

AIQ

Opening Bell

Newsletter

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Opening Bell Interview with Dan Zanger

How Does He Do It? AIQ User Holds World Record for One-Year Portfolio Appreciation

By David Vomund

This month we are pleased to present an interview with Daniel Zanger, publisher of Chartpattern.com. Dan has used AIQ's TradingExpert since 1992. Dan holds the world record for one-year portfolio appreciation, gaining over 29,000%. In about two years, he turned \$11,000 into \$42 million! As a result, he was featured in *Fortune* magazine. Dan is a frequent speaker at AIQ's fall seminars at Lake Tahoe.

Vomund: *At the height of the bubble you set the world record for portfolio appreciation. Can you tell us about that experience?*

Zanger: I'd love to except that we don't have enough space or time here to write about it to give this topic justice for either the reader or me. I will say it was a life changing experience of epic proportions and I'm thrilled that it happened to me.

Vomund: *Can you update us on what*

happened to this portfolio during the bear market and during the bull of the last two years?

Zanger: As you know, the tax rate was over 40% at the Federal level back then, and then add in the 10% California tax rate, Social Security, and a few other items and I kissed over 50% of



Dan Zanger
Chartpattern.com.

"With the strong bull market we've had over the past 24 months I'm back in the saddle again and if 2005 is as strong as the last 2 years, I should easily get back to the \$40+ million range where I was at the top."

it good-bye quickly. Then one day the fiber optic sector gapped down close to 20% at the open and I was fully margined 2 to 1. There went another 30% of

what I had. I then whittled down the rest over the next two years as the market plunged 80% to where I retained just about 17% of what I had at the very top.

However, with the strong bull market we've had over the past 24 months I'm back in the saddle again and if 2005 is as strong as the last 2 years, I should easily get back to the \$40+ million range where I was at the top.

Vomund: *Has your approach changed over the years?*

Zanger: I have not changed my trading style at all during bull markets such as the one that began in March 2003. What has changed is that I now understand what a major bear market is all about and the devastation that a once every 30 or 70-year bear market can bring. I can assure you that when the next big bear comes around I will be out on my yacht in the Mediterranean or the Caribbean and not trading the market at all. I will say that one must experience every trading situation and market condition to be able to fully take advantage of

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While the information in this newsletter is believed to be reliable, accuracy cannot be guaranteed. Past performance does not guarantee future results.

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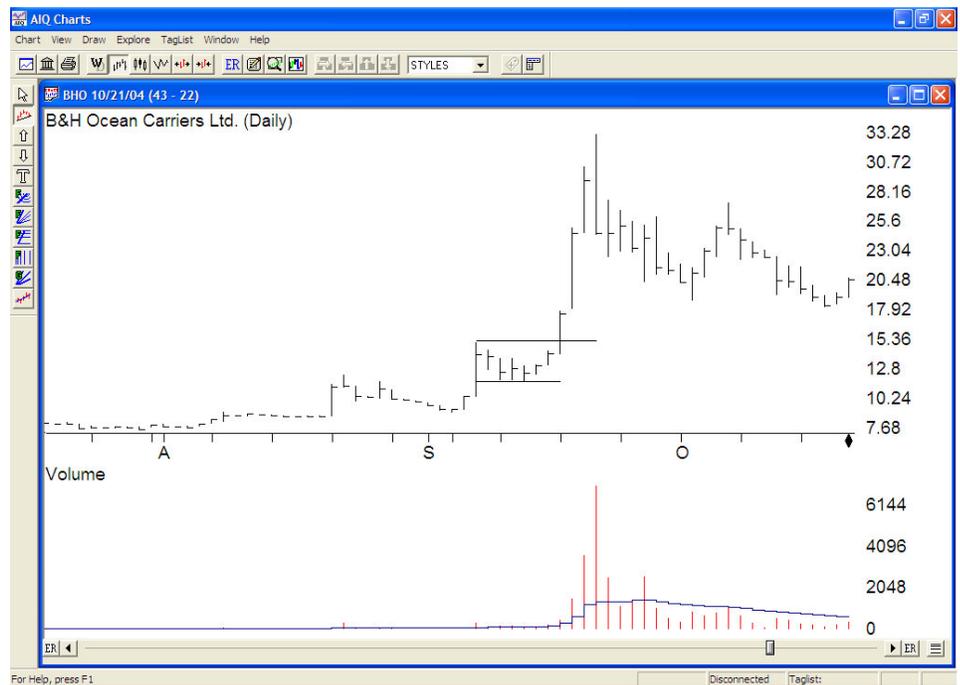


Figure 1. Daily chart of B&H Ocean Carriers. The Bull Flag pattern that developed in early September 2004 preceded a sharp price increase on heavy volume.

current circumstances, and I'm now fit to take advantage of being out of the market when the next bear comes around.

Vomund:
What are TradingExpert's most valuable features?

Zanger: For years the Tag List has been the most important feature. This tool allows me to manually churn through 1300 or more stocks every night in rapid fire succession. There is nothing better than to look at a ton of charts every night. This will hone your skills on identifying chart patterns faster than anything else out there today. In fact, I would say that if it weren't for this tool my learning curve would be years behind. There is no substituting this feature or the time necessary to learn pattern analysis. At least 15 hours a week is a minimum to learn this, plus it is important to follow the market most of the day.

Vomund: *You monitor lots of stocks each day. How do you determine the Tag List of the stocks you track most closely?*

"I now understand what a major bear market is all about and the devastation that a once every 30 or 70-year bear market can bring. I can assure you that when the next big bear comes around I will be out on my yacht in the Mediterranean or the Caribbean and not trading the market at all."

Zanger: I'm looking for stocks that make big moves so when I see a stock up \$3 or more on heavy volume day in and day out, I add it to my Tag List. Most stocks that I load in die shortly after this initial move, but often reemerge for a second move up later and I want to be there when they do that. The only way to do that is to track all of them every day so that you are ready to grab them when they move.

Vomund: *Your analysis is almost*

completely dependent on price patterns. Can you explain why they are so important and why indicators play only a small role in your analysis?

Zanger: It's more than just price patterns; it is the combination of patterns and price action of the stock during the day plus the strength of the groups that these stocks are in that makes my stock selections so powerful.

Indicators are lagging in nature so by the time they issue a buy or sell signal or tell you that a stock is weakening or strengthening the stock might have already moved 5 to 20%. This is way too late for me. You have to know the meaning of each daily bar combined with its volume to get in or out of a position at what can often turn out to be critical times.

Vomund: *What are some of your favorite price patterns?*

“It is the combination of patterns and price action of the stock during the day plus the strength of the groups that these stocks are in that makes my stock selections so powerful.”

Zanger: One of my favorite patterns is the Bull Flag pattern. This is a continuation pattern and for the most part a stock has already broken out and has succeeded since the breakout. A Bull Flag occurs after a rapid and fairly extensive advance. After a nearly vertical move, the stock fluctuates sideways in a narrow range. The completion of the pattern occurs on a break above the consolidation, ideally on heavy volume. A good example of a Bull Flag is found in **Figure 1**.

Vomund: *You pick very high growth stocks. These stocks go up fast, but can fall even faster. Please tell us about how you protect the downside.*

Zanger: For me it's the behavior of the stock more than anything else. Also, how long the stock has moved

up and how far it has moved up from its base has a lot to do with getting out before it takes a big hit. When I get caught in a falling stock these days it's because my trade size is very large and the float is small and it can take days to effectively get out before a stock gets whacked.

Travelzoo (TZOO) is a case in point. I owned 10% of the total outstanding float of this company back in August of 2004, which amounted to over 100,000 shares. This stock had a huge run from the mid \$60 area to over \$100 in just a few short weeks. I was selling shares all the way up

and was not completely out when news hit the wire that the owner of this company just sold a meager 30 thousand shares of his holdings. This guy owned

80% of the company, which equates to over 10 million shares, so what's 30 thousand shares? Well the street went nuts and this stock tanked over \$12 in an hour and I was not completely out of it, so down I went selling with the other folks. I got tagged for \$12 on about 40,000 shares but still made a huge chunk of money on the whole experience.

Vomund: *What market timing techniques do you use to determine the health of the market?*

Zanger: I use a lot of them, but the one I use most is the McClellan Summation Index. This works pretty good, but nothing works better than watching the charts set up on the leading stocks. This is by

“The Tag List tool allows me to manually churn through 1300 or more stocks every night in rapid fire succession. There is nothing better than to look at a ton of charts every night. This will hone your skills on identifying chart patterns faster than anything else out there today.”

far the most important timing mechanism out there today. That is because no market can rally unless stocks are set to move up from solid basing patterns.

Vomund: *Can you give us some examples of your newsletter stock picks, including when and why they were bought and sold.*

Zanger: A good example of a stock that I've made lots of money on both long and short is Travelzoo Inc. (TZOO) in **Figure 2** (page 4). The down arrows represent buy points. The August buy came after a

“Nothing works better (for market timing) than watching the charts set up on the leading stocks. This is by far the most important timing mechanism out there today. That is because no market can rally unless stocks are set to move up from solid basing patterns.”

mini-Bull Flag pattern. TZOO more than doubled in price after then. In November and December it was hard to trade. A support trendline was broken in early January and

then completed a Bear Flag in mid-January. TZOO was shorted below \$78 when its support trendline was broken.

In today's falling market environment it is also useful to show a stock like Research in Motion (RIMM) found in **Figure 3**. We bought this stock in November 2003 at \$22, but big moves can last only 8 to 20 months before they cave in. RIMM has topped out and currently looks like many other expired growth issues. Don't jump into a falling stock. A good rule is to never own a stock that is below a descending trendline.

Vomund: *Now that you've lived on both coasts, is it easier analyzing and trading stocks on East Coast time or West Coast time?*

Zanger: There is nothing better than trading on the East Coast. I used to have to go to bed around 9:00 pm on the West Coast, which meant coming home early from dinner parties. I had to get up at 5:00 or 5:30 am, get my coffee, turn on the monitors, and bone up on a few selected news items. I'm not a morning person.

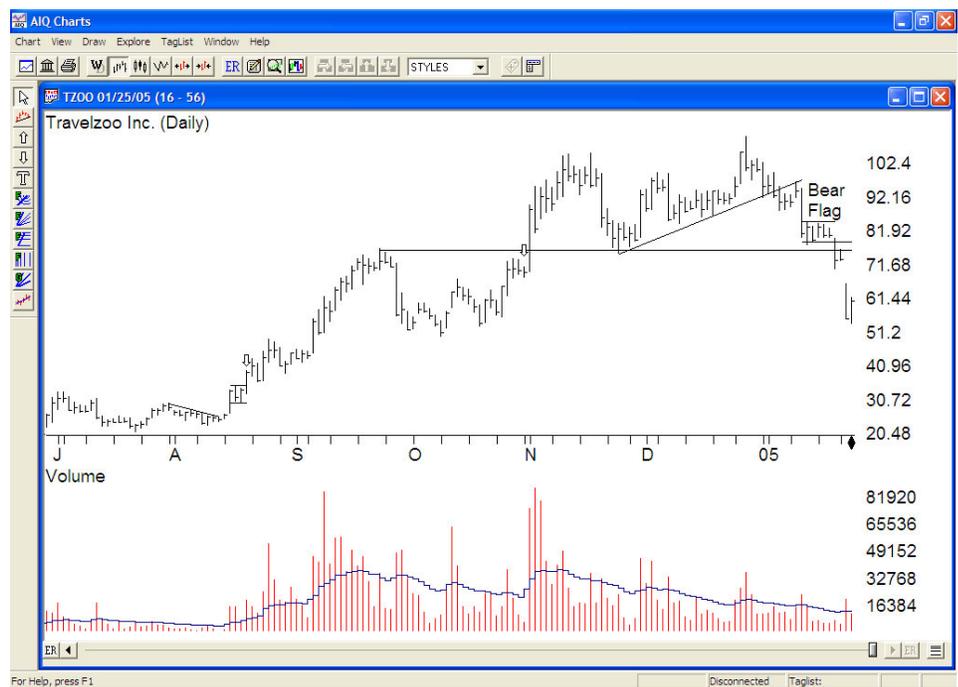


Figure 2. Daily chart of Travelzoo Inc. Down arrows shown on chart signify buying points. Stock was shorted in mid-January following completion of Bear Flag pattern (drawn on chart).

Now that I'm on the East Coast nine months of the year, life is so much better. Now I can stay out till midnight and get up at 8 am and still have an hour and a half to get ready before the market opens. I even have time for a morning swim or jog, or maybe even head into South

Beach Florida where I live today and grab a Starbucks. Life for the trader is very good on the East Coast.

Vomund: *Thanks for sharing your thoughts with us.*

More information on Dan Zanger can be found at www.chartpattern.com.



Figure 3. Daily chart of Research In Motion Ltd. an example of a stock that peaked near the end of 2004 and is currently continuing to decline.

MARKET REVIEW

The market fell three straight weeks in January, the first time that has happened since 1982. For the month, the S&P 500 fell 2.6% and the Nasdaq Composite fell 5.23%. The Russell 2000, which has led the market higher over the last two years, fell 4.2%. Most of the damage came during the first three trading days of the month.

The S&P 500 fell right to the March 2004 high, which represented the high point of an eight-month consolidation. What was resistance became support as the S&P 500 bounced off that level during the last week of January.

Dogs of the OEX Value Strategy

Try 'Dogs of the OEX' When Value Investing Outperforms Growth Investing

By David Vomund

When President Bush cut the dividend tax rate, it made dividend-paying stocks more attractive. In past research, we found that dividend-paying stocks have less growth potential but they offer more stable returns. The dividend paying stocks shine during times when value investing is in favor. In this

popularity. Mutual funds were formed to follow that specific strategy. Its popularity waned in the late 1990s as growth investing became the rage. The Dogs of the Dow strategy is a value strategy so it underperformed badly at the height of the bubble. Since then, its

performance relative to the S&P 500 has improved but the high yielding

“This is how the Dogs of the OEX strategy works: On January 2 of each year, we purchase the 10 highest yielding stocks in the S&P 100 and hold them for an entire year, at which time a new list of high yielding stocks is purchased.”

article we'll update the "Dogs" strategy that we first presented in the March 1998 *Opening Bell*.

In the mid 1990s the Dogs of the Dow investing strategy gained great

stocks still haven't responded as well to the tax cuts as many predicted.

The key to this strategy is that the stocks that are purchased are all high-yielding well-established stocks. The strategy buys those stocks in the Dow that have the highest yield and holds them for an entire year.

In the March 1998 *Opening Bell*, we took the concept of the Dogs of the Dow strategy and modified it to comprise a broader set of large-cap stocks. Our concern was that too

Table 1. Dogs of the OEX Yearly Returns

Year	Dogs Return (%)	S&P 500 Return (%)
1995	32.65	37.58
1996	16.23	22.96
1997	27.34	33.36
1998	4.77	28.58
1999	4.72	21.04
2000	9.35	-9.10
2001	19.40	-11.89
2002	-19.45	-22.10
2003	33.89	28.69
2004	7.89	10.88
Avg. =	13.68	14.00

many people were following the Dogs of the Dow strategy and for that reason it would stop working. Since the strategy relies on choosing stocks with high yields, in our modified approach we picked the highest yielding stocks in the S&P 100 index (otherwise known as the OEX).

This is how the Dogs of the OEX strategy works: On January 2 of each year, we purchase the 10 highest yielding stocks in the S&P 100 and hold them for an entire year, at which time a new list of high yielding stocks is purchased.

Table 1 shows the yearly returns of our Dogs of the OEX strategy. Dividends are included in these returns. Notice that the average yearly return for the Dogs of the OEX strategy is about the same as

Table 2. 2005 Dogs of the OEX

Ticker	Stock Name	Yield
SBC	SBC Communications	5.0
GM	General Motors	4.9
T	American Tel & Teleg.	4.9
MRK	Merck & Co.	4.7
MO	Altria	4.7
BMJ	Bristol Myers Squibb	4.3
SO	Southern Co.	4.2
AEP	AEP	4.0
VZ	Verizon Communication	3.8
BAC	BankAmerica	3.8

the yearly return of the S&P 500.

The return from the Dogs strategy, however, is more stable than a buy-and-hold approach. Over the 10-year time period, there was only one down year.

Looking closely at the returns in Table 1, the Dogs strategy performed poorly in 1998 and 1999 when growth investing was in favor at the height of the bubble. During the 2000-02 bear market, value investing held up while the rest of the market fell hard.

A list of the stocks that make up the 2005 Dogs of the OEX is shown in Table 2. For this strategy, these stocks are held through the rest of this year.

I realize that holding stocks for an entire year is not a strategy that most AIQ users are interested in. The analysis is still helpful, however, as users may choose to analyze these stocks individually or buy a basket of these issues during times when value investing outperforms growth investing.

Figure 1 shows the Nasdaq 100 index on the top of the chart and the Dogs stocks on the bottom of the chart. Notice during bullish periods, such as in late November, the growth stocks in the Nasdaq 100 tend to outperform. During bearish periods, however, the Dogs hold up better.

To find the 2005 Dogs of the OEX stocks, we downloaded an AIQ list of the Nasdaq 100 stocks from AIQ's web site at www.aiqsystems.com. To get the yield for each S&P 100 stock, we used AIQ's Fundamental Module on the first trading day of the year and retrieved yield information for each stock. This information was sorted from highest to lowest. You can't retrieve historical funda-

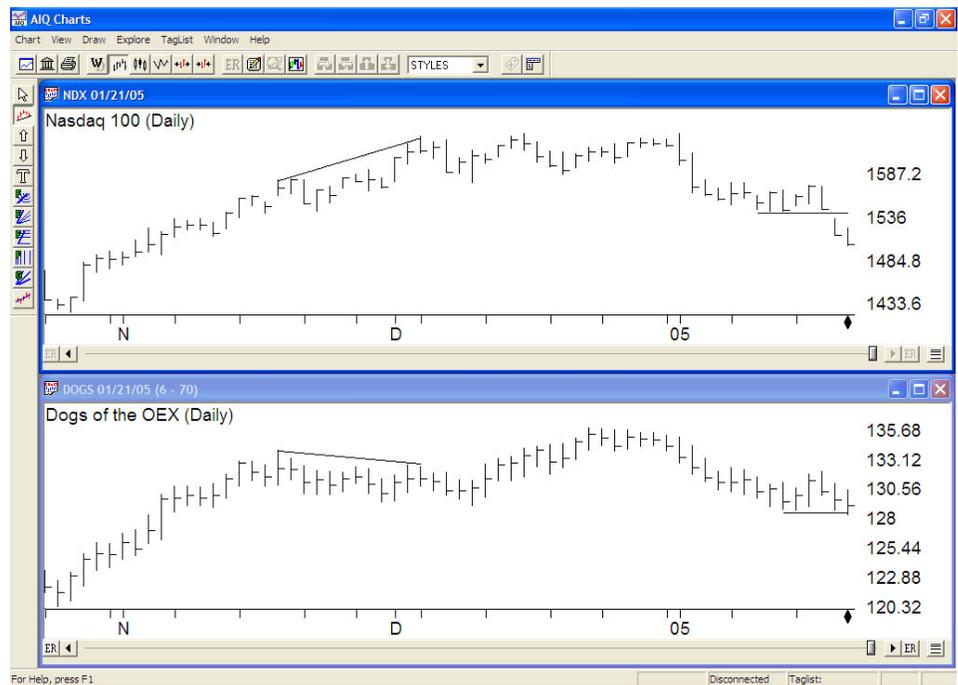


Figure 1. Comparison of Dogs of the OEX (lower chart) and Nasdaq 100 (upper chart). Charts show daily price data for three-month period, mid Oct. 2004 to late Jan. 2005.

mental information so it is important to run this function on the first trading day of the year.

At the beginning of each year, we'll update the performance of the Dogs of the OEX strategy. In an

upcoming issue we'll cover a strategy that switches between growth and value stocks by trading two Exchange Traded Funds.

STOCK DATA MAINTENANCE

The following table shows stock splits and other changes:

Stock	Ticker	Split	Approx. Date
Wolverine World Wide	WWW	3:2	02/02/05
Micros Systems	MCRS	2:1	02/02/05
Matria Healthcare	MATR	3:2	02/07/05
Fast Set Research	FDS	3:2	02/07/05
Tarragon Corp.	TARR	3:2	02/11/05
Bio-Logic Systems	BLSC	3:2	02/14/05
World Fuel Srvcs.	INT	2:1	02/16/05
eBay Inc.	EBAY	2:1	02/17/05
TALX Corp	TALX	3:2	02/18/05
Interchange Fin'l	IFCJ	3:2	02/21/05
Chico's FAS Inc.	CHS	2:1	02/23/05

Trading Suspended:

First National Bankshares of Florida (FLB); Peoplesoft (PSFT); Stelmar Shipping Ltd. (SJH); TransTechnology Corp (TT)

Name Changes:

Ivanhoe Mines Ltd. (HUGO) to Ivanhoe Mines Ltd. (IVN)
Z-Tel Tech. (ZTEL) to Trinsic Inc. (TRIN)

S&P 500 Changes

There are no S&P 500 changes this month.

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David and Steve will show seminar attendees a variety of ways to make money in the market with AIQ TradingExpert Pro. Attendees will see specific trading systems being used by full-time traders in the current market, as well as see how the systems were developed and tested on the AIQ tools. This is a fantastic opportunity to learn from two experienced AIQ users who actively participate in the market everyday.

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Speaker Biographies

Over 70 attendees participated in AIQ user Steve Palmquist's seminar at the 2nd Annual Las Vegas Traders Expo Sunday November 21, 2004

Steve's session on learning proven methods for improving your results in current market conditions from a full time trader was a big success at the Las Vegas Traders Expo. Attendees learned how to use Market Adaptive Techniques (MAT) for dealing with specific trading environments, and how to use that information to select setups and adjust holding timeframes.



Steve Palmquist

Steve Palmquist is a full-time trader with nearly 20 years of experience. He is the founder of www.daisydogger.com, which provides free market analysis, trading tips, and educational material. Steve is also publisher of the Timely Trades Letter available through the web site. Steve was a featured speaker at AIQ's October Lake Tahoe Seminar.

David Vomund is AIQ's Chief Analyst, AIQ Opening Bell monthly editor, VISalert.com publisher and experienced money manager and market timer

David has earned a reputation as one of the country's top market timers. He teaches his analysis techniques to hundreds of individual and professional investors each year. David has been published in Stocks & Commodities and Active Trader magazines, and was a contributing author to Computerized Trading.



David Vomund

David Vomund, the chief analyst at VIS, graduated from the University of California at Davis with a degree in Economics and California State University at Hayward with an MBA in Finance. He worked four years at Target Inc. as a market analyst before joining AIQ Systems as chief analyst in 1991. At AIQ, he published a daily fax service for institutional investors. He currently authors their highly acclaimed Opening Bell educational newsletter. Vomund's analysis and forecasts have appeared in Stocks & Commodities, Los Angeles Times, USA Today, and Barron's.