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Sample Issue
Sample Alert

The Trading Climate

Aug. 31 Issue
Aug. 17 Issue
Aug. 3 Issue
July 20 Issue
July 6 Issue
June 23 Issue
June 9 Issue
May 26 Issue

Investor Glossary
Customer Service

Stock Trader

Trader's Profile

JUNE 23, 2004

Show Me the Sentiment

Tony Carrión has earned great returns by understanding how market patterns arise from the mood of investors and by playing these cycles

The road Tony Carrión took to active stock trading was long and winding. Back in 1976, he had dropped his studies in economics at Columbia University to pursue what he imagined was his true calling -- the theater.

When the mid-1980s bull market arrived, he had an inspiration: Rather than toil endlessly to raise money for shows he wanted to produce, he would simply fund his own projects with profits he would make by trading stocks. With that decision, his real education began.

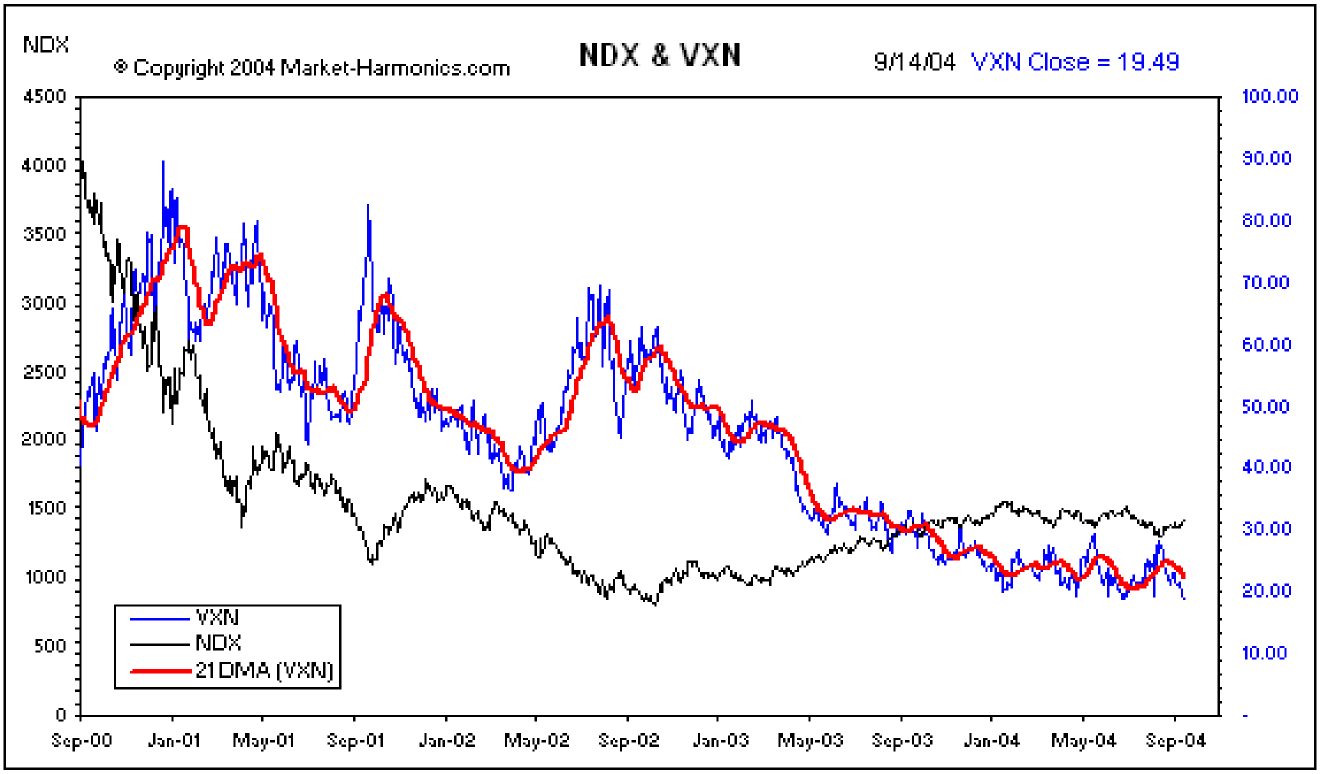
He started by finding a broker whose specialties were fundamental research and a traditional approach to investing. That meant buying the stocks of companies with solid balance sheets and stellar track records -- stalwarts such as General Electric (GE) -- and holding them forever. "I had read somewhere that that was recommended," he recalls. "I was a little wet behind the ears."

LIKE THE TIDES. After several experiences at watching buy and hold turn into buy and lose, Carrión decided to experiment with technical analysis. He was seduced by the Elliott Wave, the theory developed by market analyst Ralph Nelson Elliott in the 1930s. Elliott's devotees, who call themselves Elliotticians, subscribe to the theory that the mood of investors moves in predictable wave patterns from one extreme to the other. They also believe that tracking those patterns is a good way to predict overall market direction.

Once Carrión understood that stock prices tend to follow reasonably predictable patterns, he suddenly found that by charting the movements of everything from energy futures to specific stocks, he could figure out when to sell. He would no longer cling to a sinking stock because the company had attractive balance-sheet ratios and an impressive history. The decision to sell switched from one reflecting that the company had lousy prospects to one reflecting that the company was at a lousy place in its cycle.

"You can always go back," he still reminds himself, whenever he sells shares in a company he likes. "Nothing says you can't take a profit, let the stock price pull back as it naturally will, then get back in again."

Carrión was different from a lot of active traders: He didn't just follow charts -- he made them. For some charts, he simply takes data available to anyone, such as the Conference Board's Consumer Confidence Index, and puts it in a chart so that it's easier to understand the trend. Others he created, such as the VIX-VIN Composite Index:



FRIENDS CAME CALLING. Many investors like to look at volatility to find out where the market is heading. Some look at the volatility of the S&P 500-stock index, while some use the Nasdaq as a barometer. Carrión found a way to make a composite of both indexes to get a view of the overall market.

Meanwhile, his friends were impressed that he turned $800 into $10,000 in three months when he first started trading. By 1998, he was averaging a total annual return of 70 percent. His friends started asking him for help. He set up a Web site for all the charts he was making, calling it simply "Tony's Web site."

Nowadays, though he still makes a living mostly by trading, he also sells subscriptions to his chart site, Market Harmonics . He's also part-owner of a currency-trading brokerage, called Market Harmonics FX.

BETTING HIS BUCKS. Carrión recommends that newcomers to active trading start by following the volatility charts (see "Charting the Fear Factor"). The volatility indexes are easy to read for beginners, he says, and they show how sentiment interacts with the market.

He feels that he's a sharper market analyst because he invests based on his predictions. "You can't be an effective forecaster if you don't have a stake in it," Carrión says.

For his own trading, Carrión prefers the leverage of stock-index options -- contracts that give the purchaser the right to buy or sell an underlying index at a set price and date. If an investor buys an index options contract, the premium (the price of the contract) is all that he or she can lose, but the option controls a much greater amount of equity than the investor would have been able to buy for the price. Hence, the gain is potentially much greater.

SEASHELLS AND PYRAMIDS. Carrión typically uses a tool popular with Elliotticians, the Fibonacci retracements. Named after a 13th-century mathematician, these specific series of ratios (0.236, 0.382, 0.5, 0.618...) mysteriously show up in a variety of shapes in nature and art, from seashells to the Pyramids, and they describe a natural law. Thanks to computer programs, today's traders don't even need to know how old Leonardo Fibonacci came up with his numbers.

To make practical use of the Fibonacci numbers, Carrión plugs in a stock average and the software draws the Fibonacci ratios on the chart. Carrión then reads those lines as a stock support and resistance, or the floor and ceiling of a stock's trading range. (Technical traders believe that stock prices will usually stall out when they hit a line of support or resistance. But if the share price does manage to keep moving it will break out rapidly.)

Carrión grew up in the Bronx and spent much of his life in New York. But at age 50, he has recently moved to Florida, partly to look after his parents -- who are thrilled that he abandoned the theatre for a respectable career.

"They're jazzed," he says -- just as he has been, ever since he discovered the benefits of trading done right.

By Carol Vinzant, Editor

INVESTools METHOD

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