Easy Ways to Increase Your Portfolio Return

5 Trading Tools to Make More Money

Learn the tactics and techniques to trade more effectively.

It's being called the "lost decade," but somehow that's still an understatement, particularly for investors. With the market today essentially where it was ten years ago, buy-and-hold stock owners are now a decade behind on the growth they expected. Indeed, that lack of growth these investors were counting on to pay for a college education, or even start retirement, wiped out the dreams such growth should have brought.

That's not even the most agonizing part about the last ten years, however. The most painful part about the lack of net progress we've seen from the market since 2000 is that the opportunity for progress was there - if you knew how to take advantage of it.

During that time, the market fell 45%, rallied 87%, fell 52%, and then rallied 49% again. Each of those major moves was a trade-worthy trend lasting for months and could have potentially meant net progress of up to 233% for portfolios of investors who just knew how to spot and tap into those moves. Moreover, being able to spot and trade the interim trends – both bearish and bullish - would have further enhanced a trader's total gain for this ostensible "lost decade."

Is this just a mere history lesson at this point? Not quite – this horror story doesn't end there. The really scary chapters of this tale are the reality that the next ten years could be as stagnant as the last ten in terms of total progress. Two back-to-back "lost decades" are a distinct possibility and **buy-and-hold proponents simply can't afford to take that chance.**

The solution (and likely the only one for a while) is a more pro-active approach. Call it active investing, trading or anything else you want but it's all the same – taking advantage of the meaningful opportunities when they present themselves and locking in gains at the right time before the inevitable reversal.

The bottom line is that buy-and-hold is dead until further notice - active investing is now your best bet for actual wealth building via the equity market.

For those who have already tried it, you'll know it's not an easy game. The key to success, however, isn't necessarily tons of experience or more information. **The key to success as an active trader is using the right tools, whether you're a rookie or a seasoned veteran.** Indeed, such "seasoned veterans" were able to reach that status by using the right tools.

And here's the really interesting part….the "right tools" aren't necessarily the most common indicators you'll find in your charting software or your stock screener - at least not when used in the conventional way. Some of these tools aren't even indicators at all.

Rather, top traders put a new spin on the old (and sometimes less-used) indicators, and they have a fierce adherence to a proven, disciplined trading plan. The net result is a trading system that allows its owner and user to (1) find big opportunities before anyone else does, and (2) stick to that proven plan when the market is trying to lure other traders into a trap.

With that in mind, here are the four top trading tools plus three key disciplines that traders and investors should master if they want to get the most out of the market over the next ten years. And frankly, given the last ten years, nobody can afford not to learn them.

After you've reviewed all seven lessons, be sure to review the last section where we drive home some powerful realities that can solidify your trading success.

Tool #1 - Acceleration Bands

Most momentum-based indicators are significantly flawed in at least one way. They can spot a trend's direction and most of them can even spot a new trend once it's set into motion. However, in the current market environment particularly, too many trends are already slowing down by the time you finally get that momentum-based trade signal.

Said another way, **the best trade-worthy trends are entered at the point of acceleration,** even though finding the point of acceleration is something these tools were never designed to do. That is, all of them save for one.

Subscribers to our free, as well as our premium, newsletters will occasionally hear us talk about Price Headley's proprietary Acceleration Bands. These bands are a technical indicator that spot growing momentum in its early stages to define the top 5% of big trends where fortunes can be made.

Acceleration Bands are especially useful in highlighting strong trends in emerging market and commodity ETFs. At first glance, BigTrends' Acceleration Bands may look like Bollinger Bands, surrounding a stock or index chart with an equidistant boundary above and below. That initial assumption isn't far off base – Acceleration Bands do indeed surround a chart's price bars.

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Other traders may decide that Acceleration Bands behave like a moving average envelope and again, that basic assumption is a starting point.

However, **our Acceleration Bands eliminate the problematic volatility of Bollinger Bands yet are more responsive than a moving average envelope.** In other words, the downside of each of the other tools is negated, while the upside of each is retained.

It's a simplified explanation, but the acceleration-spotting ability of this tool is tremendous - a perfect mix of an overly responsive indicator and another that's not responsive enough.

The best use of this tool is as a stock search tool - look for consecutively higher closes above the upper band or consecutively lower closes under the lower band.

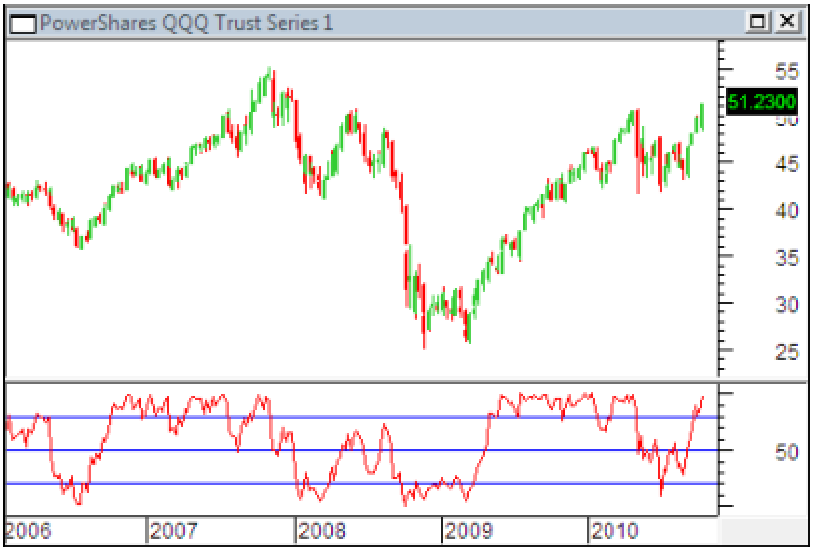
Tool #2 – Williams' Percent Range (%R)

Developed by famed trader Larry Williams, the Williams' %R indicator has been well-accepted by the trading community, but hasn't necessarily been widely used.

While its function as an oscillator isn't unclear, it has been considered a little too complicated and erratic relative to the comparable stochastic indicator and the RSI indicator. That doesn't mean it's not a top trading tool though. In fact, BigTrends has found the %R tool to be a highly effective aid **when interpreted in a particular way.**

As is the case with most oscillators, we prefer the %R indicator to be plotted on a 0 to 100 scale (low to high), or alternatively, you may also see it plotted on a 0 to a -100 scale (high to low). However you use it, when the plot line is at the extreme ends of the scale – usually the upper and lower 20% – the security or index in question is overbought or oversold. And, like most oscillators, an overbought or oversold condition usually sparks the belief that the chart is ripe for a reversal.

Despite its lack of popularity, the Williams %R tool has generally proven to "make the turn" before the underlying stock or index does, with minimal fake-outs. It is therefore quite surprising that the trading community hasn't adopted the tool more aggressively. Perhaps the plot line is simply too erratic in appearance for traders to trust its signals.



With one small tweak, however, Price Headley has found a way to take full advantage of the power of Williams' %R, while simultaneously weeding out many of the fake-out signals. We call it the %R Retest Method and you'll sometimes hear us refer to it an additional term known as the **"bend but don't break" strategy.**

We also use the Williams' %R indicator in the exact opposite way of its conventional use, buying into persistently overbought charts, and selling/shorting persistently oversold charts. And this tactic works far better than the standard use of the %R tool.

The market is always pushing back on trends - something of a litmus test. The strongest trends survive these tests while the inferior ones don't. When the %R indicator "should" signal a reversal but doesn't (and if the trend in question remains technically intact), then the renewal of the %R overbought/oversold condition is actually a buy/sell condition, respectively.

Subscribers to our coaching programs have access to the full details of the trading system, but you get the idea here - the best of the best (the most trade-worthy) trends are those that stay overbought or oversold for long periods of time.

When the %R indicator does so while the price trend doesn't come unraveled, we don't bet on reversals – we bet on a renewal and continuance of that trend.

<u>Tool #3 - Efficiency Ratio</u>

Some of you may know the "Efficiency Ratio" as a Perry Kaufman invention. Price Headley's version of the Efficiency Ratio is built on Kaufman's idea - the aim is to find stocks that are making the most of their time and day-to-day movement.

Plenty of stocks move higher or lower, and are technically trade-worthy as a result. However, you want to limit your trades to charts that aren't wasting time or momentum. A higher (or lower, in bearish cases) Efficiency Ratio allows you to find those "best of the best" trades.

Let's start at the beginning though, just to make sure we're all on the same page.

Like most oscillators, the Efficiency Ratio is plotted on a static scale. The Efficiency Ratio's scale is from -1.0 to +1.0 (or from -100 to +100, depending on the charting software).

Readings under the -30 mark tend to mark very strong bearish

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trends, while Efficiency Ratios scoring above +30 tend to accompany highly bullish charts.

But how does an Efficiency Ratio get to – and stay – at those levels?

The Efficiency Ratio is calculated by dividing the net change in a stock's price over X days by the sum of all the day-to-day price changes over those same X number of days.

For example, if we were to plot a 10-day Efficiency Ratio of a stock that made gains every single day over a ten-day stretch, that Efficiency Ratio would be 100% which is a very strong trend indeed (though that never happens in the real world).

As for the mentality of an Efficiency Ratio interpretation though, the smoother and more reliable the trend is, the greater or lower the Efficiency Ratio. Efficiency Ratio readings around zero indicate a lot of inefficiency - typically more choppiness than is worth trading.

Tool #4 - Use "Closing" Stops

If it seems like the rest of the market is standing over your shoulder and knows exactly where your stops are – and pushes a stock just far enough to trip you out of a trade – you're not paranoid as professional traders can "see" where other traders' stops are. While they may not bother trying to stop you and only a few other smaller traders out of a stock (and turn your loss into their gain), if many traders have set the same stop-price for a widely-held equity, you can bet there's a pro looking to shake you out of a loss. How? By pushing the price against you just enough to trigger your stop.

The solution is simple… if at all possible, don't use "hard" stops.

For some this is simply not feasible, as regular "day jobs" or other commitments may not allow you to monitor your trades on a continual basis during trading hours. In those cases, it may be best to stick with very large stocks that can't be pushed around by professional traders (or to the extent possible, only trade stocks that have little to no history of such wild swings).

An alternative might be to set very wide stops. Here, you'll be taking on a little extra risk but can be confident that you'll not be easily shaken out of a trade. Conversely, you could set very tight stops, which limits losses to absolute minimums, but may create more trading activity than you'd like.

Both will work, but neither is ideal. Ideally, if at all possible, hard stops should be avoided and stocks should be monitored at least occasionally during the day.

There's a nice twist to the rule, however, that not only circumvents the inherent problems with stops, but also doesn't require you to stare at a trading screen all day long.

Though it requires a little more effort, a "closing" stop is the ideal way to protect yourself without showing your hand to the market makers.

Have you ever noticed that the last 20 minutes of the trading day are often the most volatile phase of the trading session and where most of the daily net changes materialize? That's because by 3:30 pm EST or so, professional traders and institutions are unwinding their day trades or making overnight commitments to positions that they're willing to start with the next day. Needless to say, this means the last price of the day is also the most meaningful one as it is reflective of what the aggregate market ultimately thinks of a stock.

With that in mind, a "closing" stop isn't an actual, physical stop price for a stock. Rather, it's a mental-only stop that exclusively applies during the last 15 minutes or so of the trading day – when the most important pricing of the day occurs.

This approach accomplishes two goals. One, it prevents you from being knocked out of a trade by all the meaningless (and temporary) intra-day noise, and two, it only requires you to interrupt your day for a few minutes around the closing bell.

Almost all of our services use the closing stop idea and we've found it to be an enormously beneficial technique.

Tool #5 - Never Let Your Total Unrealized Stock Losses Exceed 30%

You've probably heard the adage "never let a small loser turn into a big loser." Consider this a specific methodology to put that idea into action but also a methodology that offers the trader some flexibility about what he or she boots or decides to hold.

As the rule stated plainly, never let the sum total of all the unrealized losses in your stock portfolio exceed 30%. This means you can let six trades all sink 5% before you pull the plug on any of them. Once one or more sinks 6% though, the rule says you have to bail out of at least one.

This rule also gives you the option of letting three stocks dip into the red by 10% each without being forced to dump one. If one of them should move to an 11% loss though (for a total of 31% worth of losses), then one should be cut loose.

Obviously there are several combinations of losing positions that can reach that 30% threshold, but you get the idea – once the total risk to the portfolio reaches that threshold, defense is imperative.

Just to be clear, the net gain (sum of all gains minus the sum of all losses) of the portfolio at any given time doesn't play a role in this defensive rule. This is simply a way of disciplining yourself to dump losing trades before they damage your portfolio and detrimentally affect your proper trading psychology (nothing can wreak havoc with an otherwise-smart approach like seeing too much red in your portfolio at any point in time).

The nice part about this rule is that it gives you the flexibility in choosing which losers you want to keep holding, and which ones you want to dump.

This 30% rule of thumb has worked well for us with stock portfolios but with option portfolios – which tend to be more volatile – we have to be a bit more tolerant of losses before we start shedding the weakest trades.

Whether you're a stock trader or an option trader, you should decide on a similar 'total loss' rule of thumb that works best for you, in your given situation. Over time though, we've found the above allowances to be the right risk-control balance.

Turning Ideas Into Action

As we mentioned early on in this report, there are a few key trading realities that may seem simple on the surface but are powerful at the same time (and part of too few trading approaches).

The four tools and three disciplines need to be explained first though, as they are the means with which one can act on these key philosophies. In no particular order, here are the core principles adopted by top traders (and the ones specifically not adopted by weak traders):

• Find low risk entry points: If you're using the news or if you're using the most common and most conventional technical indicators to find stock trades, then here's some bad news - you're buying leftovers. In other words, you're trading trends that have already exhausted the bulk of their useful life and, if anything, you're stepping into a trend at its riskiest point. Seek out low-risk entry levels flagged by successful retests (like our %R technique spots) or emerging momentum (like our Acceleration Bands find). The Efficiency Ratio also specifically finds low-risk trades by spotting the strongest trends.

• Never lose big: It may be a cliché but that doesn't mean it's not good advice. However, it's easier said than done as traders just don't know how or when to cut a losing trade loose. By defining a specific closing-stop, and implementing a "total net loss" rule, it should be easier to avoid letting small losses turn into big ones.

• Have a specific plan: Even a mediocre plan is better than no plan at all. With a plan, at least you have a disciplined and specific approach you can execute and evaluate. If you're flying by the seat of your plants, you'll likely chase trends (rather than find your own new trading setups), and you'll stick with losing trades for too long (rather than cutting bait).

• Don't get emotional: Gordon Gecko, from the movie "Wall Street," may have been a scoundrel, but he was right about one thing - you shouldn't get emotional about stocks. Unfortunately, without confidence in your offense (stock picking indicators) and your defense (trading rules that inherently limit losses), a logic-skewing and reason-skewing emotional response is very likely.

It's This, or Nothing At All

To reiterate a point made early on in this special report, anyone can become a great trader. In fact, if the next ten years is anything like the last ten – and that's very likely – then all of us will need to become great traders.

And to repeat something else we already mentioned - becoming a great trader isn't a matter of experience or intelligence. It's a matter of using the right tools.

We've introduced seven of them today - four specific indicators and three clear rules which should put you well on the path to trading success. Frankly though, we've only scratched the surface. Tools come in many forms, such as our option-trading newsletters, our market timing updates and our coaching classes (where we really dive into the details of the concepts discussed above).

The question is though - can you financially afford for the next decade to be another "lost decade?"

With the real estate market still down for the count and with tax hikes on the way to finance a massive deficit, it will not only be difficult for you to grow wealth via a salary but it will be difficult for corporations to run the kinds of profitable operations that will actually drive stock prices higher - the kind of progress the buy-and-hold crowd is unwisely hoping for. There should be lots of up-and-down volatility and tapping into it may well be the only route to a bigger account balance by the time 2020 rolls around.

You can do it. You just need tools and methods that work.

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Trade well!
Price Headley and the BigTrends Staff