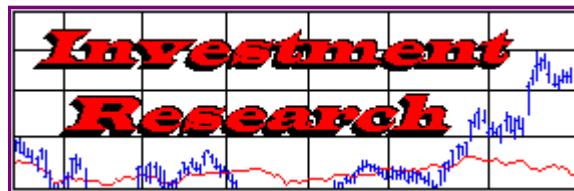


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Introducing the MIDAS Method of Technical Analysis (10) by Paul Levine

This is the tenth article in a series. Click here to go to the [first](#), [second](#), [third](#), [fourth](#), [fifth](#), [sixth](#), [seventh](#), [eighth](#), or [ninth](#) article.

Midterm Report:

We are now approximately at the "midterm" of what I view as a course here at Cybercollege, one in which you have enrolled by sticking with the articles to this point. Your midterm "exam" is simply to provide me with some feedback: what you like and dislike about the articles, any points you found unclear or particularly enlightening, and in general any comments which may assist me in making the remainder of the course as useful as possible to you. On a personal level, a brief biographical paragraph would also assist me in visualizing the faces on the other side of my modem... Thanks.

Submit your midterm to Paul Levine: [WinMidas website">winmidas@winmidas.com](mailto:winmidas@winmidas.com) or visit the [WinMidas website](#)

The tools have now been provided to analyze stock price behavior relative to the theoretical hierarchy of support/resistance (S/R) levels. How to use these tools to improve one's trading performance -the "engineering" aspect of MIDAS- is the focus of the present article.

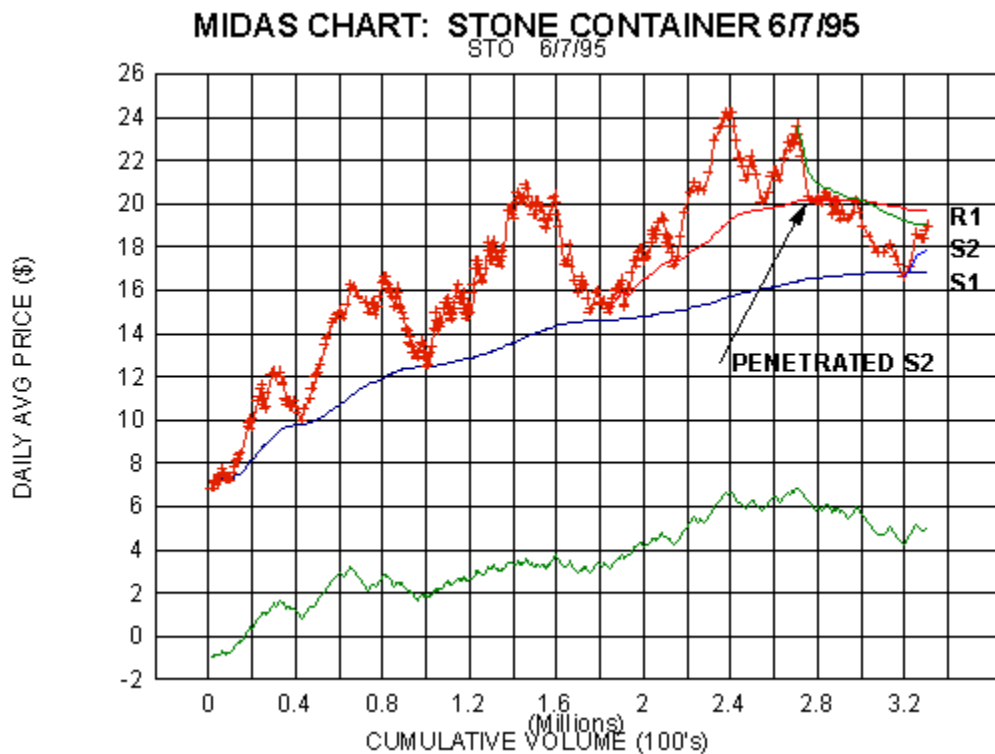
To paraphrase Hamlet, the basic question is "to bounce or not to bounce". Our theory predicts where a bounce (i.e. a trend reversal) should occur, and if it does occur, where such a bounce should carry to as a minimum objective. But, since the market is in the final analysis probabilistic rather than deterministic, our decision whether to trade an expected bounce - by buying at the theoretical support and selling at a theoretical resistance - will require some ancillary assessment of the likelihood that the support level will in fact hold.

In the familiar and apt analogy between the stock market and the motion of a cork floating on the sea, one associates the broad tidal motion with the influence of the overall market on a particular stock. Superimposed on the tide are individual waves which are analagous to the effect of the group (i.e. computers, cyclicals, golds, etc.) to which the stock belongs. Finally there is the microenvironment of ripples and wisps of wind which relate to the particular dynamics of the stock itself.

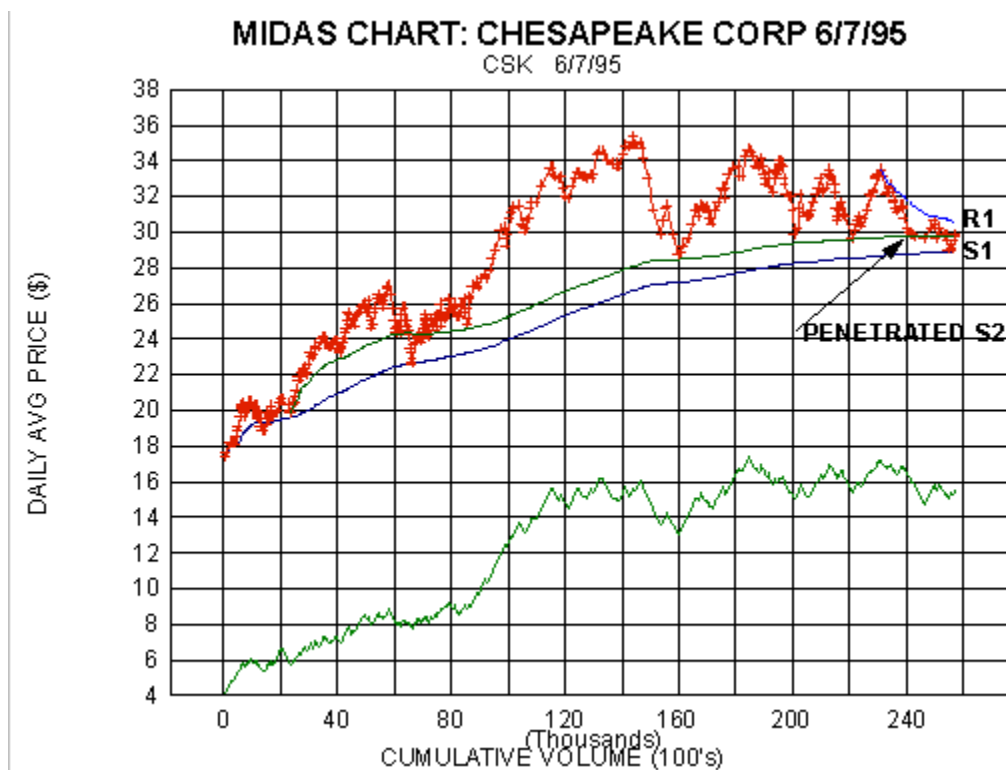
Relegating to a later article the important topic of the application of Midas methods to the overall market, we look to the other two factors for the clues we seek. Specifically, we can examine Midas charts for two or more stocks in the same group on the assumption that one of them will provide a leading indicator of the group's behavior. Also, for a single stock we can consider the Midas techniques in concert with other tools from conventional technical analysis, seeking independent confirmation that a tradable bounce may be at hand.

To pursue the group angle, we consider two paper product stocks: Chesapeake Corp. and Stone Container. The Midas chart for Stone Container updated to the time of this writing is shown in the first figure. The astute reader will recall that we visited STO before (in article #2), at a time roughly corresponding to the tip of the arrowhead in the figure. To recall our exact words: "...the expectation is that the secondary (i.e. S2) will hold and the price will resume its upward motion. If the

secondary fails to hold, the price would be expected to decline at least to the primary support level at about 17." In the event, the secondary did hold for some time and then ultimately failed after which support was found precisely at S1. The subsequent bounce has carried to the expected minimum objective, the resistance level R1, and at this moment is attempting to penetrate it.



Now look at the Midas chart for Chesapeake Corp. Now look at the Midas chart for Chesapeake Corp. As with STO, the S2 support was penetrated after holding for some time, and a bounce has started from the S1 level. It, however, has not yet carried as far as R1 and in this regard is lagging behind STO. If STO in fact is subsequently able to convincingly penetrate its R1, then this would give incentive to buy CSK since the implication is that the paper stocks have completed their correction and are about to start a new bull leg.



Turning now to the concept of synergistically combining Midas methods with other techniques of technical analysis, this gives us an opportunity to redeem the promise made at the end of the previous article to show how Midas can be integrated into existing commercially available charting software. Windows on Wall Street (tm), a product of Market Arts Inc., is one such package which automates the importation of daily updates or historical stock data and allows the user to produce charts incorporating a variety of standard tools of technical analysis. As with other similar products it also permits the introduction of user-defined curves (or "custom indicators") to be plotted on the same graph as the price data. Unfortunately, however, in common with all such packages (of which I'm aware) one is limited to plotting vs time rather than vs cumulative volume.

Nevertheless, it is quite simple to plot S/R levels using these packages. In the case of Windows on Wall Street, one merely defines the following "custom indicator":

$$\text{CUM}(.5*(H+L)*V*IF(\text{CUM}(1)>\text{DAYS},1,0)) / \text{CUM}(V*IF(\text{CUM}(1)>\text{DAYS},1,0))$$

where DAYS is a parameter equal to day (i.e. record) number at which the S/R level is to be launched. (Defining several such indicators, labelled S/R#1, S/R#2, etc, permits as many S/R curves to be simultaneously plotted as one wishes). A particularly useful feature is that since DAYS is an adjustable parameter, one can readily shift the launch point around by simply clicking on the S/R curve with the mouse, and then clicking on a parameter-change button.

More importantly, one can combine on one graph other indicators and technical aids together with the Midas S/R levels. The third figure gives an example of this for Western Digital (WDC). Here we have defined three windows, one for an MACD histogram, one for on-balance volume, and the main window for the price and other technical aids. In addition to three Midas S/R levels, we have included conventional trendlines (straight lines joining peaks and troughs), so-called Bollinger Bands (2 standard deviations above and below a moving average of price), and bullish (green) and bearish (red) flags derived from Japanese Candlestick pattern recognition software.



Focus particular attention on the March 1995 time frame. The price has consolidated down to the primary (S1) Midas support with a degree of porosity similar to the previous contact (in May-June 1994). When the three bullish candlestick signals appeared, this became a compelling buying opportunity (especially the third such signal at which time the price was simultaneously at both the trendline and the lower Bollinger band).

The key to profitable trading using Midas is to have a sufficiently large number of stocks under surveillance, so that when such "golden opportunities" come along - as they surely do from time to time - one can recognize them as such and concentrate enough buying power on one's position to take full advantage of the situation. This leads naturally to the question "when should I sell?". We'll discuss that in the next article.

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Paul Levine first became interested in technical analysis when he was a "runner" on Wall Street as a high school student. After graduating from MIT and gaining a PhD in theoretical physics from CalTech, he took a fresh look at the problem some thirty years ago and stumbled upon what has now evolved into the Midas method. Following retirement as Chief Scientist and a co-founder of Megatek Corporation in 1981, he developed further elaborations of the method and is now in his fourth year as a professional trader. He can be reached via e-mail at [WinMidas website](mailto:winmidas@winmidas.com)">winmidas@winmidas.com or visit the [WinMidas website](#).

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