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AFTER READING THE FIRST 2 CHAPTERS WE HAVE PROVIDED YOU WITH A SPECIAL ACTION TAKER BONUS

INTRODUCTION

WHY YOU SHOULD READ THIS BOOK

During the first third of the 20th century, Richard D. Wyckoff (1873 – 1934) was an extremely successful trader in stocks, bonds and commodities. As his wealth increased he turned his attention to understanding how the financial markets behaved and the forces that made them move.

Wyckoff believed that markets are made by the minds of men and that all the fluctuations in the market should be studied as if they were the result of one man's operation. He called this his Composite Man theory.

He also felt that the best way to make money in the financial markets was to identify which stocks had attracted professional interest. Then, using his technical trading strategies and techniques, he would wait until he saw the professionals were ready to move a stock, bond or commodity. This was the time to take a position.

In Wyckoff's day the professionals were the great speculators like Jay Gould, Jesse Livermore and James Keane. Today they are hedge, mutual and pension funds, along with other major financial trading institutions.

The players may have changed, but Wyckoff strategies and techniques work as well today as they did 100 years ago.

Richard D. Wyckoff was the very first stock trader to include volume studies in stock market analysis. He combined his knowledge of stock market volume with the price studies developed by his good friend Charles Dow. The result were the Wyckoff stock market strategies and techniques that are well detailed in the two courses produced and distributed by the Stock Market Institute (SMI) through the website WyckoffStockMarketInstitute.com.

Most importantly, Wyckoff's concepts remain as valid today as they did in the first third of the 20th century, when Mr. Wyckoff was actively trading. The fact that these strategies work as well today as they did 100 years ago is testament to their validity in our different and ever-changing markets.

While the basic precepts have not changed, several important enhancements have been made to the Wyckoff strategies and techniques. Many were introduced by Robert Evans, who owned the Stock Market Institute from the 1940's through the 1960's.

Mr. Evans developed the Optimism – Pessimism Index. This is an index strictly of volume as it appears on individual indexes and stocks throughout the trading day.

He also enhanced the Trend Barometer, which was conceived by a Wyckoff student in the 1930's. Made up of the Technometer and the Force Index, this important trading tool helps Wyckoff students better identify turning points and the relative strength or weakness of both rallies and reactions.

These, coupled with the Group Leadership Stocks, are the Wyckoff Tools. They are the signposts that help guide the Wyckoff student towards stocks, bonds, futures and commodities that are ready to move and then, point out the appropriate entry and exit points.

This book studies the basic Wyckoff concepts and principles and then shows students how to get the most out of their Wyckoff Tool Kit.

It also includes many of the lessons I have learned during my 40 years as a Wyckoff student. The charts that accompany the text are of recent market action. Every concept is supported by an accompanying chart that helps the reader understand and appreciate the value of these wonderful trading tools.

Unlike many publications of this nature, I have not tried to find the perfect chart that portrays the Wyckoff principle that is being studied. In the real world, those perfect charts are often not quite so perfect. However, the Wyckoff principles, discussed in this book, appear on vertical line and point and figure charts every day. It's simply a matter of an intelligently studying each chart, looking for and validating these important Wyckoff concepts.

Successful Wyckoff investors and traders do not look for Wyckoff indicators discussed in this book and then automatically take mechanical action. Instead they analyze the indicator in conjunction with other Wyckoff tools and previous market action. Finally, they consider alternative scenarios and the placement of stop orders, before taking a position.

My purpose in writing this book is to share, in a more pragmatic manner, how the Wyckoff strategies and techniques work and more importantly, how you can profit from them.

I have learned many of these lessons through trial and error and as a result have paid a bit of tuition to the "University of Wall Street". I hope this book substantially reduces yours.

WHAT YOU WON'T FIND IN THIS BOOK

If you are looking for an easy automatic method to make money in the stock market, this book will disappoint. Too many traders spend a great deal of time and money trying to find easy mechanical methods that will tell them when to buy and sell stocks. In truth, the only people that make money are those that sell those "easy" automatic methods.

The Wyckoff strategies and techniques are filled with important indicators like Buying and Selling Climaxes, Springs and Upthrusts, Signs of the Strength and Weakness, to name a few. If these are treated like mechanical indicators, without a basic understanding of their supply and demand relationships, opportunities will be lost and, even worse, bad trades will be made.

These indicators are simply signposts that tell the experienced Wyckoff student that a potential opportunity lies ahead. It is that students responsibility to then analyze the stock's activity to see if the price and volume relationships warrant taking a position.

The experienced Wyckoff student will use the criteria established in the Position Sheets, Buying and Selling Tests and the other Wyckoff Tools to determine if a position should be taken.

They should also develop a trading action plan. The plan will include a written summary that includes:

- Why the position was taken and what the stock will do in the immediate future
- An objective area where a successful trade can be terminated and profits taken.
- A specific price where the trade should be closed, if the stock does not behave as expected.

Trading in the stock market is hard work. The stock market is a cruel mistress. If you are looking for an easy way to make money and not committed to putting in the time for extra study and analysis, this book is not for you.

CHAPTER 1 - ANALYZING THE MARKET

BASIC CONCEPTS

At first blush, the financial markets, appear to be a disorganized and uncontrolled mass of seemingly unrelated activity. Often pundits will offer reasons as to why markets rallied or reacted. Sometimes the given explanation for a market rally, appears a few weeks later to justify a reaction. However, within these seemingly random fluctuations there is a logic to the chaos. The question is, how does one make sense out of mayhem?

The answer is in the most fundamental of all trading concepts. The stock market is the last great bastion of free market capitalism. It functions solely on the laws of supply and demand. When more shares are bought than sold, the stock market goes up. When more shares are sold than bought, the stock market goes down. The battle between supply and demand is being fought every single second of every market day.

Every market move is comprised of a series of smaller fluctuations, which in turn are based on the relationship of the price and its associated volume. These smaller moves occur throughout the trading day. They are called waves. This is because they rise and fall like beautiful ocean breakers. Like ocean waves, market fluctuations have powerful underlying forces that transform seemingly quiet and peaceful swells into powerful giants that can distinctly and irrevocably alter the trading landscape.

The secret to trading the stock market is learning to observe the minor wave fluctuations and understand the relationships between price and volume. This knowledge helps the trader prepare for future moves in either direction. Successful stock traders combine that basic understanding, with the Wyckoff strategies and techniques, to better understand how the markets, and their individual stocks are performing and, more importantly, how they can be expected to act in the future.

The Wyckoff Wave is the market index of choice for most Wyckoff students. Along with the Trend Barometer, they are critically important tools that help analyze market action. They provide a comprehensive package designed to help every trader reach responsible conclusions on what the market has been doing and why. Then, they help the Wyckoff student predict what will happen in the near, intermediate or long term future.

Why are these tools special and unique? Because, unlike other indicators the Wyckoff tools drill inside the market action and examine the price and volume relationships of each intra-day wave. The resulting data provides important clues that, if used correctly, can help make sense out of what to many, seems like disorganized market activity.

The stock market rallies and reacts throughout every trading day. These minor up and down fluctuations need to be tracked and monitored. These fluctuations are called intra-day waves.

Tracking each intraday wave's volume is extremely important. Many market analysts believe that if a stock advances during the day, all its volume should be categorized as demand or up volume. Conversely, all reactions consist of down volume.

Wyckoff realized that this was not correct. A stock could advance, but much of the up volume could actually be supply. If a stock reacted some of the down volume could've been demand. The intra-day volume provides the important data that comprises the Trend Barometer. The Trend Barometer consists of the Optimism – Pessimism Index, Technometer and the Force Index. These important indicators are often called Wyckoff Tools.

Even if the intra-day information is not available, the end of day volume can provide clues in identifying the amount of demand or supply present in the stock or index.

Demand is considered to be present if a stock rallies on increased price spread and increased volume, or reacts on decreased price spread and increased volume.

Supply is present if a stock reacts on increased price spread and increased volume, or rallies on decreased price spread and increased volume.

If a stock rallies on reduced price spread and reduced volume, it is considered to have a lack of demand. There is also a lack of demand on a reaction that has increased price spread, but decreased volume.

Finally, if a stock reacts on reduced price spread and reduced volume, it is considered to have a lack of supply. There is also a lack of supply if a stock rallies on increased price spread, but reduced volume.

SUPPLY AND DEMAND DRIVE THE MARKETS

Richard D. Wyckoff understood that the basic law of supply and demand governed all price changes and they were the best indicator of the future direction of a particular stock or index. The concept of rising prices when demand exceeds supply and the lowering of prices when supply exceeds demand is universal. It is found not only in the stock market but in commodities, real estate, labor and everything else that contains a monetary value.

The more Mr. Wyckoff learned about the stock market, the more he realized that the actions of stocks exposed the plans and purposes of those who dominated the markets, or took large interests in those stocks.

All of us indicate our future intentions by how we behave under a given set of circumstances. The stock market does the same. It indicates its future direction by its current actions.

Stock markets are huge repositories of thousands of bits and pieces of miscellaneous information. These can be news items, rumors, stock tips and even guesses and hunches. They are spread in newspapers, telephone conversations, e-mails and through the Internet.

Consciously or subconsciously a great majority of these tidbits have an impact on traders and investors who are making buying and selling decisions.

Whenever a trader buys a stock, or sells short, the trade makes a small impact on the overall market. The amount of impact depends on the size of the trade. The larger the trade, the more impact it will have on the stock's price. A 100 share or odd lot trade will have little impact on a stock's price. A trade of 10,000 or 20,000 shares gets everyone's attention and could have an immediate impact on the stock's price.

For example, a buyer wants to purchase 20,000 shares of a certain stock, but only 10,000 shares were available within a 3-5 point range of the order. In this case, in order to complete the trade, the extra 10,000 shares of that stock would have to be purchased at higher prices. The demand created by the purchase could not be met by the available supply. This caused the price to increase.

Conversely, if 20,000 shares of stock were available, the trade would be easily consummated and have no impact on the stock's price.

The same happens when large quantities of stock are sold short.

Wyckoff understood that the plans of these large operators could be seen on the tape as they unfolded. He could also see the eagerness or anxiety in individual trades and could also measure the effort behind the buying or selling. This force was evident in the number of shares in each transaction. This also helped Mr. Wyckoff understand the purpose behind a stock's market action. Was it to:

- buy or sell without substantially impacting the price, or
- to force the price up or mark the price down, or even
- to discourage buying or selling by other traders or investors?

Each transaction was evidence. While it was not always possible to understand every minor event, it was much harder for the dominant traders or institutions to hide their intentions from the ticker tape or, these days, from the real-time data available over the Internet.

Mr. Wyckoff believed that future events could be seen on the tape, because these large interests disclosed their anticipation of advances or declines by how much and when they bought and by how much and when they sold. The Wyckoff strategies and techniques help traders learn to recognize what is in the mind of these larger interests and how to take advantage of this important knowledge.