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## Updating Our EDS Models thru 2002

# How Have Our EDS Models Performed? Much Better Than S&P 500!

By David Vomund

**S**ince AIQ's Expert Design Studio (EDS) was released, we've created and published several trading strategies in the *Opening Bell*. As we complete more tests, our strategies are becoming more effective.

Of the strategies that we've published, some buy stocks into strength and some buy stocks into weakness. Some are active trading systems while others hold stocks for several weeks. Let's see how these models have performed.

### Divergence Model April 1998

One of our first EDS models was published in the April 1998 *Opening Bell*. This model looks for positive divergences in OBVpct and Money Flow. In addition, it requires the RSI Wilder to be greater than 50, the MACD to be above its Signal line, and Money Flow RSI to be above 70. Originally, we used a 7-day RSI but time has shown that the default of 14 days is more appropriate.

This model was created shortly after AIQ released EDS and we've since created more powerful models, but this strategy continues to have respectable

returns.

To test the strategy, we used a large database of about 2,000 stocks and sell parameters of 90% capital protect, and 90% profit protect when there is a 5% profit. The test was run from the time the model was published in April 1998 to January 2003.

Place  
Vomund Photo  
Here

DAVID VOMUND

*"Our Growth Model average trade gained 4.50% compared to an S&P 500 loss of 2.38% with 268 trades. Amazingly, if you just run the test for 2001 and 2002 the average trade still makes money!"*

Results of our testing showed that there were 481 trades with an average gain per trade of 1.18% compared to an S&P 500 gain of 0.36%. The average holding period was 19 business days.

### Growth Model March 1999

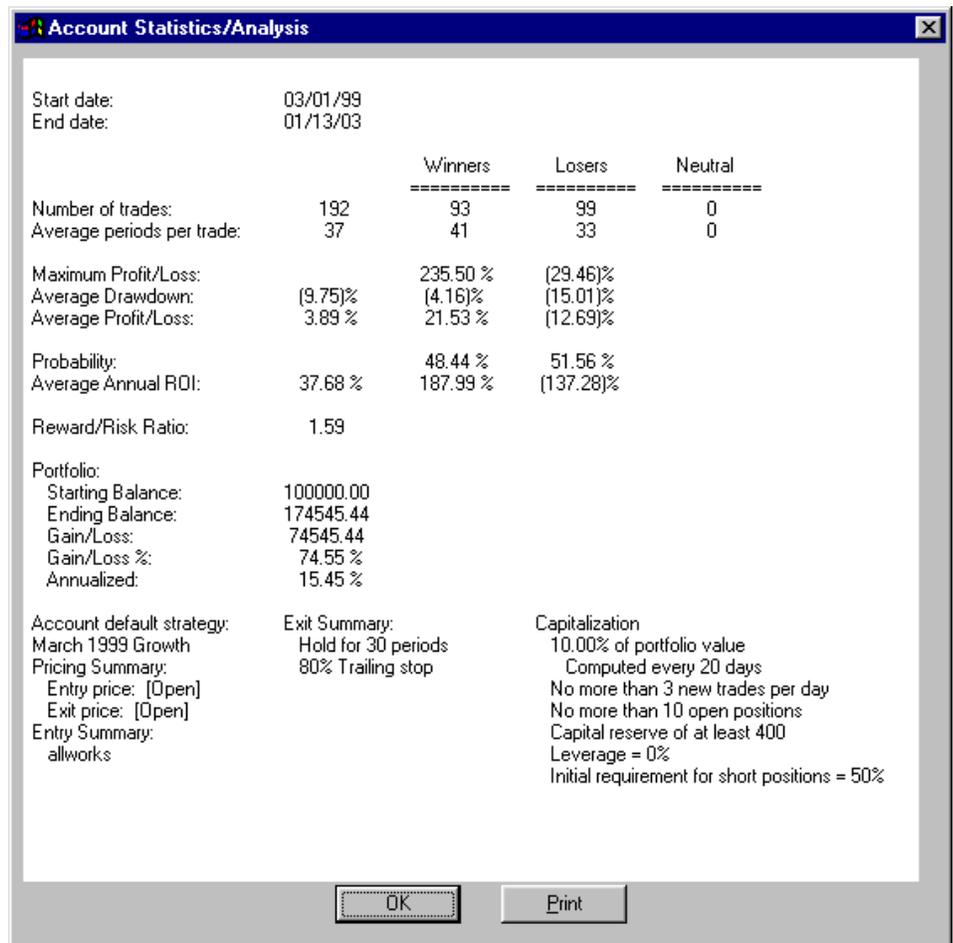
In March 1999, we ran a timely article that contained an EDS model for

growth investors. Growth investors buy into strength rather than trying to pick lows. The theory is that what is high often goes higher. Therefore, the key component in our model was that the stock must be above its 28-day ESA for all of the previous 60 days. Only stocks that experience a strong rally can accomplish this.

Having a stock remain above its 28-day moving average for 60 days backtested well, but in the original article we added to the model the criteria that the stock must be below its upper AIQ Trading Band. This eliminated stocks that had run too far. In addition, we added a rule stating that the Volume Accumulation Percent indicator must be above 30. We used a fixed 30-day holding period.

Year 1999 was great for growth investors, but the last three years were terrible years for growth investing. So how has the model performed over these years?

A test was run from March 1999, the date the model was created, to January 2003. A database of 2,000 stocks was used with the same fixed 30-day holding period that we used



**Figure 1.** Portfolio Simulator test results for EDS Growth Model developed in March, 1999. Test covers 03/01/99 to 01/13/03 time period and was run on a database of 2,000 stocks.

in the original article. The average trade gained 4.50% compared to an S&P 500 loss of 2.38% with 268 trades. Amazingly, if you just run the test for 2001 and 2002 the average trade still makes money!

To get a feel for how much money would have been made by using this system, we used the Portfolio Simulator on the model. We stated that 10 stocks was a fully invested portfolio with each new position being 10% of the portfolio value. For a sell strategy we used a fixed 30-day holding period and an 80% capital protect.

The Portfolio Manager showed a return of 74% during a time that the S&P 500 & Nasdaq Composite fell in

value. There were 192 trades (**Figure 1**).

These tests were run on a 2,000-stock database so a lot of stocks that were purchased were names that we've never heard of. If the same

*"The Portfolio Manager showed a return of 74% (for our Growth Model) during a time that the S&P 500 & Nasdaq Composite fell in value."*

test is run on the well known S&P 500 and Nasdaq 100 stocks, then the number of trades is dramatically reduced to 47 and the overall return falls to a 10% loss. That's still better than the 25% loss in the S&P 500.

## AIQ Opening Bell Newsletter

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## Citizen Kane Model

April 2000

In April of 2000, we created what we believed was our best EDS model. Appropriately, we named the model Citizen Kane. The foundation of the model is a rule that states that the stock must have corrected by at least 30% sometime between 10 and 50 days ago. This is a bottom-fishing model.

In addition to this rule, two rules using the Volume Accumulation Percent (VaPct) indicator were added. The first rule states that the VaPct indicator must have a value greater than zero. The second rule states that the 45-day slope of VaPct must be positive.

We tested this model starting from April 2000, the date it was created. The test was run on S&P 500 stocks using a 10-day holding period. There were 863 trades with an average gain per trade of 1.23% compared to an average loss of 0.22% in the S&P 500 (Figure 2).

When this model was created, having a stock correct 30% meant something. During the bear market

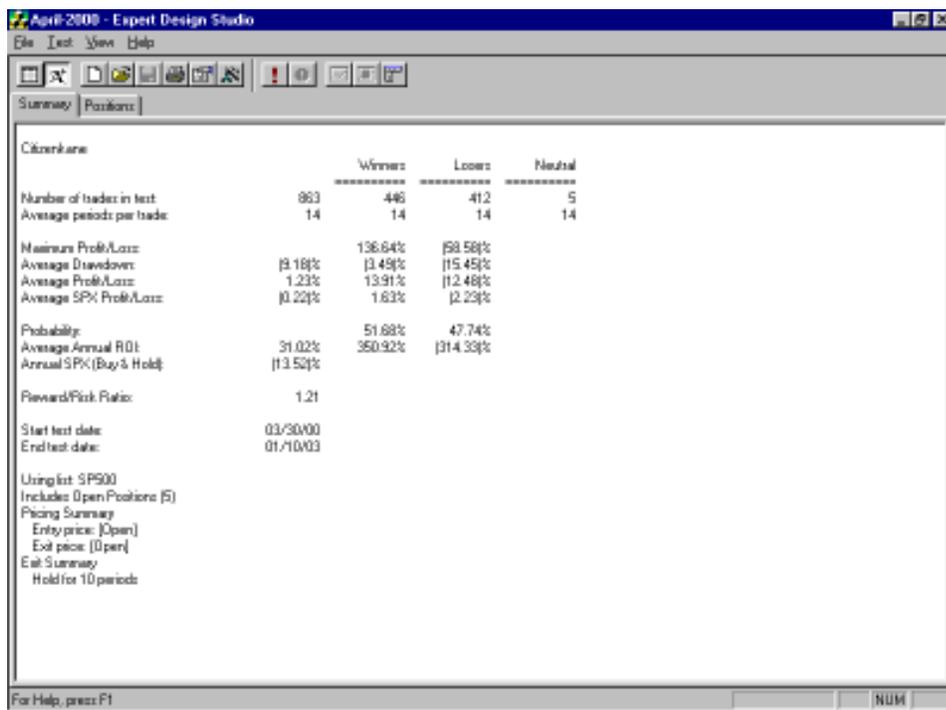


Figure 2. EDS backtest results for Citizen Kane Model developed in April, 2000. Test covers 03/30/00 to 01/10/03 time period and was run on a database of the S&P 500 stocks.

*“In April of 2000, we created what we believed was our best EDS model... the Citizen Kane. There were 863 trades with an average gain per trade of 1.2% compared to an average loss of 0.2% in the S&P.”*

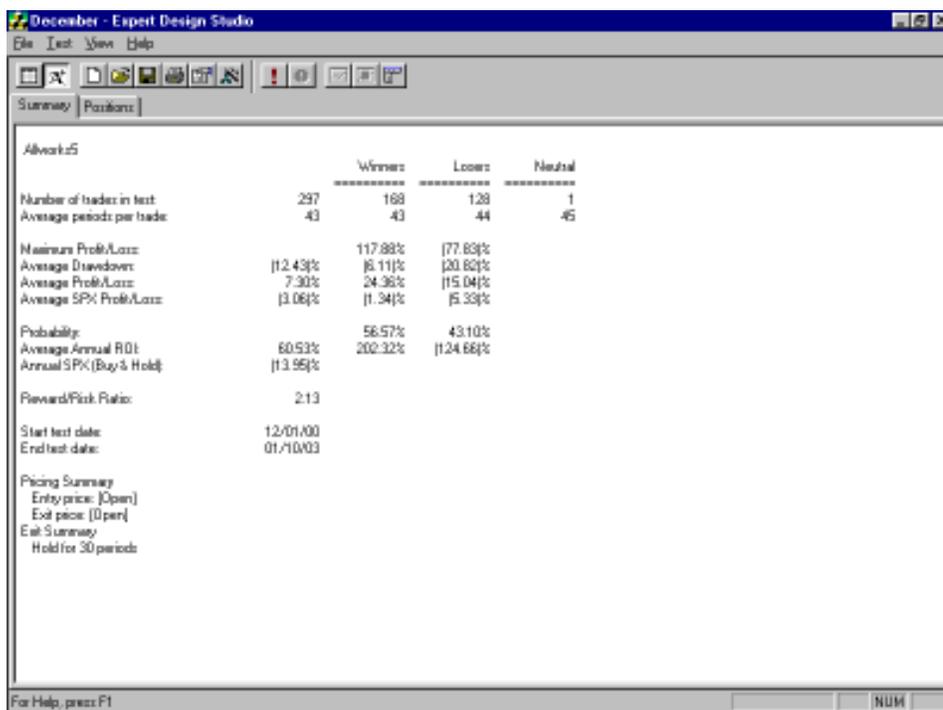


Figure 3. EDS backtest results for Extreme Growth Model developed in December, 2000. Test covers 12/01/00 to 01/10/03 time period and was run on a database of 2,000 stocks.

many stocks passed that test so the model became more of a VaPct screening model. As the market ends its collapse, it is likely that the model’s effectiveness in beating the S&P 500 will improve because a 30% drop in a stock will again mean something.

## Extreme Growth Model December 2000

In the December 2000 *Opening Bell*, we created a model that bought into high-flying stocks. The model is very simple. The model looks for stocks that have increased in value by at least 50% in the last 66 business days but have stalled or moved lower for the last 10 days. In addition, the Volume Accumulation Percent indicator must be above 25. Stocks that pass this model are obviously very volatile.

In the 1990s there were a lot of stocks that rose by at least 50% in the last 66 days. After this model was created in December 2000, only 13 of the current S&P 500 and Nasdaq 100 stocks passed that screening. Still, the average trade on those 13 trades made money.

Using a 2,000 stock database with a fixed 30-day holding period, the return is extremely impressive. From December 2000 to January 2003, the model's average trade was 7.30% compared to a 3.06% loss in the S&P 500 (**Figure 3**).

Obviously returns are even higher when 1999 is included.

To get a more realistic feel for the percentage return of this model since the start of 1999, we ran the Portfolio Simulator on a database of the current S&P 500 and Nasdaq 100 stocks. A fully invested portfolio had 10 stocks with each stock representing 10% of the portfolio.

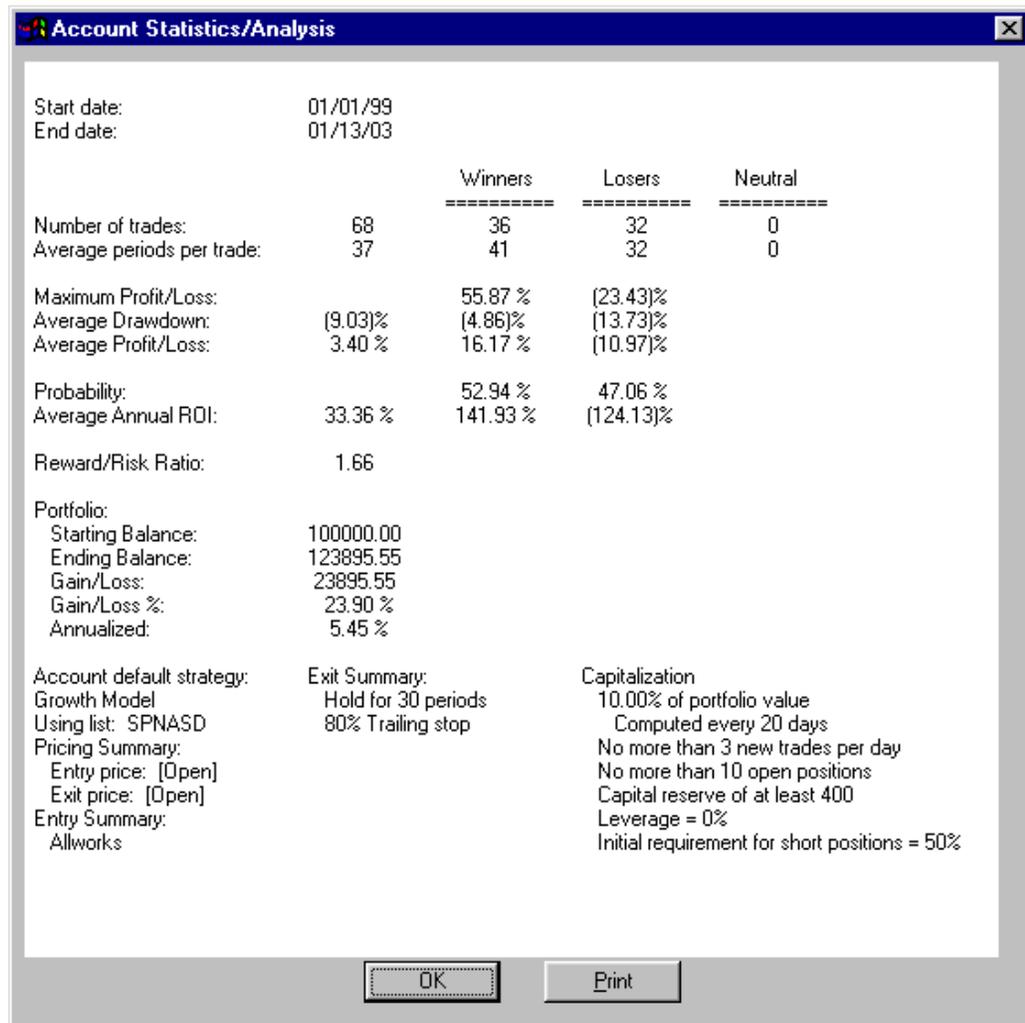
The overall return was 23.9%, or 5.45% annualized (**Figure 4**). That's very good considering the S&P 500 and the Nasdaq Composite were sharply lower during this time period.

In reviewing the models that we've published in the *Opening Bell*, it's nice to see that so many have

*"The return is extremely impressive (for our Extreme Growth Model). From December 2000 to January 2003, the model's average trade was 7.30% compared to a 3.06% loss in the S&P 500."*

continued to perform well after they were published. They weren't over-optimized.

These are backtests, however, and actual returns would be different. Past performance does not guarantee future returns.



**Figure 4.** Portfolio Simulator test results for Extreme Growth Model. Test covers 01/01/99 to 01/13/03 time period and was run on a database of the current Nasdaq 100 and S&P 500 stocks.

There were also models that didn't meet our expectations.

Among these were two short-selling models covered in the December 1998 and November 1999 issues. Because the market went down, these models made money but they failed to significantly outperform the S&P 500. They tested well

in the bull market but they lost effectiveness in the bear market.

Two more EDS models were created in May 2002 and in December 2002. It is too early to know how they will perform. At the start of next year, we'll review these two

models and also update the performance of the models covered in this article.

*David Vomund publishes VIS Alert, a weekly investment newsletter. For free trial issues, call 775-831-1544 or go to [www.visalert.com](http://www.visalert.com).*

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## What Every AIQ User Should Know, Part III

# It's a 'Simple Process' -- Using AIQ's Powerful Expert Design Studio To Create Trading Systems

By David Vomund

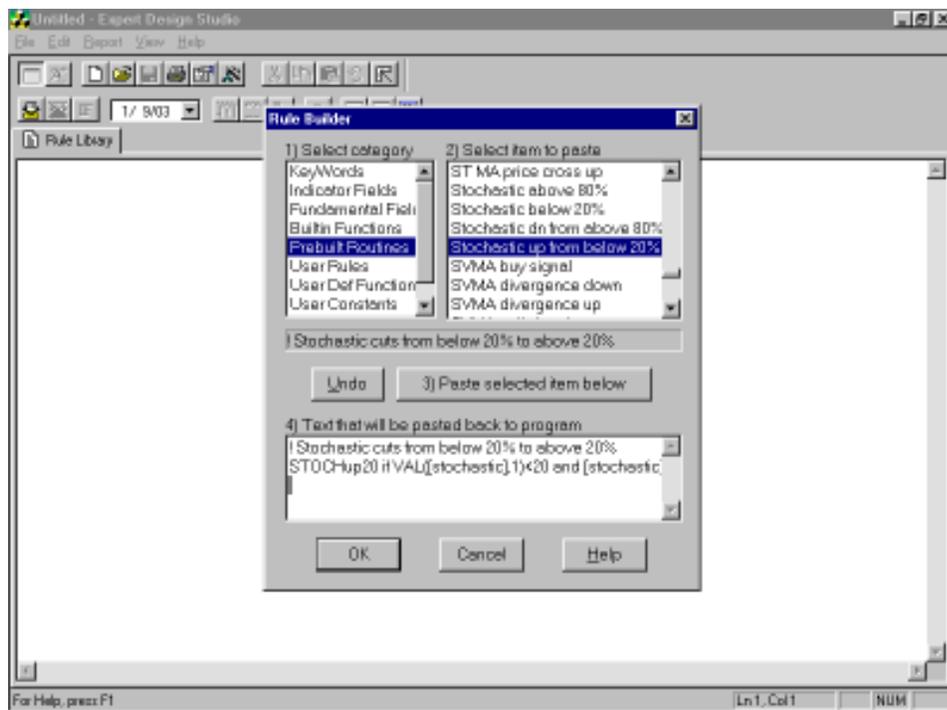
In this third article of our series covering features that every TradingExpert Pro user should know how to use, we will focus on the Expert Design Studio (EDS) module. This is an extremely powerful module but many AIQ users don't use it because they believe EDS involves difficult programming. In reality, EDS can be as easy or difficult as you want it to be.

The EDS module comes with about 200 pre-built routines. This allows users to build effective screening models by cutting-and-pasting rules that have already been created. Therefore, the user can build EDS models without any programming.

Before we describe how to create and run an EDS model, we'll first show you how important it is to learn how to use this feature. In the October 2002 and November 2002 *Opening Bells*, we printed the results of extensive testing of all the pre-

*"In Opening Bells, we have printed the results of extensive testing of all the pre-built rules, showing those that are the most effective and those that are the least effective... Users should know how to take advantage of this powerful information."*

built rules, showing those that are the most effective and those that are the least effective. Making the tests even more useful, the backtesting



**Figure 1.** Expert Design Studio Rule Builder screen. Panel 2 displays list of pre-built routines that can be selected and transferred to the lower panel (4).

time period covered both bull and bear markets.

The most effective strategies outperformed when the market was moving higher and also did well when the market was moving lower. We'll run similar tests using shorter holding periods in the March 2003 issue. Users should know how to take advantage of this powerful information.

At AIQ training seminars, we ask attendees to give us some technical buy rules. We then use the pre-built screening formulas to create a model based on those rules. For this article,

we'll assume that we want to create a model that screens for stocks that have given a Stochastic buy signal (i.e., the indicator moving above 20) at the same time that the MACD's Phase line rises above its Signal line.

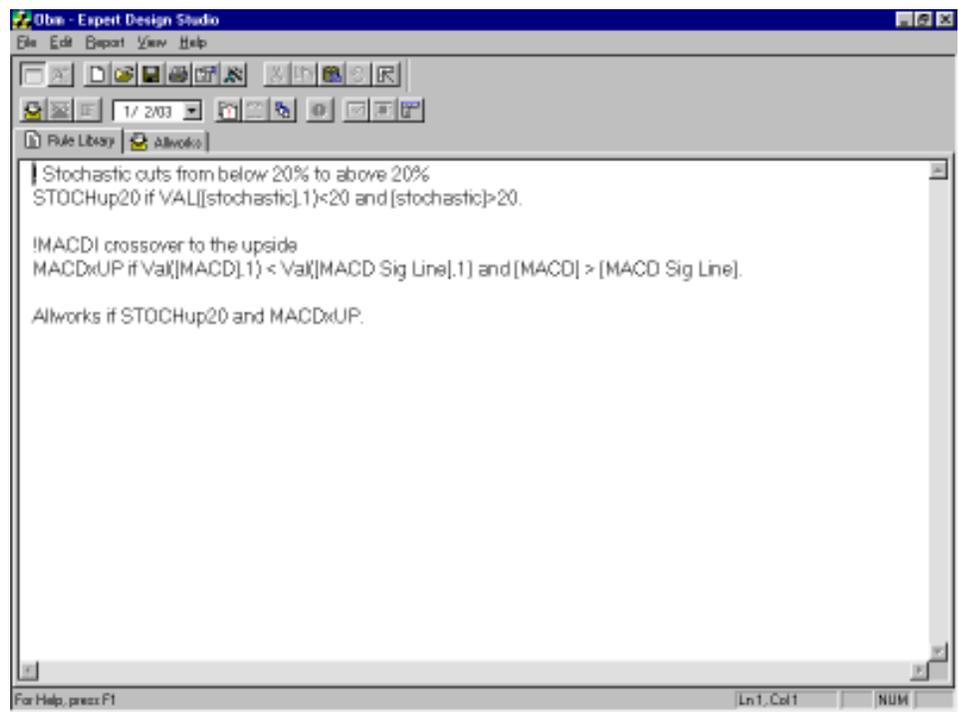
To create this model, go to the Quick Launch Menu and open EDS (the icon is marked *Studio*). The model will be created in the Rule Library folder, which appears when you open EDS. At this stage, the Rule Library folder is empty. We'll copy and paste the pre-built rules into this folder.

To see the pre-built rules, click *Edit* on the menu bar and then *Builder*. The Rule Builder screen will appear. From section 1, *Select category*, choose *Prebuilt Routines*. A list of the screening rules will appear in section 2, *Select item to paste*.

You'll see that nearly every indicator in the TradingExpert software has three or four pre-built rules associated with it.

For our model, we are first looking for stocks with Stochastic buy signals. Therefore, we need to scroll down through the list of indicators to the Stochastic rules. There are four pre-built Stochastic rules. We want the one called *Stochastic up from below 20%*. Single-click this rule and click *Paste selected item below*. The code for this screening will appear in section 4 of the Rule Builder screen (**Figure 1**). Click *OK* and this rule will be pasted into the Rule Library.

The second rule in our model states that stocks must have a MACD indicator crossover. Therefore, we repeat the process but this time look for the pre-built MACD rules. Again click *Edit* on the menu bar, and *Builder*. In section 1, choose *Prebuilt Routines*. In section 2, scroll down to the MACD rules and click



**Figure 2.** EDS Rule Library screen listing screening rules for the test model. Lines designated with an exclamation point (!) in the first position describe the rule appearing in the line below.

simple code:

```
Allworks if STOCHup20 and
MACDxUP.
```

Make sure there is a period at the end of the code.

The code for our model is now complete (**Figure 2**). All we have to do now is run the screening to see which stocks pass both rules. A report needs to be created for

the database for the stocks that pass our model. Click on the *Allworks* folder tab (next to the *Rule Library* tab) to make it active. In the date scroll box (above the *Allworks* tab), choose the date you want to run the screening. Then click *Report* on the menu bar and choose *Run Single*. If any stock passes the criteria, its ticker symbol will appear. Simply double-click the ticker symbol to see a chart of the stock.

That's it. We have created an EDS model by utilizing the pre-built routines. Creating a model in EDS

*"That's it. We have created an EDS model by utilizing the pre-built routines. Creating a model in EDS may be initially intimidating, but we have shown that it is a simple process."*

on the *MACD Cross Up* rule. Click *Paste Selected Item Below* and *OK*.

Our two rules are now in the Rule Library folder. Their rule names are the first word in the codes. Thus, the rule name for the Stochastic filter is *STOCHup20* and the rule name for the MACD rule is *MACDxUP*.

One additional rule is needed which states that stocks must pass both of our screening rules on the same day. We called our rule "Allworks" but you can call the rule any name you wish. Here is the

the new screening. On the EDS menu bar, click *Report* and *Insert*. If you want to see which stocks pass each indicator screening, then you would create a report for each of the rules. We are only interested in the stocks that pass both indicator rules, so click on *Allworks* and *OK*.

We are now ready to screen our

*"We chose EDS as a tool every AIQ user should know because in this newsletter we've published and will continue to publish some very effective screening models. You should know how to run them."*

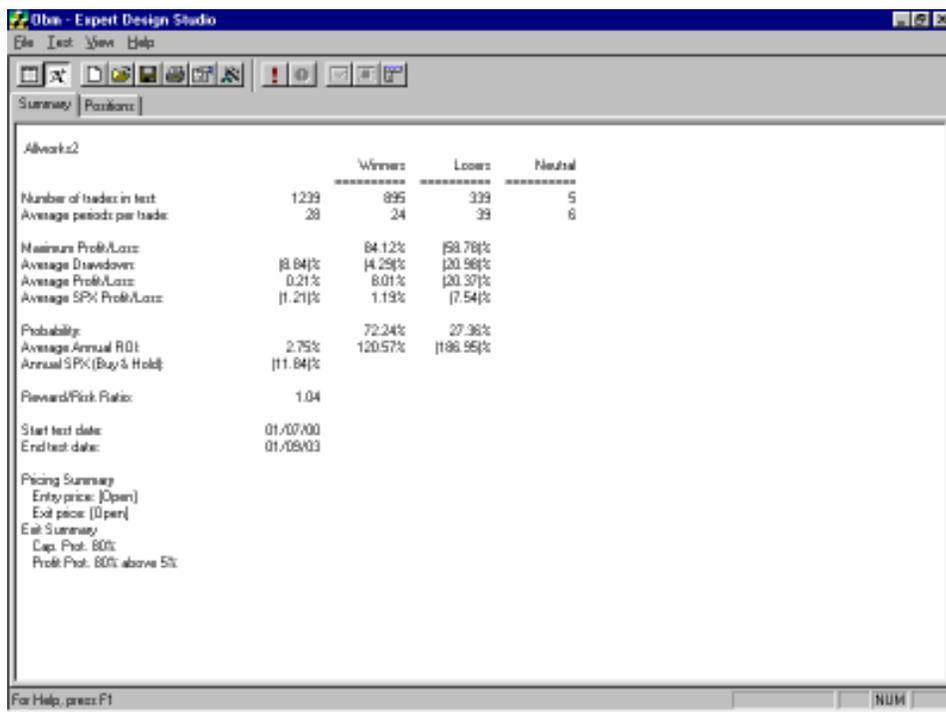
may be initially intimidating, but we have shown that it is a simple process. The bonus of creating a

model in EDS is that the model can be backtested.

To run a backtest, select the *Allworks* folder. From the menu bar, click *Report* and then *New Backtest*. TradingExpert uses the rule name as the name of the backtest. Click *Next*. On the *Entry* page, select *Buy Long* and click *Next*. On the *Range* page, enter the time period for your backtest and click *Next*.

On the next screen, *Pricing*, accept that trades are made using the next day's opening price. Click *Next*. On the *Exit* screen, choose the sell strategy. A useful exercise is to see how results change when a model is run using different sell strategies. Click *Finish*. The parameters of the backtest are now complete. To run the test, click *Test* on the menu bar and choose *Run*.

The result of our backtest is found in **Figure 3**. The most important statistic is the average profit/loss per trade compared to the average profit/loss for the S&P 500. In our test, the average trade gained 0.21% compared to an S&P 500 loss of 1.21%. If the average equity trade has a lower return than the average S&P 500 trade, then the system has



**Figure 3.** EDS backtest screen showing test results for example Model. Test covers 01/07/00 to 01/09/03 time period and indicates a 2.75% avg. annual ROI.

no value.

Some people want to create their own models but most people don't. We chose EDS as a tool every AIQ user should know because in this newsletter we've published and will continue to publish some very effective screening models. You

should know how to run them.

In the March *Opening Bell*, we will publish the most effective screening rules using a 5-day holding period. You should know how to combine the best rules to create effective stock screening models.

**STOCK DATA MAINTENANCE**

The following table shows stock splits and other changes:

Stock	Ticker	Split	Approx. Date
Tarragon Realty	TARR	3:2	02/18/03
Security Nat'l Financial	SNFCA	5%	03/03/03

**Trading Suspended:**

American Water Works (AWK), Applied Microsystems (APMC), Infinium Software (INFU), Nortek Holdings (NTK), Rare Medium Group (RRRR)

**Name Changes:**

Amerigroup Corp. (AMGP) to Amerigroup Corp. (AGP)  
 Boston Celtics (BOS) to Henley LP (HYN)  
 CPB Inc. (CPBI) to CPB Inc. (CPF)  
 Stilwell Financial (SV) to Janus Capital Group (JNS)

**S&P 500 Changes**

Changes to the S&P 500 Index and Industry Groups:

There were no Changes this month.

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## Market Review

**S**tocks began 2003 with the best three-day New Year's spurt ever, fueled by details of the tax cut. Then they faded fast.

Worries about Iraq combined with a weakening economy sent stock prices lower. For the month, the S&P 500 fell 2.7% and the Nasdaq Composite fell 1.1%. This is one of the few times that the Nasdaq outperformed during a market decline.

AIQ's timing model registered two signals in January. A 98 sell

came on January 17 and a 97 buy on January 29. The sell signal was confirmed by the Phase indicator on the day of the signal but the buy signal was not confirmed.

From a charting point-of-view, January 24 was a critical day for the market. That's the day the S&P 500 broke below a support level at 866. This level acted as support on October 29, November 13, and December 31. What was support became resistance as the market tried but failed to rise above this level.

At month's end, the market was very oversold. That could be seen in AIQ's US Score (US Score was covered in the December 2002 *Opening Bell*). Of S&P 500 stocks with unconfirmed signals, about 96% were on the buy side.

Looking at industry groups, Gold, Developing Communications, and Biotechnology were the best performers. These groups had small gains in January. The worst performing groups were Energy Services (down 6.6%) and Brokerages (down 5.8%).

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*David Vomund is publisher of VIS Alert, a weekly investment newsletter that exclusively uses AIQ's software. Vomund is ranked one of the top 10 market timers in the country by Timers Digest.*

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