TRADING STYLES: AGGRESSIVE AND CONSERVATIVE TRADERS

By Daryl Guppy

We often talk about three trading styles - aggressive, position and conservative - without really explaining how these are different. These trading styles are related to the risk taken in the market by traders, but this is not to say that a conservative style carries less risk than an aggressive style. The approaches are used to determine the types of opportunities that the trader feels comfortable with. The risk in each trade is controlled, not by the entry point, but by the exit strategy in the face of a loss.

AGGRESSIVE TRADER

It is a mistake to think that aggressive trading means buying depressed stocks, or stocks in a downtrend, in the hope that the trend will reverse. This is not an aggressive strategy. It is more commonly called fading the trend and forms the foundation of long term conservative approach to the market as developed by Richard Dennis and his group of Turtle traders. Their objective was to get into high probability, low risk long term trends. The solution to getting an early entry into these trends was to make multiple entries as the trend looked like it was changing. If the downtrend did not change, then they followed very exact exit rules. This meant that the strategy required multiple entry and rapid exits until the trend did actually reverse. Then the objective was to stay with this long term trend development.

This is a fade the trend, or trade against the trend, approach. Other traders use it to identify downtrend reversals, or more commonly, to get out of an up trend before it changes direction. Aggressive trading, and the other styles, are more closely related to the way price action develops. Price action is tracked with a price chart, or a group of indicators, or a combination of the two. The distinguishing feature of the aggressive trader is his willingness to buy the stock in anticipation of a pattern development, or an indicator confirmation. This is fading the trend to the extent that the trade acts in anticipation.

An aggressive trading style means buying a stock in anticipation of a pattern developing, or an indicator entry signal being generated. This approach can be applied to highly speculative stocks, or to stable blue chip stocks. Please do not confuse aggressive trading with foolhardy, high risk trading that verges on gambling.

POSITION TRADER

The position trader is really a trader who buys stocks today with the intention of holding onto it for weeks or months. We also use this term to describe the trader who acts as the trading signal is nearly completed. In terms of a chart pattern this may mean deferring the entry into a trade until the last third of the up sloping triangle is under development.

This approach is more conservative than the aggressive trader and sometimes reflects a lower level of experience. The position trader waits until the pattern development is almost fully proven. The downside with this approach is that in a fast moving or bullish market, the position trader may end up behind the price action. He misses out on trades because the price takes off prematurely. In this environment, as in late 1999, the position trader might move as a stock price enters the last third of an up sloping triangle pattern.

In the current, more doubtful market, he might wait until the triangle is almost fully formed before buying the stock. The timing of his exact entry point may vary depending on market conditions, but his intention remains the same. He wants to have a high level of probability that the pattern is really the pattern he thinks it is.

These traders also use indicators to assist their entry decisions. In this case they wait until just after the indicator confirmation. Using a moving average cross over approach they will wait until the crossover actually takes place. In a Metastock search this will include stocks that give a 0 separation return. The position trader wants proof that his analysis is correct, but he is confident enough not to demand absolute proof.

CONSERVATIVE TRADER

The conservative trader demands absolute proof, and many times his trading suffers because his entry is delayed along with his exit. The conservative approach has very little to do with risk control. In fact, it often increases risk because the rewards from the trade are reduced, and the need to wait for absolute proof that an up trend has turned to a downtrend robs the trader of potential profits.

The conservative trader waits for confirmation that the pattern break, or the indicator signal, is correct. Their conservatism relates to the level of proof they require before they take action. Often these traders call for an additional feature. They want the price to pullback so they can get an entry closer to the original, and now proven, pattern.

This opportunity is sometimes available, more so in weak markets. It is not very often available in strong bullish and momentum driven markets. Here the conservative trader misses out on many opportunities. In a weak market the breakout and retreat pattern is quite common and this does provide opportunity to get into the trade.

None of these strategies is inherently more risky than the other if good money management and trading discipline is applied. Each of the approaches carries a different probability ratio of success to failure. It's easy to get it wrong when you fade the trend, and more difficult to make a mistake if you wait until the trend is proved. However, the risk is not in the point of entry, but in the way the trader handles a loss should his entry turn out to be wrong.

These distinctions - aggressive, position and conservative trading - relate to the way traders time their entry into a stock based on their understanding of the way chart patterns or indicators are developing. Every trading opportunity provides an opportunity for each of these trading styles to make money. Each of these types of traders can use exactly the same type of tool pack and collection of indicators because it is the position of their judgment in time that helps to determine the type of trader they are. Even conservative traders become more aggressive with experience, moving to act in anticipation of indicator and chart development.

We have shown these charts on a daily time scale but the same distinctions apply to intraday trading using 1 or 3 minute charts.