
Trading Futures
FOR
DUMMIES®

by Joe Duarte, MD



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Trading Futures For Dummies®

Published by
Wiley Publishing, Inc.
111 River St.
Hoboken, NJ 07030-5774
www.wiley.com

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Published by Wiley Publishing, Inc., Indianapolis, Indiana

Published simultaneously in Canada

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Library of Congress Control Number: 2008929124

ISBN: 978-0-470-28722-4

Manufactured in the United States of America

10 9 8 7 6 5 4 3 2 1



About the Author

Dr. Joe Duarte is a widely read market analyst, writer, and an active trader. His daily Market IQ column is read by thousands of investors, futures and stock traders, information seekers, intelligence aficionados, and professionals around the world.

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His articles and commentary have appeared on Marketwatch.com. He has been quoted in *Barron's*, *U.S.A. Today*, *Smart Money*, *Medical Economics*, Rigzone.com, and in *Technical Analysis of Stocks and Commodities* magazine.

Dedication

To my mother, whose long fight with cancer is remarkable and a sign of the human spirit's ability to persevere in the toughest of circumstances.

Author's Acknowledgments

A book is always more a product of circumstances than of the author's wits and ability to research data and synthesize it. No author can create without the help of others. So here's the list of important people for this one:

My family, my office staffs from my other life, and the Wiley editorial staff, especially Stacy and Tracy who worked with me despite the inevitable circumstances that arose in the production of this book.

Grace, "the wonder agent" and purveyor of recurrent gigs.

Frank, "the master of all things Web-related," without whom there would be no `Joe-Duarte.com`.

To the inventor of audio books, because they keep me sane in my travels between the places that I must go to in my search for truth, justice, and bucks.

As always, coffee, tea, vitamins, sports drinks, nutrition bars, and the game of tennis also help.

Especially to those who read my books, subscribe to my Web site, and have kept this thing going for 18 years.

And also to two long-time friends, John and Greg, whose interactions with me always prove to be worthwhile and interesting, to say the least.

If I've forgotten to mention anyone, it wasn't intentional — I'm not as young as I used to be.

Publisher's Acknowledgments

We're proud of this book; please send us your comments through our Dummies online registration form located at www.dummies.com/register/.

Some of the people who helped bring this book to market include the following:

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Introduction



Risk and uncertainty go hand in hand with opportunities to make money. Those who can shake off the chains of preconceived notions and ideology and who discover how to make money as markets rise or fall are more successful than investors who buy and hold.

And that's what this book is about: embracing the inherent volatility of the world and the markets and using it as a wealth-building tool.

Goods, services, and basic materials probably will undergo major price swings, up and down, at one time or another during the next 20 years. The volatility of the markets is only going to increase. And the chances for sustainable trends that last for decades, the way the stock market rallied in the 1980s and 1990s, are less likely than they were a few years ago.

If global warming doesn't get you, then politicians, militants, or dictators are almost certain to try. That's why finding out how to trade futures is important for investors who not only want to diversify their own portfolios but also want to find ways to protect and grow their money when times are hard in traditional investment venues such as the stock market, a point well illustrated by the action in the financial markets in 2007 and early 2008.

The world has changed since the events of September 11, 2001. China, India, Brazil, and other economies are now competing with the United States and Europe. This competition is not likely to ebb or change for several decades, which means that market volatility is not likely to go away any time soon.

Whereas in the past investors could afford the luxury of buying and holding stocks or mutual funds for the long term, the post-September 11, 2001, world calls for a more active and even a speculative investor. The new world calls for a trader. And the futures markets, although high risk, offer some of the best opportunities to make money by trading in volatile times.

So you need to get ready to work as a stock trader, a geopolitical analyst, a money manager, and an expert in the oil and commodity markets. In my line of work, I have to keep up with news about the economy, disruptions in the supply of oil, the weekly trends of oil supply, weather patterns, and the stock market, both in a macro and micro universe. As a futures trader, you have to do the same with your contract of choice, and you have to pay attention to

time factors, especially expiration dates and how much time you have left to decide whether you have to exercise your option.

Remember that successful traders

- ✔ Have a plan, follow it, and adjust it to changing conditions
- ✔ Look at trading as a business
- ✔ Are disciplined in their personal and professional lives
- ✔ Understand the risks and the game they're playing
- ✔ Know and accept that they will make mistakes
- ✔ Never forget their mistakes and benefit from them
- ✔ Never enter into a trade without knowing their exit strategy — how they'll get out of the market
- ✔ Never risk money that they aren't willing to or can't afford to lose
- ✔ Never allow a bad trade to lead to a margin call

Trading futures isn't gambling; it's speculating. It's also about being prepared, gathering information, and making judgment calls about situations that are unfolding, and it's a process of self-protection and an ongoing education.

You may think of yourself as a dummy. But after you read this book, you'll know how trading futures is done and how to stay in the game as long as you want, not necessarily by hitting home runs but rather by showing up to work every day, getting your uniform dirty, and playing good, consistent, fundamental baseball.

About This Book

Futures markets are resurging and are likely to be hot for several decades, given the political landscape. Changing world demographics and the emergence of China and India as economic powers and consumers, coupled with changing politics in the Middle East, are likely to fuel the continued prominence of these markets.

I take you inside these markets and give you tools that you can use for

- ✔ **Analyzing, trading, or just gaining a better understanding of how money works and affects your daily life.**
- ✔ **Starting fresh in your views of how the markets work.** A traditional buy and hold mind-set is a recipe for trouble in futures and options trading, while profit-taking or hedging a position before the weekend is normal operating procedure.

- ✔ **Discovering that time is on your side in the stock and bond markets, but it's your enemy in futures.** You have to be on top of how much time you have left before your trading position expires, becoming worthless, or you have a load of something delivered with a bill for a large sum of money.
- ✔ **Reading a sentence just the way it's written.** No tricks, hidden clues, political agendas, or attempts to make you look foolish. If you don't get it, I didn't do a good job of writing it.
- ✔ **Remembering that measuring the return of your money is more important than measuring the return on your money.**

Conventions Used in This Book

To help you make the best use of this book, I use the following conventions:

- ✔ *Italic* is used for emphasis and to highlight new words or terms.
- ✔ **Boldface text** is used to indicate key words in bulleted lists or the action parts of numbered steps.
- ✔ `Monofont` is used for Web addresses.

What I Assume about You

I had to start somewhere, so I assumed some things that may or may not apply to you. I'm not trying to offend you or to be condescending. So here's what I've assumed about you:

You're not a beginner. In fact, you've got some experience in investing and at least conceptually know that professionals are not the buy and hold investors that Wall Street would like to make the public believe that they are.

- ✔ You're looking for a better way to make money in the markets, but even though you have some experience, don't know enough to trade futures and want to find out how to do it without losing your shirt.
- ✔ Even though you've been a stock trader or investor, you'd like to know more about using charts, indicators, and trading psychology.
- ✔ You want to find out how to decrease the risk within your portfolio.
- ✔ You want to become a more active trader and make money more consistently by letting your profits run and cutting your losses short.
- ✔ You want to know how to make sense of the big picture in the markets and to try your hand at trading currencies, bonds, and commodities.

- ✔ You like the idea of trading on margin, and you're not afraid of leveraging additional money.
- ✔ You aren't afraid of being wrong five or six times in a row when trading, but you're willing to try again until you succeed.
- ✔ You want to investigate more about how politics, wars, weather, and external events can be used as opportunities to trade.
- ✔ And most important, you know that reading an introductory or intermediate work, such as this, is an excellent beginning, but that you'll have to read more, find out more, and make changes to your trading skills as time passes.

If these assumptions describe you, you've picked up the right book. Nevertheless, I also assume that you have some tools and resources at your disposal. Here's what you need to get started in futures trading:

- ✔ **Plenty of money and a cast-iron stomach to boot.** You need to have at least twice the amount that your broker/advisor lists as a minimum for opening an account. And you have to be ready to lose it all, fast, although if you follow the money management rules in this book, that won't necessarily happen.
- ✔ **Your head screwed on straight before you start.** Futures trading is really dangerous and can wither away your trading capital fast.
- ✔ **A quiet place to prepare, set up your trading station, and make sure that you know your market stuff really well.** Exchange hours, what brokers do and don't do, what trading terms like bid and offer mean, and how to read a brokerage statement are only some of what you need to know.
- ✔ **A fast computer with a fast Internet connection.**
- ✔ **Access to good charts.** You can gain access to charts either through the Web or a good trading software program, which gives you the ability to test your strategies before you commit to them.
- ✔ **Subscriptions to newsletters, books, magazines, and software.** Be ready to spend some money for these important information resources. You can also take courses, and you need to get used to paper trading (practicing without money) before jumping into the deep end.

How This Book Is Organized

I've organized *Trading Futures For Dummies* into six parts. Parts I and II introduce you to the futures markets and market analysis — technical and fundamental. Parts III through V take you into the nuts and bolts: the exchanges, the contracts, trading strategies, and indicators. Part VI is the now-famous *For Dummies* Part of Tens, in which you can discover a little about a lot of different futures information.

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