**

I pride myself on explaining these instances so that all are able to understand and realize that this stuff really isn't as complicated as the books and teachers make it seem.

So let's paint a picture here to help assist you in understanding these tools of the tape!

First things first, imagine over a million people all at the computers right now placing orders for where they specifically want to buy or sell BAC. As one might suspect, these orders can range in prices from $10 all the way to $15. Realize though that at EVERY cent, there are buyers and sellers actively exchanging shares with each other. Every transaction holds a buyer and a seller.

Let's examine this Time and Sales data before delving into 'Bid' and 'Ask'...



- MMID- Market Maker ID. This shows what exchange the shares are being offered on.
- Bid Price - The price of the BEST bid. ($11.96)
- Bid Size – The number of shares at the BEST bid price. Keep in mind this is often times a collective number of all bids at this price. It's not necessarily one guy sitting at his computer wanting to buy 94,200 shares. (In the Time & Sales and Level 2, bids and offers are displaying omitting two zeros to save space so if you see 942 that means 94,200)
- Ask Price - The price of the BEST offer. ($11.97)
- Ask Size – The number of shares at the BEST offer. (57,600 shares)
- Last Transaction - The last price at which the most recent transaction took place ($11.96)
- Route- the route that was used to place the trade, using abbreviations (P=Arca, T=Knight).
- Size – The number of shares that exchanged hands during the most recent transaction (10,000 shares)
- Time - The time at which the most recent transaction took place (9:56:01:492)

Now, before you go bonkers on me check this out...

The last quote displayed above shows a 'Bid' of $11.96 and an 'Ask' of $11.97. Let's say you want to get active in this stock and buy it. You have two options you can either place an order to buy ('Bid') at $11.96 and WAIT for a seller to sell you their stock OR you can just buy the 'Ask' price at $11.97 and not have to wait. This is why I define the 'Ask' as the BEST price you can buy the stock for RIGHT AT THIS MOMENT. Placing bids is advantageous if you want to make sure you get a better price than just simply buying the 'Ask'.

This works vice versa if you want to sell as well. Let's say you own 400 shares of the stock and would like to sell your position. You can either place an offer 'Ask' at $11.97 and WAIT for a buyer to buy your shares OR you can just sell your stock to best 'Bid' at $11.96 and not have to wait.

The thing to realize here is that your limits may or may not get filled. If you want out of your 400 shares and you place a limit at $12.05 you must wait until the ebb and flow of the stock pushes it higher to your price.
Now that you understand the basics of 'Bid' and 'Ask', we're ready to talk about how to analyze and actually 'read' the constantly changing quotes and transactions in order to develop a theory as to where the stock will move in the future!

THE LOST ART OF TAPE READING PART 3 - LONG TRADES

Folks we continue this popular series by exploring some of the things you want to see on the tape if you are on the long side of a trade. This is an updated version of my previous post on the subject.

Alright lets get into it. If you find yourself long a stock, make sure you watch out for this stuff on the tape, it may help you out in providing even more conviction for your trade.

- **Look for large bids that step up.**
  - For example, if you are in Apple (AAPL) and see a 100K bid that shows up. Buyers step in front of that bid and you see that bid periodically moving up with the stock. This could mean that buyer is aggressive, wants more stock, and is willing to pay for up it.
- **The majority of transactions are going off on the offer price. ('Ask')**
  - You want to see people buying immediately and not waiting for their bids to get filled. You basically want to see them saying, '"Screw it, I want to buy and I don't care what price I get it at." People buying on the offer are saying they are willing to sacrifice the price difference between bid and ask in exchange for immediately getting into the stock.
- **Level 2 is 'thin' on the offer.**
  - This means that if you took a glance at your Level 2 as far down as you can go, you don't want to see too much size (resistance) all the way up. For example, you don't want to see GIANT offers that will possibly hold your stock down. You want your long to go as smooth as possible with the least amount of complications on the way up!
- **Lack of down ticks**
  - Down ticks suggest selling on the bid. That means that sellers are aggressively exiting their positions instead of letting themselves get taken out at the offer price (where they would make more money in their exit). Down ticks create downward pressure on the price of the stock.
- **Futures (SPY) pushing higher**
  - The level of correlation between the S&P 500 (SPY) and large cap stocks has only increased in the last few years. For certain sectors, it can be as high as 90%. That means the SPY will be a very good indicator of where your stock is likely to go. If the SPY starts dropping, you better have some good arguments to stay in the trade. Otherwise, consider dumping that long position.
- **Controlled pullbacks**
  - You need to see buyers holding run-ups. If your stock goes up $.60, you want to see the sellers UNABLE to push the stock lower. During pullbacks, you don't want to see your stock dropping quickly. You

want to see evidence that heavy buying activity is still present. This will most likely result in second or third legs higher.

- **Higher highs**
  - Buyers should be unafraid of new daily highs. A stock that slows down at it's highs may mean buyers are unsure and it's time to take your profits.
- **Large Prints**
  - If you're seeing big transactions sizes go off on the offer and resulting sweep ups, chances are you've found a buyer that means business. He might be marketing large orders to get in to your stock and it's important to watch for continuation of that similar activity going forward.

Every situation and every stock is different. These are simple guidelines, however, that you should always keep in mind if you're long a stock!

HE LOST ART OF TAPE READING PART 4 - SHORT TRADES

It's been almost a year since I wrote the last part to this series and with the introduction of our educational tape reading/options class, I've decided to bring it back for further exploration.

Ironically, price action analysis is starting to resurface from increased scrutiny of algorithmic trading. People are now trying to fully understand the ways that high-frequency trading affects equity prices on a second to second basis. Unfortunately, if you're looking at your charts, the only HFT you visually experience is the news algorithms that cause large spike-ups or spike-downs off of breaking news. Or you may see flash crashes in sporadic names at random when there has been no fresh news issued on that security. HFT goes way beyond what you view on your red/green candlestick charts.

On the tape, you'll watch HFT's decrease or increase liquidity within fractions of a second by pulling back bids or offers. You'll watch large orders influence buyers and sellers for a short period of time and then cancel soon after. You'll see manipulation of equities by order-execution algorithms or large hedge funds needing to achieve certain prices for buy or sell orders.

Of course, if you don't know how to decipher your time and sales, then you won't be able to follow the footprints of the larger players. Large funds buying or selling is what moves equity prices and if you can understand their digital signatures, you might just find that edge you've been looking for.

Trackers are known in the wild for their unique ability to find and follow trails & correctly read their surroundings. Modern tape readers are, in essence, using similar principles to properly analyze their environment.

So let's continue where we left this series by delving into the short side and what you basically want to watch out for on the tape when you're in a short trade.

- **Look for large offers that step down**
    - A large trader or fund that needs to clear out of a large position will try everything they can to hide their true intentions. But often times you will see a large offer come into the market and then people sell right ahead of that offer, forcing the big seller to get aggressive in order to dump their shares. As a result, you may see that big offer slowly step down. For example, you see a 200K share offer at $550.24 and 20 minutes later that same size offer steps down to $549.40. That's an aggressive seller that wants out.
- **Transactions are going off on the 'bid'**
    - You're looking for motivated sellers. You're looking for people who want to get out of their positions and they don't care what price they get filled at instead of waiting for their offers to get taken out by potential buyers. Ideally, you're looking for panic.
- **Level 2 is 'thin' on the 'bid'**

    - When you glance at your Level 2 while short a stock, you don't want any unforeseen obstacles that will block your path to riches. In order for a stock to go down in price, you must have increased supply over the current demand. You're looking for liquidity to dry up on the bid side because buyers are bracing for a pullback. You also don't want to see any large bids standing in the way and keeping the stock up.
- **Lack of upticks**
    - You don't want to see increased buying activity when you're short a stock. Remember, the daytrading game is all about timing and if you want to have successful trades, you must be able to feel around correctly for the right timing. If you do see upticks, make sure they're few and far between.
- **Lower lows**
    - You're looking for your stock to continually make fresh lows and hold previous lows on the downside. You don't want to hold a short position on a stock that rallies back through previous support levels. This makes your trade much more difficult to hold.

Again folks, these are just simple things to look for when you're trying to make sense of the time & sales. To most, the transactions that fly down your screen look like the Matrix, a cryptic feed that only certain people can decipher. You'll find out soon enough though, that market makers, institutions and large traders all have unique footprints which can only be tracked through the tape.