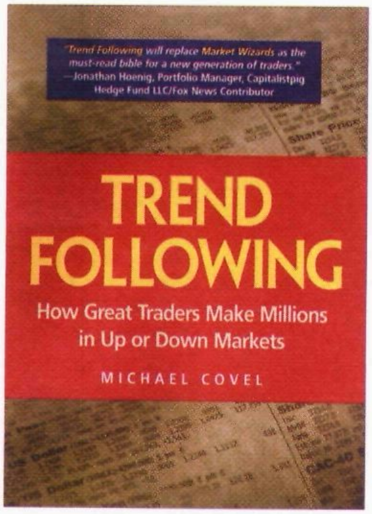
Book Reviews

Trend Following: How Great Traders Make Millions in Up or Down Markets

By Michael Covel
Prentice Hall (2004)
311 pages, $27.50

REVIEWED BY JAMES T. HOLTER

Michael Covel had an intelligent, if somewhat ultimately slanted, approach to laying out this book. His method was to examine the players in financial disasters, but not those who were losing all the money — they've had their share of headlines. Covel wanted to know who made all the money that was lost.



Having found the winners — generally, those money managers who had strong returns during the periods of the scandals — he compared them and found that many, such as John W. Henry, who profited handsomely during the Barings Bank fiasco, were trend followers.

That led him to explore questions such as, "How do trend followers win in the zero-sum game of trading?" and "Why has trend following been the most profitable style of trading?"

Before going any further, perhaps a few trading neophytes and quite a few trading pros know those are loaded questions. Of course, more trend following money managers made money during select scandals. More trend followers also lose money when the managed money industry as a whole suffers a rough spot. The reason is simple: More professional money managers are trend followers, and that alone doesn't make trend following the best strategy anymore than it makes it the most marketable to institutional investment allocators. Understanding that, it may just as reasonably be asked how option sellers, contrarian traders, fundamentalists, pit traders or Elliott Wave enthusiasts make money trading.

Still, the point isn't to question the value of a book on trend following. It is indeed the most popular trading discipline. It is indeed profitable in the hands of many traders. Trend following is certainly a capable way to trade, but it's not the only way. If you can get beyond that nugget of bias, you'll be rewarded with a quality education in this trading approach.

One strong point of this book is it puts you into the mind of a successful trend trader. It helps you understand the sentiment, risk aversion (or lack thereof) and profit time frame you'll need to embrace mentally to make a trend-based approach work.

You'll also find practical knowledge — facts you'll need to know to implement a trend-following trading program. Covel looks at trading system development (targeting novices — it's not too technical) and basic data such as what markets successful trend traders trade well. Money management (how much to trade) is addressed and risk management (protecting the downside) is given its due. There is also practical discussion of what many traders consider far more important than whether you get into a trade using moving average crossovers or even a six-sided die: exit management.

Beyond that, however, the practical advice is limited. Those with serious intentions of systematic trend trading, would do well to pick up a general book on system development, such as *Cybernetic Trading* or *Trading Systems that Work*.

Trend Following is accessible (you can come into it completely green) and it is comprehensive in its stated subject matter. If you're a beginner who wants to trend trade or if you're an experienced Gann trader, for example, who wants exposure to another approach, this book will do it.

Candlesticks, Fibonacci and Chart Pattern Trading Tools: A Synergistic Strategy to Enhance Profits and Reduce Risk

By Robert Fischer and Jens Fischer
John Wiley & Sons (2003)
256 pages, $89.95

REVIEWED BY JAMES GOULD

The authors promise to provide readers with "an easy, reliable trading method and tools together with trading rules that can be applied to real-time trading." Their trading method is a trend-following system based on Fibonacci ratios, candlestick patterns, Elliott wave theories and PHI-ellipses. As is true of all trend-trading methods, market entry is late — OK because false price moves are reduced — and so is market exit — not OK because profits are reduced.

PHI-ellipses, the heart of the trading method, are patterns of varying elliptical shapes formed over time based on current price patterns. For PHI-ellipses to be a "reliable" trading signal, their formation must follow strict rules as a three-wave price correction, which must occur within boundaries circumvented by the ellipse. Price breakouts from a properly constructed PHI-ellipse become the signal to enter or exit a trade.

The authors contend the "accuracy" of PHI-ellipses can be improved by incorporating candlestick formations and Fibonacci ratios. Construction of PHI-ellipses is based on a proprietary data transformation; however, accompanying software enables readers to construct and use PHI-ellipses on their own data. Ten years of data having the same price scale are recommended to fine-tune PHI-ellipse patterns. PHI-ellipses can be constructed from monthly, weekly, daily or intraday prices and can be used for equities, indexes or commodities.

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