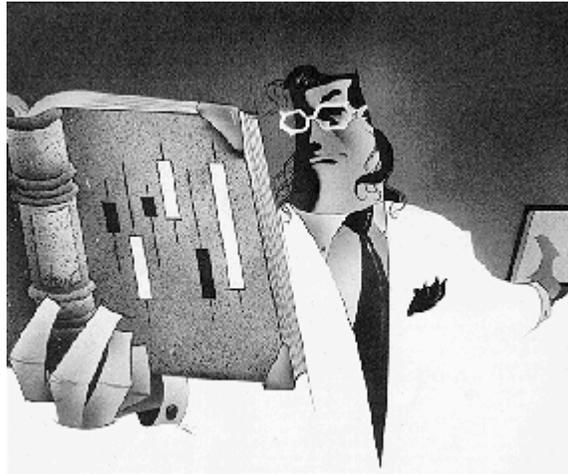


Market Turns And Continuation Moves With The Tick Index

by Tim Ord



The tick index is a little-known indicator that can be used to indicate short-term stock market reversals and provide trend confirmation. Short-term traders should consider using the tick index, for though this indicator does not always tell you a story, it can help alert you to overbought and oversold situations.

A little over a year ago, I wrote an article in which I described a buy and sell method using the tick index on the New York Stock Exchange (NYSE). The tick index is the difference between the number of issues trading with the last trade higher (an uptick) from the previous price and the number of issues trading with the last trade lower (a downtick) from the previous price. For example, if exchange X has 500 issues trading on an uptick and 250 issues trading on a downtick, the tick index would be $500 - 250 = 250$.

To summarize my method of using the tick index, a buy signal is generated when two intraday 600-plus downtick readings are recorded at approximately the same price level on the Dow Jones Industrial Average (DJIA). These 600-plus downticks should be at least one day apart but not more than 10 days apart. If the market makes a double bottom and the tick index has reached 600 or more downticks at both bottoms, then the *second* reading of 600 or more intraday downticks is a buy signal. For a sell signal, the reverse is true: When the market is making a double top and the tick index readings on both tops intraday exceed 600, then the second reading of 600 or more upticks is the sell signal.

The tick index is useful for a host of other market applications. After years of analyzing the tick index as a market indicator, I have discovered numerous trading rules that are useful in day-to-day trading. Familiarizing yourself with these rules will help you become more aware of market conditions leading to market turns.

TRADING RULES FOR THE TICK INDEX

Here are four trading rules that use the tick index and apply these rules to two recent market moves. The first rule is for a continuation move:

- 1 The New York tick index records high intraday tick readings (in excess of 600 up- or downticks) and the market closes near the high or low for the day. Further price movement can be inferred from these conditions.

The next three rules are to identify upcoming turning points in the market and confirm trend reversals:

- 2 When the difference between opening and closing prices become narrow and intraday tick readings exceed 600, a turn in the market is likely.
- 3 Closing tick index readings that exceed 600 is a sign that a market turn is fast approaching.
- 4 At breakaways from tops or bottoms, the tick index will usually record high intraday tick readings exceeding 500. This confirms that the trend has reversed and a new trend begun in the opposite direction of the previous trend.

Next, using these four rules, we'll analyze two recent market moves on the June Standard & Poor's futures contract: the December 19, 1991, low and the April 8, 1992, low.

On December 19, 1991 (Figure 1, using the candlestick technique), a downtick reading of 670 was recorded and an intraday buy signal (A) was generated based on rule 2. The next day (B), the market gapped up, 860 upticks were recorded and the opening and closing range narrowed. As mentioned in rule 4, high tick readings occur on breakouts from tops and bottoms, which turned out to be the case here. Also, the difference between the market's opening and closing range was narrow and high tick readings were recorded (rule 2), implying a pending top. Here we have a conflict between rules 2 and 4. Experience has taught me that this conflict represents an important market point, so sell stops from the previous buy signal should be tightened and a trader should go with the market direction that follows that trading day.

On Monday, December 23 (C), the conflict is resolved: the June S&P impressively rallied more than 10 points, but only recording 610 upticks intraday and a closing tick reading of +230. Because the market moved up freely and held its gains with high upticks recorded, still higher prices could be expected in the near term, according to rule 1. On December 24 (D), the market kept its momentum but showed signs of stalling, as 710 upticks intraday were recorded but only a two-point gain was achieved. Again, stops should be tightened. The market was closed December 25, while on December 26 (E) the market picked up steam, gaining five points. The uptick reading intraday was only 620. From these conditions we can infer higher prices, because tick readings decreased from the day before while the gains doubled (rule 1).

On December 27 (F), the market gained another two points and the closing tick was 538 upticks. This reading can be the market made another impressive rally, gaining over eight points and closing on 660 upticks. Such high uptick readings at the close tip us off that a top is approaching (rule 3). The next day, December 31 (H), provides more evidence that a market top is occurring. On December 31, the market opened and closed in a 1-1/2 point range and a closing reading of 796 upticks was recorded (rules 2 and 3). Here, the market traded in a narrow range and closed on an extreme uptick reading exceeding 600, conditions that imply the market has run out of steam — an excellent time to sell positions.

For our second example (Figure 2), the April 8, 1992 (A), low, the tick index method indicated a reversal based on rule 2. The intraday reading was 1,000 downticks and the market had a fairly narrow range

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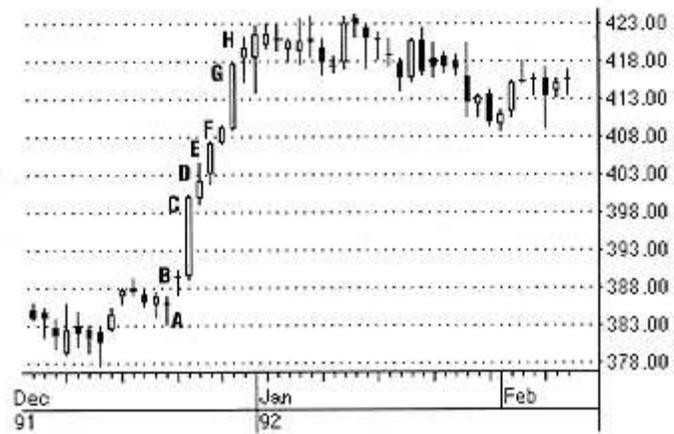


FIGURE 1: *Following the intraday and closing readings for the tick indicator can confirm market trends and forewarn of reversals.*

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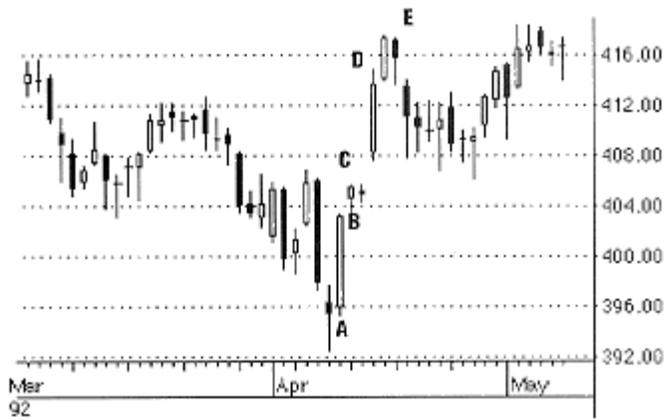


FIGURE 2: *The tick indicator helped identify the April bottom and confirmed the new trend but did not indicate the trend reversal. This is one example of the importance of using trailing stops.*

between the open and closing price. The buy signal method described above states that a buy signal is generated when two intraday 600-plus downtick readings are recorded at approximately the level of the DJIA. The next day, April 9, the market rallied, hitting 750 upticks intraday and closing up eight points on the June S&Ps. Even though high upticks were recorded, the market held its gain, so an impending top was not indicated (rule 1). In addition, at breakaways from tops or bottoms, the tick index will usually record high intraday tick readings exceeding 500 (rule 4).



"Does 'ho, ho, ho' mean yes or no?"

Following and applying these rules using the tick index should help you be able to identify impending market turns and continuation moves.

On Friday, April 10 (B), the market continued its rally, closing up about 1-1/2 points and hitting 920 upticks. This warned of a possible market top, because the June S&Ps traded in a narrower range than the previous day and on higher upticks (rule 2). On April 13, the June S&Ps were open only part of the day because the Chicago Exchange floor had flooded, precluding trading for that day. The day closed down about 1-1/2 points on 143,000 contracts. No meaningful analyses on market data can be made about the trading that day.

On April 14 (C), the market gapped higher and resumed its advance, closing up 8-1/2 points on the June S&P and hitting 1,000 upticks. Again, no top is indicated because the market held its gain, even though high upticks were recorded (rule 1). As a reminder, however, sell stops should be tightened as a protective measure. On April 15 (D), the market kept its momentum, closing up 3-1/2 points and hitting 450 upticks; again, trailing stops should be raised. On Thursday (E), action did not get into the intraday 600 range, nor did the market stay in a narrow range (rule 1). However, if a stop order had been placed at the previous day's low, the trader would have been stopped out on April 16 for a nice gain. The June S&Ps began to decline from this point. The intraday and closing tick method failed to alert me to a top in the market, which is why stop orders should always be placed with positions.

Following and applying these rules using the tick index should help you be able to identify impending

market turns and continuation moves, so that one day you will be able to read the market as you would a book.

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FURTHER READING

Ord, Tim [1991] . "Picking tops and bottoms with the tick index ," *Technical Analysis of STOCKS & COMMODITIES*, Volume 9: June.

THE CANDLESTICK METHOD

The candlestick chart can be used to interpret the movement of markets from intraday out to a monthly chart format. The basic candlestick chart depicts the market open, high, low and close. The opening and close for the day define the basic body of the candlestick (called the "real body"), while the high and low are the thin lines that extend beyond the body and are known as the "shadows." If the market closes higher than the opening, then the body is empty or white. On those days that the market closes below the opening, then the body is black or filled in.

