

INTERVIEW

The Charts Know It All

# Chart Patterns, Trading, And Dan Zanger

Trader Dan Zanger of *Chartpattern.com* first hit the media spotlight in December 2000 when he was featured in a *Fortune* article. The article, entitled "My Stocks Are Up 10,000%!" discussed how he had turned \$11,000 into \$18 million in 18 months (with a return of 164,000%), an unofficial world record for trading stocks (with the tax receipts to prove it). Not mentioned in the article was that in 23 months, the total grew to \$42 million.

Also not mentioned except in passing was much detail about Zanger's trading techniques, indicators, and philosophies or an outline of his typical trading day. He uses chart patterns to find high-volatility ("frisky") stocks. The article piqued the interest of many readers about the art of technical analysis and provided insight into what is possible for those with the skill and dedication. How is he doing more than two years later? How does he trade and what motivates him? *STOCKS & COMMODITIES* contributor Matt Blackman caught up with Dan Zanger by telephone on April 23, 2003, at his home in Florida.



**W**hat indicators do you use? Do you use momentum or other indicators with your chart patterns?

I use absolutely no indicators whatsoever. I simply rely on chart patterns, price, and volume. Who has time to look at so many indicators when you're scrolling through 400 stocks a night? I look at daily bars intensely and dissect them and then add in the volume bars to come up with sort of a pressure factor that tells me what the stock wants to do next and when it wants to do it. Is it ready now or does it need more time? That's the job at hand every day.

**You use price volume and chart patterns and that's it?**

That's 100% of what I use.

**How have you found trading chart patterns over the last few years during the current bear market?**

Like most people in the market today, I learned about trading with the

major secular bull market that started in 1982. All my learning was to the upside and knowing when to step aside when the charts predicted a correction was about to start. It took at least seven months for me to get the hang of the charts for a bear market, and other items took over two years. Even with the chart knowledge I learned, news stories and interest rate cuts would and could and did rocket stocks right out of the bear patterns. It was brutal, but a great learning experience.

**What trading tools have you found to be most useful?**

As far as trading tools are concerned, I like AIQ's proprietary moving average trading bands. When a stock breaks out of a base or pattern and if it blows through the upper trading band, that

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tells me it's a very strong stock. That also tells me I need to sell half or all of my position on the second or third day above the trading band. AIQ bands employ moving averages over a long time. No other bands replicate them that I know of. Bollinger Bands come close in some ways but not others.

**Some traders use volume and price as well but also employ support and resis-**

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***tance levels and moving averages to trade. Do you use Fibonacci or support/resistance levels?***

Support and resistance yes, but Fibonacci rarely; but I do use them more often in bear markets/corrections and certainly on the leading averages during pullbacks. As I mentioned, I have 400 stocks that I look at every night. I view them every day and have a feeling for their personalities and behavior. They are my buddies. It's very important to get to know your stock's personality. I don't use any intraday charts, but I do refresh and check daily charts every hour during the day and scroll through stocks that look particularly inviting or have good action. I highlight those to focus on when I look at the daily chart after the market closes.

***Do you use money flow at all?***

No. I have not found a way to make it work effectively. I have seen it fail so many times and in no way will this indicator highlight or pinpoint the big movers in the market. Again, I use only chart patterns and volume.

***Do you prefer candlesticks or bars?***

Bars. I look for patterns on daily charts using daily bars. However, I do understand what candlesticks are all about and use that knowledge in viewing and interpreting my daily bars.

***What do you use as your market proxy?***

When the market rallies, I focus on the leading index at the time, be it the Philadelphia Semiconductor Index (SOX) or the Biotech Index (BTK) or whichever index is leading the market. Right now, it's the Goldman Sachs Internet Index (GIN) that is leading this market move. BTK looks interesting, and so does the Biotech Holders Trust (BBH), with its long tight channel base.

***So you're still playing the techs?***

Yes, and I will continue to do so until something becomes more volatile. But really, I go with what is moving in the market the most. It used to be cellular phone stocks in the 1980s and then health maintenance organizations (HMOs) in the late 1980s and early 1990s.

In the early 1990s you couldn't give a semiconductor stock away. Then all of a sudden they became stock darlings in 1996-97, as did networking stocks and telecommunications stocks. It's whatever the market chooses to play, be it biotechs, chips, networks, fibers, Internet — you've got to go with what the market is going to push up the most.

I scan through my 400 stocks and I can tell you in 25 minutes which are the strongest groups and the fastest stocks and the ones to own and play with.

***You don't use automated scans to help you?***

No. Because then I have to look through the stocks that the scans spit out as well as my 400 stocks, and scans are not going to get all the movers the way I will on a manual scan. The charts tell you everything you need to know about the stock. If a stock is lying dormant, no scan will tell you it's time to go before it goes, but viewing the chart manually will.

***How have you been doing in the last couple of years?***

The bear market has been brutal. This is my first true bear market, and we must learn from our mistakes. However, starting in October 2002 since the market bottomed, I'm up about 60%. I'm still leery about the market and have jumped out far quicker than I would have before. The fear factor of things breaking down is so embedded in me now, it will take time to change that. I will say, though, that this market is acting like one of the great bulls of yesteryear. I'm pretty thrilled to be up 60% at this point.

***Have you been playing some of the bear rallies from the end of September 2001?***

I played it in October 2001 and others, but they came and went lightning fast. Just when you thought it was going to continue, it ended. I grew up in a secular bull market. It was a period of higher highs and higher lows on the long-term charts with an occasional break, but the market would pick up and head higher again. It was an 18-year bull market. I never lived through a bear

market and never learned bear patterns or bear analysis. It took me two years to learn, and now that I've learned bear market tactics, the bear might be over with, at least for a year or two.

***How is your website, Chartpattern.com, going? Have you been playing some of the shorts in this bear market?***

Things are going well. We have a lot of members and many leading institutions and hedge funds. Business is down because the market has been brutal, but overall I'm very pleased with what I've accomplished with the site, and doing the newsletter four nights a week keeps me very focused.

As far as shorting goes, people say that you're going to make a lot of money because you have a lot of great shorts on the site. Shorts only go down by 15-35%. Rarely will a stock go from \$80 to \$0 like Enron. In a bull move, you can get stocks going from \$10 to \$40 or \$20 to \$60 or \$80 over several months or a year. That's a 400% move, and on a 2-to-1 margin you can double that. The big money is in a bull market. There are no two ways about it. You play the bear market just to hang around so that when the big move finally does come, you're there.

***How did you get started in your trading career?***

I started in about 1976 watching The Business Channel in Los Angeles on UHF. They would have guys coming on talking about technical stuff. Sherman McClellan used to come on once a week and talk about the McClellan oscillator. Other people talked about cycle analysis. You could see what they were doing and how it worked on the market. So I learned at a very early age how technical analysis was an important factor in the market.

There was a guy named Gene Morgan, who every day at 1:30 pm would come on with his show called "Charting the Market," in which he would show charts that were marked up manually — they didn't have TelePrompTers or digital stuff then. He'd show parabolic curves and explain that here was a stock that went parabolic. Then he'd show a

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cup and handle formation, and he'd explain the growth that the stock would have out of that pattern. Then he'd show a pennant formation or a flag or a falling wedge and how they would forecast price movements. I was absolutely astounded and it changed my life.

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*What did it inspire you to do?*

We had no personal computers back then to help us plot charts, so I would watch the tickertape and buy stocks that would light up the tape. I bought one stock at a buck and sold it a couple of weeks later at \$3.90. I was hooked. That's how I started.

Then in 1983 I got a chart book. I'd look through it for cup and handles, pennants, and flags. I'd be looking at cheap stocks that I felt I could afford, but I couldn't pick out anything. Cheap stocks rarely have good patterns to identify and to tell you the truth I couldn't identify *any* pattern back then. So I basically gave it up for the time being. But I always picked up the financial papers and followed stocks. I did predict the crash in 1987 the day before it happened, for what that's worth, and that cemented my calling to be in stocks full time.

*What tipped you off about the crash?*

I used to go to the gym every night at the time, and everyone there would be talking stocks and how much money they were making in the market. Then one Friday the market took a 200-point hit, but markets usually have their big drops on Mondays. I told my mother — who was the person who got me into stocks in the first place — to wait until Monday, as that would be *the* big day. I didn't watch the market since I was [at work], but on the way home that Monday the evening news announced that the Dow Jones Industrial Average (DJIA) had dropped 508 points. I had friends who went broke that day, but I was elated because I'd called it. My prediction had come true and I felt connected to the markets for good.

*What made you make the transition from trading the ticker to learning to trade chart patterns?*

My mother passed away and left me \$100,000. I took a seminar by William O'Neil, who showed us a few chart patterns and his CANSLIM formula. I spent the next six months to a year taking chart patterns that he gave us and trying to find them in the charting books and on my new ultra-fast 286 PC. I would overlay a chart pattern over stock charts and do this every evening and for about six hours every Saturday and Sunday until I finally found one. I would keep doing this over and over for thousands of hours until I could identify the cup and handles.

Then I got pretty good at it and realized that there was a lot more to it than the cup and handle or channel patterns that he'd taught us. So I called him up one day because he had a weekly TV show back then and asked him if he had an advanced course. He said that *was* the advanced course. I realized I was on my own and spent the next six years learning everything I could about trendlines, daily bars, reversal patterns, how to spot a correction and so on. I now give a very advanced charting seminar about twice a year.

*Who were your other mentors?*

Gene Morgan, host of the *Charting The Market* show.

*What did you do to learn after that?*

I read Edwards and Magee. I looked more at the charts than reading the text, though. But really, from then on it was the school of hard knocks. We got into a strong bull market in early 1991. I made a lot of money right after the first Gulf war and then gave it all back during the summer with the very first correction because I didn't know what a correction was. I didn't know you could go broke or close to it because I believed that my stocks were so good that they couldn't go down in price by 30% or 50%.

*Famous last words!*

When you think that a company is too good and the earnings are too strong for it to go down, that's when you'll have

your head handed to you. That's exactly what happened to me. A lot of these stocks came back, but when there is a 35% to 40% correction and you're on 2-to-1 margin, you're close to broke. There was something going on that I didn't know about. That's when I got serious, went back, and studied my mistakes. And I did this *many* times.

I didn't understand that corrections could last two to four months or even longer. I didn't understand how to spot the next winners. I realized that I didn't know *anything*. You just have to keep going back over and over again until things sink in.

*So you did a post-mortem on your trades?*

Pretty much. A lot of it was that at first, I believed in stocks instead of believing in trends, trendlines, and rising trendlines, and when a trendline is broken after a stock has been rising for some time, it needs to be sold, period. Other items that took years to learn how to identify were several reversal patterns or reversal bars such as a spinning top or a bearish engulfing day after a big runup in price. I don't use candlesticks, which is what these terms are normally applied to, but I *do* understand how they work. Daily bars work the same way but don't have fancy names, the way the candlesticks do.

*It took a while to learn, I would imagine.*

I remember getting hammered on a market correction more than once and saying I'll never do stocks again and walking away. After a few months of my not paying attention to the market, it was taking off again, and I was missing the move because I'd walked away. Worst of all, I'd missed the new winners because I was asleep at the wheel instead of watching the market during the correction like I should've been.

*What did you learn from that?*

I realized I'd been wiped out in a market correction but if I decided not to go back, I would have *never* gotten my money back. At that point I realized you could never, *ever* turn your back on the

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market. You have to be there every single day. Then you're ready to go when stocks make their move out of a correction. You have to be there every day in a bear market and every day in a correction. You have to anticipate the correction as well and be ready to go to cash when it comes.

It took me six years at 50–60 hours per week to finally put it all together. I was in the construction business back then, and the severe housing market downturn during the early 1990s when the construction market came to a screeching halt allowed me to devote so much time to learning everything that I know today.

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*o let me get this straight. You got started in 1976 and then got into trading more seriously in 1989 and then gave it all back in 1991?*

Yes, that's about right, I gave it all back several times. I gave it all back three or maybe four times. My aggressive 2-to-1 margin style took years to learn, and getting in and out and understanding money management is key. If you want this lifestyle and the rewards it can bring, it will take time and heartache before you can put it together. And spotting a correction and being ready to go to cash is top priority to surviving.

*Do you think it's necessary to give it all back a few times before you finally get it? Is it necessary for someone starting out today to go broke before they become successful?*

It's not necessary, but I'm not sure you are going to be able to do it unless you get hammered a few times, and you won't fully understand the seriousness of the market until you do. And it also depends on your style. I'm a type-A personality kind of guy. I enjoy the adrenaline rush. To get that thrill, I have to be on 2-to-1 margin and that keeps my interest in the market. I'm the racecar driver doing 180 MPH around the course inches from the wall. And that's what I like. If you aren't like that, then you have to adjust yourself and your risk

factors accordingly. That's how I turned \$10,775 into \$18 million in 18 months and ultimately went to \$42 million in 23 months. I would own the one or two fastest stocks of the week during the bubble, and I would know exactly when to buy it on 2-to-1 margin and be out within a few points of the top and compound my money weekly, swing trading these lightning-fast moving stocks leaping \$10 to \$25 a day or more. I would be so glued to the computer screen you would almost have to peel my eyes off the monitor with a spatula.

*What do you watch for during the trading day?*

I'm watching the heartbeat of the stocks. I'm watching the action. I have five screens, but focus on one main monitor running MyTrack with a backup on another monitor using eSignal. I have a Level II, which I use rarely, on another monitor, but it also has my stock positions; I have AIQ on another monitor and LiveWire on another. I don't watch futures or any of that other stuff. I don't have time. I just watch the chart, the price action, and the volume of the stock during the day. I want to know how institutions are treating the stock and do that by watching price and volume action.

*Are you looking for price and volume breakouts and chart patterns that you like?*

Yes. But I want to see how the institutions are treating the stock as well by watching the ebb and flow during the day. I watch bid, ask, and volume as well as price change throughout the day and I watch how they run through it on volume spikes. I watch to get a feel of the stock on the quote screen. On various chart patterns, stocks should be doing certain things at certain times. When the stock is acting right, volume should come in and do certain things. If it doesn't do what it's supposed to do, when it's supposed to do it, then something isn't right and I'll pass on that stock until the time is right. A stock might suddenly go limp or it may be very hot for a week and then volume just disappears. Whoever was playing with the stock is gone and if they're gone,

then so am I. If it's no longer the stock it was last week I'll just walk away until it gets frisky again.

*What would be a typical size of your trades today?*

It depends on the volume. If a stock trades six to 10 million shares a day, I can be happy owning 100,000 shares. If the stock trades only one million shares a day, then owning no more than 20,000 to 30,000 is about my max.

*You set a record in turning \$10,775 into \$18 million in 18 months. Are you aware of anyone else who beat that record?*

No one has come close, as far as I know. There was someone trading on the CBOT who turned \$50,000 or \$100,000 into \$100 million or something like that, but that was commodities or futures and the time frame was longer. No one has done it trading stocks that I am aware of.

*What were your single best and worst days in the market?*

There were so many wonderful days for me during the bubble that I can't list them all. I could go on and on about stocks like Amazon leaping from \$120 to \$200 on the day it split 3 for 1, or CMGI running up from \$118 to \$305 in just two days on its way to splitting 2 for 1, or QCOM running up from \$256 to nearly \$800 in eight weeks and selling it the day it split 4 for 1, \$5 off its all-time post-split high of \$196. Then there was National Discount Brokers (NDB), which has since been bought out, which ran from \$32 to more than \$85 in a few days, or UBID as it ran from \$63 to \$180 in four days. Just to name a few that I was in.

*What else? Good days and bad days?*

There was also the time one day after the market topped in March and the market had come down from 5132 to 3200 where I covered my shorts and went long on margin 2 to 1, only to watch the market soar on some ridiculous news story. The market soared something like 200 points that day and I made around \$5.2 million in one day. It was a good day at the office.

The worst day was in October 2000 when fiberoptic stocks were the rage

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**CANSLIM**

William O'Neil founded *Investor's Business Daily*. CANSLIM is an acronym for the seven criteria that he considered most important in finding winning stocks.

**C Current quarterly earnings per share:** Should be accelerating.

**A Annual earnings increases:** Look for meaningful growth.

**N New products, new management, new highs:** Buy at the right time.

**S Shares of common stock outstanding:** Keep it small.

**L Leader or laggard:** Find an industry's leaders, not laggards.

**I Institutional sponsorship:** A little goes a long way.

**M Market direction**

—MB

and almost every fiber stock was set up to break out and run on earnings news from each company as it reported. By this time I had so much cash it was mind-boggling. Even worse, with that kind of money leveraged on 2-to-1 margin, it's very tough to buy stocks as they break out. I had to start buying stocks during basing periods, which is what institutions do, and why you get the base patterns you get.

I was in just about every hot fiber stock at the time from Corning (GLW) to Juniper Network (JNPR), Broadcom (BRCM), and Newport Corp. (NEWP), just to name a few. Wouldn't you know it, I had just loaded up on these and other very high-beta stocks on 2-to-1 margin, when Nortel Networks (NT) preannounced a short fall in revenue and earnings after the close of trading one day. Since it was the sector leader of the group at the time, the news caused every fiber and fiber-related stock to gap down anywhere from \$15 to \$20 in

after-hours trading. Things got worse the next day, with stocks such as NEWP getting whacked as much as \$45 or a third of its value during the day. Good thing I wasn't 100% invested in fibers and luckily had a few shares of some software stocks, which didn't take the hit that the fibers did. I lost about 32% of my total portfolio in just one day.

***You made a comment about Royal Gold (RGLD) in Forbes. Do you trade gold stocks as well?***

I trade whatever the market is going to push up the most. At the time, gold was the no. 1 group of equities moving up. The market was bad, gold was a countermarket, counterdollar safe haven play at the time, and the market was pushing gold up. Royal Gold (RGLD) was one of the leaders of the gold group. I could never figure out why this stock was holding up so well, as there were no earnings and very poor revenues. There were certainly much better gold stocks to own at the time, but somewhere, someone decided to support and push this stock.

***Do you use cycles in your analysis?***

I have been doing more work with cycles over the past six years, even though I've known about them for 25 years. They are powerful and an absolute must. They help to explain why stocks act the way they do if you can decipher these cycles. You have to know the various cycles and combine them with patterns and then you'll really get a boost to your trading. There are many cycles, from very short term to long term to very long term. The nine-month cycle and the Presidential cycles are two of the most powerful in the market today.

***We've got to wrap up here. You mentioned that you have to watch the markets every day. When do you take time off?***

For me, every day in the markets is a vacation. If you've ever worked in the

construction business like I did for 20 years you'd understand this. If the markets are open, I have to be here. There is nothing more exciting and enjoyable. It is the passion and love of my life. I'm so blessed to be doing what I want to do and get paid to do it. It doesn't get any better. There is nothing I'd rather do. Every day is different and your brain is being taxed and you have to figure out the puzzle. Do you hold 'em or fold 'em? What's going to happen next? It doesn't get more exciting than this. I do take time off every 18 months or so, but I can't think of anything I'd rather do than trade and watch the markets. When I'm on vacation I can't wait to get back to the market where all the action is. *This is truly exciting stuff!*

***Thank you, Dan.***

*Matt Blackman is a trader, technical analyst, software reviewer, and content provider for technical trading/investment websites. He is an affiliate member of the Market Technicians Association (MTA) and Canadian Society of Technical Analysts (CSTA).*

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