Twitter Thread by Finkarma

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Four Powerful Techniques to Trail Stop-Loss and Maximize Gains.

Are you still suffering from the problem of taking profits too early or getting stopped out too early?

Then this thread is for you.

This writeup will introduce you to some powerful techniques of trailing stop-loss which will help to stay in a trending stock for more time and hence maximize your gains.

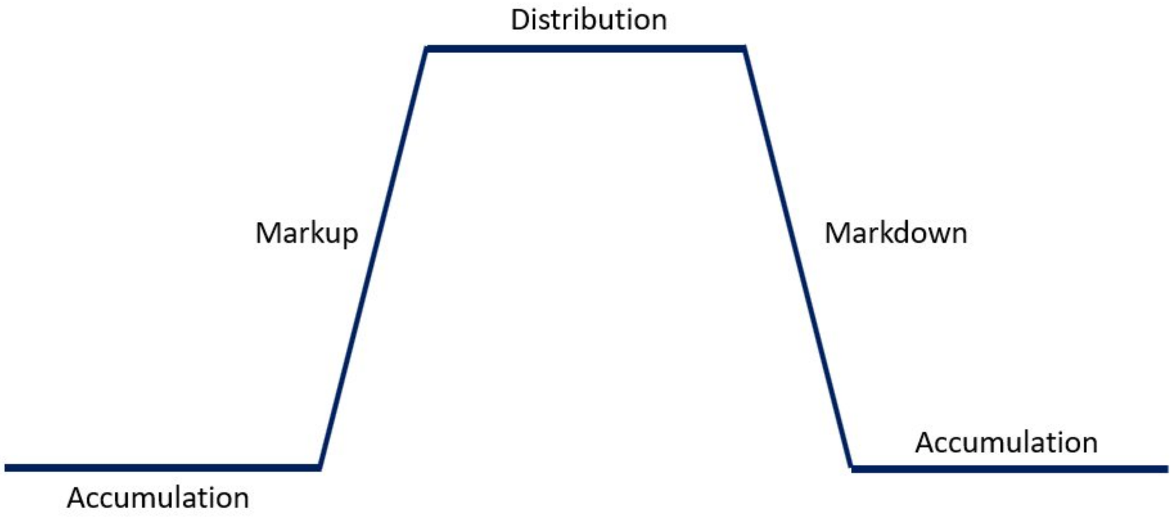
Let's dive right in! ■

I have spiced up these techniques with some tweaks to make them more effective in riding the juiciest part of the trend.

Trailing is a technique that works well in a strong trending phase of the market.

The market is said to move in four phases – accumulation, markup, distribution, and markdown.

The markup and markdown are the trending phases so, trailing would work best during these phases.



The four techniques that I am going to discuss are:

1. Moving Averages Stops

2. Super Trend Stops

3. Swing Lows Stops

4. Percentage Stops

What! Do you already know about them?

I bet after going through the text below you will learn some new tweaks.

Moving Average

MA is simply the average of specific number of previous closing prices on a candlestick chart

Traders usually like to enter at an average price in a bullish stock rather than at a price higher than the average. So huge buy orders usually pile up near the averages

Keeping our trailing stop loss just below the average, in the anticipation that buyers would emerge at moving average and take the stock higher, increases the odds in our favor.

The confusion is which moving average to use?

Each stock or index has different behavior.

You have to simply open the chart and apply different moving averages (20, 50 or 100). You will definitely get the answer in many cases.

Some stocks would behave at 20 ema while the others at 50 ema. For example, the following chart behaved nicely at 50 ema.

Placing our stop just below the 50ema line would protect us against volatility and keep us in the trend for a longer time.

You should exit under the low of the first candle that gives a closing below the ema.

But wait, what happened at 1?

Price closed under the ema. Is that an exit?

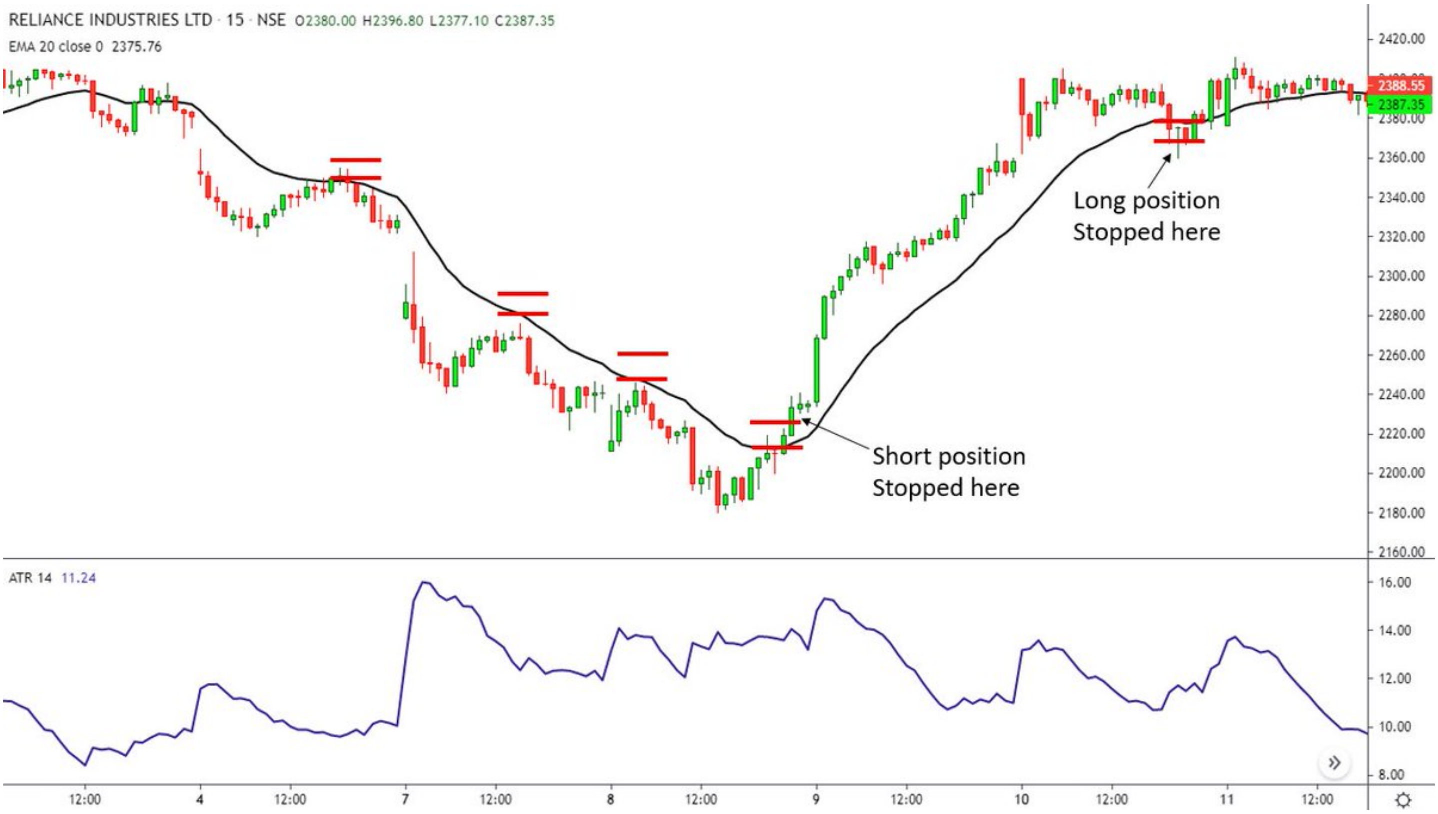
This happens in many cases that even after placing stop below the ema, market shakes you out and then proceeds in your predicted direction.

There is a simple solution to the problem.

You place your stop loss 1 ATR below the ema (in long trades) or above the ema (in short trades).

This gives you more room to absorb extra volatility due to some news.

Add/subtract the ATR value from the ema value and that is your stop loss.



Super Trend ~

As the name suggests, super trend is made to ride a trend and to identify the change in trend.

If you have entered a stock, then a closing below the super trend will generate an exit signal. The opposite is true if you are short.

The following chart is with the standard values for super trend, which is 10/3.

Means it is averaging the true range of the last 10 candles and multiplying it with 3.

This value is subtracted from the last close to give us a line.

The super trend (ST) lines would be printed higher as the stock proceeds up.

If the stock starts consolidating the ST line would turn flat.

Most of the time, if the length of the flat line becomes significant, then it may provide support to the price in the future.

A super trend with small values of ATR and multiplier would generate too many signals.

Even with standard values, you can observe a few false signals generated on the following chart.

If you increase the value of the multiplier to 5, the false signals will be automatically removed (see chart below).

It will absorb some extra volatility. But remember, I am talking about strong trending markets and not the sideways market.

There are only a few signals generated with the above settings.

Also, notice how the stock takes support at the flat ST line. These lines also act as resistance when stock is trending down.

The 10/5 settings on a daily chart are good for investment purposes. For intraday trading 10/3 values are fine.

Again, you need to play with these two values on different timeframes in your stock/index to see what has been working.

Swing Lows/Highs ~

This is the simplest method to trail your profitable trade.

You don’t have to make any calculations but watch the chart only.

Look for swings up or down and place your stop loss above or below (as the case may be) the swings.

As soon as the stock pulls back in a trend, forms a valley and then have a significant rally, you can place your stop below the recent valley low.

The opposite is true for short trades. You can trail with 1 ATR below the valley low to absorb volatility.

Percentage Method ~

The method discussed below is for investment only.

Firstly, there needs to be a consolidation (accumulation/re-accumulation) or a reversal pattern (H&S/Cup&H/Triangle etc.).

As soon as you take your entry as per your rule (close outside a range or pattern), you also place an initial stop loss 10% below the entry.

If the stop is too wide, you can adjust the position size accordingly.

Now here comes the tricky part.

Say the stock starts moving in your direction and is 20% up from your entry.

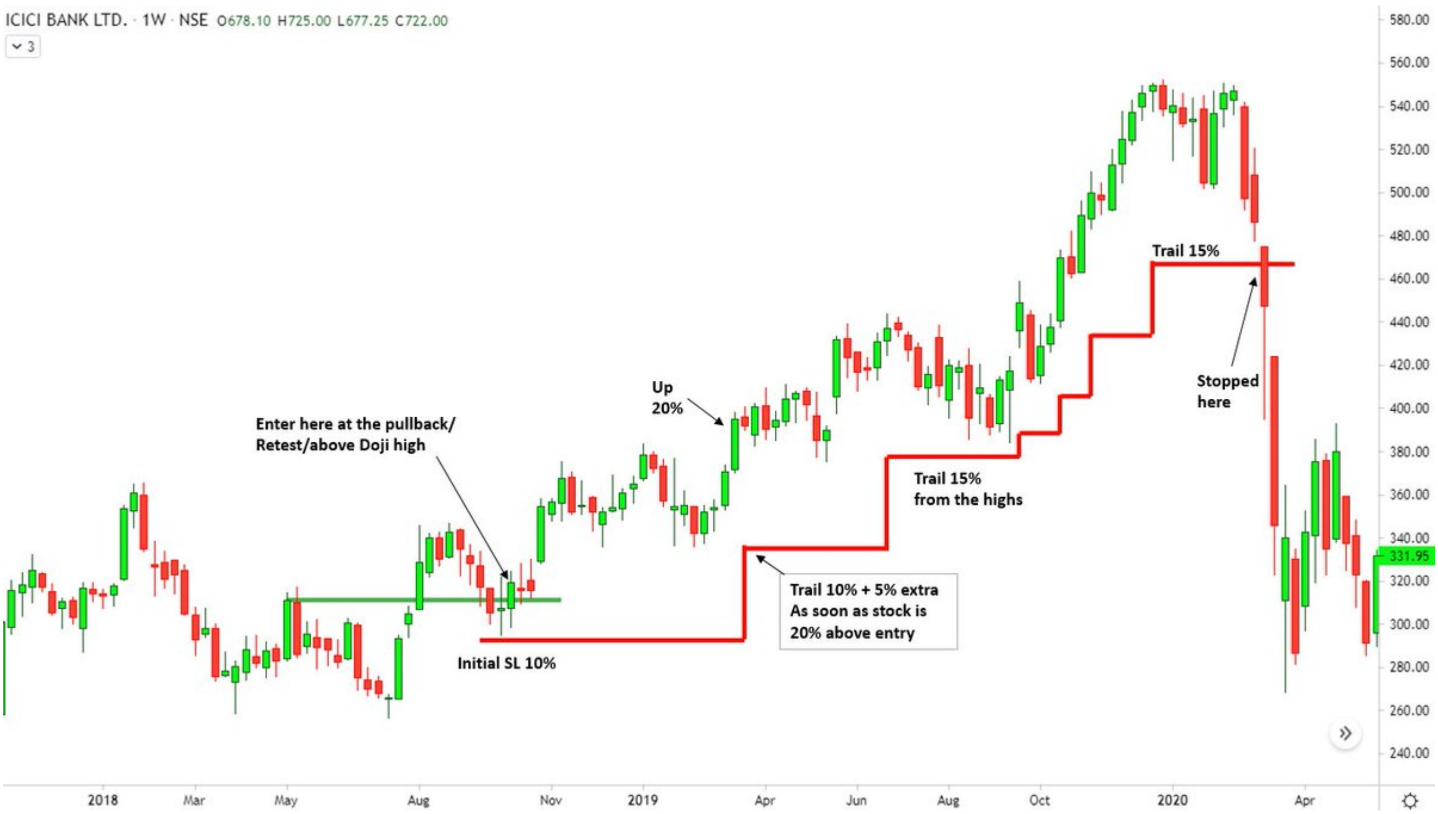
At this point you trail 10%+5% from the last trade price (You do not trail stop as long as the stock is not 20% above your entry).

You can also take partial profit if you like at this point and trail the rest.

You keep on trailing (15% from the high) as the stock trends up and keep doing that until you get stopped.

In the following example the stock came out of a resistance and is trailed with %age points to ride the entire trend.

In the following weekly chart, you might have been able to book 50% instead of the highest 70% but a stop-loss would still save you a lot of money as the stock later cracked below the entry price.



It's true that no technique works all the times but still these methods will help you ride strong trends more efficiently.

And again, none of the above techniques would work in a sideways market.

However, these techniques would work while riding micro-trends, within a sideways market, on smaller timeframes.

Practicing these techniques will make you more efficient over a period of time, as you will come to know the nuances of the one chosen from above.

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