AFRAID to TRADE
overcoming stock market fears with Corey Rosenbloom

Daily "Idealized Trades" Report

SPY (SPY 500 ETF) 5-min

What a day! The day before a Federal Reserve announcement has a tendency to be choppy and range-bound, as the market pauses in anticipation of Wednesday's announcement - which could swing the market violently (as do many "Fed Days") in either direction. Funds tend to balance out prior to these announcements, which contributes to the choppy nature of days before 'Fed Days.' As a general statement, "Range Days" are inefficient days, in which you can sometimes trade actively, feel like you're spinning your wheels, and even if you manage to make a profit on these difficult days of win some, give some back, the profit is often not worth all the work and stress and frustration it took to get it (especially when compared to trend days). Remember that trading tactics on Trend and Range days are diametrically opposite - which is why many traders struggle - they use the same strategy every single day, which works in only one environment... as I've been describing here.

For Range Days, the strategy is to be a "fader" and watch for reversal candles and divergences at the Bollinger Band extremes for trade set-ups... and to avoid trying to use the moving averages as support or resistance (or targets/entries). Let's start by walking through the day.

GAP FADE

The first trade of the day was a simple and effective gap fade of another 50 cent SPY gap that began with a 'doji-like' candle and only contained one down bar all the way up to the target of $104.30 (entry on second or third five-minute bar with stop under the intraday low near $103.60).

Not all gap fades are as nice as this one - as yesterday's gap showed us with a gap fill miss after a 50% gap fill occurred (before rising to take out the stops). Remember that the larger the gap, the lower the odds of filling.

'FADE THE FILL' UPPER BOLLINGER BAND, NEGATIVE MOMENTUM AND TICK DIVERGENCE

Successful gap fades can give us a second 'edge' opportunity in that we trade back in the direction of the gap if we start to see price weakness (in this case) or overhead resistance (ie bearish divergences, bearish candles, upper Bollinger Band).

In this case, we had a new price high that ran into resistance from the swing high into yesterday's close that also formed a negative TICK (when compared to that swing high) and momentum divergence that formed at the upper Bollinger Band. This was a high confluence trade short with entry as soon as price began to fall from $104.50 and stop above $104.60/70 with target of the lower Bollinger Band or a retest of the intraday low of $103.60.

Price fell quickly over the next 30 minutes, but fell around 5 cents shy of the lower Bollinger Band target at $103.70 before price formed a strong bullish engulfing bar. Remember not to use moving averages as targets, as price continually 'sliced' up and down through them as if they were not even there.

By this time, we could have been suspecting that the day favored a "Range" day bias and looked to see if there would be any future moves outside the first hour's range. If not, then odds favored a Range Day.

Price then rallied in two bars back to yesterday's close at $103.30 which was just shy also of the upper Bollinger Band at $104.50. Price formed a shooting star candle (see TradeStation chart) beneath yesterday's close which was an aggressive short-sale trigger (not enough confluence for conservative traders to enter short).

SPINNING TOP, LOWER BOLLINGER BAND, RETEST OF LOWS

As price fell just prior to the 12:00 EST lows, a spinning top / doji-like candle formed with lower shadows that pierced outside the lower Bollinger Band. If you happened to be looking at the 1-min chart at this time, you would have seen a lengthy positive momentum divergence had formed also on these lows.

Combined, this gave us a buy signal with entry near $103.75 and stop under the intraday lows under $103.60 with target of a retest again of the upper Bollinger Band or yesterday's close at $104.30 - both of which were hit successfully on a quick impulse up that only endured two down bars.

BULL FLAG, TRENDLINE BREAK, 'IMPULSE BUY'

Price pierced again outside the upper Bollinger Band just prior to 1:00pm, giving us an "exit longs" signal and an aggressive 'short sale' signal... which was muted (less probability) due to a new TICK and Momentum High (possible Wyckoff Sign of Strength... which later proved to be the case). Price also moved outside the opening range.

After a new price, momentum, and TICK high, we want to be a buyer of the first pullback - which I call the "Impulse Buy" Trade - because odds - under the principle "Momentum Precedes Price" favor a higher price high yet to come.

Price began to form dojis at the $104.20/$104.30 level, which happened to be the support zone of yesterday's close, and the rising 20 and 50 period EMAs (which have less sway on Range Days, but if price began to support off these zones, it would hint that the structure was shifting into a more bullish posture).

Price broke above the descending trendline that made up the bull flag at 2:00 EST, giving an official entry into the 'bull flag' trade which rose very quickly to new intraday highs (as hinted by the new momentum high) and then reversed course with a bearish engulfing candle at the upper Bollinger Band. This was both an "exit long" trade and an aggressive "short sale" trade, given that a doji formed (along with more long upper shadows) after the bearish engulfing formed at the intraday highs.

BEARISH ENGULFING, DOJI, UPPER BOLLINGER, NEGATIVE TICK AND MOMENTUM DIVERGENCE

As price expanded to a new intraday high at $104.80, price formed a bearish engulfing candle at the upper Bollinger Band which also corresponded with a negative TICK and Momentum divergence - a glaring non-confirmation of the new price high (remember divergences are important signals on Range Days). The entry would be as close to the doji or upper Bollinger Bands as possible with a conservative target being the 20 or 50 EMA (in the event that the structure had shifted bullish) or aggressive back down to the rising Bollinger Band... which indeed was the case. The fact that price ignored (did not support on) the moving averages was further evidence that a range day was favored.

TWO DOJIS, LOWER BOLLINGER BAND TEST

Under the same logic, any test of a Bollinger Band extreme - especially when dojis form - is a trade set-up. The stop would be under $104.10 with target - again - the upper Bollinger Band (or market exit on close if you decided to trade into the close). Price fell a few pennies shy of the upper Bollinger (remember, we're not trying to be greedy and capture every single penny of a price target. Don't let a few hundred or thousand dollars turn into a loss just because you had to hold on for the final few pennies). Range days are difficult enough without expecting perfection in price targeting.

New TICK and Momentum Highs at 1:00 EST served as a possible Wyckoff Sign of Strength - buying the first pullback was a good trade. The new high formed a divergence, and the range day continued, though with an upward bias.

The 1-min chart always helps confirm structure and possible turning points (through divergences) that we're seeing on the 5-min chart.

Breakouts from trendlines can serve as trade entries as well, particularly for conservative traders waiting for confirmation of possible reversals (instead of trying to be aggressive and buy the low or high ticks).

Technical structure will take a back seat to the reaction of the market participants of tomorrow's Fed Day. It's perfectly acceptable for new traders to stand aside tomorrow, though more experienced traders do enjoy the price swings - usually a three-wave volatile movement - after the announcement is made at 2:15 EST. Expect price to consolidate tightly in the hours prior to the announcement, and be ready to trade off the open if we get a gap tomorrow.

Fed Days can lead to Trend Days, and they can be quite volatile.

Looking at price structure - watch the $104.75 level (confluence of 50 EMA and upper Bollinger) for a resistance breakout, and watch $104.00 for a breakdown of a possible flag/lower trendline pattern that has formed on successively lower volume (non-confirmation).

The bias is to the downside as long as price is under $104.00 (1,040 in the S&P 500) but again the market can react strongly to the Fed Decision.

Here is a copy of the prior Day Before and then Day Of Fed Decision of September 23, which gave a sudden surge after the announcement... and then equally as sudden and devastating sell-off after traders 'digested' the report.


SPY - 5 min ARCX 11/03/09 L=104.65 0.33 0.32% O=103.74 Hi=104.80 Lo=103.54 C=104.65
Day Before: Flat
Before: Flat
Announcement
Violent Sell-Off that blindsided many traders
$TICK - 5 min NYSE 11/03/09 L=887.00 170.00 23.71% O=-55.00 Hi=1208.00 Lo=-1078.00 C=887.00
9/22
10:00
11:00
12:00
13:00
14:00
9/23
15:00

Daily chart shows price under the 50 day EMA... though potentially bouncing off support from the lower Bollinger Band.

Tomorrow should clue us in as to whether to expect support... or resistance... to hold.