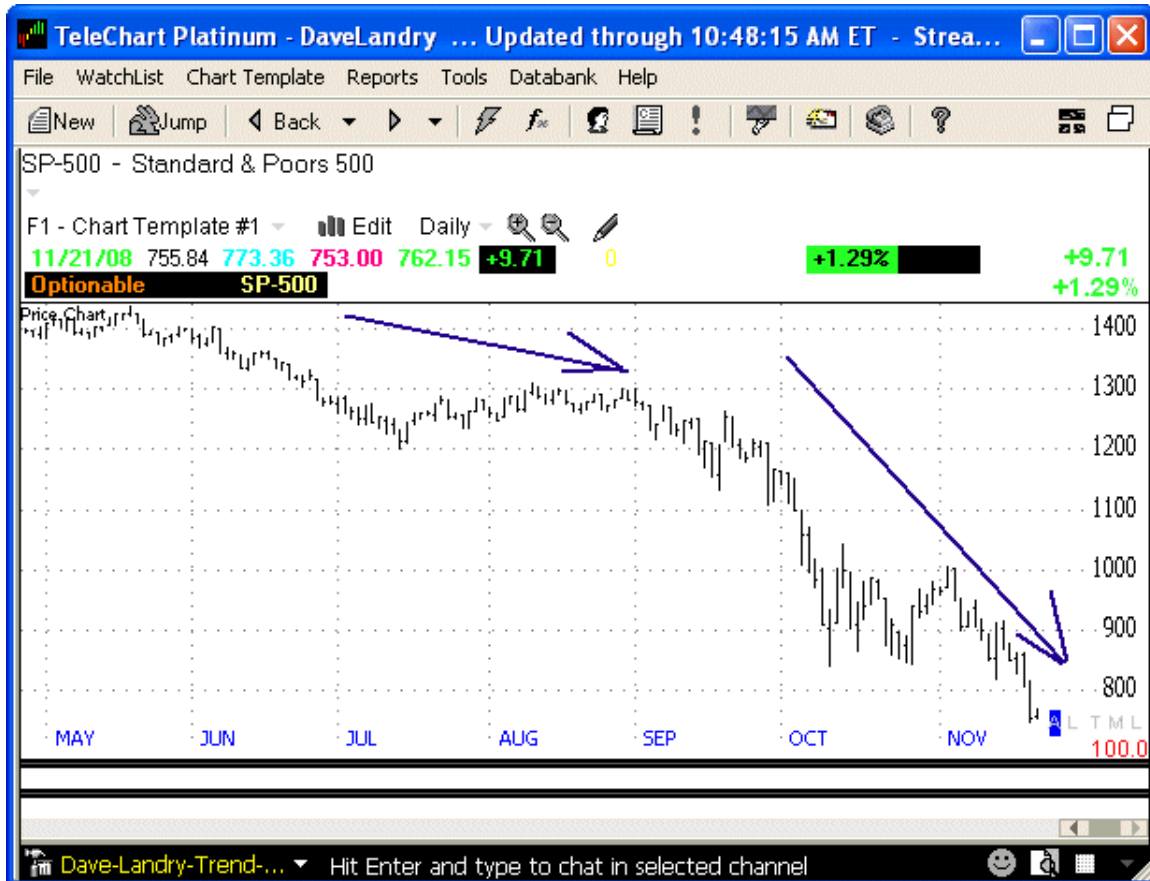


Putting the Pieces Together for a Textbook Trade

Before we get into techniques, let's take quick look at the US market. When I began these articles back in September (2008), I stressed the importance of trading with the trend. I also pointed out that we were in a downtrend. Well, since then we have dropped another 40 percent.



Of course, there's no guarantee that the market will continue to trend (and that's why I preach using protective stops!). As you can see though, it pays to follow it for when it does.

This week, I'd like to take a look at stock that set up in a perfect "textbook" manner. Below is the original recommendation I published in my service for 10/31/08 (email me if you would like the archives of all my recommendations).

SHLD-Sell Short

Sears Holding Company

Pattern: Persistent Pullback/Witch Hat

Entry: 54.70

Protective Stop: 70

Initial Profit Target: 39.40

Notice below the stock has been in a persistent downtrend (a) and then pulled back (b). This creates a pattern I refer to as a “Persistent Pullback.” Also notice that the sharp pullback forms a pattern I have dubbed a “Witch Hat.” We’ll cover these patterns in more detail in future articles. For now, just know that they are variation of a simple pullback (see prior articles for more on pullbacks).

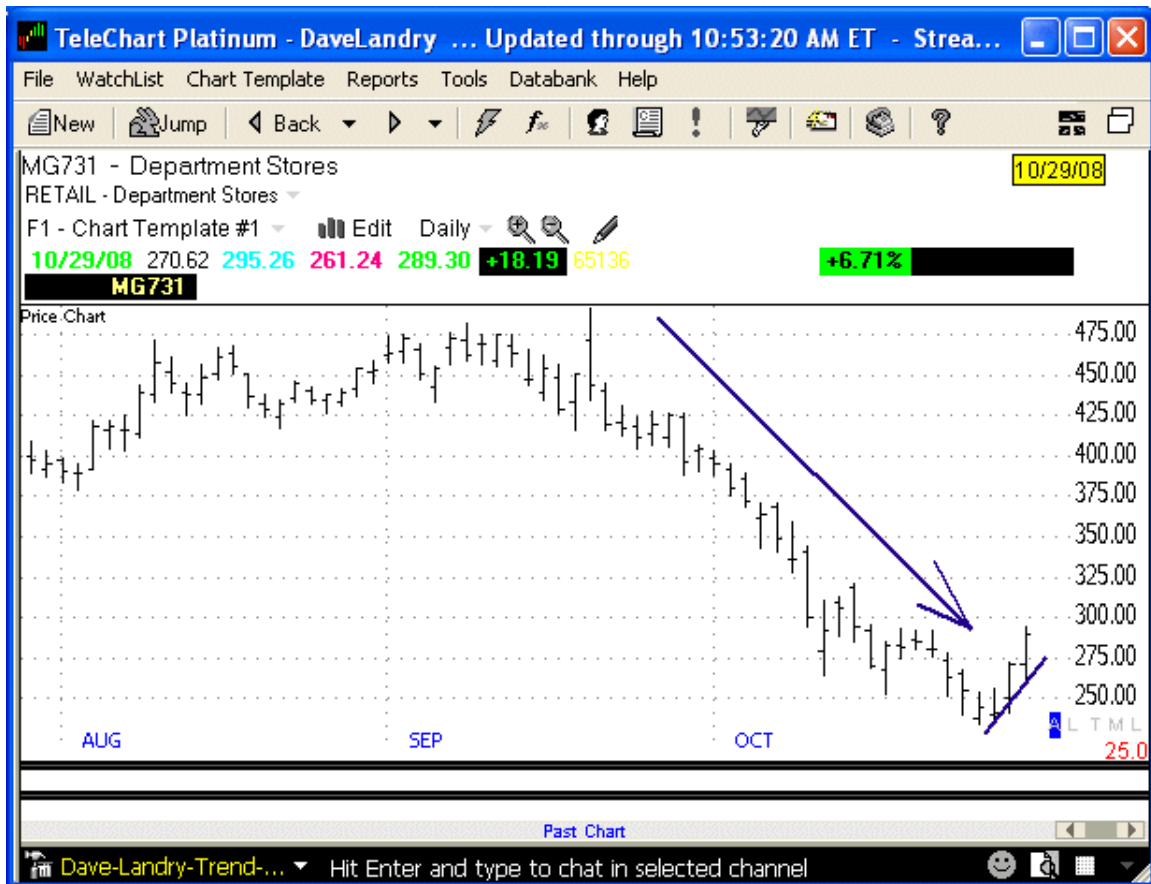
The stock is set up perfectly. It’s in an obvious downtrend (a) and pulls back in an orderly fashion (b).



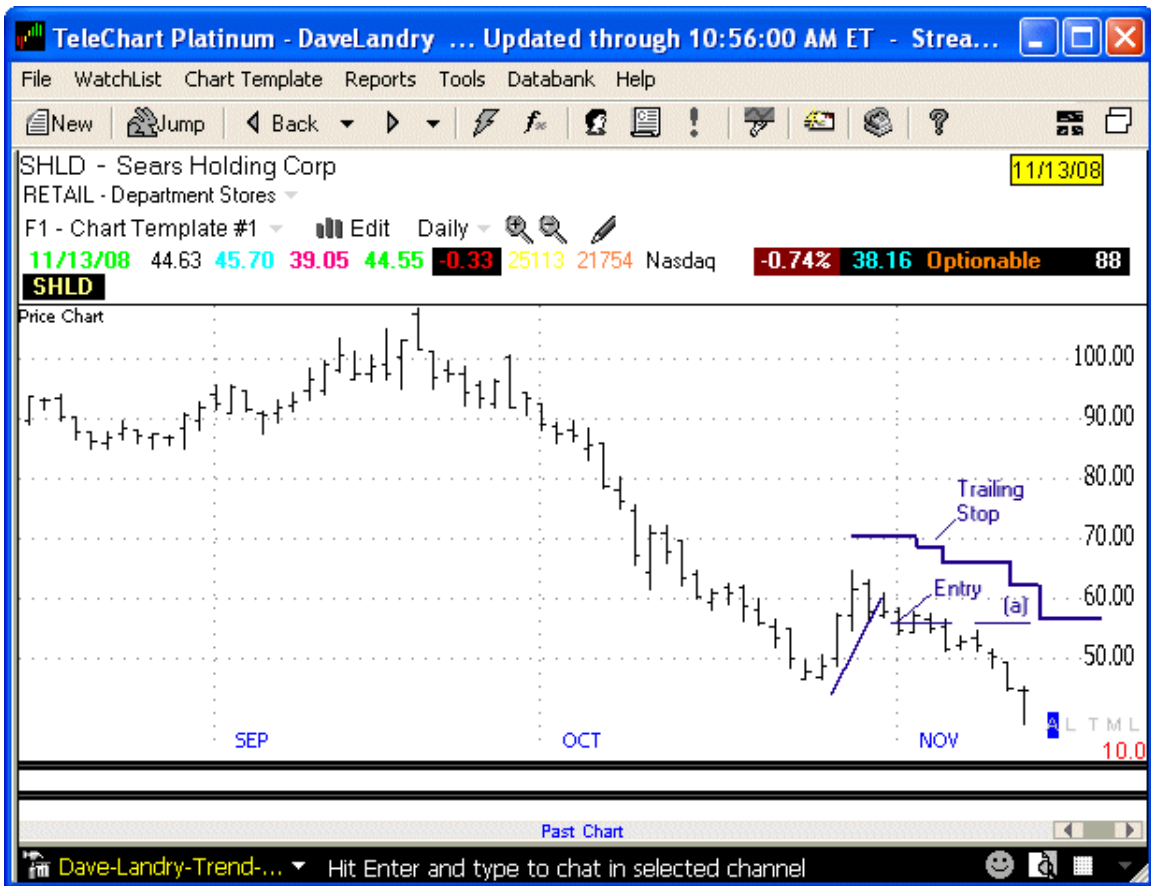
The overall market is also in a downtrend.



And, the stock's sector, Department Stores, is in a downtrend too.



The stock triggers and immediately begins to move in our favor. Within 2 weeks, the stock hits the initial profit target. At this juncture, the protective stop is trailed down to breakeven, the same as the entry (a). This way, we have a chance of capturing a longer-term gain and the worst we can do is breakeven (barring overnight gaps).



Using the technique described in a recent article, we then continue to trail the stop but now more “loosely.” This is in effort to continue to participate in a longer-term trend.



As you can see above, so far, so good. At the time this is being published, the stock has dropped over 28 points since the entry for a gain of nearly 50% percent. I'll continue to follow up on this example in coming articles.

Keep in mind that stocks don't always work this well when they set up in a "textbook" manner (that's why we used protective stops). However, as you can see, it pays when they do. Search to find the best setups and makes sure the market and sector are also trending in the same direction.