

# Using Linear Regression To Profitably Trade Futures Markets

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The combination of Linear Regression Slope (LRS) and Shem's Curve™ is a dependable method to employ in daytrading. (Although the title of this article speaks to the futures markets, this method would apply equally well when trading FOREX and stocks.)

One of the keys to this method is LRS Turn-3™ (an idea which is credited to my friend Michael Coffin, CPO). LRS Turn-3 uses LRS, and two other major indicators. It gives a signal when they are all lined up in the same direction. Shem's Curve uses Linear Regression with new adaptations. (This, of course, is an over-simplification of everything these two indicators do.)

In this article we will focus on only two indicators: LRS Turn-3 and Shem's curve - which can be used to determine profitable trading patterns a high percentage of the time.

On the first chart below (showing the afternoon of 6-21-2006 in the S&P e-mini), you will notice there are only two indicators. (Although I certainly use more than 2 indicators in my day trading, the method under discussion here only uses these two.) The yellow line with the occasional yellow (bearish) or white (bullish) crosses is LRS Turn-3. The indicator showing a line with either a magenta (bearish) or cyan (bullish) color is Shem's Curve.

Brief description of these two powerful indicators:

- LRS Turn-3 will plot a + when the market changes direction, and will continue plotting a + as the underlying components of the indicator swing back (with retracement) and then realign themselves in the same direction again. The color of the + determines the direction of the market. During the course of a market move, this indicator will give an initial signal and then many other signals as the market moves. It may continue giving signals right up to the point just before the market reverses direction again. (For this reason it is not recommended to take a signal that is too many bars into a move, as the move may be almost over.)
- Shem's Curve (line) will turn to a bullish or bearish color as the market turns. It will maintain that color until there is retracement or a market reversal. (Like its counterpart LRS Turn-3, it is better to take a signal soon after it changes color.)



The first thing we notice in the chart (above) is that LRS Turn-3 gave its first bearish signal (after a series of bullish white crosses). This is the initial setup. (The “hammer” is cocked, and we wait to “pull the trigger.”) Now we wait. (Many traders would jump in short here, and feel the heat of a hot kitchen, while the market acts like it can’t make up its mind for the next 4 bars. This produces unnecessary stress). While we wait, we see other bearish indications:

- Two, consecutive, upper long-stemmed candlesticks.
- LRS (the yellow line in the LRS Turn-3 Indicator) turning visibly down.
- Another magenta + on LRS Turn-3.

Patience pays, as Beth (MTA’s talking, trading assistant) announces that Shem’s Curve turns down. (Like a human “trading assistant,” the My-Trading-Assistant indicators speak when something happens, ensuring the trader is aware of the signal. I cannot stress enough how important this is to me!) I entered short.

The LRS Turn-3/Shem's Curve combination happens frequently. Here is another illustration the very next day:



Notice that the down move (that started in the late afternoon on the prior day), continued into the next day and lasted all morning. In this case it was not prudent to use this method to go short, as the down move was well underway.

As we can see in the chart, just after lunch there was an LRS Turn-3 bullish signal. Shem's Curve, however, continued downward. Although the market showed two, consecutive, bullish bars (with the lower long-stems) indicating the down-move was probably over, we wait. (Those who entered [and there were many] on the long bullish green bar [same bar as the LRS Turn-3] took a lot of heat as the market made lower-lows over the next two bars.)

At 14:45 Beth announced Shem's Curve. I went long for 2 points.

*Only one trade today? Let's look at it like this: One trade, trading 10 ES contracts, for a 2 point profit, is \$1,000. Not a bad day! For those who are new to trading, I would recommend waiting each day until a high-probability trade like this presents itself. Trade once, bank your profits, and build your confidence as you build account equity.*

Here we have the next day (6-23-2006) in the afternoon. (Same market.)



In this case, both LRS Turn-3 and Shem's Curve turn down on the same bar. I entered short. I took 1.75 points of heat on this trade, but taking occasional heat is part of the trading business.

**A 15-minute time frame is the most effective for this method.**

In conclusion, [LRS Turn-3](#) and Shem's Curve are just two of the powerful indicators in the [My-Trading-Assistant](#) package that I have been using for many years. I would not trade without them.

About the Author:

David (Shem) Markowitz took his first daytrading course in the early 1990's, when he started day trading stocks. Shortly afterward he shifted his trading to the S&P 500 e-mini. His focus is on "pattern recognition." Over the years Shem was instrumental in several MTA indicator ideas, which also bear his name. Shem is the 3<sup>rd</sup> person you can see in this [video interview](#).