

Stocks: Hidden Blueprint for Profiting In Stock Trades - Entering, Holding and Exiting - Part 2

Once you've put the time and effort into coming up with a sound trading plan for your stock trades, and have found a good trading opportunity, it makes sense to start the trade right. Finding a good point to enter into a position involves several issues. First, you must know the time frame of your trade. For a particular trend stock trades, for example, you might know that you should enter no earlier than a week before the event creating the trend. Next, you must examine charts to see where the stock trades have been and where its support and resistance levels are, and think about its psychological support and resistance levels as well. Last, you should wait for a pullback in price if you believe that the price is temporarily high and that it will drop and create a better buying opportunity for you.

The way to make sure you enter where you plan to is to use a limit order. A limit order is an order that can execute only at the stated price or better. Limit orders sometimes make you wait behind others who placed their orders at the same price before you did, but in most situations, placing a reasonable limit order is the only smart way to enter a position. In certain situations, it may make sense to stagger your entry by buying half the shares you want at a price you think may be the lowest the stock trades will reach, and then waiting to buy the other half either when the price does get better, averaging down, or when the stock trades starts to move, adding on strength.

The wrong way to enter a position is to chase moving stock trades. Chasing stocks is a form of panic, and it practically guarantees that you'll pay too much for the stock. Why is it so bad to pay too much? The more you pay for stock trades, the further your risk to reward ratio is shifted away from reward and toward risk. This happens because your upside has decreased due to the high price of the stock, and because the probability of the run ending increases as the stock gets more and more expensive.

There are two ways to look at the decrease in your upside: First of all, you'll capture less of the stock's movement, so your percentage return will be less; second, the more the stock trades costs per share, the fewer shares you'll be able to buy. Which means that any return you get will be multiplied by fewer shares. Remember, it doesn't matter if you miss a trade or a position because the entry price has gotten too high. It's not the last good trade in the market. There will always be more stock trades to make. It's much better to miss a trade than to chase a stock and end up with a loss.

Morning gaps down present good opportunities to buy stocks you want. Buying a gap down is an excellent way to enter a position, since when a stock gaps down, it often opens near what will turn out to be the low of the day. On the other hand, buying a gap up is one of the worst stock trades you can make. The gap up generally reflects the top of the market's level of interest in the stock. Any good news from overnight has generally been priced in, so the stock's opening price and volatility on a gap up often establishes the stock's high of the day. Therefore, buying, or really chasing, the gap up means that you will likely buy the stock for top dollar. A good trader buys stocks that have an upside that hasn't been priced into the stock.

Entering a short position on a gap up is a great plan, though shorting a gap down is foolish. The opening price and volatility on a gap down often establishes the stock's low of the day, so shorting at the lowest point would be a poor trade to make. However, if you keep these guidelines in mind, you will be able to find a safe entry point for your trade. One that fits with your trading plan, and puts you on the path to consistent trading success.

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About the Author

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