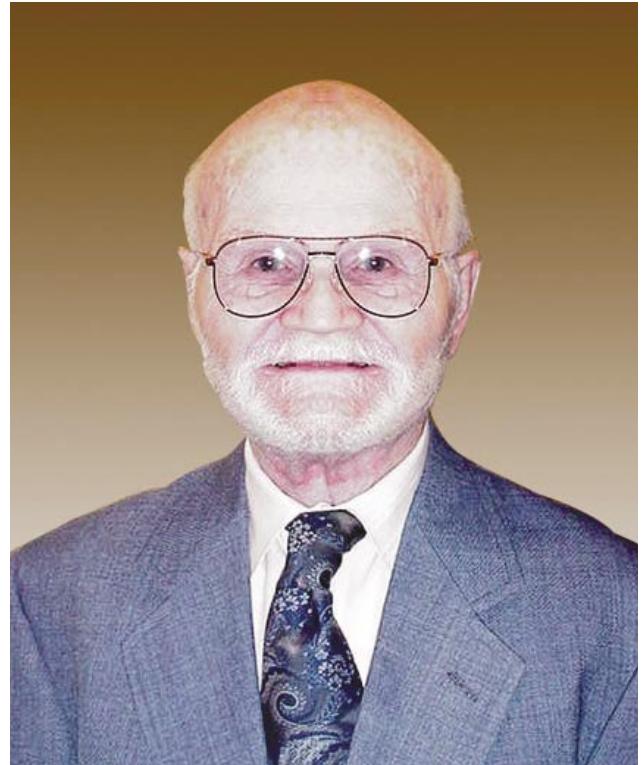


Trading Titans:

George Lane, 'Father of Stochastics'

Shares wisdom and anecdotes from 50 years of trading.

By Allen Sykora



George Lane recalls that early in his trading career, fundamentals did not seem very reliable when he was trying to decide which way a market might head. So he went to work studying technical indicators.

He eventually came upon the concept now known as Stochastics, which has become one of the most widely used oscillators for trading stocks, futures and options. It is used to measure the momentum of a move, so that traders might get a feel for when a market may be getting ready to turn around.

Stochastics became the backbone of Lane's trading after the concept was developed in the early 1950s, although he also looks at factors such as Elliott waves and Fibonacci levels. Although Lane has retired to the small community of Watseka, Ill., approximately 80 miles south of Chicago, he remains close to the markets. He

still spends his mornings trading and continues to offer a course on technical analysis.

Lane has been trading for roughly half a century. He is an outgoing man who can tell colorful stories of the past, such as when the daily range on a corn futures contract was around a half cent and a \$20 bill let somebody control 200,000 bushels of the grain.

Ten years as a floor broker

Lane worked as a floor broker for 10 years and is the former owner of the regional brokerage firm Miller, Lane & Co., which had 41 branch offices. He was a director of research for two other brokerages; author of four courses in commodities and one for the stock market; and spent years traveling around the country teaching farmers, ranchers and other producers how to hedge the risk of produc-

tion in the futures market.

More than anything, though, Lane is known as the "Father of Stochastics."

Stochastics is a momentum indicator meant to give traders a feel for when the market might be getting ready to change direction. A Stochastic reading of 80 indicates a market that is overbought while a reading of 20 indicates a market that is oversold.

"Stochastics is a momentum oscillator," said Lane. "It doesn't follow price, it doesn't follow volume or anything like that. It follows the speed or the momentum of price. As a rule, the momentum changes direction before price."

He made a comparison to a rocket speeding away from the Earth. Before the rocket can turn and head back to the ground again, it must first start to slow down.

"The slowdown of momentum

happens before the change of direction,” continued Lane. “It’s a leading indicator to the change in direction. That’s what Stochastics does. It predicts the direction of movement.

“It has turned out to be a very magnificent indicator. The darn thing works and is very reliable. You can use it on a three-minute chart – or you can use it on a daily or weekly chart.”

Stochastics originated years ago when Lane and several other traders at the MidAmerica Commodity Exchange would meet each night in an effort to come up with an indicator that would help them make their trading decisions.

“For some reason or another, most of the people in that group were Polish or Czechoslovakian,” recalled Lane. “One guy brought

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his grandfather, a Czech from the old country. He was watching us struggle. We had gone through the alphabet about twice on these indicators and hadn’t found anything that was outstanding. He

mentioned they had this formula in the old country for figuring out how much limestone to put in the mix to make steel.

“We took that formula, changed it and modified it and so forth – and ended up with Stochastics. It was reliable. We quit doing so much research and used the Stochastics to make decisions – and it worked out very nicely.

“I’ve never had to work in my entire life,” said Lane with a chuckle. “Stochastics has always provided me with a good income.”

It’s been so many years since Lane came upon Stochastics that he doesn’t recall the exact connection he discovered between a steel formula and the markets. He added that Stochastics was modified several times. “I rather doubt we kept the original formula, but we got started that way,” he commented.

Lane initially started trading on the side years ago, when he and his father were practicing medicine together in a clinic that was located in an industrial area of Chicago. The family decided to close the clinic when Lane’s father was ready to retire. Lane recalls going to talk with their broker about why they hadn’t been doing better in their trading.

“The brokerage office grabbed me,” he continued. “Someone said, ‘Say, young man, what are you doing?’ I said, ‘Well, I’m kind of between jobs now.’ He said, ‘How about if we send you to New York and make a broker out of you?’”

Lane became a stockbroker, but found that he was not particularly fond of the job.

“I was out having lunch one day away from the brokerage office,” he said. “I went into a

building to buy a cigar. And while I was at the counter, all heck broke out upstairs – screaming, yelling and so forth. I thought somebody was getting murdered or some-

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thing, so I ran upstairs to see what was happening.

“There were about 35 or 40 guys in a pit screaming and yelling. I had discovered the Chicago Open Board of Trade... I asked an old man what was going on. He said, ‘Come here, kid.’ He took me into an office and sold me a membership for \$25.”

Lane recalled that the range for the year on corn, the hottest commodity at the time, was around 12 cents.

“Margin was awful small because daily moves on commodities were about 3/8 to 5/8 of a cent. You could come in, throw [down] a \$20 bill – and go out and trade 200,000 bushels of corn. If it went up 1/4 or 3/8 of a cent, you did quite good.”

Corn: The hot commodity

Lane feels fortunate to have learned about markets at a time when “everything was quite simple,” before certain commodities – such as soybeans and pork bellies – were even traded. Since, markets have become much more volatile in general, prompting him to

comment: "I'm glad I don't have to start now."

Early in his career, Lane figured "there had to be something somewhere" to help him make trading decisions besides relying on funda-

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mental factors.

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Money management critical

Lane considers money-management to be critical for successful trading, especially when it comes to minimizing losses so they do not exceed the winning trades.

"We teach that when anybody enters a market, they should not be interested in how much money they're going to make. They should be more interested in how much they're going to lose. Most of the work we do in trading is to protect ourselves against losses.

Loss control essential

"The secret to making money in commodities is to control the size of your losses. You have no control over the number of times you have

a loss. But you do have control over the size of your losses. You can actually make a good living if you have more losses than wins, as long as you control the size of your losses."

Lane emphasized that every time he takes a position in stocks or futures, he places a stop-loss order. He won't use a "mental stop" because it's too tempting to move it.

He keeps his stops tight, commenting that he never takes a loss of more than \$175 on a bond futures contract. He places these stops on the basis of technical considerations – "where the market tells me I'm wrong" – rather than a dollar amount, however.

Suppose Lane is long and the market is climbing, pulls back and then climbs some more. Lane will move his stop up to the bottom of each of these pullbacks, sometimes raising his stops five or six times in a day.

Managing stocks

"I keep following up the market as it's going my way by bringing the stops up close," he continued. "So after a while, I can't lose because the stop is higher than where I got in. I'm forcing myself to take a profit.

"This is money-management – and the most important part of trading. Any fool can trade... but he's got to develop rules to protect himself against losses. There are lots of guys out there trading and making fabulous amounts of money, but they give so much of it back. You've got to have the attitude that once you've made money, they don't take any of it back.

"The greatest crime that an amateur can do is get in the market, make a profit, let the profit go

into a loss – and then finally get scared and get out. Don't ever let that happen!"

Lane also emphasized the importance of having the discipline to let a profit run rather than opting out of the market too quickly. He uses Elliott waves and Fibonacci levels to help him with this.

Bar charts and volume

In his trading, Lane watches bar charts and volume for an indicator of what is happening in a market. He uses Stochastics and Fibonacci retracements and trendlines, relying mainly on 38- or 40-period moving averages. While "not per-

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fect," these averages have "a high correlation of providing support to a bull market or resistance to a bear market," he said.

Lane offered the view that most of the numerous technical indicators available to the trading community nowadays are "workable." However, traders do not have time to follow too many at once, which is why he has narrowed those he uses down to a handful.

Lane looks for certain conditions before entering a trade, such

as double bottoms or double tops. "Volume is always heavy at the first bottom of a double bottom," he continued. "Volume is always light in the second bottom of a double bottom. You must never enter a market on heavy volume; you only enter on light volume – at a top or a bottom.

"Stochastics gives you convergence at the bottom or divergence at the top. And then there are chart patterns, such as closing price reversals. There are 10 variations on the buy side and 10 variations on the sell side."

Same indicators for futures and stocks

Lane uses the same indicators for futures and stocks, commenting, "We don't find any differences in them." He later added: "Charts are kind of silly things, at first, and complicated. But once you understand why they work and how they work, they are a wonderful tool."

Early in Lane's career, he began working for a school called Investment Educators, which was founded in 1948 by Ralph Dystant. When the owner had a heart attack, Lane taught the classes for six months. And when the owner came back, he taught the stock market courses while Lane taught the commodities courses. Lane took over the company when the owner later died.

Lane continues to run Investment Educators, possibly the oldest school in the country teaching technical analysis. He teaches along with his wife, Caire, herself a trader for roughly a quarter of a century. The school is described at

the Web site www.lanestochastics.com.

When asked about his hobbies, Lane chuckled and said he still likes to go to his home office to trade each morning, even though he's now in his 80s.

"I go down there most every morning by 7:00. I trade until about 11:30, then I go have lunch. Then I go take a nap... It's a very nice life."

He trades mostly the Treasury bond, S&P 500 and currency futures, but also dabbles in gold, silver and the grains.

Work with an older and more experienced trader

Lane advised new traders to develop a working relationship with an older, more-experienced trader, in order to avoid some of the pitfalls that otherwise await novices.

"Everybody who starts out in this business is fumbling around. They don't know what to hunt for, and they don't know what they've got when they get it. And, unfortunately, there is a lot of junk out there that is touted as the great answer. A lot of stuff will work for the guy who invented it, but it won't work for anybody else. They [beginners] have to avoid that, but they don't really know how.

"So I think the smartest thing for a learner is to find somebody who has been trading for years and take his advice. He has eliminated those dumb things people do in their trading, and he can help a heck of a lot.

"They're available. There are guys who would be tickled to death to help a young man get started."

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