TRANSCRIPT

Trading the dips and the downtrends

Sam Shore: Welcome to everyone this afternoon. Slightly different topic for us, but definitely important to have tools in our toolbox for all different types of market environments. My name is Sam Shore here with our Trading Strategy Desk, and we also have Colin Songer. And with our Trading Strategy Desk, we're here at Fidelity to help you, the individual investor, with coming with a trade process that you can utilize that's repeatable. Knowing what are the tools in my toolbelt, how can I employ them, and how can Fidelity's tools help me to employ them in that repeatable process? We do also host a number of the online sessions, those Strategy Desk coaching sessions that you can access via the Learning Center. As well, we have classes for beginners that you're also able to view.

As we're getting started, we do have to go over a couple of quick disclosures. Firstly, any screenshots, charts, or company trading symbols mentioned are for illustrative purposes only, and should not be considered an offer to sell, a solicitation or an offer to buy, or a recommendation for the security. Option trading entails significant risk, and is not appropriate for all investors. Certain complex option strategies can carry additional risk. Before trading options, you should read the characteristics and risks of standardized options, and have your account approved for option trading. Examples that we're going to use are not going to include transaction costs or tax implications, but of course, you should consider them prior to entering into any trade. And technical analysis focuses on market actions, specifically volume and price. It's only one way to analyze stocks. When considering which stocks to trade, you should use the approach you're most comfortable with. As with all your investments, you must make your own determination as to whether an investment in any particular security or securities are right for you, based on your investment objectives, risk tolerance, and financial situation. Past performance is no guarantee of future results, and of course, investing does involve risk, including risk of loss.

So, a brief over map of what we intend to cover while we're together this afternoon. The first thing we want to really talk about is what goes into this trade process that I mentioned? I mentioned, with our Trading Strategy Desk here, our goal is to help you have a repeatable process. What are the components that that needs to include? We're going to look at what are some of the vehicles you might use, be it equities, or exchange traded funds, or options, to take advantage of the dips or downtrends that you find in the marketplace. We want to be sure that we talk about managing risk and having an exit strategy when we're going along and doing any type of trading. And we also want to cover some common pitfalls. Colin and I have lots of experience with trading, I've been at Fidelity for a little over nine years at this point, I think Colin's been at Fidelity even longer, and we want to try to share some of the pitfalls that we see people run into. So hopefully we can take our experience, and help you avoid falling into those pitfalls in your own trading. After we cover those, we'll then go through a live demonstration using Active Trader Pro, and look at on a chart, what does the setup look like? How can I place trades to manage that risk as I'm going along in my trade?

Colin Songer: So let's talk about some of the resources that are going to be available while we go through this. We've already mentioned a few. So first off, I want to thank everyone as well, I want to echo that, for coming out and joining us here today on such a topic. Really excited. But there are a lot of resources that can help solidify some of the concepts that we're going to be covering today. But also, you can expand upon that on your, at your own pace. You know, we have ranges from archived webinars, to four-week courses that we have. So if you're not comfortable with some of the concepts that we cover, hey, join us on one of our four-week courses, we have one on technical analysis, that'll be one of the bases that we're, that you might see being utilized here today. And where you can go through, and it includes homework to solidify some of those concepts.

We also have shortened videos within our learning center, just as quick hits on some of these different parts. So just be aware, there are several different resources that are always available to you, being a Fidelity client. With that being stated, let's talk about that trade process. Because I think this is extremely important. Where we talk about how do we create this repeatable process that Sam's mentioned? And I think it's important that we start off with well, why do we think it's an opportunity? And we think it's an opportunity because we're creating an outlook on price. Now, I have spoken with some traders who said well, I feel like it's going to go down, I really feel it in my gut. Now I will tell you, there are some traders who can trade using that approach. But it's such a small percentage that can actually do it, and make money, and do it effectively. It's such a very small portion of the population that can do that. For us traders who can't do that, which is the majority, we have to make sure that we're creating, you'll hear this, objectable approach to our trades. A logical, rational approach. And we do this by using, whether it's technicals, some will use just fundamentals. And yet still, some will use actually both approaches. And that way, we're using something that generates these signals for us. We don't have that emotional response. And the way to limit that emotional response is being specific with identifying that entry and exit point for our trades.

Now I would argue that that exit point is probably the most crucial part of that. And this really should be set up before you get into the trade, not after you're in the trade.

Sam Shore: While it's important with exit points to have a loss in mind with trades that's acceptable, you've also got to keep in mind how much capital am I allocating per trade? There's this concept of risk of ruin, of when might I be trading, and I take such a large loss, or allow such a large loss, as my downside exit point, that I'm then not able to continue trading. Or the amount of gain that I would need on subsequent trades just to get back to break even, becomes a tremendous hurdle. And so when you're placing a trade, we've got to remember A, I need to be able to place the next trade, even if this trade doesn't go in my favor, even if I get it wrong, and we want to have in mind what sizing are we having for each of those trades? Be it in terms of dollars per share, or in terms of total loss. But not just where are we entering and exiting, but with how much capital are we using? How many shares or contracts are we looking to buy?

Colin Songer: No, that's a great point, right? Size of a trade and how much we're willing to risk, that's kind of a big factor going into this. You know, when we talk about, you know, size of the trades, look, if this trade keeps you up at night, this trade is too big, right? So the idea is to make sure that we don't have those emotional responses. So what that leads us into is the idea of utilizing and having our approaches so we can stay disciplined, and we stay patient. I know I struggle a lot of times with patience. I get a little jittery sometimes, but if I have a plan right from the onset, I don't really feel that need to have to do something. I can be much more patient with my trades, because I know exactly what I'm looking for. And once again, that theme of make it repeatable. All these really go into it. But I'm thinking that this is a good opportunity to talk about two different scenarios. Let's talk about that first one.

Sam Shore: Yeah. So whenever we're looking at going in and trading it, we want to look, of course, at our two scenarios, trading the dip, or trading a downtrend. So we'll talk about the dip first. The defining characteristic of what we're looking for is a broader term uptrend. Overall, you are bullish, but for whatever reason, we've seen price pull back a little bit, be it some sort of macro event, be it some news for the company, or maybe one of its competitors, what have you. And whether it's, there has been a temporary move to the downside, or you expect something to occur in the future that will lead to this pullback, we want to not get so, so focused on that small pullback, to sort of miss the forest for the trees. We want to make sure we're aware what we're trading is in a broader term uptrend. And so, with an uptrend, the characteristics that we're looking for, and most simple sense, of course, is from the lower left-hand corner of the chart, to the upper right-hand corner. But more so in practice, we want to be trading a security where we're seeing higher highs, and higher lows. Those are quite definitionally what is indicative to us of an uptrend.

The other thing we need to recognize is our risk is, if we're wrong, if the security falls. So at its heart, this is still a bullish approach, but we've found a more advantageous price point, or think there's going to be a more advantageous price point, for us to enter the security. But if we're wrong, we need to look at exiting, because it could be we're buying into what we think is a dip, but maybe it's the start of a new downtrend, or maybe it's the end of the uptrend. And so, we have to be careful, and have that risk management, maybe even risk-first approach, in mind as we're going forward. So it's a question of well what are we planning for, and not just hoping maybe it'll go up at some point again in the future. It's the very, very fine line between buying something that is in a pullback, versus the sort of stereotypical, trying to catch a falling knife. This is not the circumstance of something has fallen by 50%, and now we're looking to sort of bottom fish, and try to buy something like that. It's a circumstance of, it's still in a broader uptrend, but we're trying to catch it coming off of maybe the highs of that uptrend to take advantage of additional moves to the upside.

Colin Songer: And that's one of the things to keep in mind. That's why we set these particular points up. Remember what Sam said earlier, right? Well an uptrend is higher highs, and higher lows. Well, if it's reversing, and it's creating lower highs, and lower lows, guess what? That's (laughter) not an uptrend! Now it's a possibility of a downtrend. And that's why we want to set these in, the idea of catching a knife, we want to make sure that we're allowing our trades to give us the best possibility of making money. And that's why we want to create this trade process that this could be an initiation of a reversal, right? Initiation of a new trend in the opposite direction. So that's why we set these up. And remember, technical analysis doesn't predict the future. It teaches us how to react to price movements.

Sam Shore: Yeah, and it's really handy, a lot of times a great tool. We've tried to show it on this slide, of course we'll show it when we go into the live demonstration portion. But if you're looking at a chart and thinking about something as a dip, zoom out a little on that chart. If you're looking at six months, look at the year to date chart, or a one-year chart, or a two-year chart, to see what is this broader trend that I'm trading. If you're trading something this week, take a look at what's been going on in the past quarter, or the past six months. Don't get so focused on the singular chart that you're looking at that you ignore what's going on bigger picture. Now we have a few different vehicles, of course, to take advantage of our bullish outlook, to try to make money on the dip. The first, of course, being a long stock. Relatively straightforward, like anything else, we're looking to buy the stock, take advantage of price rising.

Our next three introduce a few different wrinkles. So we have different potential option strategies that we could use to employ as our bullish strategy. Buying a call, selling a put, or putting on some form of a bullish spread. Whenever we introduce options, we have to recognize that just an outlook on direction of the stock is insufficient for a trade. Option trading does include having an outlook on volatility. Does include having a much more defined outlook on timeframe. So it does introduce that added complexity, and that additional decision making that you're having to come to. But, there may be some benefits in some circumstances. Maybe you want a trade where you have a limited total loss amount, so you want to be buying a call versus buying the stock. And so, the vehicle selection can be part of your risk management process, and your idea of how much am I willing to risk per trade, but of course, it’s not the only factor. We’ve got to have these other components of am I just looking to trade direction? Or do I want to introduce timeframe and volatility to it?

Now, with trading the dip in mind, I mentioned earlier, are we trading a temporary pullback, or the falling knife? Are we trying to catch a bigger downtrend? So now let’s take a look at the other side of this, of well, we don’t think it’s a dip, we do think the stock’s in a downtrend. And some of the ways and things we’re going to go about with identifying that.

Colin Songer: Well let’s look at trading that downtrend. Now I mentioned the attributes that go into it, right? That’s that lower high, and that lower low. And as you can see from here, right, it’s on the top left-hand corner of that chart, and it moves to that bottom right-hand corner of that chart. So those are the attributes of a downtrend. And that’s where we’re looking at. Now remember, when we’re using something like this particular tool, you know, what we’re trying to do is, we’re trying to identify an area where we think that that downward or selling pressure is going to continue. So whatever signals that we’re using, we look at it, and we say OK, we think it’s going to continue to go down. What we’re seeing right now is this countertrend move, or a temporary rally. A little bit of a push to the upside, but it's not going to last, it's going to continue on its wayward way on the downside.

But when we do this, and we're going to trade this downtrend, let's be very aware of what we're dealing with from a risk standpoint. Remember, our job is to manage risk. You're going to hear that throughout, and I can't stress that enough. It's so important. Our risk, when we do a bearish strategy, is to the upside. OK? And in some cases that we're going to be discussing, there's potentially unlimited. So let's talk about some potential bearish vehicles that you can use to trade this outlook that we have. And when we mention bearish, I want to get this out of the way, when we talk about bearish, we mean we want to benefit from a downward move in the price. So the first vehicle is shorting stock.

Sam Shore: And with shorting stock, there are some unique risks to it that don't exist when you're looking to buy stock. The first thing is to short stock, generally it needs to be done in an account with a margin agreement. So unfortunately, it is not available for most retirement accounts. The other thing is, since you're shorting stock, you're selling something that you don't own in order to buy it back later at a lower price. And so, in order to do that, there has to be shares available of the stock that you're looking to short in order to even open your trade. Once the trade is open, short stock is a type of trade that has unlimited loss potential. Unlike when you own a stock, there's not a cap innately on how high the stock can go, hence why that risk management component becomes so important when employing an unlimited loss potential strategy.

The other thing is, as I mentioned, you've got to have margin on your account in order to short stock. So with that being the case, if the trade goes against you, so if the stock rises, you could have a margin call where the collateral in your account is insufficient for the position that you're holding, at which point you'd have to deposit additional funds or securities, or potentially close out all or part of your short position.

The last risk that's a little different is, remember how I mentioned we said we're borrowing the stock from someone to sell it? And then we're going to look to buy it back later? Well, there's something called buy-in risk. If you borrow that stock, and then all of a sudden, there are no longer shares available to borrow, well Fidelity's going to require that you buy in your short stock position, so that we can return the shares to the person that they were borrowed from. So it's important to realize there are a few different ways that you might not have as much control when shorting stock, namely margin call risk and buy-in risk, compared to when you own a stock. That being said, it is one of the bearish strategies that allows you to take advantage of an outlook where you think we might be in a downtrend, or you think that the stock is going to fall in price.

Colin Songer: Now that leads us to -- that might make a few people squeamish, right? That unlimited risk. Well here's another one. Now since we're talking about unlimited risk, how about shorting a call? That has unlimited risk to the upside for the premium that you're receiving. It is indeed a bearish strategy, but you still have that unlimited risk to the upside. Then we have a long put, we just go outright, go up and buy a put, OK? And it benefits from downwards moves, so you have substantial gain, and the most is going to be the premium that you paid for this long put. And then you have bearish spreads, OK? Whether you're buying a put spread, or selling a call spread, these have defined losses for them. But remember, we're talking options strategies. So there's that additional outlook that you've got to create, which is outlook on timeframe, and outlook on volatility. These are factors that go into option trading. So these are really the different vehicles that you can use to utilize for a bearish outlook that you have. But I think it's, when we discussed this, and as you can see, we're really focused on that risk, which I think is the most important piece, let's capitalize on that. Let's talk about probably the most important factor, which is our exit strategy.

Sam Shore: Yeah. And when you're looking to actively trade, really your job, your goal, is that of a risk manager. At the end of the day, the ideal thing is, let me keep my average loss size smaller, ideally have a bigger average win size, and then all of the sudden, it takes a lot of pressure off in terms of your win percentage. You don't need to have trades that are profitable as frequently if the average loss size is very, very small, and when you get it right, you really get it right. And this speaks back to that question of managing capital, and managing position size. Whenever you're looking to enter a trade, there should be a point where you say if this occurs, I was wrong. Whether that's based around a given price of the stock, whether that's based around a total loss amount, there needs to be a point where whatever thesis you were trading has been disproven, and you're looking to exit the trade. Some more advanced technicians may even use given technical signal. So for instance, if they're trading a price pattern, or utilizing support or resistance in their trading, based on crossing a certain threshold, might be where they look to exit.

Now when we talk about that capital management, and that position sizing, those are, go hand in hand. So for instance, if we're looking at a trade, and we say if the trade goes against us by $1, then I'm wrong. And on a trade, you're willing to risk $100 per trade, well very straightforward. For that trade, the position size that's appropriate would be about 100 shares. Conversely, if based on what you're looking at, you're willing to risk 50 cents per share, or you think that if it goes down by 50 cents, that that would invalidate the thesis that you were looking to trade, well then maybe you look at sizing your position for that trade around 200 shares. And so, it can be very handy to think how much am I willing to risk per trade, then separately, look at what price point for the stock am I going to be wrong. And with those two pieces of information, you can come up with your position sizing on any given trade.

Now, where that threshold exactly is risking $100, or $500, or $1,000, there's not a uniform answer to that question, of course. But, having an idea of well, if I have multiple trades that go against me, so let's say I get three or four, even five trades in a row wrong, how much capital might I have after that? You've got to have that sort of thinking, as opposed to the thinking of wow, look how much money I could make, there's so much upside, wouldn't it be great if I made 20% per trade? All of that, of course, would be fantastic, but that's not the hat we want to wear when we're going into thinking about our trade. We want to have a plan together that's based around well, what are some of the worst case scenarios, and let me make sure I have objective approaches to exiting, should I wind up being incorrect. And oftentimes, it can make a lot of sense to write that down. Put pen to paper, get out a spiral notebook, or a notepad, and jot it down, it's really hard to argue with the ink on the page later, as opposed to sort of waffling about it internally, or psychologically.

Colin Songer: I know in the past, I've always joked with my colleague Brian about how he used to have his trading notebook right there, and yeah, he's a little old school, I as well incorporate that, where you actually write it on paper, but you don't have to do that. You don't have to hold that paper or notebook right by your desk while you're trading, to hold yourself to those trades. We actually have a notebook built into the platform that you can use to take notes. I use it myself now. Go in, I actually write in why I'm putting on the trade, where I'm looking to get out, and how much, what I'm really looking for in my outlooks to help hold me to that trade. Because my memory's not as good as it used to be. I'm getting up there in age, so you know, this allows me to reflect back on my trade, why I got into it, where I'm going to get out.

And I just want to kind of jump back to another concept about the idea of, you know, a lot of times when we put on these trades, the vehicle that we use is going to also define the style of trade that we're putting in. So in Sam's example about having one trade outweigh the risk that we're taking on, there are other types of trades, you know, like selling strategies, using options, where look, it might be just the opposite, where you have several winning trades, and hoping that one losing trade doesn't outweigh all those winning trades we have. So it depends on your style of trade that you're utilizing, or the vehicle that you're utilizing, that can help you with your style of trading, and making sure you manage that risk appropriately. It definitely varies to the vehicle that you're using. But I agree, that notebook is huge. That's going to help you hold your feet to the fire for the particular trade that you're doing.

Sam Shore: And the thing that's important is that thought process of what is my exit strategy is something that really, you should be thinking through before you enter the trade. It shouldn't be I've entered the trade, now what, it should be I'm looking to enter a trade, here's the criteria that are causing me to enter, here's the price points where I'll be looking to exit at a loss, here's the price points where I'll be looking to exit at a profit. And then of course, the important thing is that we've got to stick to that plan. It doesn't do us any good to use the Fidelity notebook tool, to use your spiral notebook or notepad at home, if you write it down and never look at it again. Or if you write it down and you don't follow it. So it's vitally important that we've got to come up with our plan, execute our plan, and we need to stick with our plan. So we'll cover a couple of common pitfalls that Colin and I see, and then we'll start to look at some of the, what this actually looks like in practice, and walk through maybe a couple examples in Active Trader Pro.

Colin Songer: So, when we're discussing about some of these common pitfalls, and hopefully some takeaways that you're going to get from our presentation here today, hopefully the theme of limiting that emotional impact is coming across, right? And we want to make sure that we try to reduce -- is there any way to completely wipe it off the table? I would say no. I tried to reduce it as much as possible, but it's still there. It makes you question your approach, but guess what? We want to limit it. We want to make sure that we have a game plan that we already have in place. If it works, great, if it doesn't, OK, I know what to do. Already know the course of action.

Are there going to be scenarios where you get stopped out, or you exit out of the trade? And eventually, you would have been right? Yes, that's going to happen, but that's a part of trading. What we're trying to avoid are what Sam was talking about, about those big losses. We are avoiding those, and I'll tell you what, the one, well I'm going to -- let me rephrase that. So a couple of times, I didn't stick to my plan, I paid dearly for it. I made the mistakes, so you don't have to, right? So that's why we share these experiences with you. Look, we put these places, these exit points in place so our losses don't get too big. We can always reenter at a different time when it's more advantageous.

And that gets to the next point, which is look, part of having a plan is have a very specific entry and exit points, right? Whatever that may be. Whether -- we're going to be discussing that as we walk through these examples, but this is going to make it a lot easier for you to stay disciplined, and be patient with your trades, allow them to evolve, right? If it's not doing anything, OK, then we just wait it out, it hasn't hit my loss point, it hasn't hit my profit point. Let me wait it out, see what happens. And this kind of gets away from that trading by gut feeling. Right? When you trade by gut feeling, that's your emotions kind of weighing in on you, pulling you to one side or the other. It's going to do that. What we would try to do is, we want to reduce that. We want to take that off the table, and that allows us to stick to the plan.

Sam Shore: Yeah, and when those emotions come into play, you've got to remember, those are some of the strongest emotions, or probably worst decision making time for you as a trader. Either you're at a loss, obviously very frustrating when that occurs. Or you have the euphoria of oh, I have a winning trade now. And generally, those are not the times where we make our best decisions, and so we should defer to when we were coolheaded, calm, collected, and coming up with well, what are the objective points where we're going to be looking to exit our trade? Otherwise, all of the sudden when we veer from our plan, or we don't have those objective points, it becomes very, very easy to rationalize staying in a trade where if we didn't have a trade on, you'd tell your buddy, I would tell Colin, you'd tell anyone you're talking with, if they told you this was the trade that they're in, that they should be looking to exit it, or they have no business still being in that trade. But, when emotions come into play, it's very easy to rationalize that to yourself, and we want to try to avoid that.

Colin Songer: And it's really, when we get down, you notice that depending on the vehicle you're using, that's going to adjust how you manage that trade. And that's so true, because they all have their different characteristics. They all have the different advantages and disadvantages. So we want to weigh that, and make sure that we fully understand where we're going to get in, where we're going to get out, and why we're doing so. That helps plan that out, because of the different characteristics of them. And once again, if there's anything that you're going to take away from today, I hope it's this. Which is a trader's primary job is to manage your risk, that is your job as a trader. The profit is the byproduct. Managing your risk is our job as traders. So hopefully, that's come across crystal clear for you. I'm sure that it has, but we just want to emphasize that point over and over again, and we'll continue to do so, because really, in essence, from what I've learned, from what I've spoken, and from other traders, this seems to be a consistent theme that that would help out, or improve, the trading experience.

Sam Shore: Yeah. So hopefully now, we've gone ahead and pulled up the screenshare here, we're getting into the demonstration component of our time together. And we are going to use Active Trader Pro. If you have not used it before, you can access it at Fidelity.com/ATP. It also indicates that on the slide, so certainly if you forget that, don't worry, just check back on the slide, it gives you that URL. And you can use it if you have a Mac or a PC, it is a downloadable piece of software, so you have to download it, install it, and it will use the exact same username and password that you use on Fidelity.com. So don't have to remember different login credentials. And it does not change your Fidelity.com experience. So if you go in, you use Active Trader Pro, for some reason you don't like it, don't worry, you can always go back to using the regular Fidelity.com website. We like to use it for this demonstration because the charting capabilities are a lot more flexible, and a lot more customizable in the Active Trader Pro platform. And really, that's what we're going to focus on for our examples here.

We’re going to run through an example of trading a dip, and then run through an example of trading a potential downtrend, and give you an idea of, as a trader, how might you go through and set up what are my entry points, and set up what are my exit points on each of these trades. And so the goal is not to say oh, I saw XYZ stock, that’s the stock I should go out and buy, it’s to say here is what this process looks like, and using it in an action. So hopefully you can replicate that process using the analysis that you like to use best, be it different technical indicators than we use, or be it fundamental analysis or what have you. So for our trading the dip example, we’re going to use the Fidelity MSCI Consumer Staples ETF. And whenever we’re looking at a chart, we want to try to discern what the trend is. Just looking at the chart, maybe with this one you say I got it, I think I know what the trend is here. But let’s add some indicators on so we can help get a little bit of a visual aid.

A common indicator traders will use to discern trend is called a moving average. And a simple moving average just takes the closing prices from a set of days, say 50 days, so the closing price for each of those days, adds them together, divides it by the number of days, commonly referred to as a calculation period. And that tells us what is the average price from the past 50 days? So then of course, we can plot that day by day, as a line on our chart.

To add that to our chart, we'll go up here and click on indicators. You can scroll left or right through the different indicators, but there's also this type of search field, and since we know what we're looking for, we'll go ahead and type that in. Type in "simple," and we can see simple moving average. We'll click on that, and we'll see it adds a simple moving average line to the chart. It's going to default to a 20-period simple moving average. The other thing we want to have an eye toward is, what is our frequency for our chart? Because our frequency defines what does one candle on our chart represent, and also defines well, what is this moving average calculating? So it's a daily frequency, it's calculating a 20-day simple moving average. A common period for a simple moving average is going to be looking at the 50-day. It corresponds roughly to one quarter worth of trading. And then we're also going to add the 200-day simple moving average, which corresponds roughly to one year. Now this is not to say that those are the only moving averages that you should use, or the best moving averages. Certainly, based on the timeframe you're looking to trade, you might find the 20-day is what you want to use. Or maybe you want to use a 5-day, or a 30-day, what have you.

But let's go ahead and make this adjustment. If we click on simple moving average up here, we get a little menu where we can go in and modify. Here's where we can change our period, so we'll change our calculation period from

20 to 50, hit apply, and now you'll see it's flattened out that moving average line a little bit. It looks a little different now. To add our 200-period moving average, we'll click indicators, do the exact same thing, start to type in the symbol, that'll give us a simple moving average, we'll click it, it adds it to the chart. Once again, it defaults to a 20-day, so we'll go ahead and modify it, and make it a 200-day simple moving average.

So we can see, for this very long-term moving average, we have that sloping, positively sloping line. And when we're looking at trading something, we of course want to see that longer term uptrend, so we see a circumstance of it had these Christmas Eve lows, and ever since then it seems to have made higher highs and higher lows, and has stayed above the 200-day simple moving average, at least so far. And for the most part, it stayed above this 50 period moving average. And this is actually what we're going to go in and use for our indication, in this circumstance, of a pullback occurring. We're going to look at well, if it comes back to this 50-period moving average, that might be a point that we want to look at entering the stock with an eye toward above it, and continue proceeding to the upside.

So we've taken our sort of macro look, this is looking at one year of time, let's actually zoom in a little, so to speak. So we'll move from one year to six months. And so here on our six-month chart, and let me even draw just a little box around it, so we can all be looking at the same point in time, we have this period of time where we had the stock, or the ETF, go below our 50-period moving average, and then come back up above it. So our indication that we would want to be looking for something is these are the indicators that we're using, is that short-term dip. We've gone below the moving average, that sort of perks our ears up, we're looking for the opportunity to enter if it should continue this uptrend. We see we have a day that passed where it stayed below the moving average, then the subsequent day, it crossed above. And so now we've got to ask ourselves, "Self, might this be the opportunity we were looking for, where we've had a dip, it seems to be coming out of the dip, might we want to look at entering the stock using one of those bullish vehicles, based on what we're looking to do, be it a long call, or be it buying the stock, or be it a short put, or bullish spread, what have you, to get in and get exposure to our anticipated upside move, based on this thesis we've loosely constructed?"

Colin Songer: Now, a very interesting point Sam is that, I just want to point out, is you just covered about utilizing things like a close above that 50-day moving average to help be specific, which is definitely specific. But there are different approaches that you can use. So as an example, you can use different approaches, things like what's known as a piercing, OK? Which means intraday, it's above that 50-day moving average, as soon as it does, I'm getting in, right? Yeah, it's an aggressive approach, but you get more of that movement, because you're getting in right when it gets above that 50-day moving average. The drawback, well you may get more of it if it moves up, but it could also be a false signal. So by the end of the day, it could be back below. So, that's the advantage and the disadvantage of what's known as a piercing, or intraday being above that 50-day moving average.

As the example that we're using here, he mentioned about a close, right? So the market closed above that 50-day moving average. Well what if you want to be even more ... I want more data that it's going to stay above and continue on its way up. Maybe you use two closes, right? But now I'm giving up that movement, right? I'm getting in later. So yeah, you are sacrificing that, but you're more confident, or have more evidence that it's going to continue in that direction. It's basing on that data. So you, as you can see, there are different advantages and disadvantages when you're using specific examples of when to get in. You've got to choose which one's right for you. There's no right or wrong answer, you've just got to use which one is most comfortable for you to make these decisions.

Sam Shore: And you'll notice throughout this whole example of setting up our entry, at no point have I said I think this is the low point, or I hope it doesn't go any lower. We've tried to set objective rules, so that we're creating a situation where we're not just buying as it's going down, hoping it comes back up, we've found a dip, and something is giving us an indication where we think that dip was temporary, that it was a temporary move below the 50-period moving average, and we think it's going to go back up above it, and continue to the upside. And those filter rules that Colin mentioned can be used on the open, as well as the close. So maybe on your open, you have that two close filter, you could do the same thing with your close as well. Alternatively, you could actually utilize some of our tools to help you with choosing other exit points. And I'd say the focus should be on what is my exit point to the downside, when am I pulling the plug? Not oh, look how much money I can make on the trade.

So a great tool that we have that can help with this is our trade armor tool. If you click on trade and orders, you can go to trade armor. I'll pull it up here on the left-hand side of the screen. And one thing I do want to mention, a really handy usage, with the trade armor, and especially when you're using charts, is you can actually link the two together. So if we link our great tools, this will make it so when we change what we're looking at in trade armor, or change what we're looking at on the chart, it's going to change it to the same symbol. So you'll see it already went ahead, plugged in our symbol for us.

So, we had the discussion of what's going to have us to enter? So, we have bought into this, let's say we have a position on, and we own some stock. And we want to have in mind well, where are we going to look at exiting out of our trade? Trade armor can draw for where Recognia, a third-party firm that we work with, identifies support and resistance levels. And they can identify these levels with their algorithm based on differing lookback periods. They could be looking at the past 10 days, 20 days, 40 days, 100 days, what have you. So let's go ahead and we'll choose 100 days, and then we'll click trade. We'll say we're trading stocks, the action we want to set here is a sell. Because we're wanting to set, if we're wrong, when are we looking to exit the position? And so to utilize that, we're going to do what's called a trailing stop. Since we're trying to take advantage of a trend, we'll set an order type where it's going to increase our exit to the downside as the trade is going in our favor, while at the same time, giving us a downside point. And let's say we want to start that trail a little bit below where they identify support.

So support's going to be the price point where in the past, price has bounced off, because buyers have come in, or found the stock appealing at that point.

We'll say if that support no longer holds, or if our trend gets broken, so maybe if we get stopped out from our trail, which is eventually going to likely increase above our support level, if we're right and the trade goes in our favor, that we're looking to exit our trade. And so right here, we can set up our trail, all we have to do then is preview and place our order. And we have our exit to the downside to manage risk.

We still have to keep some eye on what's going on with the price action and the moving average. Because if we see price come back below that moving average, perhaps by our filter amount, that also is going to want to have us exiting the trade. And that might be exiting at a profit if that occurs in the future, it crosses below after a week, or a few days of price action to the upside, and then comes back below the moving average level.

Colin Songer: So let's use another example. So we use one that has a moving target, it gives you that high water mark, even though it's below where it's currently trading. But this moves up as the market moves up. But you know, maybe you're a little worried about volatility and got stopped out before. You'd rather just have that line in the sand, and that doesn't mean you have to stick with it. So as an example, if I want to put a line in the sand, you could use just a stop order. You could just put a stop order saying look, if it gets down to here, I was wrong, I'm walking away from my trade. Because I identified the support, I want to stick with it.

Now does that mean that's the only stop level I'd have to stick with? Absolutely not. You could do that and stick with that throughout, but another approach is after it's gone in your direction, and has moved up, now you've got some profits, you know what? Maybe I move that stop order above, and I put that above where I entered. That way, if it does get back down there, I'm getting out roughly around where I entered into the trade. In theory, and remember, I'm saying in theory, you're exiting out of the position, hopefully at where I got in. So in other words, I haven't lost anything on the trade. Now that's obviously in theory, but you could use, you don't have to stick with that initial approach of where to get out. I could always move it up. But you want to do it as a, once again, not an emotional response, but a logical, rational reason for that. And you could plan that out at the beginning of your trade and say look, if it gets up by X amount, I'm going to move it up above where my basis was. You could use that, right? But you just got to be careful when doing that. Because if you don't, if you move it up too soon, you don't give it enough room, you could be stopped out before your trade could actually evolve.

Sam Shore: Now if you're choosing exit points that make sense, so certainly putting an exit point a couple of pennies behind the stock, high probability you're going to get stopped out. But you'll still get stopped out sometimes, it will certainly happen. And if the trade winds up going back in your favor, you can always reenter into the trade. Yes, there are costs associated with that, you may have some loss on the stock, there's going to be a commission, potentially there could be some tax implications. But the goal is to try to avoid staying in a trade as a dip turns into a downtrend. And certainly, you could start off trading something that you think is a dip, exit it, and maybe later on the road, you've decided the stock has turned into a downtrend, and you choose to enter it as entering into a downtrend. But we, of course, don't want to be holding a stock through buying on a dip, and then the stock plummeting, or going into that downtrend while we're still owning it.

Colin Songer: So let's talk about that. And we were talking about worrying about that risk, well what if it does turn into a downtrend? So let's bring up a security that does exhibit that, where it's in currently a downtrend. Now remember, a downtrend is what? Lower highs, and lower lows. I think that this qualifies. (laughter) So we're looking at a co-ETF here, and you can see that it does exhibit that lower highs, and lower lows, so in essence, what I want to focus on is kind of the thought process of why would we even think about doing this?

Well let's use the same moving averages that we did before. Now we'll notice, right around that July area, Sam, let's bring that in. Let's go to six months on that.

So as he's doing that, let's talk about OK, well what if it does close below that 50-day moving average? Let's say that's our entry point. Now you could see here, right around that July area, it crosses back below that 50-day simple moving average, we get a close there. Let's say that's our entry point, which means we are going out, and we're going to sell shares at 12.59, OK? So let's say that's our entry point. But I want to use a different method. Let's go to something that's a little bit of a different approach, where we're basing it on risk to reward. So sometimes, traders will use a basic rule of thumb, which is having at least $2 of reward for $1 of risk, OK? You can have a higher factor, you can have a lower factor, you've got to use what's best for you. But just in general, it's going to what Sam mentioned earlier about having one winning trade equaling two losing trades, right? This is a way that we can deal with it. Do you have to use this factor? Absolutely not. You have to use the factor that helps you make money, or become successful in your trading experience. You've got to use what works best for you.

But let's say we enter that 12.59. Now I'm just going to, for this example, use a two to one ratio. So remember, we shorted. So our risk is to the upside. As you can see with the theme, I'm starting with the risk side, because that's my job. So, let me risk $1, and add that to the upside. So that means I'd be doing a buy stop, and we're going to use this bracket order, right? This bracket order is stating, if it goes up, because I'm already in the position, get me out, I was wrong. So I'm willing to risk $1, which puts our stop at 13.59. And that's a beautiful part about this trade armor, it allows us to input it directly. And guess what? My profit target is going to be that 10.59. So my buy limit, which is going to be below, because remember, we make money if it goes down, is that 10.59. That's funny. When we look at the chart, it puts us right around (laughter) one of those lows there. So, you could see how you could plan this out, putting that on there. Now can I adjust it? I can absolutely adjust this. I can grab any one of those designations or boxes on the right-hand side, adjust it up or down for that amount, but guess what? I'm just really looking to -- you could see, it gives us a readout for gain or loss, based on that if we click that preview button.

But this is a way that we can manage our trades and plan out our trades appropriately. So when we look at this, this is the beautiful part about trade armor, we can see how it is shown on the chart visually, as well as having one button to be able to place both these orders.

Sam Shore: And the thing I like to keep in mind, if we're making adjustments, is remember, we picked those price points for a reason when we put the trade on. Does that mean you never want to adjust them? No, it does not mean that. But, if we're adjusting them, we need to have some sort of rationale for it, and a lot of times, it doesn't make sense to adjust in a way that allows for more loss. So for instance, if we take our buy stock, where we would close out our short stock position, if we adjust it up to 14, and then 15, then 16, then 17, I imagine you sort of get the picture from here, well we just allow ourselves more, and more, and more, and more loss while we're waiting to your right. And remember, with short stock, there's unlimited loss potential. We could lose more, and more, and more money, as we're moving that up. So generally, if you're making an adjustment, you usually don't want to use that stock, and move it up more. If you think it's going to trade in a narrower range, certainly we could move that stop in. That means we're allowing less risk overall in the trade, just like with our trading the dip, maybe the trade has gone in our favor, and we want to move our stop down so that we're looking to exit sooner, so to speak, right? A lower price point.

The other thing to keep in mind is, if we're adjusting one of these, keep that risk/reward in mind. If you have a two to one risk/reward, and we're moving our stop, well is our limit still in the right spot? If we want to leave that where it is, that's fine. Just keep in mind, our risk/reward going forward is no longer two to one. Maybe it's switched to a one to one. Maybe it's changed, if you lower where the limit is, to a four to one. What have you. But, we've got to try to keep as much objectivity in it as we can, because otherwise, that's when we start making bad decisions, when we start rationalizing changes to our initial plan to the ink on the page in our spiral notebook without a good rationale for that outside of emotion.

Colin Songer: Exactly. And when we use this example, it just happened to work out perfectly for that two to one. So you remember, all we're trying to show you is that you can use any one of these approaches, you got to use what's most comfortable with you. And just remember, you always have resources available here at Fidelity. Where it's Fidelity.com and the different resources in the Learning Center, whether it's these, attending these webinars, whether it's even calling Fidelity and discussing with one of our knowledgeable representatives to help you out, any one of these can certainly help you out, and put you in a better position to realize we do have the resources available.

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