LETTER FROM THE EDITOR

This month, we have tried to collect examples of thought provoking analysis techniques. Several members have contributed their unique perspectives and our hope is that others can benefit from the ideas they share. This issue is focused on the practical aspects of technical analysis.

As a group technicians tend to focus on obtaining practical results in the markets. Being right is secondary to making money. That means the analysis presented may be outdated by the time you read this. They are still valuable examples of the analytical process.

We’ve been using this new format for several months and would appreciate any feedback you have. The goal of Technically Speaking has always been to offer interesting information about technical analysis and the MTA, but over time the format has changed. Please let us know what we can do to deliver content that meets your needs by sending an email to editor@mta.org.

Sincerely,

Michael Carr

Mike Carr, CMT

December 2011
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TOWARDS PROVING THE VALIDITY OF TECHNICAL ANALYSIS
BY GEORGE RAHAL

From where does the theoretical stance against technical analysis come? Although often paired against it, fundamental analysis attempts neither to prove nor disprove technical theory. On the other hand, according to the efficient market hypothesis, *only* previously unknown material information, once publicly available, can alter the price of a stock. Therefore, predicting future prices by means of past prices, technical analysis, is *impossible*. An experiment by which to disprove this conclusion is the subject of this essay.

Through an example, let us first discuss the traditional treatment of benchmarks and alpha. The S&P 500 is comprised of ten sectors and 500 stocks. For an actively managed portfolio benchmarked against the S&P 500, in order to outperform the benchmark, the portfolio manager has two tools at his or her disposal: security selection and sector weighing. As of November 2011, IBM has an index weight of 1.73% and GE has a 1.62% weight; the Health Care sector has a 11.57% weight and Basic Materials a 3.60% weight. Weighting IBM and GE at 1.90% and 1.45%, respectively, and Health Care at 11.00% and Basic Materials at 4.17% based on expectations of outperformance and underperformance, would be an example of active management. If the overweighed stock and sector outperform their counterparts, all else equal, the portfolio will have a greater return than its benchmark, alpha.

Technical analysis also provides two primary tools for outperforming a benchmark: market timing and position sizing. As an example, assume a swing trader or trading system solely trades SPY, with the S&P 500 serving as the benchmark. The portfolio is long a weighted average of 70% of the time, and the capital committed has ranged from 50 to 100%, with a weighted average of 80%. *In theory*, a portfolio not fully invested in its benchmark should underperform it; in this case, it should earn 56% (70% x 80%) of the benchmark’s annual returns (which could alternately be defined as the *required rate of return* for investing in equities, or as *compensation for systematic risk exposure* to equities) plus the returns earned on T-bills for the portion of the portfolio not invested in SPY. This time-and-capital weighted return, here, 56% plus T-bills, can also serve as a benchmark. However, since its returns will necessarily be lower than that of a traditional benchmark, the latter is a better gauge of value-creation. In short, if this portfolio earns more than passively investing, through market timing and position sizing, that excess return is alpha generated by technical analysis.

Once a specific trading strategy and benchmark have been selected, next one must gather a group of traders, the experimental group, utilizing that strategy. These traders would have to volunteer to have their results

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1 Selecting an *appropriate* benchmark is crucial for analyzing alpha. Portfolios with motley holdings or strategies must have a properly constructed benchmark. Otherwise, the comparison is not as meaningful. In this essay, I am using simple examples; however, the discussed principles would equally apply to more complex portfolios.
tracked, and must stick with the given strategy and underlying investment for the benchmark, which would serve as one type of control group, to remain appropriate. Another type of control group would be time-and-capital weighted benchmarks in which the timing and position size would be generated randomly. After a predetermined period of time, one can measure alpha, which would be attributed to technical analysis.

To return to the efficient market hypothesis, the deduction that technical analysis cannot be successful can be reformulated as, “Technical analysis cannot generate alpha,” which would serve as the null hypothesis. If, from the experiment above, alpha is produced and is determined to be statistically significant—meaning it is not likely the result of chance—then the null hypothesis can be rejected as false. (To be scientifically rigorous, in statistics, nothing can be proved; hypotheses can only be disproved, which is why a null hypothesis is tested.) Stated concisely, statistically significant alpha derived from technical analysis disproves the claim that it does not work. Such a conclusion would be a step towards proving the validity of technical analysis.

George Rahal has been writing about financial markets for several years. He began his career in Lazard Capital Markets’ equity research department. He has since been involved in technical research and trading, which he applies in his current role at Landor Capital Management. He earned his B.A. in Literature from NYU. Mr. Rahal has passed all 3 CMT and CFA exams.
A GAME OF TELEPHONE
BY CARSON DAHLBERG, CMT

“I had the story, bit by bit, from various people, and, as generally happens in such cases, each time it was a different story”. – Edith Wharton, Ethan Frome (1911)

This line pretty much sums up the reason for the markets’ volatility. One market that is definitely painted by this is the EURUSD. Since volatility is the order of the day (and it really is every day) let’s take a look at Volatility Based Technical Analysis (VBTA) to see if we can see to make sense of it – cause the news isn’t helping a whole lot.

This is the EURUSD cross. The main thing to focus on here is that the range of support or resistance is dependent on the amount of noise in the market. If you are doing multi time framed (MTF) analysis, think about how the noise on the time frame above you will affect your trade’s timing and management.

For example, with a weekly time frame, you have more time to decide what to do and to be flexible with the management. Essentially, a weekly time frame is a larger tool and not as precise. It’s like the surgical instrument that opens the chest. But once inside, it’d be prudent to switch to a scalpel, maybe even a laser.

There are advantages to the big and slow weekly time frame. For example, once a level is put in, it takes considerable time and price movement to create a new one. With this semi-static phenomenon, you have the
advantage of time to plan your strategy. Then, you can come up with the precise execution once the security comes into range on your time frame.

Another advantage is leaning against the precision of two or more time frames. Going back to our surgical analogy, you’d want to open the chest with the large tool to get the heart, not the brain. It’s the same with trading. The bigger time frame gives you the generalities, and the smaller one the precision and additional risk management considerations, and levels to manage your trade through.

Let’s get back to the quote. There is a lot of news hitting the wires all day long on euro land and the US. It seems to constantly change the story (read – what the outcomes might be). One thing that technical analysis does well is help lift the fog of war. When done correctly, it should give clarity and add actionable info to the decision making process. Let’s take a look at the EURUSD futures contract for some additional info.

Below is a chart of the CME futures contract, and included along with the VBTA is volume analysis. This chart gives some clues to where buying and selling pressure are located. From the weekly time frame, on 4/8/11 a wall was put in using volatility based resistance. This gave us a range to watch. Then, we could see from our volume work that sellers came in and acted on this level, and later more aggressive levels further away from weekly resistance. This was an important clue.

Finally the EURUSD is beginning to come upon MTF support near 1.325. Below this is projected buying pressure at 1.270. So what would add even more weight to the 1.325 MTF level? To see evidence of new buying pressure coming into market near the 1.325 level. If the news is not
favorable, larger buyers may wait for that lower level.

Carson Dahlberg, CMT, is a technical trader and researcher. He specializes in Quantitative Technical Analysis & Trading, revolving around volume and volatility. He was awarded the Chartered Market Technician designation in January of 2008. He founded and served as Chapter Chair of the Charlotte Chapter for the Market Technicians Association. In addition, he is the Director and an Instructor for the CMTInstitute, an online series of classes to assist with passing the CMT examination. He serves on the Board of Directors for the Market Technicians Association on the Ethics Committee, the Admissions Committee, and the Journal Committee. He received a degree in Chemistry from the University of Cincinnati.

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WHICH INDICATOR WILL WORK FOR YOU?

Editor’s note: ChartFilter Newsletter originally published this article.

To choose which technical indicators work best for you, we suggest following some key steps to develop a technical analysis checklist.

We can assume that traders have at least one common goal: To make profit.

Traders have various levels of expertise, different experiences, risk levels and general market exposure and therefore different investment goals. This is why traders will have different criteria in their checklists and why something may work for one but not another. Part of understanding which indicators will work for you is to think about why you would be willing to either buy or sell a stock. You can do this by creating your own technical checklist.

Setting up a system

This system will comprise of the following elements: a technical checklist for each buy or sell decision; a fundamental checklist for each buy or sell decision; and a set of rules.

Setting up a technical checklist can help you decide whether it is a good or bad time to buy/sell the stock (and to ultimately answer the question: "Which indicators will work for me"). The checklist(s) should be able to mark the change in the trend you are trading as well as the direction. For example: when trading a minor swing, the checklist will move from downtrend, to sideways to uptrend. Some point during this progression will be the traders entry point. The entry point should have the "perfect score" on your technical buy checklist. The exit point will be covered by your technical sell checklist, a perfect score here means sell.

The intention of the fundamental checklist is to help decide whether or not the company is worth investing in. Does this company have the base fundamental characteristics to justify the current or future stock price? This checklist is a combination of earnings reports/expectation, news, revenues, politics, etc. A high score here is bullish while a low score means bearish fundamentals.

The rules are to keep you on track. Don't break your rules since the only person you hurt is yourself. Rules can also be statements which define your goals like "ride the profits and cut the loses" or "take out emotion". Several of these nifty rules and statements will also be provided in the example checklists however, each trader should really define their own.

We will only be covering the technical checklist in this newsletter,

Defining what trend you plan to trade

If you have not decided yet what trend you plan to trade let's consider some key points.
It is important to note that not all technical indicators work well in all time frames. This is also why most technical indicators allow the ability to adjust certain parameters. These differences in time frames will result in different indicator and parameter choices. This is why what works for me may not work for you.

Quick note on trend overview
There are three types/categories of trends.

1. The uptrend which is defined as a price movement with successively higher peaks (highs) and higher troughs (lows).
2. The downtrend which has successively lower peaks and troughs.
3. The sideways trend which peaks and troughs don't successively rise or fall.

Each trend has (typically) three parts/stages. The primary (major) trend is a long term trend lasting from a year to several years. The secondary trend (or mid-term trend) lasts three weeks to three months and represents corrections of one third to two thirds of the previous movement - most often fifty percent of the movement. The minor trend (or short-term trends) lasts less than three weeks and represent fluctuations in the secondary trend.

Test your trading system on paper first! If you don't understand why you are buying or selling a stock, don't do it. Until you are confident in your decisions don't worry about what you are missing out on while paper-trading. A little bit of practice and patience will save you a bundle here. Be confident in your "why should I buy it checklist" and "when should I sell it checklist."

The Technical Checklist
A technical checklist is a list of technical indicator conditions which must be met to make a buy or sell decision. Here are two important reasons to have a technical or fundamental checklist.

A technical checklist helps you to time your buy and sell decisions. Technical
analysis, for the most part, is based on trend analysis. Whether through overbought/oversold, momentum, or other technical conditions, they primarily mark trend direction and changes in the direction of the trend. Technical signals do not offer any real forecasting ability. The ability to mark trend and changes in trend is an important key to improving your investment decisions.

A technical checklist helps you structure your goals and define the minimum trading requirements that must be met to define a buy and sell condition. It will also give you the ability to fix and modify your decision requirements.

A side note: A technical checklist should be balanced with a fundamental checklist. The intention of the technical checklist is to help decide whether it is a good or bad time to buy the stock (i.e., direction of trend) or if it is time to sell the stock you have (trend reversal). The intention of the fundamental checklist is to help decide whether or not the company is worth investing in. Does this company have the base fundamental characteristics to justify the current or future stock price?

A complete trading system should have a technical and fundamental checklist to decide to buy and a technical and fundamental checklist to decide to sell.

Fitting technical indicators to your timeframe

Different parameter settings will make the difference between an effective technical system and one that produces signals outside your preferred time frame.

Parameters should be based on your trading time frame. A short-term trader needs a more sensitive indicator, using smaller numbers; while a long-term trader can use a larger number of trading days in their formula.

To figure out which parameter fits, here are some tips:

1. Are you a short-term trader? **Using smaller numbers for your parameter will make the indicator more sensitive to recent price moves and trigger signals more often.** However, the older data is ignored (it is more difficult to apply the longer term trend lines). So if you trade a longer term and use a small parameter, you can be whipsawed. It is also more difficult to draw accurate trend lines since the indicator is more volatile (moves quickly up and down).

2. Are you a long-term trader? **Using larger numbers for your time frame ensures that older prices movements are still accounted for. Signals are generated less often and sudden price movements are averaged out.** The larger your parameter, the less sensitive the indicator to short term swings.

The concept behind larger parameter numbers versus smaller parameter numbers is extremely important in our next step, so I will go over some example parameter settings before we choose some indicators.
Example parameter settings (RSI & Stochastics)

RSI parameter settings

Signals generated by RSI

1. Extreme values:
Crosses extreme values, 70/30. The 70% and 30% levels are used as warning signals. An RSI above 70% is considered overbought and below 30% is considered oversold.

2. Double Tops and Bottoms:
Traders watch for double tops or what Wilder referred to as "failure swings." If the RSI makes a double top formation, with the first top above 70% and the second top below the first, you get a sell signal when the RSI falls below the level of the dip. Conversely, a double bottom at or below 30% (with the first low below 30% and the second at or above the same level) gives you a buy signal when the RSI breaks above the previous peak.

3. Divergences and Convergences:
Trend of the RSI relative to the trend of the price is where a trader sees the convergences or divergences. A convergence is when the price is downtrending, yet the RSI begins to uptrend (the two lines converge). A convergence is a bullish warning signal. A divergence is then the price is uptrending and the RSI begins to downtrend (the lines separate). The divergence is a bearish warning signal.
Stochastic parameter settings

Signals generated by Stochastic Oscillator

The Stochastic Oscillator generates signals in three main ways:

1. Extreme values when the 20% and 80% trigger lines are crossed.
   Buy when the stochastic falls below 20% and then rises above that level. Sell when the stochastic rises above 80% and then falls below that level. The pattern of the stochastic is also important; when it stays below 40-50% for a period and then swings above, the market is shifting from overbought and offering a buy signal. And vice versa when it stays above 50-60% for a period of time.

2. Crossovers between the %D and %K lines. Buy when the %K line rises above the %D line and sell when the %K line falls below the %D line. Beware of short-term crossovers. The preferred crossover is when the %K line intersects after the peak of the %D line (right-hand crossover). Crossovers often provide choppy signals that need to be filtered through the use of other indicators.

3. Divergences between the stochastic and the underlying price. For example, if prices are making a series of new highs and the stochastic is trending lower, you may have a warning signal of weakness in the market.

For a more conservative approach, extreme values should be used as the warning signals and the follow through the 50 line for the confirmation of
the trend change. Some traders also state that by moving the extreme values to the 10 and 90 lines helps ensure a more reliable signal.

Examples of the different slow stochastics parameter settings

The general rule of thumb for most indicators is that when you increase the parameter the indicator "smooths out." Larger numbers for parameters make the indicator less sensitive to recent moves and the longer-term trend is more apparent. When you decrease the parameter value, the indicator becomes more sensitive to the recent price moves and allows the trader to react more quickly. The shortfall to this is that the indicator no longer shows the longer-term trend well and may report signals during a correction rather than a breakout (which are what some short term traders are looking for).

Choosing some technical indicators

Now that we have covered trend, timeframes and parameter settings, we can get down to choosing some complimentary technical indicators.

So here is the next tip. According to Bollinger, one of the biggest mistakes in technical analysis is the multiple counting of the same information. For example, using different indicators all derived from the same series of closing prices to confirm one another.

There are quite a few technical indicators featured on ChartFilter.com. Where do you begin? I would recommend starting with the following approach to using a combination of indicators in your analysis.

1. Start with moving averages and draw trendlines to give you an idea of mid to long-term trends.

2. Use one or two oscillators, such as MACD, stochastics, RSI, etc. Pick one or two that you feel most comfortable with and go with them. I often use MACD (because it provides such clear signals) and one
other. MACD compliments, but does not replace, some of the others which are better suited as overbought/oversold indicators.

3. Use a volume indicator, such as OBV, MFI, etc. (see the last issue of ChartFilter newsletter for examples of their value).

4. You might want to check if one of the bands or channels gives you any additional information (Bollinger bands, price channels, MA envelopes, etc.).

5. You may also want to use a more advanced indicator. I recommend Wilder’s indicators; DMI, ADX and the Parabolic SAR. These are in themselves complimentary indicators and provide extremely useful buy and sell signals.

Once you have chosen a base set of indicators, you will need to fit them to the curve you are trading. To do this, take a charting program (we suggest StockTools), take your/any stock, apply indicators and alter parameters so that the signals line up to your curve.

**Sample checklist**

**Point values**

This checklist will be scored the following way: if sideways or no signal, put in negating column.

In this case I have chosen only a couple of easy indicators to start with. The following checklist on MSO is more complex.

**SAMPLE simple DJIA technical checklist**

**Trendlines & Patterns**

 +/- 1 point - strong pattern, major trend +/- 0.5 point - weak pattern, minor trend
 +/- 1 point - Above or below price line +/- 1 point - moving averages cross
 +/- 1 point - signal line cross +/- 1 point - zero line cross
 +/- 1 point - convergence / divergence with price line
 +/- 1 point - crossed extreme point (30/70) +/- 1 point - convergence / divergence with price line
## Conclusion

The answer to the question: "Which indicators work for me?" can best be answered by building a checklist, setting up your indicators to your timeframe, testing, fixing and repeating. When you are confident in your signals, then you will know what indicators work for you.

Some basic rules should apply no matter what your indicator choices are. Ride your rights and cut your losses. When you are wrong, find out why (there is always a reason) and fix the system so you do not repeat the mistake. Stick to the rules - they are there for a reason.

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Chartfilter offers charting, stock screening, portfolio management, fundamentals, and free technical analysis education along with free stock analysis newsletter. The company offers one place to meet all of your technical analysis needs. They also pledge that "If MTA members require any technical indicators and/or functionality we don't currently offer, just e-mail us and identify yourself as MTA members and we will put your request in our development time line." Additional details are at [www.chartfilter.com](http://www.chartfilter.com).

| **Stock Check List - DJIA short term trend checklist** |
|---|---|---|
| **Stock:** DJIA | **BUY/SELL Rating:** +2 | **Date:** sample (April 2005) |
| **Indicator** | **Confirming** | **Negating** |
| **Trending Indicators** |
| Trendlines | bounced off support +0.5 | Major down |
| 5 & 20 day SMA's (no cross yet) | 5 day SMA below price line | 20 day SMA above price line no 5 & 20 day sma cross |
| MACD | MACD signal line cross did not quite cross yet (+0) | MACD-H convergence |
| | MACD-H zero line cross |
| RSI | RSI crosses up through 30 |
| | RSI convergence, trend did not fully break, +0.5 |

| **Points:** | **5 positive** | **3 negative** |
TRIFECTA: STOCK, OPTION, IMPLIEDS
BY KIRK NORTINGTON, CMT

Editor’s note: This article is reprinted as an example of a well-defined and insightful style of technical analysis. The chart is an integral part of the analysis and should be viewed in full size at http://go.mta.org/175

This morning (11/15/11) the stars lined up for IBM. A form of triangulation is to simultaneously perform Volatility-Based Technical Analysis on three important time series. Strap on your thinking cap.

1) IBM underlying equity
2) IBM $190 call option, expiring 12/17/2011
3) VXIBM, which is the IBM VIX Index; proxy for implied volatility

Below are three side-by-side 30 minute charts of the above. The bottom indicator in each chart shows the MetaSwing Extremus indicator which is a volatility-based momentum indicator. Plotted next to each is the distribution histogram of the recent reading of the Overbought (red) line. The upper end of this indicator construct is unbounded and rises with the volatility of the short term move.

In the price pane of each chart MetaSwing N bands, and Support/Resistance lines. Also shown are MetaSwing directional signals.

Chart 1: At about 11:00 am this morning IBM shares fell to the SR5 line and found support. Simultaneously its Overbought momentum reaches a volatility high. Relative to its readings over the past 30 days, this level was
extreme; which is confirmed by the red distribution histogram at lower right. Combined with a bullish trend indication, this makes four different reasons why price should pause or reverse: trend, momentum, support, and high probability (quantitatively tested) directional signals.

Chart 2: At about 11:00 am this morning IBM 190 calls also drop to the N Band support and slide down the right (right translation), to the SR4 support line. Simultaneously its Overbought momentum reaches a volatility high. Relative to its readings over the past 30 days, this level was extreme; which is confirmed by the red distribution histogram at lower right. Just like the underlying, the call has four different reasons to pause or reverse; trend, momentum extreme, support, and in this case a HS directional signal. (that’s a High Slope rising N band reversal signal).

You get the picture right? The stock and the call agree; star alignment. But there’s more.

Chart 3: At about 11:00 the IBM VIX (volatility) is at a midpoint between support and resistance, and its momentum measurement are at equilibrium. There’s nothing to limit volatility for a move in either direction. However in this case it would have been more favorable if the VXIBM had been higher moving into resistance.

From a risk reward perspective your target is about 1 ATR below the upper N band at 190, and the risk is 1/2 ATR below SR 6 at 184.40. With an SRS line entry at 185.65, this gives you a 4.35 to 1 reward to risk ratio.

This setup combines two different groups of traders; option and equity. It also presents four different reasons for a long directional trade: trend, momentum, support, and high probability (quantitatively tested) directional signals. This all contributed to a healthy price reversal.

What’s next? In looking at Chart 3, the Overbought momentum is not near an extreme and could rise much further. Also the VXIBM has room to fall to the SR7-8 support zone. Likewise IBM and its 190 call have room to rise into overhead resistance. Right now there’s enough reason to think that price will continue higher. Actually the next resistance at SR2 on the daily chart is at 196.21. I think that’s its next most probable destination in the next two weeks.

Kirk Northington, CMT, is the founder of Northington Trading, LLC, and the co-creator of MetaSwing; advanced analytic software for Bloomberg Professional, MetaStock and TradeStation. He is the author of Volatility-Based Technical Analysis: Strategies for Trading the Invisible, Wiley Trading Series, John Wiley & Sons Publishers. Kirk is a quantitative technical analyst. Kirk has a BS degree from Nicholls State University, in Thibodaux, Louisiana. He has extensive experience in control system and software engineering.

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Investment Courses For Professionals

A sample of a growing list of fundamental and technical courses is shown below. The courses are associated with global destinations and dates, both for open and private client formats. They are produced by various knowledge vendors throughout the world. Details can be provided by contacting NYIF.COM, or John Palicka (palicka@pipeline.com).

**FUSION ANALYSIS**
This is a professional approach thatblends fundamental, technical, behavioral and quant strategies.

**EQUITY PORTFOLIO MANAGER**
Serious managers will utilize this course to analyze leading Wall Street valuation models and investment strategies for equities using fundamental, behavioral/technical and quant approaches, and then study how these are modified by the best performing equity portfolio managers to produce risk-adjusted excess returns.

**INVESTMENT FUND SELECTION**
This is a must attend course for all professionals involved in the selection and management of third-party investment managers.

**TECHNICAL ANALYSIS CMT 1**
A must attend course for investment professionals wishing to gain the CMT Level I professional qualification in Technical Analysis from the Market Technicians Association (MTA).

**INTRODUCTION TO STEALTH TRADING USING FUSION, ALGORITHMS, AND DERIVATIVES FOR PROFESSIONALS**

Today, portfolio managers increasingly must use stealth trading in order to disguise their intentions and thus benefit from best execution.

**ADVANCED CAPITAL MARKETS ANALYSIS**
Spot, forwards, futures, swaps, options, and statistical issues are discussed in dynamic capital market strategies.

**STRATEGIC GOLD INVESTING**
Gold has been one of the very few assets to have created wealth in the past several years. Gold offers investment opportunities for investors, traders, and financial engineers.

**GLOBAL SMALL CAP INVESTING**
Global small cap stocks offer investors the ability to participate in the world’s future big winners.

**PORTABLE WEALTH INVESTING**
Portable Wealth (PW) management offers investment opportunities for wealthy investors and their advisors. PW can generate attractive risk-adjusted excess returns to traditional and alternative investments.

Instructor John Palicka CFA CMT is a top-ranked portfolio manager of Global Emerging Growth Capital ([WWW.GLGEBC.COM](http://WWW.GLGEBC.COM)) with over 30 years experience of managing $ billions. He has doubled client money, on average, every 4 1/2 years since 1980*. His high course ratings from major investment firms reflect clear interpretations and practical applications of complex topics; knowledge applied to examples and cases found in the current worldwide and GCC marketplace; his experience with specific situations actually encountered in his career and consulting contracts that parallel the learning topics. John has an MBA from Columbia University and also teaches these courses for leading training institutions, including The New York Institute of Finance ([WWW.NYIF.COM](http://WWW.NYIF.COM)).

* Past performance is no guarantee of future results.
INTERVIEW WITH AJAY G. JANI, CMT
BY AMBER HESTLA

How would you describe your job?
I manage an emerging markets focused Global Macro fund which invests in all liquid asset classes (interest rates, credit, currency and equity) on a directional basis. I also manage an emerging markets equity trading fund, and help develop ideas to better hedge our firm's distressed credit portfolios.

What led you to look at the particular markets you specialize in instead of another tradable?
I studied International Economics as an undergraduate, and spent a year abroad in Hong Kong as part of my curriculum. After school I worked for a large asset management firm, focusing on the US fixed income market. I worked with very smart people and learned a lot. The experience gave me a good base in finance but it wasn't my true calling. I went to Columbia Business School to earn an M.B.A. and during my summer internship at a large investment bank; I had the opportunity to spend some time on the emerging markets desk.

This was in the early 90s when they still called it LDC (Lesser Developed Countries) instead of emerging markets. Wall Street still hadn't figured out EM so they put all the products on one desk and hoped for the best. I was hooked right away; since there were so many different asset classes and strategies that one could be a part of. After business school, I was offered the chance to join the EM desk directly instead of going through the rotation process again, and I've never regretted taking the leap.

Do you look at any fundamental or economic inputs to develop your opinions?
Absolutely. I am not a purist that forsakes all other options for the sake of ideological rigor. I will use all information I think is relevant to finding the best ideas and will use the best techniques to manage risk while trying to grow our capital. Within the emerging markets space, fundamental and especially political developments are much more important than they are in developed nations and it would be almost irresponsible to ignore this information while making investment decisions.

Can you share any longer term market opinions?
We're screwed! We no longer have the dilemma of good or bad choices. Because of the poor decisions we've made in both the public and private sector over the past 30 years, we are now in a situation where we only have bad and really bad choices.

The next decade or two are going to be very challenging to our society as we seek to reduce our debt to levels that are more manageable. This probably means more frequent recessions, shorter recoveries, and higher volatility in asset prices. Some characterize this as the "New Normal". In fact, it is the old normal that prevailed prior to the debt fueled 1982-2000 boom.
The implication for investment behavior seems pretty clear; being tactical and flexible will be absolutely necessary to prosper. If I am correct, technically oriented investors may have a leg up on their fundamentally based peers.

I also believe, and not just because I am an emerging markets specialist, that the game plan going forward should be the mirror image of the 1982-2000 playbook. In that earlier era, EM crises would periodically cause pressure in developed markets, which provided an opportunity to buy healthy assets at good prices. Think Mexico 1982 or 1994, Asia 1997, Russia 1998 etc. Now the reverse should be true; use distress in the West to buy assets in the East. The 64 thousand dollar question is "when to buy" and I believe investors that incorporate technical strategies into their investment methods will be best prepared to answer that question.

What advice would you have for someone starting in the business today?
I'd have 4 suggestions:

1) Find a mentor as early as possible in your career. There is nothing new in Wall Street and there is no need to re-create the wheel.

2) Try every style of investment that intrigues you early in your career with small amounts of money. If you are honest with yourself, you will eventually discover which method is really suited to your temperament.

3) Never risk your livelihood on a trade. Always manage risk so that if you are wrong today, you'll have enough capital to trade tomorrow.

4) The most important advice is to make sure you really love the game. There is no use trying to work 16 hour days developing your craft if you don't really enjoy what you do. There are so many ways in this world to succeed beyond your wildest dreams that it’s not worth it trying to pretend you enjoy it when you really would rather be doing something else.

Ajay G. Jani, CMT, has 22 years of investment experience including 17 years in emerging markets. He currently runs the Macro business for Gramercy. Prior to joining Gramercy, he managed the quantitative emerging markets macro strategy for London Diversified Fund Management. In 2005, he became Managing Partner of Single A Capital LLC. From 1999 - 2005 he was at Banque Paribas, where he was head of the London-based European emerging markets external debt trading group which included oversight of a profitable client flow business and investing proprietary bank capital in credit. Mr. Jani is a frequently published author of various investment articles dealing with systematic and quantitative investment strategies and has studied Mandarin Chinese.

These questions and answers have been compiled by Amber Hestla, an independent market researcher. If you’d like to participate in a future interview, please contact her at hestlaresearch@gmail.com.
IF HISTORY TENDS TO REPEAT ITSELF, THEN EGYPTIAN STOCK MARKET INDEX IS LOOKING FOR A BOTTOM
BY RAMY RASHAD, CMT

It’s our job as technical analysts to search for repetitive patterns in the charts. Who lied to you and told you that TA is all about H&S and trend lines? Technical analysis’s most basic concept is that “History tends to repeat itself over and over.” Of course, recurring patterns may not be identical, but knowing that a certain manifestation is being repeated could help make a difference. In our unstoppable search, we found something and would love to share with you, the Egyptian Exchange EGX 30 Index. A current market quote can be found at http://go.mta.org/177

Relative Strength Index (RSI): Taking out the Red Resistance Line in 2009 was the first real signal of a rally that would see the market reach a level of nearly 7,700. A thrust up over this line, which gave a Negative Reversal signal (see green lines in both price chart and RSI), has followed by a thrust down to the rising dotted brown line, slightly over the red Bear Support Line. The RSI, before any other tools, has signaled a beginning of a rally just at a bottom. We have, so far, a nearly similar pattern; triangle, multiple positive divergences, a thrust-up over both the dotted declining line and the Bear Resistance Line, Negative Reversal signal and a thrust-down to a confluence of support from the apex of the triangle. Should history repeats itself, the RSI will find support somewhere over the 20 level, and will bounce strongly giving an early signal of a BOTTOM. The Negative Reversal Signal may force the index to the 4,000 level (a measured target of the NR signal), the Oct low, or even slightly lower. But as long as
the RSI lies over both the rising dotted brown line and the red Bear Support Line, I don’t care where the market will hold its breath, because, given this recurring pattern, it will do that in the near future. The RSI is making me bullish and only a decline to below the 20 level in the RSI will make me completely bearish.

MACD:
Do you know that the MACD is giving its second strong Positive Divergence signal since 2009 bottom?!

The indicator, since 2008 top till now, is moving in just two channels. A breakout over the first channel took place at mid December 2008, months before the bottom in the price itself (see the first green rectangle). The MACD has built a double bottom, successfully penetrated its neckline, found an obstacle near the declining dotted red line and is currently pulling back to a SZ. Taking out this line offers a very important conservative Buy signal.

**Ramy Rashad, CMT is Senior Technical Analyst & Head of Trading Desk at Jazira Capital, a securities brokerage and asset management firm in Egypt. He has been trading currency and equity markets for several years, has carried a position as a Co-owner at Markets Analysis (A specialized website in stocks and currency market analysis). He holds a Bachelor degree in Communications Engineering from AAST, Arab Academy for Science & Technology. Mr. Rashad is a CFA candidate.**

**The Future of Technical Analysis has arrived.**
MAJOR CATALYSTS AHEAD TO TRIGGER NEXT BREAKOUT IN GOLD MARKET
BY JORDAN ROY-BYRNE, CMT

In bull markets, corrections and consolidations are needed to periodically cleanse the market of extreme optimism and an overbought condition. After a market has strong run it inevitably reaches a point of resistance. This is where there are more buyers than sellers. A market can correct in two ways. Either it declines and retraces much of the preceding gains relatively quickly or a market will consolidate near its highs for a long period of time. The first correction is a function of price while the second, time. The correction or consolidation ends when a fundamental catalyst emerges which triggers greater demand that overwhelms current supply.

The consolidation has endured due to a working off of the overbought condition from 2009-2010 gains as well as the lack of a real catalyst. The Fed, though accommodative has been on hold while emerging markets turned their focus to inflation. European bond markets were in fair shape into the summer. However, the good news for gold investors is that a trio of major catalysts lie on the horizon and should easily trigger the next breakout.

The obvious catalyst is a massive bailout of European nations and European banks through a $3 Trillion debt monetization (the figure stated by many). Until last month the European crisis was limited and a hope of being contained. Since then interest rates on French bonds, which had been following Germany began following Spain and Italy higher. The 10-year yield on French bonds has surged in the past six weeks from about 2.50% to nearly 4%. Meanwhile, Ambrose Evans Pritchard, the intrepid reporter wrote that Asian investors are pulling out of German Bunds and Europe all together. Bund yields (10-year) look to be forming a double bottom just below 2%. Bunds stopped rising in last month as yields surged in Spain, Italy and France. Understandably, Germany has stood in the way of an ECB...
bailout. However, the sooner the crisis spreads to Germany, the sooner we can expect a German-led ECB bailout.

Moving over to Asia, we hear that China has started to turn its focus away from inflation and towards growth. Last weekend the Chinese Vice-Premier, Wang Qishan indicated publicly that “ensuring growth is the overriding priority,” and “unbalanced growth would be better than a balanced recession.” He also noted the persistent weakness in the global economy.

China’s tightening, which began October 2010 has been effective. It was recently reported that Chinese inflation rate has fallen in recent months from a high of 6.5% to 5.5% and industrial production growth slipped to a one-year low. GDP growth has slowed in recent quarters from 9.7% down to 9.1%. According to analysts at Citigroup, the slowdown could intensify. Bloomberg reports:

If tightening measures aren’t relaxed, property investment will “scale back significantly” in the next two quarters, “dragging down the whole production chain and GDP growth,” Minggao Shen and Ben Wei, analysts at Citigroup, wrote in a report dated yesterday. Exporting firms are also facing an environment worse than in late 2008 due to the overseas slowdown and rising costs, they said.

Last but not least let us consider the USA. Our bond market remains the strongest in the world while the US Dollar is likely to rally further in the near term. This combination along with lower commodity prices and a global move to inflationary policies will allow the Fed the political cover to institute another round of debt monetization. Combined with potential action in China and imminent action in Europe, this is powerful policy that should result in a massive catalyst for select markets.

The current investor psychology of fear, indifference, and surrender is leaving them vulnerable as they miss the big catalysts that lie directly ahead. Gold and gold stocks remain in excellent position for a potentially tremendous 2012 and 2013. Required action from Europe, a shift in Chinese policy and more monetization on steroids from the Fed is going to catapult the bull market in precious metals like we haven’t seen since the late 1970s. In our premium service, we seek to manage the short-term risks in this volatile sector while keeping focused on the major opportunities. The technicals are lined up while fundamental catalysts are soon to emerge. The combination could lead to an explosive 2012 for gold bugs.

Jordan Roy-Byrne, CMT, is the editor of The Daily Gold Premium, a service began in July 2009. The model portfolio gained 57.0% in the last six months of 2009 and gained 86.5% in 2010. As of June 6, 2011 the portfolio was up 10.5% year to date while GDXJ (junior gold stocks) was down 9.5%. His work has been featured in CNBC, Barrons, Financial Times Alphaville, BusinessInsider, 321gold, Gold-Eagle, FinancialSense, GoldSeek, Kitco and Yahoo Finance. Additional details can be found at http://thedailygold.com/.
TECHNICALLY URANIUM

BY MERV BURAK, CMT

BASIC NOTES

Uranium Companies: There are very few pure uranium companies. Most companies, especially the small exploration type, are active in more than the uranium industry. This blog makes no attempt to gauge the percentage of a company’s activity that is related to the finding, mining or processing of uranium. They all do, however, have some uranium activities (to the best of our review).

Merv’s Uranium Indices: I have developed two Uranium Indices. They each have the same component stocks but are calculated using different methodologies. My weekly Index is based upon the average weekly performance of the component stocks. My daily Index is based upon the daily average of the component stocks open, high, low and close prices along with the daily average volume of all component stocks.

Merv’s Daily Uranium Index, Market Data for Friday 25 Nov 2011

Open: 128.56
High: 130.60
Low: 126.85
Close: 128.12
Volume: 1459

Note that the volume is an average volume of round lot sales for the 50 component stocks. For total volume, multiply by 5000.

Every now and then I like to look back to see where we have been. This week’s long term charts once more take us right back to their respective beginnings, the Weekly Index from the start of 2003 and the Daily Index from late 2006. We can only compare their respective performances since late 2006 as the Daily only started then. What we see here is basically the same as what I have seen in the precious metal stocks (gold and silver) when comparing the performance of the speculative stocks versus the performance of the “quality” stocks.
As long time readers to these commentaries remember, the Weekly Index is most influenced by the low priced (speculative) stocks while the Daily Index is most influenced by the high priced (quality) stocks. Both Indices have the very same set of 50 component stocks.

From their highs in 2007 to their lows in late 2008 BOTH Indices lost just about the same percentage, the Weekly lost 87% while the Daily lost 84%. From the 2008 lows to their peaks in early 2011 the Weekly gained 517% while the Daily gained only 205%. Now, from their early 2011 high to the present the Weekly has lost some 66% and the Daily lost 55%. When one views the significantly higher upside potential of the speculative stocks versus the quality stocks and then you see that they BOTH decline about the same amount during a bear market, which class of stocks are you interested speculating in (and ALL uranium stocks are speculations)?

Of course, as technicians or those who follow the technical discipline, one would not be holding the stocks all the way down praying for a quick recovery while one would be holding the stocks as they continued their climb during a bull market. The net result should be even more spectacular than the Weekly Index itself would suggest.

As the saying goes, “you buy the performers and dump the bummers”.

Editor’s note: What follows is a normal weekly commentary.

What can I say? It was a bummer of a week for uranium stocks with both the Weekly and Daily Indices falling by about 9%. It looks more and more like we’re in for a test of the early Oct low although we just might not get that far as the Daily Index short term momentum indicator has already entered its oversold zone from where previous rallies have occurred.

On Friday the Merv’s Daily Uranium Index closed lower by 0.93 points or 0.72%. There were 14 daily winners, 23 losers and 13 stocks that didn’t have a clue which way they wanted to go. Looking at the five largest stocks in the Index, Cameco lost 0.8% on the day, Denison gained 1.6%, Paladin lost 2.7%, Uranium One lost 0.5% and Uranium Participation didn’t have a clue which way to go. The best daily winner was Benton with a gain of 11.8% while the loser of the day way Strathmore with a loss of 10.7%. Market Vectors
Uranium + Nuclear Energy ETF lost 0.5% while Global X Uranium ETF lost 0.7%.

For the full week the Merv’s Weekly Uranium Index lost 412.90 points or 8.83% (the Daily Index lost 9.07% on the week). There were only 2 weekly winners but a whole bunch of losers (45 of them). There were 3 stocks that didn’t have a clue which way to go. Cameco lost 10.4% on the week, Denison lost 16.2%, Paladin lost 7.6%, Uranium One lost 11.6% and Uranium Participation lost 5.1%. A slaughter all the way around. The best weekly winner (of those brave 2) was Kivalliq Energy with a gain of 8.6% while the loser of the week was Uranerz Energy with a loss of 22.3%.

Market Vectors Uranium + Nuclear Energy ETF lost 7.3% while Global X Uranium ETF lost 10.6%.

**LONG TERM**

Trend: The long term trend remains negative with both the Daily and Weekly Indices moving lower below their respective negative sloping long term moving average lines.

Strength: The long term momentum indicators for both Indices remain in their negative zones and below their respective negative sloping trigger lines. At the present time there is no real sign of either strength or weakness in this indicator versus the performance of the Index itself.

Volume: The volume indicator has been tracing a basic lateral path although it did move slightly above its long term trigger line the other week. It is once more below its trigger and the trigger continues to point in a downward direction.

Putting it all together one can only give the long term a rating of BEARISH at the Friday close.

**INTERMEDIATE TERM**

Trend: The Daily Index continues to move lower and lower and heading towards a test of the 118 early Oct low. It remains below its intermediate
term moving average line and the line continues to slope in a downward direction.

Strength: The intermediate term momentum indicator almost reached its neutral line about a month ago but has been reacting lower ever since. It remains in its negative zone and below its negative sloping trigger line. A close look at the indicator might suggest that it is not quite as weak as the price action might suggest but let’s wait and see how it develops.

Volume: For the past two months the volume indicator has been trending higher but this week it fell below a well established intermediate term up trend line and down it goes. It is also below its now negative trigger line.

On the intermediate term BEARISH is the only rating I can give, at the Friday close. This bear is further confirmed by the short term moving average line tracking below the intermediate term line.

SHORT TERM

This is where one would expect new trends to show up first. Unfortunately, nothing new is yet showing up.

Trend: The short term trend collapsed a month ago and since then it has been a downer all the way. The Daily Index remains below its negative sloping short term moving average line. There is a little hint that the slide may be about to end, if only on a very short term basis, but it is a very little hint and needs more confirmation before jumping for joy.

Strength: The short term momentum indicator has been in a steady decline for the past month and remains in its negative zone below its negative sloping trigger line. The indicator may or may not already be in its oversold zone. The level used as the oversold level can be fluid with different stocks or Indices and depends upon the volatility of the ongoing market action. Most software programs automatically use 30% as the oversold level while I am inclined to often use 20% for more volatile stocks or Indices. In one case the momentum indicator is not quite in its oversold zone while in the other case it already has entered the zone. In whatever case, it is at a level where one can start looking forward to a rebound of some sort.

Volume: The daily volume action has been pretty low during the week. This may be due to the American’s taking some time off to celebrate their Thanksgiving or it just might be some additional effect due to my component stock revision this past week. I had deleted 5 stocks and introduced 5 new ones. Their volume actions may not have been directly replaced. In any case the volume during the week was low and this, under most negative days, would not be a surprise.

Putting it all together the short term rating at the Friday close is BEARISH. This bear is confirmed by the very short term moving average line moving ever lower below the short term line.

As for the immediate direction of least resistance, I’m going to go with the upside for the next few days. Although there is no clear sign of a trend
reversal yet there are some hints that the Daily Index and Stochastic Oscillator are strengthening and may be wanting to reverse. You pays your money and you get the bold predictions (of course, if the Indices should continue to decline we WILL forget about this prediction, wouldn’t we?)

Yes I know, it’s frustrating as hell this continual negative market BUT looking at the long term Weekly Index we can guess that once the stocks finally do bottom there will be some really, really great gains to be made for those who have waited.

Merv Burak, CMT, works as a Consulting Aerospace Engineer. As an underground surveyor in the gold mines of Canada’s Northwest Territories in his youth, he became well acquainted with the resource industry and now applies technical analysis to the stock market sectors and equities associated with that industry.

This has been previously published at http://go.mta.org/178 and is reprinted here with the permission of the author.
ETHICS CORNER: DEFINING PROFESSIONALISM
BY MIKE CARR, CMT

Technical analysis is a profession, but it is also an activity that is undertaken by many nonprofessionals. Professionals are experts who practice in accordance with well-defined standards.

The MTA’s Code of Ethics is one of the defining factors that separate the professional from the nonprofessional. To explain why the Code of Ethics is so important, we will step back and consider what it means to be a professional.

Numerous definitions of the term professional are offered. All revolve around the central idea of someone with specialized knowledge who makes a living in the field. For example, doctors and lawyers are considered to be professionals with very specialized areas of knowledge. This definition offers a simple way to distinguish those who are professionals, but more detailed definitions are also available.

Bloomberg News recently featured an op-ed that defined what makes the military a profession. The key part of the article read:

The 1957 publication of Samuel Huntington’s “The Soldier and the State: The Theory and Politics of Civil-Military Relations” occasioned a new degree of self-awareness among soldiers. Huntington insisted that the “modern officer corps is a professional body and the modern military officer is a professional.” He defined a profession as an entity that adheres to a codified set of institutional values; preserves the trust of those it serves; and employs practitioners with expert knowledge and skills, a sense of specialized vocation, and a commitment to a career of education and self-development.2

Using Huntington’s definition, technical analysis is a profession as practiced by some and the MTA plays a central role in raising the discipline to a profession. Although in this article, I will refer to the MTA, there are other professional organizations that professional analysts can join. It is also possible to be a professional without belonging to an organization. However, it would not be possible to have a profession without organizations such as the MTA.

Professionals in the field of technical analysis are distinguished by:

1. **A codified set of institutional values**, which is in part the MTA Code of Ethics. This is the first step towards defining a profession. Ethics are largely a set of common sense guidelines. However, a true profession has the most fundamental ethical principles captured with clear statements. Professionals adhere to values by choice and voluntarily subject themselves to discipline for violations.

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2. **Preserves the trust of those it serves.** Again, we can see that MTA Code of Ethics is important to this aspect of professionalism. Fair dealing with clients is a requirement of the Code, and several specific actions like insider trading and buying ahead of a favorable research report are specifically prohibited. Grey areas may exist in the minds of some professionals and the MTA maintains and operates an Ethics Committee to address questions and, in extreme cases, violations.

3. **Employs practitioners with expert knowledge and skills.** There are two key items in this part of Huntington’s definition – employments and expertise. Professionals make their living from their chosen field. It may not be a popular position to take, but it is not possible to be a true professional technical analyst while holding a full-time job in another career. Web sites offering technical analysis are easily found, and most are the work of nonprofessionals. The CMT designation further defines the professional nature of technical analysis by recognizing expert knowledge and skills and is limited to those who devote significant time to technical analysis and have demonstrated that they are professionals in the field.

4. **A sense of specialized vocation** is found in the organizations such as the MTA. The organization started as a way for professional technicians to meet and share ideas. Three professionals wanted more than a place to exchange stock tips, they wanted to advance the study and use of technical analysis. Prior to the founding of the MTA, there were a number of professionals in the field, but the MTA enhanced the profession and have technical analysis an enhanced degree of credibility.

5. **Commitment to a career of education and self-development.** The CMT itself signifies a commitment to education and the voluntary continuing education program offered by the MTA ensures that the commitment can be met throughout one’s career.

Individual technicians do not necessarily have to be part of an organization like the MTA to be professionals. But without professional organizations, there would not be professional technicians given the current state of regulation. Research made available by professionals to the general public must be based on accepted principles and practices, and a professional organization is needed to define standards.

The Code of Ethics is a vital factor in professionalizing the discipline by defining what the public can expect from technical analysts. As with other professions, there is no guarantee of success but there is an assurance that best efforts will be made to provide accurate and timely information with well-formulated opinions.

*Ethics Corner is intended to be thought provoking, it is not an authoritative source on ethics nor does it reflect the official positions of the MTA, the MTA Board of Directors, or the MTA Ethics Committee. This article is also not intended to be used as preparation for the CMT examination.*