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1 Art of pair trading

You can download the pair trading video for example and in-depth analysis and explanation from the following link

http://www.smartfinonline.com/pair-trading.zip

Pair trading is a process of buying the cheaper stock and selling the costly stock simultaneously in future segment to benefit from all kind of market condition . In this article, you will learn the followings.

a. What is pair trading?
b. How to choose pair of stocks for trading?
c. Important Statistical parameters for pair trade.
d. Trade initiation process
e. Position protection and profit estimation and exit process
f. All mathematical formulas associated with pair trading.

a. What is pair trading?

Definition: when two correlated stocks are chosen for the trade with market neutral approach then the trading method known as pair trading.

Example: icici bank and hdfc bank both in the private banking sector and has close similarity in the business model.

Download or view the following videos
Link to our Google group http://www.smartfinancein.com/contactus.php

Note : smart finance future and option course discusses the advanced pair trading method named as " Beta decoupling method"
Link to our Google group http://www.smartfinancein.com/contactus.php

Any viewing or download issue email to admin@smartfinance.in

b. How to choose pair of stocks for trading ?

1. Both the stocks must be from the same industry.
2. Stocks must be a component of a sectorial index.
3. Stocks must have a close correlation in business model and business structure.
4. Technical parameters

a. The volatility in annual terms for the pair must not defer by 50%

b. The high volatile stock must be the dominating partner in the pair

c. correlation coefficient must exit either in +ve or –ve zone

d. spread difference must show some correction.

c. Important Statistical parameters for pair trade.

1. **Correlation** – statistical parameter gives value between -1 to +1. Positive correlation means both the stocks in the pair moving in the same direction, –ve means both are moving in opposite direction, 0 means both are moving randomly. Ideal correlation is +/- 0.6018

2. **Alpha, Beta** – This two calculation is required to calculate the below ratios.

3. **Ratios –** a. Jensen's alpha. b. sharp ratio c. Trey nor ratio
   Above ratios are required to identify the expensive and cheaper stock

d. Trade initiation process: Pair trade is initiated by the way of purchasing the cheaper stock and by selling the costly stock.

When the trade will be initiated?

1. If the current spread is above or below 2% of the mean spread.

2. If the correlation changed from + ve to – ve or vice versa.

3. If the correlation increase or decrease by 50% from its previous recorded data.

4. If the beta shows decoupling nature.

e. Position protection and profit estimation and exit process

Once the pair trade initiated, the position must be protected by using the options. The process of involving the options must be taken from the volatility study.

Profit estimation and exit process: Book partial profit once the price spread approach the mean spread. Book full profit once the price spread move 10% above the mean spread.

f. All mathematical formulas associated with pair trading.

J-Alpha = return on the stock 1-(interest rate+ stock beta*(return on stock 2- interest rate)

Sharp Ratio : (Return given by the stock – Risk free interest rate)/ annual volatility

Trey nor Ratio (Reward to volatility): (return on stock – risk free interest)/ beta of the stock. Lower the ratio stock is cheaper and higher the ratio stock is costly.

Alpha = Sum(Y)/N-[past N days Beta X sum(X)/N]

Beta = (N X sum (XY) – (sum(X) X sum(Y)))/ (N X sum(X^2)-(sum(X))^2)

Alpha: If the stock x-y has positive alpha then x is overpriced. If x-y has negative alpha then x is underpriced.

Beta : if beta of a stock is –ve then it will move in the opposite direction of its pear company. If beta is +ve then both will move in the same direction. If beta is 0 then both stock does not have any relationship.

2 Intraday trade using volatility

Intraday trade using Gann Angle method

1. Free intraday trading gann angle calculator to practice http://www.smartfinancein.com/gann-angle-calculator.php

In my book on **"Gann Method"** though I have explained various principles of W.D.Gann's method and its application on the stock market but the one which inspired me a lot is "Gann angle" principle. The Gann angle is defined as the set of trend lines drawn from an individual price point or from different price points (i.e. high, low, and midpoint) in order to identify the supports and resistances of a future price move. At this stage, do not worry much about this definition. It will become simpler as you proceed to the next part of this article. The next big thing about the gann angle trend lines are that they are drawn at a particular angle with respect to the X-axis or to the time line. This concludes the basic formation of gann angle trend lines.

Now let me explain this concept with the help of an example. Say I wish to draw a trend line at 1X1 (read it "one by one") gann angle. This means my trend line is a straight line drawn in the price time chart which makes an angle 45 degree with the X-axis. You must ask me that how I have derived the 45 degree. Quite simple! This is a trend line drawn assuming 1 unit of price change happens with 1 unit of time change. If I will plot 1 unit of price change with respect to 1 unit of time change in a semi log scale and measure the angle with the help of a protractor I will get the angular measurement as 45 degrees.

For making an intraday trade decision, we need a point to make buy or sell entry. We need a stop loss point and couple of target points. However, this job can be done with any guesswork but we need perfection. The perfection will be achieved only through the mathematical calculation, which is accepted by the market.

W.D.Gann has given us 11 different trend lines which will guide us in making a trade decision. These trend lines are drawn based on the geometrical angle proportion in X and Y axis. For example the 2X1 (2 by 1) trend line is drawn assuming the 2 unit of price rise or fall happens in 1 unit of time. This trend line makes geometrical angle of 63.75 degrees with X-axis when drawn from a lower price point and projected towards the higher price points. Similarly, this trend line will make 26.25 degrees with respect to x-axis when it will be drawn from a higher price point and project towards the lower price point. This is the mathematical logic available in origin shifting, parallel line algorithm.

Now the 11 sets of trend lines from a lower price point towards the higher price point are as follows 1X1, 1X2, 2X1, 1X3, 3X1, 1X4, 4X1, 1X8, 8X1, 1X16 and 16X1.

The geometrical angle made by these trend lines with the X axis in an **up move** corresponding to **2X1= 63.75** degrees, 1X2= 26.25 degrees, 1X1= 45 degrees, 1X3= 18.75 degrees, 3X1= 71.25 degrees, 4X1= 75 degrees, 1X4= 15 degrees, 8X1= 82.5 degrees, 1X8= 7.5 degrees, 1X16= 3.75 degrees, 16X1= 86.25 degrees.

The geometrical angle made by these trend lines with the X axis in a **down move** corresponding to 1X2= 63.75 degrees, **2X1= 26.25** degrees, 1X1= 45 degrees,3X1= 18.75 degrees, 1X3= 71.25 degrees, 1X4= 75 degrees, 4X1= 15 degrees, 1X8= 82.5 degrees, 8X1= 7.5 degrees, 16X1= 3.75 degrees, 1X16= 86.25 degrees.

Gann Formula for calculating the support and resistance:

In gann study, the 180 degree considered as factor 1. This is because between the sunrise to sunset the solar motion happens approximately 180 degrees and it is considered as 1 day time.

The 2nd universal concept accepted by the financial analysts is that the supports are always calculated in a falling trend and it used to be calculated from the high.

The 3rd universal concept accepted by the financial analysts is that the resistances are always calculated in a falling trend and it used to be calculated from the low.

Gann formula for calculating the support and resistance is as follows:

a. Support = (square root of (high)- Degree factor)^2
b. Resistance = (square root of (low) + Degree factor)^2

Trading Rules as per gann and as modified by me (Soumya Ranjan Panda Author of this article)

a. The 3rd support or resistance of any price move is important (as per W.D.Gann).
b. In intraday trade 45 degree support break (1X1 support) will favor sellers and 45 degree resistance (1X1 resistance) break will support the buyers. Provided the annual volatility of the trading instrument must be higher than 50% (as per my own research)
c. In low volatile or medium volatile market (i.e. the annual volatility of the trading instrument is less than 50 %) the (1X4= 15 degree) resistance and (4X1=15 degree) support must be utilized for long and short entry provided no congestion or entry error should be present in the calculated price. (as per my own research)
d. If sell entry price at 15 degree or at 45 degree greater than buy entry price at 15 degree or 45 degree price point then it is considered as error and rectified by changing calculation procedure from the high and low to midpoint of high and low. This says that instead of calculating the supports down from high and up from low you can calculate the same from the midpoint of high and low (as per my own research)
e. If the price unit of the trading instrument is a 4 digit number then between the buy entry and sell entry price at least 5 unit difference is required to take unbiased decision as per this principle or else it is considered as congestion and it is rectified by changing the high and low to midpoint. (as per my own research)
f. If the price unit of the trading instrument is a 3 digit number then between the buy entry and sell entry price at least 3.5 unit difference is required to take unbiased decision as per this principle or else it is considered as congestion and it is rectified by changing the high and low to midpoint. (as per my own research)
g. If the price unit of the trading instrument is a 2 digit or single digit number then it must be converted to 4 digit number by the way of multiplying it with 10 or 100 or even with 1000 and the resistances and supports will be derived from the 4 digit number. And the results need to be dividing by the multiplier to reconvert it back to its original form. (as per my own research)

h. The smallest time interval in which you can identify the high and low is 5 minutes after the opening bell or the highest time interval you can consider is the 1st 15 minute after the opening bell. Any auction period must be ignored. Like now in Indian market 9 a.m. to 9 :15 is considered as call auction period. Hence the data from 9 a.m. to 9:15 a.m. must be ignored (as per my own research)

i. If any trade of yours triggers the stop loss or trailing stop loss then do not reenter the trade in the same direction again.

As a day trader speculation is my profession and I will follow these calculations like religious testimony.

Example: on 11th November 2010 SBI between 9:15 to 9:30 a.m. made high 3238.35 at 9:16 a.m. low 3214.10 at 9:27 a.m.

Below given are the calculation of resistances and supports for reference.

(You can download a readymade free to use gann angle calculator from our web site from the following link

			Low		High		
			3214.1		3238		
	Degree	Degree Factor	Resistance			Degree Factor	
16X1	86.25	0.479166667	3268.6604	1X16	86.25	0.479166667	3184.0442
8X1	82.5	0.458333333	3266.2787	1X8	82.5	0.458333333	3186.3958
4X1	75	0.416666667	3261.5178	1X4	75	0.416666667	3191.1015
3X1	71.25	0.395833333	3259.1387	1X3	71.25	0.395833333	3193.4557
2X1	63.75	0.354166667	3254.383	1X2	63.75	0.354166667	3198.1667
1X1	45	0.25	3242.509	1X1	45	0.25	3209.9592
1X2	26.25	0.145833333	3230.6567	2X1	26.25	0.145833333	3221.7735
1X3	18.75	0.104166667	3225.9219	3X1	18.75	0.104166667	3226.5053
1X4	15	0.083333333	3223.5558	4X1	15	0.083333333	3228.8725
1X8	7.5	0.041666667	3218.8262	8X1	7.5	0.041666667	3233.6095
1X16	3.75	0.020833333	3216.4626	16X1	3.75	0.020833333	3235.9793

http://www.smartfinancein.com/free-software.php . The paid calculator that is given along with the master course validates more number of logical conditions and infuses more number of gann principles in the decision making to give you greater success in intraday trade.)

As per the above discussion and calculation procedure, we have made the calculation of resistances and supports. As per the current volatility condition, we are being advised to buy the stock at 3223.5558 or sell at 3228.8725. This is violating the point D trade principle and considered as an entry error henceforth we will change the high and low to its midpoint and do the calculation from the midpoint of 3238.35 and 3214.10 is 3226.225 . The modified calculation table is as follows.

			Low		High		
			3226.225		3226.225		
	Degree	Degree Factor	Resistance			Degree Factor	
16X1	86.25	0.479166667	3280.8878	1X16	86.25	0.479166667	3172.0214
8X1	82.5	0.458333333	3278.5016	1X8	82.5	0.458333333	3174.3685
4X1	75	0.416666667	3273.7318	1X4	75	0.416666667	3179.0654
3X1	71.25	0.395833333	3271.3482	1X3	71.25	0.395833333	3181.4151
2X1	63.75	0.354166667	3266.5837	1X2	63.75	0.354166667	3186.1172
1X1	45	0.25	3254.6874	1X1	45	0.25	3197.8876
1X2	26.25	0.145833333	3242.8129	2X1	26.25	0.145833333	3209.6796
1X3	18.75	0.104166667	3238.0692	3X1	18.75	0.104166667	3214.4025
1X4	15	0.083333333	3235.6986	4X1	15	0.083333333	3216.7653
1X8	7.5	0.041666667	3230.9601	8X1	7.5	0.041666667	3221.4934
1X16	3.75	0.020833333	3228.5921	16X1	3.75	0.020833333	3223.8588

As per the modified calculation, we are advised to buy at 3235.6986 for final target 3280.8878 and sell at 3216.7653 for final target of 3172.0214

Trade outcome:

1. At 9:34 a.m. We got a chance to sell at 3217 and kept out stop loss at 3235.70 this as per our calculation. Upon achieving the 1st target 3214.4 we trail to stop loss to 3216.80, then upon crossing the 2nd target we trail the stop loss to 3214.40. Unfortunately, after touching the low 3211 at 9:39 a.m. the trailing stop loss triggered at 3214.40 and we just bagged less than +3 points.
2. Considering our short trade adventure is wrong and as per the last protocol set in the trade rule, we waited for the 3235.70 to come which we have got a chance at 10:07 a.m. and achieved till 3254 till 11:27 a.m. which is close near to our 45 degree target point.

If you are not quick in changing the stop loss also it will not dampen your trade performance.

In this case if my shell stop loss triggered at 3235.7 I will accept close near to 18.9 point loss and be a buyer at this point keeping the stop at 3235.7 and aim for the last target 3281 with some logical trailing stop loss.

This concept works in commodity, currency as well as in stocks. However, the limitation of this article is that it does not discuss all the trading rules and conditions that are being researched by me. In the gann master course the supplied software uses all the extended set of logics.

Day trading using Gann Angle dynamic approach: if we will make use of the volatility along with the gann angle then this concept will become dynamic and it will produce great result. All the above process that I have explained in the earlier section will remain same only additional parameter daily volatility will be used with the gann angle. In this method, we will calculate the daily volatility based on the past 10 days last trade price of any instrument.

1. Daily volatility calculation:

a. Take past 10 days last trade price of any stock or index.

b. Calculate the **absolute return** by using the natural logarithm function LN(). You will get 9 data points.

Formula: Absolute return = LN (Current price/ Previous price)

c. Calculate the square absolute return for all 9 data points.

d. Calculate the average of absolute return and square absolute return.

e. Calculate variance.

Formula: Variance = square absolute return – $(\text{absolute return})^2$

f. Calculate daily volatility percentage.

Formula: Daily Volatility percentage = square root of (variance) X 100.

From the daily volatility percentage, we understood in the coming day the stock or index whose daily volatility percentage was calculated as per the above process would fluctuate to the extent of daily volatility percentage.

I have taken the state bank of India 12 October to 25 October 2011 to predict the intraday level for next trading session using the gann angle and the volatility.

a. I have calculated the daily volatility as explained above for sbi.

Date	LTP-SBI	Absolute return	Square absolute return
12-Oct-11	1880	0	0
13-Oct-11	1875.35	-0.002476468	6.13289E-06
14-Oct-11	1883	0.004070941	1.65726E-05
17-Oct-11	1885.5	0.001326788	1.76037E-06
18-Oct-11	1885	-0.000265217	7.034E-08
19-Oct-11	1909.25	0.012782674	0.000163397
20-Oct-11	1933.9	0.012828195	0.000164563
21-Oct-11	1949	0.007777731	6.04931E-05
24-Oct-11	1911	-0.019689755	0.000387686
25-Oct-11	1842.25	-0.036639015	0.001342417
	Average	-0.002253792	0.000238121
	Variance	0.000233042	
Daily Volatility %		1.526570684	

Above calculation says the daily volatility is 1.5266%. Hence, the stock has the probability to fluctuate by 1.5266% in the coming day. Base on the above conclusion I will see a price fluctuation of 28.1233 (i.e. 1842.25 x 1.5266/100) rupee in the sbi counter in future trading session.

Hence my expected high is 1842.25+28.1233 =1870.3732 my expected low is 1842.25-28.1233=1814.1268.

Now in order to get the buy sell level in the gap up opening with uptrend I will use the 1842.25 as low and 1870.3732 as high in the gann angle tool and follow all its rules to derive the targets.

Using the above price points I observe that the **trading rule–d** is being violated, hence I have done the changes in the data point to 1856.32 (i.e. midpoint of the above data points) and derive the following levels for the future trading session.

			Low		High		
			1856.32		1856.32		
	Degree	Degree Factor	Resistance			Degree Factor	support
16X1	86.25	0.479166667	1897.8394	1X16	86.25	0.479166667	1815.2598
8X1	82.5	0.458333333	1896.0247	1X8	82.5	0.458333333	1817.0355
4X1	75	0.416666667	1892.3978	1X4	75	0.416666667	1820.5894
3X1	71.25	0.395833333	1890.5857	1X3	71.25	0.395833333	1822.3677
2X1	63.75	0.354166667	1886.964	1X2	63.75	0.354166667	1825.9269
1X1	45	0.25	1877.925	1X1	45	0.25	1834.84
1X2	26.25	0.145833333	1868.9077	2X1	26.25	0.145833333	1843.7748
1X3	18.75	0.104166667	1865.3069	3X1	18.75	0.104166667	1847.3548
1X4	15	0.083333333	1863.5078	4X1	15	0.083333333	1849.1461

1X8	7.5	**0.041666667**	**1859.9122**	**8X1**	7.5	**0.041666667**	**1852.7313**
1X16	3.75	**0.020833333**	**1858.1156**	**16X1**	3.75	**0.020833333**	**1854.5252**

In the future trading session which follows the 25th october 2011 any gap up opening above 1849.14 and below 1863.50, if the price cross over 1863.50 then I will buy sbi for optimum target of 1898 and any gap up opening and price below 1849 I will sell for target 1815.25.

Similarly, to get the buy sell levels in the gap down opening and downtrend I will use the 1842.25 as high and 1814.1268 as low in gann angle tool and derive the targets.

Using the above price points I observe that the **trading rule–d** is being violated, hence I have done the changes in the data point to 1828.19 (i.e. midpoint of the above data points) and derive the following levels for the future trading session.

			Low		**High**		
			1828.19		**1828.19**		
	Degree	**Degree Factor**	**Resistance**			**Degree Factor**	**support**
16X1	**86.25**	**0.479166667**	**1869.3954**	**1X16**	**86.25**	**0.479166667**	**1787.4438**
8X1	**82.5**	**0.458333333**	**1867.5943**	**1X8**	**82.5**	**0.458333333**	**1789.2058**
4X1	**75**	**0.416666667**	**1863.9947**	**1X4**	**75**	**0.416666667**	**1792.7325**
3X1	**71.25**	**0.395833333**	**1862.1962**	**1X3**	**71.25**	**0.395833333**	**1794.4971**
2X1	**63.75**	**0.354166667**	**1858.6019**	**1X2**	**63.75**	**0.354166667**	**1798.029**
1X1	**45**	**0.25**	**1849.6312**	**1X1**	**45**	**0.25**	**1806.8738**
1X2	26.25	**0.145833333**	**1840.6822**	**2X1**	**26.25**	**0.145833333**	**1815.7404**
1X3	18.75	**0.104166667**	**1837.1086**	**3X1**	18.75	**0.104166667**	**1819.2931**
1X4	15	**0.083333333**	**1835.3232**	**4X1**	15	**0.083333333**	**1821.0707**
1X8	7.5	**0.041666667**	**1831.7548**	**8X1**	7.5	**0.041666667**	**1824.6286**
1X16	3.75	**0.020833333**	**1829.972**	**16X1**	3.75	**0.020833333**	**1826.4089**

In the future trading session which follows the 25th october 2011 any gap down opening above 1821.07 and below 1835.32, if the price cross over 1835.32 then I will buy sbi for optimum target of 1869.39 and any gap down opening and price below 1821.07 I will sell for target 1787.44.

If the price in future day may have a gap up **opening above 1863.5078 or below 1849.1461 or gap down opening below 1821.0707 or above 1835.3232** then the above calculation will not solve our requirement then we need to take the opening price of that day into account for calculation of volatility. We will use the opening price with projected high and opening price with projected low in gann angle tool to derive the entry levels. Say SBI open at 1870 on the future trading day which follows the 25th october 2011 then in the volatility calculation replace the 1842.25 with 1870 and calculated the new volatility and expected high and low. The new data points will be as follows

Date	**LTP-SBI**	**Absolute return**	**Square absolute return**
12-Oct-11	**1880**	**0**	**0**
13-Oct-11	**1875.35**	**-0.002476468**	**6.13289E-06**
14-Oct-11	**1883**	**0.004070941**	**1.65726E-05**
17-Oct-11	**1885.5**	**0.001326788**	**1.76037E-06**
18-Oct-11	**1885**	**-0.000265217**	**7.034E-08**
19-Oct-11	**1909.25**	**0.012782674**	**0.000163397**

20-Oct-11	1933.9	0.012828195	0.000164563
21-Oct-11	1949	0.007777731	6.04931E-05
24-Oct-11	1911	-0.019689755	0.000387686
25-Oct-11	1870	-0.021688234	0.00047038
	Average	-0.000592594	0.000141228
	Variance	0.000140877	
Daily Volatility %		1.186916667	
Expected high		1892.195342	
Expected low		1847.804658	

New trading levels in uptrend will be as given below. Since the opening is gap up the uptrend, calculation will be followed for trade decision. In this case, the downtrend level calculation is not required.

			Low		High		
			1881.1		1881.1		
	Degree	Degree Factor	Resistance			Degree Factor	support
16X1	86.25	0.479166667	1922.8941	1X16	86.25	0.479166667	1839.7651
8X1	82.5	0.458333333	1921.0674	1X8	82.5	0.458333333	1841.5527
4X1	75	0.416666667	1917.4167	1X4	75	0.416666667	1845.1306
3X1	71.25	0.395833333	1915.5926	1X3	71.25	0.395833333	1846.9208
2X1	63.75	0.354166667	1911.947	1X2	63.75	0.354166667	1850.5038
1X1	45	0.25	1902.8483	1X1	45	0.25	1859.4767
1X2	26.25	0.145833333	1893.7713	2X1	26.25	0.145833333	1868.4712
1X3	18.75	0.104166667	1890.1466	3X1	18.75	0.104166667	1872.0751
1X4	15	0.083333333	1888.3356	4X1	15	0.083333333	1873.8783
1X8	7.5	0.041666667	1884.716	8X1	7.5	0.041666667	1877.4874
1X16	3.75	0.020833333	1882.9076	16X1	3.75	0.020833333	1879.2933

Trend termination point: Gann angle also helps us in identifying the trend and the trend termination. 1 X 4 or the 4 X 1 angle price point cross over is known as the preliminary trend confirmation points for uptrend or downtrend. However, the 1 X 1 angle price resistance crossover signals the strong up trend break out and the 1 X 1 angle price support break considered as strong down trend break out. In gann angle concept we assume all the trend action will terminate at 1 X 16 or 16 X 1 angle price point.

3 Option intraday trade techniques

Introduction: many people want to trade in option for intraday due to its low capital requirement and huge profit potentiality. However, it is being experienced that the option buyers used to lose money very often. The reason is quite simple traders jump into the option trade without knowing the answer of the following questions. I will request you to find the answer of these questions then jump into the option trade for intraday. Certainly I will give you the valid mathematical answer for the below mentioned questions.

A. Which strike option to trade for intraday in nifty?

B. **When to trade in options and when not to trader in options for intraday ?**

C. **Use our binomial option calculator (only free tool available in web till date)?**

D. **How to initiate option positional strategy?**

Let us start the discussion from the 1st point "**Which strike option to trade for intraday in nifty**?" this method is not limited to nifty option it is useful to all stock options too.

While making a choice of strike to trade in option we often find the following problem.

A. Just In the money and at the money call options of nifty used to have high time value and has greater risk to trade for intraday.

B. Deep out of money options have less chance to appreciate in comparison to the just in the money options. Hence it is not suitable for intraday trade.

Simple mathematical approach to choose a right strike for trade:

a. Go to the www.NseIndia.com

b. Click on the get quote under the future column

c. Get the quote for nifty

d. In the bottom find the daily volatility

e. For 12th January it was 1.04

f. 11th closing price was 5256.10 as per the volatility principle explained by me in the article "**Trade in nifty future intraday for making sure profit**".

g. The high to low range will be 54.66 for the day.

h. Hence I will see nifty at 5310 or at 5201 for 12th January 2011.

i. **Hence, 5200 and 5300 strike options either call or put is important for me as a trader for intraday trading point of view.**

j. The midpoint of **5310 and 5201 is 5255.50** will decide the trend. Price above 5255.50 will scale maximum till 5310 and below 5255.50 will scale till 5201 under this volatility condition.

When to trade in options and when not to trader in options for intraday ?

As per the above discussion I will have maximum price range 54.66 for intraday.

1. If current high, low difference is less than 27.33(54.66/2) point then time has not come for trading in the chosen strike options.

2. If the current price is above 5310 or below 5200 then strike chosen by me to trade in options is not correct.

3. If current opening is above 5255.50 but below 5310 then good time to trade in 5300 ce option

4. If current price is below 5255 but above 5201 good time to trade in 5200 put option

5. If the current price is above the 1.618% growth retracement level of last settlements high and low then do not trade in call options for intraday.(to know why 1.618 revisit the Fibonacci principle)

6. If the current price is below the 1.618% decay retracement level of last settlements high and low then do not trade in put options for intraday.(to know why 1.618 revisit the Fibonacci principle)

How to use binomial option calculator?

Now I have following information

I will do intraday trade only in 5200 or 5300 strike call or put option.

Nifty has a chance to go up to 5310 or to 5201

Price above 5255.50 trends is in favor of the buyer

Price below 5255.50 trends is in favor of the sellers.

Price range set for the day based on volatility is approximately 54.66 points

I need to calculate the trend confirmation point: Just use the price point 5255.50 in the binomial option calculator it will give you the buying entry point and selling entry point.

I will buy 5200 call option if nifty cross above 5270.30(0.272 % retracement from 5255.5 to 5310) and buy 5300 put option if nifty fall below 5240.70 (0.272 % Fibonacci retracement drawn from 5255.5 to 5201)

Why so ? This is the option going to becoming deep in the money; it will have less time value component.

Now I need 3 things.

1. Price of 5200 call option at 5270.30 (this is my entry price)

2. Price of 5200 call option at 5240.70 (this is my stop loss)

3. Price of my call option at 5310(this my maximum target)

Similarly, I need the 3 things for the put option.

1. Price of 5300 put option at 5240.70 (This is my entry price)

2. Price of 5300 put option at 5270.30 (this is my stop loss)

3. Price of my put option at 5201(this my maximum target)

Now I will use the following information in the binomial option calculator:

Current price is midpoint 5255.50,

Strike price 5200

I will input the current option premium (this will be used to calculate the actual volatility in the option and actual volatility will be used to calculated the target and stop loss for the option) 105 when nifty was trading at 5250 on 12th January 2009.

I will choose the call option.

In volatility field I will entry any positive number >50. (This will be used only once for reference to calculate the actual volatility). I have entered 50

Days till expiry will be the number of calendar days. I have entered 17

It has given me the following output (I have got 5267.70 and 5243.30 since I am using the Gann angle proportion instead of the Fibonacci proportion. However Gann proportion is more accurate as compared to the Fibonacci proportion)

Buy 5200 ce at 111 when nifty will be at 5267.70 for target 119@5180, 127@ 5293, 144@5316. Since I know nifty in upside can scale to 5310 I will keep my final target below 144. Stop loss for the call option is 88

Now keeping all other information as same I will change the strike to 5300 and will select 5300 put option. This too has given us the information buy 5300 pe at 111 when nifty will be 5243.30 for target 118 @5231-125@5219-139@5195. since I know nifty may scale max till 5200 I will keep my final target below 139. Stop loss will be 92 for this entry.

Currently both strike options at 105 and nifty is at 5250. I will wait for my entry to come in order to initiate the position.

From the above I know to buy nifty 5200 ca at 111 for target 144 stop loss 88 and 5300 pe for target 139 and stop loss 92.

If you wish to buy 2 call and 1 put then your maximum profit at 5310 will be (144-111)X100-(111-80)X50=1750

Max loss (111-80) X100+ (139-111) X50= 1700 at 5200 level.

By simulating other option strategy with different strike one can make wonderful money using this calculator.

Other benefit of this binomial option calculator:

13th January: Intraday volatility 1.03. Previous day close 5208.90. Hence, price range set for the day is 55.26. Upside target are 5264.10, down side target 5153.64. Midpoint is 5209. 5200 call and 5200 put will be best choice. Since nifty has less chance to go to 5100 or 5300. At that time nifty was at 5190.

I have used current price as 5209, strike as 5200, selected call option, entered the call premium as 86.

I have been advised to buy 5200 ce at 93 @5221, stop loss 74 @ 5196.75 target 100 at 5233, 106 at 5245,121 at 5269.

I have been advised to buy 5200 pe at 96 @5196, stop loss 80 @ 5221 target 101 at 5184, 107 at 5173 and 119 at 5149.

Since the current price of 5200 ce and 5200 pe are 86 and 90 respectively 5190 this says it is mispriced. As per the calculation call option must trade below 74 and put must above 96. Hence buying 2 put and 1 call at this moment is advisable. Hence binomial option calculator of Smart Finance will also inform you the miss pricing of the option.

If you have read this article seriously from start to end you must be in a need to get this calculator. **Do not worry I have developed this calculator for you. It is FREE to use. It uses simulation process to find the real time volatility and does all the calculation for you.** You just need to feed the values as advised by me. I am 100% sure it will help you in making money in option trade. You can access to this calculator by visiting http://www.smartfinancein.com/real-time-option-calculator.php (Note: you need to register yourself to use this tool)

4. Intraday trade using displaced moving average

Step1: find the 3 period or 3 days moving average

Step2: Find +3 or -3 displaced moving average as per the 2/ (n+1) approach

Step 3: price above the 3 period moving average + 0.382 X upper band of displaced moving average make buy entry

Price below the 3 period moving averages - 0.382 X lower band make the sell entry

Formula :

a. **3 period Simple moving average** = (price 1 + price 2 + price 3)/3
b. **3 period exponential moving average** = (current closing price (C)- previous period EMA)X smooth constant (K)+ previous period EMA
   Smooth constant = 2/(1+N)
   In the 1^{st} period, the SMA is used.
   N= Number of time period in this case N is 3

c. Displaced moving average forward indicator
+3 displaced moving average = EMA + (2/1+3) % of EMA
-3 displaced moving average = EMA - (2/1+3) % of EMA
Example: if the EMA is 5200 then
+3 Displaced Moving Average = 5200+2/4 % of 5200 = 5200 + ((5200*0.5) /100)=5226
-3 Displaced Moving Average = 5200-2/4 % of 5200 = 5200 - ((5200*0.5) /100)=5174
Buying price will be 5200+ 0.382*5226/100=5219.96
Selling entry will be 5200-.382*5174/100=5180.23
Final Buying target will be 5200+ 1.618*5226/100=5284.55
Final Selling target will be 5200-1.618*5174/100=5116.28