Steidlmayer on Markets
Trading with Market Profile

Second Edition

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FOREWORD

A chart is a communication vehicle. Its purpose is to com-
municate what is transpiring at point A (trading pit) to an ob-
server at point B (some distant location). One can look at any
charting system (e.g., bar, point and figure, candlestick) as a lan-
guage. Each was developed to communicate market condition to
an observer. The language of trading has its own vernacular. Ex-
amples include: "it feels heavy here," or "it feels like we have
more to go." Market Profile is the product of a professional floor
trader's ability to communicate the pit trading experience sym-
bolically in chart form. Here is how this is accomplished.

The standard 30-minute bar chart automatically moves to
the right to start a new bar every 30 minutes. The horizontal di-
mension in this chart is automatic—dictated by chronological
time, not market activity. The involuntary nature of this action
inhibits the ability of the bar chart to communicate market ac-
tivity in the horizontal. This limitation is analogous to trying to
communicate detail or nuance using only nouns and verbs but
no adjectives or adverbs—less than adequate communication.

Market Profile has no chronological restriction. It expands
horizontally only when prices repeat. Horizontal expansion of
the chart reflects only market activity, never chronological ac-
tivity (the passage of time). Market Profile more clearly illus-
trates to the trader a new directional move beginning in a dead
market or a directional move losing momentum. The feel of the
market is objectively illustrated using the horizontal dimension.

Visual focus = Accurate communication = Better trade identification
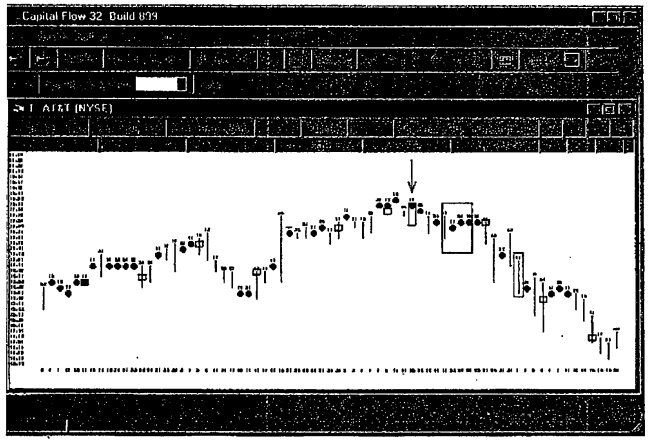
Jim Mayer—President
Mayer Investments

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Figure 13–10   Market activity display of AT&T with directional arrow. Provided by Steidlmayer Software Inc.

curve. It is a function of using the latest technology and best product. This is the model used by a well-known options trading group to make Chicago synonymous with options and put the city on the trading map. Their name was Chicago Research and Trading (CRT). They attempted to be part of every trade with their cutting edge technology and traders populating every pit (access). They were looking for the edge. They were creating a low-margin business, the grocery store model of high-volume, low-markup. They were the first to commit to this model in such a grand scale, and as in anything in life, it pays to be first with a good idea.

What is Access?

Access means different things to different people. At its core, it is getting an order to the exchange. This can be accomplished by talking to your broker, being on the floor, or using electronic order entry. In the investment world, technology has probably affected access more than any other facet of the business.

This revolution has taken place over the last 10 years and really came to a head over the past 2 years. Let us use the access flow chart pyramid in Figure 13–11 to illustrate this point.

At the base of the pyramid, we see raw price data at the exchange level followed by connectivity to exchange. Earlier, we listed raw price data and the broadcast of that information as a commodity just as electronic access would have been considered a commodity early in its existence. By saying electronic access is a commodity I mean all front-end providers offered essentially the same utility with the same limitations. In the access flow chart pyramid, the next level is "price display on front-end." This price display, which we call the first generation of electronic order entry, was keyboard-driven, clumsy, and unique to each exchange. The next generation brought front-end providers that accessed multiple exchanges with point and click technology. During the time of commoditization of order routing, the only thing that set the order routing firms apart was their logo on the splash screen. However, during the last 2 years, these providers have attempted to differentiate themselves by offering

third page2 mark back. Moving onto volume, any of the volume studies covered in Chapter 7 can be built into a system and traded. Volume is the "footprint" the market leaves in its wake; picking up on heavy volume, light volume, and volume excesses communicates a great deal of information to the trader. Once again, this short list of applications is not meant to be exhaustive; its purpose is to give the reader a flavor of what is available and can be automated in Capflow32.

Remember the two ways to make money in trading are recognizing opportunities and getting the edge. Up to this point, our entire focus has been on understanding and applying the Market Profile methodology to finding trading opportunities. It is a necessary process one needs to go through to become successful. You need to go to school and pay your tuition and study your lessons before you can go out into the real world and attempt to make a living.

The second way to make money in trading is a bit more straightforward, is more interactive, and has a shorter learning
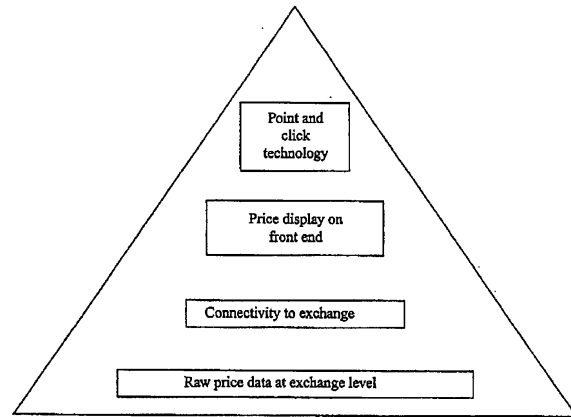
Figure 13–11   Access flow chart pyramid.

different bells and whistles, creating the "x" generation of electronic order routing.

Looking at front-end providers, the common denominators to use for comparison purposes are speed of access and reliability. How long does it take to get an order from your desktop to the exchange? How much downtime does the system experience? In reality, speed is a function of the desktop layout, coding, technology, and routing. A person looking intently at the order routing screen takes between 80 and 130 milliseconds to react to price change, volume info, news blips, and so on. The big attraction to trade electronic exchanges lies in the level playing field offered to all participants. By that I mean once the order reaches the exchange, it is processed and queued by the standard accounting practice of *fifo* (first in, first out). It does not matter who you are or who you know, if your order is first to the exchange you will get filled first. Therefore, if a trader hesitates for an instance because she or he is not confident, her or his mouse is positioned over the correct price, volume numbers need to be accumulated, or she or he needs to fo-

cus on another screen to get some relevant information, the trade could be gone or the trade price could be significantly different.

MD_Trader

Trading Technologies' (TT's) X_TRADER® with the MD_Trader™ display presents prices with accumulated volume traded at a price in a patent pending static vertical price display. (X_TRADER® is a registered trademark and MD_Trader™ is a trademark of Trading Technologies International, Inc., of Chicago, Illinois). In the display, consecutive prices in a price array are displayed in a static vertical format, with changing bids and offers denoted in columns to the left and right, respectively, of the static vertical price column. Figure 13–12 is an
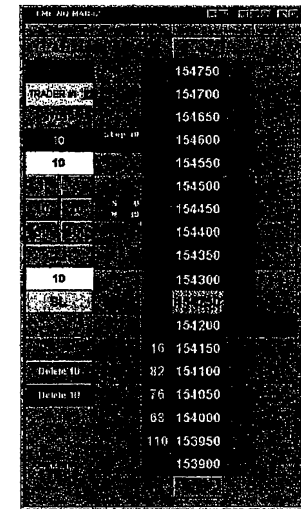

Figure 13–12   MD_Trader™ display of the Mini Nasdaq.

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MD_Trader™ display of the Mini Nasdaq. On the left-most side of the display are the components needed to enter trade size, account number, and other relevant information. In the next column to the right, all your working orders are denoted. Farther to the right is the price array for the underlying instrument with the book (existing bids below and offers above). The last column lists the price and quantity for the last trade. This superior format—and we know it is superior because all the competitors are attempting to copy it—has a consolidation feature that allows for more or fewer prices to be displayed in the MD_Trader™ display. This feature comes in handy during periods of extreme volatility (e.g., release of economic numbers, news events). Combining all these features elevates your confidence level in responding and clicking the price you want to be trading. Another feature of the MD_Trader™ is center clicking, which positions the currently traded price to the center of the MD_Trader™ display window. Therefore, from a pure speed perspective, TT's X_TRADER® front end with the MD_Trader™ display provides what you are looking for, the fastest access to the market.

Two satisfied customers have had this to say about the product: D.J. Martin, independent trader with an MBA from New York University (NYU), whose dream was to move to Chicago and strike it rich as a trader. He moved to Chicago during the summer of 1997. Over the next 4 years, D.J. came close to losing his nest egg more times than he cares to remember; however, he always managed to fight back and make enough to live on. He realized there was something missing in his trading, so he made the change to TT during the summer of 2001. Since switching to TT, he has not had a losing week, has had 6 straight winning months, and has strung together 94 winning days in a row. "Since I started using TT, my income has increased by almost $600,000 a year. My trading approach has remained the same; therefore, I must conclude my recent success is directly related to using MD_Trader™ and other innovative tools and cutting edge technology offered at TT." This from Chuck McElveen, owner/operator Kingstree Trading, a

large Chicago-based proprietary trading firm that accounts for the largest percentage of daily mini volume traded at the Chicago Mercantile Exchange (CME). "Since opening our doors, TT has been our company-wide solution for trading software. Without question, we could not have achieved the same success or traded as much volume without MD_Trader™. No other application allows you to fully capture the flow of the market and to capitalize on that flow with speed and precision. Our relationship with TT goes back to the company's inception, so it's difficult to assign a dollar amount or percentage by which they have contributed to the bottom line. I can say, however, that having my traders use TT front-end has positively impacted profitability at Kingstree Trading." With speed being our basis of comparison, TT has the others beat hands-down. The process is faster and more reliable.

The next layer of comparison is looking at what front-end providers have done to differentiate themselves from a value-added perspective. This is where TT has really distinguished themselves. They have created automated order execution and management tools. At this point in time, the application that really sets TT apart from the rest of the competition is the Autospreader. The Autospreader allows for the entry of two-legged spreads with a high degree of reliability. The key word here is reliability; it is one thing to offer the functionality, yet another to deliver. There is no worse feeling than entering a spread order, getting hit on one leg, and subsequently watching the market move sharply against you. The Autospreader allows the trader to set up a spread and enter spread orders in an MD_Trader™ display. After an order is entered, the tool automatically enters orders into the outright legs and manages those orders. The Autospreader automatically sends offset orders into the other leg once an order in one leg has been filled.

Figure 13–13 is a screen capture of the Autospreader with the corresponding underlying futures contracts. The Autospreader is the leftmost MD_Trader™ display, and the futures contracts are the right two MD_Trader™ displays. In setting up the spread ma-

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