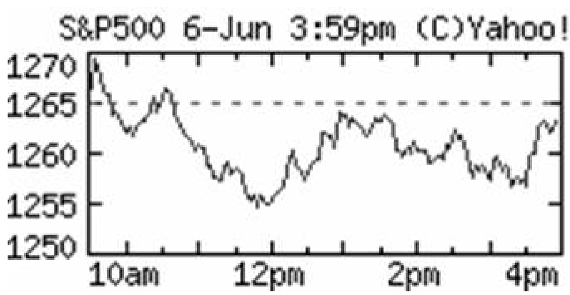
SECRETS OF TRADERS

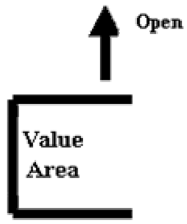
Value Area Help Guide



The Value Area: Is the range of prices where 70% of yesterday's volume took place. (For instance, if the Value Area in the S&P's is 138500-139000, then 70% of the previous day's volume took place between the prices of 138500-139000.)

The 80% Rule: Is when the market gets (or opens) above or below the Value Area, and then gets in the Value Area for two consecutive half hour periods. The market then has an 80% chance of filling the Value Area. The Value Area (and the 80% rule) can be an excellent tool for judging market direction. Many traders familiar with the Value Area and the techniques that go along with it use it to help them decide what trades to do each day. You will find (once you get used to it) that using the Value Area each day will be very valuable in your trading. (Pun intended!) First we'll talk about the basics of the Value Area and what to watch for, and then we'll talk about the impressive 80% rule and how to trade that technique. The market has some predictable reactions when it's in and around the Value Area.

Value Area Basics:

1) 

When the market opens above the value area and does not get inside the value area, this is a strong BULLISH SIGNAL. If the market does get inside the value area, you should look to exit your long position.

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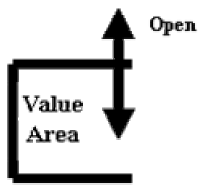
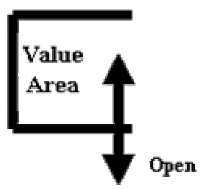
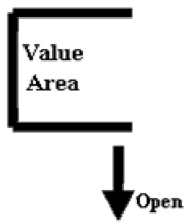
2) 

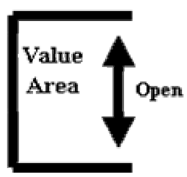
When the market opens above the value area and then gets inside the value area, you could then possibly have an 80% rule to the downside.

3) 

When the market opens below the value area and then gets inside the value area, you could then possibly have an 80% rule to the upside.

4) 

When the market opens below the value area and does not get inside the value area, this is a strong BEARISH SIGNAL. If the market does get inside the value area, you should look to exit your short position.

5) 

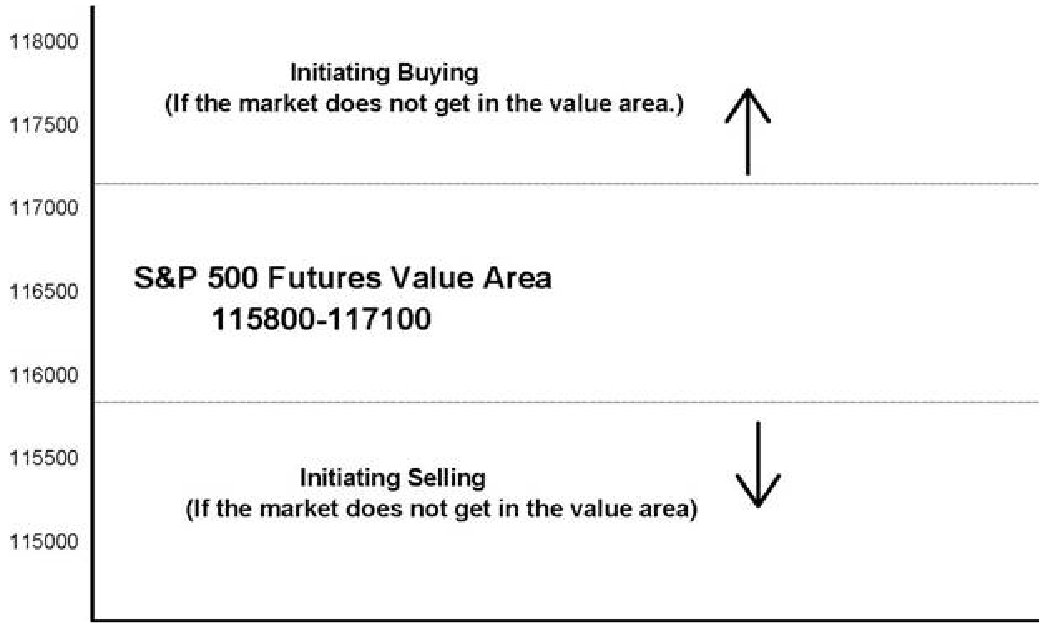
When the market opens inside the value area and remains inside the value area, this is a neutral market.

Initiating Activity: When the market opens above (or below) the value area and does not get inside the value area.

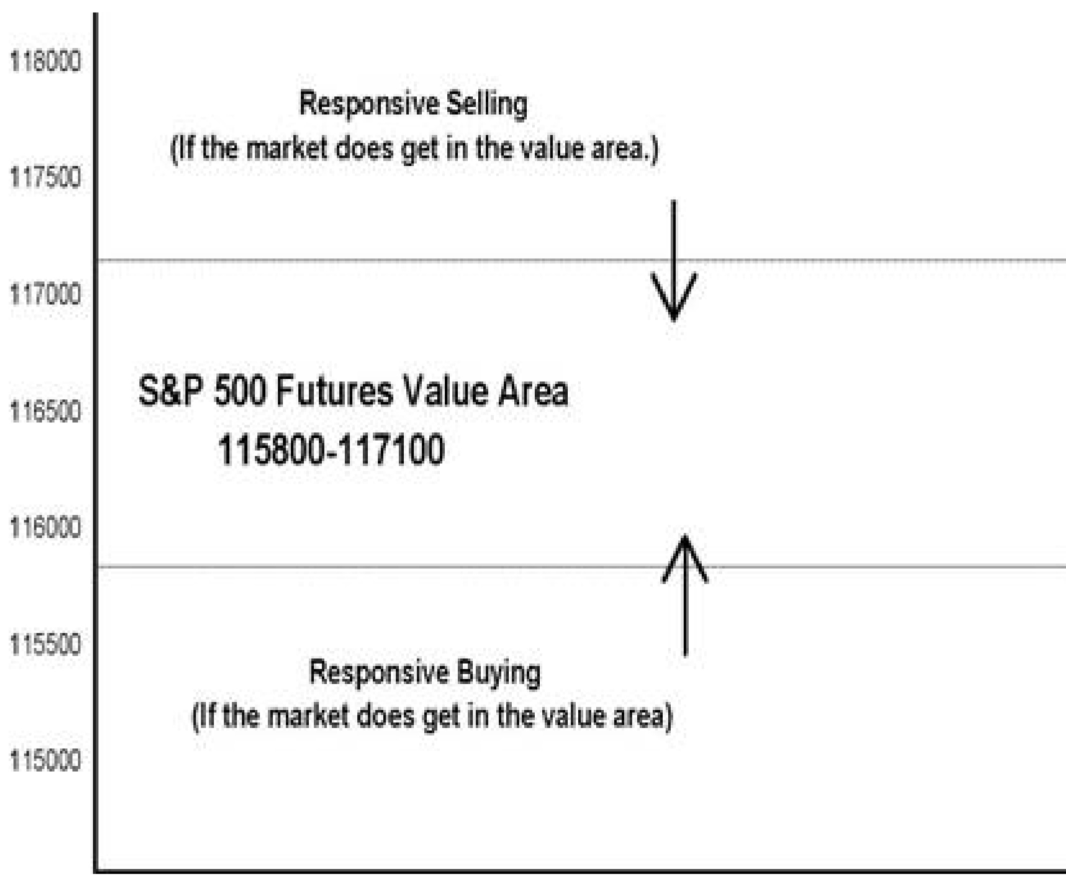
Initiating Buying: When the market opens and stays above the value area, this is a strong bullish signal. When this happens, you have dealer and institutional buying going on in the market. When the dealers and institutions are long, you don't want to put on a position opposite of what they are doing. The best chance to profit on a day like this will be from the long side. Buying breaks (dips in the market) to get long will be the best strategy. In fact, I would say that when the market has opened above and stays above the value area, you should be afraid of being short.

Initiating Selling: When the market opens and stays below the value area, this is a strong bearish signal. When this happens, you have dealer and institutional selling going on in the market. When the dealers are short, you don't want to put on a position opposite of what they are doing. The best chance to profit on a day like this will be from the short side. Selling rallies to get short will be the best strategy. In fact, I would say that when the market has opened below and stays below the value area, you should be afraid of being long.

INITIATING ACTIVITY



RESPONSIVE ACTIVITY



Responsive Activity: The opposite of initiating activity. When the market is above (or below) the value area and does get into the value area.

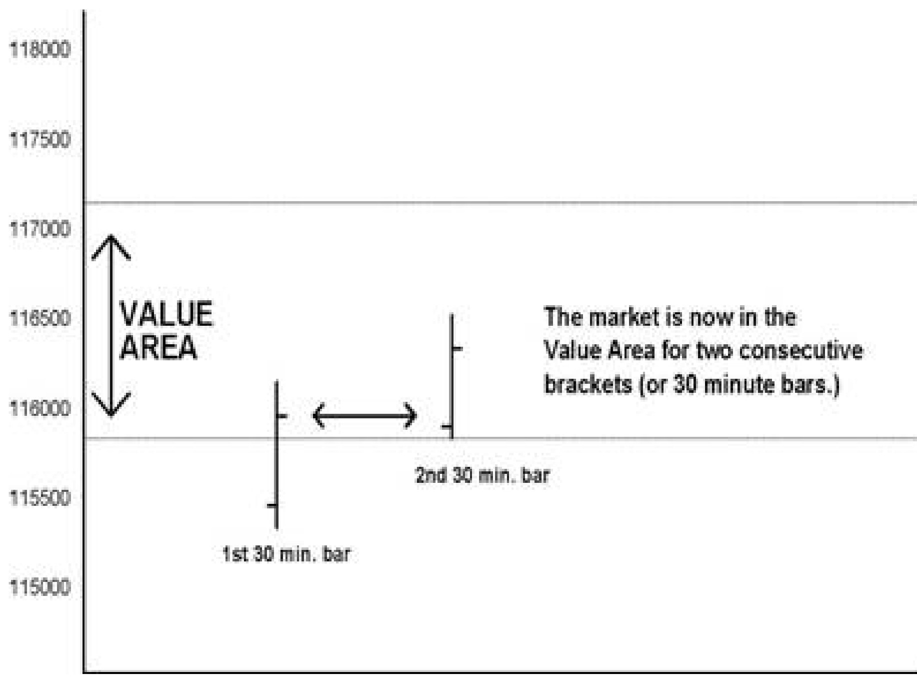
Responsive Buying: When the market opens below the value area and buying starts coming into the market (in other words, the market starts moving higher when it is below the value area.) Buyers are "responding" to the market being below the value area and they are attempting to buy the market cheap, thus pushing the market back towards the value area. When we get responsive buying in the market, there is a good chance we will see the 80% rule come into play.

Responsive Selling: When the market opens above the value area and selling starts coming into the market (in other words, the market starts moving lower when it is above the value area.) Sellers are "responding" to the market being above the value area and they are attempting to sell the market at higher prices than yesterday. When we get responsive selling in the market, there is a good chance that we will see the 80% rule come into play.

The 80% Rule:
The 80% rule is easy to understand. It simply means, if the market opens above (or below) the value area and then gets in and stays in the value area for two consecutive half hour bars or brackets (see definition below,) it then has an 80% chance of filling the value area. With that in mind, a good strategy is to try and ride the market as it fills the value area. There are two scenarios to watch for:

- **If the market opens above the value area** and then gets in the value area for two consecutive brackets, there is an 80% chance of the market filling the value area.
- **If the market opens below the value area** and then gets in the value area for two consecutive brackets, there is an 80% chance of the market filling the value area.

Two Consecutive Brackets: When looking at a 30 minute bar chart, if the market is in the value area for one bar, and when the next bar opens, if the market is still in the value area, *the market has then been in the value area for two consecutive brackets.* This is the time to watch for the 80% rule. (See chart below.)



Important Exception to the 80% Rule:

The market does not have to open above or below the value area to have the 80% rule come into play. Here's why:

1) If the market opens in the value area, and then gets either above or below the value area, you can still have an 80% rule.

2) Once the market has moved above or below the value area, and then gets back into the value area (for two consecutive brackets or 30 minute bars,) you then get the 80% rule. When this happens, it's as if the market had opened above or below the value area. The market now has an 80% chance of filling the entire value area (even though the market didn't open above or below the value area.)

Some Important Things To Remember About the 80% Rule:

When the market has opened <u>above the value area</u> (and then gets in the value area):

When the market gets into and stays in the value area for two consecutive brackets, that is the time I'll look to get short (looking for the market to move lower and fill the value area.) But I want to try and get short as close to the top of the value area as possible because my protective buy stop should be above the value area. Here is why that's important:

1) I want to take as little risk as possible, so the closer I can enter my short position to the top of the value area, the better.

2) I don't want to get short too close to the bottom of the value area because my objective (exit point) is the bottom of the value area. It certainly wouldn't be smart to try and get short very close to my objective, because the risk to reward ratio is not very good.

3) In this scenario, the market will often give me a chance to get short at the top of the value area. If I miss my chance to get short near the top of the value area, I will usually not attempt this trade. Remember, the further away you get short from the top of the value area, the more risk you must take because the correct place for your buy stop should be above the value area.

When the market has opened <u>below the value area</u> (and then gets in the value area):

When the market gets into and stays in the value area for two consecutive brackets, that is the time I'll look to get long (looking for the market to move higher and fill the value area.) But I want to try and get long as close to the bottom of the value area as possible because my protective sell stop should be below the value area. Here is why that's important:

1) I want to take as little risk as possible; so the closer I can enter my long position to the bottom of the value area, the better.

2) I don't want to get long too close to the top of the value area because my objective (exit point) is the top of the value area. It certainly wouldn't be smart to try and get long very close to my objective, because the risk to reward ratio is not very good.

3) In this scenario, the market will often give me a chance to get long at the bottom of the value area. If I miss my chance to get long near the bottom of the value area, I will usually not attempt this trade. Remember, the further away you get long from the bottom of the value area, the more risk you must take because the correct place for your sell stop should be below the value area.

<u>The Top and Bottom of the Value Area are</u>
<u>Excellent Support and Resistance Numbers!</u>

I will use the top and bottom of the value area as support and resistance numbers. For instance, if I were long above the value area, I would put my sell stop just below the top of the value area because if the market got into the value area, it would cancel out the bullish signal. And, if I were short just below the value area, I would put my buy stop just above the bottom of the value area. If the market gets back into the value area, it cancels out the bearish signal.

<u>The reason I put my stops just inside the value area:</u> Most futures markets (especially electronically traded markets) are very volatile. You've got to think of support and resistance numbers as an area and not just a single price. If you place your sell stop at the very top of the value area (if you're long) and at the very bottom of the value area (if you're short) then you run the risk of getting stopped out of the market if it only touches the bottom of the value area instead of actually trading back into the value area. I want to see if that particular level will hold, not necessarily, just that one price.

<u>Some Final Notes</u>

The value area is something I watch everyday. It's an excellent gauge of market direction, and you should always be aware of it. The 80% rule can be very profitable once you get used to it. (But remember, 80% means it will work 8 out of 10 times, not 10 out of 10. So make sure you always have your protective stop in place to protect yourself.)
The other thing that I must mention is about initiating activity. If the market opens above the value area and can't get inside the value area, this is when you get initiating buying. Does this mean that the market can't go down? Of course not! The market can go any way at any time. (If there are more sell orders, it will go down, it's that simple.) But when the market opens above the value area (and can't get in) there is a better chance that it will go up. So, looking to buy breaks and get long will be you best chance for success. And the opposite is true. If the market opens below the value area (and can't get in) the market can still go up if there are more buy orders. But in this case, looking to sell rallies to get short will be your best chance for success.

<u>Frequently Asked Questions about the Value Area and the 80% Rule</u>

Q. How do I get the value area each day?

A. The Value Area, as well as other key support and resistance numbers is available from Secrets of Traders LLC. All of the day's key numbers are emailed to you each day before the market opens. Contact us for further information.

Q. What is the market telling me when it is in the value area? What is the market telling me when it is above or below the value area?

A. When the market is inside the value area it's telling you that the market is basically in balance, and neither the buyers nor the sellers are in control of the market. When the market is above or below the value area it's out or balance and is currently rejecting the value area. In other words, when the market is above or below the value area, it's showing that either the longs (if the market is above the value area) or the shorts (if the market is below the value area) are currently controlling the market.

Q. Does the market have to be in the value area for a full hour to get the 80% rule?

A. No, that's a common misconception. To get the 80% rule, you need this: One 30 minute bar needs to close inside of the value area, and when the next 30-minute bar opens inside the value area, you then have an 80% rule! So it can happen very quickly, sometimes as short as a few seconds and sometimes much longer. The important thing to remember is the market does not have to be in the value area for the full 30-minute bar (or even two 30-minute bars,) it simply needs to have one 30-minute bar close inside the value area, and the next 30 minute bar open inside the value area. But remember, the market needs to be outside the value area at some time first, and then get inside the value area to possibly have an 80% rule.

Q. Can you have an 80% rule when the market has not gotten outside the value area yet?

A. No, the market must start outside the value area, get inside the value area for two consecutive brackets, and then you have an 80% rule. Or it can start inside the value area, get out of the value area, then go back inside the value area for two consecutive brackets, and then you have an 80% rule.

Q. Is the 80% rule still in effect if the market gets inside the value area for two consecutive 30 minute bars, but then it gets back outside the value area? Is there still an 80% rule?

A. Yes, the market still has an 80% rule. Even if the market gets outside the value area (after being inside the value area for two consecutive 30 minute bars,) the market still has an 80% chance of filling the value area. Also, it is often said that if the market does not fill the value area before the end of the day, always look for it to happen the next day.

If you have questions, or comments we would like to hear from you. Simply contact us at:

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