Dana Trading System

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Disclaimer

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Overview

This short-term active trading system has evolved through my own trial-and-error stock trading over the past decade. It is distinctly different from the standard "entry-exit-stop" method that most short-term and day traders use, and which I learned during a one-week course conducted by the [Online Trading Academy] in 2010. (I do not necessarily recommend the OTA course, although it did acquaint me with the world of online trading, which turned out to be quite valuable despite my not using their trading system. There are other ways to accomplish the same learning outcome.) My system relies on the historical long-term upward trend of the Russell 2000 index, and exploits short-term (daily/weekly) volatility to produce gains — higher volatility allows greater profit (it's hard to surf on a windless lake). Since 2011, it has produced annual gains exceeding 20% with less risk than standard investment methods. That percentage has increased as I have continually improved the system. This document describes the most basic, no-frills version of the system.

Assumptions

The effectiveness of this system relies on three primary assumptions:

1. *The stock market (specifically, the price per share of broad-based indexes of American companies, such as the Russell 2000) will eventually be higher than it is today.*

   EXPLAINER: This has been continuously true since the inception of the New York Stock Exchange in 1792, despite some extended periods of decline following market crashes. And, it is also true of high-volatility, triple-leveraged ETF's, which are often called "dangerous" in trading advice newsletters due to their decay and other valid reasons for not holding them as long-term investments.

2. *You are able to retain sufficient cash (liquid assets, regardless of whether that liquidity resides in your trading account) to support your lifestyle for a self-determined period of time (Risk Variable #1).* (See below for definitions of Risk Variables.)

   EXPLAINER: That is, you will not need to sell any stock positions in your inventory for less than you paid for them in order to pay your ordinary living expenses for that period of time. Employment earnings and other liquid assets can partially or entirely offset the need to sell inventory to raise cash, depending on your employed/retired status and other conditions.

3. *You have adequate funds in your trading account to enable the system to work.*

   EXPLAINER: It takes money to make money. The smaller your trading account, the less profit this system will yield without increasing risk to an imprudent level (Risk Variables #2, #3, and #4). It is up to you to determine whether "the juice is worth the squeeze."

Your "TNA Shop"

It is instructive to think of one's trading account as a retail shop in which you sell shares of TNA, a highly volatile exchange-traded fund (ETF) based on the Russell 2000 index. Your shop's customers are traders/investors who think the price of TNA will rise above your sale price (they are buying from your inventory with the intention of selling later for a higher price). Your suppliers/vendors are traders who think TNA will decline from your purchase price (you are buying to build your inventory with the intention of selling later for a higher price). Repeated buying/selling (recycling your capital) enables you to use several times the amount of money in your account as working capital, without borrowing, while safely retaining enough cash to avoid selling at a loss to pay living expenses. (My current ratio of deployed capital to account value in 2017 is nearly 5:1.)

In order to sell shares of TNA, you must first acquire them. Of course, you want to sell them for more than you paid for them (your sales revenue must exceed your costs, as in any business). Shares that you have purchased, but not yet sold, constitute your inventory. Without inventory, you have nothing on your shop's virtual shelves to sell to your customers. So, it is necessary to buy shares at a price that you reasonably expect to increase in the (near) future (i.e., your "wholesale" purchasing), so that your shop's shelves are stocked with shares to sell when the price of TNA rises. One of the safeguards of this system is to retain enough cash (by managing Risk Variables #3 and #4) to buy new inventory when the market begins to recover following any deep plunge/correction/recession.

Why TNA?

Over 2000 ETF's are available. I selected TNA (https://finance.google.com/finance?q=tna) because:

1. It has high daily volume (there are plenty of active buyers/sellers, so trades can be completed quickly),

2. It has high daily volatility (range between highest and lowest filled price within each trading day),

3. It is an index of 2000 companies, so it is negligibly vulnerable to economic shocks affecting individual companies or industrial sectors,

4. Those 2000 companies are domestic (US-based), so it is negligibly vulnerable to economic or political shocks affecting other countries or regions. I regard the domestic economy to be more stable than most non-US regional markets, and it is the largest (highest volume) single-country stock market.

Your On-line Broker

I use TradeStation (tradestation.com) as my online trading platform because it allows OSO (one-sells-the-other) orders, which automatically enter your paired sell-order when your buy-order is filled so you do not have to monitor your account throughout the trading day. Also, TradeStation's commission is only $0.01/share (one cent per share) with $1/trade minimum. However, there is a monthly fee unless a minimum number of trades are made each month. I am unfamiliar with the terms and costs of other trading platforms, some of which are free. Google "online brokers" to explore options.

Your Trading Log

It is essential that you maintain a trading log using a spreadsheet. Enter new open orders when your buy-orders have been filled, and move data to a "completed orders" section when your sell-orders are filled.

Columns (with sample data):

A. Date bought: 11/24/2017
B. Price/share: $67.58
C. # shares bought: 100
D. Cost of purchase: $6758.00
E. Commission on purchase: $1
F. Total cost (price/share X shares + commission): $6759.00
G. Date sold: 12/5/2017
H. Price/share: $69.62
I. #shares sold (normally equal to # shares bought): 100
J. Total proceeds (price sold X shares): $6962.00
K. Commission on sale: $1
L. Net proceeds (total minus commission): $6961.00
M. Dollar gain (net proceeds minus total cost): $203.00
N. Percentage gain (dollar gain divided by total cost): 3%

You may use color-coding to distinguish raw data from formulas, etc. You may also allocate areas of your spreadsheet for weekly/monthly profit totals, to automate calculation of buy- and sell-prices of standing orders, etc.

How It Works

The trading procedure outlined here assumes default values of several Risk Variables, listed in the next section, that you may adjust in accordance with your particular financial circumstances and risk tolerance.

1. Maintain at least five standing buy-orders, separated by 1% of share price (Risk Variable #3), starting at 1% below your most recent filled buy-price. Each buy-order is paired with a sell-order with a target gain of 3%. Order duration should be set for "GTC+" meaning they are "good till cancelled" during NYSE's regular (9:30 am – 4:00 pm) plus pre-market (8:00 – 9:30) and post-market (4:00 – 8:00) sessions. Review and update buy-orders each day, preferably before the pre-market session opens each morning at 8:00 EST. If you

currently have no inventory, the price of your first buy-order may be set at the morning opening price of TNA, or any lower price.

2. After the close of the post-market session (8:00 pm) until approximately midnight, update your trading log spreadsheet, entering that day's filled buy- and sell-orders. Alternatively, this can be performed in combination with the preceding task prior to the NYSE open the next morning.

3. Suspend buying if/when your cash cushion shrinks to your predetermined limit (Risk Variable #1). Never sell for a loss. Wait for TNA's share price to recover and your inventory resumes selling. Fear and greed are the two famous/infamous emotions that plague investors: Fear causes you to sell when you shouldn't sell; greed causes you to buy when you shouldn't buy. It is not necessary to modify this system in response to market conditions, economic news, or anticipated events. This is not a market-timing system.

4. Refrain from attempting to predict (guess) whether the market (share price of TNA) will rise or fall in the near future. Recognize that the stock market is "efficient" (all publicly knowable information is already "baked in" current prices). Even the "experts" are often wrong. Let the system do the thinking.

Risk Variables

#1: Cash cushion: Keep sufficient liquid assets to sustain ordinary lifestyle expenses (housing/food/entertainment/etc.) without selling inventory for a self-determined period of time. Lower risk = longer time = larger cash cushion. I suggest at least one year, preferably more.

#2: Account size: The dollar-value of your trading account. Lower risk = larger account. Trading in a small account, using my default values, may make your gains impractically small, and commissions charged by your on-line broker disproportionately large. Deviating from those default values, hoping for greater profit, would expose you to higher risk.

#3: Order price gap: Percentage of share price between buy-orders. Default is 1%. Lower risk (and therefore lower potential profit) = larger gap.

#4: Order size: Default is 1% of total account value. Lower risk = smaller order size. However, having a small account may require an increase in order size as a percentage of account value to prevent commission cost from being disproportionately large.

#5: Profit target per trade: Default is 3%. If your online broker permits OSO orders, set your sell-price at 3% above your buy-price. If your broker does not offer this feature, you must manually enter a sell-order after the triggering buy-order has been filled. Setting a profit target higher or lower than 3% is less a matter of risk than a matter of how frequently you want to recycle your gains. If your broker's commission is relatively high, you may want to increase your profit target, thereby reducing the frequency of trades and therefore commission cost.

Use TZA in Combination with TNA?

TZA is an ETF that is the daily inverse of TNA. That is, its daily chart is a vertical mirror-image of TNA: If TNA rises 1%, TZA declines 1%, and vice versa. TZA can be traded in precisely the same way as TNA. However, the first assumption listed above (that the share price will someday be higher than today's) is not assured. TZA can be used to profit if you are confident that the price of TNA will decline in the near future, and therefore TZA will rise. (This introduces market-timing into the system, which is notoriously unreliable). The risk is that if your prediction is wrong, your funds may become permanently stranded and you will be forced to sell for a loss to recover liquidity. So, caution is advised. The safer choice is to trade only TNA.

Understanding Why It Works

This trading system is a "no brainer" – it works without understanding *why* it works. Most people, however, are cautious about allocating a significant portion of their life savings to an investment program without a fuller understanding of its underlying dynamics. Recommended resources:

- Search https://www.investopedia.com/ for these and related terms: market efficiency – zone of support – zone of resistance – trend analysis – volatility – market correction – bull market – bear market

- Examine historical data (past performance) of TNA, IWM (TNA's underlying index), and any other stocks: http://bigcharts.marketwatch.com/

- Monitor https://www.cnbc.com/ for real-time market news, but don't alter your trading strategy in reaction to news or opinions you find there (beware "fear and greed").