



**How To Avoid Paralysis of
Analysis And Know At A Glance
If A Stock Should Be Bought,
Sold Or Just Left Alone...**

By Paul Lemal



How To Avoid Paralysis of Analysis And Know At A Glance If A Stock Should Be Bought, Sold Or Just Left Alone...

If you have been a trader for any significant period of time there is one thing you have probably learned for certain and that is that there is an abundant amount of subjectivity when it comes to stock trading.

If "X" happens then "Y" always results...

Reality check, there is no such thing as **always** in the stock market. Oh, I'm sure someone could dig up one thing that hovered near perfection but for the most part if you approach stock trading as more of an "art" than something finite black and white "cut in stone" then you are much more apt to respond and adjust accordingly when one of those "always" becomes a "not this time".

Such is the nature of the beast. But as traders we can do quite well by playing the odds and focusing on proven strategies that work (a good portion of the time) and using the right strategies to exit stage left quickly with capital intact when they don't.

To keep us out of the muck there are several strategies for stock selection and stock timing that when used correctly can:

- Lower Risk
- Super-charge returns
- Minimize the stress of trading
- Provide clear signals for what to do with the trade

Let's go over a few of them here.

The first and probably most important thing is:

#1-Know Thyself

I know you are wondering what this has to do with stock analysis. ...It has everything to do with it because you are the one making the

decisions and interpreting what you can see about the "subjectivity".

Fear is a by-product of either incomplete information or all the "what-ifs" based on assumptions, speculation or what has happened in the past.

Have you had a history of pulling the trigger too early? Too late? Have you lost your confidence as a trader due to lack of success? These memories can color our decision process and cause us to "freeze" when making current trading decisions.

By knowing who we are, what we think about ourselves as far as trading we can begin to sort and make rational decisions.

Becoming a cold, calculating and sober professional trader comes from learning to tame our friend, fear. Fear in fact can be helpful (it keeps us from touching the burners on the stove) but its irrational fear that is not the friend of the trader. Irrational fear can be tamed by:

- Allocating capital in proportion to not only your current skill levels but the trade risk and your confidence or lack of confidence in the trade (just a caution: is the confidence grounded in reality or "pie in the sky")
- Having solid and finite rules for the trade going in, including:
 - Stop placement
 - Rules for staying in the trade
 - Rules for exiting a trade
 - Rules for what to do if the stock doesn't do _____ (ex: breakout strong on the next earnings release date)
 - Violation of key levels of support

Using the trading strategies that follow can help put an end to paralysis of analysis and give you clear cut signals for what to do next with a trade. These rules were developed based on a study of successful stock run-ups and are consistent and predictable.

Success leaves clues and there are no more telling clues than those left by some of the best performing stocks of all time.

#2 Know What The Reasons You Have For Considering Buying Or Selling A Stock And Plan Accordingly...

Are Your Reasons For Buying:

- Is it speculation based on rumors, gossip, analyst reco etc.?
 - If so, have you allocated capital properly to compensate for increased risk? (speculation that doesn't pan out will often crater a stocks price)
- If it's a "fundamentals" based decision does the current trading action suggest that the prices will continue up from here? Current and future fundamentals can broadcast the stocks potential via subtle and not so subtle price action.
- If it's a price action based reason do you have a Plan B (stop, exit strategy, etc.) in case the prices falter?
- If it's a particular trading pattern that has been productive in the past do you again have a clear exit strategy if the trade doesn't pan out?

Are Your Reasons For Selling:

- Have you heard some rumors, speculation or analyst reco about the stocks coming demise?
 - Are these rumors or speculation reflected via weak price action in the stock?
- If it's a "fundamentals" based decision does the current trading action suggest that the prices are running out of steam?

- If it's a price action based reason do you have a Plan B in case the prices find support and head back up?
- If it's a particular stock chart pattern (head and shoulders, descending triangle, etc.) have you paid attention to the price in relation to the moving averages for signs of weakness? (See Table #3 Page 10 Below)

Trading Rules To Help End Paralysis Of Analysis

Having firm trading rules in place for a stock in case it doesn't do what you think it will do (*Hint: this is one of the biggest complaints of traders-the trade that didn't pan out and they are still in it with the prices down 90%-don't let this be **you***) can be a great stress reliever.

Not only that, it can help you to move on to more productive trades when the stock is just not following the script.

Being a nimble pro-active trader is the key to success in the markets.

By having a "take no prisoners" approach to stock trading you can maximize your annual returns by not staying in less than productive trades any longer than you should and instead moving your capital on to trades that are.

This is how fortunes are made in the stock market-by keeping your money working hard and not allowing it to languish in ineffectual trades. If a trade is not doing what is expected pull the capital and put it into one that is.

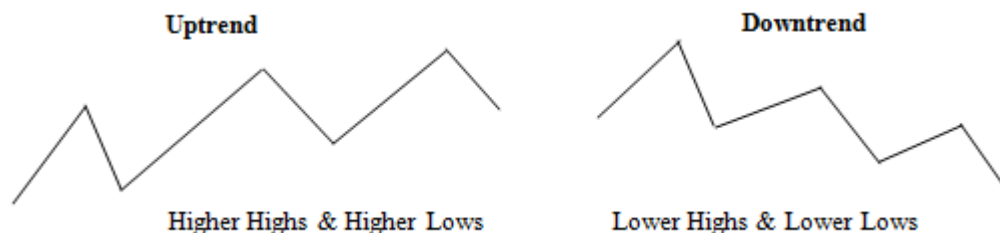
Next...let's look at some trading strategies that can be very helpful for evaluating stocks to buy, sell or just leave alone...

#4-Respect the Trend

As we well know, for the most part-stocks do not go up in a straight line. Although there is the rare stock that will shoot up on news and go nearly vertical for a few weeks they usually flame out pretty quickly.

Is the stock in an uptrend (higher highs and higher lows) or a downtrend (lower highs and lower lows)?

If it is in a downtrend and you are already in the trade did you enter the trade early enough in the trend to survive a re-test of support?



If not, evaluate your buy point in relationship to potential areas of support and make sure you have a stop loss in place to preserve your capital.

If you have a basic understanding of stock cycles is the trade early in a trend (1-3 months) or later (4-6 months or more)? The longer a strong trending stock trade progresses the closer it should be monitored for weakness.

The moving averages in table 3 on page 10 can provide valuable insights on how to evaluate waning momentum.

Although a stocks fundamentals can continue to be the driving force to a trend-even what may appear to be strong fundamentals does not guarantee an extended trend – so let the strength or weakness of the price action be your ultimate guide.

There are some key strategies to use for trending stocks to evaluate the continued strength of the stock. Now there are some variables with this approach since stocks tend to group themselves in "families" meaning they have a certain "DNA" and tend to trend like other stocks in their "family".

This DNA is often a by-product of a few things:

- The stocks levels of trading volume
- The price range of the security
- The industry group it is in
- Whether the stock has any "buzz" due to new products, pending news, etc.
- It's historical trading action (though this can change over time as a company evolves)
- It's current price in relation to longer-term levels of support and resistance

This DNA can provide valuable clues as to the health of the stock. Kind of like a doctor using a stethoscope to detect a heart murmur.

Once you learn to read these clues it can give you excellent insights into weakness or strength in a stock.

Let's get right to it and examine some of these factors.

Some stocks, due to the fact that they are in certain industry groups trend in a somewhat stodgy and lethargic fashion because they are just not that "sexy" (ex: durable goods) while stocks in another industry for example bio-tech stocks that have a lot of buzz going for them may trend in a completely different manner.

Depending on the overall market and economy this DNA can change for a period of time but will usually revert back to its historical

trading tendency over time.

For example, banking, car, retail and even coffee stocks which had in the past been generally stodgy trending stocks all of a sudden became market mega-movers as the economy began to “right” itself in early 2009 many producing 300-1,000% plus gainers in a few months.

The first thing to do get a feel for the DNA of your stock is to examine how the stocks prices acted in prior up trends-or consolidation zones.

Although the broad market conditions can influence how a trend has played out in the past you can usually find a similar trading zone in the stocks own prior trading history.

Now here is an example of how a stock’s price trends based on its DNA:

Figure 1- VPHM



Hot moving stocks like VPHM in Figure-1 a biotechnology stock above that have an orderly progression of prices (as opposed to explosive 1-2 week moves) tend to find support in an uptrend on pullbacks to the 10, 21 and 35 EMA (Exponential Moving Average).

Knowing this can help you to avoid exiting a trade too early before the run-up is complete.

Hot trends that have “legs” uncannily find support almost to the dime on these moving averages. For example when the prices dipped below the 10 EMA in early July they found support right at the 21 EMA.

In August when the trend was a little more seasoned the pullback was a tad deeper to the 35 EMA with the prices still able to maintain a close at the EMA before blasting off again—a sign of continued strength.

Can you see how the momentum is waning on the pullback in November with the price slicing through all 3 moving averages in 1 day? Although the prices did pull back further over the next month they managed a few more months in the run but with a huge 6-month run-up of over 1,000% the writing was on the wall that the trade was entering a “danger zone”.

Stocks that run hard often fall hard when they reach their destination and the risk/ reward begins to work against the trade. VPHM was an example of that with the prices eventually falling off of the cliff in early 2006.

DDRX in figure 2 on the next page, a stock in the coffee distribution sector that would typically be a stodgy moving stock broke some rules here in its 12,000% run in 2009 (.21 – 26.00) in 5 months. Using the moving average strategy outlined here would have kept you in through most of this run.

Very strong trending stocks that are just a little less frisky but still strong will often find support at the 50, 75 and 100 SMA on pullbacks so don't use this in a vacuum—the main thing you want to pay attention to is how orderly the pullback is and low-volume pullbacks are definitely more preferable than pullbacks on expanding volume.

Figure 2-DDRX



So, as you can see what to generally expect from a strong trending stock here is an overview of some moving averages and some suggestions for analyzing the price action:

Table 3-Moving Averages

Buy	Sell	Leave Alone
10 EMA Crossing Up Through The 21 EMA	Prices collapsing down hard through the 10 EMA after a big run-up	Prices straddling both sides of the 10 EMA in a consolidation zone
10 EMA Crossing Up Through The 35 EMA (especially after an extended period below)	10 EMA Crossing Down Through 21 EMA	10 EMA line maintained above the 21 EMA
10 EMA Crossing Up Through The 50 EMA	10 EMA Crossing Down Through The 35 EMA	21 EMA line maintained above the 35 EMA
10 EMA Crossing Up Through The 75 SMA	10 EMA Crossing Down Through The 50 EMA	Stocks <u>sideways</u> basing in an extended cup consolidation where 50 SMA stays above 100 SMA or thereabouts
	10 EMA crossing down through 75 SMA	
Stocks inside of a cup and handle-that have orderly pullbacks and maintain closes above the 200/250 SMA	Stocks in an extended sideways consolidation where the 50 SMA fails to stay above the 100 SMA (unless insignificant amount)	10 EMA maintaining support above the 50 EMA in a consolidation zone

Obviously this was meant to be a general example. For example when prices reach an extreme and drop down hard through the 10 EMA they will often form bottoming candlestick signals or short-term price action that may ultimately become the bottom of a pullback and provide an excellent trade entry signal-despite what may initially appear to be weakness.

So like anything with the "art" of trading it should not be looked at in a vacuum.

For example in March of 2009 FUQI in Figure 4 below formed a 2 day hi-lo reversal (circled in red below) below the 10 EMA at the ultimate lows of the pullback before being launched for a 630% move over the next four and a half months.

But as you can see once the prices reclaimed and held the 10 EMA with the other MA crossovers in lockstep the stock prices were off to the races.

Figure 4-FUQI



Following these rules will keep you out of trouble and sure to avoid the problems traders face by staying in a trade longer than they should.

There is a lot more to trade selection that will not only insure keeping yourself out of trouble but also help you to super-charge your stock market returns-but that would be a whole other book.

But let me share a few more simple rules that should be very helpful...

#5-Respect Market Cycles

When deciding whether or not to buy a particular stock it is in your best interest to pay attention to the market cycles. Is the broad market in an uptrend, downtrend or trading sideways listlessly? Are the indexes also respecting the moving averages in Table 3-on page 10?

Also, are the seasonal cycles conducive to follow-through or would it be better to wait?

Table 5-Market Cycles

Bull Cycles	Bear or Pullback Cycles
Mid-March to Mid-May Bull cycle	Mid-January to Mid-March
Mid-August to Mid October bull cycle	Mid-May to Mid-August
Mid-November to Early January	Mid-October to Mid or late November

These are some general rules which will vary from year to year depending on the markets primary trend but there are definite "lulls" or spikes in market activity producing generally 3 two month bull cycles and 3 two month bear or consolidation cycles annually.

Paying attention to this can help you to be on the right side of the market and give your stock "lift".

The exception will be at times the company's own industry group and how it has historically done in various parts of the calendar year. Some industries may trend upwards in different parts of the year than others while the majority of other stocks stay in sideways consolidation zones so this again should not be used in a vacuum.

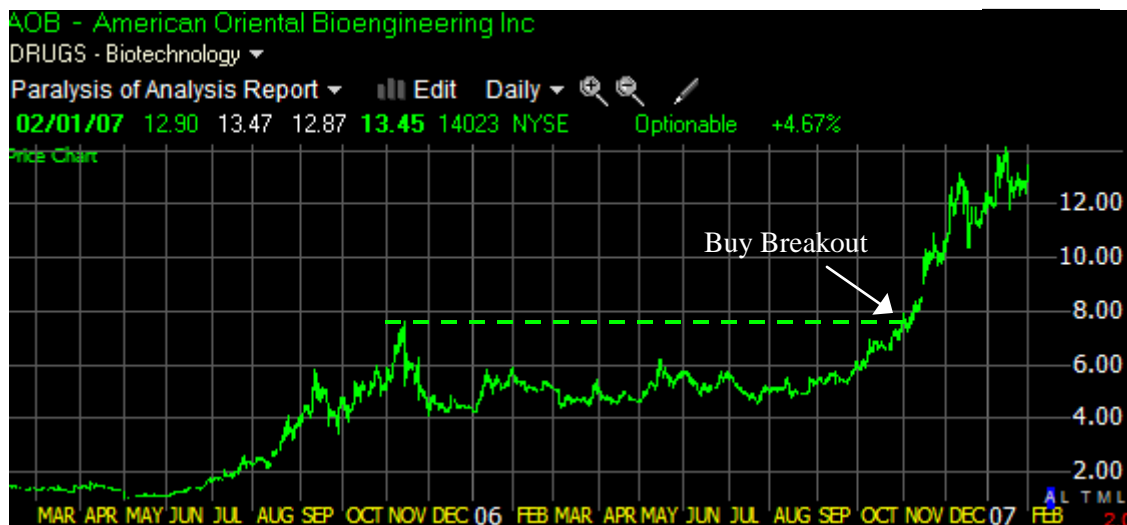
So if you are unsure as to whether or not the particular stock you are considering for is ripe for a buy or sell, observe its historical price action within the common market cycles above and see if it correlates.

#6-Respect The Trend Line

Proper placement of trend lines has evolved almost to the point of a science based on common stock cycles. Knowing how and where to place trend lines to avoid getting into a trade too early or leaving too late is made much easier by understanding a few simple concepts.

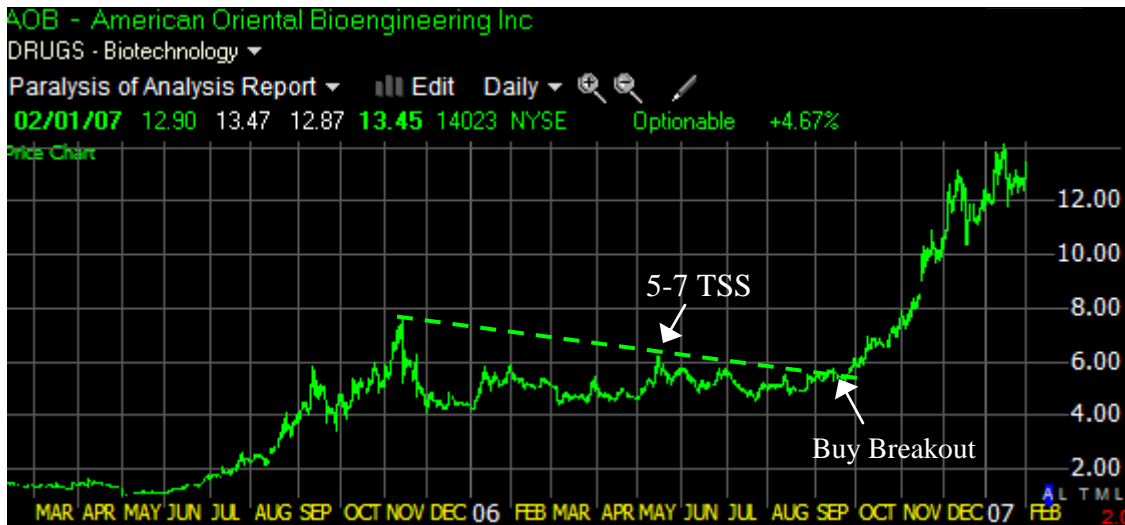
Obvious trend line placement for AOB in figure 6A below would be across from the pivot (the original breakout high directly across the consolidation zone to the same price point on the right side of the pattern):

Figure 6A-AOB



But had you followed that strategy for AOB your gain out of this cup and handle pattern would have been 69% over two and a half months (7.45-12.95). Now if you had instead entered at a common cycle inside of the cup (Figure 6B on the next page) your gain would have been nearly twice that in a little over one more month, a 135% gain in three and a half months (5.50-12.95).

Figure 6B-AOB



Common cycles for trend line placement can vary for any cup and handle pattern based on the levels of momentum and where a stock is inside of a super-cycle and has too many variables to explain in-depth here.

But the primary advantage of using stock cycles as you can see is to avoid unproductive consolidation zones and to keep your trading capital working hard.

Stock cycles when used correctly; especially if combined with moving average analysis can lead to an uncanny ability to enter and exit trades at nearly exact turning points.

#7-Use Stochastics

The next parameter we will use for overcoming paralysis of analysis is stochastics which is well-entrenched in technical analysis. It was developed by George C. Lane in the late 1950's, and is a

momentum indicator, showing the location of the current closing price relative to the high/low range over a set number of periods.

Now, don't worry if you don't understand what I just said – it will become very clear how to use stochastics soon.

Basically, stochastics will be used to tell us – again at a glance – if a stock is “overbought” or “oversold”. For our purposes, we will be using the “Fast” and “Slow” stochastics.

Again, I won't be getting into all the math here, since it's not really necessary in stock chart analysis.

We will be using for this example the 5,3,3 stochastics. The numbers relate to number of periods used in the calculation and number of periods used in the moving average. Now that I've said that, forget it – it's just not important. All we need is an idea of how “overbought” or “oversold” the stock is.

As with stock cycles, the correct stochastics that may be best to use for a more accurate buy or sell signal can vary for various parts of a super-cycle or the style of trading you are doing.

Stochastics are depicted on a scale from 0 to 100. Based on stochastics theory, the stock is considered “overbought” – in other words, under excessive accumulation – if the stochastics are above 80.

Conversely, the stock is considered “oversold” – in other words, under excessive distribution - if the stochastics are below 20. Stocks can stay “overbought” for quite some time, with stochastics remaining above 80 for days – sometimes even weeks at a time.

And they may remain “oversold” for long periods of time too, with stochastics staying below the 20 area. But there's a “secret” in using stochastics effectively – using them to identify turning points in a stock – alerting you to the exact times to buy or sell the stock.

Figure 7-ASTI



In figure 7 above the 5,3,3 stochastics crossing below the 20 oversold line provided excellent swing signals in August before a major price run-up and again in November with a 100% move off of a double bottom in the stochastics in a little over a month in its final leg in its bull-run.

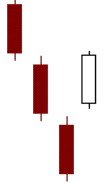
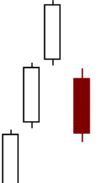


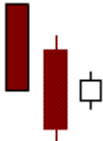
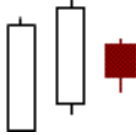

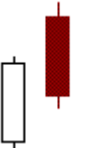


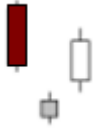

With a divergence in the stochastics during December despite higher peaks in the price going into the end of a 2-month bull "market cycle" the trading action broadcast a "no-brainer short" as the prices plummeted due to profit-taking.

#8-Use Japanese Candlestick Signals


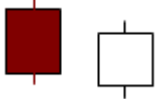

The next strategy that we will use to analyze a stock for what to do next is Japanese candlesticks. Developed by rice farmers in Japan in the 1600's they are an excellent tool when used properly for forecasting turning points in a stocks trend.

In table 8 on the next page are some common bullish candlestick patterns and the Bearish equivalent.

Table 8-Japanese Candlestick Signals

Bullish Candlesticks		Bearish Equivalent	
Bullish Kicker		Bearish Kicker	
Bullish Engulfing		Bearish Engulfing	
Bullish Harami		Bearish Harami	
Piercing Pattern		Dark Cloud Cover	
Hammer		Shooting Star	
Morning Star		Evening Star	

On the next page are a few more candlestick patterns to pay attention to...

<p>Hanging Man-In an uptrend could signal an imminent reversal ahead-caution</p>	
<p>Spinning Tops-Neutral-no clear buy or sell signal yet</p>	
<p>Doji-Candle-this usually indicates a reversal pattern (If found in a pullback consolidation zone may be signaling final support levels have been reached)</p>	

#9-Pay Attention To Volume

Now we come to the final parameter needed in my system – Volume. This one is probably the easiest to understand of all. Volume is simply the number of shares traded for the day.

Volume is important because it can give us huge clues as to the strength of a price movement, and for the future trend of a stock.

For example, if a stock has been trading very quietly for days, weeks, even months at times, and then all of a sudden it gets a big spike in price on huge volume, then the stock is at that point a “different animal”.

Something about it has changed, often violently!

Larger than usual volume can launch the stock into a new uptrend, depending on the amount of volume and how much above normal it is.

The catalyst is usually some news item related to an earnings or sales announcement, a new product, FDA approval for a drug, a new contract landed, etc. But the fact is...

It Doesn't Really Matter!

Something has changed about the company, and therefore the stock of the company. And the volume traded is a telltale sign of that change.

Figure 9 – DDRX



Diedrich Coffee, Inc. (DDRX) in Figure 9 above had a huge volume spike after several months of trading listlessly.

In the fall of 2007, the company announced its intention to divest its retail and distribution operations in order to focus exclusively on roasting and wholesale sales.

During 2008, the company exited from all company-owned retail operations, including Diedrich Coffee coffeehouses and Coffee People coffeehouses, selling the sites to a major chain of coffee houses.

From a Press Release: "As an outcome of this strategy," continued Heeschen, "we have been realizing dramatic growth in this more profitable wholesale business as our renewed focus meets the

increasing demand for specialty coffees in homes, restaurants, and offices."

Needless to say, the market's liked the news. Besides a nearly 200% gain in one day the stock managed a run to the \$26 mark over the next 4 months.

So, there I've just eliminated hundreds, possibly thousands, of hours of your time which might have been spent in unnecessary studying of dozens and dozens of other investment and trading systems.

This simple system has allowed me to capture many of the stock market's biggest winners consistently through several market cycles each year and I know it will do the same for you.

It has kept me from getting bogged down in lackluster trades and from buying stocks that were overpriced short term.

After 15 years of research (and yes, some "hard knocks" too) I have concluded without a doubt that this is the single most productive and profitable way to trade.

This style of trading is designed to turn down the noise and get you on the winning side of the market.

*Coming soon is more information on tips, tools and trading strategies for succeeding in the markets as well as information on an **upcoming webinar** that will forever change your perceptions about what is possible in the stock market. Stay tuned!*

A handwritten signature in blue ink that reads "Paul Fernald". The signature is fluid and cursive, with the first name "Paul" being larger and more prominent than the last name "Fernald".

P.S. If you missed my previous "The Triton Convergence" report you can download it here:

<http://elitewavetrader.com/stock-trading/tcd.html>

A Little About Me...

My name is Paul Lemal and no reason why you should know me unless you have read a few of my editorials on alternative medicine (a passion of mine) that have been published in Time and Newsweek magazine.

I've been very much under the radar quietly researching and refining my stock trading methods over the past several years including developing the most comprehensive momentum trading system you'll ever come across.

You won't see me on the national "talking head" circuit (I'm rather shy)...but I am well known to a small group of professional traders and money managers who paid big money to look over my shoulders in a real-time trading environment with my trading partners Daryl Thompson and Gary Lane-who are some pretty darn good traders in their own right and who I've worked pretty closely with in the past few years.

This was my "Hamburg" you know the place where the Beatles went before they hit it big. This is where I refined, tweaked, tested and hammered my system into a rock-solid money generating system worthy of the title "Elite."

This is where many new trades were developed and where my biggest mega-winning stocks were generated.

I no longer have the real-time trading environment (it is not necessary with this style of trading as this is not a "day trading" system) and besides I wanted to enjoy life more and trade less so that's exactly what I'm doing.

Traveling, writing, spending time with family – balance is something we all seek and sometimes you just have to decide that it can no longer wait...

So in order to get some balance and actually "have a life" I closed the real time trading lab and spent the necessary time to bring all my years of research into a format that others can benefit from.

This report is just a small sampling of the powerful trading strategies I've used over the past several years for consistently targeting the stock market's hi-performing stocks.

Let's Rule The Market's Together!

Paul Lemal