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**Letter from the Editor**

In this month's issue of Technically Speaking, we proceed from the theoretical side of technical analysis to the practical application of technical analysis. The theory is important to understand, ideally before you start putting real money into trading ideas. Perhaps that last idea is what separates the professionals in our audience from the many failed traders that find technical analysis doesn't work. It's not that technical analysis doesn't work – it's more likely that the default settings of an indicator they saw on a web site don't work.

Several prominent technicians offer examples of what they have read over the years. Combined with the CMT reading list, which can be downloaded [here](#), there is a lot to learn. If you haven't reviewed that list in a few years, it's worth taking a look at the changes that have been made over the past couple of years. The MTA library has many, if not all the technical analysis books that are worth reading.

We also include two articles showing how to turn theory into actionable analysis as we attempt to continue offering something for everyone in each issue of the newsletter. Larry Berman’s analysis is long, but our electronic format allows us to reproduce it in its entirety. It can serve as a valuable example of quality analysis to those new to the profession.

Finally, I'm looking forward to seeing many of you in New York City for the Annual Symposium. I'm not sure what the official numbers say, but the early registration seems to be much higher than last year and the attendees and speakers I’ve had a chance to speak with are enthusiastically looking forward to the event. If you haven’t decided to join us yet, please think about it. You won’t be disappointed and you’ll learn a lot, no matter how much you already know. While you’re in New York, you can also stop by the MTA library and see the physical enormity of the literature in our field.

Sincerely,

Mike Carr, CMT

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**The MTA Library: An Overlooked Benefit?**

*By Mike Carr, CMT*

Learning technical analysis is different than mastering many other disciplines. Until recently, there has been little in the way of formal education. The introduction of the CMT Institute and proliferation of college classes in technical analysis has changed that. The MTA Educational Foundation has worked for years to increase the availability of classes at the college level. College students at the undergrad and graduate level are now benefiting from these efforts. Among the recent successes of the MTAEF, they:

- Developed a complete course in technical analysis, comprised of 12 lectures, including all necessary charts and exhibits. These lectures are available for use by academic institutions.

- Partnered with University of Maine at Fort Kent to offer an affordable and accessible course online. The course is given three times a year.
With the focus on education, I recently asked members of the Foundation’s Board of Directors what books had a strong influence on their careers. After all many experienced technicians have spent countless hours reading the work of pioneers in the field and these technicians include some of the best in the field.

Charlie Kirkpatrick told me, “The first book I ever read on technical analysis was Abe Cohen’s *The Chartcraft Method of Point and Figure Trading*. It was on my father’s desk when he worked at Fidelity in the 1950’s, and I was only a teenager. After that I immersed myself in the Boston Public Library and later in the New York Public Library, reading everything I could find on TA. As I recall Elliott’s work was there, as was Granville, Edwards & Magee, Wyckoff, Jiler, and many others. From all that reading then I think the most influential authors on me were: Edwards & Magee, Jiler, Cohen, Granville, Dines, Whelen, Appel, Arms, Wilder, Dewey, Lowry, Fosback, Weinsteine, Gartley, Hamilton, Rhea, Hurst, Levy, Mitchell (Wesley), Nelson (S.), Schabacker, Schultz (Harry), Sobel (Robert), Wilder, & Zweig. Since then some of the best books are those written by members of our board and advisory committee.”

It’s interesting to note that some years after he was a teenager, Charlie’s work was recognized with the Charles H. Dow Award. In his second award-winning paper, “Stock Selection: A Test of Relative Stock Values Reported over 17 ½ Years” (published in 2001), Charlie showed the results of a stock selection strategy that incorporated ideas he would have read about in Cohen’s book. It is interesting to see that the book really did influence his work, and the ideas in an old book are still useful in modern markets.

Board President Bruce Kamich agrees with Charlie that some good very good books are still being written today. He told me, “over the years I have taken great interest in reading galley proofs of books by friends --- Charlie and Julie’s book for instance.” Bruce is referring to the must-read *Technical Analysis: The Complete Resource for Financial Market Technicians* by Charles Kirkpatrick and Julie Dahlquist, a required cornerstone of the CMT reading list. For those unfamiliar with this book, it includes an overview of nearly every important concept in technical analysis. There is also an Appendix “Basic Statistics” which offers an introduction to the what is likely to be the next frontier in technical analysis. Written by Dr. Richard J. Bauer, Jr., a professor of finance at St. Mary’s University, this short section explains “the basic premises and statistics related to modern portfolio theory” in an easy to understand writing style.

Turning back to his initial days of study, Bruce remembered, “The first two books I read on technical analysis was the classic by Edwards and Magee and *How Charts can Help You in the Stock Market* by W. H. C. Bassetti. However, even more important were several pamphlets, “Practical Relative Strength Charting” and the newsletters of of E.S.C. Coppock. Equally important were the monthly letters of Steve Leuthold. (I have contributed quite a bit of Coppock and Leuthold material to the library.)”

John’s insight is that some of the obscure works may have the most impact on you personally. Coppock and Leuthold are not especially well known, although Coppock has been recognized as an MTA Annual Award winner and Leuthold received a Charles H. Dow Award (1999). What John didn’t say is that he is unusually well read, and has probably read the majority of the books in the library. While many weren’t important to the shaping of his investing philosophy, some were – and he had to read a great deal to find what would work for him.

J. Cody Tafel, CMT, is an Equity Trader with Thompson, Siegel & Walmsley LLC. Cody reminded us that not all the classic books were written a long time. He said, “*The Market Wizards Series* by Jack Schwager would have to be at the top of my list. I also thought Michael Covell’s recent updated version of *Trend Following* was great.” Cody’s idea to study the lives and work of great practitioners is a time tested path to success in many fields. It should be noted that many have tried to follow Schwager’s example and create great interviews. Most of those efforts failed to reach the teaching level of the Market Wizards books. A notable exception is “*The Heretics of Finance*” written by Andrew Lo and Board member Jasmina Hasan Hodzic. Published in 2009, this work is a true heir to the Wizards books and we can only hope we see more from these authors.

By the way, for those wondering what to read next, the list of authors provided by Charlie Kirkpatrick is an excellent resource. Many of those works are available through the MTA Library, and it is even possible that borrowing one of those books could start you on the way towards your own project that will culminate in a Dow Award.


*By W. H. C. Bassetti*

This article was originally posted at [http://www.edwards-magee.com/2010/01/14/bull-market-bear-market-nu-](http://www.edwards-magee.com/2010/01/14/bull-market-bear-market-nu-).
There is a famous zen story (mondo) about a monk who asked, does a dog have the Buddha nature? To which the zen master answered, mu. Mu means in this case both "no" and "nothing".

When asked if we are in a bull market we answer, Nu?

Good god, what is the point? our readers ask.

Here's the point. As you may know one of Magee’s books we edited is The General Semantics of Wall Street which concerns itself with the way we think about the market and how it affects our decisions. If you think of this market as a bull market you react one way. If you think you are in a bear market rally you react another.

Good god, does Bassetti think at all our readers are saying. Mu. Nu?

Best not to think at all. Best to analyze.

So we do not think of (or describe) this market as a bull market. We observe that this is a trend. Think about it. A bull market is describable in mainly emotional terms. (The term itself is emotional.) A trend is describable in both mathematical, statistical, basing point, and graphic (chart analysis) terms.

Viz, (nu?) we have just had 31 days of sideway (a kind of drift in this case) and we are now 10 days into an upwave.

Think about that. If you fully comprehend this it will revolutionize your relationship to the market, the dog and to investing itself.

Noted technical analyst WHC Bassetti has over 40 years’ experience in the financial markets and is Malcom S.M. Watts III Adjunct Professor of Finance and Economics at Golden Gate University. He is editor of the Ninth Edition of Technical Analysis of Stock Trends, widely considered to be one of the true classics of market analysis.

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**Real Data Versus Fake Data**

*By Tom McClellan, Editor of The McClellan Market Report*

I appreciated the inclusion of the article by Jasmina Hasan Hodzic, Andrew W. Lo, and Emanuele Viola
I have heard that criticism of technical analysis in the past, and many years ago a technician (who shall remain nameless) was confronted by a critic offering this very point. The critic proposed to prove that technical analysis was meritless by challenging the technician to examine some actual price charts and some charts of random data, and see if the technician could tell which was real.

The technician thought for a moment, and agreed to the challenge on one condition: he would provide some real corporate earnings data and some fake earnings data, and the critic would need to see if he could tell which sets were real.

The critic lost his smug expression, and declined the offer. The technician then twisted the knife a little bit more by pointing out that the difference between price history data and earnings data is that the price history is almost never subject to later revisions and restatements.

Concerning technicians being able to detect real price history data versus random data.

Editor's Note:

We have often seen charts of the price-to-earnings ratio. A classic piece of work in fundamental analysis is Dr. Robert Shiller’s book, *Irrational Exuberance* [Princeton University Press 2000, Broadway Books 2001, 2nd ed., 2005]. In that book, Shiller explained the idea of the cyclically-adjusted price-earnings ratio (CAPE), which defined as price divided by the 10-year moving average of earnings. Shiller claims this offers a more balanced idea of market valuation regardless of the position of the economy in the business cycle. The CAPE is usually presented as a chart. For those wanting to explore the data, stock market data used in the book is available for download as an Excel file from Dr. Shiller’s web site, [http://www.econ.yale.edu/~shiller/data.htm](http://www.econ.yale.edu/~shiller/data.htm). This data set consists of monthly stock price, dividends, and earnings data and the consumer price index, which Shiller explains can be used to allow conversion to real values instead of the nominal values usually used in analysis. The data starts with January 1871 and is continually updated.
An example of the chart can be seen at http://www.multpl.com/. An example of analysis based on this data is economist David Rosenberg’s current opinion that stocks are overvalued, http://www.businessinsider.com/rosenberg-stocks-now-35-a-whole-standard-deviation-overvalued-2010-4.

Another response came from Jarrod Hazelton:

“In response to "US Stock Market Returns – What is in Store?” by Dr. Prieur du Plessis, I would posit that P/E ratios are definitely a part of technical analysis, and that this research supports the claim. If fundamental and technical analysts can claim that the “trend” is the environment in which their analysis works, then P/E ratios being historically over- or under-valued can be added to the list of indicators speaking to the macro trend.

Technical analysis starts with an extremely basic question: What is the trend? From there we assess support, resistance, buy and sell signals, etc. that correspond to the overall trend. “What is the trend? What are the P/E ratios? Which sectors are leading/lagging in the P/E ratio trend?” P/E ratios used in such a sector study would be similar to using index breadth indicators. What are the internal buying/selling pressures on the market? What's leading and lagging? Divergences amongst P/E ratios in certain sectors and market level, etc. P/E ratios can also be viewed as a sort of relative strength indicator, confirming a trend's strength. Sentiment indicators are a part of technical analysis, and sentiment indicators overlaid with P/E ratios, or sentiment towards P/E ratios, can be very revealing. If peoples' sentiment is disregarding high P/E ratios and buying stocks anyway, then this would be the equivalent of an overbought extreme, more so than simply assessing P/E ratios.

Seeing low P/E Ratios at the end of a downtrend at oversold levels using traditional technical indicators (or the converse at a rally high) is just another piece of the technical analysts’ tool kit and should not be ignored as only a fundamental tool. After all, fundamental analysts spend a lot of time dealing with P/E ratios and other fundamental indicators... the technical analyst must remember that they, too, are not immune to the psychological winds that the technician studies.”

Theory to Practice – Bollinger Band Tools

By Mike Carr, CMT

Elsewhere in this issue, we offer examples of influential books. Experienced technicians often read a wide variety of materials to find what works for them. Eventually, they find a suite of tools that work for them. Martin Pring has written that he makes decisions based upon the ‘preponderance of the evidence’ which requires multiple inputs.

John Bollinger developed Bollinger Bands in the early ‘80s. Since their introduction, they have become one of the most widely used technical indicators by investors and technical analysts. There is a very simple reason for the popularity of Bollinger Bands – they work, and they work in a variety of ways. The indicator can be applied to price, another indicator, or almost any data series.

Recently, Bollinger wrote, “As the developer of Bollinger Bands I am often asked how to best utilize my bands. To answer requests for guidance I wrote Bollinger on Bollinger Bands. In my book I explain in simple language how to use Bollinger Bands and the wide array of technical tools and indicators I use to make rational investing choices. I also provide three trading systems that you can employ and integrate into your investment style.”

Although John didn’t mention it in our article about the MTA library, his book is an invaluable resource for technicians. It is short, which to me is often the sign of a good book. But every page has valuable information on it and the book requires many hours of study to fully understand. Even a cursory reading, however, illustrates how to build a trading system and the depth of study required to succeed in the business.

In addition to the book, John developed a web site to help investors see how he uses Bollinger Bands and the additional tools he analyzes to assess the preponderance of the evidence. BollingerOnBollingerBands.com provides that service, along with tutorials to expand on the ideas from the book.

Specifically, John provides list of daily stocks that fit the criteria defining Volatility Breakout, Trend Following, Reversal, and Confirmed Breakout. This lets novice system developers or traders check their skills and see if they are identifying the same stocks as John does himself.

Another feature of the site is a listing of stocks that are in an Implied Volatility Squeeze. In essence the IV Squeeze identifies a low in implied volatility and then checks on the likelihood of a trade working out. If that likelihood is very high that issue makes it onto our weekly IV Squeeze list. This is a tool that John has developed over time, and is based on his general ideas that volatility is cyclical.

Another section at BollingerOnBollingerBands.com, and as you can see is a tool that John actually uses to make investment decisions, highlights stocks completing the M & W patterns developed by Art Merrill. Many of the works of Merrill can be found in the MTA library, and if you unfamiliar with his work, you do need to check out at least one of his books.
The evolution of John’s thinking will be evident for those who study his book and spend time going through the site. His book is available through the library, and you can register for a free 30-day trial and learn more about BollingerOnBollingerBands.com for yourself. If you decide to continue your subscription after the free 30-day trial, MTA members and affiliates receive a 20% discount. Details on this, and other member discounts, are available by clicking here.

A Detailed Technical Strategy

The Daily Notes of Larry Berman, CFA, CMT, CTA

Editor’s Note: Technical analysis is a complex field. Larry has allowed us to reprint one of his daily reports which demonstrates this. There is some commentary, but this report presents an overwhelming amount of data in the charts and tables that make up the bulk of the analysis. What Larry does well is present an amazing volume of information in a clear and usable format.

Too often, new analysts don’t understand the importance of considering multiple data points and looking at as many variables as possible. That is probably because they don’t know how to organize the data. The report that follows is an excellent example of consistently portraying the technical conditions of the market, sectors, and individual stocks. It also illustrates the importance of looking at the data differently than everyone else to spot trades before the crowd – Larry’s sector RSI charts are pictures that are worth a thousand words, and potentially thousands of dollars when used consistently and with discipline.

Success in technical analysis takes a lot of time. Professionals, like Larry, create detailed reports like this every day. That itself is a tremendous time commitment. But, don’t overlook the fact that it took thousands of hours of study and experience to allow Larry to create these unique displays. To newer MTA members, the question is simple - If you don’t have a similar discipline, can you really compete in the markets?

S&P 500 Technical Strategy

By Larry Berman, CFA, CMT, CTA

More details on Larry’s work can be found at ETF Capital Management (http://www.etfcm.com/index.php)

It was impressive to see the market bounce back after the Goldman Sachs debacle and it is impressive to see the continued strength despite the challenges the economic markets face. We knew earnings would be strong this quarter and we have heard virtually nothing about the stronger dollar hurting foreign revenues in the quarter.

There is enough economic momentum in Q2 to suggest that these strong earnings could continue for another quarter, so all these small dips created by economic anxieties probably continue to be shaken off. There is a point in a market cycle when bond yields are rising and asset allocation shifts back to stocks are such a powerful force that is frankly hard to measure. We believe we are in that phase now, as few like bonds, and it probably has more to run.

The financials (XLF) are critical to the health of this market, and so too are the consumer cyclicals (XLY) and industrials (XLI), and while there is some natural wear and tear showing up because the recovery rally since February is strong, extended, and overbought, there is scant evidence yet that the trend is over.

MTA Announcements

MTA May Symposium 2010 - Don't Miss Out!

Register today and join 200 of your colleagues and fellow MTA members at this year's MTA
Annual Symposium. This event will be an excellent opportunity to further your networking while expanding your education of technical analysis. Sign up today to join this growing list of attendees which is on pace to be one of the highest attended events in recent MTA history.

Keynote Speakers

Mary Bartels
John Bollinger, CFA, CMT
Jeremy du Plessis, CMT, FSTA
Mark Fisher
Larry Williams

To register online, click here. Alternatively, you can register over the phone by calling Cassandra Townes at 646-652-3300.

For complete event information, please click here.

MTA Knowledge Base - Recent Additions!

The MTA would like to announce the following articles have been added to the MTA Knowledge Base.

- Equities: Blending Technical And Fundamental Analysis by Sam Subramanian
- The Trend(Line) Is Your Friend by Nicholas McGaw
- Capturing Forex Trends In Seven Steps by Billy Williams
- Fixing Bollinger Bands by David Rooke

MTA Educational Web Series - Upcoming Schedule!

Registration is now open for the following upcoming presentations of the FREE MTA Educational Web Series.

- **Sign Up Now** - Wednesday, May 5th - Jan Arps, owner and president of Jan Arps' Traders' Toolbox. Jan will be presenting "Red Devils, Hunchbacks, and Lobster Tails: A revolutionary new way to look at divergence patterns between oscillators and price" at 12 PM EST. Register for this webcast.
- Wednesday, May 12th - H. Price Headley, CFA, CMT, founder of BigTrends.com. Price will be presenting "My Favorite Indicators for Stocks & Options Traders" at 12 PM EST. Register for this webcast.

View the entire schedule of upcoming webcasts...

MTA Podcast Series - Upcoming Schedule and New Addition!

**Upcoming Schedule** - The MTA is pleased to announce the following interview has been added to the Podcast Series schedule:

- Wednesday, May 5th - Jonathan Arter
- Tuesday, May 25th - Robin Griffiths

Visit the MTA Podcast Series page to listen to this podcast and subscribe to our RSS feed, where you'll receive updates automatically every week.

**New Addition to the Schedule** - The MTA is pleased to announce Michael Reisner has been added to the Podcast Series schedule. More information on this Podcast will be available shortly.
MTA Library - New Additions!

The MTA would like to announce the addition of the following new books to the MTA Library:

- "The End of Wall Street" by Roger Lowenstein
- "Technical Analysis Plain and Simple, 3rd Edition" by Michael Kahn, CMT
- "The Complete Idiot's Guide to Technical Analysis" by Jan Arps

If you have any suggestions of books that should be included in the Library, please contact Cassandra Townes.