The OWL Handbook



Timeless Trading Methods for a New Generation

By Gil Morales

Published by G. Morales, LLC.
Copyright ©2024 G. Morales, LLC – all rights reserved.
Charts Copyright ©2024 HGS Investment Software, LLC – used by permission.

This book is dedicated to the memory of the "O" in the OWL, my former boss and mentor, legendary trader and investor William J. O'Neil (1933-2023).

Table of Contents

Foreword.....4

Foundational Philosophies.....8

Chapter 1 – A Review of O'Neil Disciple Set-Ups

Pocket Pivots.....13

Continuation Pocket Pivots.....20

Buyable Gap-Ups.....25

Chapter 2 – OWL Variants

Five-Day Pocket Pivots.....32

VooDoo Pullbacks (VDU).....38

Bottom-Fishing Pocket Pivots.....52

Bottom-Fishing Buyable Gap-Ups.....69

Price and Moving Average Undercut &
Rally (U&R) and MAU&R) Set-Ups.....87

Chapter 3 – Odds & Ends

Timing & Risk Management.....106

Final Thoughts.....107

Foreword

At one time in my career as a professional trader and investor I considered myself an O'Neil Disciple. This made sense since my original mentor and boss was in fact investment legend William J. O'Neil, founder of *Investors Business Daily*, a highly innovative investment newspaper at the time, and author of a true investment bible, *How to Make Money in Stocks*. Bill recruited me to run money for him and to manage his institutional advisory department back in October 1997. I spent the next eight years as a Vice-President and Internal Portfolio Manager at William J. O'Neil + Co., Inc.

During those glorious times, the O'Neil institutional advisory group I managed was responsible for advising over 700 of the world's top institutional investors ranging the gamut from hedge funds, mutual funds, pension funds, bank trusts, and insurance companies. In the process I was able to meet, observe, or otherwise interface with many of the top names in the institutional investment world. One of the main lessons that I took away from all of this is that while institutional investors may represent the letter "I" in O'Neil's CAN SLIM investment "algorithm," they did not really pay any attention to it as the backbone of their own investment methods and techniques.

In my view CAN SLIM spawned as a sensible and logical investment methodology for the stock market because it emphasized the prevailing characteristics of the post-World War Two growth investing strategies developed and adopted by institutional investors. The end of World War Two led to great prosperity in the United States as the pent-up savings of the public that piled up during wartime were unleashed. At the same time, the public became more involved in the ownership of equities as a way to gain their share of post-war prosperity and invest it smartly. This gave rise to the growth of mutual funds that were created to cater to this new public demand for stocks. In turn, mutual funds began to dominate the institutional investment landscape as a massive buying force.

Thus, *institutional sponsorship* became a significant variable in O'Neil's algorithm. Combined with minimum requirements for simplistic parameters of business growth and performance such as earnings, sales, return on equity, and profit margins, CAN SLIM became an extremely useful, effective, and popular method with which individual investors could invest their own money. It was the ultimate expression of the American ideal of individual freedom and independence.

As my career progressed, I began to find the methods of my mentor to be less effective during the strange and unique environment that draped the markets after the Federal Reserve Bank began its off-the-charts money-printing experiment known as *Quantitative Easing*, or QE. In 2008-2009 we became acquainted not only with QE, but also ZIRP, or zero interest-rate policy, as the Fed took interest rates to zero. This preceded an extended period of extremely low interest rates that, along with massive QE money-printing, created an artificial prop to the economy and the markets.

Massive levels of liquidity injected into the system by the Fed's QE actions of course found their way into stocks. Large member banks of the Fed and other financial institutions were easily able to access this large pool of liquidity for their own market activities, and this alone exerted a tremendous buying force in asset classes of all kinds. In addition, the Fed's zero interest rate policy kept the cost of borrowing absurdly low and distorted the true cost of capital. This created a second-order effect where companies could borrow money cheaply and then use it to buy back their own stocks with obvious effects.

By 2018, most buying in the market came from corporate buybacks as traditional institutional investors took a back seat. There was also the *ETF Effect* where record buying of Exchange Traded Funds that in turn bought stocks resulted in a large amount of algorithmic trading when ETFs balanced and rebalanced positions in response to the rise and fall of the underlying stocks.

I observed a great deal of choppy action, even within most uptrends. Chasing strength usually led to getting shaken out on sharp downside weakness. Breakouts often failed but would just as often break out again after a sharp pullback under less obvious circumstances. While I will never know for certain, this type of action in many stocks struck me as a machine-generated reversion-to-the-mean phenomenon.

Whatever the basis for the *new normal* in the Age of QE, the final litmus test was whether my new long and short set-ups proved to be more effective than more traditional breakout buying and shorting into weakness. I postulated that one had to think like an algo and trade the trader, taking an opportunistic approach that responded in a more contrarian manner.

Fortunately, I did not have to go far beyond my roots, as I found the solutions to be adaptations and evolutions of methods and basic philosophies already espoused by my former boss and mentor, William J. O'Neil, Richard Wyckoff, and Jesse Livermore. Thus, the OWL approach to the markets was born. And it worked.

I do not pretend to be a market guru. I am a trader and investor, yes, but most of all I am a humble student of the market. As I see it, there are no gurus. There cannot be. Markets change, they ebb, they flow, they shift, they evolve. Sometimes they exhibit *form*, other times they are *formless.* Like the cosmic dance of creation and destruction performed by the Hindu deity *Shiva* in his role as *Nataraja,* markets symbolize in their own way the interplay of dynamic and static energy flow, encompassing the five principles of eternal energy – creation, preservation, destruction, illusion, and emancipation.

The market has taught me many lessons over several decades of experience, some brutal, some harsh, some intoxicating, and some enchanting. So far, I have never heard of anyone, much less a *market guru*, who has avoided these lessons. Reflecting on these lessons as *pure students of the market,* however, we become better traders and investors. Unfortunately, I did not have the honor and privilege of knowing Richard D. Wyckoff and Jesse Livermore personally. I did,

however, know Bill O'Neil quite well, and I know that he never considered himself a market guru, but he most certainly conducted himself as a *student* of the market.

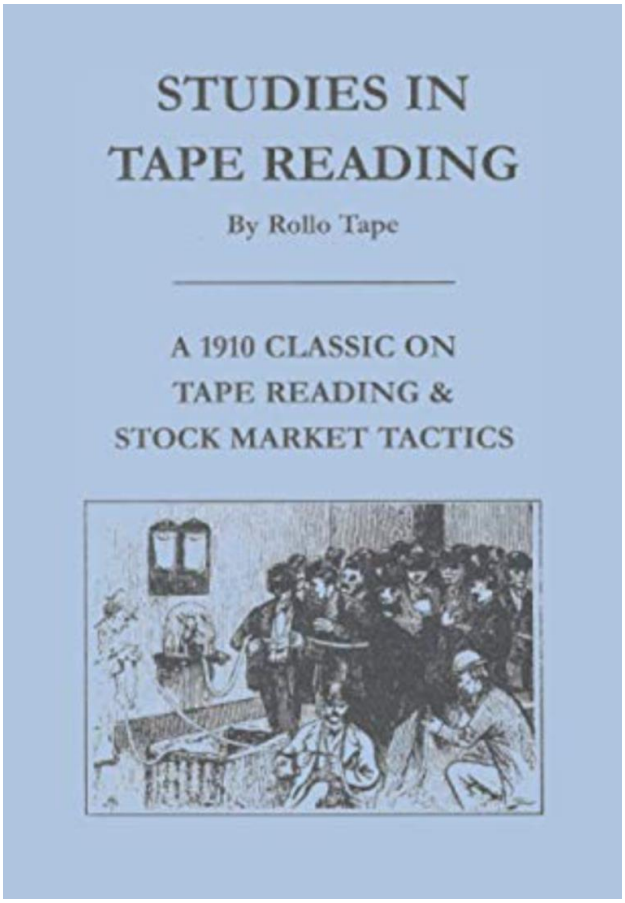
I view the material in this book as a starting point for becoming a student of the market. I have evolved and adapted my methods to changing underlying conditions and market dynamics while remaining rooted in the O'Neil-Wyckoff-Livermore trading ethos and philosophical tradition. Understanding how I have done that will hopefully help you, the reader, understand how to approach the problem on their own, through observation, study, and action as you refine your methods and tactics.

Bernard Baruch once wrote that, "The word *speculator* comes from the Latin *speculari* which means to spy and observe. A speculator, therefore, is a person who observes and acts before it occurs." As students of speculation, we also *observe and adapt*. Jesse Livermore committed suicide in 1940 when, in a mentally susceptible state as he watched his personal life spin out of balance, he lamented that his market methods no longer worked. While market pundits may account for Livermore's demise by emphasizing his deteriorating mental health, I see it as a unifying principle: Adapt or die.

Gil Morales, January 2024
Playa del Rey, CA

Foundational Philosophies

Willam J. O'Neil, Richard D. Wyckoff, and Jesse L. Livermore all had much in common, but they often differed in the details of technique. I first became acquainted with Richard D. Wyckoff when Bill O'Neil recommended that I read *Studies in Tape Reading* by Rollo Tape. *Rollo Tape* was Richard D. Wyckoff's pseudonym. Once I had devoured that book my interest in all things Richard D. Wyckoff was piqued and I went on to read his seminal works, *Stock Market Technique I* and *Stock Market Technique II*, as well as *How I Invest in Stocks and Bonds*, among others.



Richard D. Wyckoff also published *The Magazine of Wall Street* where he first wrote about the exploits of the *boy plunger* Jesse Livermore. He also published many small booklets or pamphlets as an adjunct to the magazine with titles like *Simple Methods of Analyzing Financial Statements*, *How to Detect the Beginning & Ending of Major Market Movements*, and *How to Avoid Loss Through Knowledge of Brokerage House Technique*. These booklets and pamphlets are out of print and considered rare but can be found at online auction houses like eBay, for a price!

Wyckoff interviewed Jesse Livermore for a series of articles published in *The Magazine of Wall Street* and later compiled into the book, *Jesse Livermore's Methods of Trading in Stocks*. Jesse Livermore authored his own book, *How I Trade in Stocks.* Most everyone who has read O'Neil's books has also probably read Edwin Lefevre's *Reminiscences of a Stock Operator*. When John Wiley & Sons published a beautifully illustrated edition of that book in 2005, complete with the original illustrations from the *Saturday Evening Post*, Bill O'Neil was more than happy to write the Foreword for the book.

In that Foreword, O'Neil reveals the impression that Livermore made on him when it came to basic market philosophy. The preeminent principle that O'Neil shared with Livermore and Wyckoff was the idea that "markets are always right, opinions seldom are." Only by listening to the market and being entirely open to perceiving its message in real-time, can one succeed in the stock market. Taking the rigid approach of trying to enforce one's opinion on the market or an individual stock is a recipe for disaster.

From this principle stems the basic idea that averaging down on a losing position is essentially defying and denying the market's message. You are wrong, and the market is telling you so. Livermore was quite plain about his view that there was no bull side or bear side of the market, but only *the right side*, so when the market tells an investor that they are on the wrong side of the market, the only remedy is to quickly get on the right side.

This in turn spawns another common principle that O'Neil, Wyckoff and Livermore promulgated, which is that when a position is moving against you then losses should be cut short before they blossomed into a cancerous sore in one's portfolio. Livermore chose a flat 10% as the maximum loss he was willing to sit through before selling a stock position. O'Neil tried to inject some refinement into this by advocating 7-8% as a maximum stop-loss point based on his methods of buying breakouts and asserting that breakouts rarely pulled back more than 7-8% from the buy point. Through a more rigorous statistical analysis, I found that this does not hold true as you will see later.

All three, O'Neil, Wyckoff and Livermore, also advocated the use of price and volume charts and data when analyzing individual stocks and the general market. They believed that it is impossible to determine where a stock is going unless and until you know where *it has been*. Patterns of prior accumulation by the well-financed *smart money* set the stage for intermediate to longer-term price movements.

Bill O'Neil once told me that if he had to choose between using daily or weekly charts, he would choose weekly charts. In his view, weekly charts were much more useful in identifying patterns of institutional accumulation because it was a time frame more appropriate to their scale of buying. The massive positions taken by mutual funds often took days and weeks to build, and weekly charts helped to reveal their buying patterns.

While Richard Wyckoff was a keen advocate of using daily charts, Jesse Livermore used a different method to track patterns of buying and selling in individual stocks through his Livermore Market Key. All three were tape readers who believed that observing real-time price and volume action was the most direct and accurate way to anticipate and understand developing market and stock trends.

Bill O'Neil used to talk about certain stocks as being *big* stocks. I recall when he was long 1.5 million shares of the old internet leader, American Online (AOL) back in 1998. He called me on the phone one

day as I sat in my office at William O'Neil + Co., Inc. and he abruptly said to me, "See that AOL? Now THAT'S a big stock."

Like a lightning bolt, it hit me. He was essentially saying that one should focus on the big stock leaders in any bull market cycle. Understanding what makes a big stock is discussed in detail in the first book I wrote with my colleague Chris Kacher, *Trade Like an O'Neil Disciple: How We made 18,000% in the Stock Market (*John Wiley & Sons 2010)

This is also what Jesse Livermore advised when he talked about sticking to the *Leading Issues of the Day* when investing and trading in the stock market. Back in his day, Livermore wrote an investment newsletter, believe it or not, something else I have in common with the man in addition to the fact that early in investment careers we both worked for the now swallowed-up firm *PaineWebber, Inc.* Newsletters.

In one of those newsletters, Livermore wrote, *"If an investor can make up his mind that he will never own any stocks – unless they are consistently, day in and day out, among the 15 most active issues traded in, he will find, those stocks always have a ready market that one can take advantage of – and sell, if one so desires – without seeing them fade away points and points between sales of a 100 shares of stock."*

Livermore's idea of sticking to the "15 most active issues traded in" dovetails nicely with his rule that "if you cannot make money out of the leading active issues, you are not going to make money out of the stock market as a whole." And this, in turn, is what Bill O'Neil was talking about when it called certain stocks "a big stock."

In Livermore's day, the leading issues of the day were also the names that the big pools and trusts were trafficking in. The big pools and trusts were Livermore's *institutional investors*. They had the clout necessary to move stocks, and when they wanted in or out of a particular stock, Livermore could see it on the tape.

As stock investing and stock markets evolved, eventually mutual funds replaced pools and trusts. This is what Bill O'Neil identified as *institutional sponsorship*. During the post World War 2 era, the rise of mutual funds as individual investors poured money into these investment vehicles made them a formidable buying (and selling) force in the stock market over the next several decades.

For both Livermore and O'Neil, understanding the major driving forces behind any market move was essential to making money in stocks. Richard D. Wyckoff was no different in this respect. He instructed the public about "*the real rules of the game"* as played by the "smart money." In Wyckoff's day, as a contemporary of Livermore, these were also the big pools and trusts that drove market trends.

All three brought certain foundational philosophies to the investment process, all while adapting to the investment environment and its concomitant price-moving forces. While they are quite similar with respect to being rooted in common sense, they also reflect slight variations that represented adaptations to a particular market environment. In today's market, where the environment is beset by the most unusual and bizarre underlying conditions, it is not a big leap of logic to synthesize the similar philosophies into one unifying methodology – the OWL.

The Long Side

Chapter 1: A Review of O'Neil Disciple Set-Ups

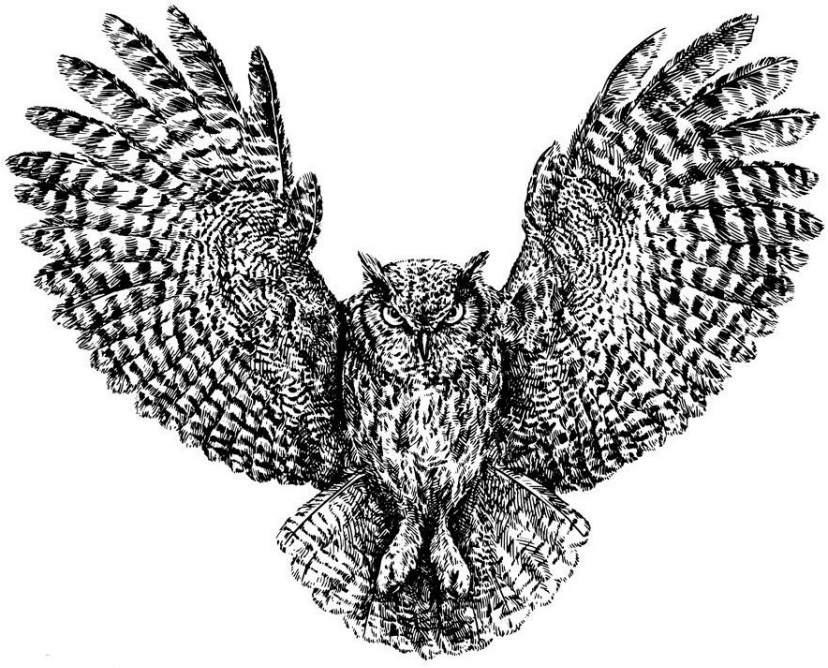
Pocket Pivots

These were originally discovered by my colleague Chris Kacher back in the early 2000's and discussed in detail in the first book we co-authored, *Trade Like an O'Neil Disciple – How We Made 18,000% in the Stock Market* (John Wiley & Sons, 2010).

In that book there were ten basic rules or requirements for a proper pocket pivot. They were:

1) As with base breakouts, proper pocket pivots should emerge within or out of constructive basing patterns.
2) The stock's fundamentals should be strong, i.e., excellent earnings, sales, pretax margins, ROE, strong leader in its space, etc.
3) The day's volume should be larger than the highest down volume day over the prior 10 days.
4) If the pocket pivot occurs in an uptrend after the stock has broken out, it should act constructively around its 10-day moving average (10-dma). It can undercut its 10-dma if it shows resilience by showing volume that is greater than the highest down volume day over the prior 10 days.
5) Pocket pivots sometimes coincide with base breakouts or with gap ups. This can be thought of as added upside power should this occur.
6) Do not buy pocket pivots if the overall chart formation is in a multi-month downtrend (5 months or longer). It is best to wait for the rounding part of the base to form before buying. That said, bottom-fishing pocket pivots can provide entry points especially if coinciding with undercut & rally formations.

7) Do not buy pocket pivots if the stock is under a critical moving average such as the 50-dma or 200-dma. If well under its 50-dma, and getting support near the 200-dma, it can be bought provided the base is constructive.
8) Do not buy pocket pivots if the stock formed a 'V' where it sells off hard down through the 10-dma or 50-dma then shoots straight back up in a 'V' formation. Such formations are failure prone.
9) Avoid buying pocket pivots that occur after wedging patterns. Wedging patterns occur as a stock is rallying with volume simultaneously declining.
10) Some pocket pivots may occur after the stock is extended from the base. If the pivot occurs right near its 10-dma, it can be bought, otherwise it is extended and should be avoided. Give the 10-dma the chance to catch up to the stock, where the stock would consolidate for a few days, before buying such a pocket pivot.



Examples:

The first epic price move in Bitcoin as it emerged from relative obscurity and entered the consciousness of the average investor occurred in 2017 and was playable using the **Grayscale Bitcoin Investment Trust (GBTC)** (Figure 2.1). GBTC was the first tradeable equity market vehicle that offered investors a way to play price moves in Bitcoin.

Bitcoin as measured by GBTC started 2017 just above $1,000 and initially ran up into a short-term peak in late August. From there it went on to build a two-month base that got very tight around the $3,000 level.

In late October, GBTC flashed a strong-volume pocket pivot that marked the embryonic beginnings of the parabolic portion of Bitcoin's total price move in 2017. That took it back up towards the August highs where it then spent another month consolidating. In late November it gapped up to new highs in late November and went into a parabolic frenzy that took Bitcoin to within $130 of the $20,000 mark.

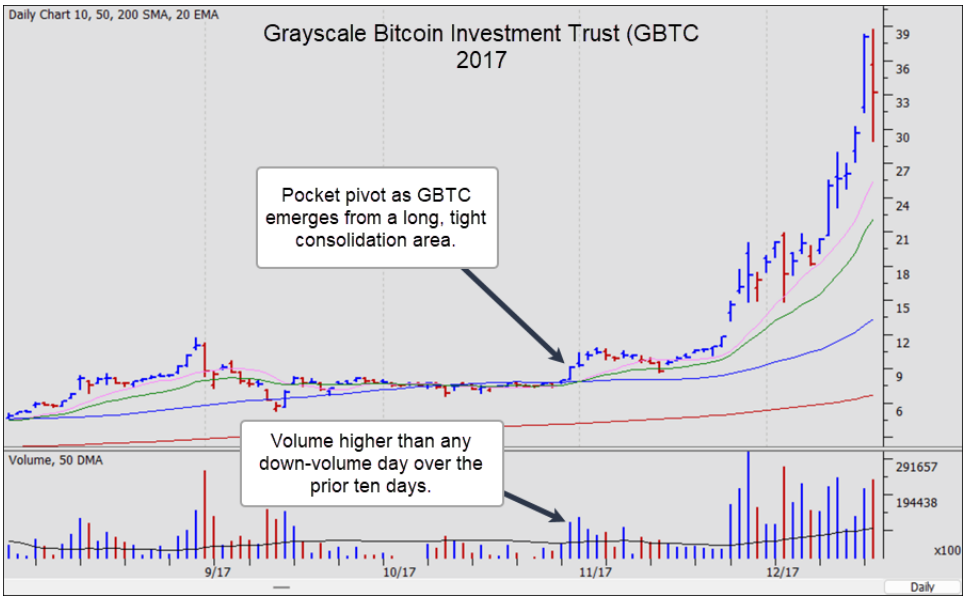


Figure 2.1 - Grayscale Bitcoin Investment Trust (GBTC) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Pocket pivots within tight price areas, like bases and consolidations may not necessarily lead to immediate upside but are more indicative of what I refer to as *percolation*. In April of 2017 **Square (SQ)** (Figure 2.2) today known as Block (SQ), posted a pocket pivot as it tracked tight sideways along its 10-day and 20-day moving averages. That was followed by a small pullback to the moving averages where volume dried up in the extreme.

In this case we have a pocket pivot followed by a constructive, low-volume pullback. This creates a compelling and opportunistic entry where the two moving averages serve as selling guides. SQ then moved higher from there in a steady uptrend.

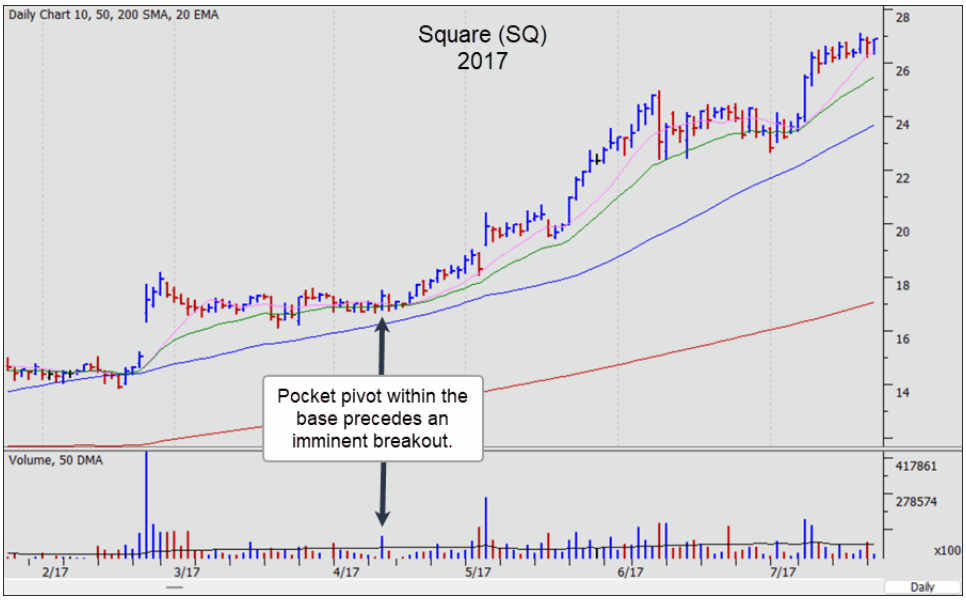


Figure 2.2 - Square (SQ) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

When the Covid pandemic hit in early 2020, the Fed went on a two-year money-printing expedition that took the total amount of U.S. Dollars in circulation from $4 trillion to $20 trillion. While this certainly had its effect on stocks, it also ignited a big move in precious metals. The **iShares Silver Trust (SLV)** (Figure 2.3) had split wide open with the market in March 2020 when the pandemic hit, but

rallied up from its pandemic lows by late spring and spent the next six weeks moving tight sideways.

It eventually posted a pocket pivot in late June along its 10-day moving average. This was followed by a two-day pullback after which the SLV began a price advance that culminated with a parabolic price move into the early part of August. Interestingly, right at the peak, Warren Buffet, who had previously derided gold as a *pet rock*, was suddenly buying gold and gold stocks, adding an anecdotal accent to the peak of parabolic move that began with a humble pocket pivot.

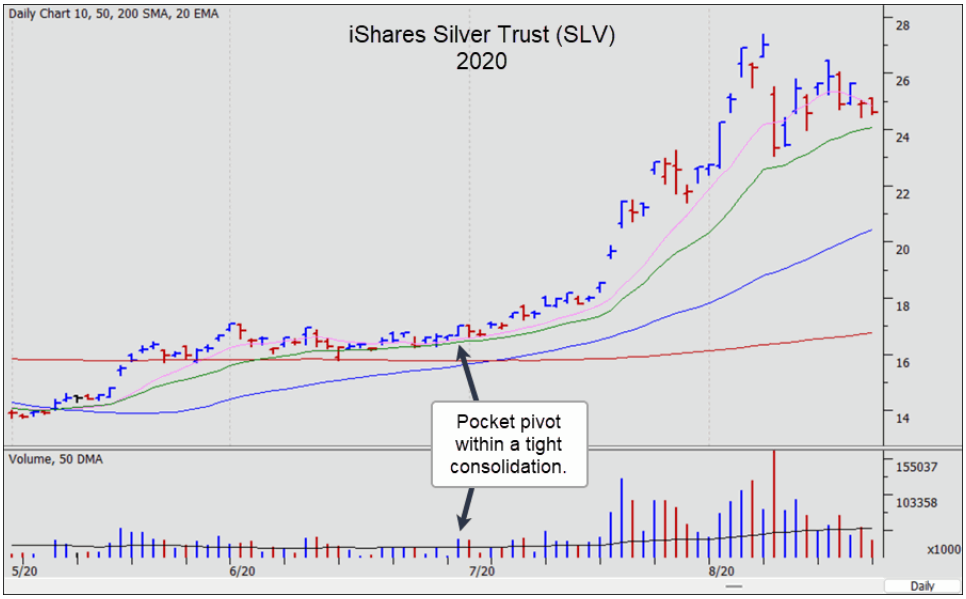


Figure 2.3 - iShares Silver Trust (SLV) daily chart, 2020.Chart copyright 2024 HGS Investor Software, LLC, used by permission.

During the 2020-2021 Everything Bubble Bull Market spawned by massive fiscal and monetary stimulus in response to the Covid pandemic, electric vehicles quickly became all the rage. Suddenly, every manufacturer of any kind of electric vehicle, whether luxury EVs or battery-powered three-wheeled oddities, was coming public in rapid succession.

Many came to life as publicly traded companies through special purpose acquisition companies, or SPACs as they were more commonly known. The fact that most of these companies did not sell

more than a handful of electric vehicles, if that, was of no concern to FOMO-infused buyers of these stocks.

This in turn gave rise to so-called cousin stocks related to the entire EV phenomenon. Since electric vehicles are powered by batteries, battery technology came into focus, including the companies that mined the stuff from which lithium-ion batteries are made. That would of course be lithium.

Piedmont Lithium (PLL) (Figure 2.4) caught fire during this period when it stepped firmly into the crosshairs of investor awareness on news of a lithium supply deal with big-stock electric vehicle maker **Tesla (TSLA)** in late 2020. A big gap-up move was soon followed by a long, three-month period of digestion and consolidation as the stock set up again.

As it began to round out the right side of its new base two stark pocket pivots showed up along the 10-day, 20-day and 50-daymoving averages. These presaged a new-high breakout 3-4 weeks later which was difficult to buy given how erratic PLL acted around the breakout point.

The price movements after the pocket pivots, however, were much more coherent and relatively much easier to handle. Not only that, but they enabled an investor to capture roughly another 40% of upside before the stock every broke out to new highs.

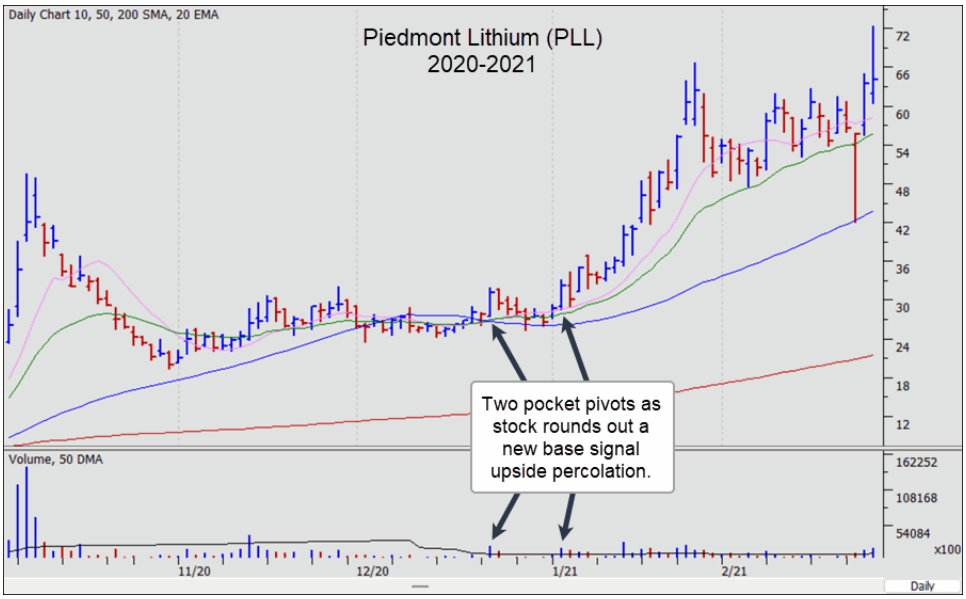


Figure 2.4 - Piedmont Lithium (PLL) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Aluminum shortages leading to higher aluminum prices in 2021 propelled a big move in **Alcoa (AA)** (Figure 2.5) that did not top until March of 2022, three months into the 2022 bear market. Along the way, in February of 2021, AA was correcting sharply before finding its feet amid a near-term oversold condition. It then rallied back above its 20-day exponential moving average but had yet to clear its 50-day moving average until it posted a strong pocket pivot on February 19th and began an accelerated uptrend. Note the way volume dries up sharply in the days just before the pocket pivot.

Again, the advantage of using pocket pivots instead of relying solely on base breakouts as buy points is well demonstrated. Three days after the February 19th pocket pivot, AA broke out to new highs but immediately reversed and broke down sharply over the next two days. If using a standard O'Neil-style stop-loss of 7-8% one would easily have been stopped out of the position just as the big move was beginning.

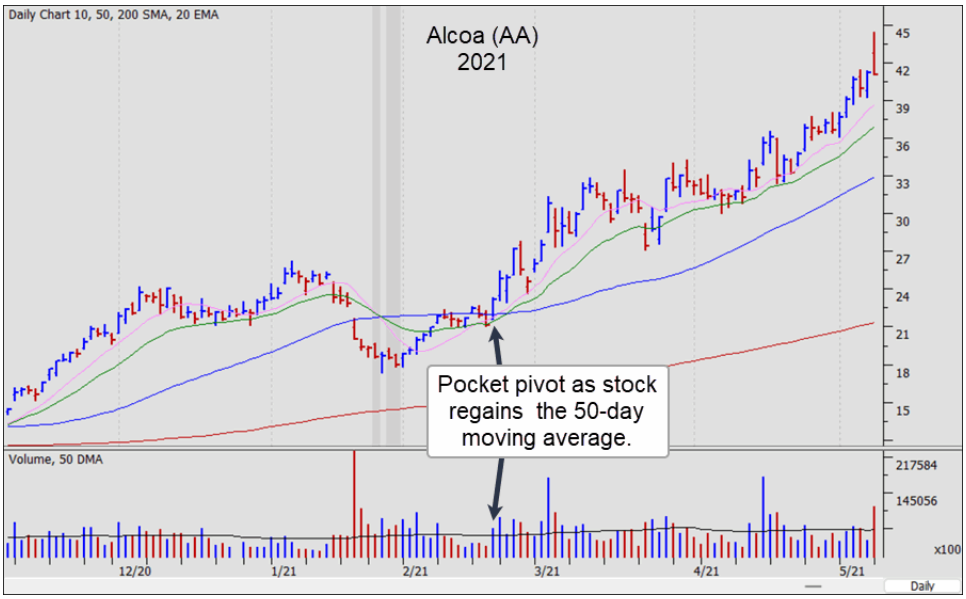


Figure 2.5 - Alcoa (AA) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Continuation Pocket Pivots

A variation of the pocket pivot occurring within a base or on a breakout is the *Continuation Pocket Pivot* which occurs in an uptrend once a stock is up and out of a base. This was discussed in *Trade Like an O'Neil Disciple* and defined as a pocket pivot that occurs along the 10-day moving average as a stock is in an uptrend and has made some progress to the upside as it gets extended from a recent breakout.

Examples:

Silver's epic run to $50 an ounce in 2010-11 featured a very steady uptrend along the 10-day moving average in the **iShares Silver Trust (SLV)** (Figure 2.6) that began in late summer 2010. Along the way, two pocket pivots occurred as the stock was trending strongly along its rising 10-day moving average in September 2010. Silver eventually got to within an eyelash of the $50 level before topping at the end of April 2011.

This trade was memorable for me because as silver was rising through the $35 level in early 2011, I appeared on Fox Business News to be interviewed by Stuart Varney, host of Varney & Company. Stuart pressed me on my price target for silver, but as a trader I do not operate with rigid price targets in mind. The trend is your friend until it bends at the end, as the legendary futures trader Ed Seykota would say, and I was simply waiting for the trend in silver to bend, at which point I would sell.

Mr. Varney would have none of this since cable financial TV tends to cater to an absolutist view of the markets where everything is reduced to easily digestible but useless predictions. Finally, I blurted out something like, "My price target is $50!" As it turned out, that "prediction" was off by only a few cents by the time silver topped in April 2011 at $49.82 an ounce.

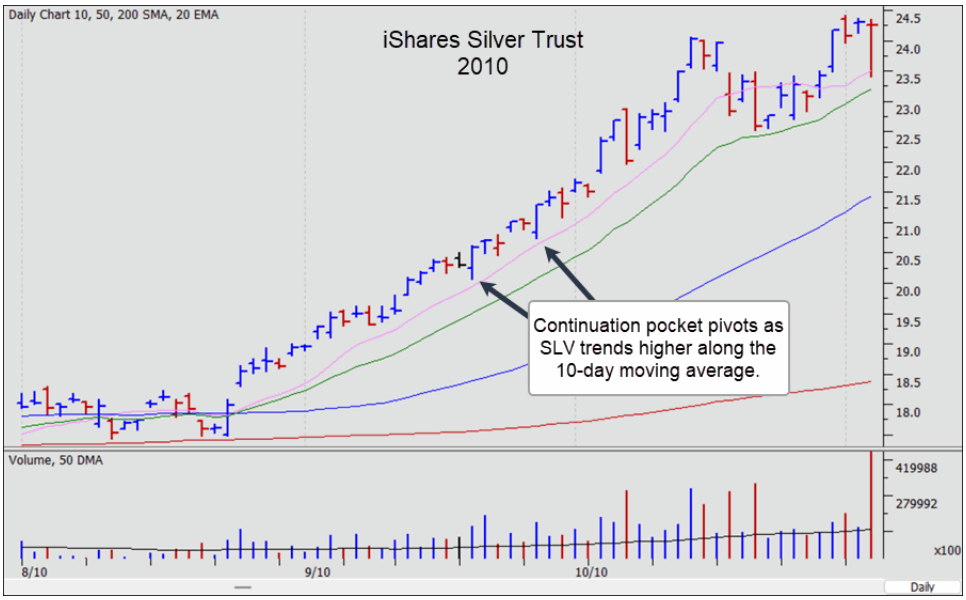


Figure 2.6 - iShares Silver Trust (SLV) daily chart, 2020. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

The continuation pocket pivot in **Alibaba Group (BABA)** (Figure 2.7) in April of 2017 occurred within a shallow uptrend and out of a short seven-day consolidation. That stock had already broken out of a base about three weeks earlier so was slowly lifting off the launch pad. As

it did, this continuation pocket pivot served as a useful add point just before the uptrend began to steepen along the 10-day line.

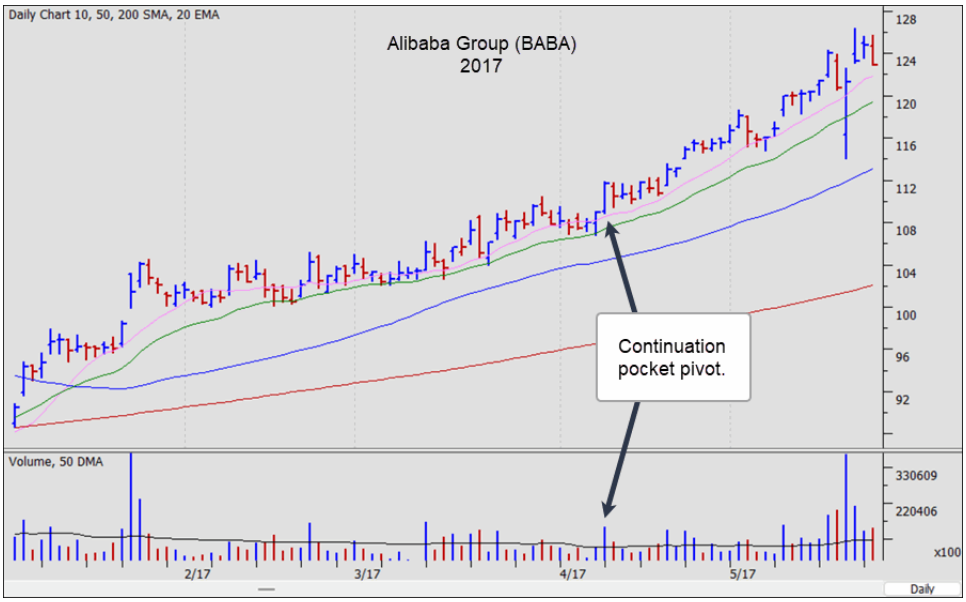


Figure 2.7 - Alibaba Group (BABA) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Twilio (TWLO) (Figure 2.8) posted this continuation pocket pivot along its 10-day moving average in March of 2018 following a big-volume gap-up breakout (also a buyable gap-up move) two weeks earlier. Note the steady uptrend following the gap-up breakout on light volume that looks like wedging but holds the 10-day line the whole way before bursting higher in a big-volume pocket pivot move off the 10-day moving average.

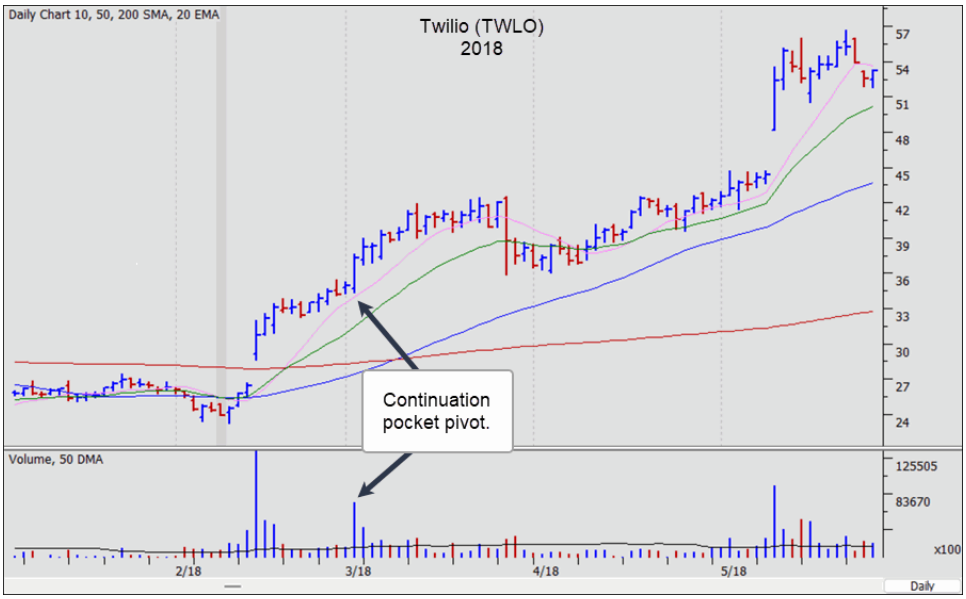


Figure 2.8 - Twilio (TWLO) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Two variations of the continuation pocket pivot are seen in **Roku (ROKU)** (Figure 2.9) during 2020. The first one occurs within a short uptrend in November where the stock has been wedging higher on very light volume. An initial breakout attempt two weeks earlier failed, but ROKU was able to breakout again on a pocket pivot that occurred on a re-breakout as the stock resumed its uptrend. The second continuation pocket pivot in December was more orthodox as ROKU showed strong volume at the 10-day moving average within a steady uptrend along the line.

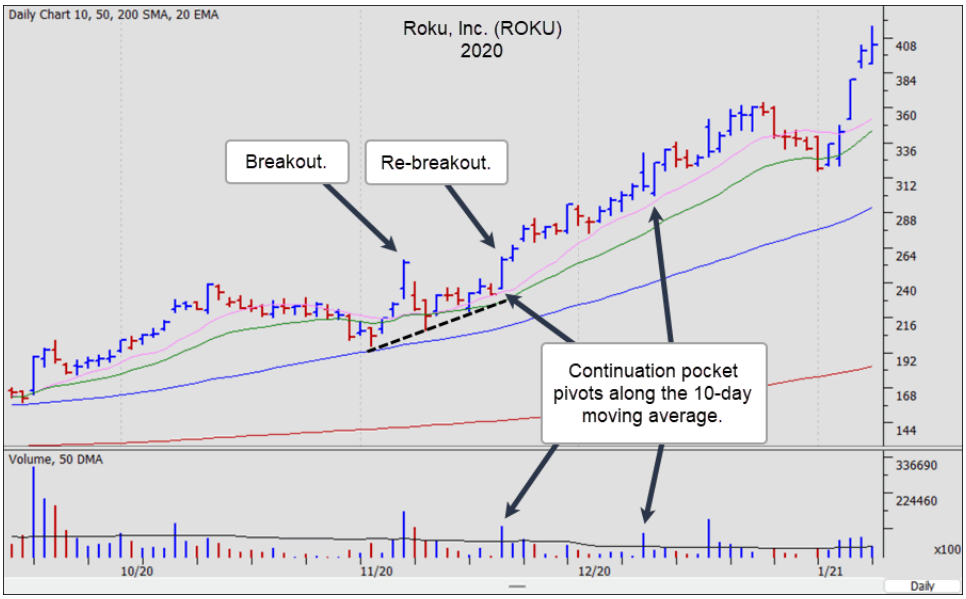


Figure 2.9 - Roku (ROKU) daily chart, 2020. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Chinese electric vehicle maker **Nio, Inc. (NIO)** (Figure 2.10) in October 2020 was a typical continuation pocket pivot that occurs as the stock pulls in for a few days and meets up with the rapidly rising 10-day moving average. While NIO had posted several breakouts prior to this continuation pocket pivot, including a gap-up breakout two weeks earlier, its uptrend began to accelerate sharply once it posted this strong-volume pocket pivot after a two-week pullback.

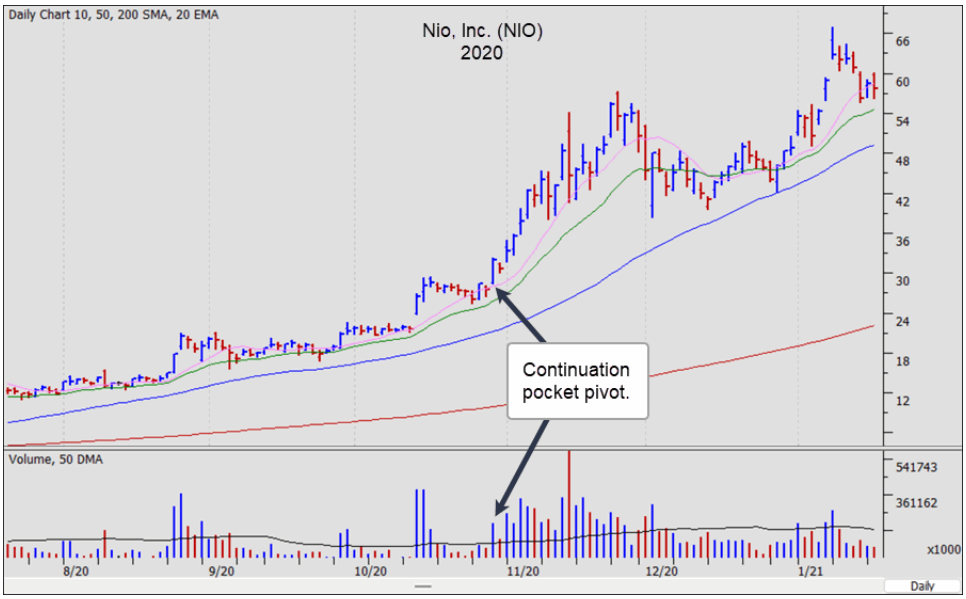


Figure 2.10 - Nio, Inc. (NIO) daily chart, 2020. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Buyable Gap-Ups

The "BGU," as it is abbreviated, was also discussed in *Trade Like an O'Neil Disciple*. The rules for a buyable gap-up can be distilled as follows:

1) The gap-up price move should be at least 0.75 times the 40-day Average True Range of the stock.
2) Volume on the gap-up price move should be at least 1.5 times the 50-day moving average of volume.
3) Sell if the stock breaks below and violates the intraday low of the buyable gap-up price range.

Examples:

Lumentum Holdings (LITE) (Figure 2.11) in July 2016 illustrates a buyable gap-up that took a few days to get moving. It also gave buyers a second chance to enter the stock on the long side when it tested the intraday low of its buyable gap-up day price range three days later. That coincided with a very clean test and hold of support at the

10-day moving average. Following a buyable gap-up, such pullbacks can offer additional long entry opportunities.

Generally, however, the longer a buyable gap-up takes to develop upside momentum and instead moves sideways for several days after the initial gap-up move the greater the chances of failure. In LITE's case, however, the stock eventually developed upside momentum and trended higher along the 10-day moving average over the next several weeks.

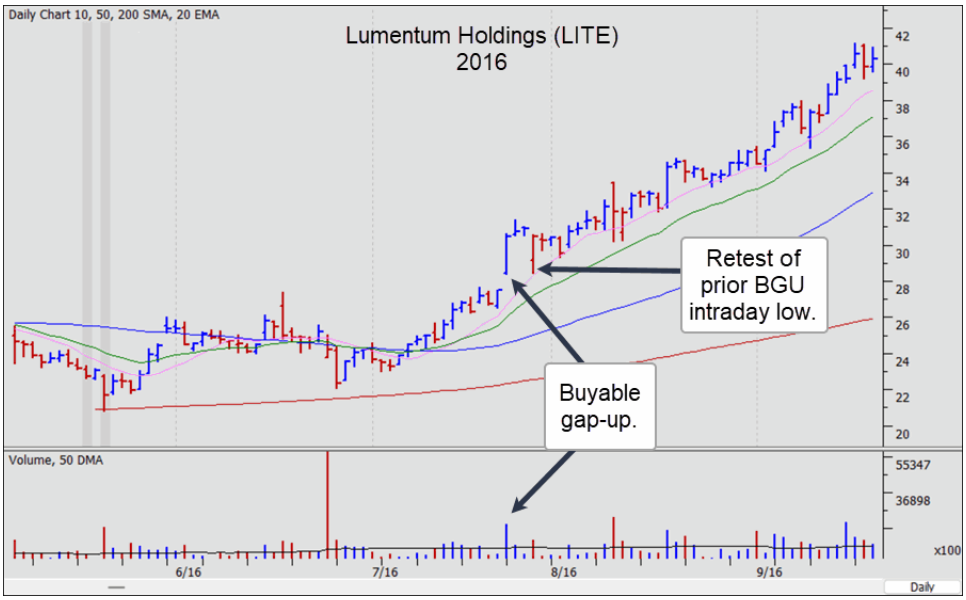


Figure 2.11 - Lumentum Holdings (LITE) daily chart, 2016. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Amazon.com (AMZN) (Figure 2.12) in October 2017 posted a massive-volume pocket pivot and began a slowly developing uptrend that eventually gained momentum in late December. Note that the buyable gap-up came from a point off the deep lows of a base and broke out on the same day. That was what Bill O'Neil would refer to as a suspect *straight up from the bottom* or "SUFB" breakout.

In my view, this is a meaningless qualitative assessment since one can simply take the objective view of this as a standard buyable gap-up long entry trigger using the intraday low as a tight selling guide. Doing that also ensures that one takes a position lower in the long

price bar, nearer to the intraday lows, *before* the actual breakout that likely occurred later in the day.

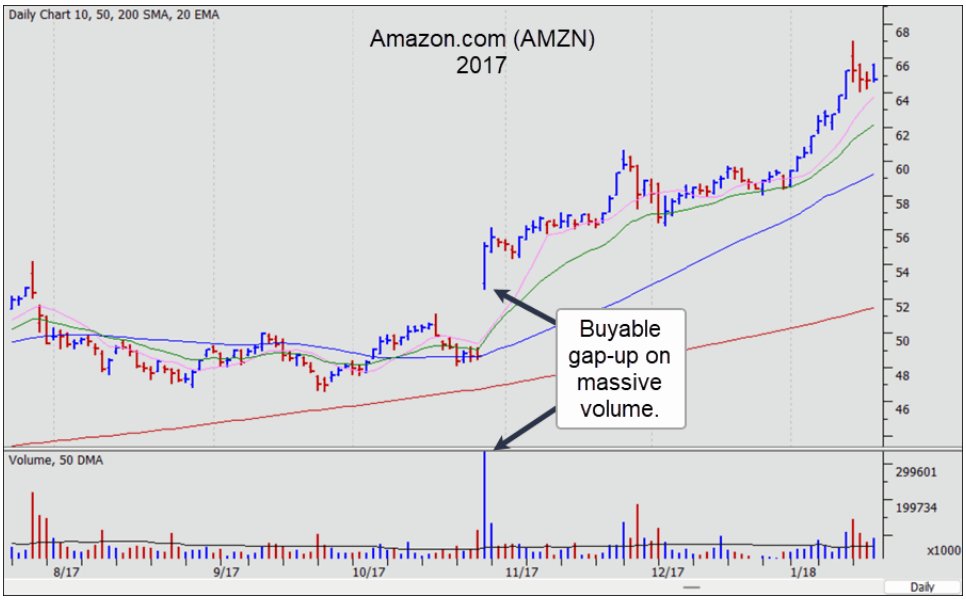


Figure 2.12 - Amazon.com (AMZN) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Way back in December 2004 **Research in Motion (RIMM)** (Figure 2.13(a), which in 2013 changed its corporate name and stock symbol to **Blackberry Ltd. (BB)**, posted a massive-volume buyable gap-up that started with an opening print at a split adjusted price of 9.75 and ended the day at 11.60. Because RIMM had immediately posted an intraday low at 9.72, three cents below the opening price, right at the open, one could have acted early in the day by buying the stock and using the 9.72 low as a selling guide.

As the move progressed throughout the day the 9.72 low held and RIMM shot more than 20% higher from there. It then spent six days moving sideways before breaking out to higher highs on the seventh day following the BGU. If one was a breakout buyer, then RIMM was immediately extended and beyond buying range of the very tight six-week base at the open. Breakout buyers were effectively shut out, but those using the BGU method as outlined by my colleague Chris

Kacher were presented with a very easily actionable long entry trigger well below the $10 level.

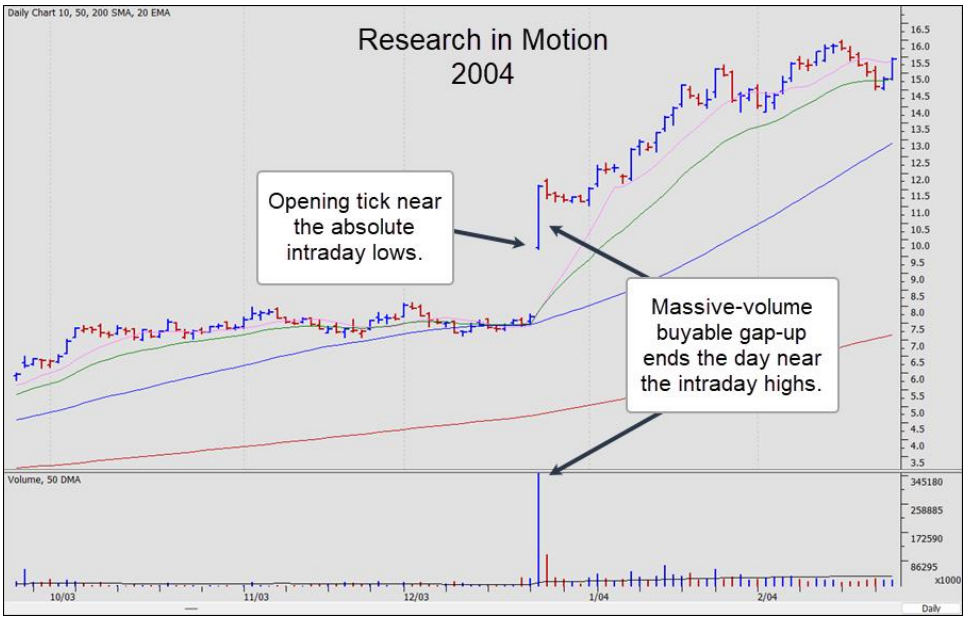


Figure 2.13(a) - Research in Motion (RIMM) daily chart, 2004. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

The example of **Research in Motion (RIMM)** in Figure 2.13(b), the 2004 weekly chart, illustrates the imprecision of O'Neil-style qualitative base-labeling relative to the specifics of a buyable gap-up long entry set-up. Back in 2005, O'Neil came up with the so-called *Short Stroke* base formation which was derived directly from this RIMM example. To my knowledge, RIMM was the only example of this pattern, and in my view a statistical sample size of one is pathetically inadequate to draw firm, predictive conclusions from such a pattern.

The short stroke pattern, as Bill O'Neil described it, consisted of a long weekly price bar to the upside followed by a very narrow weekly range that holds very tightly along the highs of the prior week's high. In RIMM's case, it has the appearance of a breakout from a very tight six-week flat base and then an excruciatingly tight one-week flag as the stock refuses to give back any ground.

The reality is that *Short Stroke* type patterns typically are just buyable gap-ups that hold tight near the highs of the BGU price range for several days and then move higher. Thus, they can simply be treated as BGU long entries. There is no reason to treat them as anything else. Labeling these types of moves as Short Stroke patterns is primarily qualitative and certainly far less precise. In fact, had one sat around waiting for this so-called Short Stroke pattern to form, one would have missed the immediately buyable gap-up move in RIMM as we see in the daily chart above (Figure 2.13(a).

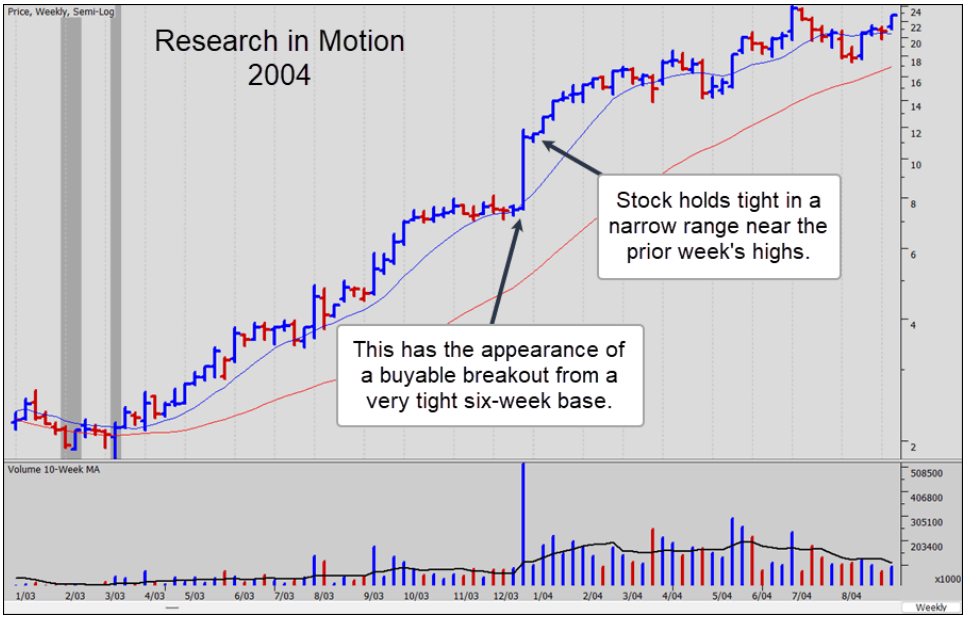


Figure 2.13(b) - Research in Motion (RIMM) weekly chart, December 2004. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

SolarEdge (SEDG) (Figure 2.14) in February 2018 is another example of a buyable gap-up that opens on a gap move and then posts an intraday low not too far below the opening print before streaking higher. It then chugs higher along the 10-day moving average before forming a new base from which is breaks out in May 2018 in a powerful move.

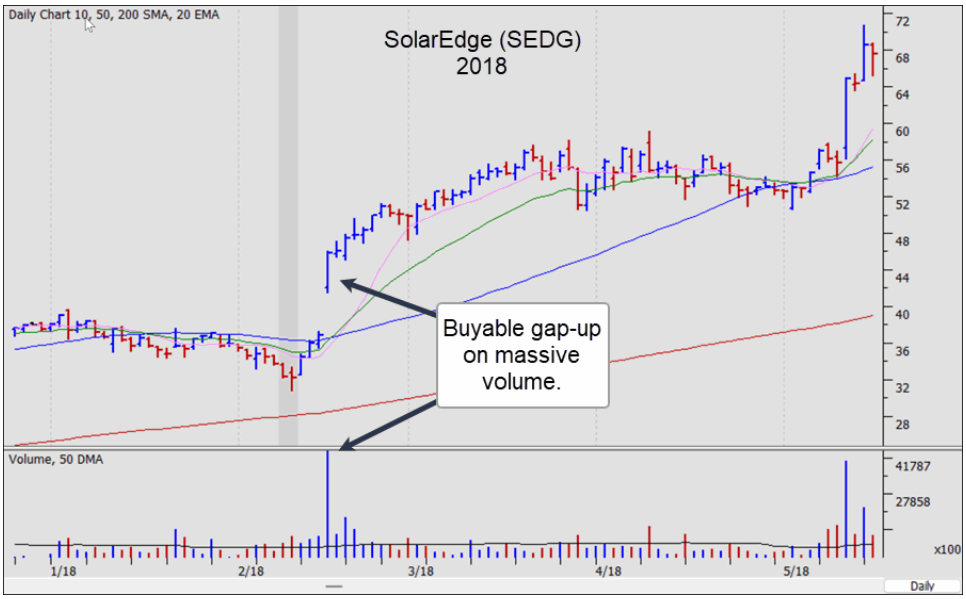


Figure 2.14 - SolarEdge (SEDG) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Tesla (TSLA) (Figure 2.15) shows more upside velocity following its buyable gap-up in October 2019. It streaks higher the day after the BGU and then begins to pull back. Volume eventually dries up as it pulls into its 10-day moving average and the stock proceeds higher from there.

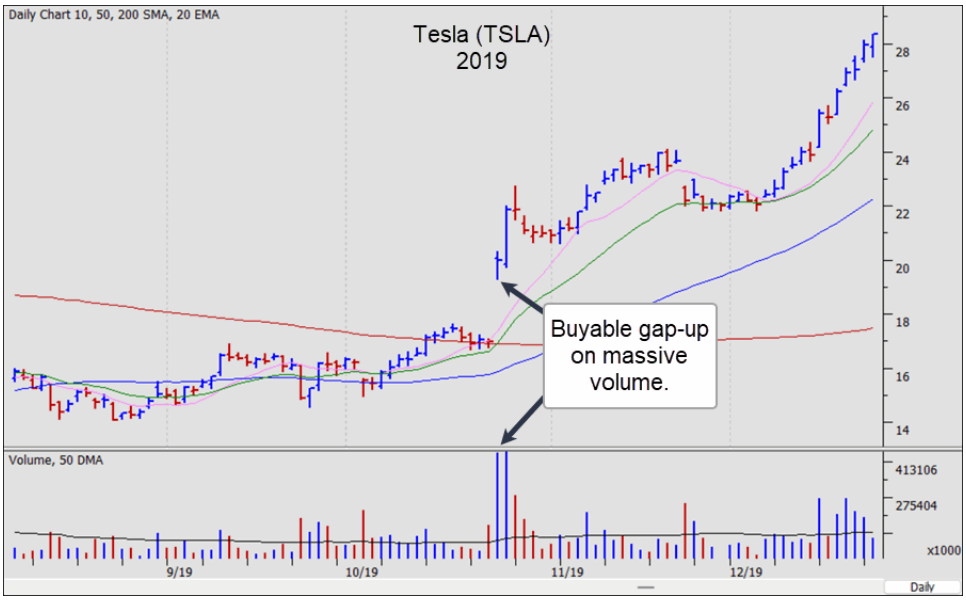


Figure 2.15 - Tesla (TSLA) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

CyberArk Software (CYBR) (Figure 2.16) in early November 2018 is an excellent example of how buyable gap-ups fail. The stock gaps higher and then reverses from the intraday highs to close near the intraday lows. It then quickly breaks below the intraday low of the BGU day two days later and then spends another three months building an entirely new base.

CYBR eventually sets up in its new base and breaks out in January 2019. Following two pullbacks to the 20-day exponential moving average the stock then posts a massive-volume gap-up move which is imminently playable as a BGU. It spends a week holding tight and then begins to trend higher along its 20-day exponential moving average.

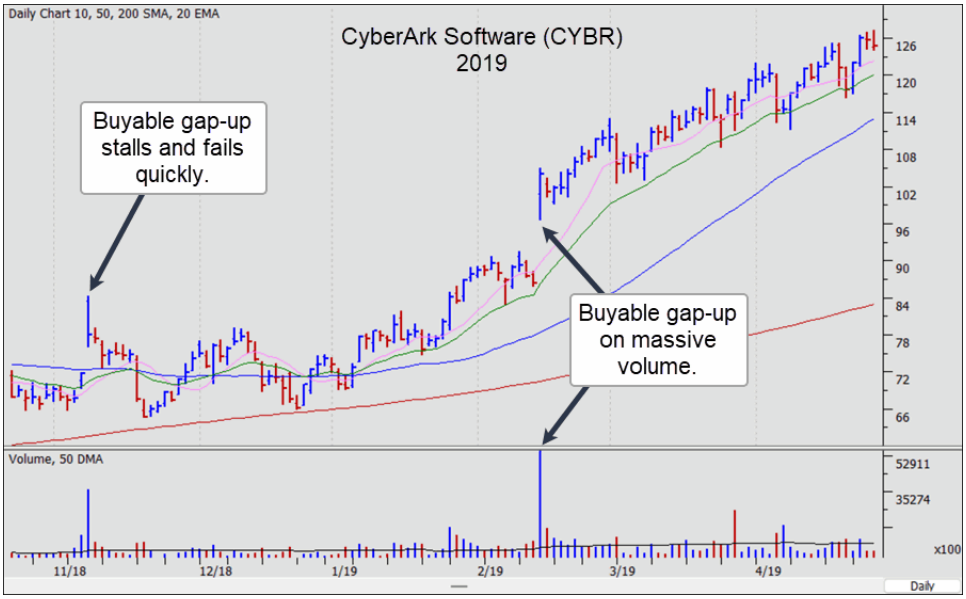


Figure 2.16 - CyberArk Software (CYBR) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Chapter 2: OWL Variants

Not too long after *Trade Like an O'Neil Disciple* was published, I began to observe certain variants of the pocket pivot and the buyable gap-up that were appearing in various forms.

Five-Day Pocket Pivots

As the name suggests, this type of pocket pivot occurs when the volume is higher than any down-volume day over the prior *five* days instead of the usual ten that we use for a standard pocket pivot. All we are doing here is taking the list of Pocket Pivot rules shown in Part 1 of this chapter and changing every instance of the word *ten* in that paragraph to *five*. Easy enough.

Another characteristic I look for is that I want to see these five-day pocket pivots occur in *clusters* of two or more. Sometimes, when there are several clustered together during a weak market period, it can be a useful indicator of constructive action. Ron Brown of HGS Investor Software created a special chart view for me that highlights five- and ten-day pocket pivot volume bars in blue, making it quite easy for me to pick these out as a scan through my watch lists.

When a stock is moving sideways within a consolidation, and it starts to show more of these blue-highlighted volume bars it gives the impression of *percolating action* as the volume patterns begin to develop bullishly. If this is preceded by several days where the stock is *flattish* or even slightly down as volume dries up to extremely low levels, the proverbial VDU or VooDoo type of action as I call it, it can provide clues of impending upside.

Examples:

In March 2021 Russia invaded Ukraine, impacting the availability of commodities like aluminum, copper, and steel, among others. This set off a thematic move in industrial metals stocks like steel producer

Steel Dynamics (STLD) (Figure 2.17). Here we see three five-day pocket pivots occur along the 10-day simple and 20-day exponential moving averages.

I view moving averages less as rigid lines in the sand, so to speak, and more like *fuzzy* zones not unlike how quantum physics views the location of electrons as they move around an atom's nucleus. Sometimes the 10-day and 20-day lines can move together in parallel or semi-parallel fashion, creating a support zone in between.

That is what we see here as these five-day pocket pivots occur within the zone between the 10-day and 20-day moving averages. What is important here is not necessarily that the stock is holding tight along a single moving average, but also the tightness of the movement as the stock remains within a well-defined consolidation.

I do not necessarily view five-day pocket pivots as immediately buyable. The pocket pivots instead alert me to the stock's action as it moves tight sideways and so I will then monitor the stock to watch how it develops. When it finally runs into support along the 20-day exponential moving average a week later and shakes out along the line, it is ready to move, and off it goes, posting a low-volume intraday pullback to the 20-dema exactly four days after the third five-day pocket pivot.

STLD is a perfect example to start with because it highlights what I consider the best way to utilize five-day pocket pivots. That is as an indication of constructive action that bears watching for a timely and opportunistic entry that may occur immediately or which may require a few more days to *percolate*.

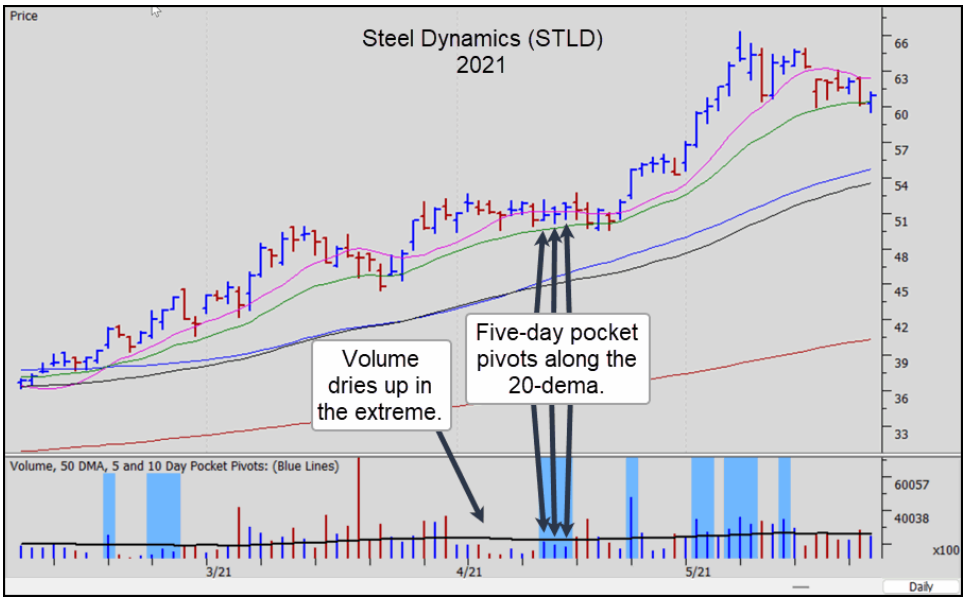


Figure 2.17 - Steel Dynamics (STLD), daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

The example of **ZScaler (ZS)** in August 2021 (Figure 2.18) shows a situation where three five-day pocket pivots are posted in a row as the stock starts to trend off support at the 20-day exponential moving average and up through the 10-day moving average. The difference between ZS and STLD, above, is that in this case the stock is showing strength – each five-day pocket pivot takes it slightly higher.

This lift begins occurring right after volume dries up in the extreme. Note that the day just before the first five-day pocket pivot shows an extreme volume dry-up, which on its own is an OWL long entry point. Thus, by the time ZS clears the 10-day line on the second five-day pocket pivot it may become buyable along the 10-day line with the idea that one may have taken an initial position right along the 20-dema the day before the five-day pocket pivot sequence began.

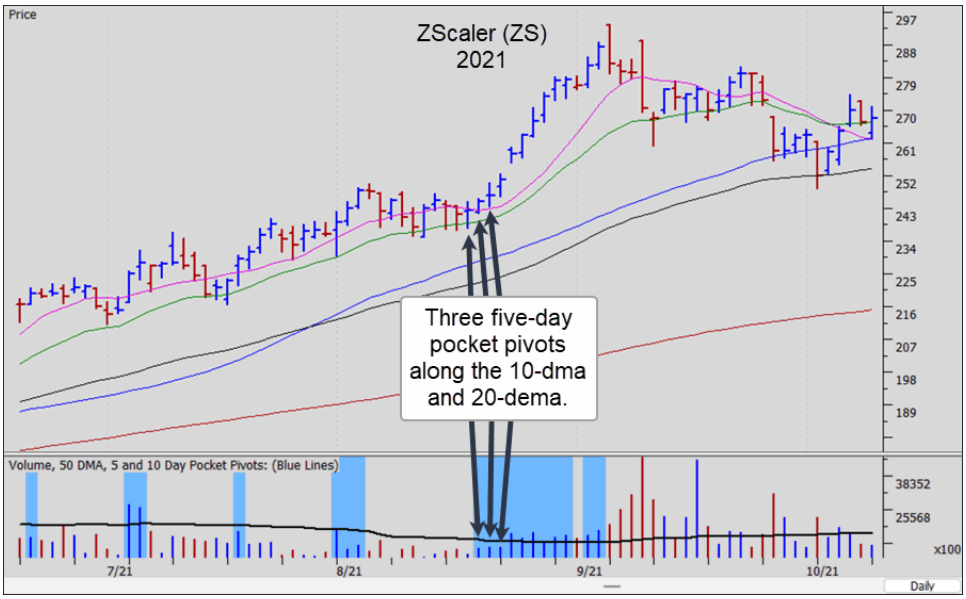


Figure 2.18 - ZScaler (ZS), daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

We see a similar type of extreme volume dry-up in **Nvidia (NVDA)** in October 2021 (Figure 2.19). This occurs along the 10-day moving average as well as the black 65-day exponential moving average (65-dema). I find the 65-dema to be a useful additional moving average to have on my charts as often a pullback that does not hold support at the 50-day moving average may be holding support at the 65-dema.

NVDA then posts two five-day pocket pivots, one off the 10-day line and one as it comes up through the 50-dma. Within the context of the extreme volume dry-up occurring lower along the 10-dma and 65-dema a few days earlier, it is possible to take a position along the 50-dma while using it as a tight selling guide.

Other contextual factors to consider when interpreting this chart are the shakeout along the 65-dema seven days before the first five-day pocket pivot which is then followed by tight sideways action along the 10-dma and 65-dema as volume dries up in the extreme. By putting all these puzzle pieces together, one could have been buying NVDA

along the 10-dma and 65-dema and then adding on the second five-day pocket pivot at the 50-day line.

NVDA then slowly edges higher before gapping to higher highs on a typical buyable gap-up (BGU) move on the eighth day after the second five-day pocket pivot. I emphasize that there is nothing mechanical about the use of five-day pocket pivots. They must be interpreted within the context of the overall chart as well as the general market environment.

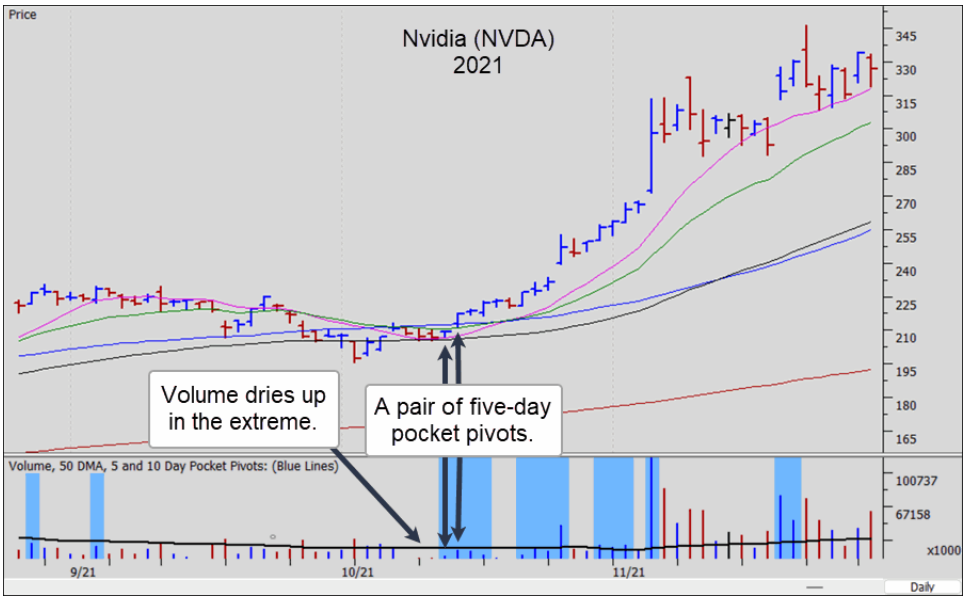


Figure 2.19 - Nvidia (NVDA) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Alcoa (AA) in December 2021 (Figure 2.20) is another interesting example as the five-day pocket pivots all occur on above average volume, and they occur right after the stock shakes out along the lows of its base. In a case like this the strong volume is a positive indication, but for some reason, likely contextual in nature, the stock cannot get going. This was not an unusual occurrence given that during the Age of QE one-day shows of upside strength on strong volume would often go nowhere.

Contextually, however, note that the first five-day pocket pivot was followed by two days of pullbacks that came on extremely light

volume. The second five-day pocket pivot came on heavy volume, but the next day it came in to test the 10-dma, 20-dema, and 50-dma where one could have taken a position while using the three moving averages as tight selling guides.

The day after the second five-day pocket pivot was buyable on that basis, and by the close it played out as a third five-day pocket pivot. From there AA gapped slightly higher and then broke out to higher highs four days after the third pocket pivot. Note that the action after the breakout showed little upside impetus as the stock chopped around, and any breakout buyer would have easily been thrown out of the stock at a loss when it came in sharply to test the 50-day moving average in late January 2022.

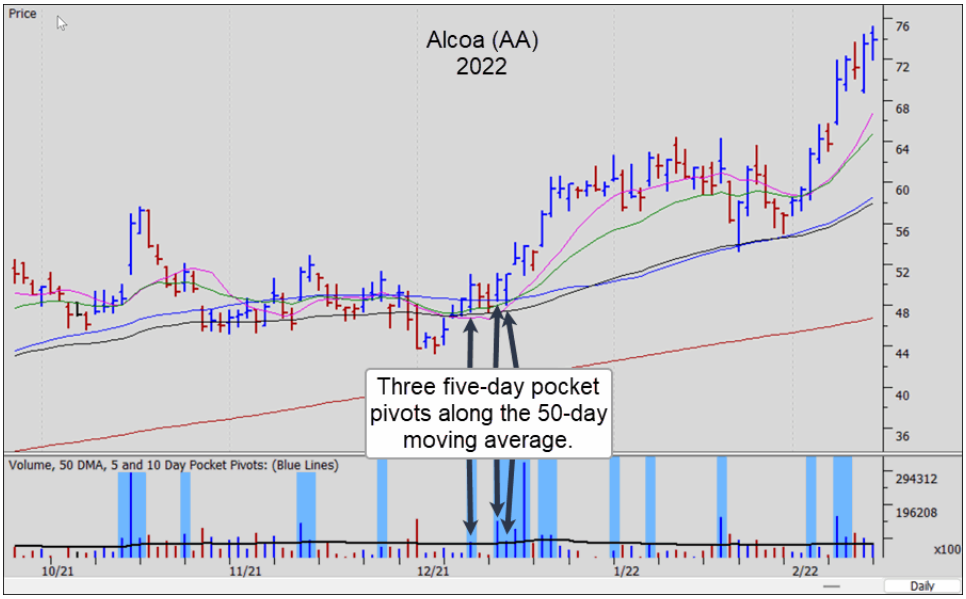


Figure 2.20 - Alcoa (AA), December 2021 – January 2022. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

To summarize, five-day pocket pivots are no different from ten-day pocket pivots except that they only need to have volume higher than any down-volume day over the preceding five trading days. They are also most useful as interpretive indicators when combined with other types of contextual price/volume action, such as low-volume consolidations. For this reason, they are often not immediately

actionable, but may indicate *percolating* price/volume action leading up to a potential price move higher, thus hinting that we should vigilantly monitor the stock for an optimal entry point when used with other OWL indicators like the VDU.

Voodoo Pullbacks (VDU)

Before continuing with the other OWL variants, it is useful to explain VDU or VooDoo pullbacks. I first described *VooDoo* action back in 2004 when I co-authored with Bill O'Neil the short-selling treatise, *How to Make Money Selling Stocks Short* (John Wiley & Sons, 2004). In that book, however, I was referring to volume drying up in the extreme as a stock moved *higher*, usually up into moving average resistance. As a short seller, that is often where I looked for opportunistic short entries right into these low-volume rallies as they approached, met, or slightly exceeded moving average resistance.

The term comes from the acronym VDU, which I saw written all over the *Model Book of Greatest Winning Stocks* chart books that Bill O'Neil created and used. He marked these up like someone afflicted with a chart-oriented version of obsessive-compulsive disorder, but these annotations possessed a wealth of information if you studied them carefully. When I ran money for Bill O'Neil, he allowed me to borrow his model books and study them.

During my examinations of Bill's model books, I saw the letters VDU scribbled all over charts at points where volume levels had dried up sharply, indicating a lack of selling pressure. I eventually turned VDU into a two-syllable word, "VooDoo" which is easier to say compared to the three-syllable acronym VDU. On the other hand, the three-letter acronym VDU is easier to write than VooDoo so I use both interchangeably in this book.

The original VDU concept was applied to the short side of rallies like that seen in MicroStrategy (MSTR) (Figure 2.21) in late April 2021. Note that the stock had failed from a bear flag "shake-in" in mid-April and promptly failed. It then rallied off support along the early and

late March lows on light volume that declined day by day until the stock reached the 20-dema on a volume bar that is virtually invisible on the chart below. That marked the end of the rally, which gave shorts a clean re-entry or even an initial short-sale entry point at the 20-dema.

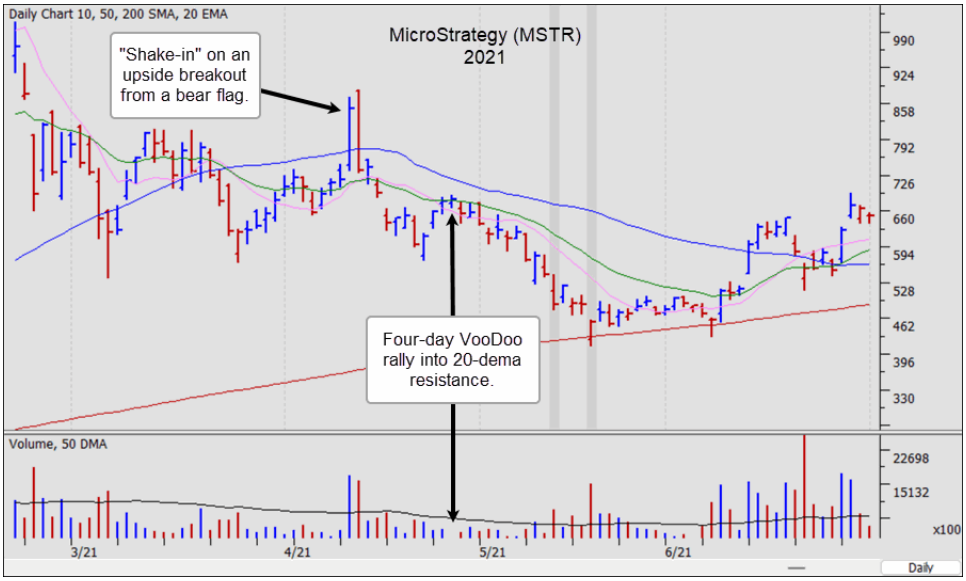


Figure 2.21 - MicroStrategy (MSTR) in 2021 shows the original concept of a voodoo rally where a short-sale target stock rallies back up into a moving average on extremely light volume. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Examples:

VDUs are often used in conjunction with other signals. For example, **Square (SQ)** (Figure 2.22) in April 2017 posted a VooDoo pullback to its 20-day exponential moving average four days after it posted a pocket pivot. While the initial pocket pivot was a sign of strength, the shrewd OWL trader takes the opportunistic approach of entering on the extremely low-volume pullback to the 20-day exponential moving average which is then used as a tight selling guide.

One major point about using moving averages as selling guides: I do not view moving averages as hard lines in the sand, or rather the concrete, but more as *fuzzy zones*. For this reason, one should also

determine whether to allow for some porosity or movement a little further below the moving averages, say 1-3%, when setting a stop-loss point. This, of course, depends on one's risk-tolerance as well as an assessment of how volatile the stock in question might act.

Following the VDU pullback, SQ then launches higher from there and eventually breaks out of a seven-week base a week later. This is an excellent example of how the pocket pivot three days prior to the VDU pullback was a show of near-term strength that in my approach would have flagged the stock as one to watch for any opportunistic pullback as volume declined.

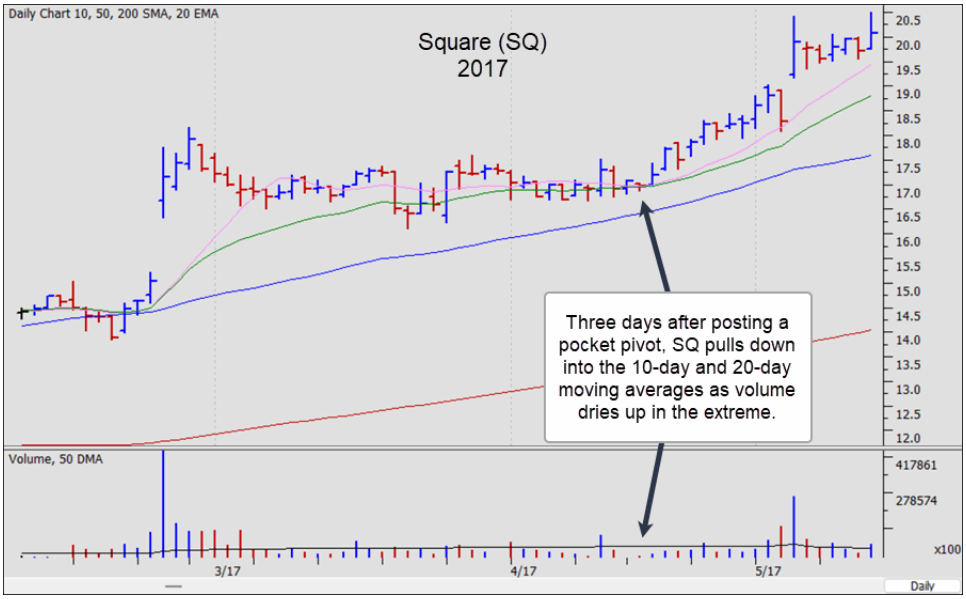


Figure 2.22 - Square (SQ) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Netflix (NFLX) (Figure 2.23) in mid-2018 is another textbook example of VDU pullbacks providing opportunistic, lower-risk long entries. The first occurred in early May along the 50-day moving average after which the stock moved slightly higher and again began to consolidate in a very tight, sideways pattern. It tested the 20-day exponential moving average in mid-May as volume decline to -64.84% below average.

At that point one can easily surmise that sellers have likely disappeared and taken a position on that basis. The 20-dema is then used as a tight selling guide. NFLX immediately began to move higher the next day and then broke out two days later. In this manner one can gain an edge by entering early based on the VooDoo price/volume action along the 20-dema. One can then choose to add on the breakout with more confidence given the lower cost-basis for portion of the position taken at the 20-dema.

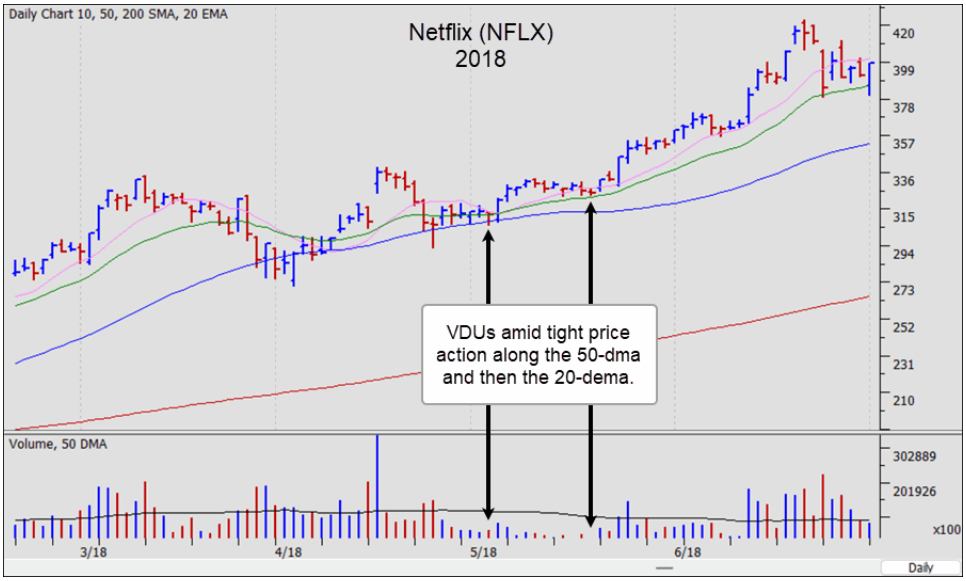


Figure 2.23 - Netflix (NFLX) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Another textbook example is found in **Tesla (TSLA)** (Figure 2.24) during May and June 2020. After a short uptrend into early April 2020, TSLA began to consolidate. Initially, some of the action was on the volatile side as we see a heavy-volume two-day sell-off in late April where the stock runs into moving average support at the 20-dema and then rights itself. From there TSLA starts to tighten up and becomes excruciatingly so as we progress into the latter half of May 2020.

There is a sequence of five VDU pullbacks in that area of the chart, but notice we also see two five-day pocket pivots at the points labeled 1 and 2 in green, and then a ten-day and a five-day pocket pivot at

the point labeled 3. Those lead to a breakout that is below average, but that does not present a problem for any buyer who was focused on the VDU pullbacks and entry points *within the base*.

TSLA then pulls back one more time to the 10-day moving average in early on the fifth VDU pullback in the pattern and then bounces off the line to higher highs. Notice that heavy buying volume does not come into play until the stock is up and away at which point it pulls in to test the 10-dma and 20-dema as mid-May approaches.

In this example we see how one only needed to operate based on the VDU pullbacks in combination with five-day and ten-day pocket pivots to determine valid entries. Sitting around waiting for a breakout on heavy volume was not feasible at all since volume did not start to come into the stock until four days after the fifth VDU pullback and in an extended position from the breakout.

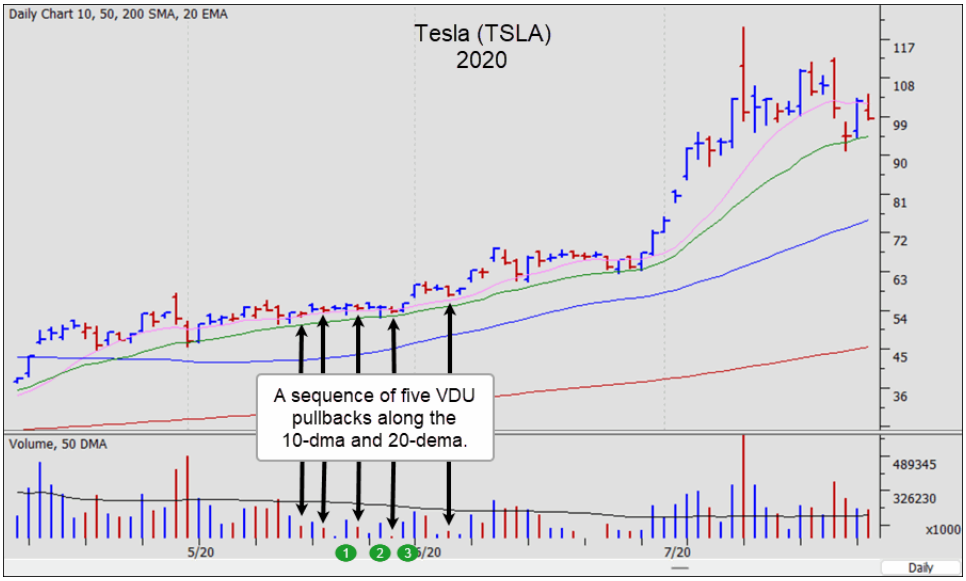


Figure 2.24 - Tesla (TSLA) daily chart, 2020. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

In addition to my colleague Chris Kacher's and my outstanding play in silver when it ran from the mid-teens to $50 an ounce in 2010-2011, I also played a nice move in silver during 2020. While I used the **Sprott Physical Silver Trust (PSLV)** (Figure 2.25) to play the

move, I show the chart of the **iShares Silver Trust (SLV)** since it is more familiar to most investors. However, I tend to favor gold and silver ETFs and ETNs that are directly backed and convertible into physical metal as a rule.

Starting from the left side of the chart we see the uptrend into early May 2020 that is met with some selling and a little bit of turbulent price action. SLV weathers that and then begins to consolidate as we head into summer 2020. Note that it tightens up considerably before posting several extreme VDU pullbacks along the 10-day simple and 20-day exponential moving averages. Study the chart more closely and you will also notice several five-day and ten-day pocket pivots, all of which serve to highlight the nascent strength of the white metal as it percolated along its 10-day and 20-day lines.

Eventually silver, and its yellow metal cousin, gold, went into parabolic moves in July 2020 that ended with silver falling just short of $30 an ounce and gold hitting an all-time high of $2,074.88 an ounce. An interesting sideline to this story is that Warren Buffet, who historically has shunned gold as a *pet rock*, as he put it, was suddenly buying gold and gold stocks in August 2020. This made silver (and gold, for that matter) an easy sell into the parabolic move that saw silver top out at $29.26 an ounce. Within the context of this parabolic, climactic type of move, the news of one of the biggest gold critics throwing in the towel and buying the yellow metal was almost too textbook as a sell signal for silver and gold as well.

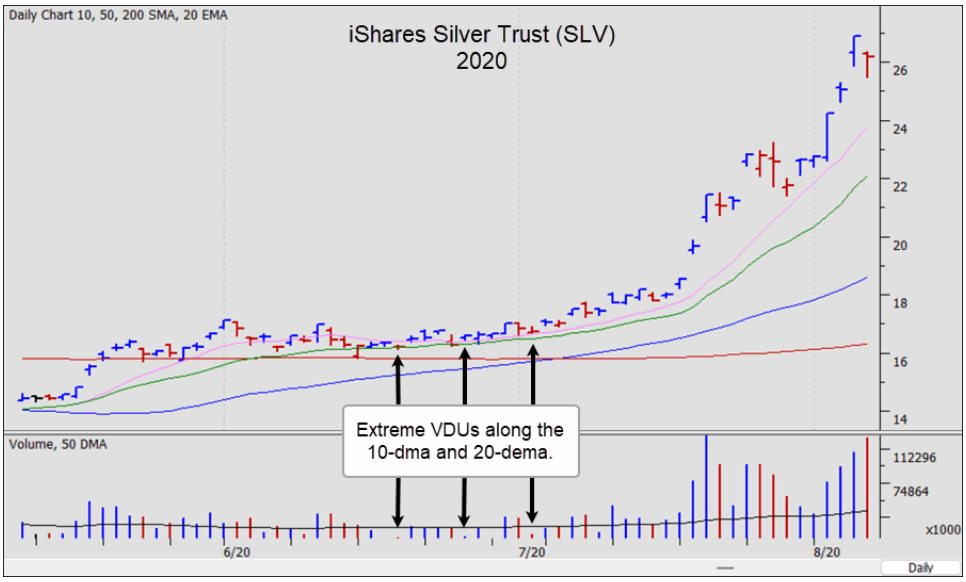


Figure 2.25 - iShares Silver Trust (SLV) daily chart, 2020. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

When stocks are moving tight sideways and flashing VooDoo/VDU days the action is generally easy to pick out, especially when combined with pocket pivots simultaneously occurring within the pattern. But they can also work well in other situations. Often, powerful moves will have pullbacks where secondary entries occur not on strength but on VDUs along potential moving average support. With respect to market context, these types of moves generally have a very powerful thematic driver.

In the case of **Riot Blockchain (RIOT)** (Figure 2.26) in 2021 it was the tulip-like mania over cryptocurrencies and the related stocks. The initial uptrend along the 10-day moving average from November 2020 to January 2021 was very steady to the upside with short three- to four-day pullbacks at most. The first serious pullback occurred in the latter half of January as RIOT began to pirouette around its 20-day exponential moving average.

Finally, as the market headed into February, RIOT held tight right at the 50-day line as volume dried up in the extreme. That was your entry, and it then shot radically higher from there. If you review this chart after reading the rest of this book you will notice a *miniature*

undercut & rally (U&R) set-up along the lows of the pullback which occurs three days prior to the VDU entry point. More on U&Rs later.

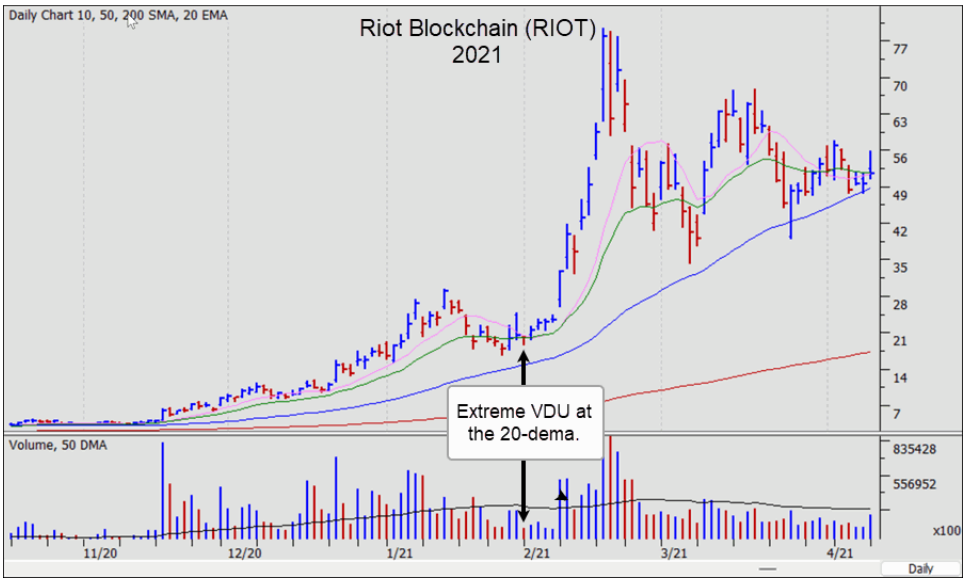


Figure 2.26 - Riot Blockchain daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

A similar type of situation is seen in **Snap (SNAP)** (Figure 2.27) during early March 2019. A massive-volume buyable gap-up in early February continued to drift higher until it gapped higher once more in mid-February. That was more of an exhaustion type of move and so SNAP corrected as it was certainly entitled to. What makes this quite interesting is that the pullback has the look of falling out of bed as SNAP suddenly snaps out of the tight sideways action along the 10-day line, even after posting a VDU at the line. If one had taken a position, there then a sell signal was likely quickly issued.

Volume selling hits the stock as it breaks the 10-dma but then immediately turns up sharply right at the 20-dema and 200-dma. An opportunistic OWL-style trader would view this as a potential shakeout and therefore buyable along the two moving averages. Risk can certainly be mitigated by using the 20-dema and 200-dma as tight selling guides, just as one would have used the 10-dma on the first VDU Day, so the trade was viable unless and until it failed.

It did not, and SNAP rallied back to the upside before breaking out on another buyable gap-up four days later. Study the chart further and you will see that it later posted several VooDoo days along the 10-dma in late March and early April 2019.

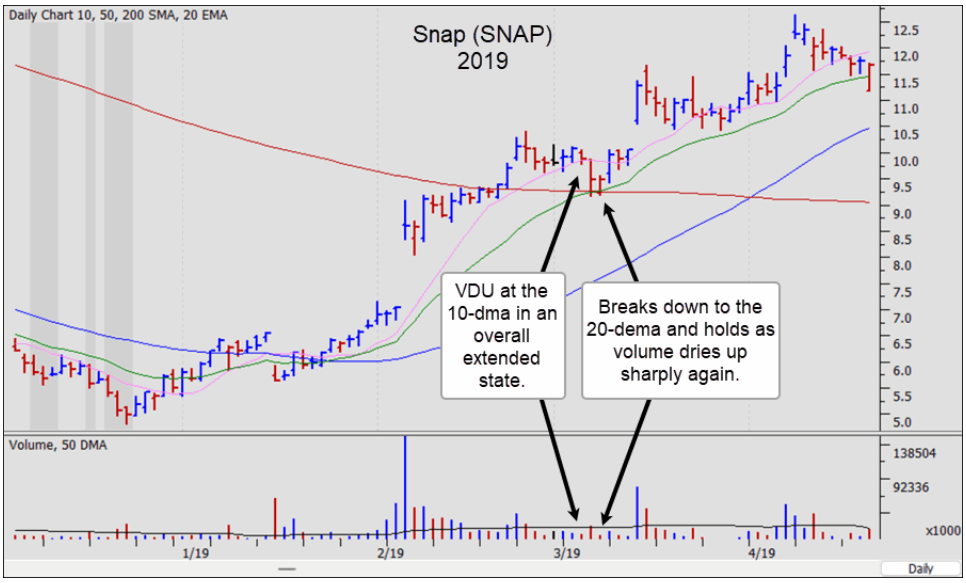


Figure 2.27 - Snap (SNAP) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

In 2018 the *Weed Patch* had sprouted, essentially a group of companies in the cannabis cultivation business that came public during that time in response to relaxed marijuana laws across the globe. One of the biggest winners of that powerful THC-infused thematic was **Tilray (TLRY)** (Figure 2.28) which came public in July 2018. A green gold rush ensued as investors flocked into this nascent industry space.

TLRY obviously benefited from a very strong thematic driver as most investors were persuaded that big money was to be made mining green gold. At its peak, I was even approached with an offer to invest $1 million in a cannabis farm that would operate in the desert community of California City, California. Frankly, I just did not see the potential for profit margins that would justify such an investment. But that kind of number-crunching did not stop the profit margins that came from trading TLRY stock, and I preferred to keep my cannabis investments limited to the stock market. After all,

why get bogged down in all the operational expense as a grower when you could just trade the stocks?

TLRY came public in July 2018 and had the typical multi-day post-IPO run-up before pulling back and forming its first base. This has the textbook tight sideways action where we see a VDU occurring amid some extremely narrow price ranges and tight price closes along the 10-day moving average. However, the chart had no 20-day exponential moving average while one also had to interpret volume relative to prior volume in the chart since there was no 50-day moving average of volume.

We can see that three days after the VDU Day TLRY tried to push higher but stalled. That was then followed by a sharp downside break through the 10-dma, but volume was exceptionally light on that shakeout. Notice also that the close is near where the 20-dema starts to form the next day, so could be interpreted as a VDU at the 20-day line. The next day TLRY posts a healthy-volume pocket pivot and proceeds to trend higher from there.

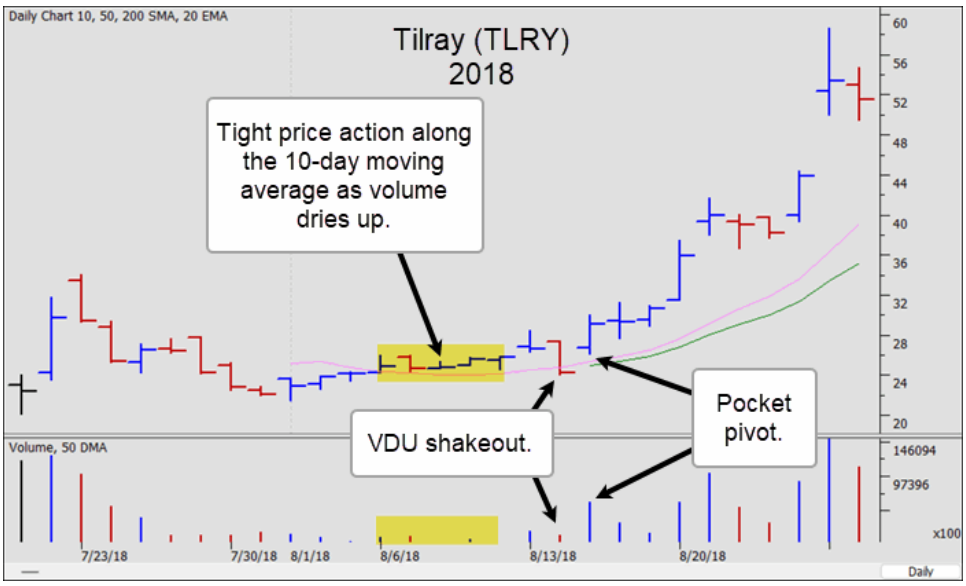


Figure 2.28 - Tilray (TLRY) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

In January of 2019 website building service **Wix.com Ltd. (WIX)** (Figure 2.29) was on a tear as it accelerated into a near-term climactic run that finally peaked out mid-February. At that point WIX was up

seven days in a row and twelve out of the last fourteen days in a row. It then gapped down big after earnings on February 20th despite reporting a 163% increase in earnings. It then slowly worked its way down to the 50-day moving average in early March.

At that point, all the sellers that hit the stock after earnings in February disappeared. Selling volume dried up in the extreme as WINX moved tight sideways along the 50-day line while posting two VDU days at the moving average. That action provided several entry opportunities along the 50-dma towards mid-March with the simple idea of using the 50-day line as a selling guide. A few days later, WIX launched higher and then formed a short cup-with-handle, before trending higher.

If one were looking to buy WIX solely on the idea of looking for a cup-with-handle breakout one missed a good chunk of the move off the 50-day moving average. The OWL VDU entry enabled one to capture more of the overall price move by gaining an early entry to which one could have added on the ensuing cup-with-handle breakout in April



Figure 2.29 - Wix.com (WIX) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

As we have seen, voodoo pullbacks within consolidations are some of the easiest to buy. Here we see high-performance PC gaming headset maker **Turtle Beach Corp. (HEAR)** (Figure 2.30) posting a sharp run-up in early May 2018 before forming a three-week flag formation. Within that flag, HEAR posted two VDU pullbacks, one that was -58% below average volume and the second -45% below average volume.

It then broke out on a pocket pivot volume signature in early June but only rose slightly before forming another three-week flag formation. I suppose one could call it a flag-on-flag formation, although others may try and invoke the mythical "high, tight flag" that Bill O'Neil supposedly identified. Bill essentially cherry-picked a handful of examples from the past over a span of nearly a hundred years, thirteen in all, and wrote about them in his book, *How to Make Money in Stocks* as if they were automatic guarantors of immediately massive upside gains.

The bottom line is that labeling a chart as this or that has zero predictive value when proper statistical sample sizes (100 examples or more) are examined. A few examples over the years do not provide prima facie proof of a pattern's reliability or ultimate outcome. We can only determine constructive action as it unfolds in the moment and thereby draw conclusions that in turn drive real-time trading decisions. In the HEAR example, all one needed to do was identify the voodoo pullbacks in both flag formations and take long positions at those points.

Once that is done one can use breakouts as add points and let the stock play out as it will. Trying to impose some idea that it *fits* the definition of the so-called O'Neil high, tight flag and will therefore automatically lead to massive upside gains is not recommended. In fact, note that while HEAR had a decent upside move following the formation of this flag-on-flag pattern it certainly did not amount to hundreds of percent of upside profits before topping and rolling back to the downside in the late summer into fall of 2018.

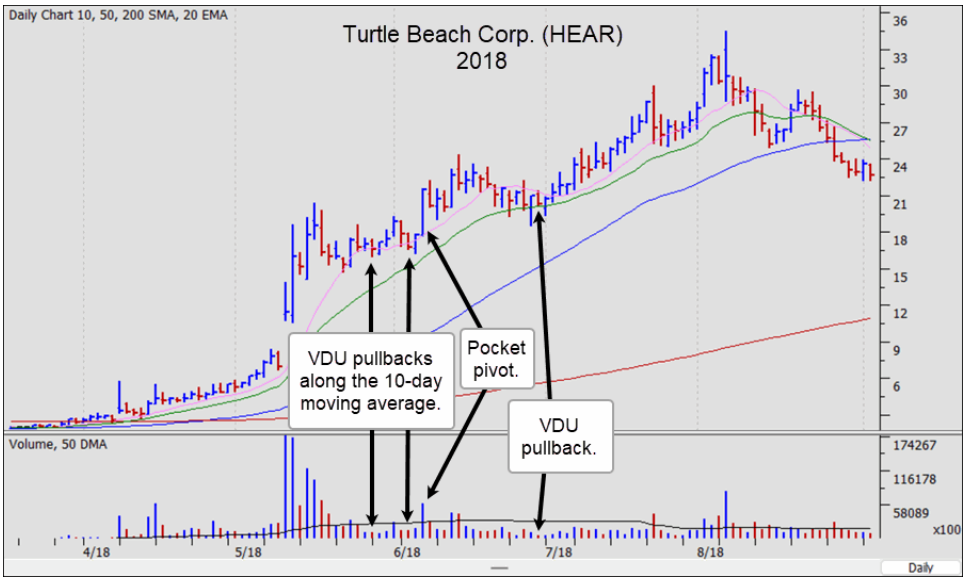


Figure 2.30 - Turtle Beach (HEAR) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

We should also understand that while VDU or voodoo long entry points are useful, they are not always reliable. This is why reasonable risk-management techniques must be imposed. Generally, when a VDU Day occurs along a moving average, I will use the moving average as a tight selling guide. In some cases, I may also add 1-3% additional downside to account for porosity since moving averages in practice do not necessarily act like hard lines but more like *fuzzy zones*.

Stitch Fix (SFIX) (Figure 2.31) is a typical example of a failed VDU Day. In November 2017 the stock came public and began trading as a very hot IPO that immediately shot higher. At that point SFIX formed a four-week flag formation before breaking out in a powerful one-day price move. That move lasted all of one day, the type of move that I have often referred to as a *one-day wonder move*; basically a big-volume upside price spike that has a very short half-life of one, single day.

That was certainly the case with SFIX's breakout in this example, as the stock immediately stalled and turned tail. It broke below the new-high breakout point in the prior four-week flag formation and held support along the 20-day exponential moving average for the next two weeks before posting a VDU Day at the 20-dema in mid-January 2018.

Like the TLRY example, SFIX was a recent IPO at that time so had no 50-day moving average of volume on the chart. Note that the 50-day does not show up until late January. But, as with the TLRY example, one can compare relative volume to what the stock has traded daily since coming public whether that is even just a few days or weeks. When SFIX posted the VDU Day at the 20-dema in mid-January it traded 203,000 shares, the lowest daily volume in its short two-month trading history.

Once it decisively breaks the 20-dema the position is stopped out, hopefully limiting any downside damage to 3-5% at the most. I prefer to operate this way as opposed to giving the stock a wide berth of 7-8% per O'Neil or 10% per Livermore before stopping out of the position.

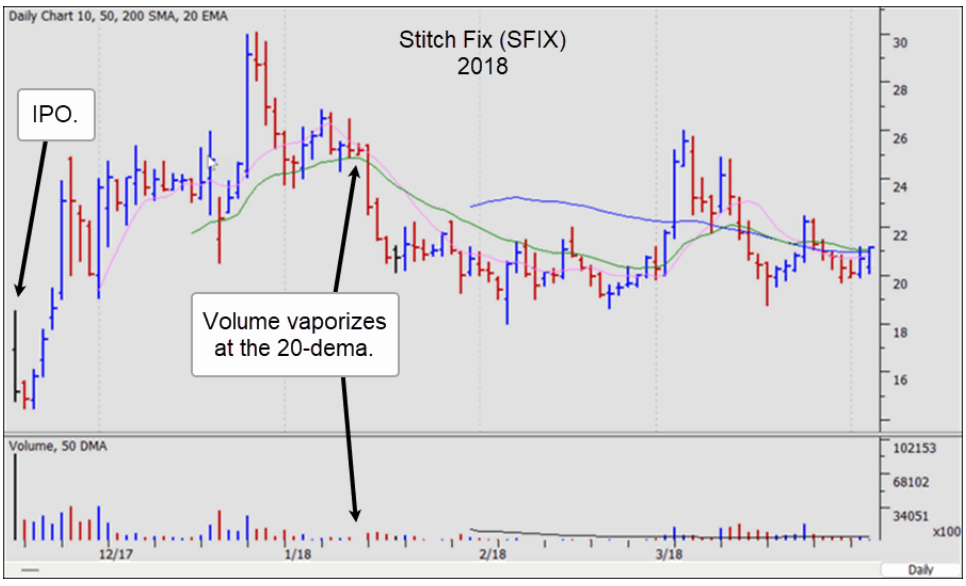


Figure 2.31 - Stich Fix (SFIX) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Bottom-Fishing Pocket Pivots

Bottom-fishing pocket pivots occur very near to the absolute lows of a chart pattern or after a period after which the stock has rounded out the bottom of a potential new base and may be starting to move up the right side. If the stock is nearer to the absolute lows, I will refer to it as a *bottom-fishing* pocket pivot, but if it has spent some time moving sideways with a slight bias to the upside, rounding out the lows of a new base, I will refer to it as a *roundabout* pocket pivot. Either way, the concept is the same: a pocket pivot occurring nearer to the lows of a pattern and often well below the major moving averages such as the 50-day and 200-day.

Chinese social-networking concern **Momo (MOMO)** (Figure 2.32) back in late September 2015 illustrates a typical bottom-fishing pocket pivot chart position. This one is coming up through the 10-day moving average which sits well below its 50-day and 200-day moving averages. The pocket pivot begins from a point just below the 10-day line and then pushes up through the 20-day exponential moving average. The following day MOMO streaks higher before reversing at 50-day moving average resistance.

If one were quick on the draw here, then entries could have been taken near the 10-day line and then just above the 20-dema on the day of the pocket pivot. That would put one in a position to profit from the rapid move up to the 50-day line. At that point, selling at least a partial position into what played out as a high-velocity 20% move in two days was prudent.

MOMO gave swing-traders another entry as it then pulled back into the 20-dema with volume drying up sharply. That also represents about a 50% retracement, and a long position could have been re-entered there using the 20-dema as a tight selling guide. An interesting example of a bottom-fishing pocket pivot that set up two potential lower-risk long entries before it settled down and MOMO slowly drifted higher.

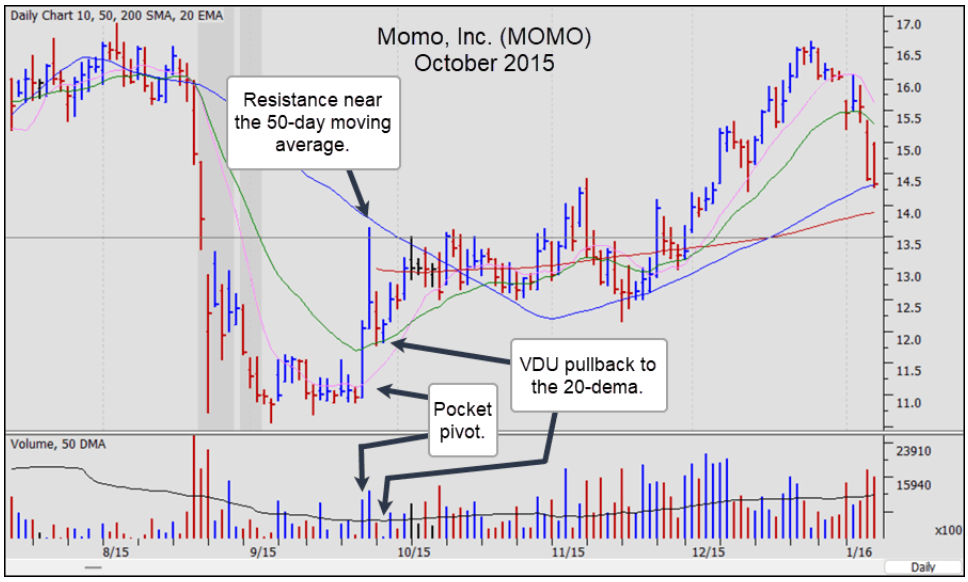


Figure 2.32 - Momo, Inc. (MOMO) daily chart, 2015. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Bottom-fishing pocket pivots, as opposed to roundabout pocket pivots, are what I call U*gly Duckling* set-ups because by virtue of occurring near the absolute lows of the pattern they look quite ugly. **Adobe Systems (ADBE)** (Figure 2.33) without question appears quite ugly in September 2015. In fact, after a five-day cascading sell-off that ended August 24, 2015, a day known as the *Flash Crash* of August 2015, ADBE found its feet and began to bounce. The flash crash occurred after U.S. markets had already been selling off for several days and was prompted by an 8.5% overnight decline in the Chinese Shanghai Composite Index. Study the chart of MOMO, above, and you will see that it was also a victim of that particular crash.

With Chinese markets down big overnight, sellers swarmed the market as buyers pulled their bids, creating a massive air pocket underneath stocks of all stripes. Instantaneous declines of 10-20% or more flashed across traders' quote screens before the market found its feet and began to bounce. Note that this created a powerful market context in the form of a climactic, panic low as sellers who hit the market were washed out all at once.

The flash crash hurled ADBE through its 200-day moving average but it quickly regained the 200-day line once sellers had been washed out in the panic low. Nervousness still remained, however, as the stock bounced around at even reversed at its 50-day moving average two weeks after the flash crash low, looking like a ripe short-sale target.

But it found support along the 10-day moving average where volume declined, and a pocket pivot then sprouted. ADBE slowly and eventually moved to higher highs from there, albeit with much volatility, but once posting that pocket pivot along the 10-day line it never looked back. In this case it was important to evaluate the set-up within the context of the August 24th panic low in order to assess its odds of success. At the very least, if it failed, the 10-day moving average offered a very tight selling guide that kept the risk quite manageable.

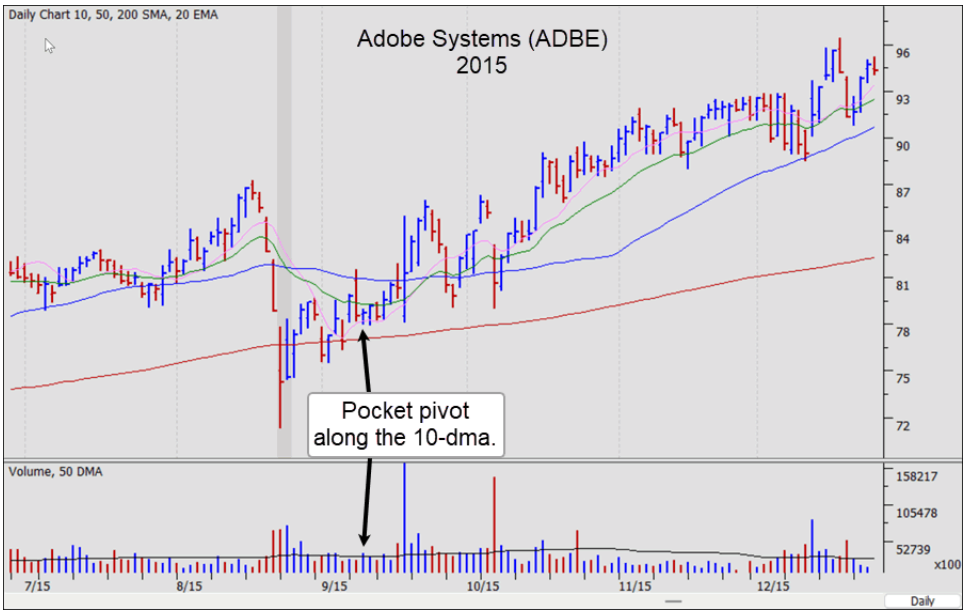


Figure 2.33 - Adobe Systems (ADBE) daily chart, 2015. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Alert readers will notice that the lows seen on the charts in MOMO and ADBE above are accompanied by vertical darker gray bars on the charts. Those are Bingo indicator bars, an oversold indicator created

by my late friend Ian Woodward of HGS Investor Software fame. I incorporate the Bingo indicator into my assessment of a bottom-fishing pocket pivot or any other OWL-style Ugly Duckling set-up.

The chart of **Alibaba (BABA)** (Figure 2.34) in 2016 shows two distinct groupings of Bingo bars in early January and February as the stock was coming down. Finally, a gap-up move off the lows, what I call a bottom-fishing buyable gap-up (BFBGU) that will be discussed in the next section of this chapter, brings the stock back up on top of its 20-dema.

Certainly, at that point, if the 20-dema holds as support, BABA has a reasonable chance of moving higher. When it posts a pocket pivot along the 10-day moving average in late February, the stage is set for a move higher. Indeed, BABA quickly rallies above the 50-day moving average before eventually trending higher from there.

BABA is a good example of how I use proprietary HGS Investor Software indicators in conjunction with bottom-fishing pocket pivots. The reader may have their own favorite oversold indicators that they prefer to use, and I would suggest studying bottom-fishing pocket pivots and other Ugly Duckling set-ups in conjunction with such oversold indicators to understand how these may help their own process.

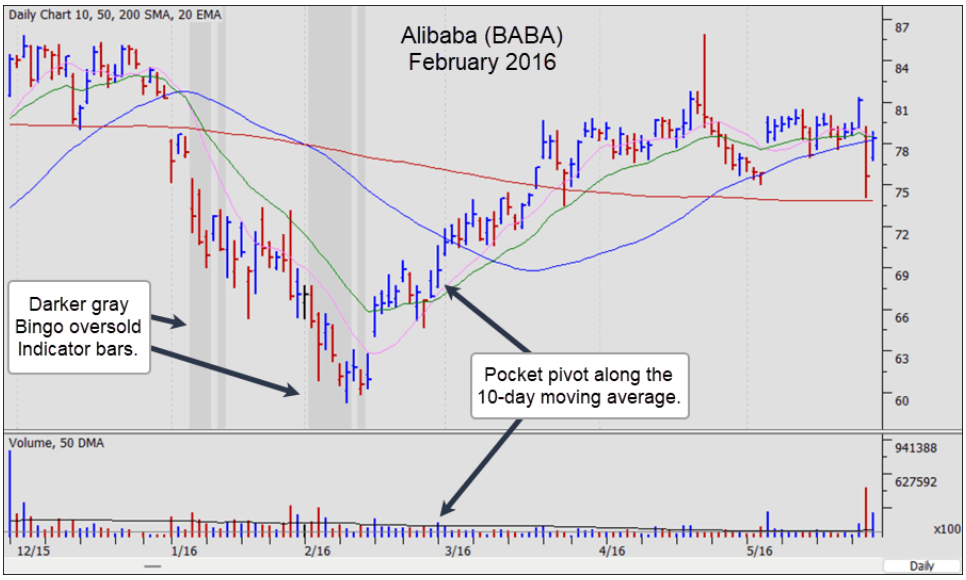


Figure 2.34 - Alibaba (BABA) daily chart, 2016. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Tesla (TSLA) (Figure 2.35) in early December 2016 has a little bit more of a roundabout pocket pivot feel to it as it spends some time bouncing along its late 2016 lows. It even plays out as a short-sale entry at the 50-day moving average on the first rally off those lows before holding price support at those same lows on the ensuing pullback from the 50-day line.

Once TSLA tests price support at the early November lows and turns, it regains the 20-day exponential moving average on a pocket pivot move and then moves tight sideways for three days. On the third day of that tight sideways action, it trades extremely low volume in classic voodoo style and the very next day launches up through the 50-day line on another roundabout pocket pivot. At that point it is full speed ahead for TSLA as it begins to run higher in a sharp uptrend along its rapidly rising 10-day moving average.

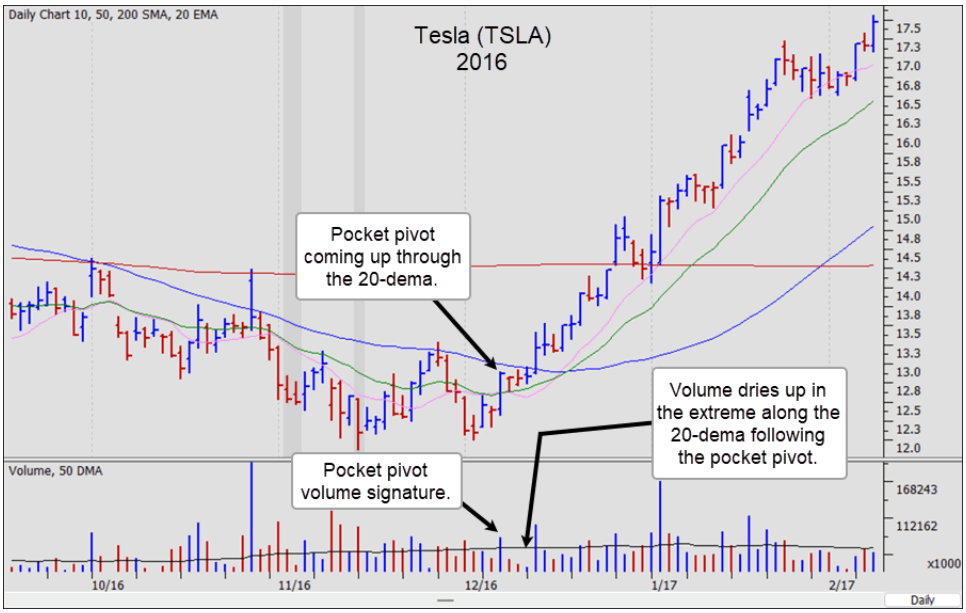


Figure 2.35 - Tesla (TSLA) daily chart, 2016. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

I love this example of **Facebook (FB)**, now known as **Meta Platforms (META)** (Figure 2.36), in early January 2017. After getting chopped up in a general market break in late October and into early November 2016, the stock forms what appears to be a bear flag. The low point is reached in early November at 113.55 and it then flags sideways while setting two additional lows at 114.00 on December 1st, 2016, and 114.77 on December 30th.

Note that the heavy selling volume dissipates from left to right within the bear flag as FB hammers out these three lows. Normally, in a bear flag, I would look for low-volume rallies into the *highs* of a bear flag to gauge the general weakness of the pattern. In this case, FB is showing volume drying up on each subsequent pullback to the *lows*.

That creates an interesting technical context for the pocket pivot that occurs on January 4th, 2017, as FB comes up through the 10-day and 20-day moving averages. While the move stalls slightly, it holds support along the 20-day exponential moving average the next day and moves higher in two subsequent pocket pivot moves in a row. The first one pushes through the 50-day and 200-day moving averages while the second one moves off the two moving averages.

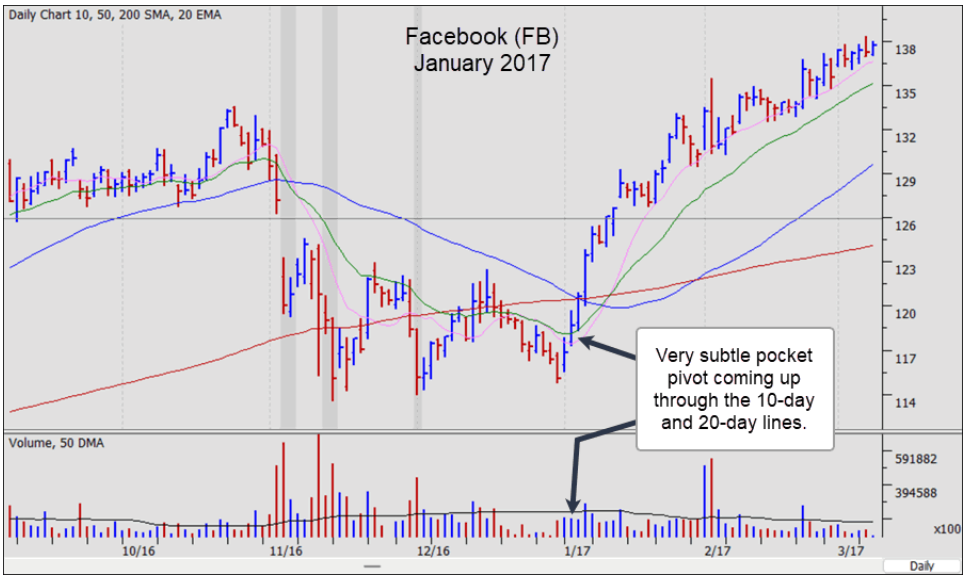


Figure 2.36 - Facebook (FB) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

The market sell-off that hit FB/META in late 2016 also hit **ServiceNow (NOW)** (Figure 2.37) but with a delayed effect. Whereas FB/META broke down in late October/early November 2016 that bout of market weakness did not get to NOW until late November. And as FB/META was forming the second of three lows in what at the time looked like a bear flag in late December 2016, NOW logged a second low as it found support at the 200-day moving average and pinged higher.

Two days up from the test and minor shakeout along the 200-day moving average NOW then posted a pocket pivot first at the 10-day moving average and then as the stock came up through the 20-day exponential moving average later in the day. From there it never looked back. Once it broke out a little over three weeks later it edged slightly higher before coming apart and failing. So, while the standard-issue base breakout at higher highs failed, the OWL entry along the lows provided a reasonable swing-trade back to those highs.

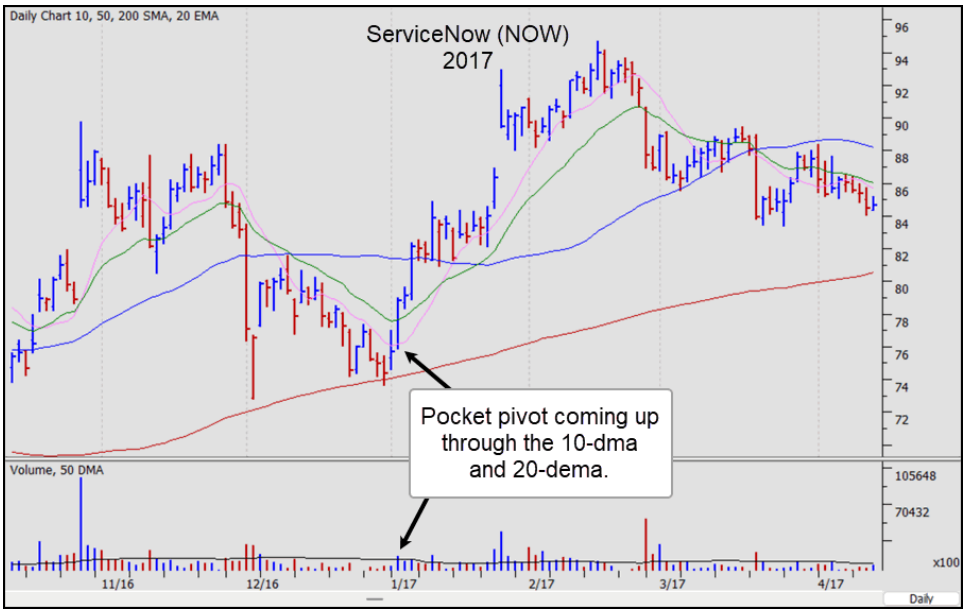


Figure 2.37 - ServiceNow (NOW) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

In late April 2017 **U.S. Steel (X)** (Figure 2.38) released an unfavorable earnings report and suffered a massive gap-down break that took a lot of wind out of the stock. In fact, one could have treated that gap-down move as a typical shortable gap-down short-sale set-up. For more on shortable gap-downs, or SGDs, I refer the reader to my treatise on short-selling, S*hort-Selling with the O'Neil Disciples* (John Wiley & Sons, 2015).

Even though volume was contracting as X moved lower following the gap-down break, the balance of volume remained in favor of the bears. X simply drifted lower as volume continued to dry up. Eventually, a *pivotal point*, as Jesse Livermore might have referred to it, occurred with a pocket pivot as the stock poked its head back above the 10-day moving average for the first time since the post-earnings carnage took its head off.

X never looked back after posting that bottom-fishing pocket pivot off the lows as it zigged and zagged its way higher. Study the chart carefully and see if you can pick out additional pocket pivots that occurred along the way. Those additional pocket pivots also

represented potential entry points for opportunistic OWL-style investors and traders.

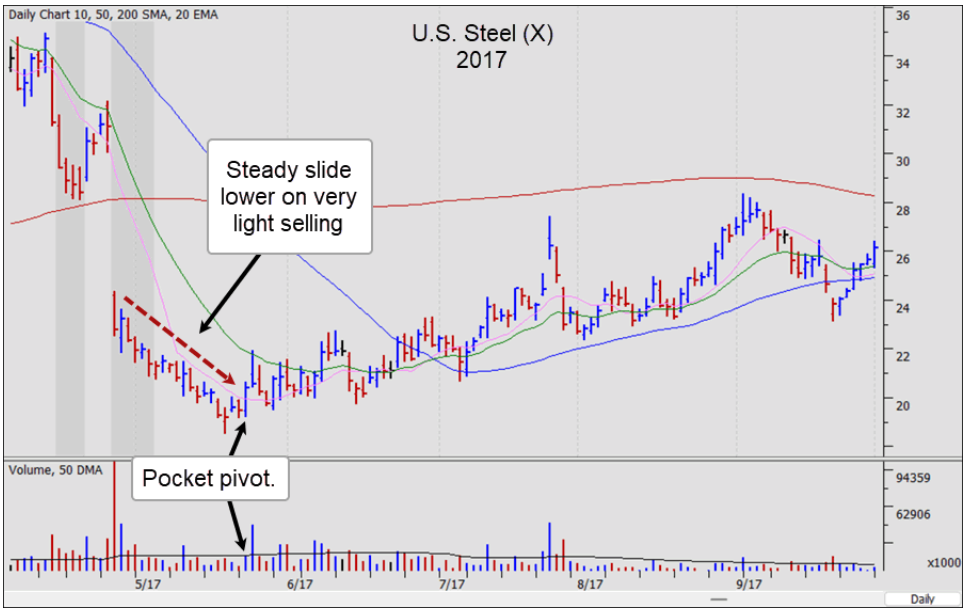


Figure 2.38 - U.S. Steel (X), daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

SunPower (SPWR) (Figure 2.39) broke to fresh lows in March 2017 after a prior failed breakout attempt in late February. The break to lower lows led to the formation of a tight, sideways bear flag. Initially this may be interpreted bearishly. But within the tight little bear flag SPWR posted a pocket pivot along the 10-day line after which it continued to tighten up even more on a closing basis. That led to a stronger-volume pocket pivot three days later, which in fact turned to be a tactical short-sale entry point.

SPWR backed down from there, but shorts were advised to take their profits as it again set up along the 20-dema with volume drying up. From there, the stock edged higher before clearing the 50-day moving average and reversing, where it again set up in an Ugly Duckling OWL long set-up that we will discuss later.

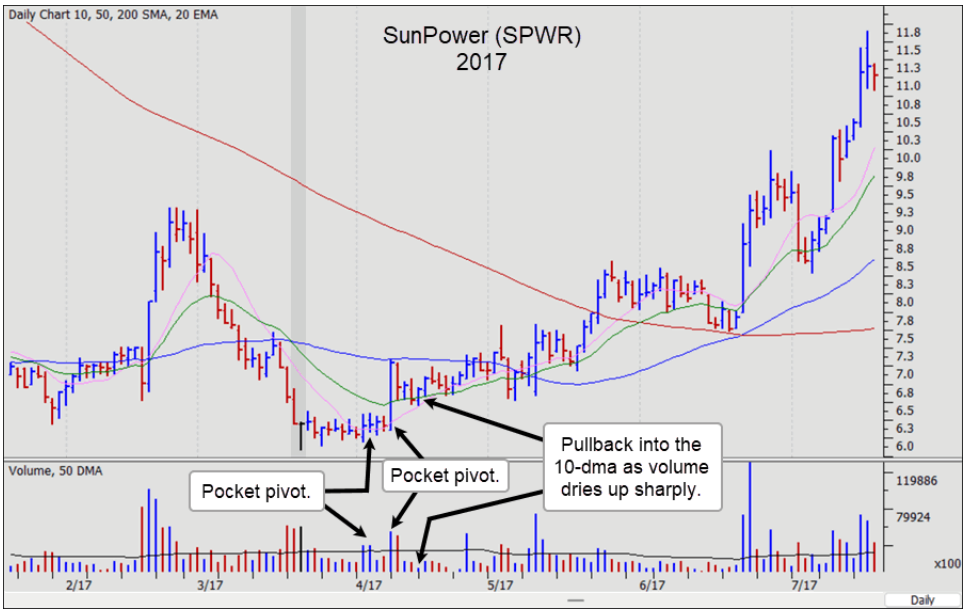


Figure 2.39 - SunPower (SPWR) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Context is always important whenever one is evaluating an Ugly Duckling type of set-up. General market action is of course one very important contextual factor. Another can be overall chart position. Note that in the example above, as **SunPower (SPWR)** (Figure 2.39(a)) was posting that bottom-fishing pocket pivot at the 10-dma and 20-dema, it was also undercutting the lows of a prior bear flag, complete with a big fake out breakout that reversed and took SPWR down to fresh lows.

That undercut, or rather downside fake out breakout, from the bear flag set up the pocket pivot, which occurred on the third up week off the final low. This is not something I would consider a *checklist* type of criteria that is required in every instance of a BFPP, but when a BFPP on the daily chart occurs within the context of a big undercut of a prior support level, it provides an additional clue when evaluating the set-up. The reader could go back and review all the examples in this chapter in conjunction with the weekly charts to gain an understanding of how clues can be gleaned from the weekly charts as a contextual factor.

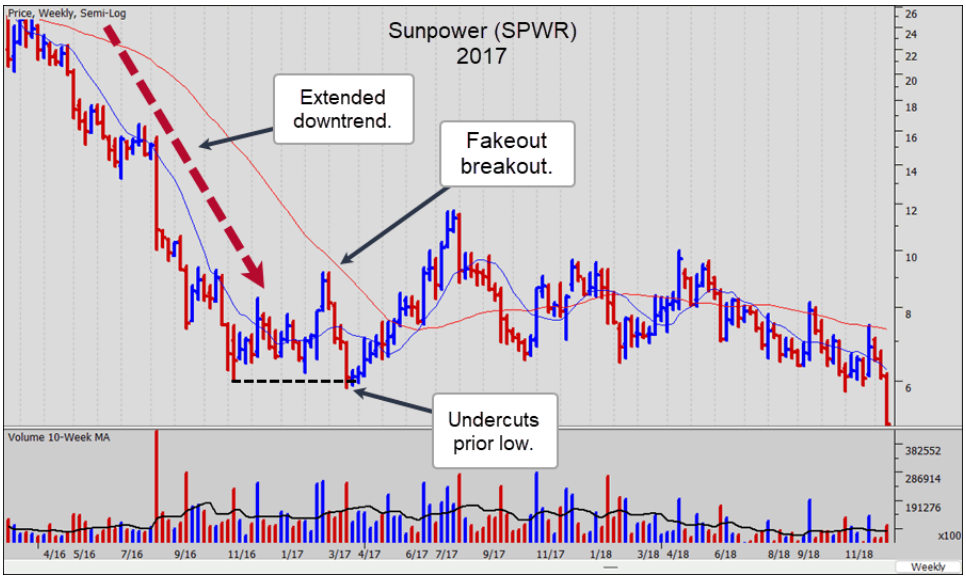


Figure 2.39(a) - SunPower (SPWR) weekly chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Any honest discussion of trading methodologies cannot ignore the need for a well-considered risk-management program. That is why I include examples of various OWL long set-ups that fail. Here we see **General Motors (GM)** (Figure 2.40) in August 2018 posting decent-looking bottom-fishing pocket pivot and then quickly failing. The action preceding the BFPP was constructive as GM drifted lower in a descending flag formation following a late July gap-down break.

As it proceeded to drift lower selling volume dried up in the extreme just before the pocket pivot was posted. As GM moved up through first the 10-day moving average and then the 20-day exponential moving average it provided simple references for selling guides at each moving average. Once it cleared the higher 20-dema, that would serve as a logical selling guide as part of a well-considered risk-management plan.

Note that as GM pulled back into the 20-dema over the next two trading days following the BFPP, volume dried up sharply. This certainly would have added to the favorable price/volume evidence surrounding the pocket pivot. But GM did not hold support at the 20-dema and instead slashed lower, breaking below the 10-day line

as well. If one were slow to pull the risk-management trigger, GM proceeded to post seven more down days in a row, making for a total of ten down days in a row immediately following the bottom-fishing pocket pivot.

The lesson here is clear. Even when you may not want to believe that such a constructive-looking BFPP would fail, ignoring your risk-management plan can be fatal. In my experience, even the most perfect looking pocket pivots of any kind can fail, sometimes more quickly than others.

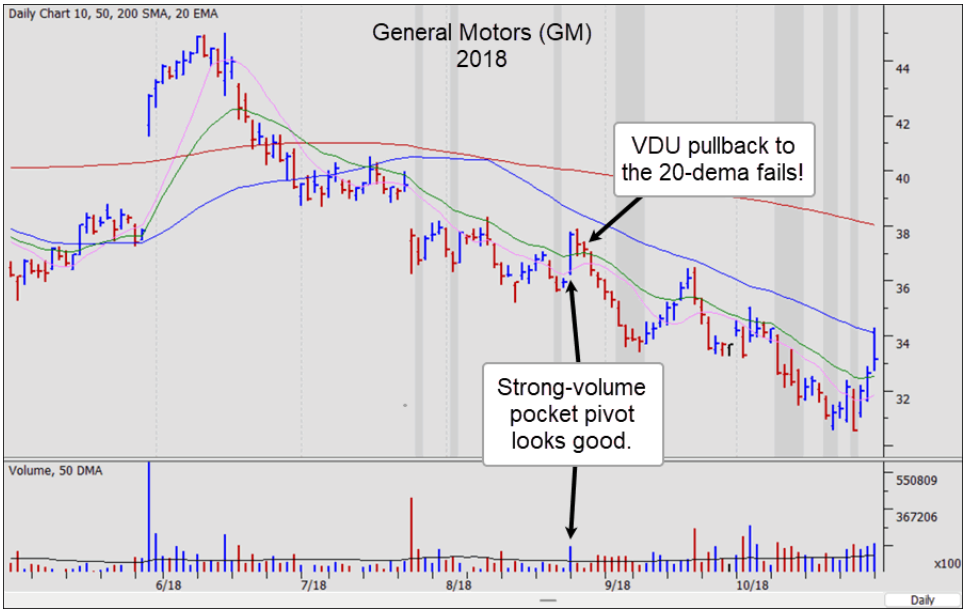


Figure 2.40 - General Motors (GM) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Bottom-fishing pocket pivots can also often try to fake you out when they look less than perfect but end up working quite well. In this example of **Roku (ROKU)** (Figure 2.41) from January 2019 we see one strong-volume BFPP along the 10-day moving average that is immediately followed by a higher-volume sell-off that takes the stock right back to 10-dma support.

Since it holds support at the 10-day moving average, using the 10-dma as a selling guide would have kept one in the stock. The next day ROKU launches off the 10-day line and up through the 20-day

exponential moving average on even higher volume, even though the immediate reversal on heavy and much higher volume the day after the first pocket pivot looked quite discouraging.

The lesson here is clear as well. Stick to your risk-management plan, since ROKU never busted the 10-day moving average even when faced with heavy selling volume. And, if you were scared out you should also be willing to come right back to the stock if it sets up again as ROKU did on the second, far stronger bottom-fishing pocket pivot.

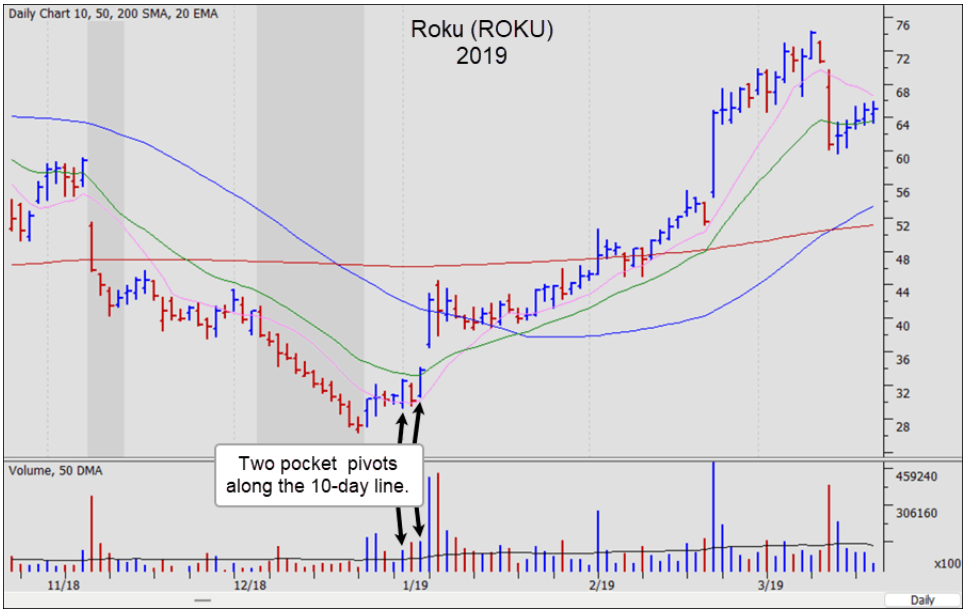


Figure 2.41- Roku (ROKU) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Nvidia (NVDA) (Figure 2.42) in May 2021 has a similar look to the ROKU example above, except that it bottomed out near its 200-day moving average where it posted a pocket pivot volume signature from a point just above the 200-day line. The next day NVDA gapped through the 50-day moving average and then proceeded to clear the slightly higher 10-dma and 20-dema on a pocket pivot signature.

While I do not believe that labels are important when it comes to the predictive value of a set-up, we could argue that this NVDA bottom-fishing pocket pivot (BFPP) is more like a roundabout pocket pivot

(RAPP). Once it kicked in it set the stock off in the process of quickly rounding out the right side of a new base from which it broke out less than two weeks later.

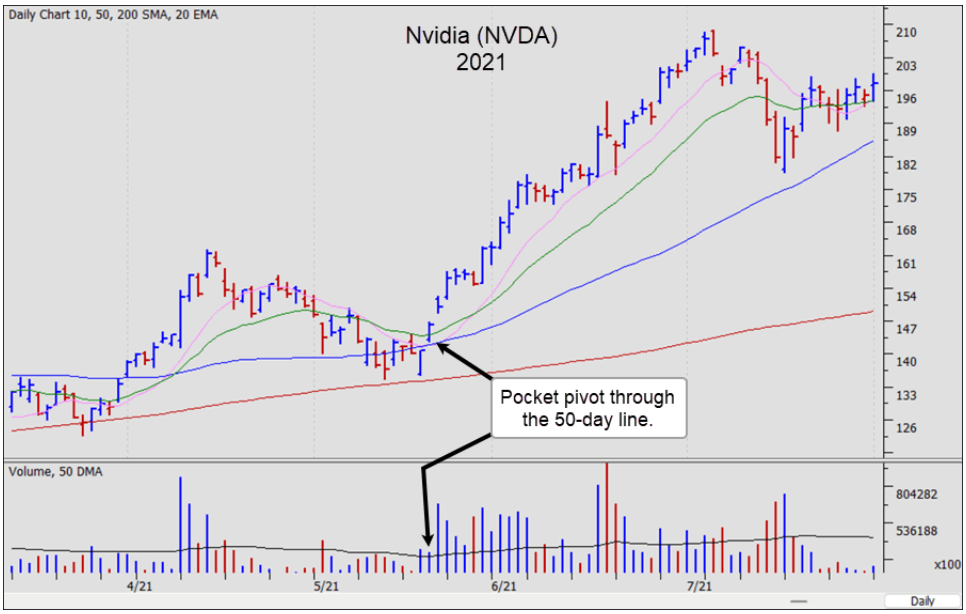


Figure 2.42 - Nvidia (NVDA) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

The roundabout pocket pivot look is more evident in the example of **Enphase Energy (ENPH)** (Figure 2.43) in October 2021. After trending steadily lower in August and September it begins to live below its 10-day and 20-day moving averages. In early October it suddenly regains the 10-dma and 20-dema and sets up along the 20-dema before posting a pocket pivot that stalls at the 50-day and 200-day moving averages but holds up. The next day it posts another pocket pivot as it clears what is major moving average resistance at the 50-day and 200-day lines.

From there, it rounds out the right side of a base and breaks out over two weeks later in a buyable gap-up move. As a rule, I find that bottom-fishing and roundabout pocket pivots, if they are going to work well, will tend to work quickly. Often this is a function of the general market turning after a short-term or intermediate-term correction.

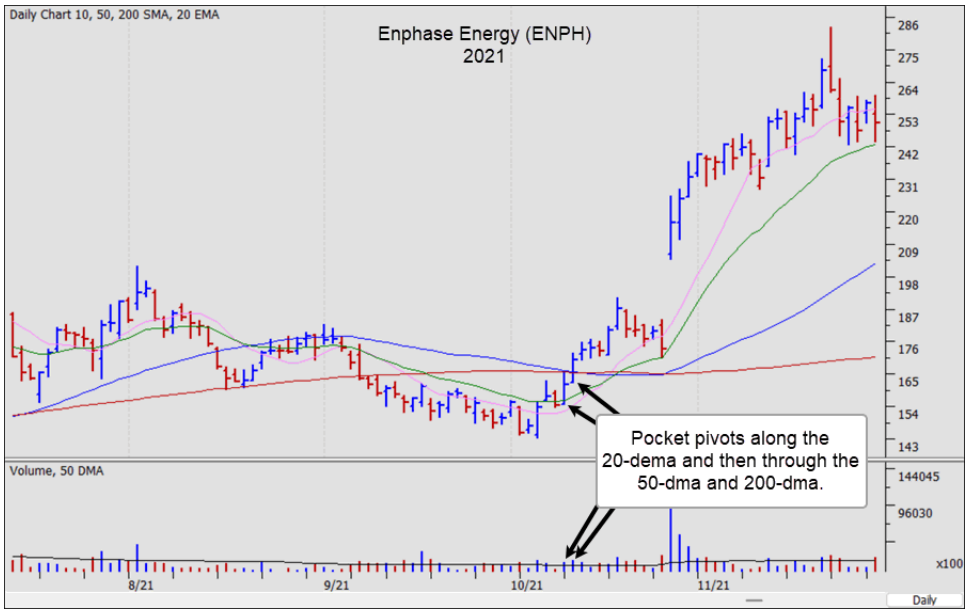


Figure 2.43 - Enphase Energy (ENPH) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

The 2022 bear market period was a difficult one for many leading stocks following the 2020-2021 Pandemic Bubble Bull Market. **Salesforce.com (CRM)** (Figure 2.44) was one such former leader that peaked in November 2021 at 331.75 and proceeded to decline to a final low of 126.34 in late December 2022. That constituted a total decline off the November 2021 peak of 59.47%. That bear market decline in CRM occurred in synchrony with most cloud-related names, many of which were selling at the high end of extreme PE-expansions, as I noted in my old *Gilmo Report* posts at that time.

In January 2023 the general market began to turn off its lows and as it did a beaten-down CRM came back to life as hopes of a *Fed pivot*, e.g., a return to interest rate *decreases* after a year of raising rates at a record-setting pace, blossomed. As the market turned CRM posted two pocket pivots along its 20-dema in early January.

The first BFPP occurred on a gap-up move but CRM faltered briefly as it pulled back into 20-dema support. That support held as volume contracted, and the next day the stock posted a second BFPP right off the 20-dema. The next day it cleared the 50-day moving average,

consolidated for not quite two weeks, and proceeded to move higher from there. That BFPP worked rather quickly and was certainly aided by the general market turn off the lows at that time.

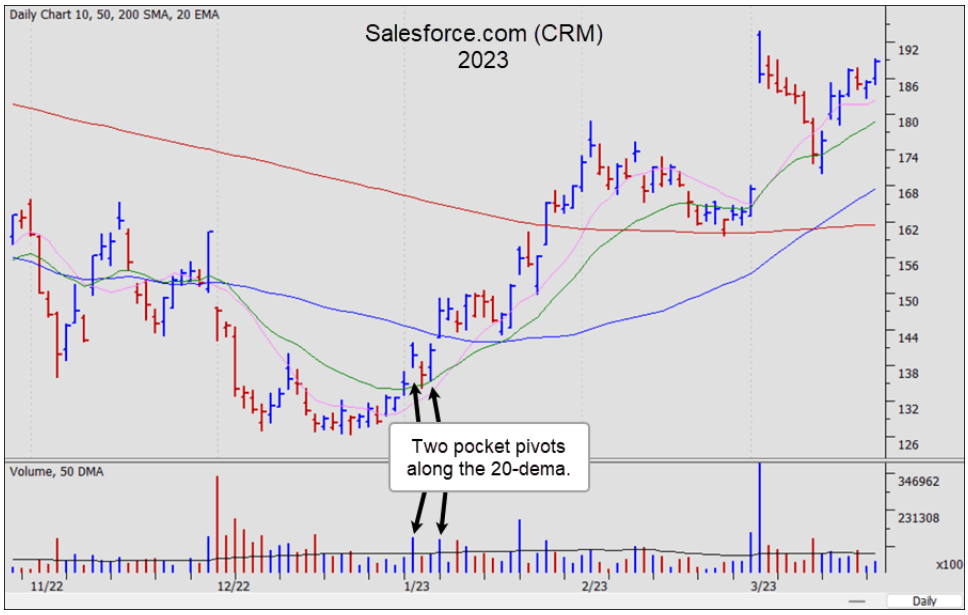


Figure 2.44 - Salesforce.com (CRM) daily chart, 2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Roku (ROKU) (Figure 2.45) was another beaten-down former leader that was crushed during the 2022 bear market. After peaking at 490.76 in late July 2021 the stock declined an astounding 92.20% before bottoming at 38.26 in late December 2022. It also suffered from an absurdly high PE-expansion, particularly since it made no profits and therefore had an infinite PE. Proof that the absurd PE-expansions resulting from extreme accommodation by the Fed as it printed trillions of dollars in response to the 2020 pandemic were ripe to contract with brutal consequences when those easy money policies were reversed.

Like CRM, however, ROKU turned with the general market in early January 2023 as hopes of a Fed pivot, a shift back to easy money policies, gained traction. ROKU gained traction as it pushed back above its 10-day moving average in early January 2023 with an initial bottom-fishing pocket pivot. That was followed by two more BFPPs as

the stock tested its 10-dma on both of those days. This was an easy one to play, however, since the action remained constructive on each test of the 10-day line, and once ROKU cleared the 20-dema after the third bottom-fishing pocket pivot, it pushed sharply higher.

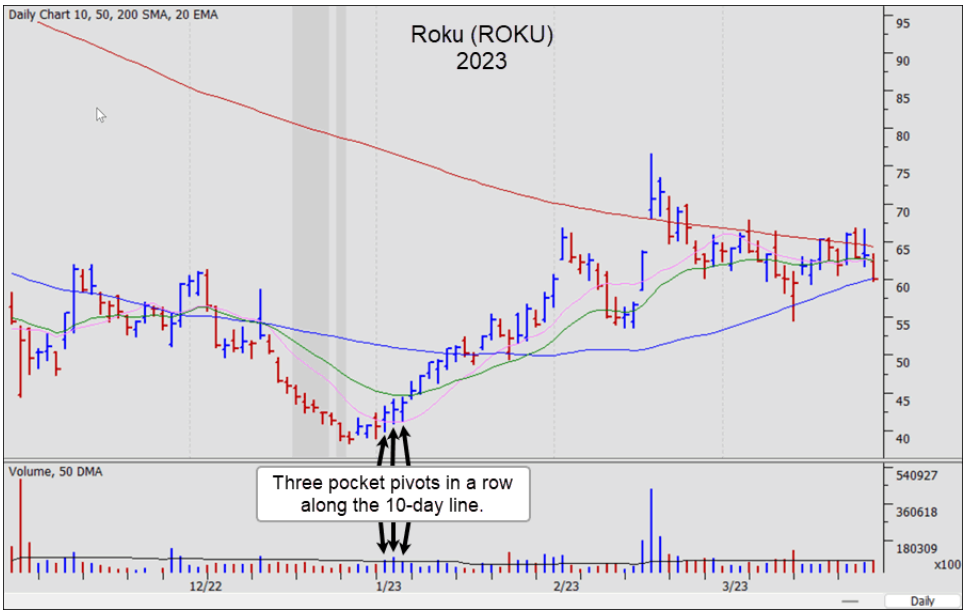


Figure 2.45 - Roku (ROKU) daily chart, 2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Nvidia (NVDA) (Figure 2.46) is another example of bottom-fishing pocket pivots that were seen as the market turned in early January 2023. As with the previous two, the success of the BFPP is highly dependent on the general market context. This is often the case for these types of Ugly Duckling set-ups that occur at or near lows in a pattern, whether after a normal correction or an extended decline.

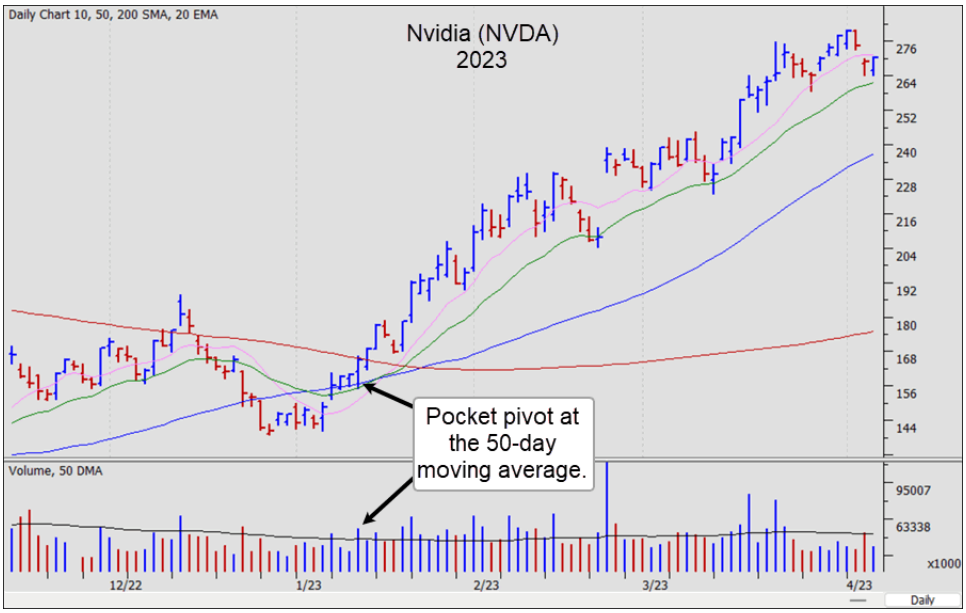


Figure 2.46 - Nvidia (NVDA) daily chart, 2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Bottom-fishing and roundabout pocket pivots can give traders and investors a huge edge in gaining early entries in stocks as they turn off the lows, often in synchrony with the general market. If one incorporates these with other general market technical signals such as MACD, RSI, and other indicators, even O'Neil style follow-through days, one can be comfortably long without having to sit around waiting for new-high breakouts in potentially recovering leading stocks.

Bottom-Fishing Buyable Gap-Ups

Our arsenal of OWL Ugly Duckling set-ups also includes buyable gap-ups that occur at or near lows in a pattern, whether after a normal correction or an extended decline; no different than BFPPs and RAPPs. The critical factor for all of these Ugly Duckling set-ups is that they are all concrete, in other words easily identifiable, and use simple and efficient risk management methods. The characteristics of a bottom-fishing buyable gap-up (BFBGU) and a

standard buyable gap-up (BGU are exactly the same. The only difference is that a BFBGU occurs near or from the lows of a pattern.

One of my favorite BFBGU set-ups occurred in gold miners back in November 2022 when investors suddenly took heart from declining inflation data and grasped onto the idea of a Fed pivot. At the time, the Fed was aggressively raising interest rates, and as inflation appeared to be slowing, investors wanted to believe that the Fed would soon end their interest rate raising campaign and *pivot* back towards *interest rate cuts*. Lower rates imply a declining U.S. Dollar, and therefore higher precious metals prices.

Gold and silver stocks went nuts on the news, and one of the more powerful movers was **Gold Fields (GFI)** (Figure 2.47) in early November 2022. At the same time, GFI was looking to acquire another gold miner **Yamana Gold (AUY)**, but at the same time AUY announced that they were going to accept a better offer from a partnership formed by gold miner **Agnico-Eagle Mines (AEM)** and silver miner **Pan-American Silver (PAAS)**.

That triggered a massive-volume gap-up move right off the lows when GFI was looking quite ugly. This is a fantastic example of an Ugly Duckling long set-up given how ugly GFI was looking as it headed for a retest of the September 2022 lows in the days just prior to the BFBGU.

GFI also benefitted from additional news that its buyout of Yamana Gold (AUY) was rejected in favor of a better offer from major gold miner Agnico-Eagle Mines (AEM) and silver miner Pan-American Silver (PAAS). GFI had made a bid for AUY earlier in the year, leading to a severe price decline on the news as investors felt GFI was overpaying for AUY. When AEM and PAAS partnered to present AUY with a superior joint buyout bid GFI was suddenly off the buyout hook.

That gave the ensuing move in GFI shares tremendous upside velocity that very quickly took the stock back up towards where it was trading prior to announcing its intended offer to buy out AUY. In

this case, two news events simultaneously came into play to create an astounding upside move in GFI off the late 2022 lows.

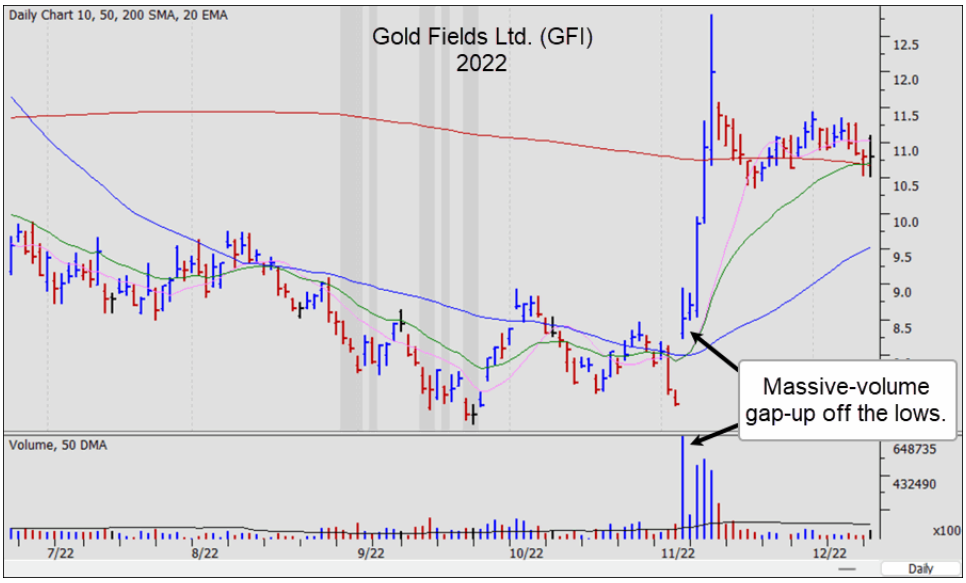


Figure 2.47 - Gold Fields Ltd. (GFI) daily chart, 2022. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

BFBGUs are often associated with news or other significant thematic developments, as the GFI example shows. If it has group implications, then other names within the same industry or thematic group will post similar moves.

AngloGold-Ashanti (AU) (Figure 2.48) is another big-stock gold miner that gapped right off its low at the same time as GFI. The move had less upside range and velocity than GFI's for obvious reasons – it was being driven by only one news event while GFI had the additional news that the selling weight placed on it because of its buyout off for AUY was suddenly removed. Still, the initial BFBGU in AU led to a very rewarding price trend over the next three months.



Figure 2.48 - AngloGold-Ashanti (AU) daily chart, 2022-2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

A more recent thematic impetus, namely the Artificial Intelligence (AI) meme-theme that struck in 2023, led to a slew of other BFBGUs among stocks that claimed a connection between their products and services and the use or implementation of AI. One of the very first stocks to feel the love, so to speak, from the newly emerged AI meme theme was a small AI-oriented technology company with no earnings to speak of, **C3.Ai (AI)** (Figure 2.49). It did, however, have the acronym "AI" as its symbol.

In the first half of 2023 AI posted two bottom-fishing buyable gap-ups, the first of which played out as what I like to call a *one-day wonder* trade. On March 3, 2023, AI gapped up at the open after reporting earnings the evening before and opened at a price of 25.29 after closing at 21.31 the day before. It quickly set an intraday low of 24.03 and then launched higher before peaking at 29.98 the next. As a quick swing-trade, the move was very profitable, but eventually reversed at left-side price resistance and AI broke down again.

Fast forward to mid-May 2023 as C3.AI (AI) was plumbing lower lows and looking quite ugly. The steady deterioration in the stock price of AI began on the massive break off the peak on April 4th after short-

seller Kerrisdale Capital wrote a letter to AI's auditor claiming, "serious accounting and disclosure issues." In essence, they accused the company of fraud.

Over the next several months the claims dissipated without any further substantiation. Eventually, a new wave of Artificial Intelligence meme fever hit the market. This time around, AI's BFBGU on May 15th had much more staying power. It closed the day before at 19.42 and gapped up to an opening price of 20.63, set an intraday low at 20.20 and then spiked up through its 50-day moving average. From there the move held above the 50-day line which served as a convenient trailing stop/selling guide, and AI eventually went on to make higher highs.

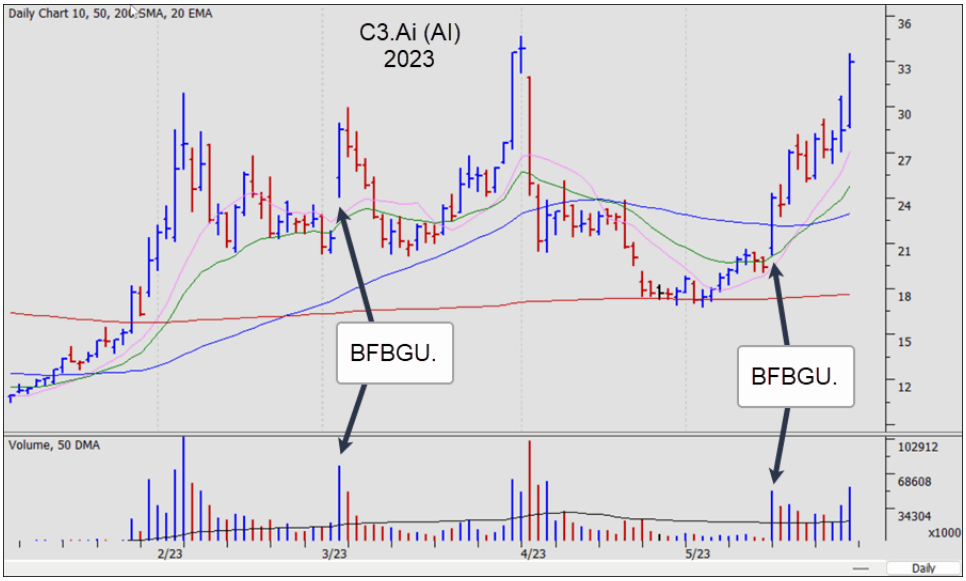


Figure 2.49 - C3.Ai (AI) daily chart, 2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Palantir (PLTR) (Figure 2.50) was another smaller technology company that caught fire during the Artificial Intelligence meme mania sweeping through the market in May 2023. PLTR was one of many stocks that suddenly caught fire, and the move began with a bottom-fishing buyable gap-up. While it looks straightforward on the chart it was in fact a tricky one to catch. After closing at 7.74 on May 8, 2023, PLTR reported earnings that afternoon and surprised the

market with earnings of five cents a share, one penny above estimates and 150% higher than the same quarter a year ago.

PLTR gapped higher after-hours that day and the next morning printed an opening price of 9.22 before backing down sharply to an intraday low of 8.65, just over 6% lower. Generally, the use of a five-minute intraday chart is helpful in determining intraday lows when a stock swings this much.

PLTR moved higher over the next day and then began to pull down, reaching a low of 9.02 four days after the original BFBGU. That brought the stock nearer to the 8.65 intraday low of the BFBGU day and right on top of the prior low-base range at peak at 9.04. Note that volume levels were drying up very rapidly compared to the BFBGU day five days prior. From there PLTR shot much higher.

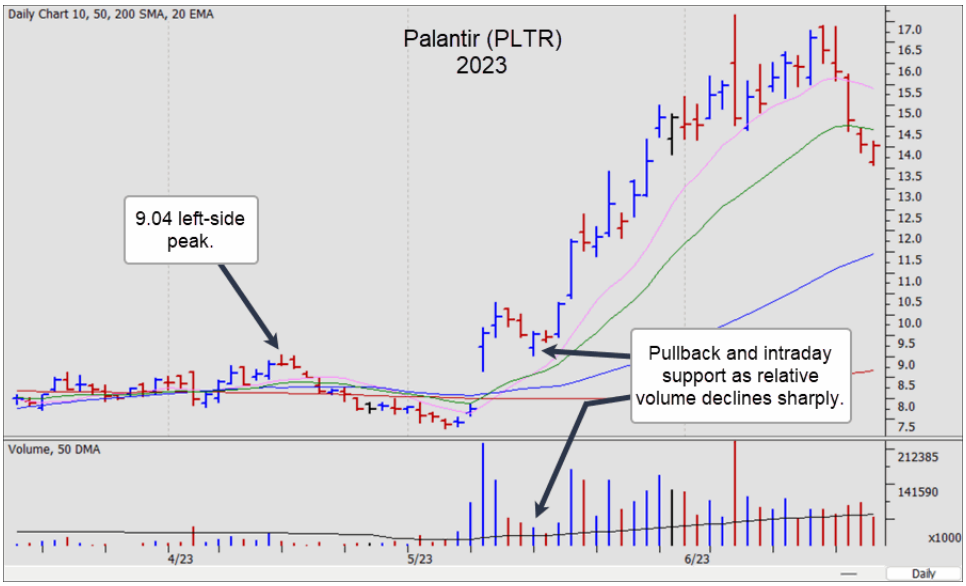


Figure 2.50 - Palantir (PLTR) daily chart, 2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Enphase Energy (ENPH) (Figure 2.51) posted two BFBGUs in December 2016 and then again in January 2017. The first one occurred on massive volume and the stock stalled to close mid-range on the day, but still well above where it closed the prior day. ENPH then pulled back towards the intraday low of the BFBGU day and

held for several days before finally coming loose and breaking lower. Proof that the BFBGU, like any other long set-up, must employ sound risk management.

Sometimes what does not kill a stock can make it stronger, although ENPH looked like it had been left for dead as it made lower lows in late December. At that point, it undercut a low in the pattern posted on November 1, 2016, and turned back to the upside. After holding up in a short bull flag along the underbelly of the 50-day moving average, ENPH launched on a second bottom-fishing buyable gap-up.

It closed near the intraday peak on that BFBGU, but still came in the next day to test the intraday low. It held, and the next day launched higher. So, while the first BFBGU stalled badly on massive volume and the second closed near the intraday highs, uncertainty came into play on the second day of each set-up. The final resolution of each was easily determined by the failure of the first and the success of the second in holding support along the intraday low of the BFBGU day.

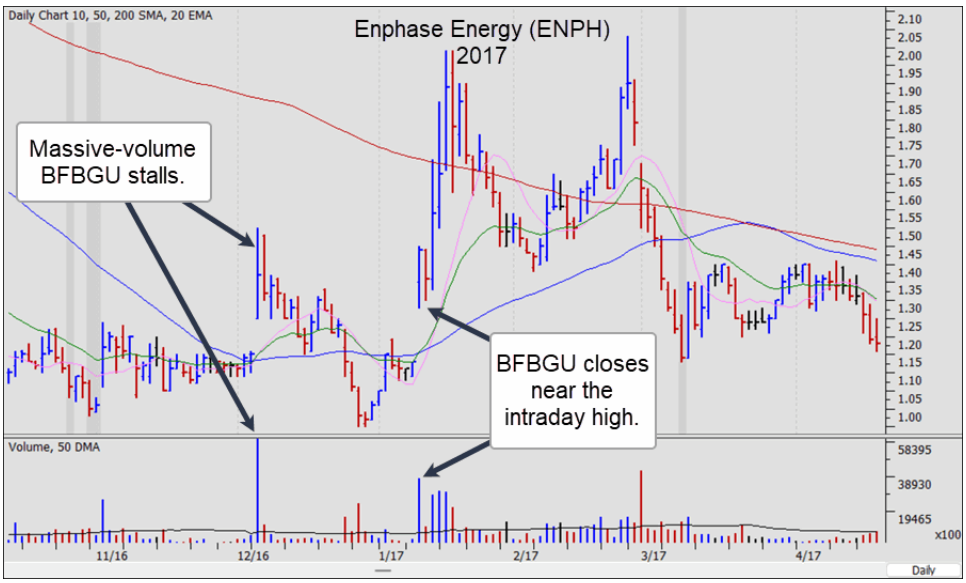


Figure 2.51 - Enphase Energy (ENPH) daily chart, 2017. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Roku (ROKU) (Figure 2.52) in January 2019 was a clean bottom-fishing buyable gap-up move on the eighth day up from the lows. The BFBGU did not produce any further, significant upside as it faltered the next day and closed negative. However, ROKU did clear the 50-day moving average and held it. From there the stock moved tight sideways along the 50-day line and then the rising 10-day moving average as it tracked back up through the 50-dma.

Note that at that point one could have implemented other OWL entries, such as VDU action along the moving averages, as long entries well after the original BFBGU. This is not unusual since most BFBGU moves will have areas of immediate overhead price congestion to work through. Some get through them faster than others, and in this case, ROKU took a little time to work off sellers as it eventually pushed beyond the 50-day line and up through the 200-dma over the next couple of months.

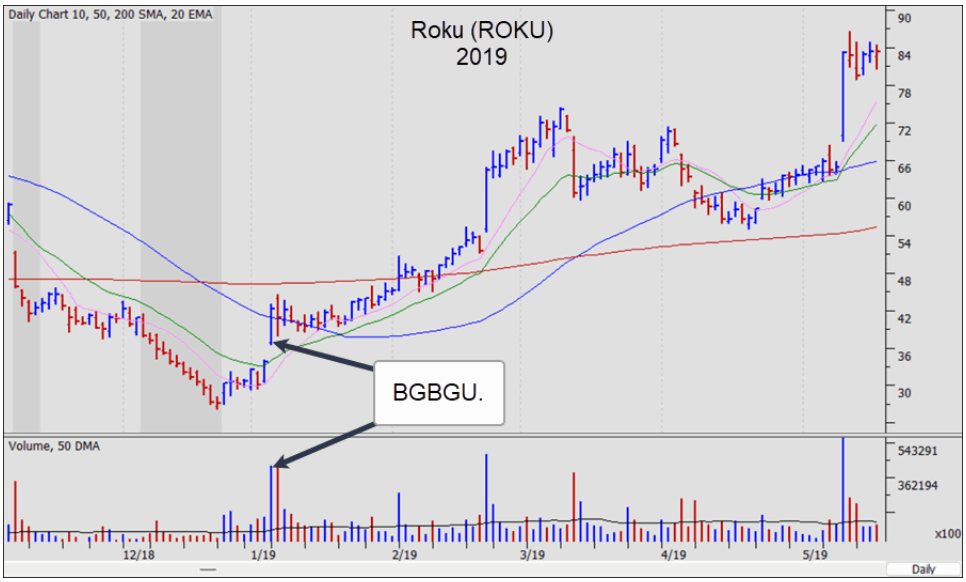


Figure 2.52 - Roku (ROKU) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Stitch Fix (SFIX) (Figure 2.53) in June of 2019 is what you call a *flash in the pan* type of bottom-fishing buyable gap-up as it was good for decent swing-trade before it lost momentum and rolled over to eventual lower lows. The BFBGU was also not an easy one to play as

it ended the first day up near the intraday lows, a serious stall out on very heavy volume. The day after the BFBGU it also dipped below the BFBGU intraday low and shook out before pushing higher. Certainly not the most sustained BFBGU you will ever see, but a tradeable one for nimble, intrepid buyers.

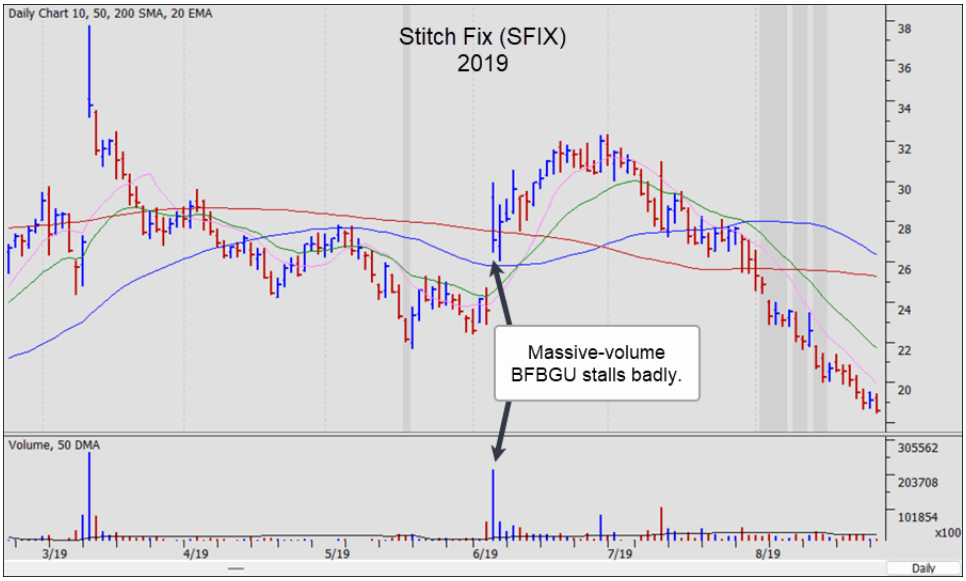


Figure 2.53 - Stich Fix (SFIX) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Semiconductor memory chip maker **Micron Technology (MU)** (Figure 2.54) in 2019 was a much more sustained and powerful bottom-fishing buyable gap-up in comparison to SFIX above. Trapped in a bear flag as it progressed towards the end of June, and looking for all the world as if it were on the verge of a bear flag breakout to the downside. MU pulled itself out of the Ugly Duckling swamp on a massive-volume BFBGU and closed near the intraday highs.

It quickly cleared its 50-day and 200-day moving averages before pulling in for three days to test the 200-day line as volume dried up to VDU (VooDoo) levels. If one were holding a position taken on the original BFBGU then this VDU pullback would have sufficed as a very reasonable add point. Three days later MU posted another BGU and

continued higher from there before peaking near-term and building a new base.

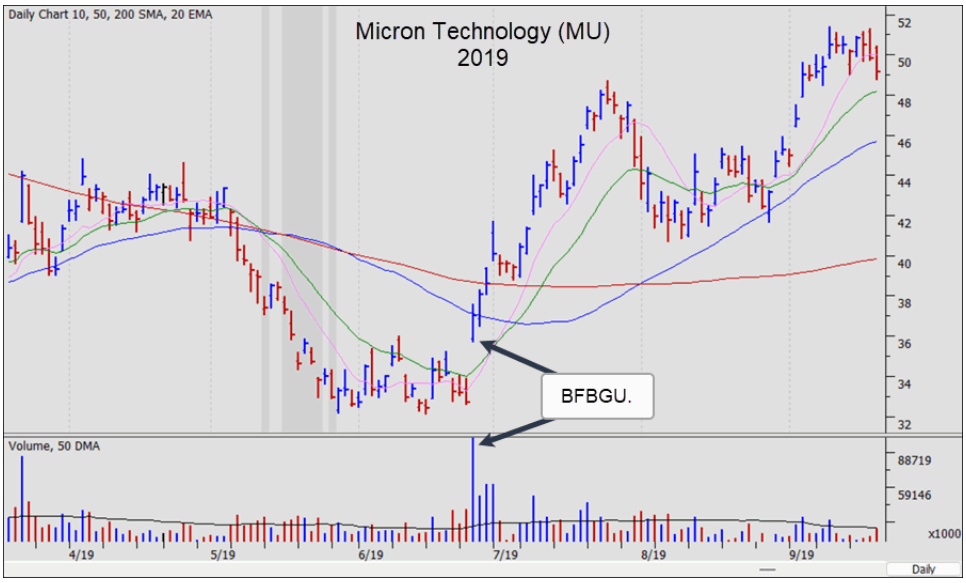


Figure 2.54 - Micron Technology (MU) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Nvidia (NVDA) (Figure 2.55) in late July 2019 looked to be heading for lower lows before it suddenly backed away from the abyss and posted a big-volume bottom-fishing buyable gap-up in August. That move just barely cleared the 50-day moving average. The next day it cleared the higher 200-day moving average and then rallied higher for three more days before rolling over in a test of the 50-day and 200-day moving averages.

NVDA dipped below the 50-day line but held support at the 200-day and then bounced slightly before rolling over to test the 200-dma once again. Study the chart carefully and you will notice that this second pullback came on VDU volume levels, basically a successful *test for supply* that I like to call a Wyckoffian Retest. A low is set, a bounce occurs, and then ensuing retest of that first low sees volume dry up sharply in classic VDU fashion. That tells you that sellers have dried up and blown out of the way, leaving the stock free to continue its rally.

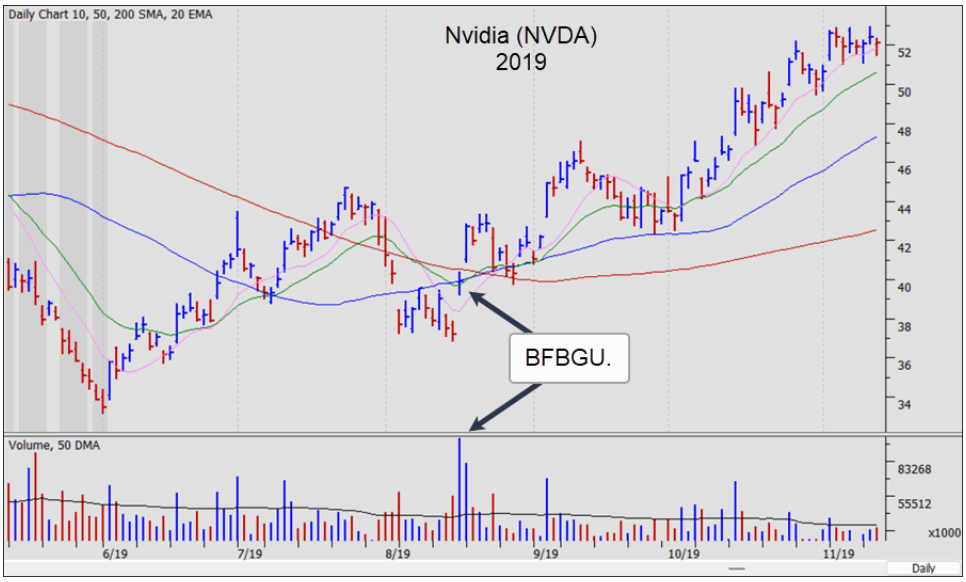


Figure 2.55 - Nvidia (NVDA) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Walt Disney Company (DIS) (Figure 2.56) illustrates how a new product or service announcement can trigger a bottom-fishing buyable gap-up. In November 2019 the company announced the launch of a new streaming service, *Disney+*, that would compete with the likes of **Netflix (NFLX)**. One advantage DIS had was the pre-existing, massive library of its own original content stored in its movie vaults.

That news set off a big-volume gap-up move off the late October lows that pulled in slightly the next day, looking a bit uncertain right off the bat. However, despite closing below the intraday low of the BFBGU day it remained within 1-3% of that low, which is why the intraday low of a BGU or BFBGU day is considered a *selling guide*, not a *stop*. Often, it is reasonable to add 1-3% to the intraday low to account for some downside *porosity* that may carry slightly below the intraday low. Applying such porosity to DIS in this example would have kept one in the stock.

The next day, the second day after the BFBGU, DIS found its feet and posted a higher closing high before going berserk to the upside the following day.

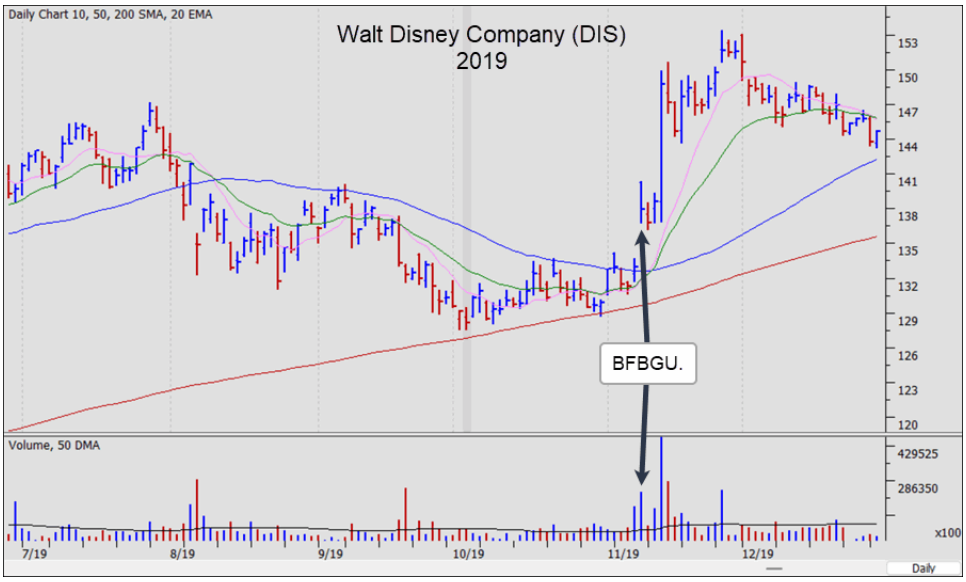


Figure 2.56 - Walt Disney Company (DIS) daily chart, 2019. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

When the Covid pandemic hit in February and March of 2020, all hell broke loose in the stock market. Nothing escaped the panic sell-off, including **Nvidia (NVDA)** (Figure 2.57) as the sudden onset of the pandemic rudely interrupted what was shaping up to be a strong upside move in the stock in the first half of February 2020. NVDA plummeted to lower lows, but as the panic raged and reached a crescendo in late March the selling subsided.

As the Fed and the U.S. government rushed to provide massive monetary and fiscal stimulus just as the world appeared to be on the brink of extinction, NVDA turned and gapped higher in the latter part of March. Volume was heavy, triggering a bottom-fishing buyable gap-up (BFBGU) long entry signal. NVDA then began an epic run during what became the great Pandemic Bubble Bull Market of 2020-2021.

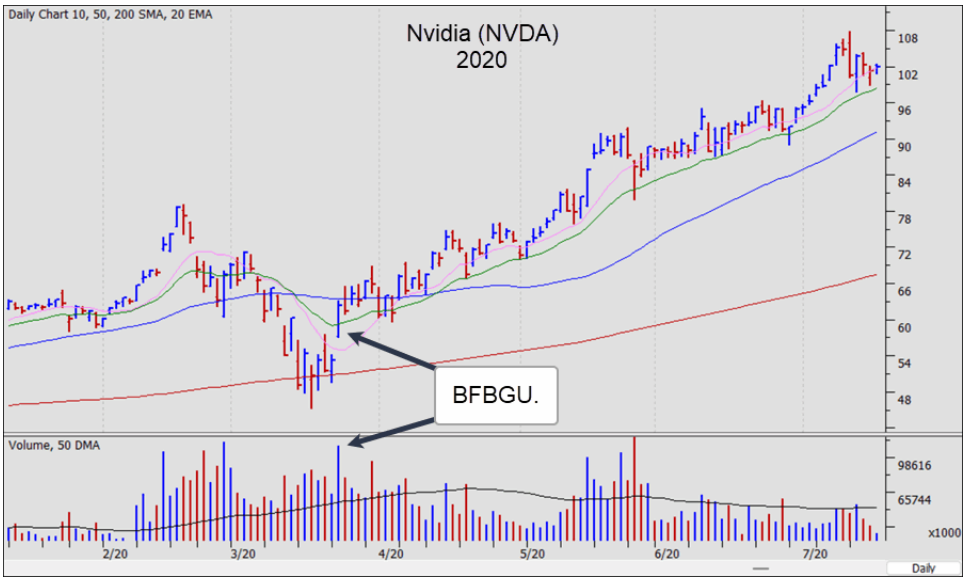


Figure 2.57 - Nvidia (NVDA) daily chart, 2020. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

With a new work-from-home, shop-from-home, play-at-home mentality taking root during the Covid pandemic as people came to the irrational conclusion that all other human beings were now toxic carriers of certain death, the online world came into focus. This included social networking services like **Snap (SNAP)** (Figure 2.58), which experienced a large increase in user activity as people conducted more of their activities online, including social activities.

When SNAP reported earnings in April 2020, reflecting the increase in user activity, the stock gapped higher on massive volume. It then chopped its way higher along the 20-day exponential moving average in a shallow uptrend channel before starting on a more robust uptrend in late May. The BFBGU remained in force the whole way as a boom in online activity took hold amid the new norm of working, shopping, and playing at home forced upon society during the pandemic.

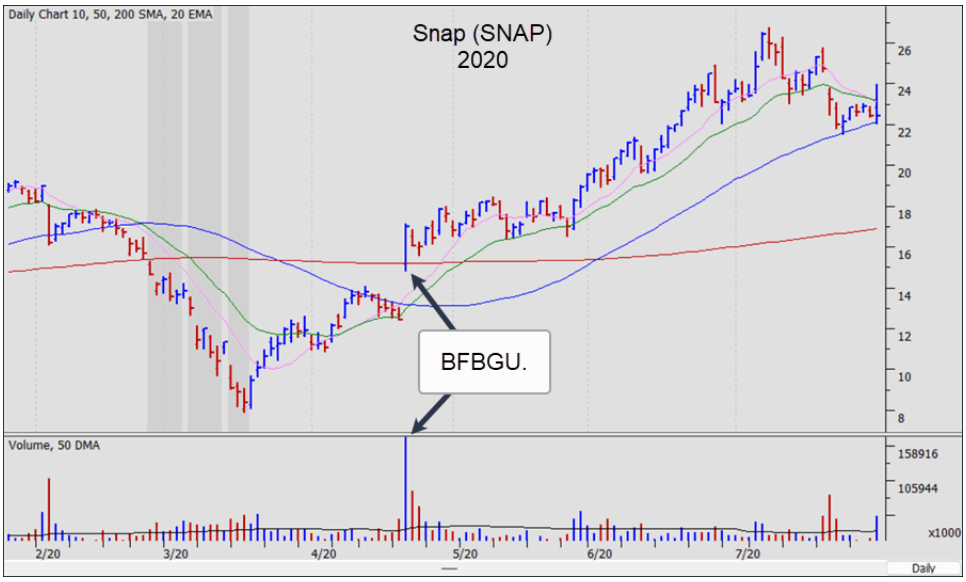


Figure 2.58 - Snap (SNAP) daily chart, 2020. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

As the pandemic affected every nook and cranny of everyday life, perhaps more people were induced to just stay in bed. While there are no hard statistics to corroborate such a possibility, mattress maker **Sleep Number Corp. (SNBR)** (Figure 2.59) benefited mightily from the pandemic environment no less. Stimulus checks coming from the government, referred to as *Economic Impact Payments* by the government, were essentially direct cash payments to individuals intended to offset economic hardship resulting from the pandemic, fueled retail spending.

With so many people stuck at home, it made sense to use the free money to enhance one's home environment via the purchase of new home furnishings, including mattresses. When SNBR reported earnings in the latter part of April 2020 this was confirmed by the earnings and sales figures and the stock launched higher on a bottom-fishing buyable gap-up at that time.

From there SNBR chopped its way higher along the rising 20-day exponential moving average, not unlike SNAP in the prior example, as it formed a shallowly rising uptrend channel before gaining momentum in June. Note the multiple VDU pullbacks to the 20-day

line along the lows of the uptrend channel which also served as potential OWL add points on the way up following the initial April BFBGU.

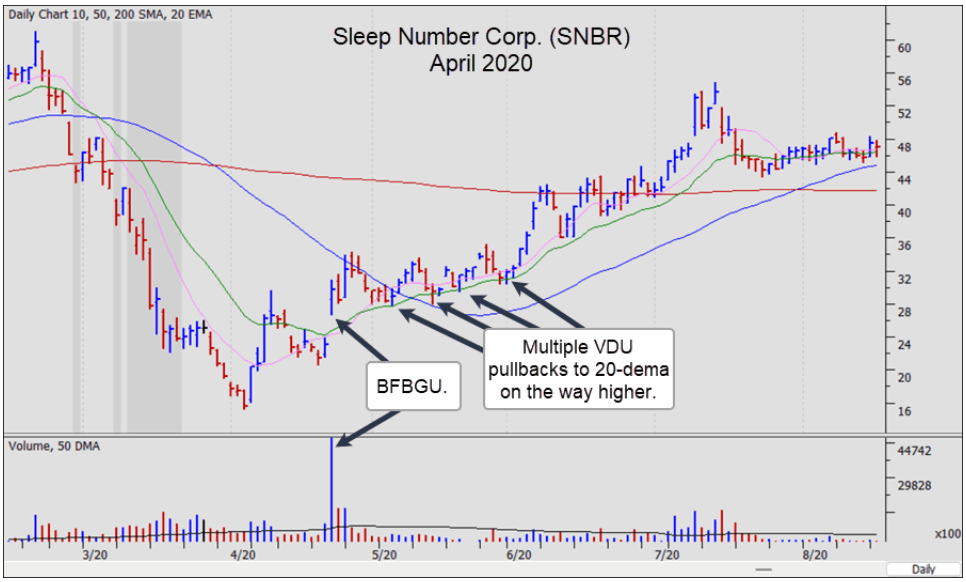


Figure 2.59 - Sleep Number Corp. (SNBR) daily chart, 2020. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Array Technologies (ARRY) (Figure 2.60), a manufacturer of smart ground-mounting systems for solar energy projects, posted an innocuous-looking bottom-fishing buyable gap-up in early August 2021 in an unlikely chart position. The stock had blown apart after reporting earnings three months earlier, and over the next three months following that massive-volume gap-down break spent its time moving sideways in what appeared to be little more than a bear flag en route to lower lows.

When the next earnings report rolled around, the outcome this time was much different. Despite reporting a 67% *decline in* earnings ARRY gapped higher on heavy volume. The move was not all that convincing as the stock stalled on the day to close just above mid-range but still above its 50-day moving average. In fact, the move could also be interpreted as a bottom-fishing pocket pivot coming up through the 50-day line.

After holding along the 50-day moving average for two more days ARRY launched decisively higher before building a new base over the next three months, but this time a *bullish* one before extending the run from there.



Figure 2.60 - Array Technologies (ARRY) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Buyable gap-ups in general are often the product of a meaningful catalyst, such as an earnings report, a new business or product development, economic news, or industry-related news. In August 2022, the U.S. government passed legislation within the so-called *Inflation Reduction Act* that raised the residential solar tax credit to 30% as part of a fresh batch of subsidies for the solar industry. Not surprisingly, that set off a move in solar installation concerns like **SunPower (SPWR)** (Figure 2.61) just ahead of the Inflation Reduction Act's passage by Congress.

That constituted significant industry-related news that launched SPWR on a streaking bottom-fishing buyable gap-up (BFBGU) move. The stock closed near the highs of the day of the BFBGU in a sign of strength. Three days later SPWR gapped up through the 200-day

moving average and continued to streak higher in a high-velocity price move that lasted all of two weeks, but which saw the stock post a 46% move from the BFBGU low of 18.55.

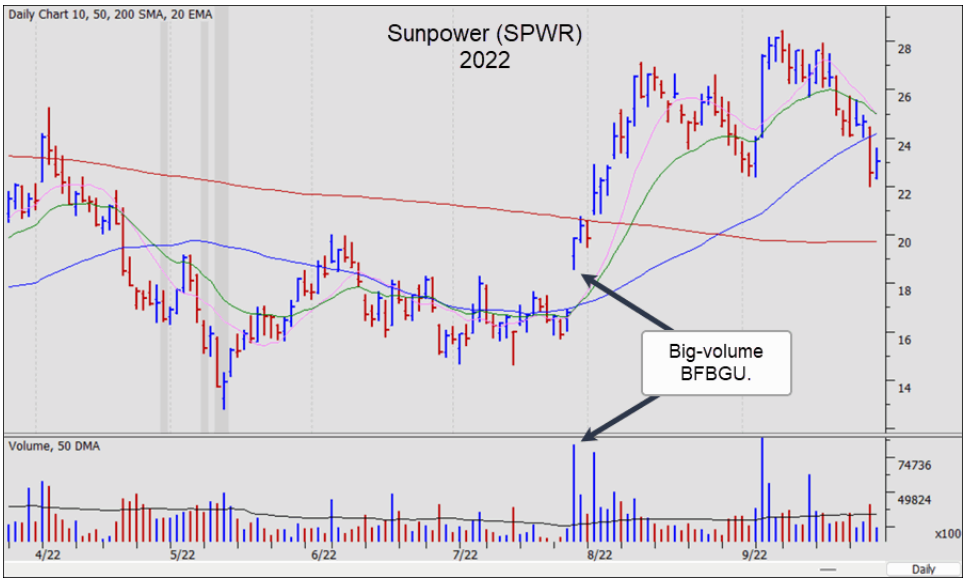


Figure 2.61 - SunPower (SPWR) daily chart, 2022. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

First Solar (FSLR) (Figure 2.62) was a beneficiary of the same solar subsidy legislation contained in the so-called *Inflation Reduction Act* that also sought to provide production tax credits to accelerate U.S. manufacturing of solar panels. FSLR, of course, manufactures utility scale solar panels.

That led to a bottom-fishing buyable gap-up that stalled initially but quickly continued higher. From the 87.34 intraday low of the BGU day, FSLR posted an impressive high-velocity price move that lasted six weeks and produced a 60% gain over that time.

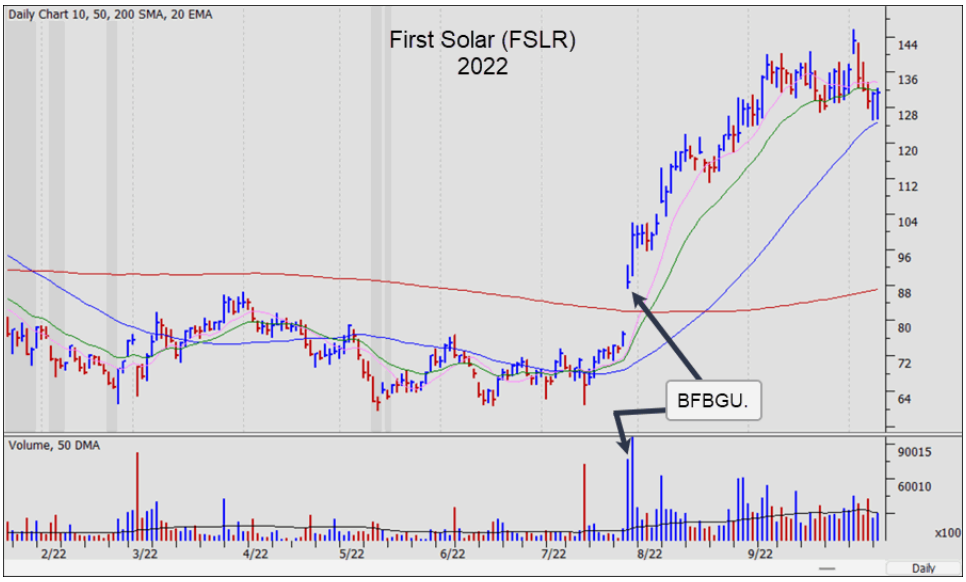


Figure 2.62 - First Solar (FSLR) daily chart, 2022. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

SolarEdge (SEDG) (Figure 2.63) differed from FSLR in that it does not produce solar cells. Instead, it manufactures storage devices for power that is generated by solar cells. Solar-related names will often gap-up out of nowhere when news of proposed legislation that includes solar subsidies hits the wires, but in this case SEDG gapped up on huge volume in early November 2022 after it reported earnings in a strong bottom-fishing buyable gap-up move.

Three months after FSLR's BFBGU in July, SEDG posted one that was just as clean and with just as much upside velocity. Unlike FSLR, however, it faltered on the day after as it ran into resistance near the 200-day moving average and reversed hard. Volume on the reversal was heavy but had contracted significantly from the BFBGU the day before.

At the same time, SEDG held support at its 50-day moving average which served as potentially buyable support. Also, if one had purchased the stock the day before the buyable gap-up move and used the 240.05 intraday low of that day as a selling guide, one would not have been stopped out of the position. And if one were nervous

about the position then using the 50-dma as a trailing stop at least insured a small profit if the BFBGU failed altogether.

The following day SEDG gapped higher again on big volume that was higher than the prior reversal day at the 200-day moving average. This time, however, on the second day after the initial BFBGU, SEDG cleared the 200-dma and worked its way higher from there.

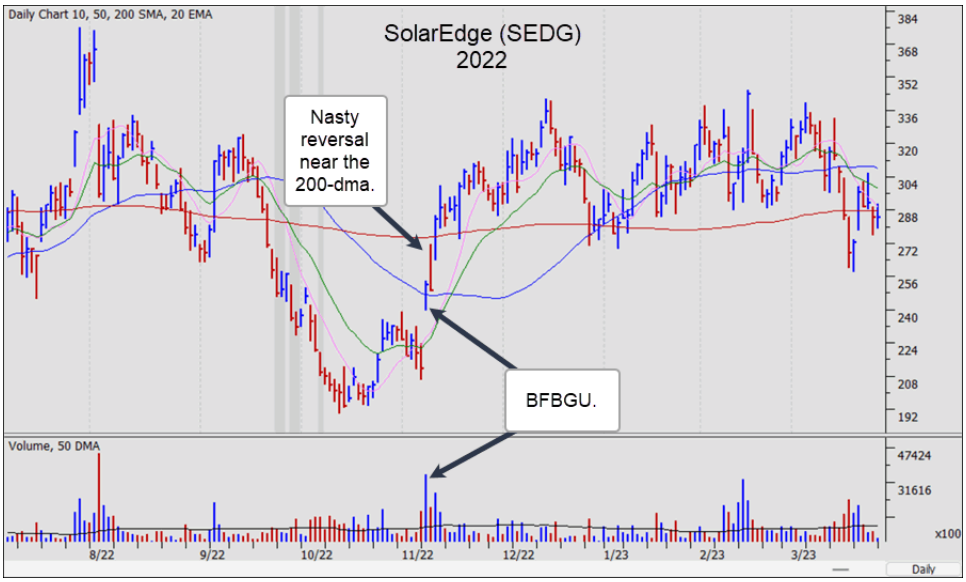


Figure 2.63 - SolarEdge (SEDG) daily chart, 2022. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Price and Moving Average Undercut & Rally (U&R and MAU&R) Set-Ups

This is the most common of the Ugly Duckling OWL set-ups that include bottom-fishing pocket pivots and bottom-fishing buyable gap-ups. The undercut & rally, or U&R, is derived from Richard D. Wyckoff's *spring formation*. If you search the internet using the term *Wyckoff Spring Formation,* you will find numerous images of line diagrams that explain the concept, some with a great deal of detail that I find wholly unnecessary.

It is much simpler to show what it looks like on an actual chart example, because U&R examples can be found anywhere and

everywhere in just about any market environment. Study the charts of stocks you have owned or traded over the years, and you will likely see numerous U&Rs throughout.

The term *undercut & rally* comes from my old boss and mentor, Bill O'Neil. Bill used it to refer to examples where stocks undercut major lows on the weekly charts and rallied higher from there as they began to build the right sides of new bases.

I began using it to refer to cover points in short-sale positions as they undercut prior lows and rallied from there. Eventually I began to realize that it could be utilized as a more intermediate- to longer-term long entry signal, replacing the arbitrary and statistically deficient *Shakeout-Plus-Three* buy signal first discussed by Jesse Livermore and then adopted by William J. O'Neil.

The U&R does away with the business of trying to calculate the number of points above a shakeout point/prior low that needs to be applied based on the price of the stock in question. Thus, O'Neil would use three points for a $60 stock, and maybe four to five points for a $100 stock. This is far too arbitrary to be practical and exposes one to the usual 7-8% loss if one is using the typical O'Neil style stop-loss policy.

The U&R distills all this Shakeout-Plus-N nonsense, where N is the number of points above the shakeout low that the stock needs to rally before generating a buy signal, to the simple concept embodied by the Wyckoff Spring. The prior low and shakeout point in the pattern simply becomes the long entry point as well as the selling guide once the stock is up and away.

In this way, one eliminates confusion over calculating some value for N while keeping risk to a minimum by entering the long position as close to the prior shakeout low as possible. In essence, the U&R is a much more precise entry method than the somewhat nebulous Shakeout-Plus-N concept.

Let's start with a very simple example in **Twilio (TWLO)** (Figure 2.64) from July and August of 2016. The company originally came public

in June of 2016 and quickly moved higher as it began to trade. Eventually it formed its first base and established a low in the base at 38.51 as it came in to test the 10-day moving average in mid-July.

Another shallow rally from there took TWLO back up near the left-side peak of the base before it again began to back down, undercutting the initial low 38.51 and then closing at 38.55 while also closing *below* the 20-day exponential moving average. That triggered a typical U&R long entry using the 38.51 low as a selling guide even though it closed below the 20-dema.

TWLO then continued to rally from there, quickly regaining the 20-dema and 10-dma and eventually breaking out decisively on the sixth trading day following the U&R that occurred on August 3rd. In this example, we also observe that the U&R occurs as part of a shakeout at the 20-dema, and once TWLO regains the 20-dema it does not look back.

Studying enough of these types of U&R set-ups, I saw many examples where there would also be a shakeout at a key moving average, such as the 20-dema, 50-dma, or 200-dma. From a practical standpoint, I began to realize that if one is uncomfortable buying a U&R that occurs just below potential moving average resistance, one could also wait for the stock to move back above the moving average which could then be used as a selling guide, which in TWLO's case would be the 20-dema in early August.

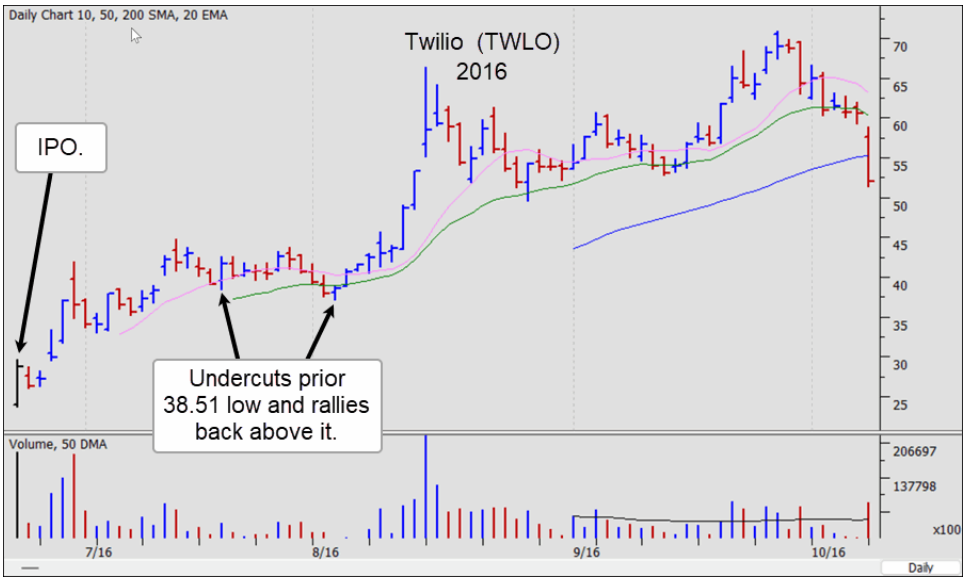


Figure 2.64 - Twilio (TWLO) daily chart, 2016. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Thus, the *moving average* U&R, acronymically known as the MAU&R, was born. U&Rs occurring at a prior shakeout low in a pattern were then categorized as *price* U&Rs, or just U&Rs for short, while U&Rs occurring at a moving average were categorized as *moving average* U&Rs, or MAU&Rs. They are two of the simplest OWL long entry set-ups as they are simple to define and recognize while simultaneously keeping risk to a minimum by using the prior price low for a U&R or the moving average for an MAU&R as a selling guide.

U&Rs and MAU&Rs are simple set-ups because they do not require any minimum volume level – they can occur on heavy, light, or just average volume. The price move does not have to be of any specific magnitude, just enough so that the stock first undercuts the prior low or moving average and then moves back above that prior low by any amount whether a penny, a dime, a dollar, or more. The primary objective of anyone keying a U&R is to enter as closely as possible to the prior low.

Price U&Rs also do not occur within a specific time period. They can occur at prior lows of just a few days ago, a few weeks ago, or in some cases a few months ago. When dealing with prior lows of more than

a few weeks ago I generally refer to these U&Rs as *macro-U&Rs*. The parameters, however, remain the same as for any U&R of any time period.

A fantastic example of a macro-U&R is **Roku (ROKU)** (Figure 2.65) in late December 2018. Following a huge price run throughout most of 2018, the stock went into a very steep and swift price decline that took it all the way back to where the initial 2018 price run began in March of that year.

That March 2018 low printed at 29.00 even, and as ROKU came streaking lower its price decline finally reached an endpoint on Christmas Even 2018 when it printed a low of 26.30. The next trading day, December 26th, it turned back above the 29.00 March 2018 low to close at 30.35, triggering a macro-U&R entry at that point using the prior 29.00 March 2018 low as a selling guide.

A few days later ROKU posted a bottom-fishing buyable gap-up (BFBGU) and never looked back from there as it streaked back to its 2018 highs. In this manner we see how an initial macro-U&R presaged the BFBGU a week or so later and gave one the first of two OWL Ugly Duckling long entries.

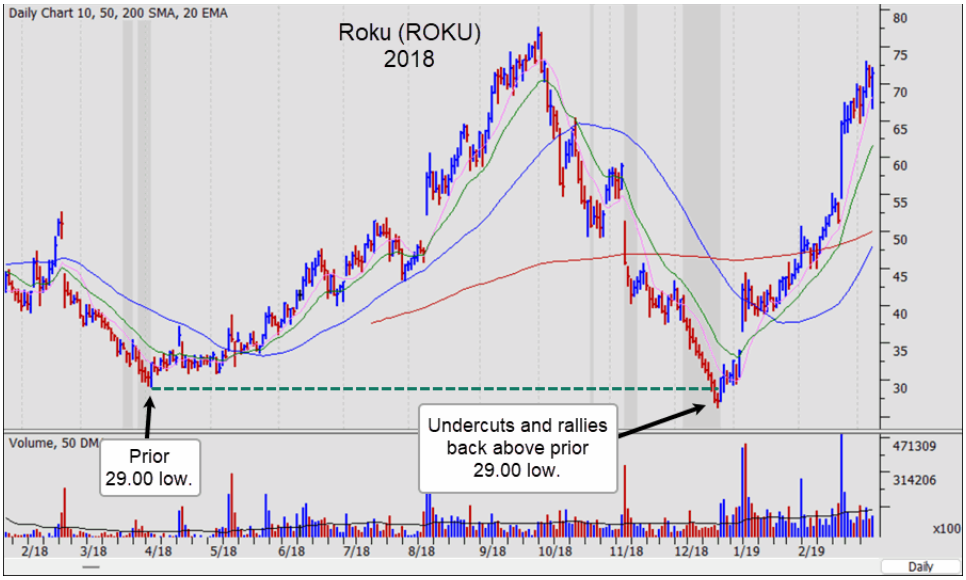


Figure 2.65 - Roku (ROKU) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Roku's (ROKU) (Figure 2.66) macro-U&R can also be viewed on the weekly chart. The weekly chart gives the pattern a much cleaner look, and we can see that coming in long on the macro-U&R and then the subsequent BFBGU allowed one to capitalize on the initial stages of what eventually blossomed into a massive price move to all-time highs and beyond.

Ask yourself, would you rather be first buying ROKU when it broke out of a deep cup-with-handle in March of 2019 or at the macro-U&R and BFBGU buy points much lower in the pattern and long, long before the obvious cup-with handle breakout? The answer should be clear.

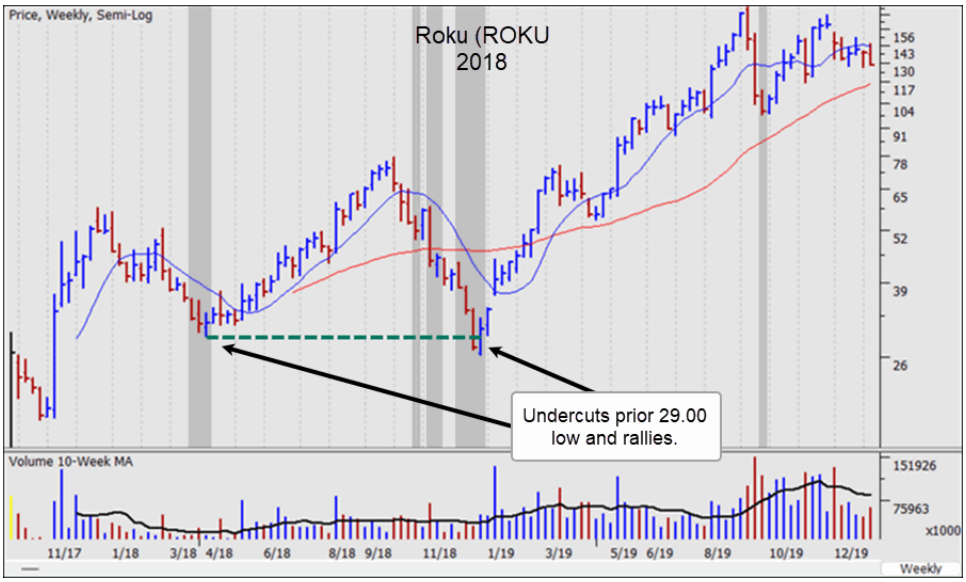


Figure 2.66 - Roku (ROKU) weekly chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Price U&Rs are often associated with general market lows following a correction or bear phase decline. Note that ROKU and the **NASDAQ Composite Index** (Figure 2.67) both bottomed out on the exact same day, Christmas Eve 2018, and then turned back to the upside just as ROKU posted its macro-U&R through the 29.00 March 2018 low on the very next trading day, December 26th.

While the synchrony between ROKU's U&R low and the NASDAQ's low in December 2018 might seem coincidental, in fact it is illustrative of the fact that many of the best U&Rs in stocks often correlate to lows or even similar U&Rs in the market indexes themselves.

As a result, such U&Rs tend to have a great deal of upside price velocity as they come shooting off the lows. This allows one to test the initial U&R in ROKU with perhaps a smaller position than they might otherwise be comfortable with and then let the price velocity do the work for them.

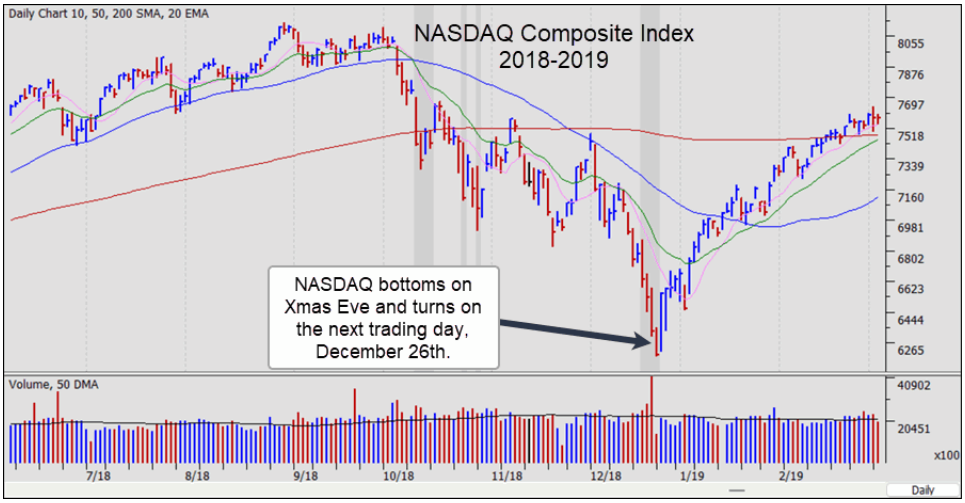


Figure 2.67 - NASDAQ Composite Index daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Market lows after corrections or deeper bear phases often correlate to U&Rs in individual stocks. Event-driven market shakeouts can also create conditions that are ripe for high-velocity U&Rs. In March of 2020 the general market was ripped to shreds as the Covid-19 Pandemic triggered a massive price collapse throughout.

At that time silver took a big hit as well, with the **iShares Silver Trust (SLV)** (Figure 2.68) imploding to a low 10.36 on March 18, 2020. As things looked to be at their most dire, the general market turned off its lows and began a massive new uptrend. The SLV followed right

along, rocketing higher the next week to trigger a macro-U&R along two prior lows on the weekly chart below at 13.11 and 13.39.

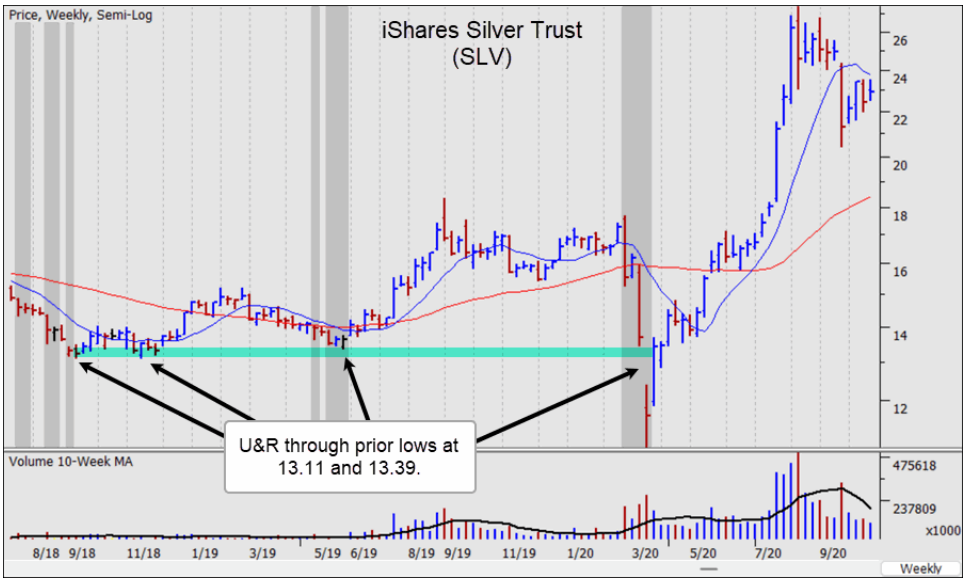


Figure 2.68 - iShares Silver Trust (SLV) weekly chart, 2022. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

U&Rs in some cases take a little time to get going, so one must be persistent as the stock in question bounces along or around a prior low. To account for this possibility, one can allow for 1-3% downside porosity below the prior low as a stop-loss point, allowing for some normal backing and filling along the prior low. My preference is to use a hard stop 1% below the prior low and remain flexible enough to come back in and buy the stock back if I am stopped out and the stock then recovers and again triggers the U&R at the same prior low.

In the example of **Alcoa (AA)** (Figure 2.69) in early December 2021 you will notice that the stock flops around the prior early November low for a few days before gaining some moderate traction and edging back above the 50-day moving average. From there it tracks along the 50-dma where it posts three five-day pockets along the line before pushing higher and breaking out later in December.



Figure 2.69 - Alcoa (AA) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

C3.Ai (AI) (Figure 2.70) in early 2023 is an interesting example as an extremely volatile, range-bound stock that never quite broke down while never quite breaking out despite some sharp price moves. In between, however, there were many actionable OWL long set-ups and short-sale set-ups that were playable as very profitable swing-trades.

The AI daily chart below has four upside spikes. The fourth upside spike at the far right eventually broke out and ran up to 44.02 the very next day, a move of 33.42% in a single trading session. AI then immediately retraced that one-day upside move and more with a 30.26% decline over the next two days.

These volatile, high-velocity, high-magnitude price moves that were AI's trademark during this market period, created insane trading opportunities, long and short. At the same time, they also resulted in the type of very dangerous and extreme whipsawing that can crush a trend-following trader or investor.

To play these moves, one had to adopt a highly contrarian approach, essentially scoffing at big-volume strength and laughing in the face of stifling and crushing downside breaks. We can focus on the long

side of this chart, reserving the short-side discussion of AI for the second volume of this book.

In this chart there are a total of four U&R long entry triggers. Every downside break posted one when it looked the ugliest. Let's look at all four. After a parabolic run-up into early February, AI then started pulling back and consolidating that exciting run-up. It established a low at 20.41 in early February and by late February was testing that low, undercutting it in early March and streaking higher in a glorious one-day move the very next day.

AI then pulled back and retraced all the way back to the prior low at 20.31, where the first U&R started. It then posted an undercut & rally long entry trigger when it undercut and ran up through that prior 20.31 low. From there, it worked its way higher before breaking out in a big-volume one-day move in late March. Would you stand in the way of that?

If you did, you made some quick money on the short side because AI's powerful breakout immediately failed and took all of two days to head back to the lows of the pattern where it bottomed out at 20.40. It then formed a short bear flag below the 50-day moving average and broke out to the downside to post lower lows along 200-day moving average support.

If you study the action along the 200-day line very carefully you will notice a couple of days where AI posted MAU&R long entry triggers along the 200-dma. It then began moving higher towards the prior 20.40 and 20.16 lows in the pattern where it posted a big-volume U&R as it slashed up through the 50-dma.

Carefully note that the final U&R was psychologically easier to buy since it occurred a) after AI had posted an MAU&R at the 200-dma and b) from a position where the stock had pulled into the 10-dma on a VDU volume signature. The very next day AI launched and began a 151.64% move as measure from the 10-dma to an eventual peak at 48.87 over the next five weeks. Nice work if you can get it.

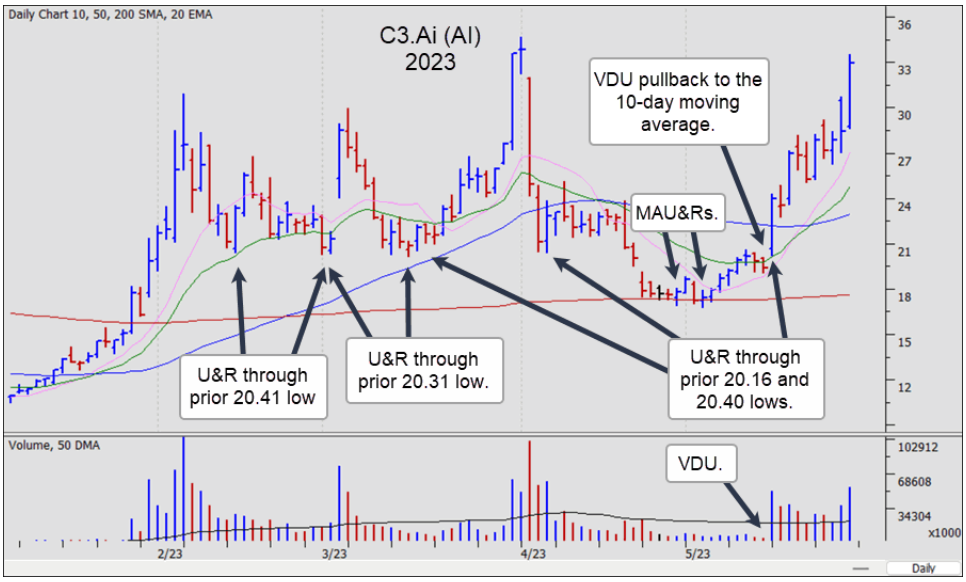


Figure 2.70 - C3.Ai (AI) daily chart, 2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Ride-sharing company **Uber Technologies (UBER)** (Figure 2.71) illustrates the need for persistence as it flops around a prior 29.97 low, moving above it on an intraday basis but then backing down to close below the 29.97 prior low. Chart context can sometimes be helpful here because you can see that UBER is attempting to post the U&R as it drifts downward from an early February peak. As it comes down it finds support along the 200-day moving average and in fact shakes out along the line the day before the second, decisive U&R.

That shakeout along the 200-dma is of course a moving average U&R or MAU&R at the 200-day line, which is in and of itself an actionable long entry trigger. In this case, maintaining awareness of the proximity of the 200-dma helps one to fixate less on the price U&R and remain open to perceiving and acting upon the MAU&R at the 200-dma.

We see this occur again in late May 2023 when UBER posts two days in a row that are both price U&Rs at the prior 37.36 low in the short base and moving average U&Rs at the 20-dema. This is not uncommon – often you will see price U&Rs occur around or even on the same days as moving average U&Rs.

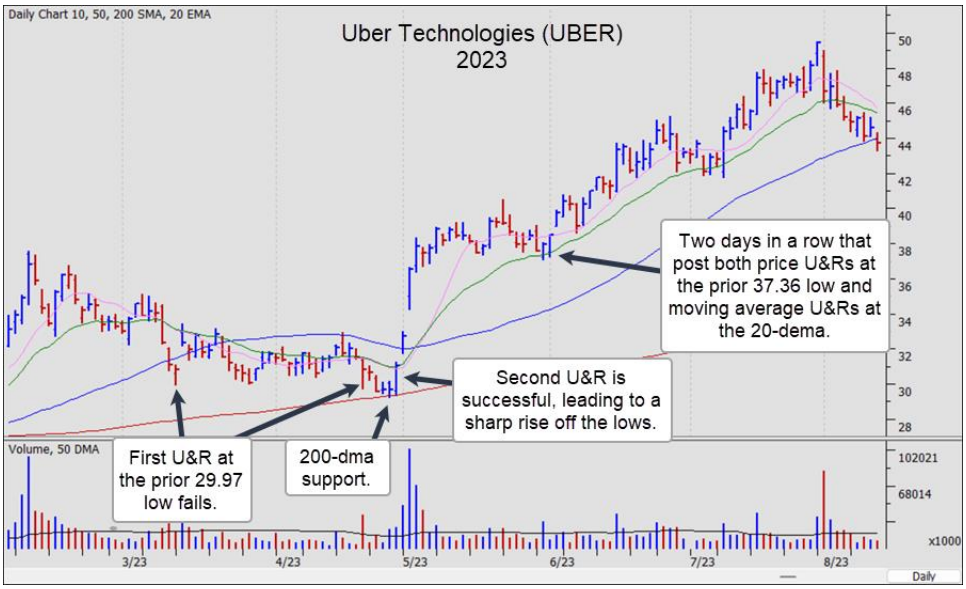


Figure 2.71 - Uber Technologies (UBER) daily chart, 2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

U&Rs often occur in funky ways, as the example of **Funko (FNKO)** (Figure 2.72) in March of 2018 shows. Note the big-volume buyable gap-up in early March that ultimately went nowhere before failing. That sent the stock back below the 10-dma and the 20-dema before it finally encountered its 50-day moving average. At that point, the stock was looking quite bearish on the chart, and the initial intraday dip below the 50-dma looked quite troublesome.

But FNKO surged back to life by quickly regaining the 50-dma to trigger a moving average U&R where the 50-day line is then used as a tight selling guide. That led to a three- to four-week consolidation that eventually tightened up and began flashing VDU long entry signals along the 10-dma and 20-dema. A pocket pivot near the end of that consolidation was the final signal before FNKO launched higher in what became a very rapid, parabolic price run that saw the stock nearly quadruple in a little over two months.

FNKO is another good example of how various Ugly Duckling OWL set-ups can come into play in sequence. It all started with the MAU&R along the 50-dma where an initial position could have been taken and then added to as FNKO posted VDU long entries along the

10-dma and 20-dema. The position could have then been capped off with one final add when the stock posted pocket pivots just before launching in the latter part of April 2018

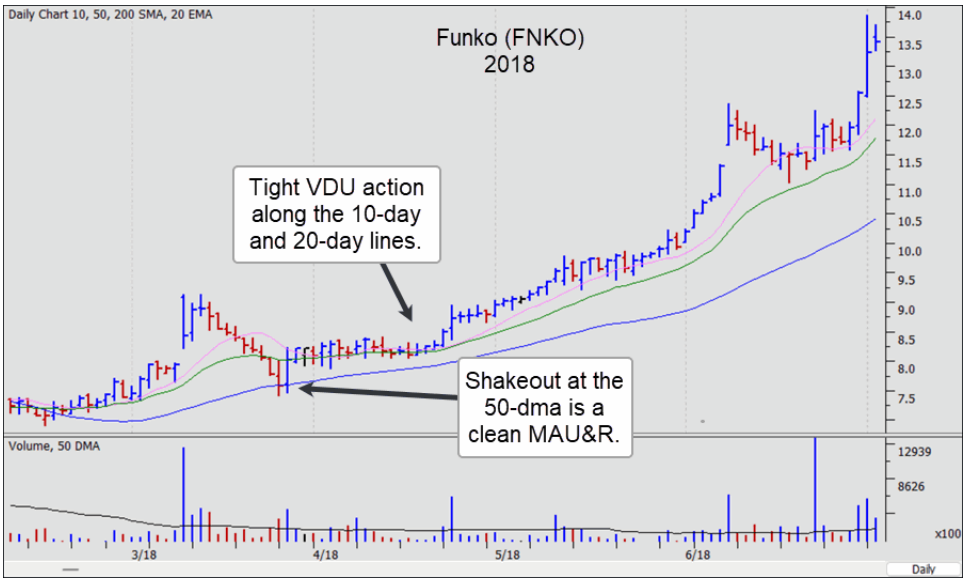


Figure 2.72 - Funko (FNKO) daily chart, 2018. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Some of the best U&R set-ups are those that occur quite abruptly as a stock remains locked in a downtrend from which escape seems impossible. After multiple weeks of downside action, the sudden turn when the crowd has likely turned quite bearish, a particular stock can work out very well.

Such was the case with **Freeport-McMoRan (FCX)** (Figure 2.73) in January and March of 2021. After a strong trending move that peaked in late December 2020 FCX nosed down and began slashing through near-term moving average support at the 10-day and 20-day lines. A gap-down move through the 50-day moving average in the second half of January 2021 looked like certain doom for the stock.

But at that point FCX suddenly found its footing and turned along the 50-dma as it shook out the last remaining sellers and closed back above the line to post a typical MAU&R long entry trigger. That resulted in a rapid price run-up and breakout to higher highs (note that the breakout in mid-February occurred on a BGU long entry trigger).

Once FCX peaked it began a base-building process that eventually led to a price U&R in late March 2021 as it undercut the prior 31.50 low in the base and then rallied. That was a relatively clean U&R long entry trigger using the 31.50 as a selling guide. FCX then spent another month finishing its base before eventually breaking out to higher highs once again.

If you study this chart very carefully you will observe that the OWL long entries, the MAU&R at the 50-dma in January and the price U&R in March were much more effective entries than buying the breakouts in the chart. The mid-February breakout started out nicely but was already failing within a couple of weeks.

That failure led to the ensuing base-building process and price U&R in March. So, ask yourself, would you rather have been buying FCX in early 2021 on the breakouts or the Ugly Duckling OWL long entry triggers. The answer to that question should be quite obvious.

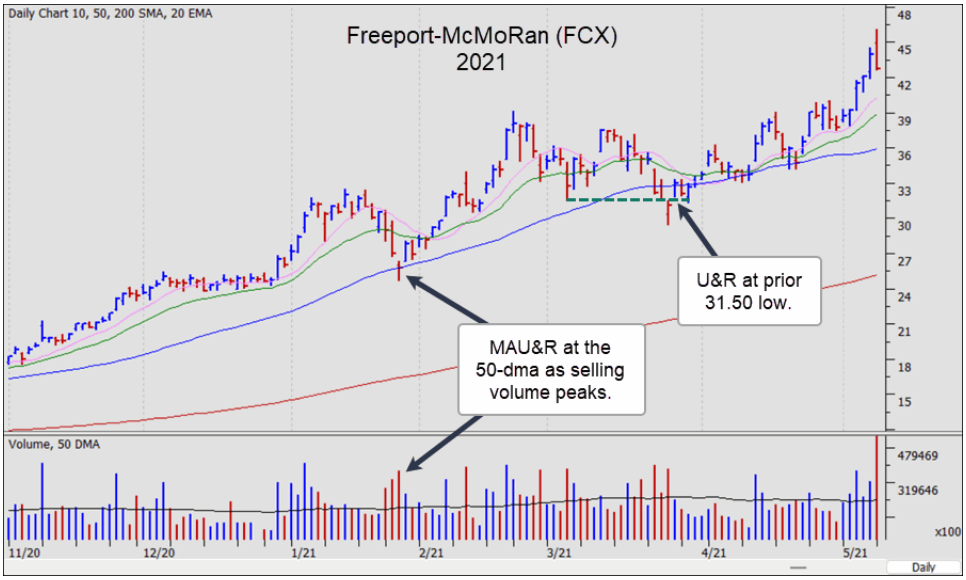


Figure 2.73 - Freeport McMoRan (FCX) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

October 2023 provided a highly instructive example of how these Ugly Duckling OWL set-ups and signals do not exist in a vacuum. Market

context is always critical. Aside from various news and other developments regarding the company whose stock is in question as a potential U&R or MAU&R long entry, the general market can often play a very important, overriding role.

This would include general market activity, news and developments at the company whose stock is showing these signals. Even more importantly, a unique aspect of U&Rs in general is that they can often help one figure out when the market has likely bottomed out. I do not rely on O'Neil's so-called *follow-through day* as an all-clear signal to start buying stocks for the simple reason that it is highly unreliable.

When I ran money for Bill O'Neil, I questioned him constantly about the whole follow-through day concept since there were numerous statistical studies being released at the time that proved follow-through days mostly fail. HIs response was a standard, "all bull markets start with a follow-through day but not all follow-through days start a bull market."

The more important side of the question, as he put it, was the action of individual stocks. When the market follows through then if there is nothing to buy, e.g., at least one leading stock breaking out of a proper base, then you buy nothing. In essence, market turns always center around the action of individual stocks, and the U&R creates a unique tool for detecting potential turns and bullish action in individual stocks, long before any breakouts occur.

In late October the **NASDAQ Composite** (Figure 2.74) was in a classic three-waves-down sell-off as leading stocks were getting kicked around. As the sell-off became obvious, bearish sentiment as measured by sentiment indicators such as the American Association of Individual Investors Bull/Bear Indexes and the National Association of Active Investment Managers (NAAIM) Exposure Index began to reach a crescendo. From a positioning standpoint, institutional buying of puts had also reached high levels.

Based on my own research of market bottoms, whether intermediate-term or longer, these sorts of anecdotal factors were meaningful. All I needed to see at that time was concrete technical action that would

help to highlight a potential market turn. In late October 2023 that came as the NASDAQ Composite undercut its 200-day moving average and then rallied back above it – a typical MAU&R long entry trigger.

That was followed a few days later by a price U&R coming up through the prior low of the second selling wave in late September. At the time I wrote a post to The OWL Market Feed indicating that the market was ready for at least a meaningful reaction rally.

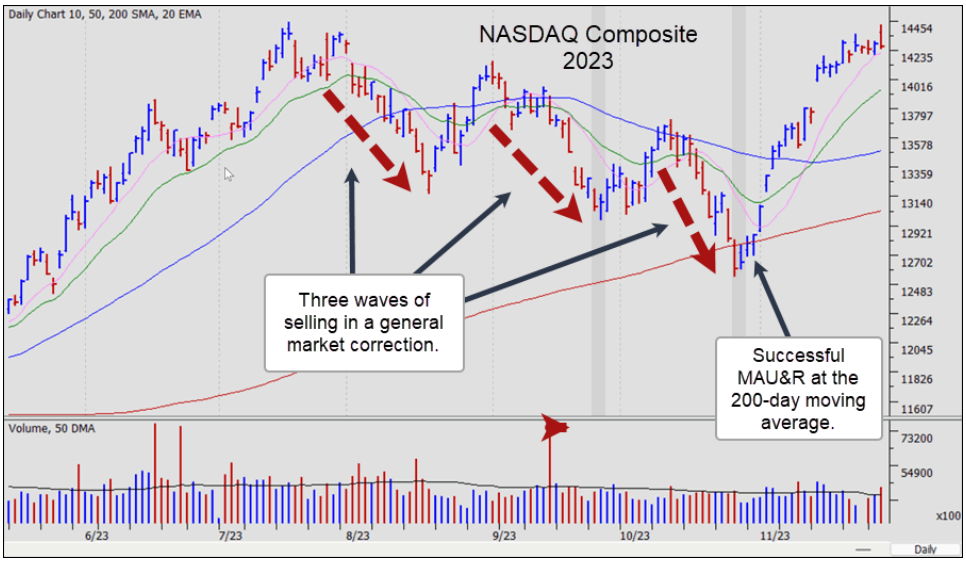


Figure 2.74 - NASDAQ Composite Index daily chart, 2023. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

At the same time, we also saw undercut & rally (U&R) long entry triggers in several beaten-down big-stock leaders. One of these was big-stock tech juggernaut **Apple (AAPL)** (Figure 2.75) as it posted a price U&R in late October. This occurred in synchrony with the MAU&R move in the NASDAQ Composite

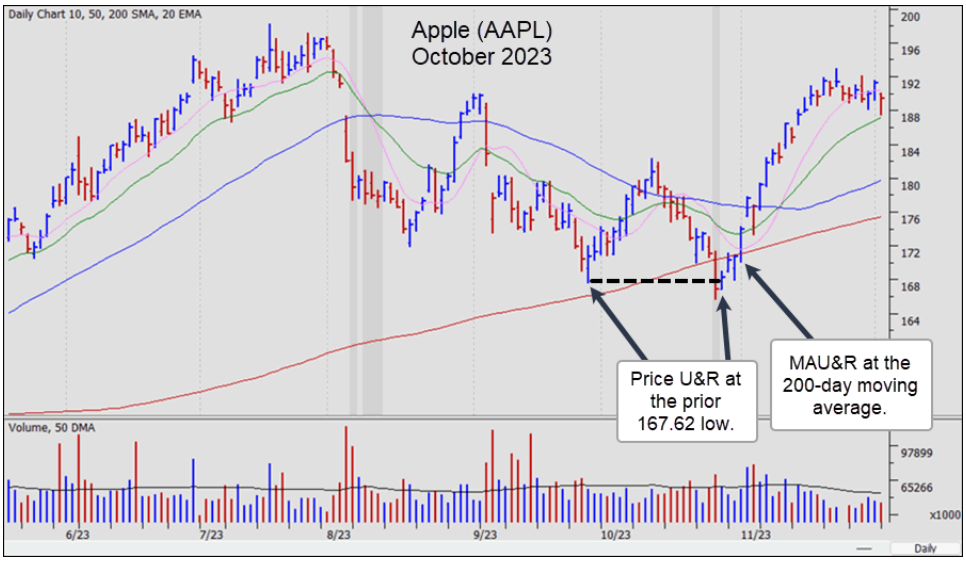


Figure 2.75 - Apple (AAPL) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

Keeping in perfect time with the synchronous U&R action seen in the indexes and a broad number of individual stocks in late October 2023, big-stock semiconductor leader **Nvidia (NVDA)** (Figure 2.76) posted its own U&R move at the prior 403.11 August 14th low. Note that one day later the stock posted another U&R at the 409.80 low of September 21st but using the first low was preferable as an earlier and lower entry point.

Both worked, however, as NVDA launched higher and never looked back. NVDA then spent some time basing just below the $500 Century Mark before eventually breaking through in early 2024. The lesson here is simple. Often, when U&R or MAU&R action is seen in one or more of the major market indexes, coincidental and synchronous U&Rs and MAU&Rs in beaten-down leaders may not only help to confirm a possible market turn but also provide your earliest and best long entry candidates, long before any standard-issue O'Neil-style breakouts occur.

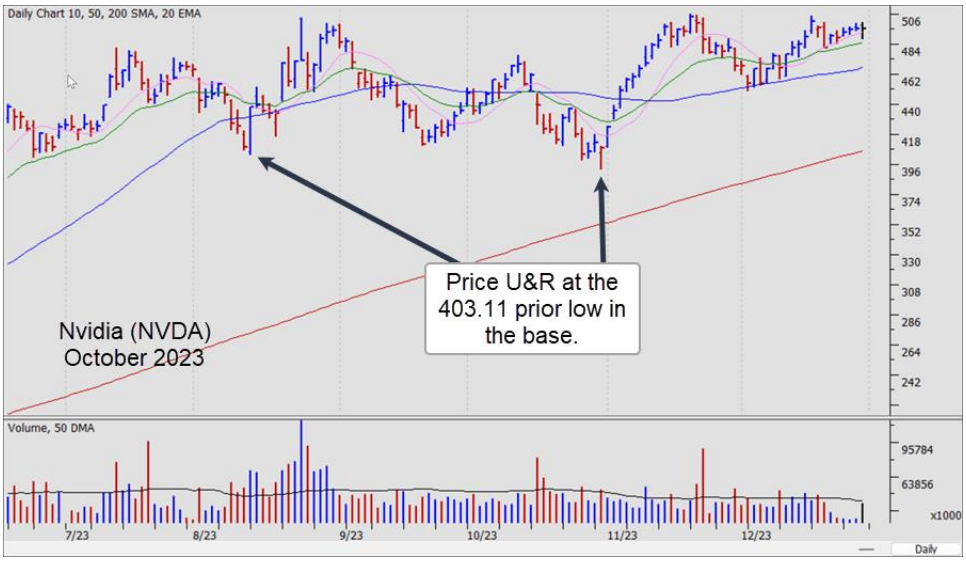


Figure 2.76 - Nvidia (NVDA) daily chart, 2021. Chart copyright 2024 HGS Investor Software, LLC, used by permission.

The price undercut & rally (U&R) and moving average undercut & rally (MAU&R) long entry set-ups are the most common OWL set-ups that you will likely see in the market. They can occur under a variety of market conditions, but the most important aspect of U&Rs is that they can be acted upon fearlessly as close to the relevant prior low as possible. This then keeps risk to a minimum as the prior price low serves as a tight selling guide.

Chapter 3: Odds & Ends

Timing & Risk Management

From a risk-management perspective, OWL long entry set-ups are much more optimal and efficient than relying solely on standard-issue base breakouts. Entries are simple – you seek to enter as close to the precise trigger point, whether a moving average or price low, as possible. When it comes to stops and selling guides, one simply uses prior price or moving average support levels as *selling guides.*

Remember, there is no perfect stop-out point. The chance that you will be stopped out of a position only to see it suddenly turn and rally back above your sell point is always real. But I must say, using a standard O'Neil-style 7-8% stop-loss policy is not only the least perfect of any that I have ever used.

It is far more efficient to use nearby price or moving average support levels as references for selling guides with the knowledge that you may very well be stopped out too quickly. But, when I am asked what the solution to this is, the answer is simple, in my view. Simply remain flexible enough to come back in if the stock turns and sets up again.

Generally, I operate based on using a maximum of 1% beyond the specified selling guide, e.g., 1% below the 50-dma if that is my reference level for a pocket pivot or MAU&R, or 1% below a prior low in the case of a U&R set-up. In some cases, I will run it even tighter than that, using the moving average or prior low as a hard stop with the idea that I can come right back in if the stock turns around and sets up again.

This approach suits my psychology since I would prefer to remain flexible taking tiny losses around a legitimate area of potential support than just sitting there on a wall like Humpty Dumpty willing and ready to take a 7-8% great fall. Since trading and investing is a very personal thing, you may feel differently.

Depending on one's own psychology and risk-preferences, one can also take an approach using a stop 2-3% beyond the specified selling guide reference point. This can be combined with using smaller position sizes since some set-ups can develop some very sharp upside price-velocity once they are triggered. The examples above demonstrate that, so it is possible to use a stop of 2-3% beyond a selling guide with a combination of smaller initial position where you look for price velocity to develop and do the work for you.

Final Thoughts

The OWL approach is rooted in the foundational philosophies and methods of my mentor, William J. O'Neil, Richard D. Wyckoff, and Jesse Livermore. What is most notable about these three legendary investors is that throughout their careers they remained honest students of the market. We should all strive to follow their example by ourselves being honest students of the market.

This should be conducted according to an ethic of *working smart*. We often hear about how someone says they will "work hard to earn it," but in my view only fools work hard. Working hard for the sake of working hard strikes me as an inefficient approach more suited to those who somehow think that self-flagellation is a path to success. It is not. OWLs work smart. Think carefully about this, because there is a difference.

This book is merely an introduction to the OWL methodology. It is also not a long book, as it was intended to serve as a *handbook*, perhaps not unlike my old Boy Scout Handbook that laid out the basics and let you head out on the trail on your own, ready to deal with and adapt to any unique and not-so-unique challenges or conditions you may face. Remember also that, as Bill O'Neil wrote in his iconic investment book, *How to Make Money in Stocks*, common sense should prevail. May the froth be with you!