

Chapter 23

THE CAMELBACK TECHNIQUE

At times, prices can be pretty wild. Sometimes we see large choppy Trading Ranges, abbreviated trends that fail to continue for more than a short duration. Lots of explosions and collapses make markets difficult to trade, even for the very best traders.

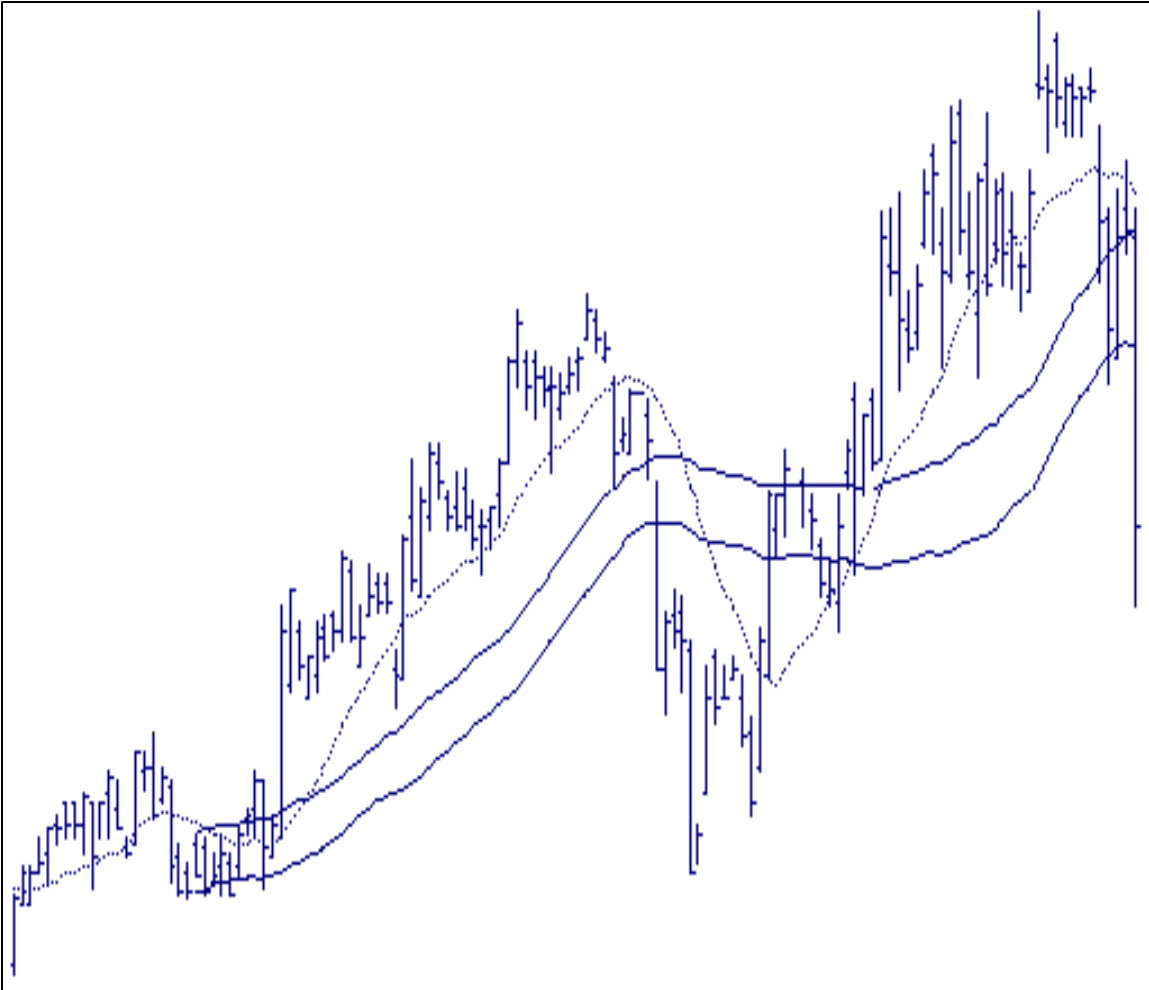
It seems that at times only the innovative and adaptive traders can consistently take money out of their trading.

Sometimes all that is needed is a simple set of tools. Let's look at just such a set of tools, that from a technical point of view are proving themselves successful in trading the kinds of charts we encounter from time to time. In the illustrations that follow, we will be using a fifteen bar exponential moving average of the close, along with a simple forty bar moving average of the highs and lows. With the forty bar simple moving average of the highs and lows we will attempt to create a channel.

When prices move beyond the bounds of the channel, we will attempt to trade pointy places. We will never attempt a trade when prices are within the channel. The exponential moving average will be a filter used to keep us from trading when the moving average is flat. So, even though prices are out of the channel, as long as the fifteen bar moving average is flat or relatively flat, we will not attempt to trade.

A trade will come when the moving average is trending and prices are out of the channel. If prices are above the channel, we will attempt trades only from the long side. If prices are below the channel, we will attempt trades only from the short side.

Let's look at a chart so that you can get the picture of how the Camelback technique works with any time interval. You can use the Camelback for intraday or longer term position trading. More details follow.



On the chart above, we see three moving averages. The most active (dotted line), is a 15 bar exponential moving average of the Close. It is used to filter out flat spots in the price action. When the 15 bar average is flat, we do not attempt to enter any trades.

The smoother moving average lines are: 1) a 40 bar simple moving average of the Highs, and 2) a 40 bar simple moving average of the lows. These two form a channel which serves to delineate the price bars in such a way that we know when it is alright to attempt to enter trades.

If prices are outside the channel, as long as the 15 bar average is not flat, we may attempt to enter trades, as will be explained in the material that follows.

The idea behind the Camelback technique is to keep us on the correct side of the market at all times. This is accomplished via the channel created by the forty bar simple moving average of the Highs and Lows.

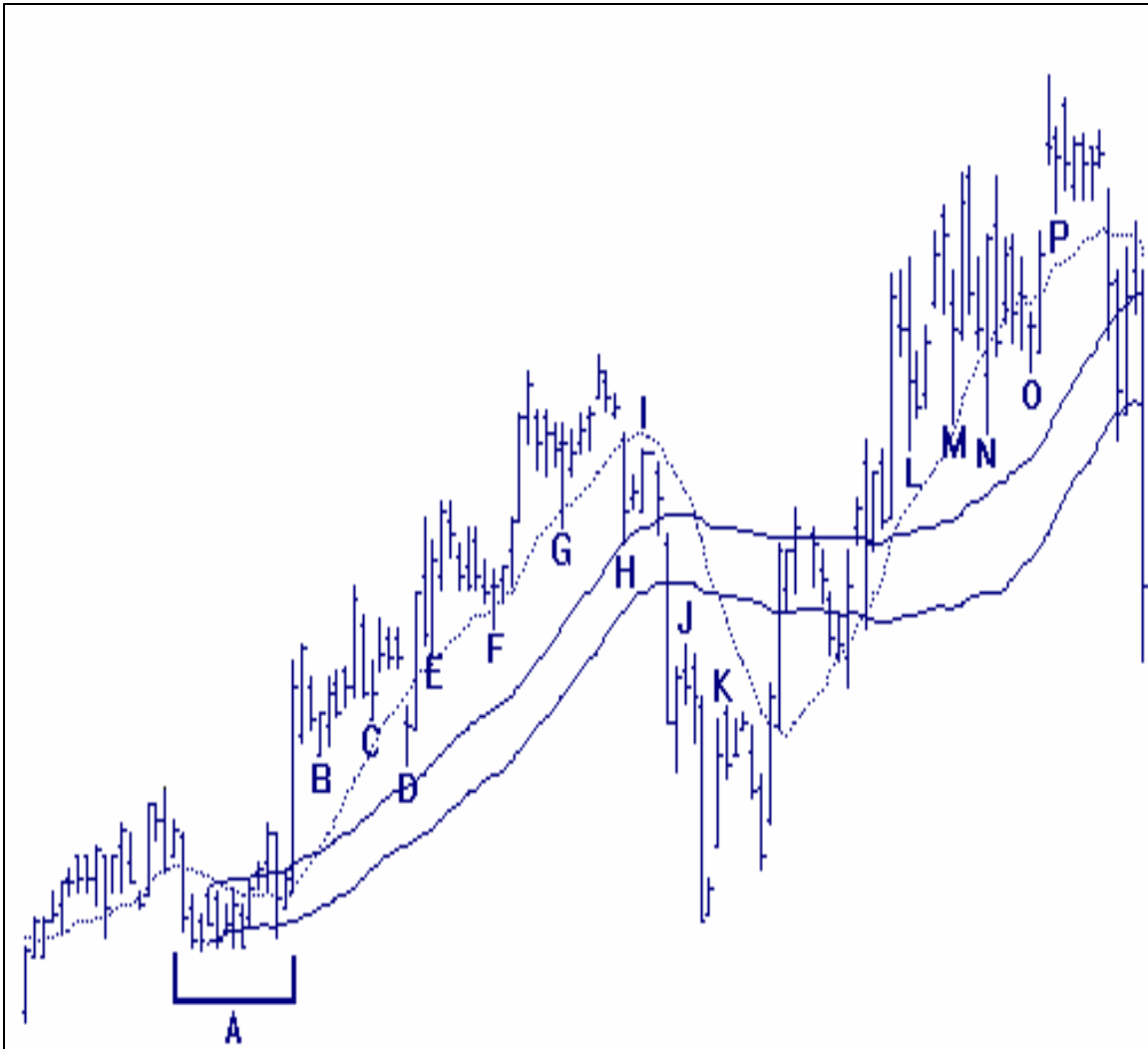
WHENEVER PRICES ARE IN THE CHANNEL WE DO NOT TRADE. WHENEVER PRICES ARE ABOVE THE CHANNEL, THE APPROPRIATE POSITION IS TO BE LONG. WHENEVER PRICES ARE BELOW THE CHANNEL, THE APPROPRIATE POSITION IS TO BE SHORT.

The only thing that will prevent us from attempting to get short below the channel or long above the channel is if the fifteen bar exponential moving average is flat or near flat. Our purpose for using the exponential moving average is to weight the more recent price action more prominently than the longer term averages for purposes of more quickly discovering when prices are flattening out.

With the Camelback technique, we are attempting a three filter method for being on the correct side of the price action. We are pursuing the age-old concept of trading with the longer term trend by entering on a short term high/low breakout signal when the intermediate term trend moves counter to the long term trend.

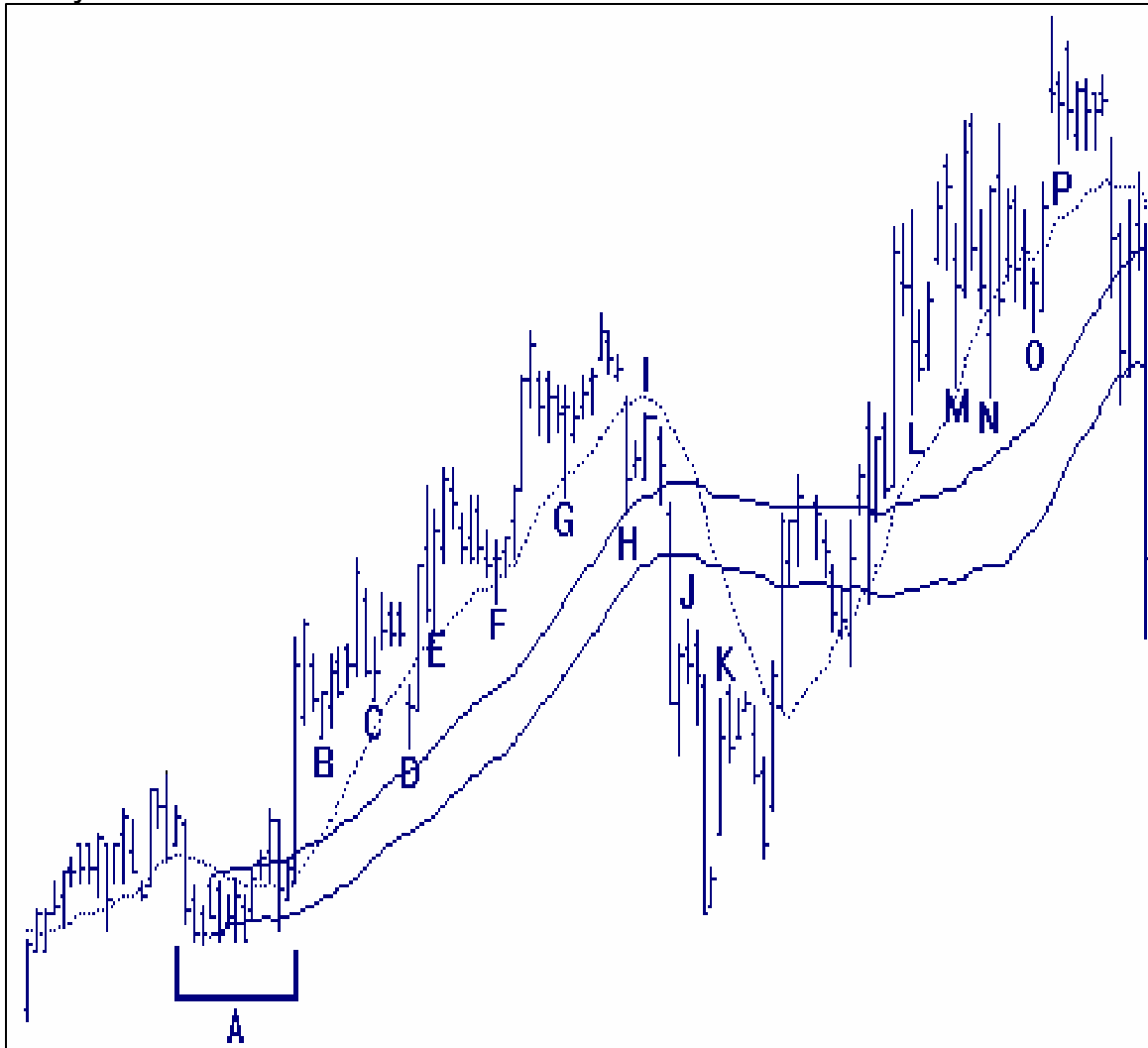
Let's look at a couple of charts to see how the concept works, and while we're at it, let's set some rules.

- When prices are above the 40 bar moving average of the Highs, we go long on a violation of the high of the bar making the local low.
- When prices are below the 40 bar moving average of the Lows, we sell short on a violation of the low of the bar making the local high.
- We do not enter on a gap opening violation of either the high or low.
- We do not enter a trade if the 15 bar moving average is flat or has turned away from the direction of the trade we want to take.



At 'A' prices are inside the channel. Price bars must be entirely out of the channel before we can use the Camelback. When prices are above the channel, we attempt to purchase a breakout of the high of the bar that makes the local low. 'B' is a local low. An entry 1 tick above 'B' would have enabled the covering of costs and possibly a small profit. A trailing stop beneath the low of each bar would have seen profits maximized 4 bars after 'B'. 'C' was the next local low. An entry 1 tick above the high of 'C' would have done little more than allow cost covering and a breakeven exit some time in the next two time intervals. The next local low was 'D'. Entry 1 tick above the high of 'D' would have resulted a profitable trade. Entry above the next local low, 'E', might have only covered costs and broken even. Entry

above local low 'F' would have given some nice profits, as would entry above local low 'G'.

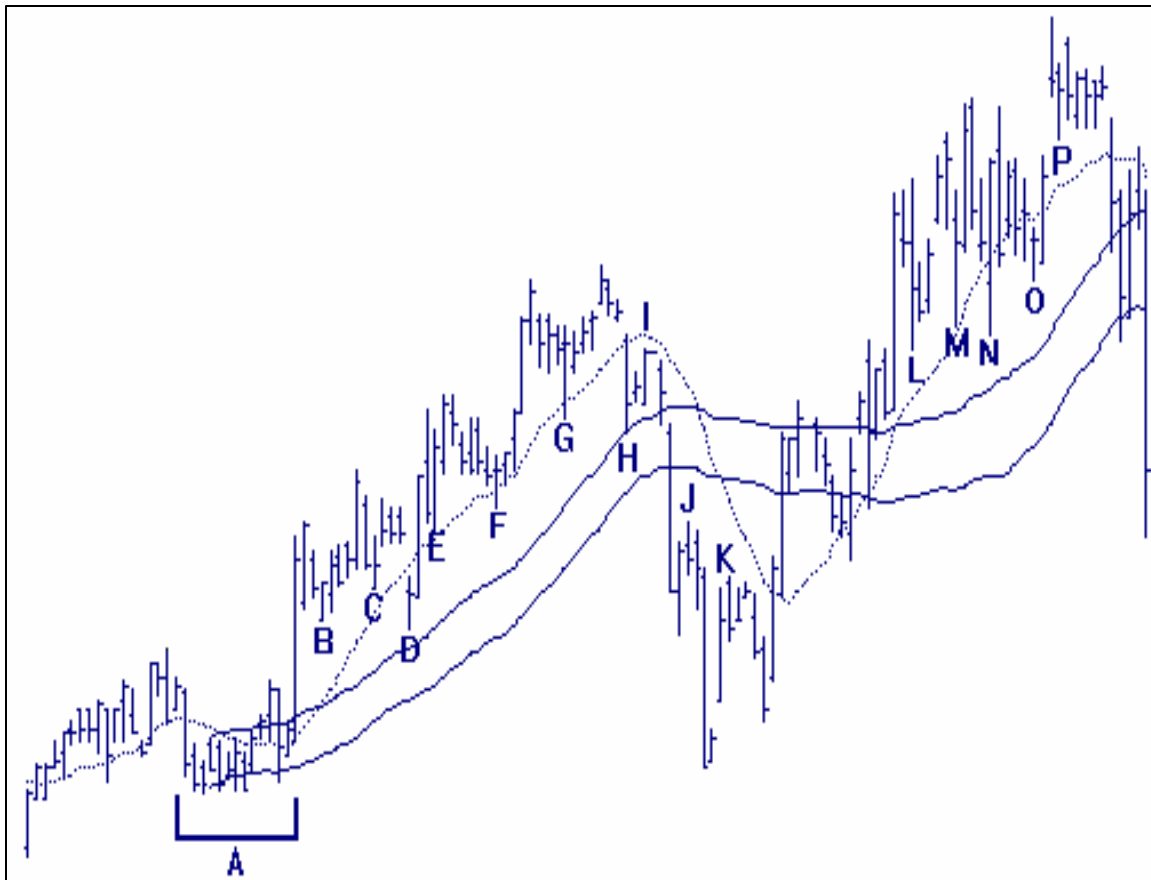


'H' was a local low whose high was never violated, so there could not have been an entry. At 'I', the exponential moving average is turning and is flat. In addition, there was no possible entry on a violation of 'I.'

Subsequently prices move to the other side of the channel. We are then looking to be short.

Once we are operating on price bars that are entirely out of the channel, we then try to sell a breakout (violation) of the low of the bar that makes the local high.

'J' is a local high. It is the top of a minor correction to the recent medium term downtrend. Shorting the breakout of the low of 'J' would have resulted in a profitable move. 'K' was a local high. Shorting a breakout of the low of 'K', when it happened 3 days later, also resulted in a profitable trade.

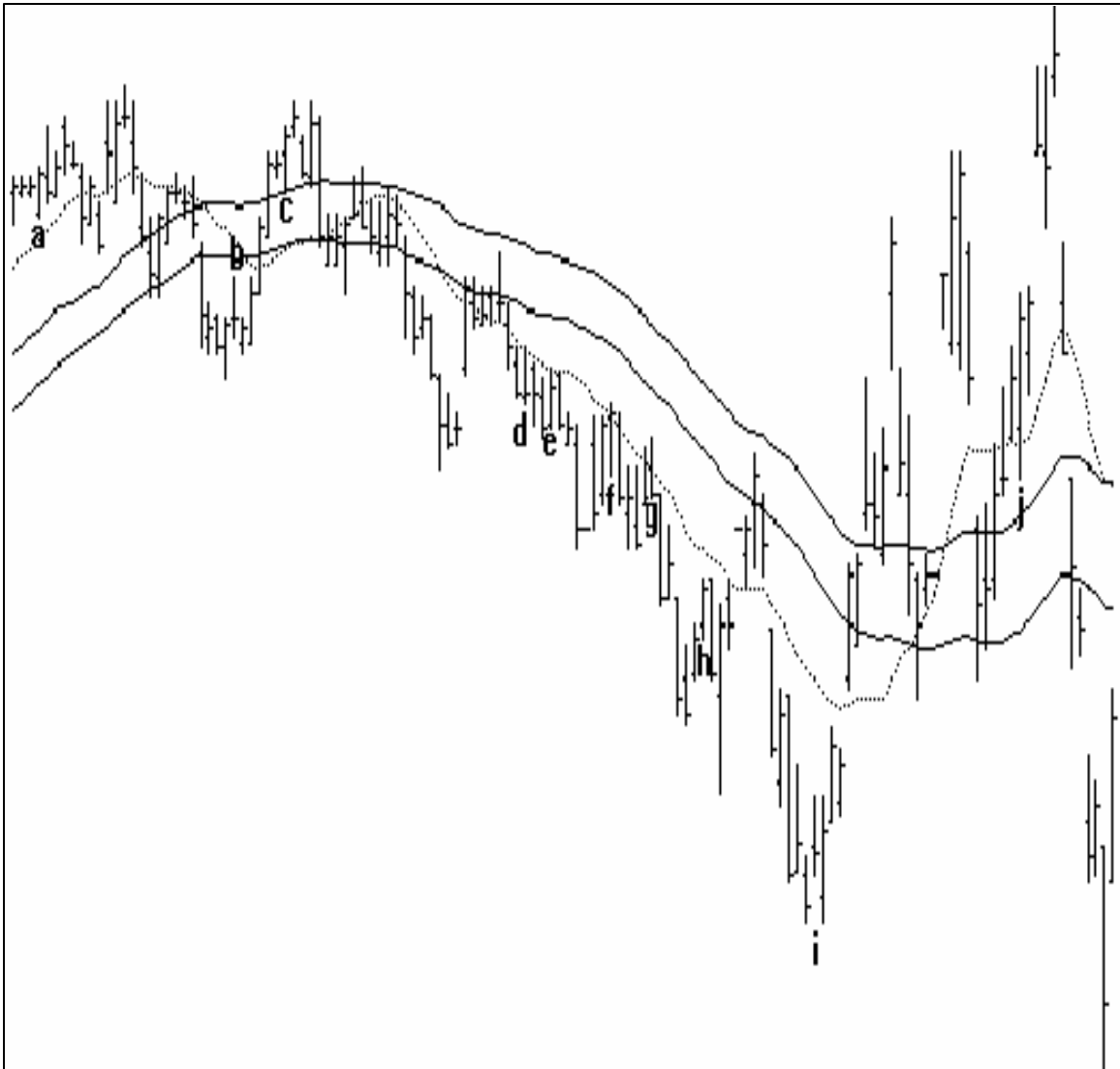


Prices subsequently moved back into and through the channel. 'L' is a local low. It took 3 bars to violate its high. When it happened, costs and possibly a small profit were recoverable. Entry based on a breakout of the high of 'M' easily made a profit.

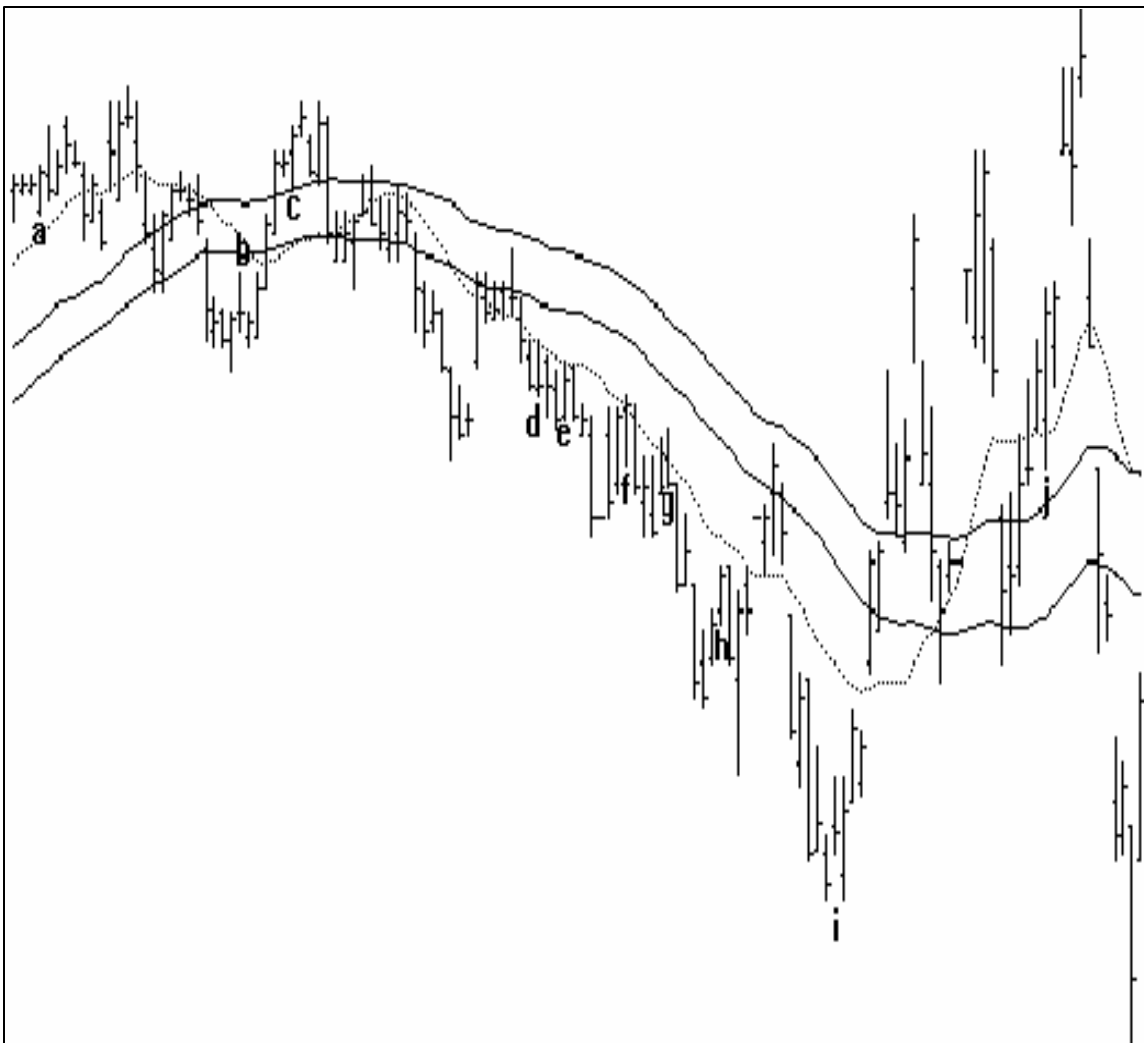
A breakout of the high of bar 'N' would not be taken, because of the gap opening. The same is true of a breakout of bar 'P'. A breakout of the high of 'O' would have resulted in a profit. What we are doing here may be termed scalping. Scalping the longer term chart using short term trading techniques is a great way to trade the kind of action we see on these charts.

Now let's look at another chart to help you lock in the idea of what we are trying to do. Please pay attention.

The next chart is of a market that was trading amidst rumors of trouble in the Middle East by the time we see the latter portion of the price action. The problem was that the situation was an on-again, off-again proposition. Prior to the takeover rumors, prices had broken out of congestion and had begun trending down. Let's notice how the Camelback method kept us out of trouble.



We'll begin at 'a', where we have a local low fully outside the channel from which to trade. At best, 'a' would have resulted in no more than covering costs and then breaking even.



At 'b', we would have tried to go short below the low of a local high, but the trade was nullified due to a gap opening.

At 'c' the 15 bar average was rising, and so a fill above the high of 'c' would have resulted in covering costs and being stopped out at breakeven.

'd', 'e', 'f', 'g', and 'h', were all profitable trades based upon selling short a breakout of the low of a bar making the local high. 'i' was unfulfilled because of the gap opening.

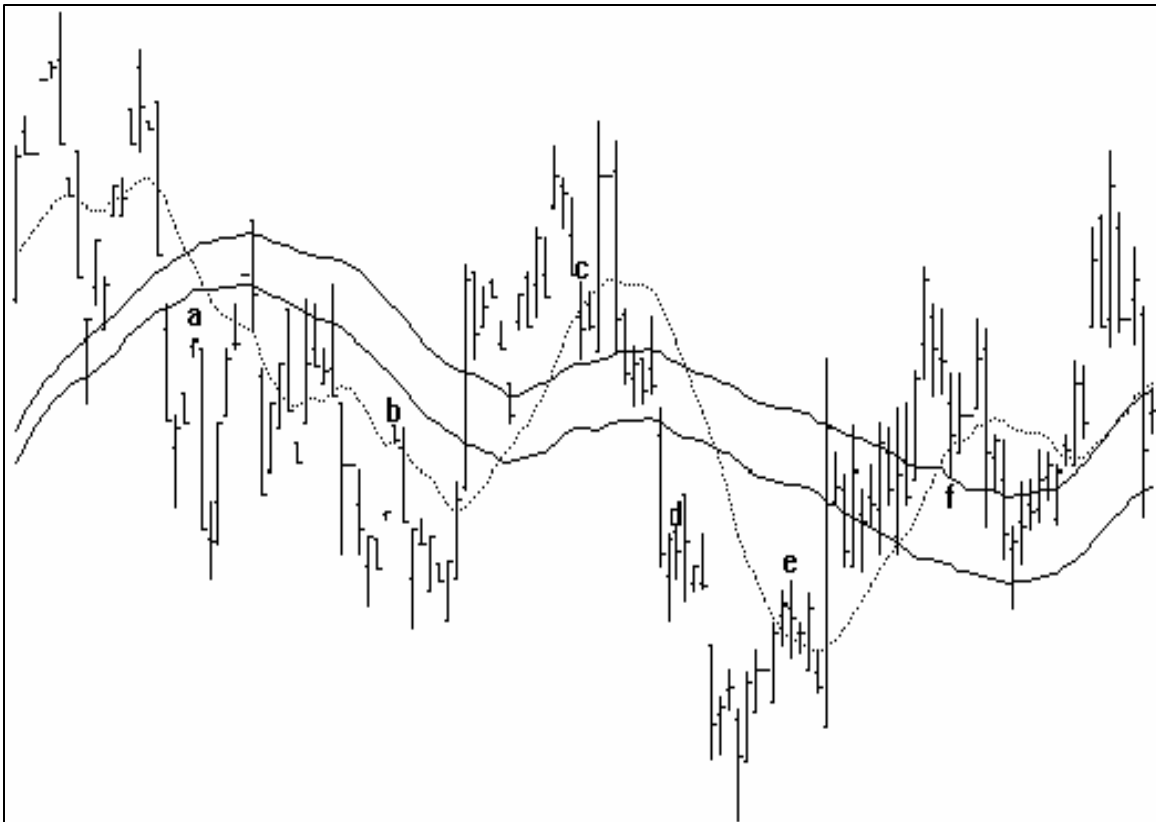
The best trade was made with a fill one tick above 'j'. 'j' was a local low.

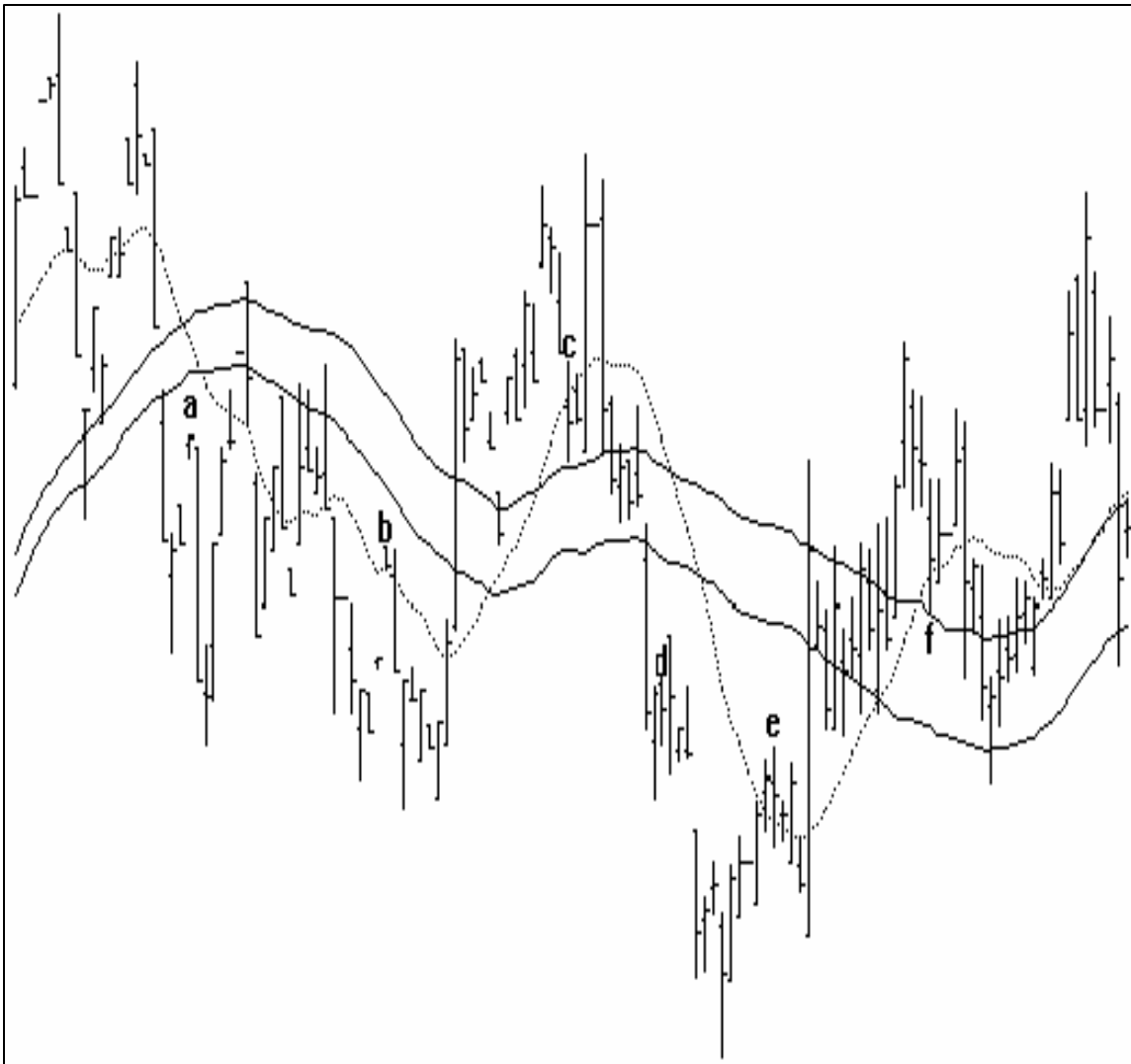
Now let's look a bit at the management of a Camelback trade. We always cover costs as soon as possible after entry, using 1/3 of our position. We set some sort of short term objective for a profit taking stop using 1/3 of our position. We then allow the final 1/3 to ride.

From time to time, when the 15 bar moving average is flat, we will miss out on large moves that would have been in our favor. These will be offset by avoiding large moves that would have wiped us out. We will be content to make steady and regular profits.

Now let's look at another chart using the Camelback technique.

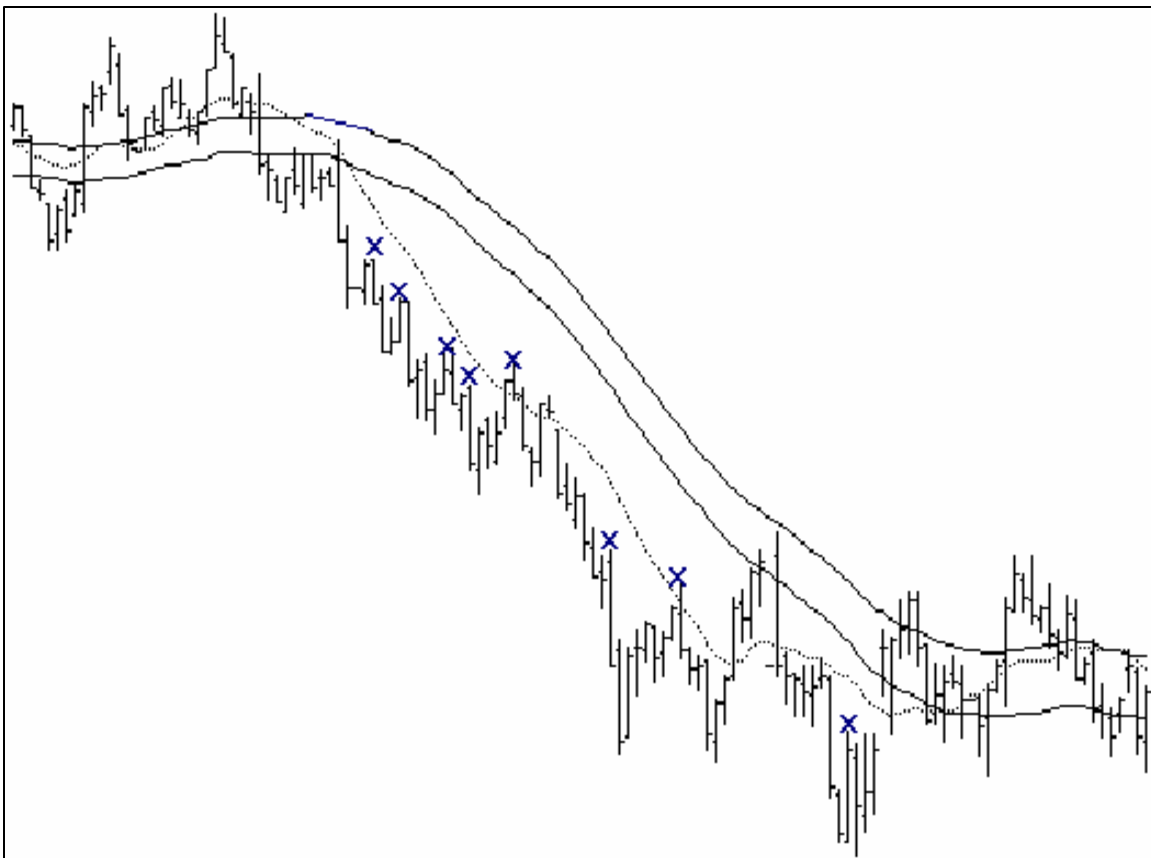
As far as we can see, there were only six trades on this next chart. It would have been rather difficult to trade on its own merits without some sort of filtration. The Camelback technique provided that filter. Obviously, the Camelback technique may at times not give a whole lot of trades, but wherever tested, it results in relatively small losses compared with relatively large wins. It seems to fulfill the requirement of keeping your losses small while you let your profits run. Let's look at the six trades.





At 'a', 'b', 'd', and 'e' we sell short a breakout of the low of a local high.
At 'c' and 'f,' we buy a breakout of the high of a local low.

Here's one last chart using the Camelback.



Once prices broke below the channel, the selling short of a breakout of the low of almost every price bar that made a local high would have resulted in a nice profit, or at the very least, have covered costs.

We've placed an 'x' by every point at which we think this could have happened.

The very last 'x' would almost surely have resulted in a loss.