

Graphs
AND THEIR
APPLICATION TO SPECULATION

BY

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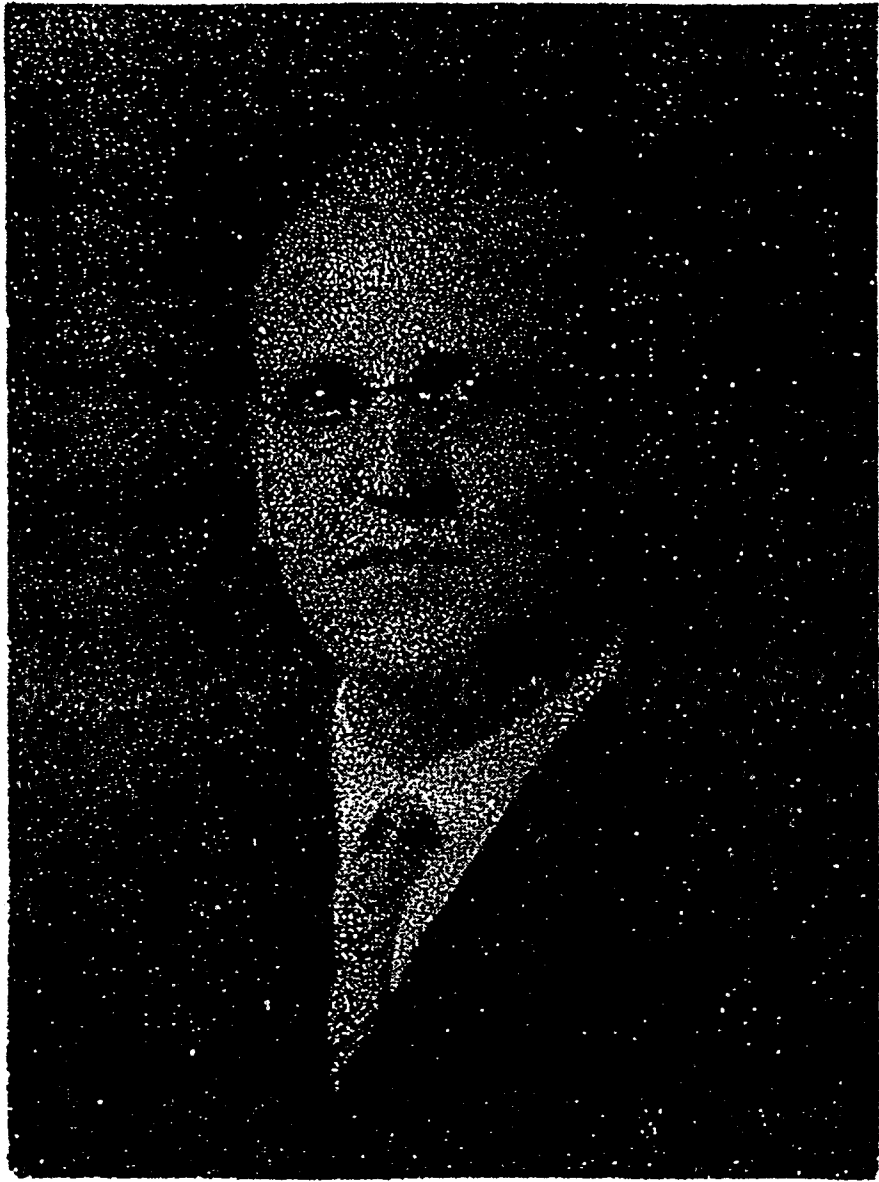
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Geo W Cole

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FOREWORD

In writing this book the prime idea of the author is to write a sequel to his book, "Successful Speculation a Business", because speculation is a business exactly the same as any other line of endeavor. In fact, speculation is more of a profession or an art than ordinary commercial business. Therefore, the intention of the author is First, to show conclusively that there is a science in speculation, the same as in any profession; Second, the same as in any line of business, a dealer in the purchase and sale of stocks and commodities physically or in contracts for future delivery is a gambler with all the inherent risks of outright gambling if he enters into such transactions without proper preparation and knowledge; Third, to logically prove that there is a science in trading in future contracts in stocks or grain, the knowledge and application of which reduces the risk in speculation to the level of all other lines of business.

There are very few books, in fact the number is almost negligible, that cover this subject as it is covered in this book. The method taught is not entirely new, but as promulgated is the result of many years of study.

The author insists upon it being clearly understood that the method which he terms The Science of the Interpretation of Market Graphs is not a "get rich quick" scheme, plan or mechanical rule by which profits are assured. There is no intention even to imply such an idea. The author's intention is to prove that Graphs of the action of the market price show in pictorial form the psychology of the mass mind as influenced by world conditions; that the future trend of prices of all commodities is based up-

on the law of occurrence or recurrence as shown by study of price action as clearly set forth in understandable form in graphs of past price movements; but, that judgment is paramount in correlating the facts and applying them successfully in buying and selling commodities.

The author faithfully believes that no matter what regulations or restrictions are placed on trading in contracts for future delivery in the commodity or security markets as long as prices are quoted the psychology of the market will be clearly shown in the graph record.

Some systems or sciences used in forecasting the market are especially good for bull markets and others are exceptionally good for bear markets. The Science of the Interpretation of Market Graphs is the only science that we have found to work with either a bull or a bear market. It always indicates when to go with the market.

In addition to the author's original interpretation of The Science of Interpretation of Market Graphs many methods of others are included. The author is indebted to E. P. Miller, Statistician and Preceptor, Pickell-Daniel, Inc., Commodity Statisticians; Robert Rhea, author of the book The Dow Theory; Thomas Temple Hoyne, author of Speculation, Its Sound Principles and Rules of Practice; Professor G. Wright Hoffman of the University of Pennsylvania, author of Future Trading; Ralph M. Ainsworth, forecaster and student of commodity economics, and of others, all of whom are given full credit in the text.

The preparation of this book has required considerably over a year of hard, persistent application and study. It has been intensely interesting and it is the author's hope that his readers will not only be interested, but also gain from this

study immeasurable benefit and material profit. It is not a subject that can be read lightly without application, but one that must be studied seriously and with the certain knowledge that the full measure of material benefit will be obtained from its perusal.

Graphs

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APPLICATION TO SPECULATION

CHAPTER I

GRAPHS, WHAT ARE THEY?

"Huh! that fellow is a 'chart trader'". You undoubtedly have heard such a remark or expression among a group of speculators. A few years ago remarks ridiculing "chart traders" were quite common, but in recent years it has finally permeated the trade that so-called "chart traders" are more successful in trading than the hit or miss, tip hunting hunch traders.

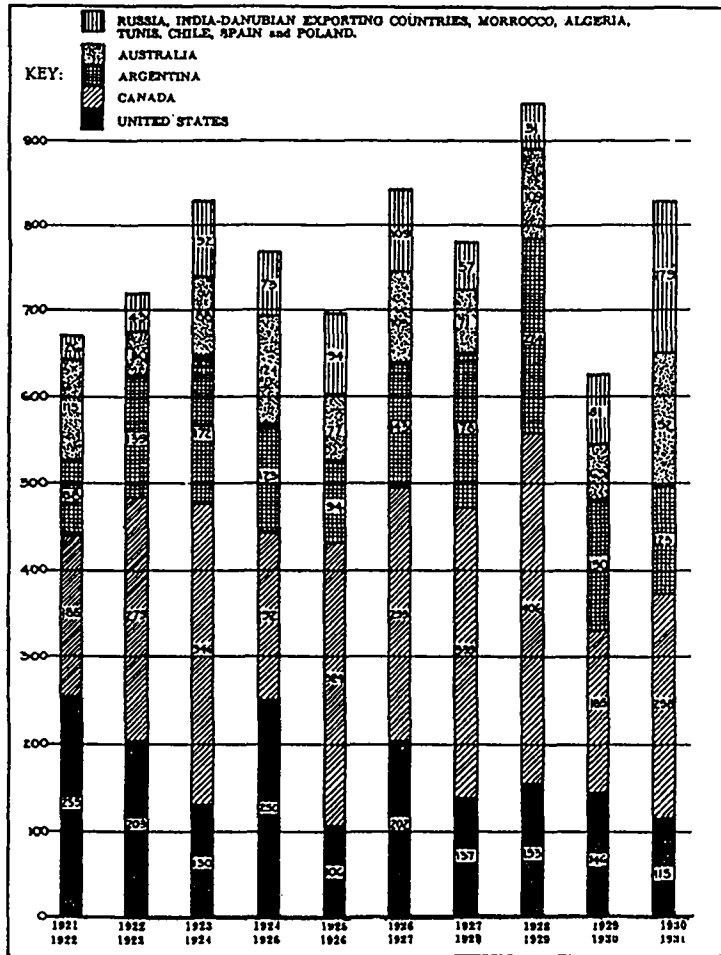
In the first place, "chart trader" is a misnomer. The proper name for the so-called "chart", recording the daily, weekly and monthly movements of grain and stock prices in a "graph", therefore, the proper name for "chart trader" is "graph reader." Anything can be graphed and most anything showing action or comparison, can be charted. There are charts as well as graphs, and both are proper in their proper places. Let us first show the difference between charts and graphs.

In Figure I, you will find an illustration of a chart of volume. The details in this chart could be graphed, but it would be a very difficult graph to make, as the lines denoting the comparisons of volume would criss-cross in such a complicated manner that it would be very difficult to read. In many following illustrations graphs are shown, and this illustration of a chart is simply to show what a

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chart is and that it is not a graph. In many instances, or where quantities and comparisons of quantities are needed to be shown, a chart is simpler, clearer and more quickly understood than a graph covering the same action or subject.

Chart of
Sources of Net Exports of Wheat and Flour
1921.22 to 1930.31



It is easily seen that the chart in this illustration, on account of the fixed quantities, shows

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the picture better than a graph would show it because the variation in the volume of the quantities in which the lines of the graph must necessarily cross over and through each other, is rather confusing. However, either a chart, or a graph of this subject would have to be studied in order to obtain the comparisons, but it is obvious that the chart of this subject shows the relative quantities clearer than a graph, with less study.

Some people like a graph better than the chart in all cases, but a graph is proper and better in covering a continuous movement of quantity or volume of any commodity, because it gives a clearer picture, showing comparison of the movements and can be continued indefinitely, while in a chart of the same movements, the movements must be definitely fixed, cannot be extended, and the details must be studied for comparison.

A chart is a dead picture. A graph is just what the name implies, a pictorial writing, and when used in recording a market movement, it shows a quickly understood picture of detail and extent that could not be portrayed in any other way so conclusively and understandingly.

Value of Graphs in Speculation

But before going into the detail, it is well to state why graphs are of value in speculation. Thomas Temple Hoyne, in his book Speculation* says: (quoted verbatim page 174. Note he refers to graphs as charts. Underscored by the author). "I do not wish to be understood as belittling the value of charts of market action. Nothing is more valuable for the study of the speculator if he comprehends their limitations. They are but drawings of the dead skeletons

* Speculation, Thomas Temple Hoyne, Economic Future Service Co., 1014 South Michigan Blvd., Chicago, Ill.

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of market actions. All life, which produces the psychology of the market, has gone out of them. Nevertheless, their instructive power is immense and even "chart players", such as I have described, invariably possess a knowledge of market action far superior to that of most brokers and speculators."

(Also page 175), "Properly used charts are the best handbook of knowledge of market action. By properly used I mean that they should be studied to discover idiosyncrasies of different types of markets, for there are many types of markets, just as there are many types of human beings. In the actual market these types cannot, of course, always be recognized before they develop positively, but often they can be detected as they unfold with a certainty that is almost uncanny."

In quoting these two paragraphs from Mr. Hoyne's book, I do not wish to in any way misrepresent him in his belief or his writings in regard to the value of graphs in speculation. Mr. Hoyne's book, Speculation, which I consider one of the best treatises of the theory and practice of speculation so far published, should be in the library of every person interested not only in speculation in stocks or commodities, but in any kind of business. Mr. Hoyne does not believe in the use of graphs in speculation beyond what he says in the quotations given above, and he goes to great length in his book to say so. I agree with Mr. Hoyne that it is strictly up to the individual to develop his knowledge and power in order to make a success of speculation, and that there are no graph market systems or any other "systems", which one can use at will and from which one can pick out profits.

I also am in thorough accord with his statement that "graphs are a dead skeleton of past events", which is as apt an expression as one could ask for,

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because graphs of a grain or stock market are just that and no more, when viewed as graphs. However, in the use of graphs of the market as a guide for speculation, the graph is something more than just a record because while in detail the graph shows every action of the past, and is an accurate history of what the market has done, it is more than that - it depicts a combination of the actions, emotions and ideas of mass speculation.

Price Controlled by Universal Laws

This speck in the Universe, which is called the Earth, is the result of universal laws. It was created by the laws of the Universe; it has rotated on its axis and around its sun without deviation, for millions of years. It has maintained its position relative to the other planets of the Solar System exactly the same, and will continue to do so through eternity as far as the race of man is concerned. Life on this planet was created in the same way, has evolved since the first protoplasm for millions of years. Also, plant life was brought into existence and has each season been producing food, the production of which has been developed by man to as near perfection as possible, according to the limitations of the understanding of man at this time, all guided by a supreme power and operating under supreme universal laws.

It is obvious that these supreme universal laws operate on the Earth even unto the smallest atom of the Universe. If such is the case, which we accept as true without question, why is it not true that all actions and every action of man or of the products of the earth are also guided and directed by universal laws? This seems obvious. Therefore, we must arrive at the fact that the price of any commodity which is bought and sold, bartered and consumed,

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must be guided and controlled by universal laws. We can also see by this reasoning that everything happens because of what has happened before. Man is a combination of action, emotion and ideas based upon heritage, environment, needs and desires. If, under certain conditions, he has certain reactions, then under similar circumstances, all things being equal, he will have the same reactions, and along this line of reasoning his operation of production, consumption and value of commodities will be controlled by universal laws.

Therefore, it seems an abstract truth that man makes the prices of all commodities, compelled and motivated by the action of natural, universal laws, inherited through thousands of years of his forbears, and while supply and demand is the material premise upon which to control values, man makes supply and demand. Also, while supply and demand in the absolute, is the correct premise for value or price, man, in his limitations, is unable to encompass it in its entirety; therefore, the reason the value of a commodity is what it is, is that it is just what man thinks it is. The psychology of the market in any certain commodity is not only the main factor, but is the entire factor in making the price.

Science of Price

With the knowledge that every atom of the Universe is controlled by universal laws, from these deductions we must conclude that there must be an inexorable law of price, which is just as exact as any science, such as the law of medicine, as an illustration, and also many other well recognized sciences. Also, while the science of medicine has made stupendous strides in the present era, and still is in its infancy as compared to the heights it will eventually reach, the science of price is in the stage of

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recognition only. Medicine has built its science from study of past wants, action and reaction (The skeleton, muscle and nerve structure of the human body upon which the science of medicine has been built, can be compared to the graph of the past action of the market). And upon the past action and reaction of the market, a science of price can be built.

Now this is where a graph of the market is of its great value as an aid to successful speculation. In studying graphs, we find many fluctuations, "hills and valleys", etc., which show just what the market has done, and the student must conclude that the market has made these fluctuations and changes because the speculator, as a mass, has backed up his thoughts and opinion by his action in the market.

Then again, in studying all graphs, the student finds that when certain "formations" are made, denoting certain activities or actions, the market as a rule does a certain thing. He also finds in close study, that this occurs time and time again. It is not an absolute rule, because there is nothing absolute in the mind of man but the recognition of these actions that recur in such a large majority of times, is of definite value in determining what action should take place in the future.

From an absolute viewpoint no man can tell what the market price will be the next day after he has recorded this day's action on his graph but, from his study and according to his individual limitations, he has the majority of the chances in his favor to make a correct forecast when he correctly reads from his graph the action of the market in the past.

My Development in Graph Reading

I have made a study of graphs for twenty years. It has not been so many years ago that graphs began

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to be used in all kinds of business, and graphs were just getting fairly started in use for making comparisons and records of business, when I first conceived the idea that possibly they could be used in recording market action.

I still have my original graph sheets and they are quite crude compared with the up-to-date and developed graphs I am now using. However, they were a start. The fact of the matter is, I started making graphs as an experiment, and kept them for several years in a simple way, not really fully understanding or realizing the importance or their application to my business. However, I gradually learned, by watching the actions and reactions, how to use some of my knowledge gained from the action of the market, to successfully hedge my grain to a better advantage.

One of the first things I found of greatest importance in graphs was their value for quick reference. Whenever necessary I could see at a glance the range of the markets for comparative purposes, the high and low of any month or any year for any certain future, and the actual detail of the opening and closing compared with the graphs of supply and demand (that is, the total crops of the season, the export sales, movements, etc). But I must confess I did not appreciate the importance and value of the movements as recorded in my graphs until I took a course under a man whom I consider the dean both of graph making and of the application of graphs to the market. That man is E. P. Miller of Chicago, to whom I give full credit for the foundation upon which I have built my knowledge of graph making and its application to speculation. My study under him opened up to me a clearer understanding of the formations and their values and the great possibilities of development in graph reading.

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Local Reasons for Actions

It is almost uncanny, when looking at the market from an unbiased viewpoint, how often the market will make its average and how often it will return to its average on a reverse and how often the same formations will recur again and again with a definite indication that materializes. And, after all, there is a logical reason behind all these actions.

In my study of graphs, I have found that price movements show what traders as a mass are thinking, and that the markets do what traders think, because they back up their decisions by their commitments in the market.

Speculation is anticipation, and market action discounts coming events before they happen. When analyzed this is obvious. The economic function of price is to regulate the supply to the demand. Price is the result of the mass mind. The fluctuations of price of any commodity indicate the hopes, desires and knowledge of everyone who is interested directly or indirectly in that commodity. The price shows activity or dullness, good or bad news, crop forecasts or political conditions. When the price is recorded particularly in the form of a graph, it is invaluable for study of the indications of future price movements. Coming events affecting the market cast their shadows before them in price movements.

Wheat is a world commodity and the price is made by the composite individual desires and needs of millions of people directly or indirectly interested in its production, distribution and consumption. A crop failure in one part of the world, an insurrection or war or political upheaval, no matter whether in any instance of great or small importance, influences the price and always affects its level long before the event is known outside of its immediate territory. The unsophisticated always are surprised

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to find that the market price does not respond to sudden or important developments and learn when too late that the event or events have been discounted in advance by the price. While the graph of price is a record of the past, the movements shown in the graph reflect the future with unerring accuracy. All coming events excepting the acts of the Almighty, such as disasters and calamities, are truly and faithfully anticipated in the price, and the effect of such calamities, including fires, earthquakes, etc., are quickly adjusted in the price.

Mob Psychology

Mob psychology sometimes carries a small legitimate liquidating or distributing movement into a broad swing far past its relative or warranted value. There is always a neutral point in the swing of the pendulum, at which the pendulum comes to a rest after many fluctuations back and forth, up and down, the arc described gradually growing shorter and shorter until the pendulum stops exactly at the average of its arc. So, in the market fluctuations there is always a neutral point or mean, between the demand and supply, a point to which the bears are endeavoring to drive down the price and bulls to drive it up. The buyers and sellers and the speculative mob are just like the pendulum - first on the one side and then on the other with their commitments, endeavoring to find that common or neutral point which is the actual, although ever-changing value of the commodity, grain or stock.

It may easily be seen that by mob action the neutral point is the Pivotal Point which is passed many times; the pendulum swings too far, practically always assisted and encouraged by master merchants and speculators who recognize the mob psychology and who, through experience, recognize the psychologic-

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al moment at which to reverse their position and start the swing the other way.

The graph records all movements and from these movements the neutral point or actual value can be closely approximated.

One important thing, and probably the most important thing in studying and speculating by means of graphs, is the human equation.

The Human Equation

If a student learns to read graphs with a measure of success, he will find the market movements will show what the markets should do according to the formations, compared with similar formations and occurrences in the past, and will know from his own experience and from his study of other conditions that the markets should do a certain thing; but right here is where the human equation enters into the picture; he does not act.

From the time of the beginning of man, he has had to live upon his own endeavors. He has had to keep a strict lookout for danger to his body and his existence. In time of prehistoric man a bent twig, a footprint in soft soil or the disturbance of foliage all meant something to him and were signs of danger.

The instinct of fear was born at that time and has ruled man to a great extent ever since, and, therefore, when, according to the student's judgment formed by reading the graph of the market, he decides he should take a certain action, he allows environment and suggestion to affect him and fear immediately takes possession of his thoughts. Naturally, he begins to look around and while he does try to eliminate the cause of his fear, most of the time he is unable to do so, therefore, he does not follow and act with cool calm judgment and do what he knows

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he should do, because of that fear instinct. Also, when he has trades open and his reading of the graphs shows that he should take profits and sometimes reverse his position, the instinct of greed takes possession of his faculties and he does not act; thus losing many opportunities that slip away from him on account of greed. Greed is also a heritage from the time of prehistoric man, when many bloody battles were fought for possession of a carcass which was not needed and which, if retained, was dragged to a hiding place where more often than not it was lost to some marauder or rendered useless by decay.

In making graphs and in studying them, the student must at the same time build up a resistance to fear and greed and accept as conclusive and correct, what his deductions and conclusions demonstrate to him as correct.

The greater his courage, the greater his confidence in himself, the stronger will be his resistance to the power of fear and greed, and the greater will be his success. This applies not only in speculation but in all activities of life.

It is only natural and reasonable to understand that one's faculties for reasoning will be at fault at times. A student must expect that he cannot always absolutely arrive at correct conclusions, but with an understanding basis or premise with a reason behind it upon which to act, the principle of which he knows is correct the majority of times, he will be successful to the greatest extent of his limitations, and that is all that can be asked for or expected.

Comparison of Grain and Stock Prices

Everything written so far applies to graphs of all commodities, but more particularly to grain as

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well as to stock prices. It must be understood that the prices of stocks can be graphed in exactly the same manner and in the same method as grain prices. However, there is a dissimilarity to some extent between formations and reactions of stocks, and those of grain. We have not been very successful in taking any single stock and graphing it and forecasting the action of that particular stock. All stocks are inter-related in one way or another, and, as a rule, the action of the prices of the basic stocks, such as U. S. Steel, controls to a certain extent, the movement of the prices of all other stocks. The action of U. S. Steel is usually conceded to be a barometer of the stock market.

The most successful graphing of stocks, therefore, is accomplished by making a graph of a certain representative group of stocks or groups of stocks of certain industries. At the time this book is being written, the Chicago Tribune has published the movement of fifty stocks each day for several years; other great newspapers are publishing lists of thirty to fifty stocks, and Barron's, The National Financial Weekly of New York City, has for many years based its forecasts of stock market price movements on weighted averages which are changed and adjusted from time to time, or two groups of stocks: forty selected industrial and thirty railroad stocks. Both groups are graphed separately and the action of the averages of one must be confirmed by the action of the other group, to make the indication definite.

This method has become widely known as The Dow Theory and it has the reputation of being wonderfully correct. In the book, The Dow Theory*, Robert Rhea says, "It is difficult to understand why Dow

* BARRON'S, New York City, N. Y. 1932, a book which every stock speculator or investor should have in his library.

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did not endeavor to explain why the two averages must conform." Then he proceeds with apologies and offers a few reasons that appear simple and logical. We quote from page 69 of The Dow Theory.

"However, let us consider a cycle of business improvement - after a period of depression. Factories are still idle; unemployment and hard times are everywhere apparent; inventories are low; purchasing power is depleted; dividends have been drastically reduced. But people are still eating and wearing out clothes, more children are being born, machinery is rusting, while labor cost has been materially cut."

Eventually, a day comes when the sales manager of a steel company reviews his field reports and finds, although no orders are in hand, that the erection of a considerable number of bridges and apartment houses, all requiring steel, is being considered for some future time. The sales manager goes to the chief executive and discusses the situation. The chief executive then asks the superintendent about how long it will take to get the mills going when business revives. The superintendent insists he has to re-line a blast furnace before much business develops. The chief executive asks his board for authority to re-line the blast furnace and the repairs are started.

Brick, lime and sand are shipped in by rail and men are employed to re-line the furnace. The traffic manager of the railroad tells his executive of this freight movement to the steel company and suggests that an improved future outlook is indicated if the steel company is spending money. The railroad executive then discusses the situation with his superintendent. They decide to service up ore cars to prepare for hauling ore to the blast furnace, which means buying a little paint and providing a little

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employment for workers. Wages paid for the repairs on the blast furnace and ore cars mean a little more purchasing power for a few people, who then buy some shoes, etc., thereby further depleting the retailers' shelves. This means, in the case of shoes, ordering a new stock from the factory, which causes the factory to require more leather and the tanner, in turn, to need more hides. Then a little steel is bought for bridges and apartment houses, the furnace is put in blast and ore starts moving. Perhaps a similar development is taking place in other lines of business.

"Now, the steel company has not earned a dime insofar as its published statement is concerned, and it may even be that orders received in the aforementioned example are so small as to be overlooked in an unfilled tonnage report. Nevertheless, the railroad has received cash for the carrying of bricks and ore, while the increased activity is almost instantly reflected in car loadings and in railroad earnings. If this line of reasoning is sound, then it is logical to say that railroad stocks should move with industrials, if not before them. Purchases of raw products must be delivered to factories by means of transportation, which still means the railroads to a very considerable extent, despite the increasing competition which these carriers are experiencing."

This book is more particularly for traders who are interested in grain. However, the Science of Interpretation of Market Graphs, or laws of price as outlined, are applicable to stock trading with very few, if any, modifications.

There is a difference in speculating in stocks and in grain. Apparently grain and stocks should be closely related but any close observer knows that stocks or grain cannot be depended upon to lead or

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follow the other in action. In fact, the same thing that affects grain prices in one way, often affects stock prices in exactly the opposite way; witness that in 1914 at the start of the great World War, grain prices boomed, starting in an unprecedented bull market, while it was found necessary to close the great Stock Exchange of New York for a long period, on account of the terrific pressure that was brought to bear on stocks.

There are many ways in which a speculator in grain helps in handling the products of the soil. In buying a contract for future delivery in grain, he not only helps advance the price, but he takes the risk for the manufacturer and the processor of the products of the soil, which the manufacturer or the processor cannot assume in the conduct of a strictly merchandising business. In other words, he takes the hedge (*) of the manufacturer or processor of the soil products, so that the manufacturer or processor can conduct his business in a safe and conservative manner. Also, the speculator in grain is an economic necessity when he assumes the risk for the consumer by selling short, that is, when not owning or at the time possessing it, executing an amply secured contract to deliver grain at a future fixed date and price to the baker, the grain products manufacturer, the farmer, livestock feeder, the home provider and thus providing a market for the farmer's grain when there is no consumer in the market that needs it at the time the farmer desires to sell. He assumes a contract to deliver, at a future date, the grain at the price agreed upon at the time the contract is made; through the necessity of eventually buying the grain to fill his short sale contract he not only creates an absolute demand for future

* Later in this volume there is a chapter on hedging which covers this point in detail.

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deliveries of grain offered in the open market, he also protects the baker, grain products manufacturer, etc., so that they may conduct their business on a strictly merchandising basis. The speculator buying grain on margin is a benefit to the producer. The speculator selling grain on a margin is a benefit to the consumer. If unhampered by governmental interference, the law of averages will balance the scales so that the producer and the consumer will be on a parity.

When a speculator buys a future grain contract, he does not assume the risk and hazards of management, which he always assumes when he purchases and owns common stocks. Therefore, while many fortunes have been made and many lost in stock speculation, there is a different objective in and an entirely different economic value between stock speculation and grain speculation.

When an investor purchases stock outright, pays for it and takes possession of the stock, he becomes a partner in the company in which he becomes a stockholder, and, therefore, is joining with others to help serve the consumer and provide employment for labor, with the hope that the company in which he has invested will, by its service, earn a wage for his share of its capital. When a speculator buys a stock on margin with the hope that the price of that stock will advance, is he performing a service to the public? Is he not assuming a risk which is of no benefit to any person or persons, but rather is an endeavor to obtain a usurious interest or return upon the money invested in his margin? If his buying a certain stock on margin helps advance the price of that stock, it has been the author's opinion that the advance thus created is of no real economic value, while, on the other hand, in buying grain on margin, he is creating a demand to advance

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the price of the product of the soil, which is absolutely the basis of all prosperity.

There are always two sides to every question, and our opinion may be biased. Many others possibly better qualified think differently than we do. We again quote from "The Dow Theory" (Robert Rhea) Chapter XVIII, Page 98, in regard to stock speculation.

"Speculation is both an art and a science. Its morality is frequently questioned, but regardless of whether it is right or wrong, it is vitally necessary to the business progress of any civilized nation. Without speculation our transcontinental railroads would never have been built, nor would we today have electricity, telephones, radios or airplanes. Most people have unpleasant memories of losses incurred through the purchase of stocks in radio and airplane manufacturing concerns, but every subscription to the stock of a company which later fell by the wayside was, directly or indirectly, a contribution to the progress of that industry."

"Speculation, even of the rampant variety, has its uses, because when prices are being whirled upward at a startling rate, the promotion of capital for new business ventures is easy. From capital so acquired, many enduring businesses have been developed."

The development of our great western states was largely the result of such speculation. Hamilton thought speculation and good business were blood brothers, as is indicated by the following extract: 'The speculation in stocks itself creates exactly the confidence which stimulates an expansion of general business. This is really only another way of saying that the stock market is a barometer, acting not upon the news of the day, but upon what the combined intelligence of the business world can anticipate. The prediction of better general business in

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sight is positive and trustworthy.' This is very logical and 'undoubtedly true. Therefore, it would seem that the grain speculator, by helping to carry the risk in marketing the farm products, assists in making prosperity, while the stock speculator is the maker of the barometer of the trend of business.

However, if a trader desires to speculate in stocks on a margin or by outright purchase, he can conduct his operations on the basis of graphs of the market prices of stocks, exactly in the same way as speculating in grain on basis of graphs of the price of grain or other commodities. While this book more particularly describes and instructs how to make graphs and shows their application to grain speculation, the instructions given can be applied to stock prices and stock speculation in exactly the same manner.

Speculation a Profession

While, after all, grain speculation and stock speculation are related, they are two different branches of the same profession, and we think speculation is a profession more than anything else. While the Science of Interpretation of Market Graphs is not infallible, it can be applied to speculation with greater success than any other method.

To some, a graph of market movements means nothing more than an endless number of lines running hither and yonder like the skyline of a city or the peaks and valleys of a mountain range, possibly of value only as a quick reference to past performance of what the market has done. If a graph is worth no more than this, it is well worth the small labor compared to the laborious effort of digging out the same facts from long lines and tables of figures. However, many a rough stone or fragment of rock has been cast aside by the careless, to be picked up la-

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ter by the student and searcher for truth, and found of precious value.

The student - the thinker - always sees possibilities in everything and always follows along straight lines of search until he proves to himself conclusively that his premise is false and without merit or foundation, or else it evolves into something worthwhile. In the latter case, it invariably means tireless research and study, trial and error, before satisfactory results are obtained. The trail is a long one, exceedingly discouraging at times, but as each step is accomplished, always intensely interesting. With the idea ingrained in our very nature that no man knows what the day or the morrow will bring forth, it seems impossible that anyone can even approximately forecast what the grain or stock market will do in the near or deferred future. Yet, after all, the desire to forecast the future action of markets of all kinds is uppermost in the minds of the vast majority of the human beings interested directly or remotely in speculation.

A comparatively few years ago it was thought that anyone who believed the time would ever come when the weather could be correctly forecast for any length of time in the future, was insane but meteorology has developed until the forecasts of the United States Weather Bureau are accepted and depended upon as a matter of course. What is more important, the forecasts are correct a large majority of the time.

All sciences are based upon the cause and effect. If the cause is known, the effect can be predicted with a certain amount of assurance. With this theory, which the author dares to call an axiom, in mind, when the cause of market fluctuations is known to be the psychology of the market, and a record is available of past action or fluctuations, why is it

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not possible to predict the fluctuations or actions for the future, with equal accuracy of weather predictions?

From a piece of ruled paper showing numerous apparently promiscuous markings, the graph of market action was born, and from the study of this graph what the author has chosen to name "The Science of Interpretation of Market Graphs" was evolved. Other accepted and reliable sciences were born with less material foundation.

It is obvious that to make the greatest success that is, profits, a student of graphs in the Science of Interpretation of Market Graphs must become very expert; he must become imbued with the theory, so that reading the graphs and recognizing what they show will become almost automatic and his decisions final. In a word, he must become saturated with the knowledge of reading graphs of the market, so that the formations and their portent will be like an open book of plain print. This requires not only time, but earnest study.

Even the novice will make some headway, but naturally, will not make as great a success in dollars and cents as one who has studied and experimented for a number of years, just as success comes in the medical profession only to those who have studied and practiced for years.

The greatest value in keeping graphs, studying them, using the information they give as a basis of speculating, is that there is a reason behind all market operations. The Science of Interpretation of Market Graphs is based upon a study of averages, recurrences and the important fact that the market does certain things, in the large majority of times, when certain formations are made in the graphs. As the student proceeds with the study of graphs and checks back over previous records, he will find that

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this is true. While the market does not always perform exactly as it has done before on account of an unexpected occurrence of a political or financial nature, as a rule these unexpected incidents only tend to change temporarily the market trend as indicated. For all practical purposes, the market sooner or later does what it should have done and has done before.

The question has often been asked the writer why, if the Science of the Interpretation of Market Graphs is so good and it should come to pass that everybody would become able to trade with graphs successfully, would this mass trading not control the market and prevent fluctuations? This is really a sensible question, because it is not only plausible but certain that if everyone traded exactly by the same rule or theory, there would be no fluctuations.

However, as referred, in another place in this chapter to the similarity between the study of the Science of Price and its operations compared to study of the Science of Medicine, again attention is called to the fact that, while the Science of Medicine is taught practically the same in numerous schools, all doctors, graduates of a medical school, treat every case to a certain extent, or in detail, differently, because the symptoms in each case are read and weighed differently. While even so, the result can be the same and a cure effected. It is just the same with the Science of the Interpretation of Market Graphs. Every student and speculator will read the indications, especially in minor details, differently from others and one will make more of a success than the other, but both may make a success in fact.

The Science of the Interpretation of Market Graphs is still in its infancy, compared to what it will eventually develop. It is not an exact science-

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no science is for that matter - but it has advanced far since its inception and far enough to be of great and intrinsic value to the student speculator. The chapters following describe the method of keeping a record of market prices and the application of the Science of the Interpretation of Market Graphs for speculation according to its development at this time and the conception of the author.

Before starting to describe the details and fundamentals of the application of the Science of the Interpretation of Market Graphs, the author wishes to impress emphatically the following facts: A speculator does not operate in the market for any length of time without having learned that an understanding of price trends is really necessary in successful speculation in commodities or stocks and, beyond doubt, he will be benefited by understanding the Science of the Interpretation of Market Graphs, which is outlined and promulgates in this book.

Experienced traders learn, sometimes to their sorrow, that there is no sure thing or "get rich quick" system of beating the market, and can be materially helped by the use of the Science of the Interpretation of Market Graphs, but will not expect too much of it. Such speculators, having learned that successful speculation is a business in itself and that, as with success in other lines, it depends upon hard work and straight thinking, will welcome the Science of the Interpretation of Market Graphs as a science worthy of study and one that will pay good returns on the time invested.

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CHAPTER II

HOW TO MAKE SIMPLE GRAPHS

In making graphs or "pictorial writing" of market movements, it is needless to state that the record must be complete and accurate, especially in the first simple graph that is made of the daily movements showing the correct high and low and opening and closing. This is necessary because the variance of $1/8\phi$ in grain and $1/8$ point in stocks might change an important calculation.

In addition, after the daily graph, upon which all other graphs are built, is made, a slight variation in reverse might lead to an erroneous result. The author does not want to be too insistent upon these slight variations that might occur from inaccurate daily graphs, but if the Science of the Interpretation of Market Graphs means anything, the foundation of it, the daily graph, must be accurate, and it is well that the student understand this at the start.

Geometrical Graph Paper

In starting to make graphs, of course the first thing that is needed is graph paper or paper ruled for the making of graphs. There are many places where graph materials are sold and may be obtained. The main thing is to have paper that is ruled in such a way that the details of the daily market may be shown clearly and correctly. The drawings of the illustrations in this book will give you an idea of what kind of paper you need. If necessary you can use common, ordinary ruled paper and make your own graph paper, but such paper is so easily obtained and is so cheap that it is not worth while to rule

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paper suited to your needs, excepting when you may need a specially ruled paper that cannot be purchased.

Graph paper for making graphs of the daily market should be ruled in small squared such as shown in the illustrations, with heavy horizontal lines to designate the even price and cross lines between spaces in order to show clearly the eighth and quarter cents of the price. The cross lines designating the fractions of the cent between the heavy lines should be transversed by vertical lines and the distance of these lines apart should denote lapse of equal periods of time. The spacing between the horizontal price point lines and the vertical time lines must be spaced with geometrical precision. The reason for this will be apparent later.

Ratio Graph Paper

In graphing action of stocks, most advanced students use a ratio scale instead of a plain or arithmetic ruling.

A ratio scale is semi-logarithmic and Robert Rhea, in his book, "The Dow Theory", says that to keep records of stock movements on plain or arithmetic paper is "a method as obsolete as an automobile without a starter." Robert Rhea conducts a forecasting service on stocks at Colorado Springs, Colorado, in which he comments upon The Dow Theory averages. He states in one of his recent circulars in regard to ratio paper, in part, as follows:

"Ratio paper is, in effect, an automatic percentage device. Those dealing in stocks profit (or loss) in proportion to the percentage advance (or decline) in their holdings. Many operators keep graphic charts of the daily price changes because such a record is more easily read than tabulated figures. Some yet keep their records on plain or

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arithmetic paper - a method as obsolete as an automobile without a starter.

"Those who judge the trend of the market by the averages will recall the amazing advances during July, August and September, 1932, but even now many students do not realize the extent by which the rails bettered the industrials on that movement. Let us consider the figures:

	<u>July Low</u>	<u>Sept. High</u>	<u>Points Ad.</u>	<u>Pct. Adv.</u>
Industrials	41.22	79.93	38.71	93.9
Rails	13.23	39.27	26.04	196.8

"Suppose this movement had been plotted on arithmetic paper. The industrials would have visually appeared to have bettered the rails because the former advanced 12.67 points more than the latter. However, an investor, placing \$100,000 in the rail averages July 8th would have realized a profit at the September peak of \$196,000 as against only \$93,900 gain had the same investment been made in the industrials. The ratio charts properly reflect the relative percentage of appreciation, but plain ruled charts would give the impression that the investor in industrials had the greater advantage. The resulting picture is a true percentage presentation of the movement."

Ratio paper may be obtained in heavy paper and thin paper. The advantage of a stock being plotted on thin paper is that it may be placed on top of any other graph of stocks and the relative advance or decline may be determined at a glance, as also the relative movement. Ratio paper may be purchased at most any place where graph paper is sold, the same as ordinary arithmetic paper.

The Four Essentials in Graph Making

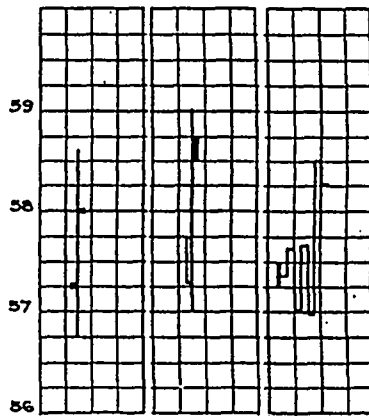
Just a few moments of your time each day will be required to make a simple graph of the daily

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movements of the market. There are four essentials in the market which encompass completely and conclusively the action for that day. They are the high and low prices showing the range of the price movement for the day, the opening price and the closing price, the latter the final settlement price of the day. We give herewith an illustration which shows the high and low prices and the opening and closing prices of the market. This is a vertical line, the top of which ends on the cross or horizontal line, indicating per the scale at the left, the high price of the range, and the bottom of which rests on the cross line, showing the low price range of the market, a dot on the left of the vertical line, showing the opening price, and a dot on the right of the vertical line, showing the closing price (see Figure 2).

Note if the opening or closing is a "split" price or shows a "range" in the prices, which frequently occurs as transactions in different parts of the pit may differ at the

moment of opening or closing from 1/8¢ or more. In a "wild" opening there are times when the opening prices will vary a cent and in some cases much more. In such cases the opening is recorded by making two dots on the left side of the range line and connecting them by a line parallel with



the range line (see Figure 2A). The closings quite frequently vary in the same way, but usually the variation is not so great. Such a closing is also illustrated in Figure 2A. This method is used when recording the daily movement after close of the market.

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The second illustration (Figure 2B) shows all the reverses and action of the market during the day and can be recorded in this manner, provided the trader has the time or facilities to copy from continuous quotations posted on a blackboard or tape showing all the fluctuations during the session.

Complete Daily Movements

For a complete and perfect graph, the method shown in Figure 2B is to be preferred, as it shows the exact action during the day and makes formations that will guide the scalper or daily trader in his actions during the session of the market. For a trader who is speculating in a small way as a side issue to his regular business, the first illustrated method is practically all that is needed for his information, but from the four essentials, high, low, opening and closing all sorts of graphs can be made at once, or at any time afterward that is desired. In fact, if you desire to do so, you can go into graph making "up to your ears", making graphs of all details of the market in every way, such as graph of closings, the daily average of the range, of the reverses, of the change in trends, resistance lines and a combination of all the different futures, etc.

Also, graphs (or charts) can be made of production of the different grains for each of the different producing countries, so that the totals or volume can be combined showing the total world production for comparison month by month or year by year, etc. In fact, a graph or chart of the annual world production of wheat especially, should be made. For illustration see Figure 1, chart of Net Exports of Wheat and Flour in Chapter I. All of these graphs will be illustrated later.

The Daily Graph, Day by Day, shows the entire movement in detail of the market (Figure 3). It

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price, and a dot on the right indicating the closing price. For instance, note on Wednesday, the fourth day of the month, the high price of the range was $58\frac{1}{2}\text{¢}$; the low price of the range on that day was $57\frac{1}{4}\text{¢}$; the opening was $57\text{--}7/8\text{¢}$; the closing price was $58\frac{1}{4}\text{¢}$. Thus, at a glance can be seen, the entire extent of the action of the market for that day.

While the opening price is considered the least important of any of the details given, it undoubtedly reflects the change in sentiment, also volume of business in cash grain done since previous close. The closing price is the most important, because the closing price is really the settling or evening up price of the day, as it is the last price made during the session of that day.

The Movement of Two Days or More Angle or Block Graph

To get a better perspective of the market movements from the Daily Graph, an Angle Graph (Figure 4) or a Block Graph (Figure 5) can be made, showing the extent of each movement in each direction, and the reverses as illustrated. Both the Angle and Block Graphs are called the "Movement of Two Days or More."

In plotting the Movement of Two Days or More Angle or Block Graphs, so some of the most prominent and successful students record the movement of any reverses of at least $1\frac{1}{2}\text{¢}$ in wheat, 1¢ in corn and $\frac{1}{2}\text{¢}$ in oats, whether or not the reverse is made in one day or two days or more. But always plot the movement of two days or more, regardless of the extent, provided it either sells higher range and not lower, or sells lower range and not higher than the previous day's range.

To illustrate how to follow the Daily Graph in making the Movement of Two Days or More, refer to

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Figure 3B, which is a part of an actual market graph of wheat. Apparently the reverses are very plain and

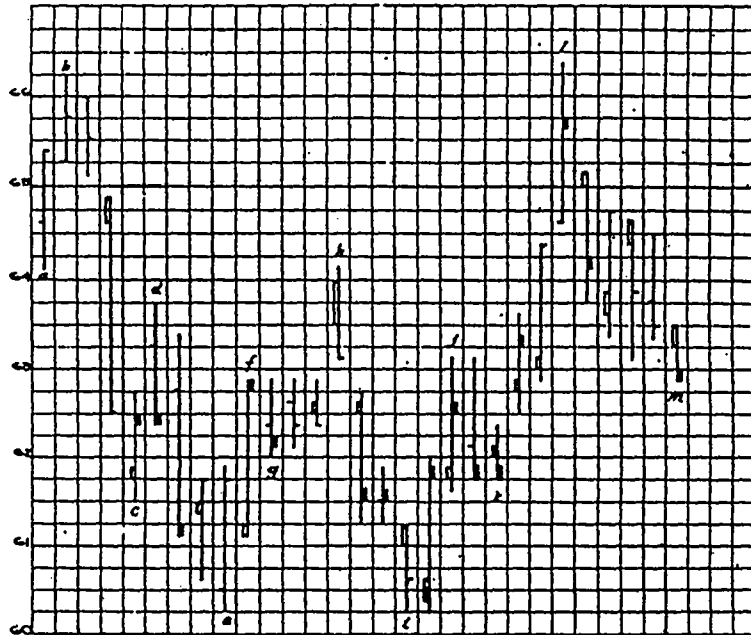


Figure 3B

simple to follow in making an Angle Graph. However, starting at a ($64\frac{1}{8}\phi$) draw the angle to b ($66\frac{1}{8}\phi$), then on the next day, after the market reached b it did not decline $1\frac{1}{8}\phi$, but as it sold lower than the previous day, the line should be plotted from $66\frac{1}{8}\phi$ to $65\frac{1}{8}\phi$, showing the reverse at $66\frac{1}{8}\phi$.

The next two days, continuing the line straight on down with three days' space latterly to c ($61\frac{1}{8}\phi$), then to d and down to e in the same method, is very simple. Also in the reverse up from e to f. The angle is not reversed from f ($62\frac{7}{8}\phi$) to g (62ϕ) because the market did not sell lower than $61\frac{1}{8}\phi$, the low of the previous day, or reverse $1\frac{1}{8}\phi$. The next two days also did not sell above $62\frac{7}{8}\phi$ or below either of the previous days' lows, therefore,

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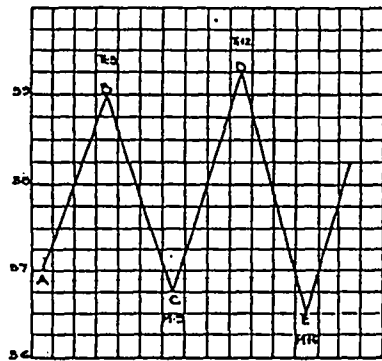


Figure 4

the angle line is still not changed unless the market sells either above $62-7/8$ or below $62-3/8$, the high and low of the last day. The next day it advanced to $64-1/8$ at h, therefore, continue the angle line from g direct to h ($64-1/8$), making a lateral time movement of ten days between the reverse at c and the high at h. Then the angle changes down from h to i, with four days' lateral movement.

Now turn the reverse from i ($60\frac{1}{4}$) to j ($63-1/8\frac{1}{4}$) and then, although the market does not reverse down $1\frac{1}{4}\frac{1}{4}$ because the market closed at the low of the next day after reaching the high at j, and especially as it closed at the same level the next day, draw the curve or angle down to k ($61\frac{1}{4}$), showing a lapse of two days between the high at j and the low at k. It is easy to follow the reverse from k up to l and then on down to m.

The reader will note that this is a copy of the December Wheat Future of 1932 from the opening designated a to l, and will find this action outlined exactly in the Movement of Two Days or More Graph of that future, which is illustrated on another page (Figure 8).

Another illustration of the Angle Graph is given in Figure 4, which is the Angle Graph of the Daily Graph shown in Figure 3. It must be noted that each reverse in the Angle Graph shows just the extent and the time between each reverse of the movements of the Daily Graph, not recording the opening and closing of each day. This graph is the most popular graph of market record, as it shows formations

the angle line is still not changed unless the market sells either above $62-7/8$ or below $62-3/8$, the high and low of the last day. The next day it advanced to $64-1/8$ at h, therefore, continue the angle line from g direct to h ($64-1/8$), making a lateral time movement of ten days between the reverse at c and the high at h. Then the angle changes down from h to i, with four days' lateral movement.

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quickly, clearly and simply. However, for the sake of space, the writer also used the Block (Movement of Two Days or More Graph which is shown in Figure 5. It will be noted that the lines in the Block

Graph are vertical and horizontal and that the Block Graph takes much less space than the Angle Graph. A comparison of the two will show you that the Figures A, B, C, D and E, indicate the prices and movements exactly the same as the Angle Graph (Figure 4). The exception is that the vertical lines do not show the spaces in the graph

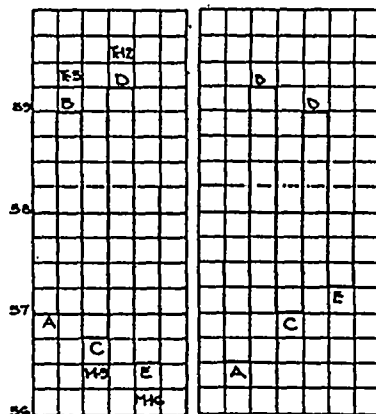


Figure 5 Figure 6

denoting the number of days between the movements and reverses, and in using a Block Graph these movements will have to be computed from dates above and below the tops and bottoms of each reverse as shown in the illustration (Figure 5).

While the Block Graph takes less space and time to plot, and also, possibly on account of its compactness, is easier to read, it will be learned as progress is made in the study of applying graphs of the market to speculation, that the Angle Graph of Movement of Two Days or More is more important on account of its indicating resistance lines (see Figure 21), which cannot be plotted from the Block Graph. Resistance lines will be fully described later.

Closing Graph

Necessary for the proper analysis of the market a very important one is the Closing Graph, which is

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very easy to make. The formation of the Closing Graph always corroborates the graph of the Movement of Two Days or More Angle and Block Graphs and usually indicates an important formation before it is apparent in the Angle or Block Daily Graph. Also, it quite frequently conflicts with and anticipates a change of the minor trend, before it is apparent in the Movement of Two Days or More Graph or Daily Range Graph.

Some students who have progressed far in the study of graphs and who have years of experience, use the Closing Graph as the main indicator of market movements, in preference to the Range Graph. As previously stated, the closing of a market is the most important price of the day, because it is, in the last analysis, the settling price of the day and this is a very important factor in the analysis.

Note Figure 7 which shows the graph of the closings in the daily movement of Figure 3. Also note

Figure 20, the complete closing graph of December Wheat 1932. The graph is simple, inasmuch as a dot is placed covering the range of the closing quotations or average of same, found on the right side of the plotted vertical range line where it intersects the proper price line in the graph, and a dot is made for the average of the closing in the

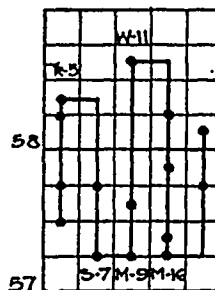


Figure 7

same way each day, connecting these dots with a light line. In Figure 7, the figures 5, 7, 11, etc. are the dates of the month, and the letters, Tr, S, W, etc., are the initials of the days of the week of the closings respectively, which give a cue to the dates of the closings in between. You will note that the formations thus made in Figure 7 are almost

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identical with the formations in the Movement of Two Days or More Graph shown in Figures 4 and 5.

Primary, Secondary, Minor Trends

There is always a trend in effect in the market and for the purpose of analysis there are three divisions - The Primary - The Secondary and the Minor trend.

THE PRIMARY trend is the general direction of the movement of the market and may last for a year or more until changed by the Secondary trend passing the starting point of the Primary trend.

THE SECONDARY trend is a movement in reverse to the Primary trend which is definite when the first previous high or low in the Minor trend moving opposite to the Primary trend has been passed.

THE MINOR trend is the daily movement and continues same direction when the movement passes the previous reverse in a movement of one day or more.

Refer to Figure 9, which shows the Minor trend graph in heavy straight lines. Superimposed dotted lines show the Primary trend. The curved lines indicate Secondary trends. The Minor trend graph is made from the Movement of Two Days or More Graph. When the market passes the low or high of the previous run, the Minor trend changes. For instance, in Figure 8, the Movement of Two Days or More Angle Graph shows the changes in the Minor trend, which is recorded in the graph, Figure 9. In Figure 8, when the market price sold from A1 to A, passing the opening at G4, the minor and primary trends were down. Technically from A to B was a secondary trend up, the primary trend continuing down unless A1 was passed on that movement. After reversing up to B, then selling down to C, passing A, the minor and primary trends continued down.

Therefore, in the minor trend graph, Figure 9,

Fig. II.6 (Figure 8)

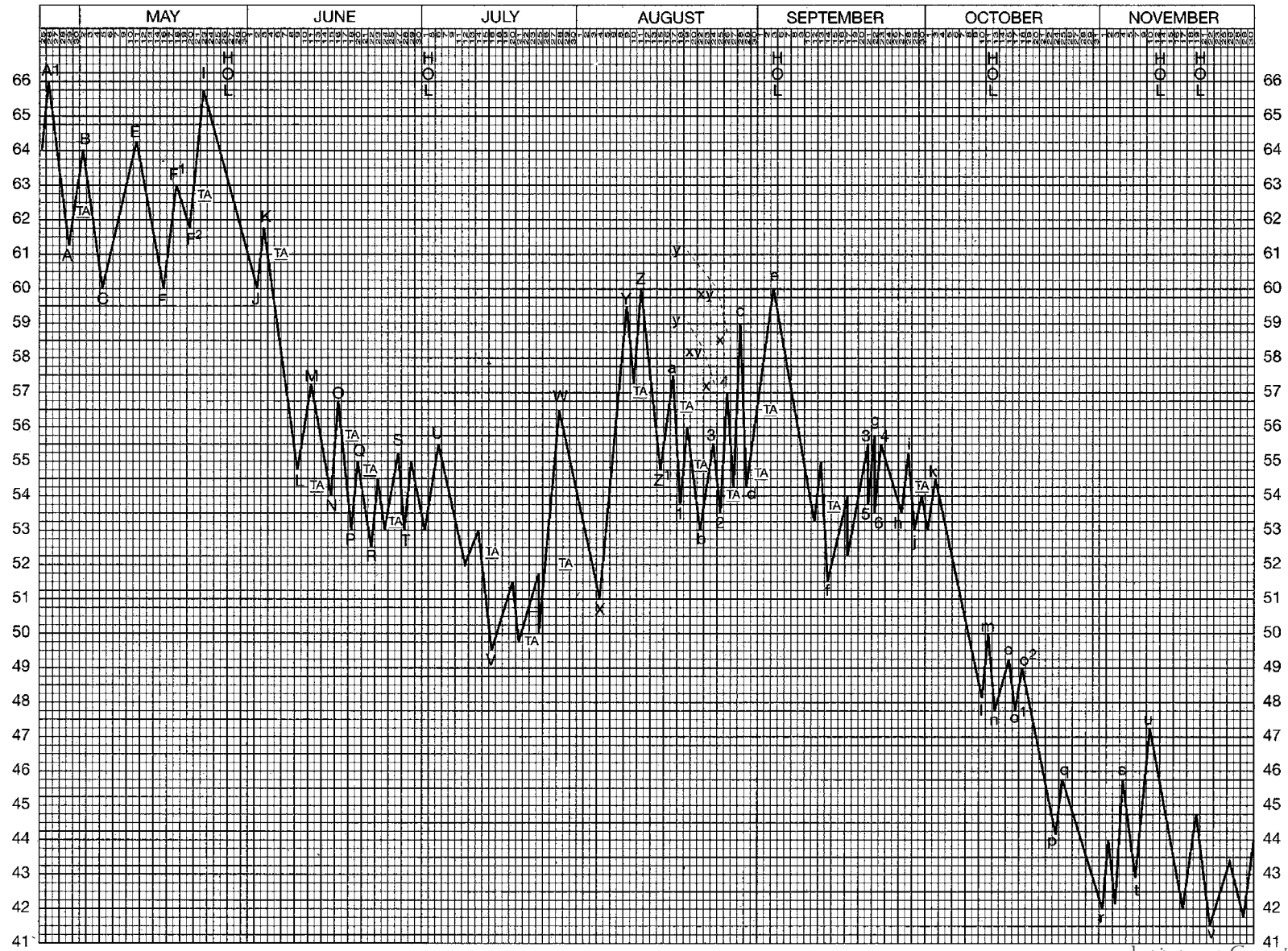
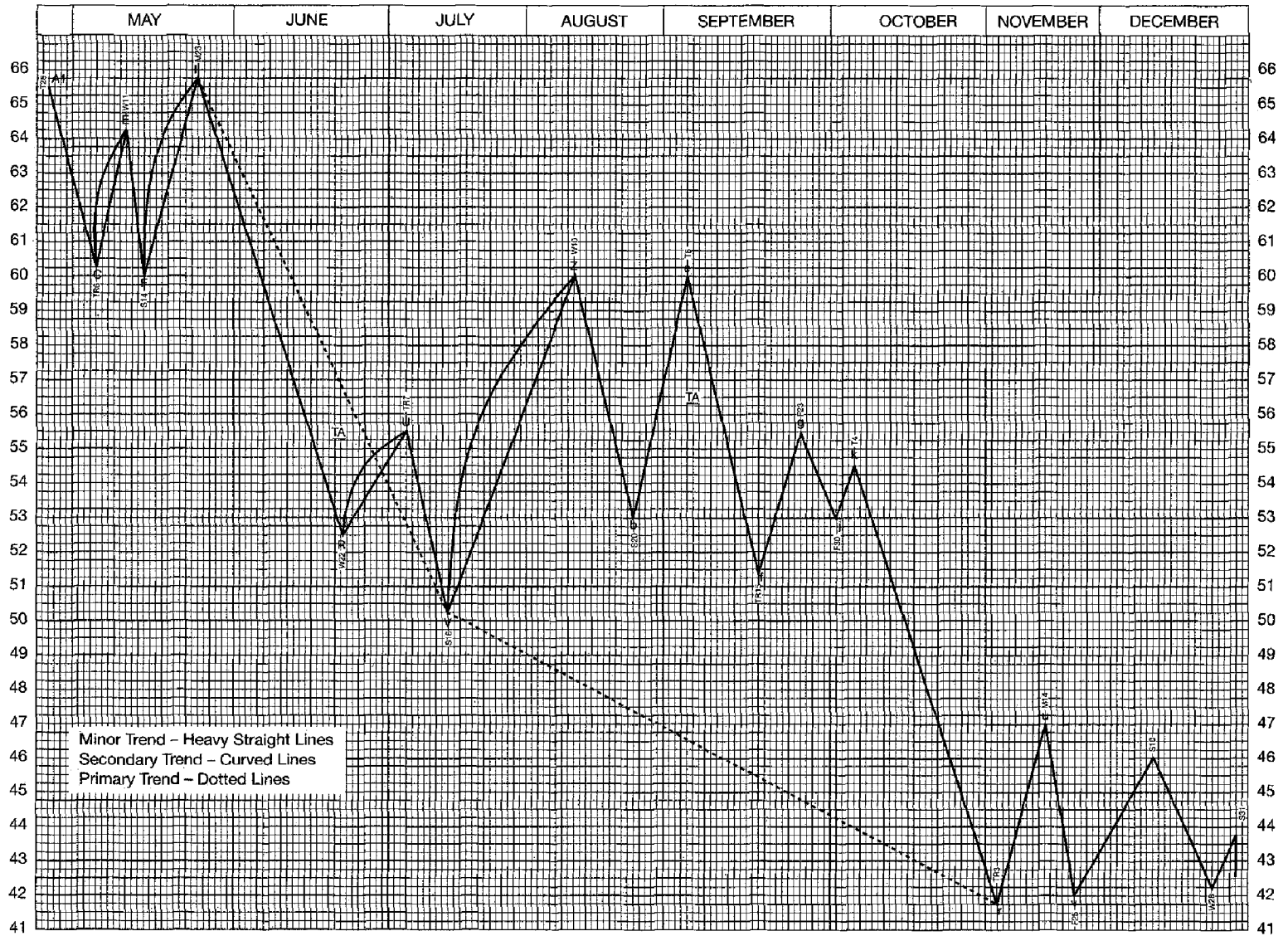


Fig. II.7 (Figure 9,



Trend Graph - December Wheat 1932

the first line from A1 is direct to C. When the market sold up from C to E, the minor trend turned up when it passed B (Figure 8), and the line is drawn from C to E in Figure 9, the minor trend graph, and the secondary trend is up. The minor trend also turned down at F when it passed C (Figure 8), and the line is drawn in the minor trend graph (Figure 9) from E to F, eliminating the secondary and continuing the primary trend down. Then again passing F1 in its upturn to I (Figure 8) the minor and secondary trends are up and the line is drawn direct from F to I in the minor trend graph (Figure 9). From I to R (Figure 8), although the market reversed several times on its downward course, it did not pass the previous high in any of the reverses, therefore, the trend continued down and the line in the minor trend graph (Figure 9) is drawn direct from I to R, again eliminating the secondary trend and continuing the primary trend down.

In the next several movements between R and U (Figure 8), the minor and secondary trends turned up from R to U, so in Figure 9, a line is drawn from R to U. Again the primary trend continued and the minor trend changed down from U to V (Figures 8 and 9). In the advance from V to Z, the market does not break the lows of any reverse, (see Figure 8) therefore, as price passes high at U secondary and minor trends are up between V and Z (Figure 9). The secondary trend remained up until in October when price sold below V (50¢). The primary trend was down during the life of the future (see dotted line in Figure 9). With this explanation, the student can follow all the trends in the graph made from the Movement of Two Days or More Graph, Figure 8 and 9 respectively, and will note that a straight line connects all highs and lows between which no reverse has passed a previous low or high. It will be noted that the

Graphs

triple average is figures in the trend graph and each triple average price is marked TA, to be used in the analysis. This is figured exactly the same as the triple average in the Movement of Two Days or More Graph, which is also noted with the same symbol in Figure 9. (The computation of triple averages is described in Chapter IV).