Diary of a Professional Commodity Trader by Peter L. Brandt, pages 48-51

I use two other methods to determine price targeting. The first involves a technique known as *swing objectives*. The principle of a swing objective is that markets tend to advance or decline in legs that are of approximately equal distance.

Finally, I may periodically use point and figure (P&F) charts to calculate a longer-term target. P&F charts measure the amount of price action over a period of consolidation and are not time related. I use P&F counts several times each year when I believe that a period of consolidation (usually a large bottom or base) will produce a trend much more extended than indicated by the pattern target.

Important note: There is *no* guarantee that any market will reach its target. Traders need to be alert for markets that run out of steam prior to attaining a target.

Intervening Patterns and Pyramiding

During a sustained trend, a market frequently will experience a pause. These pauses often form smaller independent consolidation patterns. These patterns can be a continuation in form, meaning that another thrust in the direction of the dominant trend will be produced, or reversal in form, implying that the previous trend has come to a temporary or more permanent end. Continuation patterns offer the opportunity to both pyramid an initial position and to tighten up the protective stops on the initial position. Reversal patterns offer the opportunity to avoid riding the initial position back to the starting gates (or what I call a *popcorn* or *round-trip move*).

As a trader, I have mixed feelings toward continuation patterns—and my feelings differ based on the duration of the pauses within the main trend. Long pauses (more than three or four weeks) can wear down my patience. I much prefer shorter-duration pauses in a main trend, especially if the move coming into the pause was strong and the pause takes the form of a pennant or flag. Figures 3.21 and 3.22 display continuation patterns in Australian dollar/U.S. dollar (AUD/USD) during the same advance on the weekly and daily charts, respectively.

A continuation pattern during the course of a major trend allows me to advance my initial protective stop in the direction of a profitable trade. A breakout of a continuation chart will be accompanied by its own Last Day Rule. I may elect to move the protective stop from the initial Last Day Rule to the new Last Day Rule created by the continuation pattern.

It is also possible that a pattern implying a reversal of trend could develop prior to the attainment of an expected target. I may elect to move my protective stop in relationship to a pattern that carries trend implications counter to my position.

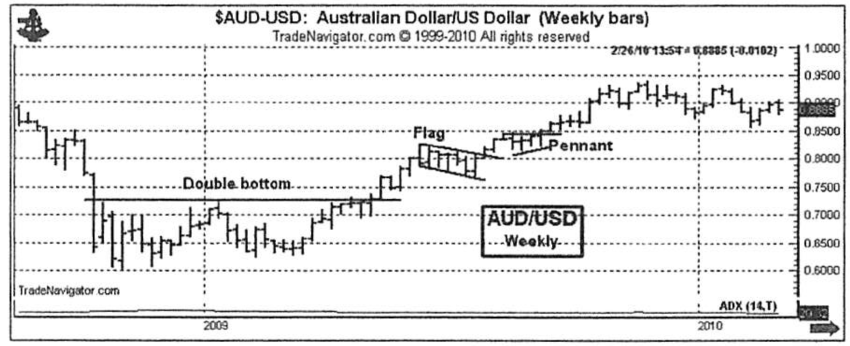

FIGURE 3.21 Continuation Patterns on the Weekly AUD/USD Graph.

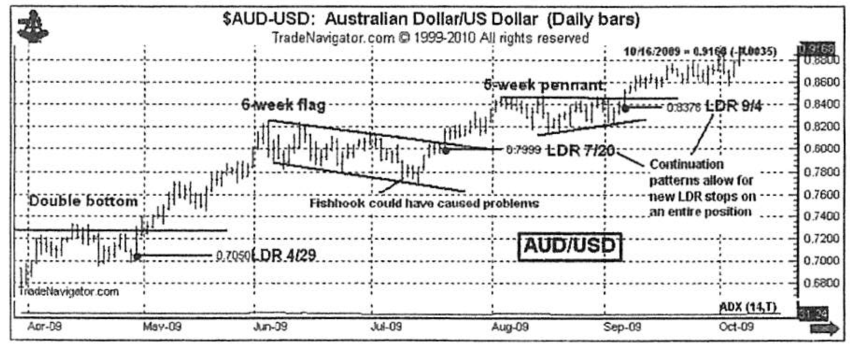

FIGURE 3.22 Continuation Patterns on the Daily AUD/USD Graph.

As previously discussed in this book, taking a profit before a target is reached can be very challenging to a trader. This area of my trading is most likely to be modified on an ongoing basis. All too often, unfortunately, my thinking is governed by the most recent trades. This type of optimization thinking is akin to a dog chasing its short tail—the short tail will always be moving just away from the dog's mouth.

Trailing Stop Rule **3DTSR**

There was a time in my trading when I never moved my stops away from the Last Day Rule. A market would either reach its target or stop me out at the Last Day Rule.

There was an inherent risk management problem with this strategy. Assume, for example, that I entered a trade with a risk of $800 per $100,000 of capital and a target equal to $3,200 per trading unit. The initial relationship of reward to risk was four to one. Next, assume that the position went my way and reached a point where I had an unrealized profit of $2,400 per unit. This meant that I had $800 left to gain before taking profits. Leaving my stop at the original level meant that I was now risking $3,200 to the original Last Day Rule stop in order to gain the final $800.

This was insane money management, so I had to come up with some means to readjust my risk and reward parameters. For the sake of brevity, I will not take the time or space to discuss the popular concepts of a trailing stop based on a dollar amount or percentage retracement.

I developed a concept I call the Trailing Stop Rule. This trading guideline requires three days of price action to be implemented: the new high or low day, the setup day, and the trigger day.

Figure 3.23 shows the Trailing Stop Rule in action on a long position in the Dow Jones. The first step to the exit strategy is to identify the highest day of the move. Of course, it will change as new highs are made. The high day in the Dow was August 28. The setup day occurs on any day a market closes below the low of the high day. This occurred on August 31. The trigger and exit then takes place when the low of the setup day is penetrated. This occurred on September 1.

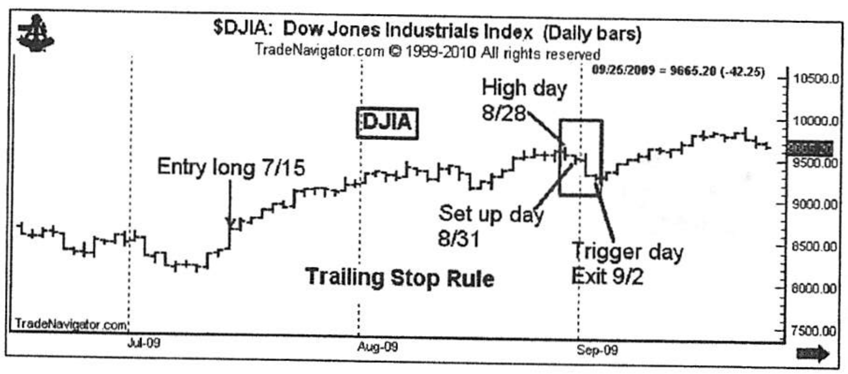

FIGURE 3.23 Trailing Stop Rule in DJIA.

I want to emphasize that there is nothing technically significant about the Trailing Stop Rule. It is simply a means to prevent a popcorn or roundtrip trade from occurring. Figure 3.24 shows the activation of the Trailing Stop Rule almost immediately after a pattern completion in GBP/USD.

Weekend Rule

The Richard Donchian Weekend Rule is a technique I may employ to extend the leverage in a trade.

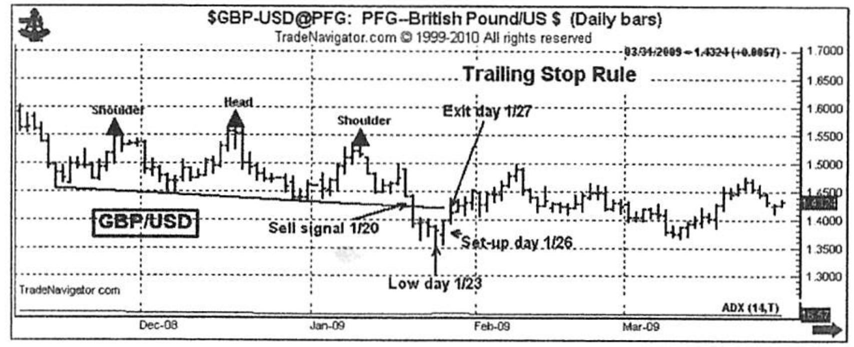

FIGURE 3.24 Trailing Stop Rule in GBP/USD.

managed futures industry and is credited with developing a systematic approach to futures money management. His professional trading career was dedicated to advancing a more conservative approach to futures trading. Donchian passed away in the early 1990s.

The Weekend Rule basically states that a market that decisively moves into new high or low ground on a Friday is very likely to continue the move on Monday and early Tuesday of the next week. The reasoning behind the Weekend Rule is that a decisive new high or low on Friday indicates the willingness of "strong hands" to take a position home for a weekend.

The Weekend Rule is even more valid when there is a long, three-day weekend.

For me, the Weekend Rule becomes most significant and useful when a pattern breakout (especially a weekly chart pattern) takes place on a Friday. In such cases, I may extend my risk from six-tenths to eight-tenths of 1 percent to a full 1 or 2 percent.

Figures 3.25 and 3.26 show major breakout days (all on Fridays) in the bull market in sugar in 2009.

Market Runs

The type of trend I most appreciate are straight-line market runs. Such runs are actually quite typical of strong trends. There are two types of straight-line moves, as shown by the accompanying examples.

Figure 3.27 of March soybean oil displays the first type of market run—a trend characterized by a series of continuous lower highs (or higher lows in the case of an advance). In this case, the market had 18 straight days of lower highs during a substantial drop. Nearly four weeks of lower lows is probably more than a trader can expect from a trend, but the point is that

Member Q&A from May 2016

Q: I read your book, 'The Diary of a Professional Commodity Trader,' back in 2012 and have repeatedly reviewed several sections. It seems to me you no longer strictly apply the Last Day Rule as you did when you wrote the book. Is this my imagination?

A: Great observation — and I should have previously addressed this. Compared to "*Diary*," I have made a couple of modifications to the Last Day Rule (LDR). First, when a breakout occurs with an extreme Wide Bodied Bar (WBB), I am not willing to risk a trade to the high (short) or low (long) of that bar. Instead, I will attempt to find an intraday reaction high or low within the WBB using an intraday graph. Second, I am much quicker today than five years ago to advance my protective stop in the direction of trade using the concept described in "*Diary*" as the "Retest Failure Rule." My goal is to adjust protective stops to insure a break-even trade within a week after trade entry.

Member Q&A from November 2016

Q: I know you usually enter buy stops to go long and same time enter protection stops. And usually protection stop loss is the low of breakout bar that completes the pattern.

But if for example on Sunday I am putting buy stops orders and want to put protection stop loss order but as there is no bar for Monday and so no low, how do you decide on stop loss level?

A: Peter still uses the Last Day Rule concept -- that being the low of the day of the breakout as long as at least half of the bar is below the boundary line. Otherwise he will use the low of the last full day within the pattern.

But, Peter has modified this LDR since the book was written and looks to find a tighter stop. He often will use the open price of the day of the breakout. This requires that he takes a look at a market that breaks out when he knows he is filled on his entry. For example, the LDR low on Oct 21 in Soybean Oil was 34.20, but the open was 34.44. In this case Peter is currently using 34.39 and 34.14 as his stop prices.

Also, see our archived Member Q&A webinar from August 2016
LINK: https://www.peterlbrandt.com/factor-member-qa-peter-l-brandt-august-webinar/