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IN THIS ISSUE

Feature

Sections

The *Opening Bell Monthly* is a publication of AIQ Systems
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VALUABLE INSIGHTS FROM USERS

THE BEST OF 2001 - THESE 'WORDS OF WISDOM' IMPORTANT TO REMEMBER

After publishing the *Opening Bell* newsletter for nearly 10 years, we believe some of our best articles come from our interviews with AIQ users. The trading perspective these experienced users provide is invaluable. In 2001, we published several interviews and guest articles. Here are some of our favorite quotes from these articles, with additional comments. These "words of wisdom" are valuable insights for both novice as well as veteran traders.

Bobby Florez – January 2001

"The point we are making is to encourage you to pay attention to the market's trend – its definitive trend. If you do, you will always be able to fix your position risk at an objective point no matter what market you trade. And you can do this before actually taking a position in the market."

The bear market of 2000-01 shows how important it is to pay attention to the trend. Going long during a downtrend is like trying to swim upstream. As tempting as it was to guess the market low, a better strategy was simply to wait until it turned. Sometimes it is better to be late than to be early.

> *"It is extremely important to know your emotional makeup…Over the long run, an aggressive strategy will never work for conservative investors and a conservative strategy will never work for aggressive investors."*

Dr. Van K. Tharp – July and August 2001

"Probably the most important part of developing a system is to know yourself and your mission in life. You then need a set of objectives to fit you and your mission. In my opinion, these are steps that a lot of people skip, but they are at least fifty percent of a good trading system."

It is extremely important to know your emotional makeup.

Valuable Insights From Users continued on page 2

VALUABLE INSIGHTS FROM USERS *continued . . .*

Many people thought they knew the level of risk that was appropriate for them. After the 2000-01 bear market, a lot of these people are shifting out of stocks and are moving to more conservative strategies. Over the long run, an aggressive strategy will never work for conservative investors and a conservative strategy will never work for aggressive investors.

"Trading is about cutting losses short and letting profits run...Trading is about watching what happens with the market. You can't do that if your ego gets in the way of being a neutral observer. Trading is about taking from the market what the market is willing to give you. You can't do that if you let your emotions get in the way of the market."

Having a big ego will get in the way of profitable trading. In fact, few things are more humbling than active trading. Those who acknowledge that the market is always right and respond well when they are wrong are the best traders. Along the same lines, emotions get in the way of successful trading. Emotional traders have a hard time following trading systems.

Martha Sipe – August 2001

"Keep exploring the different tools and the changes made in new editions of TradingExpert Pro. The pundits love to use the word "hubris." And I think it applies here in that my hubris led to my contentment with the indicators and basic charting tools with which I was familiar. It has only been in recent times that I have moved into exploring the program further. This exploring led to discovering huge time-saving features."

TradingExpert is very large software package with a great many features. No one uses all of its features. People pick and choose the features appropriate for them. It is useful to know what features are available. We find people are often unaware of features that can play important roles in their trading style. That's why in the *Opening Bell* we cover new program features in individual articles.

A good example is last month's article on list management. Merging two lists or importing a list from another format are features that serve as tremendous time savers, but most AIQ users are unaware of these list management tools.

Richard Denning – September 2001

"When you are trading you are constantly making decisions. Having a mechanical system helps avoid the common mistakes that many new traders make. One such error is to begin trading without having a well thought out plan."

Whether you plan to use a mechanical model or prefer to use judgement in your trading, backtesting a system using the Expert Design Studio and Portfolio Simulator is important. Coding the rules forces you to fully consider the entry rules and you can't run a backtest without deciding on an exit strategy. Testing also helps build confidence in a system.

"The simpler the system, the more robust it will be and the greater the likelihood it will hold up during varying market conditions. I've seen people add a lot of rules to their systems. Each rule cuts the number of trades down to where there are so few trades that it's not statistically valid. A large annual percentage return can fool you if that is all you are looking at."

Some people think that an effective trading model needs to be extremely complicated with a lot of rules. That's not the case. Extremely effective models are often based on one or two indicators.

If you add too many rules to a model you reduce the number of trades and can over optimize the model. If a model backtests well with a lot of trades, then you can be more confident that the model will continue to work well in the future. ▯

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S&P 500 Changes

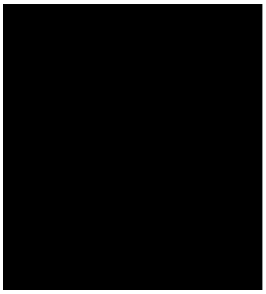
Changes to the S&P 500 Index and Industry Groups:

Genzyme Corp. (GENZ) replaces Ralston Purina (RAL). GENZ is added to Biotechnology (BIOTECHN) group.

Jones Apparel (JNY) replaces Homestake Mining (HM). JNY is added to Apparel & Accessories (TEXTILEA) group.

Waters Corp. (WAT) replaces FMC Corp. (FMC). WAT is added to Electronics-Instrumentation (ELCTRONI) group.

MORE IDEAS THAN MONEY



DAVID VOMUND

With One Position To Fill But Many Stocks Look Attractive, Which One Do You Choose?

By David Vomund

Nearly everyone runs into a similar problem when trading a portfolio. That is, there are more trading ideas than can be purchased.

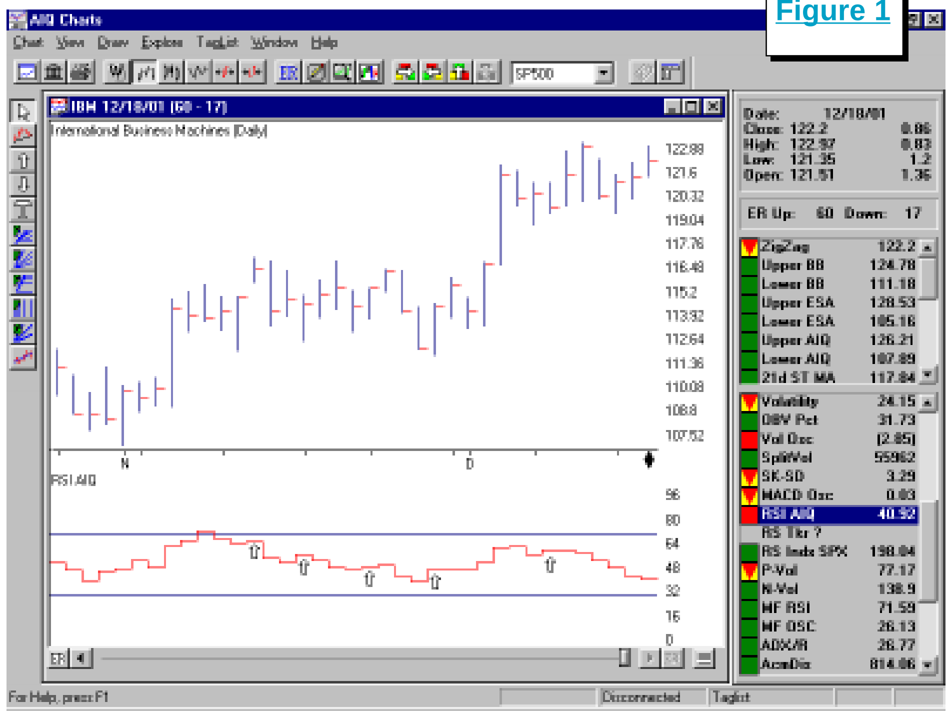
Suppose you have a portfolio that always consists of 10 stocks. If you trade 10 times a year, that averages to about two trades per week. When you have one position to fill but five stocks look attractive, then which one do you buy?

Nearly every system in AIQ provides more ideas than money can buy. The Weighted Action List shows stocks that have registered recent confirmed AIQ buy signals. This report, however, can list more than 30 attractive stocks on any given day. Of those 30, which are the most attractive? AIQ has attempted to rank the stocks from best to worst based on a weighting system that uses the Positive Volume Index indicator.

Along the same lines, the Moving Average Crossover report lists all the stocks that have crossed above a moving average. A lot of stocks can appear on this report, so AIQ ranks the stocks by the strength of their Trend Score indicator.

There are reports that don't provide any ranking or filtering systems. The Persistence of Money Flow report shows all the stocks with strong Money Flow

Figure 1



indicators over the past six months. All the stocks on this report pass the screening so the stocks at the bottom of the report may be as attractive as the stocks at the top of the report.

"AIQ's Portfolio Simulator is extremely helpful in testing techniques that are designed to find the most attractive stock(s) in a list of many attractive stocks."

The Point & Figure report lists stocks with recent Point & Figure triple-top buy signals. If the stocks all have the same patterns, then you'll need to implement an additional filtering process to know which one is the best. A tie-breaking criterion is needed in order to find which stock is the most attractive.

Deciding which is the best stock among a list of attractive stocks is an issue that everyone has to face. In fact, if a lot of stocks are attractive on a given day, then the process of deciding which one(s) to buy can be more important than the process used to generate the list of attractive stocks.

AIQ's Portfolio Simulator is extremely helpful in testing

More Ideas Than Money continued on page 2

More Ideas Than Money *continued* . . .

techniques that are designed to find the most attractive stock(s) from a list of many attractive stocks. Even if you use judgement in your final decision making process, the Portfolio Simulator is helpful in quantifying which filtering or ranking techniques are the most effective.

Let's look at a good example. Suppose we like stocks that have an RSI AIQ indicator that is moving lower but has reversed its direction by increasing in value. Here is the Expert Design Studio code:

rule1 if val([rsi aiq],2)>val([rsi aiq],1) and [rsi aiq]>val([rsi aiq],1).

This line simply says that yesterday the RSI AIQ indicator fell but today it rose.

Looking at Figure 1 we see that this isn't a strict filtering process (see arrows). Sometimes stocks pass the screening when the indicator is near overbought territory and sometimes stocks pass the screening when the indicator is in oversold territory. In any case, a lot of stocks will pass this screening on a given day.

Now let's run a portfolio simulation on this rule. We will assume that an account started with $100,000 at the start of 1998. Ten stocks represent a fully invested portfolio with each new purchase representing 10% of the portfolio value. No more than three trades are placed on a given day. Only S&P 500 stocks are purchased. The sell strategy uses an 80% profit protect above a 10% profit. There is also an 80% capital protect for trades that go bad.

Figure 2

Account Statistics/Analysis

		Winners	Losers	Neutral
Number of trades:	256	174	82	0
Average periods per trade:	56	43	82	0
Maximum Profit/Loss:		49.56%	(48.43)%	
Average Drawdown:	(11.34)%	(5.93)%	(22.81)%	
Average Profit/Loss:	1.65%	12.02%	(20.35)%	
Probability:		67.97%	32.03%	
Average Annual ROI:	10.73%	100.13%	(90.30)%	
Reward/Risk Ratio:	1.25			
Portfolio:				
Starting Balance:	100000.00			
Ending Balance:	140146.55			
Gain/Loss:	40146.54			
Gain/Loss %:	40.15%			

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The result of running this simulation is found in Figure 2. Since 1998, the portfolio grew 40%. That's not great but it is better than the S&P 500's 17% return. From an Expert Design Studio test that is not shown here, we know that 12,280 stocks passed our RSI AIQ screening. Of those, Figure 2 shows that only 256 trades were actually acted on.

Our system gives us more stock selections than we have money to purchase. What is the best method for selecting which stocks actually go into the portfolio? This is a question every trader faces and it is a question that the Portfolio Simulator will help answer.

"We ran another test using the same criteria but this time we entered a tie-breaking rule…by simply adding this rule the return dramatically jumped to 135%, well above the 40% return we saw in our initial test."

In our test shown in Figure 2, we didn't specify a ranking or tie-breaking rule so when multiple stocks passed our criteria then the system chose stocks based simply on alphabetical order. Obviously there is a better method.

We ran another test using the same criteria but this time we entered a tie-breaking rule. Each stock that passed the RSI AIQ rule was ranked based on its percentage return over the last 120 days (approximately 6 months). If multiple stocks passed our screening but only one stock could be purchased, then the system looked at price activity over the preceding six months and selected the stock with the highest percentage return. The following User Defined Function was used to calculate the return of stocks over the last 120 days:

rs is [close]/val([close],120).

The result from this test

MORE IDEAS THAN MONEY *continued* . . .

appears in Figure 3. Notice that by simply adding this tie-breaking rule the return dramatically jumped to 135%, well above the 40% return we saw in our initial test.

Our two tests demonstrate the importance of the filtering process used to determine which stock in a group of stocks should be purchased. In both tests, we screened for stocks with an upward reversal in their RSI AIQ indicators. Results were dramatically increased, however, by simply limiting the stocks that were purchased to those that performed the best in the previous six months.

It is very easy to test different tie-breaking rules using the Portfolio Simulator. For example, if you want to buy stocks that pass an initial screening based on the level of their Volume Accumulation Percent indicators, then you would use the following User Defined Function:

Vapct is [VA Pct].

In our test we demonstrated that picking the strongest stocks was a good tie-breaking strategy. This isn't always the case. A tie-breaking system may work well for one strategy but work poorly for another strategy. A good example uses the Vapct User Defined Function shown above. When you have a list of attractive stocks, buying the one with the highest Vapct indicator is often a good strategy. But when we combined the Vapct rule with our RSI AIQ strategy the results were terrible.

Whether you use a fully automated mechanical model or you use judgement in your stock selection process, you will need to pick which stock among a list of attractive stocks should be purchased. The method used in picking that stock is important.

As we've demonstrated, the Portfolio Simulator is extremely valuable in helping to determine which stock selection method works best. You should run tests to see which ranking or tie-breaking strategies work well with your personal selection process.

Note: In this article we have assumed that you are familiar with the Portfolio Simulator. If you need help using the Simulator, see the November 2001 issue of the *Opening Bell* and read the instructions for using the Portfolio Simulator in TradingExpert Pro's User Reference Manual, page 469.

Figure 3

Account Statistics/Analysis

		Winners	Losers	Neutral
Number of trades:	388	273	115	0
Average periods per trade:	37	33	46	0
Maximum Profit/Loss:		93.48%	(53.78)%	
Average Drawdown:	(10.61)%	(5.15)%	(23.56)%	
Average Profit/Loss:	3.53%	14.28%	(22.00)%	
Probability:		70.36%	29.64%	
Average Annual ROI:	34.72%	156.86%	(173.61)%	
Reward/Risk Ratio:	1.54			
Portfolio:				
Starting Balance:	100000.00			
Ending Balance:	234720.27			
Gain/Loss:	134720.27			
Gain/Loss %:	134.72%			

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AIQ MARKET TIMING -- 'LESS THAN STELLAR'

THE 'IDEAL' MARKET TIMING SYSTEM -- CASH IN 2000 AND CASH IN 2001!

By David Vomund

2001 was a great year to be in cash. In fact, the ideal market timing system would have moved you to cash in 2000 and would have kept you in cash for almost all of 2001 as well. If there was ever a time to incorporate market timing, this was it. Unfortunately, the AIQ timing system was less than stellar. Those who followed AIQ's market timing model in 2001 lost about as much as the buy-and-holders.

An historical backtest of AIQ's market timing model reveals that the highest returns come from simply using the market timing model without confirmation. That is, you buy when an upside signal of 95 or greater is registered and you sell when a downside signal of 95 or greater is registered, using ticker DJIA. The reason people use confirmation is that it helps to avoid some of the bad signals.

The confirmation technique that most people employ uses the Price Phase indicator. With this technique, a buy signal is not acted on until the Phase indicator increases. Conversely, a sell signal is not considered a sell until the Phase indicator decreases.

Although the purpose of applying a confirmation technique is to help avoid acting on bad signals, unfortunately in 2001 even the bad signals were confirmed by the Phase indicator. Adding insult to injury, some of the well-timed signals were not immediately confirmed.

An example is found in Figure 4. On March 9, a 95 sell signal was registered. That signal was confirmed by the Phase indicator the following day when the Dow fell 436 points. The market continued to move lower but those who waited for confirmation experienced a painful day. There was a time when people said that the AIQ buy signals were good but the sell signals were not. In the last two years the opposite has been true. Trends are powerful.

The 2001 buy and sell signals are listed in Table 1. The results assume that you buy the S&P 500

Figure 4

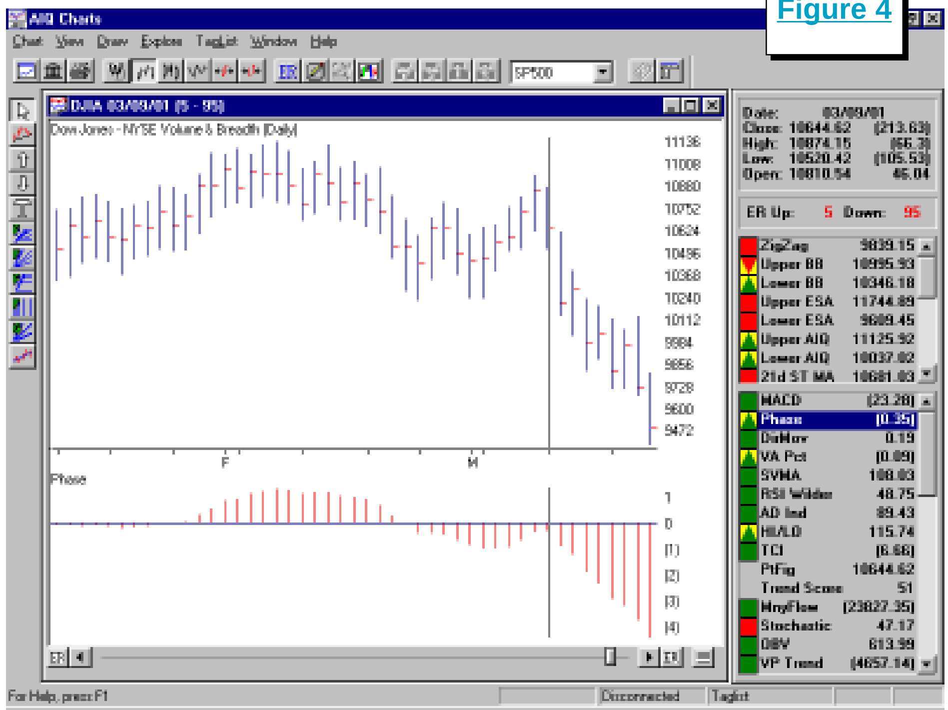

Table 1

Market Timing Model - No Confirmation

Entry Date	Expert Rating	Exit Date	Expert Rating	S&P 500 % Change
01/03/2001	100	01/05/2001	99	-10.28
12/31/2000	N/A	01/02/2001	100	-2.81
02/23/2001	98	03/09/2001	95	-1.00
03/26/2001	97	07/23/2001	96	3.33
07/27/2001	99	10/30/2001	100	-12.11
12/04/2001	96	N/A		0.29

2001 Return = -12.36%

AIQ Market Timing *continued . . .*

on the day a buy signal of 95 or greater is registered, and you sell on the day a 95 or greater sell signal is registered. The 2001 return was negative 12.36%. That compares to an S&P 500 buy-and-hold return of negative 13.04%. If you had applied Phase indicator confirmation, results would have been a few percentage points worse.

Nasdaq 100 Timing Model

In the May 1999 issue of the *Opening Bell*, we introduced the concept of using AIQ's regular market timing model on the Nasdaq 100 index. In review, AIQ's market timing system needs price, breadth, and volume in its Expert System. The Nasdaq Composite (AIQ ticker symbol OCEXCH) has all of these but Nasdaq breadth isn't representative because it is calculated from too many small-cap issues that have no influence on the Composite.

We solved this problem by using the Nasdaq 100 index instead of the Nasdaq Composite. The Nasdaq 100 index (NDX) contains the large capitalization stocks that move the Nasdaq Composite. Since the Nasdaq 100 index has no breadth or volume, TradingExpert is used to calculate breadth and volume.

Using AIQ's Market Breadth Builder function to create a Nasdaq 100 market, we plot the actual Nasdaq 100 index (ticker NDX) and use TradingExpert to calculate breadth and volume based on the 100 stocks that comprise the index. The Advance/Decline Line on the Nasdaq 100 market is more representative because the low price and low volume stocks that distort the Nasdaq Composite are excluded from the calculation.

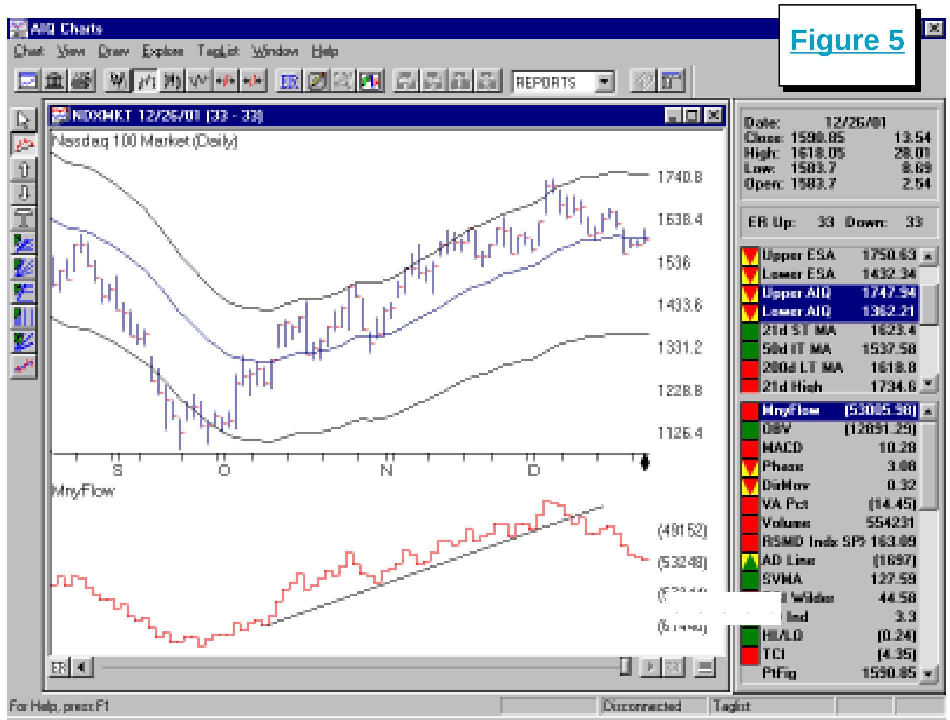

Figure 5

A link to a list of the Nasdaq 100 stocks can be found on my web page at *www.visalert.com*. An explanation of how to create a market using AIQ's Breadth Builder can be found in the TradingExpert User Reference Manual, page 49.

For this market timing model, we used a list of the Nasdaq 100 stocks as of December 31 of the preceding year. Although the stocks that make up the Nasdaq 100 change over time, we kept our list the same for the remainder of the year.

"There was a time when people said that the AIQ buy signals were good but the sell signals were not. In the last two years the opposite has been true. Trends are powerful."

This model worked beautifully in 1998, 1999, and much of 2000. Unfortunately, it didn't work in the fourth quarter of 2000 and was off the mark in 2001 as well. A list of the Nasdaq 100 signals is found in Table 2 (next page). For the year, this model lost 36.99%. That compares to a Nasdaq 100 buy-and-hold return of -32.66%.

Although the Expert Rating signals from this model were ineffective in 2001, the Nasdaq 100 market is well worth following. Analyzing the indicators on this market, especially the Advance/Decline Line and Money Flow, has become an important part of my decision making process.

Notice in Figure 5 how Money Flow confirmed the steep advance in the Nasdaq 100 during October and November but then broke down in the second half of December. This combined with

AIQ Market Timing continued on page 8

AIQ Market Timing *continued . . .*

Table 2

Nasdaq 100 Timing Model
No Confirmation

Entry Date	Expert Rating	Exit Date	Expert Rating	S&P 500 % Change
01/03/2001	100	01/05/2001	99	-10.28
02/15/2001	99	02/16/2001	97	-6.66
03/22/2001	100	04/02/2001	95	-10.87
04/05/2001	100	05/14/2001	99	18.17
05/24/2001	99	05/29/2001	98	-6.44
06/21/2001	100	07/05/2001	100	0.00
07/26/2001	96	10/30/2001	96	-19.78
11/13/2001	96	12/13/2001	97	1.32
12/18/2001	96	12/20/2001	96	-6.05

2001 Return = -36.99%

Advance/Decline Line analysis is useful information to those who tend to buy Nasdaq 100 stocks instead of the second-tier Nasdaq stocks. ▯

STOCK DATA MAINTENANCE

The following table shows stock splits and other changes:

Stock	Ticker	Split	Approx. Date
Iron Mountain	IRM	3:2	01/02/02
Middlesex Water	MSEX	3:2	01/03/02
Suffolk Bancorp	SUBK	2:1	01/03/02
Movie Gallery Inc.	MOVI	3:2	01/04/02
Varien Medical Sys	VAR	2:1	01/16/02
FTI Consulting Inc.	FCN	3:2	01/17/02
Liz Claiborne	LIZ	2:1	01/17/02
Chico's FAS Inc.	CHS	3:2	01/21/02
Copart Inc.	CPRT	3:2	01/22/02
Dentsply Int'l	XRAY	3:2	02/01/02
Symantec Corp.	SYMC	2:1	02/01/02

Trading Suspended:
Argentina Fund (AF), Arnold Industries (APCS), Banc West (BWE), Cabot Industrial (CTR), C-MAC Inds (EMS), Homestake Mining (HM), SCI Systems (SCI), XOXO Communications (XOXO)

Name Changes:
GlobeSpan Inc. (GSPN) to GlobeSpan Virata Inc. (GSPN)
Industrial Holdings (IHII) to Energy Services Inc. (TTES)
PHS Bancorp (PHSB) to PSHB Financial Corp. (PHSB)
Sanmina Corp. (SANM) to Sanmina-SCI Corp. (SANM)

MARKET REVIEW

Heading into December, AIQ's market timing model was on a sell signal. That quickly changed as a 96 buy was registered on December 4. That signal lasted through the remainder of the month.

During December, the S&P 500 gained 0.8% and the Nasdaq Composite gained 1%.

There is a saying on Wall Street that states: "Don't fight the Fed." That axiom didn't work in 2001. The Fed lowered rates 11 times, a record for a calendar year, bringing the short-term bank lending rate to a level not seen since 1961. Still, the markets fell. In 2001, the S&P 500 fell 13% and the Nasdaq fell 21%.

Most of the damage during the year came from the technology sector. Fidelity's Networking and Infrastructure sector fund lost about half of its value. Developing Communications and Wireless lost about 40%. Computers lost about 30%.

While most stocks fell in 2001, there were some very big winners. The best performing Dow stock was Microsoft (MSFT), which rose 53%. Nvidia (NVDA) was the best performing S&P 500 and Nasdaq 100 stock, gaining 308%.

The market hadn't posted two consecutive years of losses since 1973-74. The good news is that it is very rare for the market to post three consecutive years of decline. Since 1896 the Dow Jones Industrial Average has seen such bad markets only three times, the last one being the years 1939 through 1941.

We look forward to a better 2002! ▯