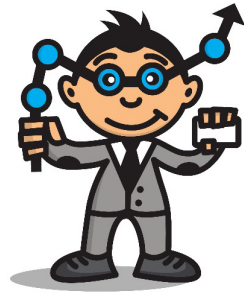




TRADE CONTEXT

**YOUR GUIDE TO BECOMING
AN EXPERT DAY TRADER**



TRADE
CONTEXT

TRADE CONTEXT

YOUR GUIDE TO BECOMING AN EXPERT DAY TRADER

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Trade Context, January 1, 2017

ACKNOWLEDGMENTS

I want to quickly thank Marcello Arrambide, CEO of DayTradingAcademy.com, and Morad Askar of Stage 5 trading, both have given much of their time to teach me how to trade over the years. One, I know well, the other doesn't know I exist, but that doesn't matter. I have made both of their strategies my own and this free book is my way of paying it forward.



INTRODUCTION

I have good news for you... If you have made it this far, you are WAY ahead of most people... You probably ended here because you want to take charge of your future. It doesn't matter whether you are 16 years old or 60, you CAN make a living from day trading. If you think you are going to get rich overnight, throw that thought away RIGHT NOW. If you want to put in a little bit of work for EXTRAORDINARY returns, then keep reading. I will not waste any of your time, read on I will get you started on the path to success.





WHO AM I? AND WHY SHOULD YOU LISTEN TO ME?

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My name is James Sixsmith and I was once a pretty good ice hockey player. Although I still play professionally at the time of writing, every athlete knows there will come a time when you are replaced with younger talent. Therefore, I knew I needed a way to secure my future. Five years ago, I decided that I would learn how to be a day trader; so that when my hockey career ended, I would still be able to enjoy the freedom I had become accustomed to.

I got my start with Daytradingacademy.com. The founder and CEO Marcello had a program with impressive testimonials, and I was hooked. Marcello lit the fire under me, and I took off from there. I made his strategy my own by keeping the fundamentals, while changing a few things to make it more...ME.

I can tell you that I have failed so many times in trading that when I look back, I don't know how I had the nerve to keep getting up and trying again. I have blown a few accounts (both before and after I became profitable) and spent many hours struggling to understand how and why the market moves like it does.

Then something happened...I found a system that allowed me to organize the market infor-

mation in a way that I could use what I learned with Daytradingacademy.com to make trades with a strong hand. I no longer had to reluctantly click the mouse when I took trade. I knew it was not going to work every time, but I was onto something I could rely on for CONSISTENCY. If I had an edge over the long term, I was going to make money; it was as simple as that. This was no magic system or a holy grail, but the synergy of the two gave me an edge over other traders. When I dissected my performance, it was obvious that the reason that I had done well some months and poorly others was simple; I was trading with a set of rules but didn't know when to break the rules and when to follow the rules. This probably sounds familiar to anyone who is currently frustrated with their trading. In short, I just never felt comfortable (even when I was doing well) with a mechanical system in a dynamic market. It just felt wrong to me. So, I shifted from thinking, "If the market does this, I do that," to "the market will **most-likely** do this based on what it has done so far today." When I made this change, I went from being an average trader to a really good one. I have made money ever since, and that's all that really matters in trading. No, I don't make a million dollars a day. In fact, I have some losing days here and there. If a trader tells you he/she doesn't

have losing days, well...you probably already know what to do.

This is where YOU come in... Let's be honest, you probably don't give a damn about my back-story, and I don't blame you. You just want to make money, right? Great, there is a lot of money to be made in this field, by people just like you. In fact, there are many reasons why YOU should strive to become a day trader. Whether you have a job that you want to ditch, you don't have a job at all, or you simply want to make some extra money so you can travel and spend more time with your family, day trading can help you achieve that. Above, I raised the question, "Why should you listen to me?" The answer is simple; I can change your life. Reading this book is not going to offer an improvement to your life, it's going to change your life. If you're an existing trader, I'm going to challenge you to think differently, so you don't just improve your trading, you *transcend* your trading.

Before we actually get into setting everything up for you to get started, I would like to quickly discuss a few terms that are essential to understand. If you are a seasoned trader and already know these things, you can skip ahead to the platform setup.

WHAT IS A DAY TRADER?

Here at Trade Context we are intraday futures traders. This means that we make trades during the day and RARELY hold positions overnight. Intraday trading does not necessarily mean that we are scalpers (the term for a trader taking aim for small profits on each trade), it just means that we like to do our business during the day. Margins are higher overnight (you must hold more money in your account), and I have found it much more difficult to predict the market overnight when the markets are subject to geo-political events that can effect it. All it takes is one news event to ruin a big account. Sure, these events happen from time to time during the regular trading hours, but at least we are able to close positions since we are awake, and watching the market.

WHAT ARE THE ADVANTAGES OF BEING A DAY TRADER?

The reason many of us are drawn to day trading is the freedom. Financial freedom and the freedom to come and go as you please, which includes spending less or no time at work, more with your family, etc. are the two most popular reasons I hear from my students. The great thing about day trading, is when you get to the point of profitability, you only need to spend a few hours a day to make a pretty good living. If you want to put in more time you can make more money, but it is not necessary to put in consistent eight-hour days.

WHAT ARE FUTURES?

The futures markets that we see today, is a product of decades of dealing with the age-old problem. How can merchants or producers protect themselves against large changes in price to their particular commodity? The futures market solved this problem by allowing farmers, or anyone selling a commodity, to sell their products at a certain price at a specific time in the future.

A futures contract is a contract between the buyer and the seller who agrees to buy or sell a commodity or the underlying asset at a price but delivered and paid for, at a future date.

While futures trading originally began with commodities such as grain and wheat, they have now advanced to include currencies (euro, British pound, yen, etc.); indexes (S&P 500, Dow Jones, Nikkei 225, etc.); precious metals (gold, silver, platinum, etc.), besides commodities such as crude oil, grain, wheat, livestock and so on.



HOW DID FUTURES TRADING START?

Dojima Rice Exchange
(Courtesy: Wikimedia)

The world's first formalized futures exchange was formed during the 1730s in Japan, called the *Dojima Rice Exchange*, which dealt with forward contracts only, but there was no third-party to ensure fairness. Around mid-1800, the Chicago Board of Trade (CBOT) was set up and the first forward contract in the U.S. was written on 13 March 1851. The CBOT acted as the exchange or the third-party to ensure the contracts' obligations were met by the buyer and the seller (*dealers and merchants*).

Once a futures contract was struck, the buyer of the contract would hold it until expiration, where in the seller of the contract is obliged to deliver the quantity of the commodity that was agreed upon.

As the primary market participants grew, so did a new breed of traders known as *speculators*. While dealers and merchants dealt with actual delivery of the underlying commodity, speculators traded futures contracts to take advantage of the volatility in prices. Speculators are not interested in taking delivery of the commodity; they tend to sell their contracts before it expires to avoid receiving the commodity.

WHAT ARE INDEX FUTURES?

Index futures are contracts that track the prices of the stock index such as the S&P 500, Dow Jones 30, the NASDAQ 100, and so on. The problem with the index futures at first was the contract value only allowed large players to participate due to the high cost for holding contracts (hundreds of thousands). To combat this problem, the "E-Mini" contracts were born. Unlike a stock or a commodity, a trader is not purchasing anything "real" when they buy an E-Mini futures contract. The trader is simply speculating on the price to go up and down. The E-Mini market only exists because we say it does and one trader is willing to bet on it going up, while the other is betting on it to go down. The E-Mini's are only traded electronically, and that was the case even when the trading pits still existed.

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Here is a chart of the ES futures contract.



Example (ES futures) E-Mini S&P 500 futures chart

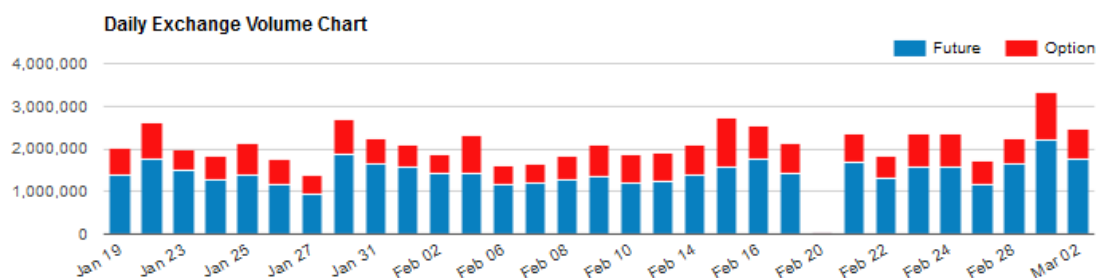
THREE REASONS WHY ES FUTURES CONTRACT ARE SO POPULAR

Among the different index futures contracts, the E-Mini SP 500 (symbol ES), are the most popular.

Here are three reasons why!

1. ES FUTURES HAS THE LARGEST VOLUME

The E-mini S&P 500 futures contract boasts of having the largest trading volume. On average, there are 2.2 million contracts traded every day. The beauty of trading markets with heavy volume is that our orders are executed at precise prices on most occasions.



ES Futures Daily Trading Volume (Source: CME Group)



2. ES FUTURES ARE BEST SUITED FOR DAY TRADING

Futures day traders love E-mini S&P 500 contracts because it moves fluidly. Some futures come to mind that trade very erratically at times, such as gold and crude oil, making them much more difficult to trade as a day trader. On the other hand, the ES is great to day trade because it's harder to get "caught" on the wrong side of the market. With so many participants in the ES, it is very difficult for a move to surprise you and take all of your money. Further-

more, the predictability that comes by trading a high volume (also known as a "thick") product like the ES, makes the path to profitability much easier. As you can see from the chart below, the E-Mini S&P 500 is also leveraged 50 times the regular cash index. This means that a one-point move in the Index is equal to \$50 in futures. Therefore, we don't need crazy fluctuations in the market to make a living day trading.

Name	E-Min S&P 500 Futures Contract	Ticker	ES
Contract Unit	\$50 x S&P 500 Index	Tick Size	0.25
Trading Hours	SUN - FRI: 1800 - 1700 ET (break: 1600 - 1615) MON - FRI: 1700 - 1800 ET	Tick Value	\$12.50

3. ES FUTURES TRADE (ALMOST) AROUND THE CLOCK

Unlike the U.S. stock market trading hours, the E-mini S&P 500 futures trade nearly around the clock, therefore it has a broader appeal as it attracts international traders (not just traders based in the U.S.) and you can day trade with

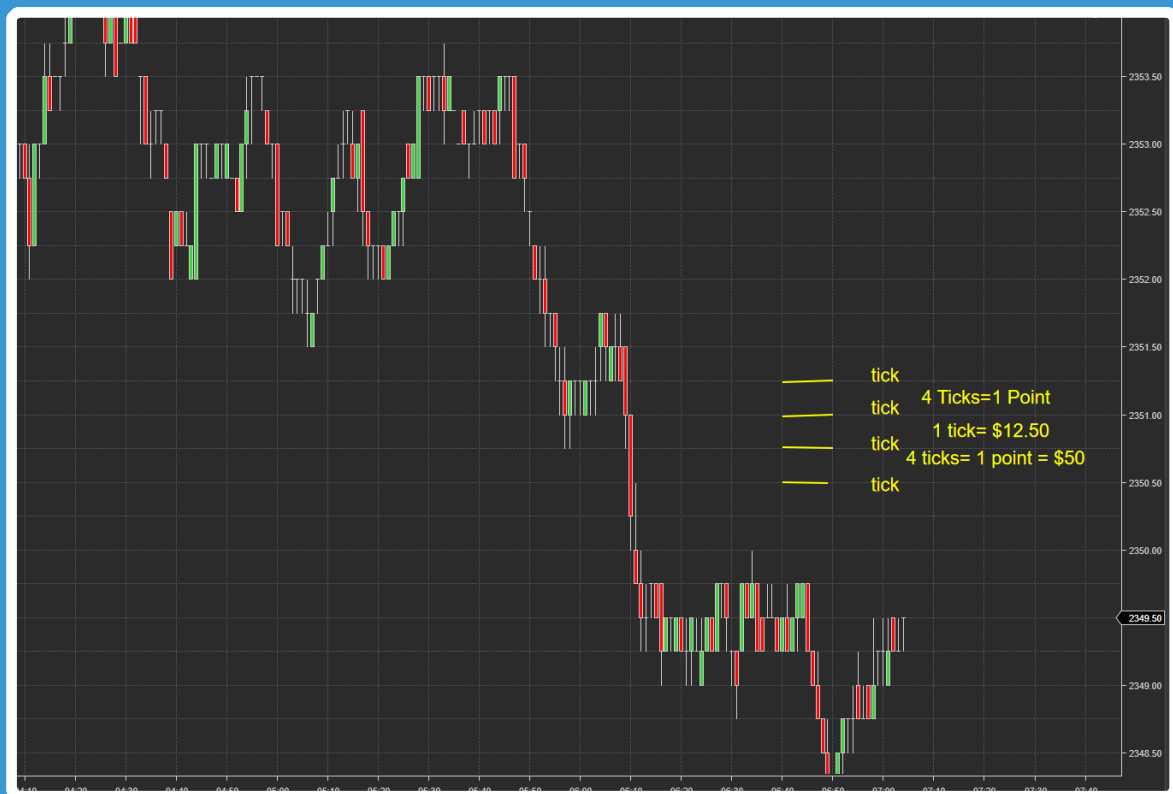
a margin (more on margins later) of just \$500. Here at Trade Context, we **do not** recommend trading on razor thin margins, however, futures allow you to LEVERAGE your capital.

TECHNICAL MUMBO JUMBO YOU MUST KNOW ABOUT FUTURES!

TICKS AND POINTS

If you were confused about the chart above explaining tick size, let me explain. Futures do NOT move in dollars and cents, they move in ticks and points. You would never hear a futures trader saying "I made 3 dollars today." Instead, they would say, "I made 3 points."

Looking at the chart above it's easy to see that the tick size for the ES is 0.25. That means that the ES moves in 0.25 increments, with each of those "ticks" valued at \$12.50. Example below:



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CONTRACTS

Since futures were originally built for commodities to be sold in the future, all futures contracts expire. Some expire monthly, but index futures expire every quarter. The symbol for the E-Mini SP 500 is ES and the ES expires the third week in March, June, September, and December. All you need to know about the contract is put the month-year after the symbol and you will get the right chart.

Example for E-Mini SP 500 (Symbol ES):

ES 03-17 (E-Mini SP 500 expiring March 2017)

ES 06-17 (E-Mini SP 500 expiring June 2017)

ES 09-17 (E-Mini SP 500 expiring September 2017)

ES 12-17 (E-Mini SP 500 expiring December 2017)

MARGINS

Margin is often misunderstood and portrayed to be a bad thing. Since we are trading index futures, we are speculating on price changes. We are not buying or selling anything tangible, so when we make a trade we don't "need" money for anything other than to cover the POTENTIAL loss if the trade is a losing trade. Therefore, we give our brokers money as collateral, and in return they loan us money to speculate with. If we lose, they take our collateral until we don't have enough money to "cover the margin." The margin cost to trade 1 contract on the ES ranges from \$500-\$5000 depending on the broker.

At Trade Context, we specialize in ONE market and that is the ES. However, there are many futures markets out there to trade. I encourage traders to start with the ES and look at other markets as they grow as traders. Some other popular futures markets are:

- DAX - German Index futures
- NQ - E-Mini Nasdaq futures
- YM - E-Mini Dow Jones futures
- TF - E-Mini Russel 2000 futures
- GC - Mini gold futures
- CL - Crude oil futures

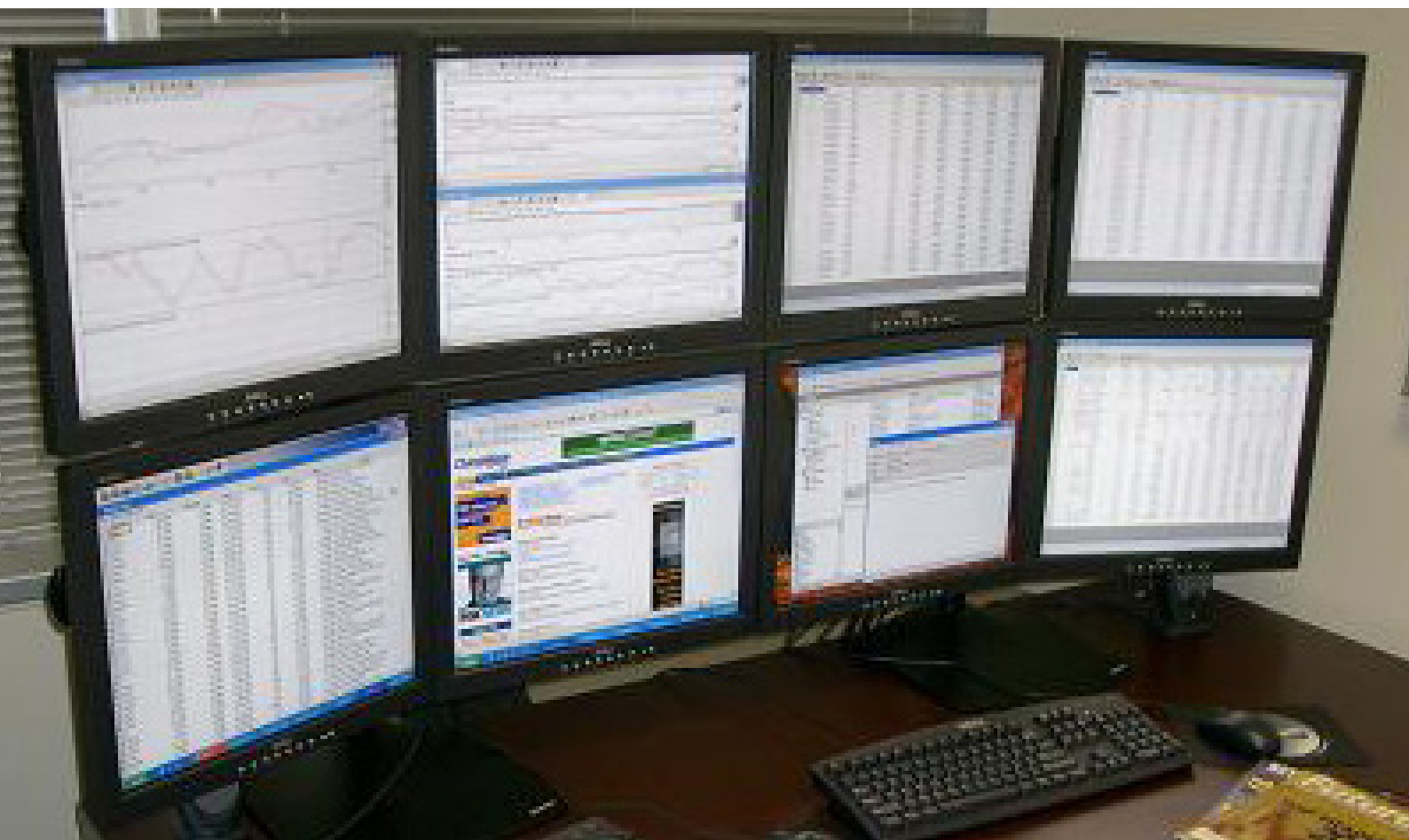
GETTING STARTED

First thing is first; you will need a laptop with Windows. I know this is a world with many Mac enthusiasts, and there are some platforms available for the OSX operating system, but the one I will talk about relies on the Windows operating system.

There are certain things you need in a trading computer. Depending on your current status in life, some may want a laptop so they can trade and travel. Others may want a desktop so they can move into an office and get more screen space. The only thing you need to know is this; you need as much memory as you can get and the best processor you can get. However, your trading office does not need to look like this...

Right now, I have a Dell XPS 13-inch laptop and it works like a dream for day trading. I can travel anywhere I want with it and whip it out in a heartbeat. I made the mistake of having a big computer with a ton of monitors but it really didn't help me that much. If you want specifics I would recommend this as a MINIMUM:

- 8 GB RAM
- 128 GB SSD (not absolutely essential)
- 500 GB Hard Drive
- I5 or I7 processor
- High Speed Internet Connection!



PLATFORM

In simplest terms, a platform is software that allows us to open, close, and manage positions in the market. There are MANY platforms out there today and they all have their pros and cons, but they all do the basics. There are some very advanced ones out there too, including some with many bells and whistles, making the learning curve very steep. Most people are familiar with brokerages like Scottrade, Charles Schwab, TD Ameritrade, and Interactive Brokers. These brokerages all have their own platforms, both mobile and desktop, where you can chart stocks and trade from them too.

The problem with these big companies is that their platforms are mostly geared towards stocks. Most of them do futures too, but it doesn't feel that they are made for futures. In my opinion, a futures trader should use a platform specializing in futures. I have tried almost all of the futures platforms and some of them are very good, but also very expensive. What I have found is that NinjaTrader is the platform that allows a trader to learn the cheapest (free while on simulation), but also gives you a reliable platform that will do everything you need. In fact, it has plenty of bells and whistles too if you want to get really crazy (automation, building your own strategies, etc.).

DATA FEED

Before we setup NinjaTrader, it's important to understand that NinjaTrader is the platform but in order to actually have your charts and place your orders in real time, you need real time data sent to the platform. The product that we trade is traded on the CME, which is the world's biggest futures and options exchange. In order to access the data in REAL TIME, the CME charges a fee. There are three ways to get the data; free trial, reduced rate for non-professional traders, and full price. I will explain the three ways below as I describe how to setup the platform.

BROKERAGE ACCOUNT

Setting up a brokerage account sounds tough and intimidating for new traders, but it's no different than a bank account. A brokerage account is needed to buy and sell stocks, futures, bonds, options, etc. My mentor explains it like this, "If you wanted to write a check, you would need a checking account. If you want to buy or sell stocks, bonds, or futures, you need a brokerage account." There are many brokerages out there, many you have probably heard of. I will not list them all but they include, TD Ameritrade, Scottrade, Charles Schwab, etc. As I explained above, it is best to use a brokerage and a platform that is geared towards futures. The commissions are much cheaper and they specialize in futures, making it a win-win situation. We are not trading equities (stocks), so why do we need to be with a brokerage that specializes in such a thing?

SETTING UP NINJATRADER

I made a video in the book resources section to show you how to setup NinjaTrader and your data feed for **free** ([Tradecontext.com/resources](https://tradecontext.com/resources)). The only issue with the data feed is that you may need to make a new Gmail account every couple of weeks. The data provider only allows two real-time data demos per email address. The demo lasts two weeks. However, sometimes you will get an email from CQG (the data provider) that looks something like this...

When this happens, all I can say is make a new email address and try again. It only takes about five minutes to make a new Gmail address and usually, that does the trick. Some students have claimed to have success with services like throwawaymail.com, where you can get temporary email accounts that are much easier to setup. You can try, and see which one works for you.

If you don't want to keep making demo accounts, you can pay for the data. There are two ways to pay for the data; reduced rate and

full price. If you are a **non-professional trader**, which most of you will be at first, then you are in luck. The CME offers the real-time data for non-professional traders at a fee of \$5 per month. However, in order to be eligible for this reduced rate, you must open **AND** fund a futures account. You can open an account for

\$1000 with NinjaTrader brokerage and enjoy the \$5 data per month. If you don't have the money to open a brokerage account, you can pay the full price for the data, which can cost a couple hundred dollars a month. I don't recommend this option.



CQGTrader@cqq.com

to me

Thank you for your interest in a free real-time futures data trial.

Data trials are limited and you have exceeded your allowance. Please contact your broker if you have any questions.

This is a system generated message, so any replies will not be received.

BASIC CHARTING ON NINJATRADER 8

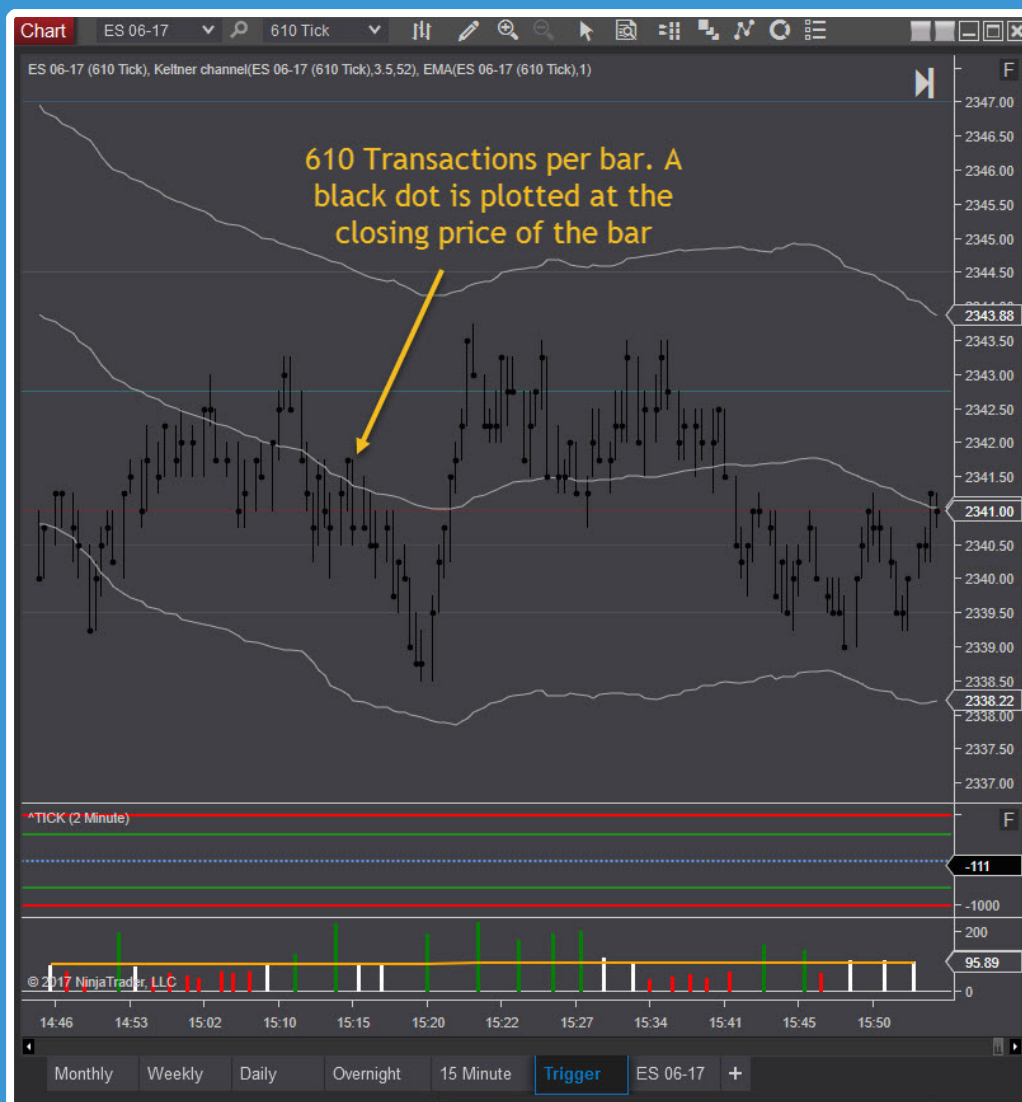
In my opinion, the best thing about NinjaTrader is the simplicity. It may seem challenging at first, but trust me when I tell you the learning curve is minimal when compared to other platforms. Here is a crash course on things you need to know about NinjaTrader.

In late 2016, NinjaTrader released NinjaTrader 8. It is a big improvement over NinjaTrader 7 in terms of load times, historical data, and overall user experience. I would highly recommend starting with NinjaTrader 8 over NinjaTrader 7 simply because all of the NinjaTrader resources are moving towards NinjaTrader 8.

Let's start with the basics...



There are many different ways to chart the price on NinjaTrader. The chart above is a simple 15-minute candlestick chart for the ES. This means that the new bars are plotted every 15 minutes. In a time based chart, it does not matter how big of a price movement, how much volume is in the bar, how many transactions occurred in the bar, it is simply time based; a new bar will plot at the end of the time period. Fifteen minutes was just an example because it's a common time period for charting. You can chart anything from 1 second to 1 year on a time-based chart. There are many other types of bars that do not rely on time, including tick, volume, range, and many more. At Trade Context, we use time-based bars to help simplify and organize the information, and tick based charts to enter into the market.



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A tick chart, shown above, is a chart variation that creates a new bar based on an amount

of transactions. I use a 610-tick chart, not because it's the holy grail, but because it is what I learned on. Each trade that occurs is a transaction, and when there are 610 transactions, a new bar is plotted. You can use candlesticks as the bar type on a tick chart as well, but I prefer to use High/Low/Close bars, otherwise known as HLC bars. It keeps it cleaner and I get a better look at the closing price or each bar, shown by a black dot.

There are advantages and disadvantages of every chart and bar type. Furthermore, there is NO bar type or chart type that will make you a profitable trader on its own. I like the 610-tick chart for my executions (taking trades) because it allows me to see the immediate momentum in the market. I use minute-based charts for a longer-term view; they allow me to get more information on one screen!

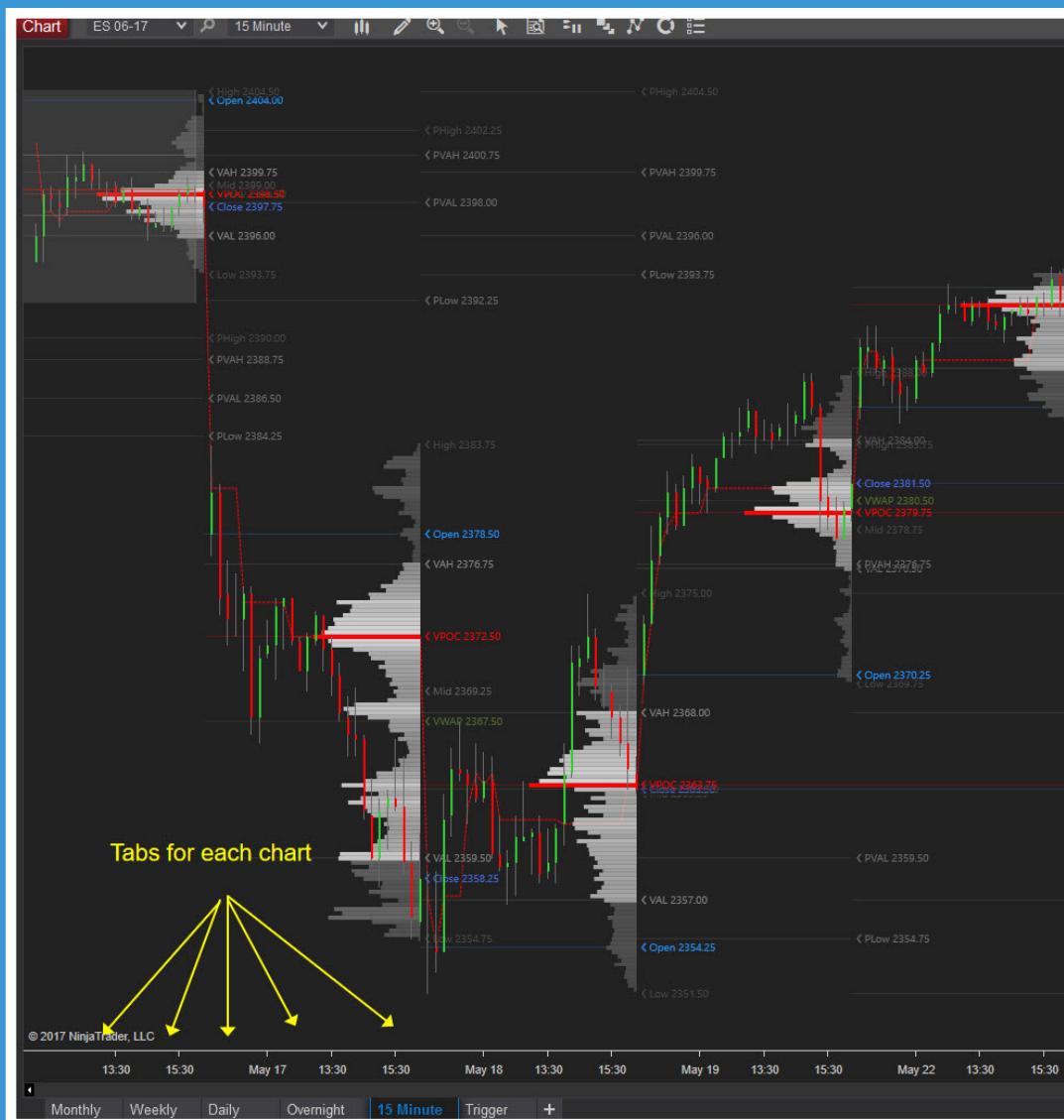
NAVIGATING AROUND NINJATRADER 8

Below is an annotated chart that shows the main things to know about the chart. This will be review to some, but something that should not be overlooked. Being proficient on your charting platform will save you A TON of time and headaches.



CHART SETUP

I have a few charts in my “workspace,” which can be seen below. If you look at the very bottom of the screen, you will see six tabs inside my main workspace. My workspace consists of a Monthly, Weekly, Daily, Overnight, 15 Minute, and a Trigger chart. Each of these charts are setup using a “template.” A template is simply a saved setting for each chart which includes everything from the period of the chart (15 minute, monthly, etc....), to the indicators that are inside each chart (and their settings). Indicators are the mathematical calculations based on the price and/or volume that attempt to foreshadow where the price may go next. These indicators are programmed so that we, traders, can see the calculations right on the chart. The workspace is designed with careful attention to detail so each of the templates and indicators play a role in figuring out what the market may do next. To make an analogy, the workspace is our toolbox, the indicators are our tools, and the template is the settings for our tools. All together the workspace gives us a space to analyze the market in.



INDICATORS AND INTERNALS

We don't use a lot of indicators at Trade Context. You will not see any moving averages, MACD, Stochastics, Gann fans, Fibonacci sequences, or anything like that. The problem with indicators is they are all derivatives of price. In simple terms, that means that indicators lag behind price. When price moves, so do the indicators, but after the fact. I do use indicators, but the only ones I rely on are based on Volume.

Most reading this will have heard of indicators. Indicators are simply programmable calculations based on historic price or volume that attempt to give a trader a forecast of future market direction. Do a search for day trading on Google and you will find a lot of indicators for sale. Most claim that they have the best indicator, and "all" you need to do is click the mouse every time the price crosses this squiggly line in pink, or blue, or whatever color it happens to be. I've seen traders with so many indicators on their chart I swear I don't know how they can see the price. How is anyone supposed to read this chart?





The market is dynamic and it should be treated that way. There are no magic lines on the chart, trust me when I tell you that.

Market internals should not be confused with indicators. Internals are market statistics and/or correlated markets, that can help dictate the future direction of the market we are trying to trade. Internals are **not** derivatives of the price of the instrument we are trading. To make it simpler, internals are indirectly related to the price, while indicators are directly related to price. The big difference is that indicators lag behind (some worse than others), while internals don't because they are their own separate markets, moving independently. Some examples of market internals for the ES include:

A/D line – # of advancing stocks – # of declining stocks on the NYSE. This internal gives us an indication of how the overall stock market is doing for the day. The calculation is based on the closing price of the stock from the PREVIOUS session. To be an advancing stock, the current price has to be higher than the closing price from the previous day. To be a declining stock, the stock has to be below the closing price from the previous session.

Ex. There are 2000 stocks on the NYSE that are trading higher than their closing price from the previous day. At the same time, there are 500 stocks trading lower than their closing price for

the previous day. The calculation for the A/D line would be:

VIX – Volatility Index. The VIX is usually referred to as the “fear” gauge in the market. While the VIX is calculated using the implied volatility of options on the SP 500 index options, the only thing needed to know is that if the VIX is rising, there is supposedly fear in the market. As fear rises (VIX up), typically money is being pulled out of the markets (price moves down).

There are so many market internals that a trader can use for the ES. The list goes on to include **bonds, gold, oil, Japanese Yen, other indices (Dow, Nasdaq, Russell 2000)** and many more. This will continue to be the case because any trader that is looking for a correlated market will find something that is correlated every once in a while. The point is, there is no holy grail (are you starting to realize that I'm trying to beat that into your head?). What works today may not work tomorrow.

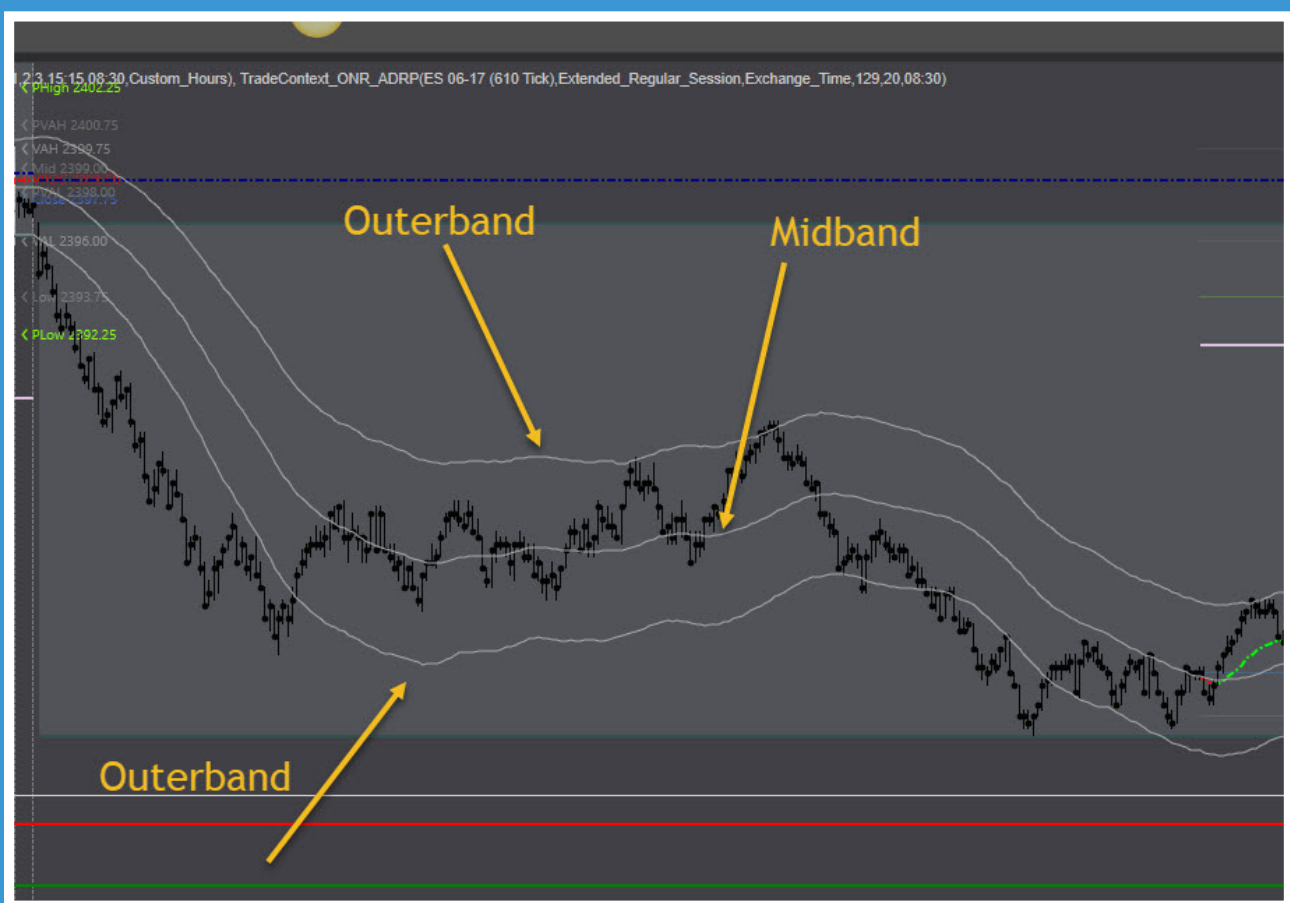
I have tested almost every market internals that you can think of. What I have found was that there is a day that one of them is leading the ES, the next day it's not. Furthermore, when I tried to watch several of them at a time, it often left me confused, since they are often contradicting each other. So, at Trade Context we try to keep it simple to avoid this information overload. We only watch one internal, the NYSE Tick.

TRADE CONTEXT INDICATORS

I think I was pretty clear on my stance on indicators, but I do find them useful when used as tools. While I continue to have new ideas developed, there are a few that are mainstays in my arsenal, and I will include them for a limited time for a low price with this book. They are as follows...

KELTNER CHANNEL

This is probably the indicator that means the least. We recommend our traders have it on their charts just to frame the price, but there is no magic here.



VWAP

VWAP is the acronym for Volume Weighted Average Price. VWAP is a simple calculation...

$$\text{VWAP} = \frac{\sum \text{Number of Contracts traded} \times \text{Contract price}}{\text{Total Contracts Traded}}$$



Don't worry, you don't have to do any calculations, in fact, the calculation is not important at all. You just have to know that VWAP is different than a regular moving average because a regular moving average depends on the closing price of a particular bar. This means that a regular moving average is only calculating the average price at the close of each bar, while VWAP is calculated every single time a trade is made. Why is that important? Since it accounts for how MANY contracts are traded at each price, and doesn't care about when the bar closes, the VWAP will ALWAYS be the same no matter if you're using a 1-minute bar chart, 5-minute bar chart, 60-minute bar chart, 610 tick chart, etc. The same is simply not true for a simple moving average. A simple moving average will change every time you change the periodicity of the chart.

However, this advantage would be useless if it were not for institutions. VWAP gained much popularity when it became known that the institutions, pension funds, and mutual funds were using VWAP as a benchmark for their traders' performance. As a trader, we want to be aware of areas that the large players are aware of. The beauty of the VWAP is it doesn't matter what kind of chart the institution is using, we can have the same moving average as them if we are using the VWAP.

To illustrate what I mean, let's take a look at these two charts below. The first one is a 1-minute chart. I threw some random moving averages on the chart, along with VWAP.



What you notice here is that the simple moving averages move quicker to catch up with the market when the market moves fast. However, I quickly scrolled to the top and changed to a different time period (15-minute) without touching anything else and everything changed, except VWAP. You can see from the second chart that VWAP stayed the same while the SMA's moved from their original positions to new positions (I left the text markers in the exact same place as the first chart).



Now that we know the daily VWAP is constantly changing with each contract traded AND it's the same no matter what chart we change to, you're probably asking, "Why should we care?" The answer to this question is easy. Since it's the same on the charts of everyone, and we know many big players are looking at it, we now have a major point of interest to observe during the day for potential support/resistance.

OVERNIGHT HIGH/LOW + ADR

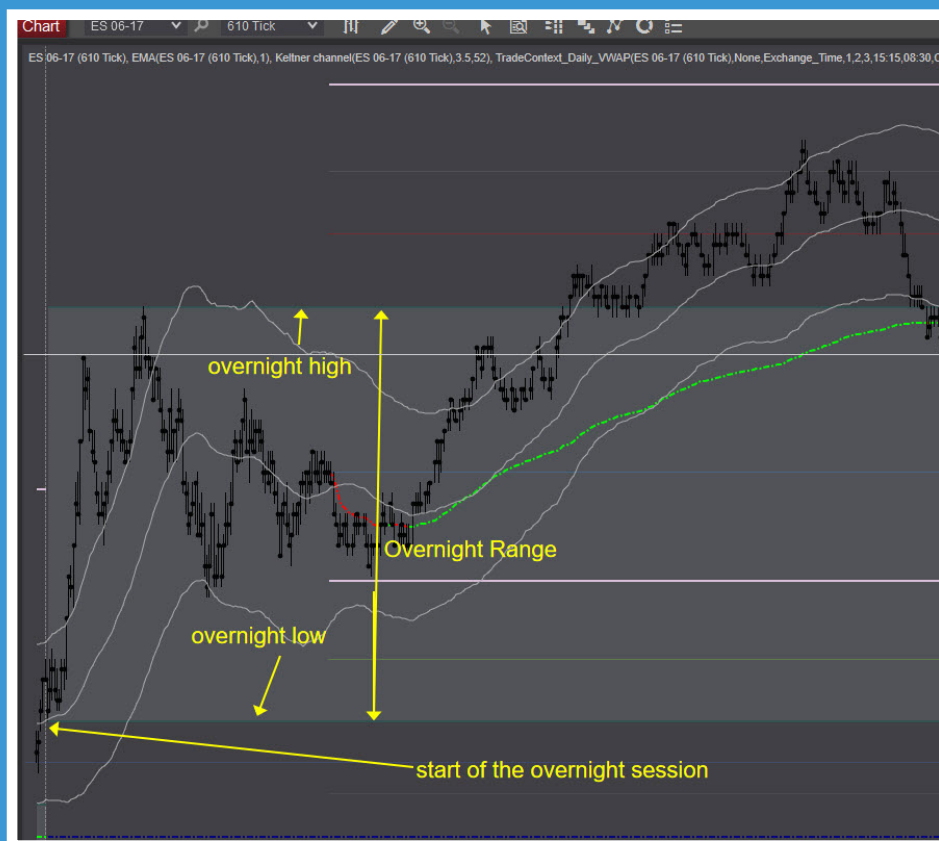
This is really two indicators in one, so I will tackle these separately.

One of the big differences between the futures and equities is the time in which they trade. Futures markets trade almost around the clock, so the overnight session becomes useful information for us as futures traders. At Trade Context, we take a few key pieces of information from the overnight and throw the rest away. One is the total volume of the overnight session, the other, the overnight high and low.

There are many market statistics that a trader can use to help them predict market move-

ment, one of the best is the overnight high and low. Let me first say that I did not invent this statistic, but I checked the statistic, by hand, for 10-years worth of data and it checked out to be amazingly accurate. Before we go further, I want to clarify that the overnight session I am speaking of begins at 6:00 PM Eastern U.S. time and goes all the way until 9:30 AM the next day, when the index futures open.

The statistic is this: The overnight high OR low will be TOUCHED OR BREACHED 97% of days during the regular session (9:30 am eastern-4:15 pm eastern). To get a better idea what I mean, take a look at the chart below.

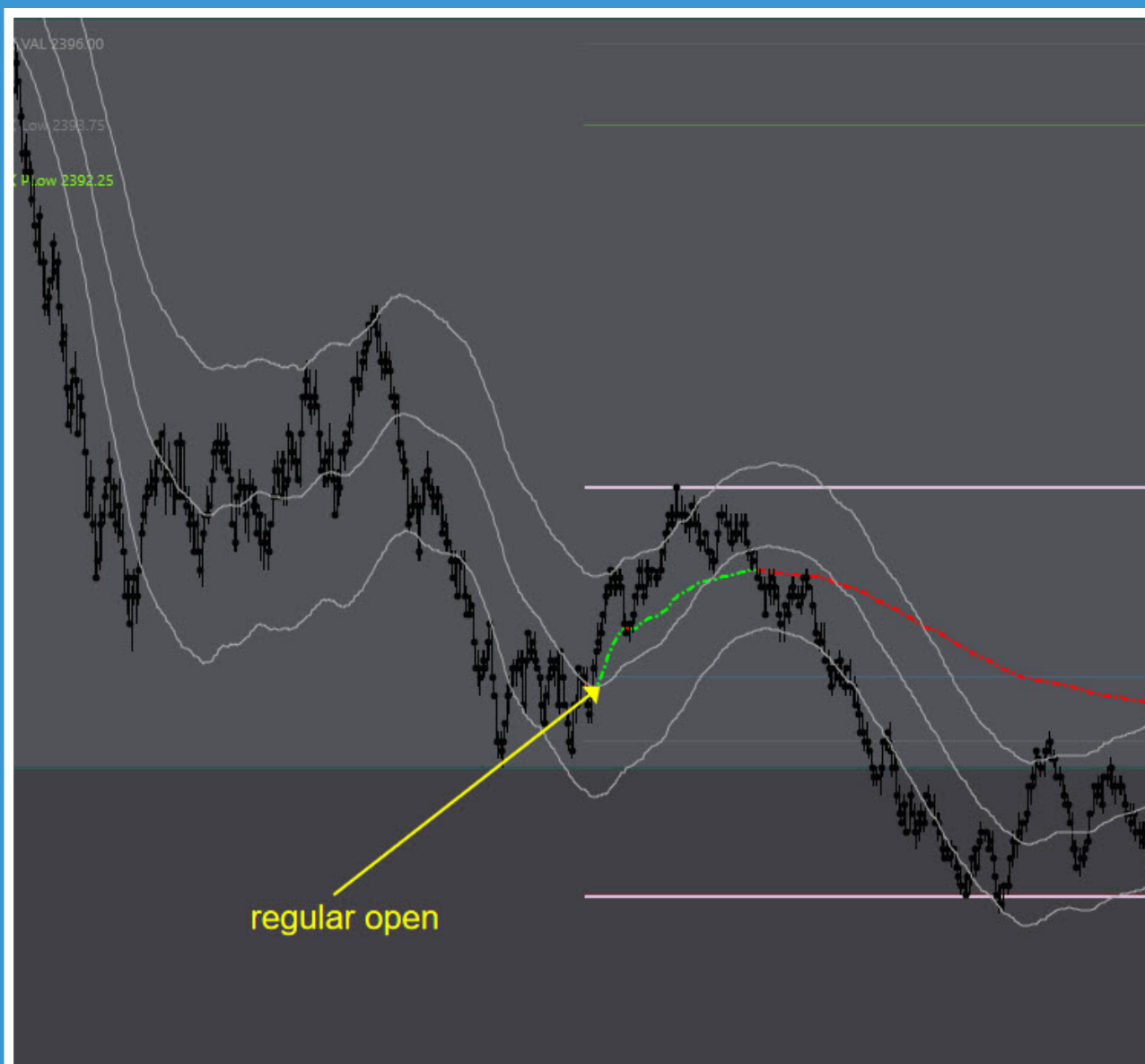


The overnight range is clearly depicted in the chart by the light gray. Once the overnight session ends and the regular session begins, the indicator will plot the overnight range across the rest of the trading session. It is important to know where the overnight high and low are throughout the day because of the second part of the statistic. Once the high or low is TOUCHED OR BREACHED, the other side only has a 28% probability of being touched.



The image above shows an instance when the overnight high is breached. If we were trading the market this day, we now know that since the overnight high has been breached, there is only a 28% chance the overnight low is touched or breached.

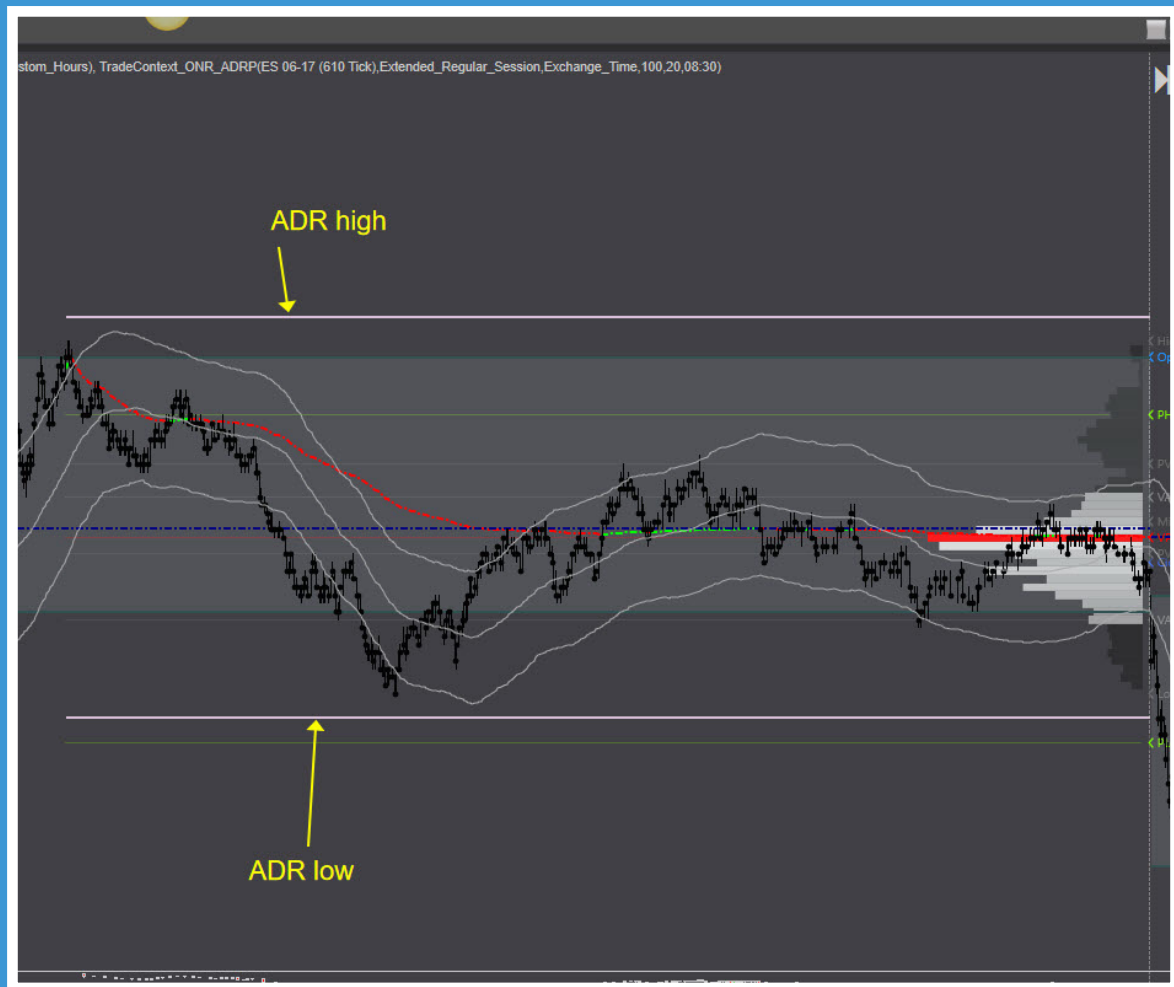
Can this help us in our trading? You bet it can! Not every day opens right in the middle of the overnight range like the illustration. I just picked a random day. What if the day looked like this...



To me this was as easy as it gets. I won't talk much about entries in this book but part of the context of the market is putting together a bunch of clues and making a quick decision. Let me ask you a question. If the market had strong momentum down in the overnight session and started to drift up at the beginning of the regular session, would it be time to panic? No, it wouldn't be because the overnight low is much closer than the overnight high, and we have strong momentum down. The overnight low would be your first target on a short trade.

ADR

This is included with the overnight indicator but it is something that stands on its own. ADR is just the acronym for average daily range. This indicator draws us two lines at the beginning of the regular session to tell us how far (on average) the market is likely to go. There are a lot of factors that need to be considered on top of ADR, but it gives us a nice visual reminder on how far the market would go on an “average” day.



You will notice in the picture that the lines seem to frame the market, and that is the key. They give us an idea of when the market may be stretched or have more room to expand. One of the great things about this ADR indicator is that it's dynamic. The lines are moving as the market moves.

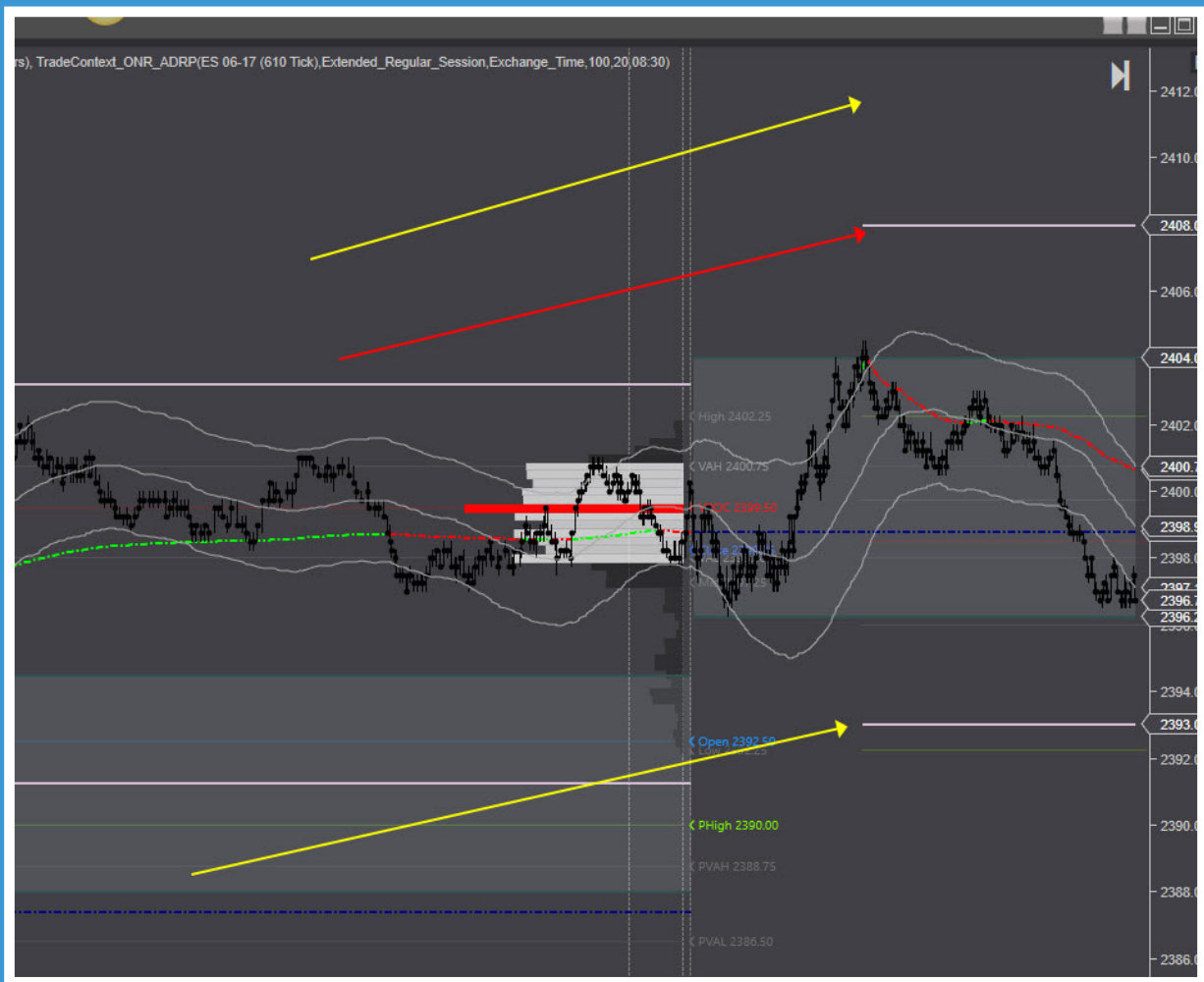
If you look at the figure below, this is actually the same day. The market has just opened and the ADR is giving us a frame as to how far the market would go, either direction, on an average day (you can customize how many days you want to use for the average calculation, I use 20).



As the market starts to fall, you will notice in the next image that the ADR high line has shifted down. This is because the market is falling and if it were to turn around and start going up, the previous ADR line would not be valid anymore since the range has already extended down.

One thing to note about ADR, which will lead directly into the next indicator—It is essential to understand that volume and volatility go hand in hand. There is a statistical proportionality be-

tween the range and the square of volume. It is not necessary to understand any of that “statistical mumbo jumbo,” it is only important to know that you must use ADR with some kind of volume tool to allow you to figure out if there is a reasonable chance that ADR is reached or exceeded, you need to keep an eye on how much volume is being traded that day. Remember, ADR stands for Average Daily Range, so it’s giving you, by default, two lines at 100% of the average daily range.

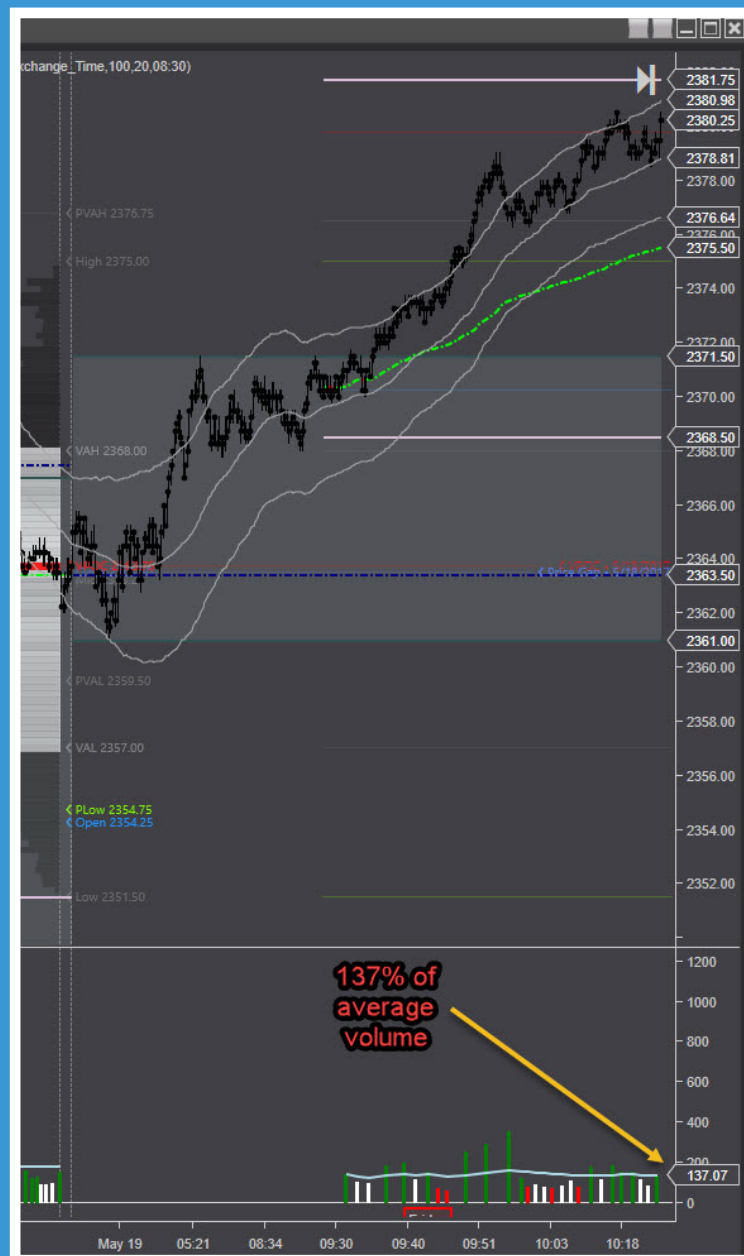


RELATIVE VOLUME

The relative volume indicator is the cousin to the ADR. It tells us how much volume there has been today, relative to the last 20 days (again, this is customizable, but I use 20 days). It doesn't matter how many days you use, just don't go back further than a few months.

I see a lot of traders talking about volume for

the day, week, month, etc. after the time is completed. To me, that doesn't make any sense because it's not actionable information. This is where relative volume comes in. It allows us to see, as the market is moving, how we stack up to the average volume. To explain better, let me illustrate...



On the image you will see green, white, and red vertical bars. This is showing you the volume in 2-minute time slices (again this can be customized). The indicator has been programmed to show you spikes in volume (the green lines) and periods of low volume (the red lines). The blue horizontal line is just showing you that cumulative relative volume for the entire day so far. Personally, I lean more on the cumulative relative volume because it gives us an overall clue for the day, but there are times when the individual time slices show important information, though that is too much detail for this book.

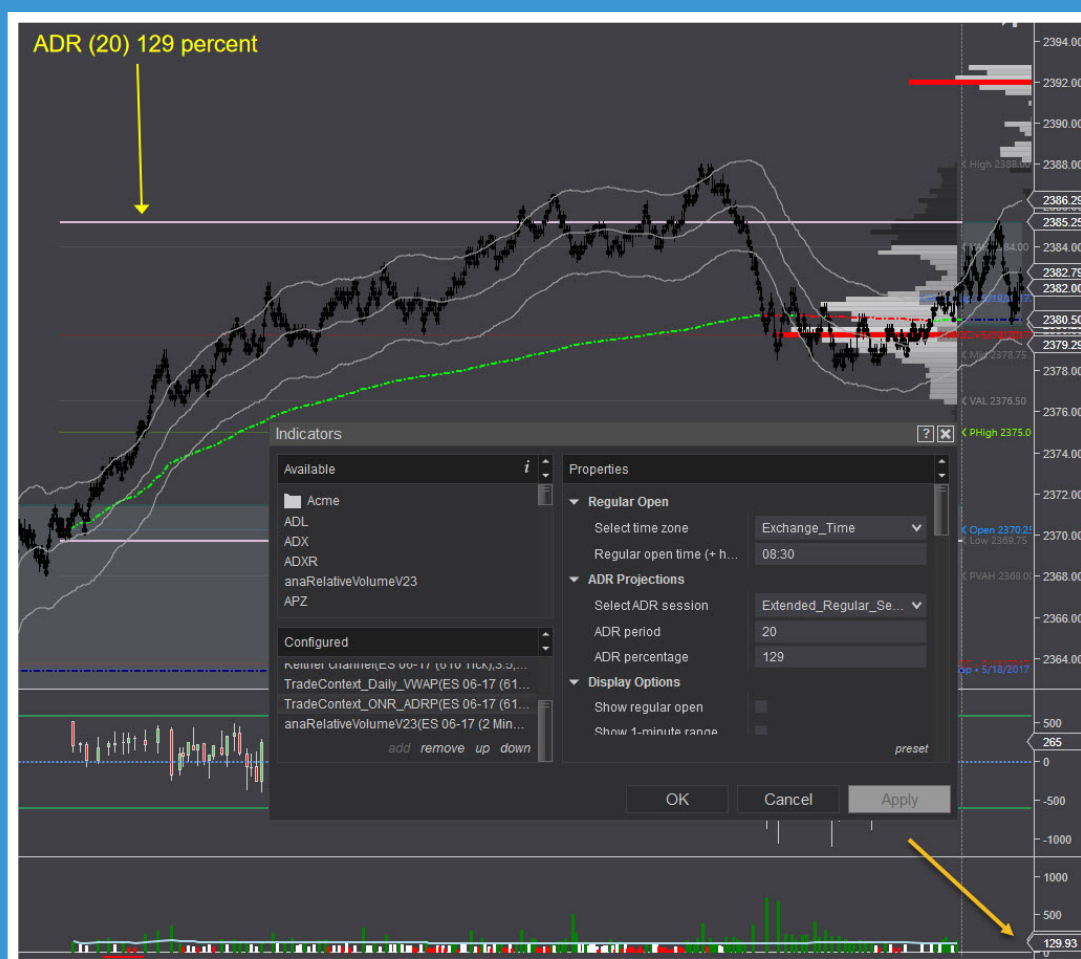
Here is an idea of how to interpret the relative volume. Like I said previously, volume and volatility have a direct correlation. Therefore, when you look down and see the relative volume is high (higher than 120%), we can expect a volatile market that can run much further than a market with low relative volume (lower than 80%). In contrast, if a market is moving in one direction with strength, on low relative volume, I don't expect the market to sustain the move; I am more skeptical. To simplify it even further, when relative volume is high, the market is more likely to trend. When relative volume is low, the market is more likely to go back and forth and close somewhere in the middle of the range.

UNDERSTANDING THE CORRELATION BETWEEN ADR AND RELATIVE VOLUME

In a perfect world, these two indicators would be one. Although it's not realistic to say there is a one to one correlation between the two, a relative volume greater than 100 usually means the ADR will be breached and one less than 100 means it will likely not be touched. Again, this is the GENERAL rule and by no means is set in stone. One thing I had added to the ADR indicator is that you can adjust the ADR projection. Let me illustrate...



In the image, you can see that the user can change the ADR percentage. How will that help us? Well, if I see the cumulative volume percentage for the day is 129%, I can easily change the value of the ADR projection to see a POTENTIAL place where the market could end up reaching. To be clear, there is NOT a perfect one-to-one correlation between the two, but like everything else we do at Trade Context, we are just looking for clues.



You can see once we change the ADR projection to match the relative volume, we get a better projection of the daily range.

The downfall of this is the relative volume is dynamic. This means it is changing throughout the day. At 10:30 the relative volume might be at 130% and by the end of the day, it may be at 97%. If you adjust your ADR projection to be 130% of the ADR and don't adjust it as the relative volume starts to fall, you could end up with a target that is unrealistic. For this reason, I think it's wise to keep the ADR projections at 100% until you have a very good idea that the cumulative volume is stable.

NYSE TICK

The NYSE TICK is not an indicator, it's known as a market internal. The definition of the "Tick" as you will hear it commonly referred to:

NYSE TICK=Stocks on NYSE ticking up-Stocks on NYSE ticking down

At Trade Context, we like to keep our eye on the Tick as a clue to strength or weakness in the market as a whole. There are a few values that are important on the Tick. The zero line is the value when the exact same amount of stocks are ticking up versus ticking down. We use this as an over/under line because it makes it easier, visually. A reading of +600 or -600 typically is a sign of strength. A value of +1000 or -1000 is typically an indication of extreme strength or exhaustion. Explaining the difference between knowing when it is strength or exhaustion is more depth than this book will cover. However, let's take the image to show some simple ways to gather information from the Tick.



First, if you notice when the market opened, notice how the market starts to climb, but the Tick is struggling to get above the zero line. The overall market is trying to tell us something here. It's screaming that you should be skeptical of the move up because more stocks in the NYSE are ticking down than up. In fact, the market barely gets over the zero line at all. See the image below.





BASICS OF AUCTION MARKET THEORY AND VOLUME PROFILE

The foundation of the way we view the market at Trade Context is based on auction market theory. We believe the EASIEST way to understand what the market is doing, and more importantly, what it might do next, is based on auction market theory. If we look at auction market theory in its simplest terms, price moves up to motivate sellers and it moves down to motivate buyers. When there is a price that is accepted by both sides as “fair,” we have equilibrium, or “value,” as we say in trading. At these fair prices, high volume is traded as both parties (the buyers and the sellers) are happy with these prices.

The best way to describe auction market theory is a practical, real-world example. Let's take gasoline for example. Let's say there is a gas station, call it Best Gas, which regularly sells a gallon of gasoline for \$3.00. One day they decide to move the price down to \$2.75 because a new gas station, call it New Gas, moved in across the street and they want to have lower prices. The buyers of gasoline (me and you) are excited, we drive by and maybe we stop in and buy some gas if we need some because we think it is a good “value.” Only last week we were paying \$3.00 per gallon. Best Gas is happy because he is not allowing the New Gas to take his customers, but not as happy as he would be if his price were \$3.00 per gallon (he would

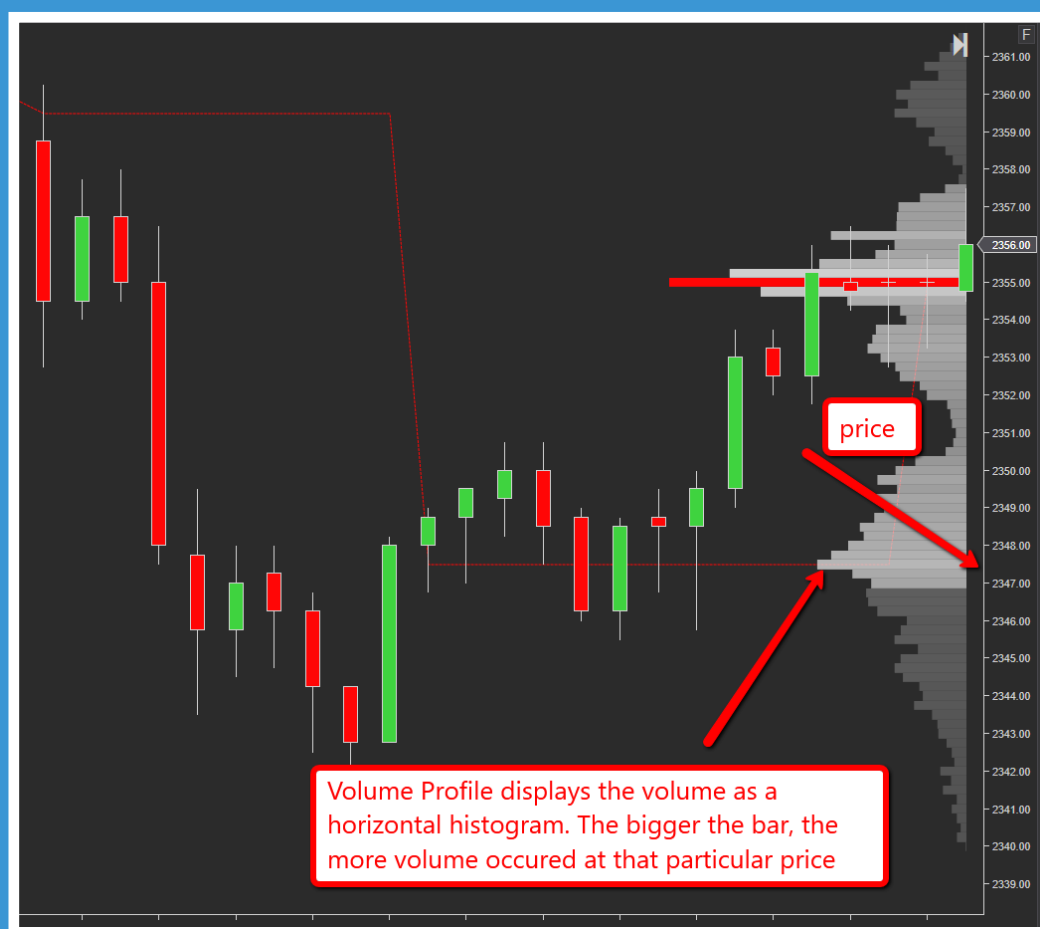
be making more money per gallon). Over the weekend, Best Gas starts to realize that the New Gas is taking some of his customers because they have a shop where they sell food. The customers are happily paying a higher price for gas at New Gas so they can grab some food too. Since Best Gas has to do something to get those customers back, he cuts the price of gas to \$2.50 per gallon. Now EVERYONE in town is excited. People are rushing to the gas station to get this incredible deal on gas. They are filling up their cars, boats, lawnmowers and everything else they have, simply because they think this is a great “value.” However, Best Gas is not making any money at these prices, they are only keeping it at this low price until they can build their own food shop to compete with New Gas. The food shop is completed and Best Gas immediately raises their prices because they can't afford to sell it at those low prices anymore. The prices did not last long because Best Gas could not afford to stay in business at those prices. The price gradually returns to the “fair price” of \$3.00 per gallon. Both the buyer and Best Gas consider this price fair and for the next few months, thousands of gallons of gas are purchased at \$3.00 per gallon.

One day a couple of months later, Best Gas goes out of business due to their inability to compete with New Gas. Immediately, New Gas

raised the price of gas to \$4.00 per gallon. They are the only station in town now so they start to raise prices to see if the market will continue to buy at higher prices. The buyers in town are unhappy but they continue to buy gas at \$4.00 per gallon because they need to drive to work, but are no longer filling up their boats or lawnmowers. New Gas is making a little more money so they are happy. The next week they drive the price up to \$5.00 per gallon and the buyers start to drive across town to the other gas stations. New Gas sells very little at \$5.00 per gallon since there are very few buyers who will pay those prices. New Gas would love to sell it for \$5.00 per gallon but the buyers are not buying at those prices because they believe the price to be unfair. The price gravitates back towards the fair price, somewhere between \$3.00 and \$4.00 per gallon.

This was obviously a very simple, made up example, but you get the point. In auction market theory, price moves from balance (fair prices) to imbalance (unfair prices) and back to balance (fair prices). In trading, it's really no different. The objective of the market is to seek the place where the most volume will be traded. This can be found where the buyers and sellers agree on price. The good news is that we can chart this information using our platform and Volume Profile.

Volume Profile is the name for the way a trader can chart the volume of trading activity over a specified period of time at specific prices. In layman's terms, Volume Profile draws us a horizontal histogram that shows us how much was traded at EACH price. It looks something like this. See diagram.



Now that we have a visual of what the Volume Profile looks like on a chart for the ES (E-Mini SP 500), it's important to start covering the basic terminology; not only for Volume Profile, but for everything we do at Trade Context. Starting with the terms from the chart above.

Open – Stands for the opening price for the session. If you are looking at a profile for today, it would be the opening price for today, 9:30 AM eastern time.

Value High – The value area covers 68.7% of the volume for the session. Value high is the top of that 68.7% and value low is the bottom of that 68.7%. In the diagram below, the value area is the entire light gray region.

Close – This refers to the previous trading day's closing price. We say yesterday's close, but if it's Monday, we are referring to Friday's close.

VPOC – Volume Point of Control. This is a fancy way of saying the most traded price of the session. It is the price where the most contracts have traded.

Previous low/high – These are the lows and highs from the previous session. I refer to these as yesterday's high and low.

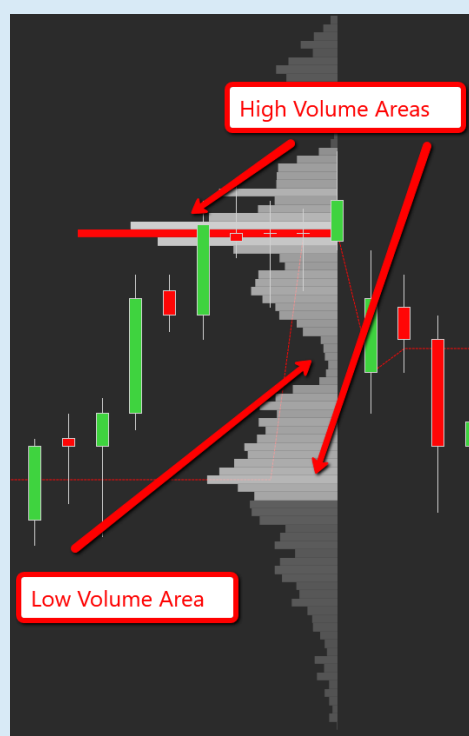
VWAP: Volume Weighted Average Price – This is the price that is the average of all the contracts traded for that day. Without complicating it, it's the average price of the day when taking into account how much volume (trades) was traded at each price.

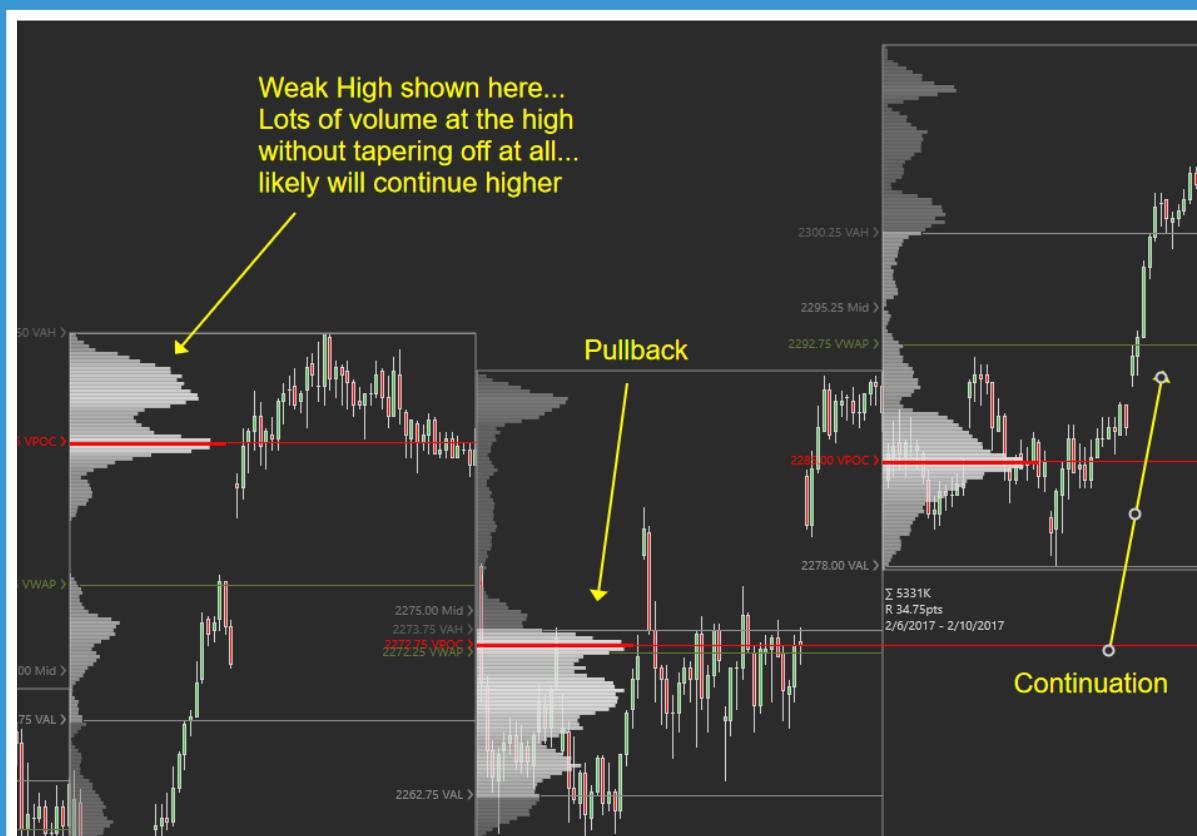
High Volume Node (HVN) – A range of prices that creates a “fat” spot on the profile. It looks like a bulge, which is due to the high amount of trading that has taken place at these prices. It is not the VPOC but it's still an area where buyers and sellers were very active. When the market enters these HVNs the market tends to slow down. The market has accepted this area before (hence the high volume) and is UNLIKELY to move quickly through it.

Low Volume Node (LVN) – A range of prices that has seen very little trading. On the profile, these areas look like valleys. These areas tend to act as a rejection spot between high volume areas. When the market reaches the LVN, a quick move can be anticipated away from the area.

Volume – To understand volume, it's essential to understand how trades take place. In futures, every single buyer is met with a seller. There are never more buyers than sellers, or vice versa. If trader A wants to buy a contract, a trade ONLY occurs if there is a trader, trader B, who is willing to sell that contract to trader A. When this occurs, we have a trade. Volume is simply the number of contracts that are traded. The more contracts that are traded, the more volume. At Trade Context, we look at volume over many different timeframes (daily, weekly, monthly) to understand what is going on in the market.

Weak High/Weak Low – Areas near the edges of the profile that have a lot of volume. These are important because the auction likely is not complete. Typically, the profile “tapers off” near the edges when the buyers think they are getting a great price and come in and buy very fast, leaving a “tail” on the profile. The weak high/low is likely to be broken before a reversal occurs.





REGULAR TRADING HOURS/ELECTRONIC TRADING HOURS

Since futures trade basically all night, the market is broken up into a few trading sessions. Electronic Trading Hours (ETH) is the entire time the market is open. The ETH for index futures, ES included, are from 6:00 PM eastern time Sunday evening to 5 PM eastern time on Friday with a 15-minute break every day from 4:15-4:30. However, the Regular Trading Hours (RTH) are from 9:30 AM eastern time-4:15 PM eastern time.

Long/Short (Buy and Sell) – This is very basic, and there won't be much talk of entries in this book, but I don't want to leave anything out!

If you buy a contract you are said to be "long" and you make money if you sell the product at a higher price.

Ex. If you buy a jar of peanut butter for \$3, you would be "long" 1 jar of peanut butter. You

would make money if you sold the peanut butter to your friend for \$4.

The opposite is true if you sell a contract. If you sell a contract you are said to be "short" and you make money if the price goes down and you buy back the contract.

Ex. You borrow a jar of peanut butter from your friend. The current price is \$4 and you sell it. You are "short" 1 jar of peanut butter and in order to make money, the peanut butter must go down in price. If the peanut butter goes to \$3, you take the \$4 you received when you sold it, buy the peanut butter, and return the jar of peanut butter to your friend. You make \$1 on this transaction.

These are basic examples just to make sure everyone understands buying and selling.

USING VOLUME PROFILE

Now that you have a general idea of auction market theory and the terms associated with Volume Profile, I'll give you a little glimpse into how I use it.

I use a top-down approach. This means, I start with the monthly chart and work my way down to the trigger chart. This allows me to see the big picture, and keeps me from putting all my emphasis on the auction from yesterday, or even worse, the overnight session. It's easy to be blinded by what is happening at the smaller

time frames, and we want to avoid that mistake at all costs. Even though we are day-traders, it's important to know what the overall market trend is.

What I'm looking for is clues on who is in control of the market at the given time. THAT. IS. IT. Sounds pretty simple, right? Let me walk you through the process to show you how simple it is. I am going to look at the current market and show you EXACTLY what I am looking at and thinking.



The monthly chart is showing us that the market looks presently ready to break to new highs. The long-term trend is up (not pictured here), and over the last two months we have been balancing. How do I know we have been balancing? Look at the profiles for the last two months. They are laid right on top of each other

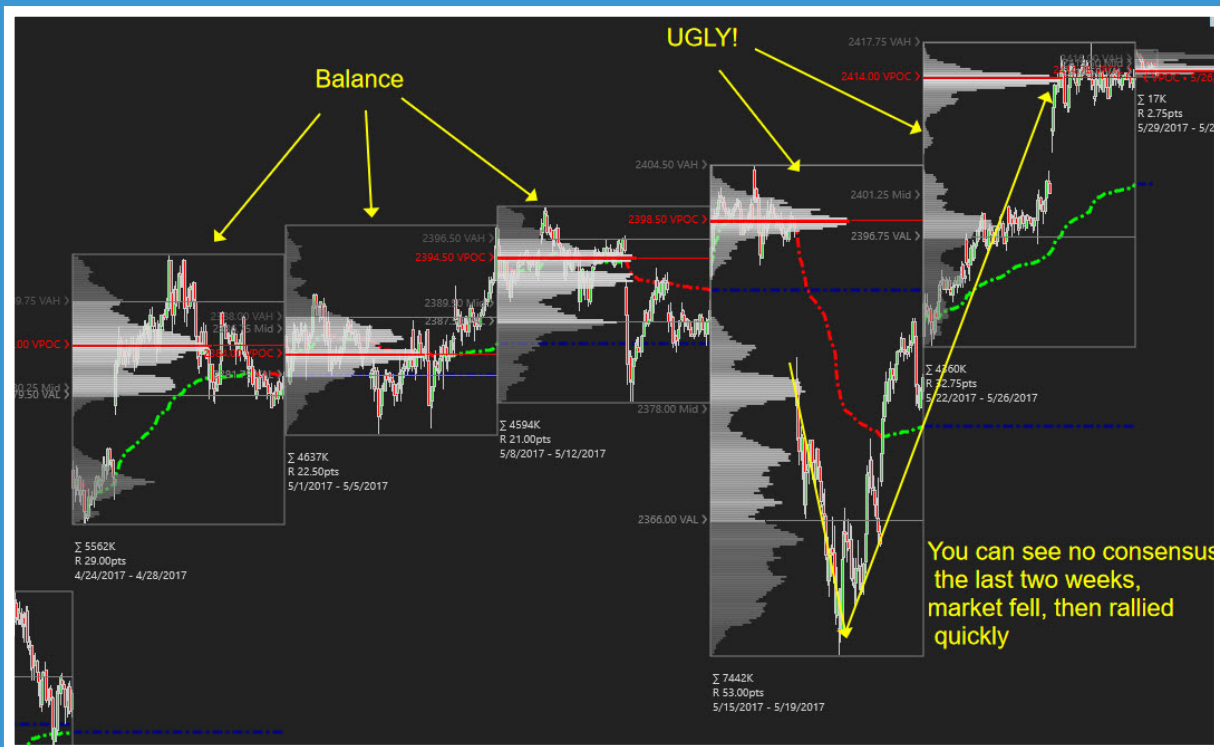
and the volume is concentrated in the middle, for the most part. Remember, the volume at every price is depicted by the horizontal histograms on the chart. The market is now sitting at the highs, and has put some volume in at the highs, meaning it's likely to continue higher.



WEEKLY

Next up is the weekly. I do the exact same thing for the weekly, try to spot things that can help me figure out who is in control. What I can draw from the image below is that the weekly shows a bit more clearly that the buyers are more dominant here. We can see a period of three weeks where the market was balanced, which I annotated on the chart. The market tested lower, and immediately the buyers stepped in and pushed the market higher. Last week's profile, like the monthly, shows a lot of volume near the highs. Also, the point of control is all the way near the high of the week, last week. This is a strong indication that the market will likely test higher prices in the near future.

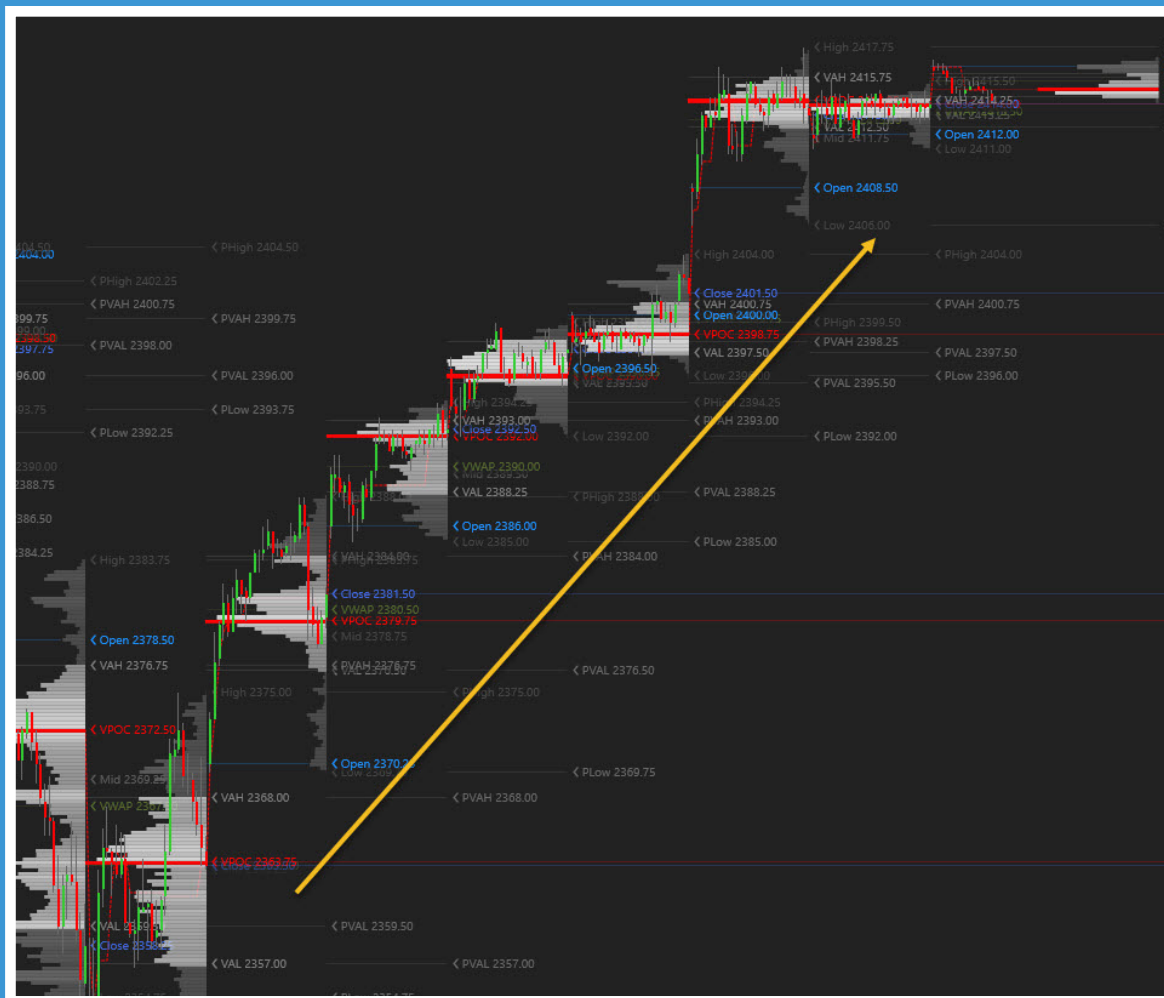
How do I know? Auction market theory tells us. Imagine you are a storeowner and your peanut butter is flying off the racks. You have moved the price up to \$8 and the buyers are still buying it like crazy. In fact, they are buying it so much that the VPOC of your peanut butter has moved up to \$7.50! That's amazing for you (the store owner) because you are making great margins on your peanut butter. However, if you're selling out at \$8 the most likely thing to do is test higher prices to see where the demand starts to taper off. Who knows, the market may accept \$10 too, and there is only one way to find out!



15 MINUTE

Next, I move over to the 15-minute chart that has daily profiles overlaid on it. What I'm looking for on this chart is overlapping days and areas of balance. Why? Because the market has memory. The market tends to gravitate back to areas of balance. The problem right now is the market has been in an uptrend the last week and there is nothing really to glean from this chart at the time. We have a gap zone underneath us. Gap zones are beyond the scope of this book, but it is not something that makes a big difference in my analysis in this case.

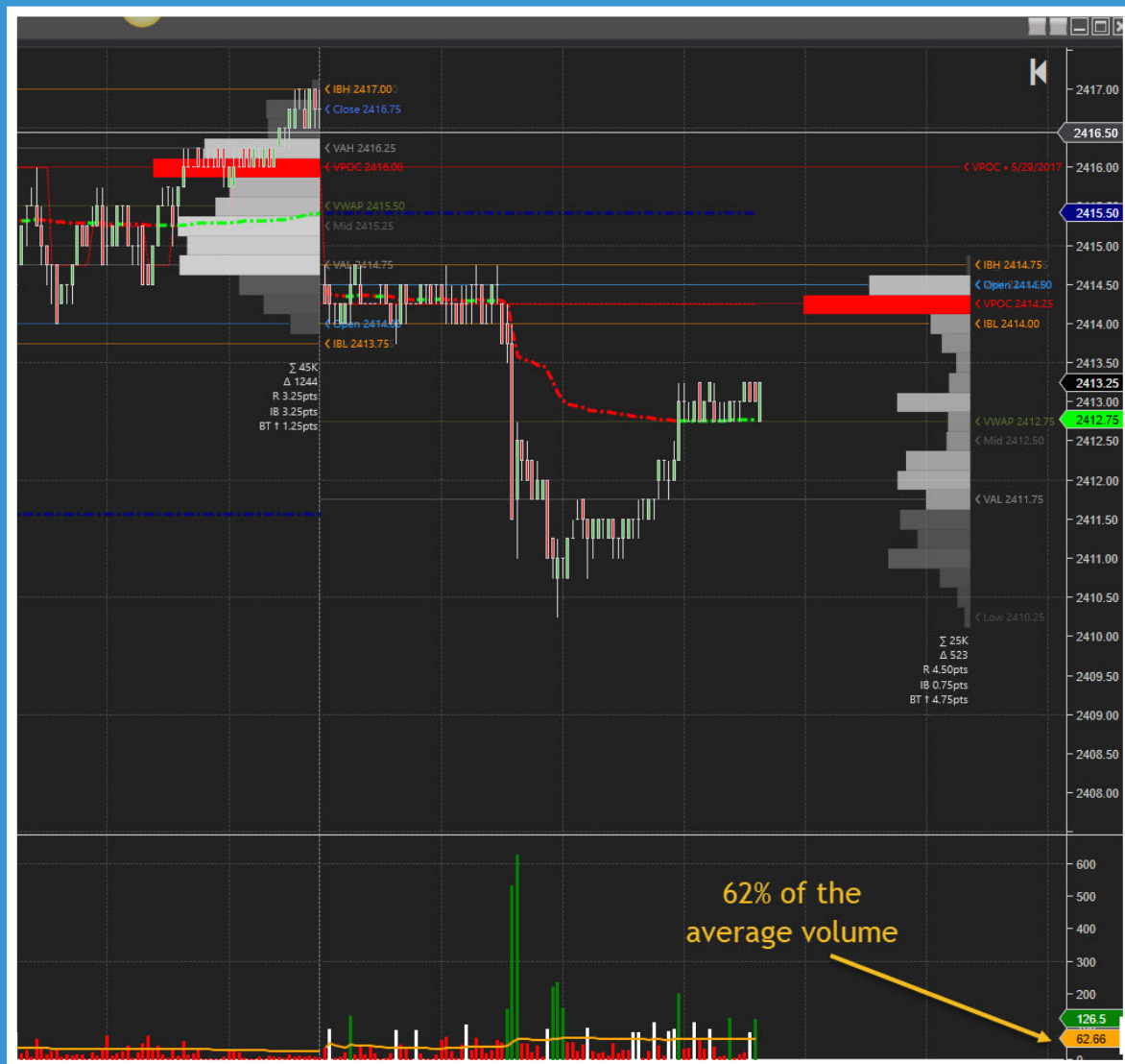
So, what do I get from the 15-minute chart today? Not that much!



OVERNIGHT

The last thing I look at before I go to my trigger chart is the overnight session. I am trying to get an indication if something happened overnight to change the auction. Usually, the answer is no, but it gives us our first glimpse as to what today “might” be like. I say might because the overnight can give you clues, but you never know until the regular open, as the regular trading hours contain the heavy hitters; the ones with the potential to move the market.

I look at the relative volume of the overnight session first, it's my first indication of the amount of volume for the regular trading session. On days with heavy volume, you can usually see heavy volume overnight as well. I also begin to look at the profile of the overnight session, to begin to form my hypothesis on which side of the overnight will likely be touched.



It's the day after Memorial Day in the United States so we can see overnight that there is not much action. We can see on the chart that we only had 62% of the average volume, which indicates a lack of participation. Remember, when volume is low, volatility is usually low. I say usually because volume and volatility can show up out of nowhere (news event).

SO, LET'S MAKE A PLAN!

You just watched me go through the charts, but what good is analysis without execution. Now,

it's time to figure out an actionable plan for the market open. Here is what I do next.

I like to come up with a plan. I do not trade my plan and try to force it on the market. I watch the open and wait and see who is in control. Is it big players? Is it small players (locals)? I use this information to validate or reject my plan. Here is what my plan would look like today based on the analysis above.

If the market were to open right now, based on where the market currently sits overnight, I would expect the overnight high to be taken out. Why? Because we have the most traded price from Thursday and Friday above us,

as well as the closing price from Friday. The market tends to head back to those areas to “check” the prices before moving on. Even more so on days where the big participants are not in play (overnight volume is low, day after holiday, etc.). After taking the overnight high, I would expect that market to be extremely dull

and stay inside of Thursday and Friday’s range. I drew a yellow line below where I would expect the market to stay above, simply because I doubt the market will have the volume to push out of this small balance zone made Thursday afternoon and all-day Friday.



On days like these, I trade the market from the outside in. I am looking for the market to spike in one direction, and I like to trade it back towards VWAP. That is the most probably trade today, and I will use that as my primary trade idea.

This is a great time to explain that I DO NOT force my idea on the market. If the market opens, and starts with a 6-point swing down and relative volume is strong, I will not blind-

ly try to buy the market back towards VWAP. It's just a trade idea; it is not set in stone. You MUST be able to adapt because the market will throw you curveballs from time to time. Curveballs are fine if you are able to adapt, find out who is in control, and trade with them.

This process takes me about 10-15 minutes at most. It will take longer to begin, but with some practice it becomes fun.



TYING IT ALL TOGETHER

We have only scratched the surface on the ways we can exploit the ES by our deep knowledge of the market. I only briefly touched on Volume Profile and auction market theory, there is so much more fun stuff to learn. As you can see from this book that one indicator or market statistic alone won't make you money. In fact, we don't want it to be that way. If it were that easy then everyone would do it.

Here is the thing, unless you have a massive amount of time and money to create fancy automated systems (which a lot of times don't work), it is ESSENTIAL you understand that you must have something that the computers don't have, a deep understanding of one market. One of the main reasons I trade the ES is that there is minimal erratic movement due to the high volume of trading. Therefore, we can use our toolbox, consisting of volume profile, our indicators, and statistical analysis, to create HIGH PROBABILITY trades.

That is what trading is all about; creating a plan that has an edge. What we teach at Trade Context is how to understand the market, to the point where you have the odds in your favor every time you click the mouse. This should not be confused with thinking that every trade will be a winner, but instead that you will win more trades than you lose. Even MORE IMPORTANT, we strive to make each winning trade bigger than each losing trade.

What if I told you that I would give you a coin to flip, and you would have a 50-50 chance of picking the right side? However, each time you win I would give you \$2 and each time you lose you only have to give me \$1. Wouldn't that be awesome? Who wouldn't want that? Now, I'm not telling you that you will win twice as much every time (sometimes it will be much more), but our winners are bigger than our losers. At the end of the day, you probably don't care about anything else except the words, "SHOW ME THE MONEY!!!"



BUT...IT TAKES WORK!

If you're anything like me, I know you're excited and thirsty for more knowledge. This book probably just whetted your appetite. But, I want to tell you something upfront, before you decide to move forward... Trading is not easy, nor is anything in life that is worthwhile. If you think you are going to be a millionaire overnight, this endeavor will NOT end well for you. You have to possess the ability to get knocked down and get up again. There is SO much money on the line in trading and it's a business that is almost infinitely scalable. If you become profitable in futures, you can instantly go from making a couple hundred dollars a day to several thousand dollars a day by doing EXACTLY the same thing, only changing the order size. Show me another business that makes scaling so easy.

With that said, it is important to realize that most people lose money day trading. It is the

fact of the matter. Big institutions have more money than you. They can have fancy trading systems built by "quants." The High Frequency Traders (HFT) that have appeared over the last 5-10 years have made it increasingly difficult to trade for short term profits. As a "retail" trader, they say you have about a three percent chance to make it. In reality, these are all excuses.

My point in this rant is not to discourage you; in fact, it's quite the opposite. I just want you to know that profitability is difficult, but has been achieved before, and will be achieved again. If you keep your head down and work on the RIGHT things, you will wake up one day with an incredible lifestyle. You can make as much money as you want on your own terms. I can lead you to that lifestyle. The only question is; are you in, or in the way?



Risk Disclosure: Futures and forex trading contains substantial risk and is not for every investor. An investor could potentially lose all or more than the initial investment. Risk capital is money that can be lost without jeopardizing ones' financial security or life style. Only risk capital should be used for trading and only those with sufficient risk capital should consider trading. Past performance is not necessarily indicative of future results.

Performance disclosure. HYPOTHETICAL PERFORMANCE RESULTS HAVE MANY INHERENT LIMITATIONS, SOME OF WHICH ARE DESCRIBED BELOW. NO REPRESENTATION IS BEING MADE THAT ANY ACCOUNT WILL OR IS LIKELY TO ACHIEVE PROFITS OR LOSSES SIMILAR TO THOSE SHOWN; IN FACT, THERE ARE FREQUENTLY SHARP DIFFERENCES BETWEEN HYPOTHETICAL PERFORMANCE RESULTS AND THE ACTUAL RESULTS SUBSEQUENTLY ACHIEVED BY ANY PARTICULAR TRADING PROGRAM. ONE OF THE LIMITATIONS OF HYPOTHETICAL PERFORMANCE RESULTS IS THAT THEY ARE GENERALLY PREPARED WITH THE BENEFIT OF HINDSIGHT. IN ADDITION, HYPOTHETICAL TRADING DOES NOT INVOLVE FINANCIAL RISK, AND NO HYPOTHETICAL TRADING RECORD CAN COMPLETELY ACCOUNT FOR THE IMPACT OF FINANCIAL RISK OF ACTUAL TRADING. FOR EXAMPLE, THE ABILITY TO WITHSTAND LOSSES OR TO ADHERE TO A PARTICULAR TRADING PROGRAM IN SPITE OF TRADING LOSSES ARE MATERIAL POINTS WHICH CAN ALSO ADVERSELY AFFECT ACTUAL TRADING RESULTS. THERE ARE NUMEROUS OTHER FACTORS RELATED TO THE MARKETS IN GENERAL OR TO THE IMPLEMENTATION OF ANY SPECIFIC TRADING PROGRAM WHICH CANNOT BE FULLY ACCOUNTED FOR IN THE PREPARATION OF HYPOTHETICAL PERFORMANCE RESULTS AND ALL WHICH CAN ADVERSELY AFFECT TRADING RESULTS