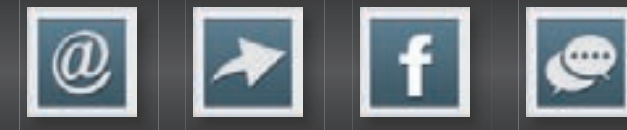


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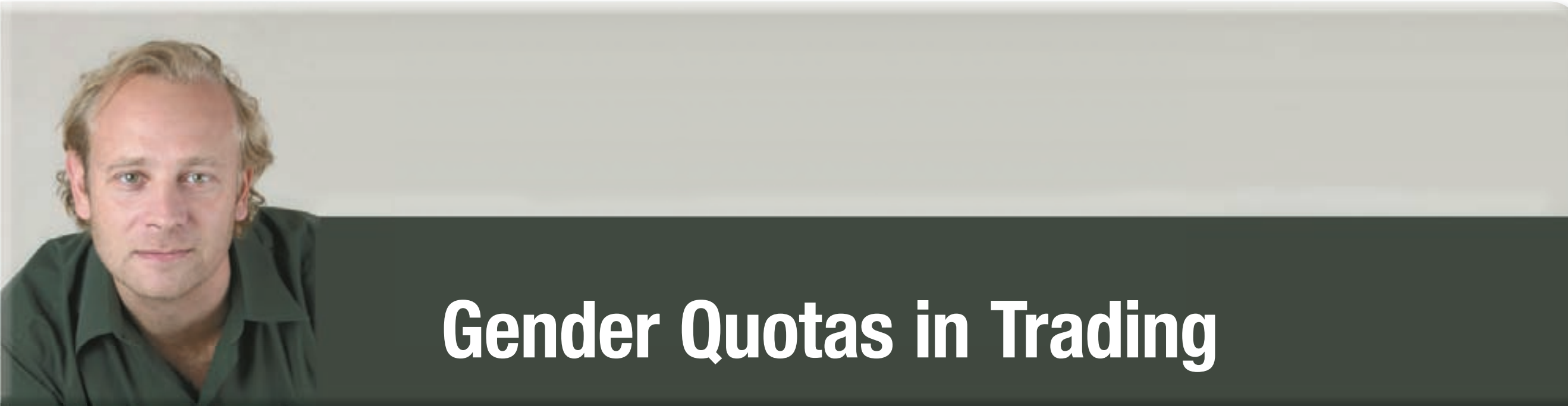
03

March 2011

Incredible Targets for Gold and Silver

Is History Going to Repeat Itself?

- »»» **ETF Swing Trading vs. Buy-and-Hold**
Who Will Be the Winner?
- »»» **Trading for Sure Profits**
One Way of Surviving All Market Conditions
- »»» **The Back-to-Basics Approach**
How Useful Is Fundamental Analysis?
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Gender Quotas in Trading

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In Germany today there is an active discussion being carried out in the political arena as to whether or not to implement affirmative action gender quotas for companies' executive leadership and board memberships in order to more fairly represent women. This is certainly not the first magazine to broach this subject. Have no fear, I do not wish to elaborate now on the pros and cons of such a quota in the executive suites of our beloved large corporations (and elsewhere). Nor do I want to discuss whether or not that might really be a good thing. As traders, you do not really care whether it is men or women that head the companies whose stock you happen to long or short at the moment. However, the idea has been floated by our politicians – who, as we know, would certainly make neither good traders nor responsible corporate executives. I am not trying to demean our well intended and

hard working politicians but rather would like to draw your attention to a different idea: How about a quota for women in trading?

There are some studies which suggest that on average, women are the better traders. Obviously, that is not because they have a “better crystal ball” for their predictions but because they arguably do not have the most problematic quality of men. The quality in question is overconfidence. I am sure that this quality ranks at the very top of the list of the most frequent reasons for an account being wiped out. It is not the market or bad luck that causes us to fail but our very own overconfidence.

Women simply are better “programmed” to avoid this behaviour and they trade in a risk-sensitive way, while men enjoy being determined now and then to show the market

who is calling the shots. Much in the same the way it was with the cavemen, men want to prove themselves in one way or another, where in contrast, when in doubt, women tend toward risk avoidance. This pattern can be found in statistics on successful trading, and supports the notion that, on average, women have a clear competitive advantage. Of course, this is not a reason to introduce women's affirmative action, but it may help you to stop and reflect the next time you “fight the market”.

Good Trading,

Lothar Albert



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COVERSTORY

6 Incredible Targets for Gold and Silver
In this issue's coverstory we present an interesting analysis of the precious metals gold and silver. The bottom line is that gold may go to 15,000 dollars an ounce and silver to 1500 – if and only if history repeats.

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Our magazine has established itself as a source for information and communication for elite traders in Germany, Europe and around the world. Current information about technical, mathematical and psychological aspects of the markets is discussed in professional articles and interviews. Each issue contains articles about trading strategies (for basic, intermediate, and advanced traders), risk management, technology for traders, business issues for traders, book and website reviews, and much more!

Still today, the trader-elite are interested in professional and current trading knowledge and experience. For dedicated traders, there is no need for buy and sell recommendations. Trading pros make their decisions with self-confidence and are self-contained. These people know that trading can be profitable in bull and bear markets. The question is: what are the markets and tools that lead to success? TRADERS' magazine addresses this question every month in several languages.



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Is History Going to Repeat Itself?

Incredible Targets for Gold and Silver

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When reading this headline, long-time readers of TRADERS' might wonder whether we have given up our neutrality now and have stooped to giving hot tips and targets. Do not worry, we have not. All we do in this issue's cover story is present an interesting analysis of the precious metals gold and silver – and this analysis packs a powerful punch as you will notice when reading the story. Besides, we will be contributing to settling the constant arguments on how much more prices of the two precious metals can still rise. After all, as you will see, the answer to that question can be found by raising a simple short question in return: Is history going to repeat itself?





Marko Graenitz

Marko studied Business Administration with Majors in Finance and Controlling. He is a freelance editor and financial journalist. He is also planning his Doctoral dissertation in the field of momentum trading. Momentum is one of the few methods scientifically proven to deliver above-average returns. Contact: momentum.trading@web.de

In the last few years we have experienced a historic revival. The markets have been surprised by the comeback of the price of gold which had been drifting downwards for some 20 years after the rally until 1980 and had not even managed to elicit a weary smile from most investors. The upward trend of some ten years can be described as slow and unimpressive at first but then it became more dynamic and actually exploded last year. The chart with the three phases and ascending lines can be found in Figure 1. Of course, on its way there that precious metal was followed in its wake by an old acquaintance: silver.

What is interesting is the multi-year formation that ultimately turned out to be an upward trend reversal: a huge Cup&Handle pattern (see Figure 2). Truly good examples are rather rare in practice. In the case of gold, the formation has evolved over a period of many years. The upward breakout from the pattern caused the long-term trend reversal to be confirmed.

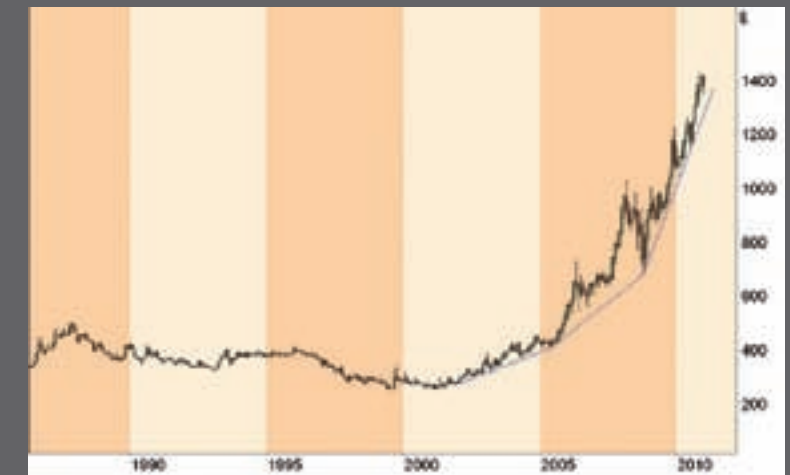
How High Can It Go?

It might be best to start with the results. Let it be said at first that the seemingly reckless projection was and is being made public in a similar fashion by Michael (Mike for short) Maloney, founder of the www.GoldSilver.com website and author of "Guide to Investing in Gold and Silver". He expects the price of one troy ounce of gold to be capable of soaring to up to 15,000 dollars in a few years' time. He made this prediction as early as 2008 at which time he was not being taken overly seriously. Meanwhile, though, public perception does seem to have changed somewhat although the \$15,000 mark continues to be a long way off. Based on a recent price of gold at 1400 dollars, a rise of nearly 1000 per cent would be necessary to make Maloney's prediction come true.

That Was Not All Yet

And Mike Maloney does not stop there. Buoyed by the mega bull market, the price of a troy ounce of silver might soar to an extreme

F1) Gold 1986-2011



The long-term monthly chart of gold is a good illustration of how the upward trend has become increasingly steep. The current "hot phase" started in 2008 when the Lehman bust caused vast amounts of liquidity to be pumped into the market. Later there was another round of quantitative easing by the Fed buying up government bonds which continues to this day. Obviously, this flexibility on the part of the central banks also has major benefits: During the Great Depression the gold-backed system made it impossible to quickly and considerably increase money supply – and we all know what that led to.

Source: www.tradesignalonline.com

F2) Cup&Handle Pattern with Gold



Here you can see a truly huge Cup&Handle pattern formed by the long-term trend reversal of gold. There are two interpretations: (1) from 1996 to late 2004 (black line) with 2004 being the "handle", and (2) from 1997 to late 2003 (blue line) with 2003 representing the "handle".

Source: www.tradesignalonline.com

of 1500 dollars. Phew, take a deep breath first. Exactly, that is not 150 dollars, which is still remotely imaginable – but that is one thousand five hundred dollars. This scenario would even be beyond the imagination of the most convinced silver advocate.

However, Mike Maloney is not just any old fool pulling his numbers out of a hat. He has a plausible explanation essentially based on a fundamental assumption that ought to be well known not only to most traders but also to long-term investors: “History repeats itself.” Or, as Mark Twain (1835-1910) put it: “History does not repeat itself but it does rhyme.”

The Fundamentals

Essentially, the prediction of the price of gold is based on the observation that over the long term, the price of gold and the money supply are related to one another. Historically, whenever there was an extensive production of paper money (US dollars), this was followed by the price of gold going through the roof – in theory until all the dollars issued were backed by gold reserves. And in practice partly even beyond that, as we will see later.

In the gold-standard era, the dollars ought to be covered by gold anyway – which obviously

was not always the case in practice, leading time and again to (more or less voluntary) adjustments.

Today we have a fiat-money system essentially based on trust – a trust that in times of a large and fast rising national debt or during periods of high inflation rates, is quickly shaken. This means that in the long term our monetary system is not immune from a breakdown and not half as robust as we would like to think it is.

Money Supply

The connection between the price of gold and the money supply refers to the long-term time horizon or rather to the extremely long-term horizon. After all, as can be seen in Figure 3 the growth rates of gold are by no means always in sync with the growth of the money supply.

Basically, there are four different definitions of money supply ranging from a very “narrow” to a “broad” interpretation of money (depending on the country and central bank, the definitions differ slightly):

- M0:** actual existing cash
- M1:** circulating cash + sight deposits
- M2:** M1 + savings, money-market funds
- M3:** M2 + longer-term deposits

Since 2006, the M3 aggregate money supply has no longer been made public by the Fed. You can imagine that speculation has been rampant among gold and silver adherents on why the Fed discontinued its publication.

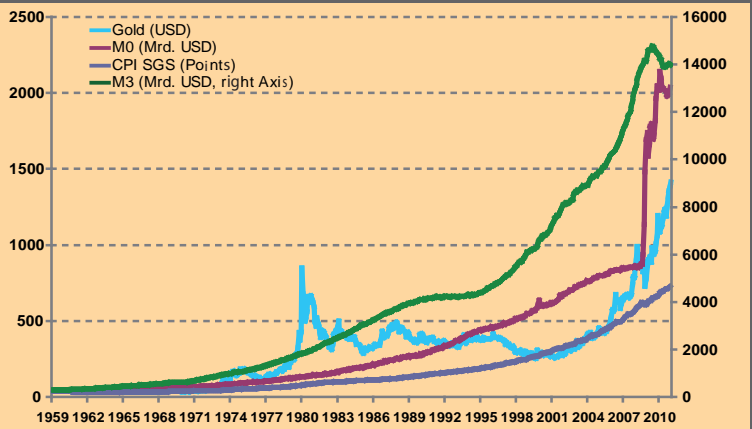
However, it is possible to do a pretty good approximation of M3. For one, a projection can be made of the data on the basis of the development of M2, which is somewhat imprecise but essentially provides a good estimate. For another, ShadowStats (www.shadowstats.com) publishes a time series for M3, starting with the Fed’s discontinuation of the publication on 23rd March 2006.

In Figure 3 you can see the price of gold, the M0 and M3 money supply as well as the consumer-price index (CPI), each since 1959.

Gold Reserves

To conduct a precise analysis, the gold reserves should be included. Not much has happened with the reserves in the US in the last few decades – the last major sales happened in the 1970s. At nearly 80 per cent, the US holds most of the gold reserves worldwide. However, changes did occur in other places: For example, the International Monetary Fund (IMF) as well as Switzerland reduced their gold stocks while

F3) Gold, Money Supply, and Inflation



Here you can see a comparison of the gold chart (in nominal dollars), the M0 and M3 aggregate money supply (in billion dollars each) as well as inflation rates (based on the “true” consumer price index (CPI)). In the case of the CPI, the official calculation is often questioned because of its underestimated inflation record. It can be seen clearly how money supply has continued to rise after 1980 while gold took almost a 20-year break. The alternative CPI as well as the M3 money supply (since March 2006) are shown according to the figures from Shadow Government Statistics (SGS). Nominally, M0 money supply is much lower than M3 (right-hand scale), but has grown significantly faster especially in 2008.

Source: Fed of St Louis, Shadow Government Statistics, Bureau of Labor Statistics, Bloomberg (gold), www.Markt-Daten.de

countries such as China, Russia, and India purchased gold. In 1980 the U.S. held nearly as much gold as it does today. Specifically, this amounts to 8221.20 tons according to Wikipedia, compared to 8133.50 tons in 2010.

Gold Extrapolation – Part 1

Based on the gold reserves mentioned, an interesting calculation can be made. The purpose of the exercise is to answer the following question: “Where would the price of gold be today if the supply of US dollars were completely backed by gold?”

M0 money supply can be obtained from the Federal Reserve Bank of St Louis by entering the key word “monetary base”. As of 1st December 2010, this figure amounted to a cool 2.039 trillion dollars. While this sounds like an awful lot of money, it is hard to fathom such a number. So we need a reference value – the gold reserves. One troy ounce of gold weighs 31.1 grams. Since the gold reserves held by the US amount to 8,133.50 tons, we need to convert this figure first into troy ounces:

$$8,133,500 \text{ kg} / 0.0311 \text{ kg} = 261.527 \text{ million troy ounces}$$

This easily leads to the next step. We simply divide the money supply by the amount of troy ounces in the gold reserves:

$$2,039,000,000,000 \text{ USD} / 261,527,000 \text{ troy ounces} = 7796.52 \text{ USD} / \text{troy ounce}$$

If your pocket calculator has any problems handling the number of digits, just leave out the final three zeroes. The result will then be the same – gold would have to be at about 7800 dollars for the money supply to be covered by the gold reserves!

The best thing about this is that we have arrived at this figure

without engaging in any hocus-pocus. Feel free to do the maths yourself. All you need to do is to get the numbers from Wikipedia and the Fed of St Louis, and then do two divisions using your calculator.

Gold Extrapolation – Part 2

Now that you have read Part 1 of the extrapolation, you will no doubt be anxious to hear about Part 2. After all, 7800 is only about half of 15,000. As mentioned before, the US had gold reserves amounting to 8221.20 tons in 1980. On 21st January 1980 the price of gold reached a high of 850 dollars.

What is so exciting about this is revealed by the third number: in January 1980 the money supply amounted to a “mere” 133.425 billion US dollars. Let us do the maths again:

$$8,221,200 \text{ kg} / 0.0311 \text{ kg} = 264.347 \text{ million troy ounces}$$

$$133,425,000,000 \text{ USD} / 264,347,000 \text{ troy ounces} = 504.73 \text{ USD} / \text{troy ounce}$$

So at this point in time a full gold backing would have required a gold price of some 500 dollars. However, gold had shot up to 850 dollars, which means that it had

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gone nearly 70 per cent “too far”.
 $850 \text{ USD} / 504.73 \text{ USD} = 1.6841$
 $= 168.41 \text{ per cent}$

Overshooting is nothing new on financial markets, but in the case of gold this is only fully revealed by our calculations.

The final step is simple: We add this overshoot to the calculated price of gold in order to determine the same backing for today’s US dollar supply:

$7796.52 \text{ USD} \times 168.41 \text{ per cent} = 13,130.12 \text{ USD}$

If we now also factor in that on 21st January gold reached an intraday high of 873 dollars (72.96 per cent overshooting) at the New York Commodity Exchange (COMEX), we arrive at the amount of 13,485 dollars in our calculation.

The Overall Calculation

Besides the M0 money supply, Mike Maloney includes in his projection the outstanding revolving credit which equals money creation and raises all the numbers yet again. This data can also be accessed from the Fed of St Louis, and Mike Maloney’s corresponding chart can be seen in Figure 4.

In late November 2010 that credit had a volume of 805.5 billion US dollars while in January 1980 the figure was 56.2 billion

dollars. If we add each of these figures to the M0 money supply, the 2010 calculation looks like this:

$2,844,500,000,000 \text{ USD} / 261,527,000 \text{ troy ounces} = 10,876.51 \text{ USD} / \text{troy ounce}$

And for 1980:

$189,625,000,000 \text{ USD} / 264,347,000 \text{ troy ounces} = 717.33 \text{ USD} / \text{troy ounce}$

Factoring in the appropriately adjusted 1980 maximum overshoot (873 / 717.33) of 21.7 per cent, this makes:

$10,876.51 \text{ USD} \times 121.7 \text{ per cent} = 13,236.71 \text{ USD}$

Other Determinants

In addition to the calculations, it is worth mentioning that the money supply charts are anything but falling – there may be more to be added. Altogether, our projections will be approaching the 15,000 mark predicted in Mike Maloney’s scenario, and we can say that this is quite a plausible explanation.

Another way of extrapolating targets for gold and silver is by looking at the Dow/gold ratio (Figure 5). If we use historical data here, we will arrive at similar results. Conversely, the Dow or all

the stock markets might also fall quite markedly. However, this is contradicted by the money supply argument that has highly diluted the value of the dollar. Besides, there is no doubt that every possible risk would be taken by policymakers to rescue the stock market (ample proof of this is provided by the current monetary policy).

Will Gold Really Climb that High?

After all these calculations you might wonder why gold has not been quoted much higher considerably longer. After all, such a process of adjustment cannot drag on forever since the data is known and also is freely available.

The answer to that is that we do not have a gold-backed currency today. Nobody can tell you whether this system will be resurrected. Should our fiat-money system continue to exist – i.e. no extremely high inflation, rising interest rates, and a complete return of confidence in paper money, then prospects for gold would unfortunately be bleak – unless everybody suddenly started to buy jewellery (by the way, the jewellery industry rather than central banks is the biggest player on the gold market today). Although the explanation described is plausible, that does not mean that it will become

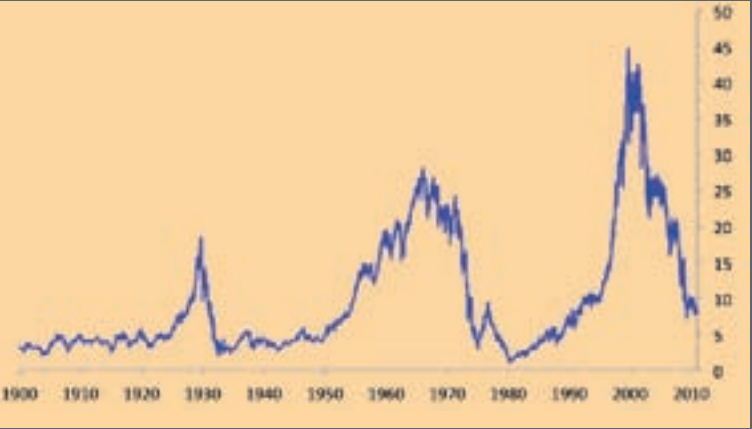
F4) Base Money & Outstanding Revolving Credit



This chart of Mike Maloney’s shows the development of the gold price (without axis), of the M0 money supply as well as of the sum total of the M0 money supply and all the outstanding revolving credit.

Source: www.goldsilver.com

F5) Dow/Gold Ratio



A good illustration of how the Dow/gold ratio has fallen since 2001. Over the decades, a value of 1.0 formed as a lower limit. Neither at the low point after the Great Depression of the early 1930s nor at the high point of the 1979/80 gold boom was the Dow Jones/gold ratio any lower than 1:1. Up to the year 2000 it soared with maximum values reaching more than 1:40. Compared to stocks, gold was valued as low as it had ever been – conversely, stocks were more expensive than ever before. In other words: There was an undervaluation bubble in gold. Assuming – in theory – a 1:1 ratio today, the Dow Jones would either have to fall to 1400 or gold would have to rise to 11,500 dollars. Mike Maloney expects a target ratio of 2:1, i.e. stronger movements still to come.

Source: www.goldsilver.com

reality. This will depend on whether history repeats itself and if so, to what extent.

Obviously, the entire analysis is also dependent on the currency. The analysis presented here only refers to the US and the US Dollar. If gold and silver reach extreme prices, exchange rates will certainly be in turmoil. In any event, what is interesting today is that gold has markedly gone up in all major currencies – a clear sign of the loss of confidence in all fiat-money currencies and hence not a phenomenon exclusively related to the dollar.

Silver Extrapolation

So much then for the reasons for the possible price of 15,000 dollars for a troy ounce of gold.

But how can a price of 1500 dollars for a troy ounce of silver possibly ever be reached?

Again, historical comparisons will help – albeit comparisons of a somewhat different kind. During the precious-metal bull market up to 1980, an approximate gold/silver ratio of 1:16 was reached. Subsequently, the ratio again rose markedly, even briefly hitting the 1:100 mark in early 1991.

Charts actually do exist that show the gold-silver ratio over the last 5000 years. Certainly, these

lack precision since you only have one data point for each aeon – but they interesting. After all, over a period of 5000 years the average gold-silver ratio stood at about 15, in particular as late as the 18th and 19th centuries (in the U.S., the legally prescribed rate of exchange of gold to silver was 1:16 for a while). Not until the 20th century did silver become significantly cheaper due to the discovery of major deposits.

So based on a gold-silver ratio of between 1:15 and 1:100,

“Gold and silver have become more interesting to traders.”

the price of silver ought to be between 150 and 1000 dollars – assuming that the \$15,000 price of gold was actually reached.

Assuming a short-term overshooting of the ratio to 1:10 in favour of silver – as does Maloney –, this would result in a price of 1500 dollars for a troy ounce of silver. Maloney himself is not saying that this scenario “must” materialise – and even if it did, that would probably be only a short-lived extreme price.

In Table 1 you can see a few sample calculations using

different ratios that lead to partly extreme scenarios.

Trading and Investing

Gold and silver have become more interesting to traders in recent years since more often than not, there have been major ranges of movement. Basically, you can observe especially in strengthening trends that these phases are developing more frequently and are following a more extreme path. By way of comparison, the development of the prices of gold and silver during the last bubble (lasting until 1980) is cited here. But in other asset categories, too, the largest and fastest movements occur towards the end of long-term trends.

The best example of this is the New Economy stock bubble that lasted until 2000.

However, the increasing dynamism may be bad for investors – especially when they are not positioned yet. By now, the price of gold and silver has already gone up markedly. Those who do not trust any projections (but do believe in the continued existence of our fiat-money system), will find it difficult to enter in a big way at this stage. Long-term investors have the basic problem of recognising

Info

By the way, Warren Buffett is no big fan of gold. When asked in a Fortune Magazine interview in 2009 what he thought of gold, he answered as follows: “You could take all the gold that has ever been mined, and it would fill a cube 67 feet in each direction. For what that is worth at current gold prices, you could buy all – not some – all of the farmland of the United States. Plus, you could buy ten Exxon Mobils, plus have \$1 trillion of walking-around money. Or you could have a big cube of metal. Which would you take? Which is going to produce more value?”

T1) Ratios and Targets

			Scenario Extrapolation		
Timeframe	Dow/Gold-Ratio	Gold/Silver-Ratio	Dow	Gold	Silver
January 2011	8,6:1	47:1	12,000	1400	30
1999-2001	40:1	60:1	9000	225	3.75
			12,000	300	5
			18,000	450	7.5
1990-1991	7:1	100:1	9000	1285	12.85
			12,000	1715	17.15
			18,000	2570	25.7
1980	1:1	16:1	9000	9000	560
			12,000	12000	750
			18,000	18000	1125
Extreme	1:2	10:1	9000	18,000	1800
Assumption			12,000	24,000	2400
			18,000	36,000	3600

Here is an overview of the actual ratios at various points in time in the past and the resulting (theoretical) gold and silver targets for today. Each is based on three different Dow index levels. Example: Assuming the Dow Jones is at 18,000 points today and the ratios correspond to the historical model of 1990-1991, gold would be quoted at 2570 dollars and silver at 25.70 dollars. The latter ratios are based on Mike Maloney's assumptions about the extreme case. As can be seen, the question as to where gold prices are going can be answered by another question about our assumptions: “Is history going to repeat itself? And if so, which scenario is the most likely one?”

the major trends early and really sticking to them long enough. For example, in 1997 Warren Buffett bought some 130 million troy ounces of silver, portions of which he sold again in 1998. However, he most likely kept most of it until 2006 – but even this exit turned out to be too soon. He himself is said to have joked about it : “I bought early and sold early. Apart from that, it was perfect.”

Investors may find that a long-term investment in physical precious metals can easily backfire. After all, not only do gold and silver not pay any dividends, but on top of that they also cause storage costs. In the

course of a few years, this can quickly outweigh a good price development, especially when compared to stocks and bonds.

Physical Investments Should Be Given Preference

Investors who decide in favour of gold and/or silver should make sure that they make physical investments – despite the storage costs. In case there really is a currency reform, national bankruptcy or the like, a precious-metal derivative may soon be worthless – either because there is no issuer any more or because the currency quite simply is worthless.

To avoid paying the storage costs amounting, as a rule, to roughly one per cent, you may, of course, store your bars or coins at home in your basement or bury them at night in your garden next to the fish pond. In that case, though, it might be best not to tell your neighbour about the location of your treasure. Otherwise you will have a problem of trust again, but one that is different from the one you have with our paper money.

VAT may be a drawback that is frequently overlooked. In the case of Germany, this amounts to 19 per cent for silver bars and 7 per cent for silver coins. In Germany, that tax does not apply to gold.

You may get around the tax problem by using Switzerland or Liechtenstein as a safe haven, but you would do well to see a bona fide tax consultant first.

Conclusion

The future is traded on the markets – with uncertainty over the future development of currencies and prices being a necessary by-product. So no matter how long our discussions may go on, in the end we will just have to make assumptions about the future. Under these circumstances, the assumption that the past might be repeated in a similar fashion is entirely

plausible. The driving force that makes such extremes possible in the first place, is a fiat-money system’s virtually unlimited potential to create money – and that is the system we have today. So if you believe that we will actually come close to the ratios of 1979/80, then you now know what to do.

As I said, the whole issue can be reduced to one single question: Is history going to repeat itself? Or will “everything be different” this time around?



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Interview with Mike Maloney

Incredible Targets for Gold and Silver

.....

In this month's coverstory we report and evaluate Mike Maloney's forecasts and insights regarding gold and silver. If history repeats itself, enormous gains in both metals are possible. As this topic is currently of interest to traders and investors alike, we put a few questions to Mr. Maloney regarding his predictions and philosophy.

Please could you briefly explain why the monetary base and the price of gold are interrelated?
Mike Maloney: The monetary base is cash in circulation (paper dollars), plus deposits that the commercial banks have at the Federal Reserve, which are redeemable in paper dollars. So base money is just a measurement of how many paper dollars exist.
In my book, "Guide to Investing in Gold and Silver," I show that

before the Federal Reserve was created, each U.S. Treasury note (paper dollar) was fully backed by gold or silver. Then when the Federal Reserve Act was passed in 1913, the dollar was only required to be 40 per cent backed by gold. This allowed deficit spending for WWI and the accompanying increase of the currency supply. Then in 1934 the U.S. dollar was devalued 41 per cent when the price of gold was

changed from \$20.67 per ounce to \$35 per ounce. In doing so the value of the gold held at the Treasury rose to match the total value of base money.
Then the currency supply was once again inflated to fund WWII, Korea, Vietnam, and President Lyndon B. Johnson's social programs. When President Nixon severed the link between the U.S. dollar and gold, the will of the public and the free market bid the

price of gold up until, in 1980, the value of the gold held at the U.S. Treasury exceeded the value of base money.
We have no empirical data before the establishment of the Federal Reserve, but it appears that gold has been doing this accounting, time after time, for the last 2400 years. I believe that gold will continue to rise in price until, once again; the value of the gold held at the Treasury meets or exceeds the value of base money. If this happens it will be nothing unusual... It will just be history repeating itself. When you look at the relationship between gold and the circulating currency media over long periods of time, they do not just appear to be interrelated, they appear to be conjoined. Two sides of the same coin, so to speak.

Fiat money is said to be backed by the strength of the economy and the taxpayer – do you think these facts still influence the amount of trust people put into the US Dollar?
Mike Maloney: No, Yes and Yes! No, because right now 99.9 per cent of the world's population does not have a clue. They do not know that the only thing that backs all currencies (including the U.S. dollar) is debt and the solemn promise of all governments to tax their citizens in the future to pay that debt. In

the United States this promise is called a Treasury bond.
Yes, because in the future everyone will know this. Right now people are becoming educated faster, and information is spreading more quickly than at any time in history.
And yes because, in the near future, these facts will affect people's faith in all currencies, especially the U.S. dollar. If the future economy is bad, those debts become difficult, if not impossible, to pay. If you look beneath the surface, the strength of the U.S. economy and the financial position of the U.S. taxpayer look shakier than ever. The U.S. national debt is \$127,000 per taxpayer, and when you add in consumer debt, mortgage debt, and credit card debt, we get over \$500,000 in debt for each taxpayer. If you throw in the United States' unfunded liabilities, such as Social Security and Medicare, you would get over \$1 million in debt per taxpayer. None of these numbers is sustainable, especially when there are 26 million people in the U.S. who are unemployed or underemployed.

Why do you use base money plus outstanding revolving credit as a measure? What about aggregates such as M1, M2 or M3?
Mike Maloney: Outstanding revolving credit is mostly unpaid

credit card balances. When you make a charge, currency is created and that currency stays in circulation until you pay off your credit card debt.

Earlier I said that in 1980 the value of the gold held at the U.S. Treasury exceeded the value of base money. Well, not only did it exceed the value of base money, it exceeded the value of base money plus outstanding revolving credit as well. In many ways credit cards are replacing cash as a medium of exchange, so I use them both because we are trying to find a measure of the total cash, and its digital equivalent, in our monetary system. If history repeats, the gold price will be bid up until the value of the gold at the Treasury is once again in equilibrium with the value of the circulating medium.

However, if credit cards were to completely replace cash, and if outstanding revolving credit is not included in this calculation, then the predicted gold price is zero. I might be wrong, but I think that is just a little bit on the low side.

M1, M2, and M3 include a lot of factors like time deposits, money markets, and repurchase agreements, that I would not consider to be cash equivalents. But if the dollar actually failed, as all fiat currencies have, then by definition the corresponding price would be infinite dollars... and that is a whole lot bigger than M3!

Do you think there will be a food crisis following extreme prices in soft commodities?

Mike Maloney: Yes. If you look at Tunisia, we have already had a food crises – and it looks like they could spread quickly. Tunisia is in the top half of GDP per capita among the nations of the world, which means it is not a dirt-poor country. This shows how rising food prices and economic disaster can stir up riots and revolution – even outside the poorest countries. While there have been weather and natural factors driving up the rising prices of food, government policy should shoulder most of the blame. Through decades of currency creation, they have driven food prices to their highest nominal prices in human history.

Do you think there is a danger of currency wars or real wars following the rise of the price of gold and/or the devaluation of the US-Dollar? Is it not the case that other countries are facing similar problems and influence the adjustment process?

Mike Maloney: There is a currency war going on right now, and it has been happening for

some time. Every country wants a weaker currency because a weaker currency helps their exports and GDP figures. It is political death to have a strengthening national currency in a world of fiat currency debasement.

There remains a serious looming threat of national protectionism with possible showdowns between western and eastern blocs. It almost

“There is no national currency that I trust as much as I trust my gold and silver, period.”

looks as though the first currency regime to establish gold again as its anchor may become the world's reserve currency, as the world will flock to stability that only gold can provide – as has happened repeatedly throughout history.

With regard to real war, there is always that potential. But if you think about it, the fiat currency system is what has allowed governments to become involved in prolonged wars in the first place. If governments were

forced to use the money that the free market has chosen time after time without exception, gold and silver, then their ability to become involved in wars would be severely limited.

What would you suggest people should invest in? What about mixing physical gold and/or silver with assets denominated in the strongest currencies available (like the Swiss Franc)? What about real estate and/or farmland?

Mike Maloney: Personally, precious metals have been my only investment for some time. Gold and silver have been rising against all national currencies since 2005. There is no national currency that I trust as much as I trust my gold and silver, period.

With regards to real estate, I believe there is a short-term deflation coming. We are in a credit bubble. All bubbles pop. If you own your real estate outright then you are in great shape, but if you are too highly leveraged you could be wiped out.

However, over the long-term inflation is inevitable; the more currency that is floating around, the higher the prices of precious metals. That is because

throughout history, every time a nation has debased and finally destroyed its currency, the free market has chosen gold and silver as the ideal money. But the massive expansion of currency supplies around the world has created ripe conditions for a currency crisis of massive proportions. Ultimately, gold will not only benefit from the massive expansion of the currency supply, but it will also benefit from the global currency crisis that lies in wait.

During these crises, it is nearly certain that holders of precious metals will be the beneficiaries of the wealth transfer that will occur as the entire globe rushes into the safe-haven asset. This is going to be a completely different type of bull market, because you will get the buyers who are looking for opportunity, but you will also get people just panicking to salvage some of their wealth. It is a once in a lifetime opportunity that will benefit from both fear and greed at the same time.

In fact, I believe it is the greatest opportunity in history. Gold and silver rising in value against fiat currencies is inevitable.

As I said in my book... “It is as certain as the sunrise.”



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On 8th and 9th of April 2011, the 8th Middle East Forex Trading Expo & Conference will take place in Jumeirah Emirates Towers Hotel, Dubai. This two day event combines exhibitions, keynote talks, presentations and breakout

networking sessions highlighting the latest trends and developments across the vast online trading community. The 8th Middle East Forex Trading Expo and Conference aims to provide individuals, retail and institutional investors, and professionals, with the latest trading techniques, new trading tools and signals available, and to choose among trusted brokers who will help them improve their trading habits and to grow their investment portfolio as well as achieve short and long term trading objectives. For more information, visit www.meforexexpo.com



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Three in Ten Americans Commit Financial Infidelity?

Three in ten Americans commit "financial infidelity" by lying to their spouses about money, sometimes suffering consequences such as separation or divorce, according to a new survey. The Harris Interactive online poll of 2,019 adults showed 31 per cent of American couples who have combined finances were not truthful about issues such as hiding cash or a bank account or about debt or earnings.

"Financial infidelity may be the new normal," said Forbes.com, which commissioned the survey with the National Endowment for Financial Education. One-third of respondents also say they have been deceived, and both sexes lie to their partners about money in equal numbers. "These indiscretions cause significant damage to the relationship," said Ted Beck, chief executive of the National Endowment for Financial Education.

16 per cent of couples affected by financial infidelity said the deception led to a divorce and eleven per cent said it caused a separation. 67 per cent said it led to an argument and for 42 per cent it lessened trust in the relationship. (Reporting by Daniel Trotta; editing by Patricia Reaney)



Source: <http://news.yahoo.com>



Wall Street Bankers Earn More than Ever

Less than three years after the financial sector was brought to the brink of collapse, bankers on Wall Street are once again making more money than ever. The 25 largest financial firms paid their employees a record total of 135 billion dollars last year, up six per cent from 2009, The Wall Street Journal reported. Salaries and bonuses had fallen to 112 billion dollars in 2008. About one third of financial firms' revenues went into worker earnings. The average Wall Street banker enjoyed earnings of 141,000 dollars, up three per cent. Part of the expansion came from firms hiring new workers as the US financial sector has stabilised. The salaries varied widely – from an average of 431,000

dollars for Goldman Sachs employees to 257,000 dollars at rival Morgan Stanley.

In response to the public outcry that reached its peak during the 2008 financial crisis, many Wall Street bankers are getting money through fixed salaries and long-term stock options that link them to the financial future of the firm, instead of lavish bonuses. The move is aimed at curbing some of the excessive risk taking that was blamed for the financial crisis, which reached a fever pitch with the collapse of Lehman Brothers in September 2008.

Source: www.earthtimes.org



ICE Launching 26 New Energy OTC Contracts

IntercontinentalExchange (NYSE: ICE), a leading operator of global regulated futures exchanges, clearing houses and over-the-counter (OTC) markets, announced the launch of 21 newly cleared OTC energy contracts for global oil and refined petroleum products, North American power and North American natural gas.

ICE also announced the introduction on ICE Futures Europe of three new U.S. thermal coal futures contracts settled against daily assessments published in Platts Coal Trader: Central Appalachian Coal (UCA), CSX Coal (UCX) and Powder River Basin Coal (UCP). Platts is a leading global energy

and information provider and a division of The McGraw-Hill Companies.

With coal accounting for around 45% of electric power generated in the United States, the new contracts complement the existing suite of U.S. energy products listed on ICE, while also expanding ICE's market-leading suite of international coal products in an increasingly inter-connected global coal market. A full list of OTC, futures and options contracts and all specification are available at www.theice.com.

Source: www.theice.com

SEC releases 'Shadow NAV' Information to Public

The Securities and Exchange Commission announced that investors can for the first time access detailed information that money market funds file with the Commission – including information about a fund's investments and the market-based price of its portfolio known as its „shadow NAV“ (net asset value) or mark-to-market valuation. The information is available on the SEC's website and will be updated monthly. As part of its overhaul of money market fund regulation, the Commission last year adopted a rule requiring money market funds to file information about their holdings and portfolio valuations.

Funds began filing the information on the SEC's new Form N-MFP in December. Under the rule, the SEC will release the information with a 60-day delay. The rule also requires money market funds to post more current but less detailed portfolio information on their own websites within five business days after the end of the month. The information on the SEC website is available through the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system. The information can be retrieved in several ways, including by typing in the fund's name or ticker symbol or by reviewing recent Form N-MFP filings.

Source: www.sec.gov

Asian Exchange Will Implement Pre-trade Risk Controls

Singapore Exchange (SGX) will be introducing pre-trade risk controls to strengthen the marketplace with increased opportunities for direct access to the exchange network. The risk controls will be implemented in the SGX derivatives market by the third quarter of 2011.

Customers of SGX Clearing Members currently connect their trading systems to their Clearing Member's risk management systems for pre-trade risk checks. With SGX pre-trade risk controls, customers can now connect their order management systems directly to SGX's trading engine.

This will help customers reduce infrastructure development costs and speed up time-to-market. Clearing Members will work with their customers to set trading limits. SGX will be the first exchange in Asia to offer such a service to the trading community. SGX continuously reviews its trading rules to cater to the diversity in market participants including algorithmic and high frequency traders. To refer to the FIA Market Access Risk Management Recommendations, please visit: <http://www.futuresindustry.org/electronic-trading-and-order-routing.asp>

Source: www.sgx.com

Berkshire Could Pay Dividend in Next 12-18 Months

Warren Buffett's Berkshire Hathaway (BRKa.N) could pay a dividend in the next 12 to 18 months, according to a report in the January 24 issue of Barron's. Berkshire had \$30 billion in cash in its insurance units as of September 30. It could have nearly \$50 billion by year end, according to the report. Berkshire's operating profit after taxes is on track for a record \$12 billion to \$13 billion in 2011, buoyed in part by Berkshire's purchase of the Burlington Northern railroad, Barron's wrote. It is also likely that Berkshire's investments in Goldman Sachs (GS.N), General Electric (GE.N) and others – made during the financial crisis – could be repaid. Such an influx of cash could prompt Berkshire to begin paying a dividend in the next year to year and a half, Barron's wrote – especially if Buffett fails to find another large investment. Berkshire has not paid a dividend since Buffett took control in 1965. Instead, it has re-invested its profits. However, the extra cash, rising asset and equity values, and Buffett's impending retirement could make a dividend an attractive option, Barron's wrote. Decreasing Berkshire's cash pile ahead of Buffett's retirement would remove some of the pressure on Buffett's successor to immediately invest, according to the report. A Berkshire dividend is expected to start out small, at two per cent or less, according to the report.

Source: www.reuters.com

The background of the slide is an abstract geometric composition. It features a large, bright green, three-dimensional shape that resembles a stylized arrow or a jagged, upward-pointing form. This green shape is set against a backdrop of various grey and white geometric elements, including triangles, polygons, and lines, some of which appear to be floating or layered. The overall effect is modern and dynamic, with strong contrasts and a sense of depth.

A Guide to Picking Stock Market Winners – Part 3

Break the Rules

.....

You hear about plenty of trading rules: Do not catch a falling knife, the trend is your friend, buy on rumour sell on fact... I will not try to list any more because there are books full of them. The key thing to remember is they cannot be right or wrong otherwise people would be making a fortune from them and nobody appears to be doing so.



Clem Chambers

Clem Chambers is CEO of ADVFN (www.advfn.com). His book "101 Ways to Pick Stock Market Winners" will be published on 24th February 2011 by Beautiful Books. Paperback. £6.99.

Rules: Seldom Profitable

To illustrate the point, I very rarely use stop losses. So recently when I was pruning my portfolio for profits I noticed one stock that was clearly going broke. I had bought it on the premise it would either go bust or rocket. It was doing the former by falling 95 per cent. Normally I would let the company vanish, the loss more than recouped by the other members of the portfolio that go up nicely and occasionally really rocket. So I sold the soon to be defunct company for a net of a very nice dinner and an excellent Claret. Why not treat myself? The stock immediately rose 1600 per cent much to my amusement.

The point being, "rules" are very seldom profitable and in some cases actively unprofitable. How can a rule be unprofitable? If a rule is slavishly followed by most people it will violate market symmetry and provide an opportunity for the contrarian to make money.

The market prices very efficiently based on the fact that most market action is highly random. The chances of the stock I mentioned jumping 1600 per cent is very low. However, it

counterbalances the downside of almost certain demise. On balance, whatever you do, if you do not have an edge, it will come out even. This is priced in.

Now let us say there is a rule everyone follows; let us say the rule is: Do not buy stocks that start with a letter P in March.

This rule has no impact if only you and a friend do it, but if everyone does it, then prices of P stocks fall in March and buying P stocks at the end of March will be cheap and consequentially the stock will jump in April.

Meanwhile everyone will look at the price of P stocks falling in March and go: "wow what a great rule; do not buy stocks starting with P in March." However buying stocks in late March will in fact be a great trade.

How the Market Pays You to Make It Efficient

The market therefore pays you to make it efficient because if you then spot that the rule is wrong and you do the opposite you will make money. In the March example, the more you buy, the more the price is supported and the less the flawed rule works. Consequentially, there is also less

F1) De La Rue



Figure 1 shows the developing cycle of Crash, Dead Cat bounce (1) and recovery (2).

Source: www.advfn.com

F2) Eaga



Here is another example of the developing cycle of Crash, Dead Cat bounce (1) and recovery (2).

Source: www.advfn.com

to make out of going against the rule. Ultimately the flawed rule is cancelled. This is the mechanism of how the market pays you to make it efficient. Eventually, moves in March for stocks with the letter P are back to their normal random jittering around.

Even trading rules that once did work will stop working in the end, because if enough people know them they will pre-empt the rule and erode it away in both time and scale.

Consequently it is very hard to find rules that work. Anyone who has traded for a bit will acknowledge this.

So considering the above points, the place to find trading rules is to pick ideas that are either:

- Unique
- Not mainstream
- Mainstream but clearly misguided
- Contrary to market efficiency concepts

My favourite is a combination of 'do not catch a falling knife' and 'do not try to trade a dead cat bounce.' Most trading books and courses will drum this into you. Dead cat bounces will kill you; catching a falling knife needs no explanation. The fact that no

one wants to buy a stock that is tanking is the reason why if you can time it right there is money to be made. The question is how.

How to Make Money from Breaking the Rules

The first thing to note is what the current market is doing to companies that fall out of their tree. If the market is so bad that

“If a rule is followed by most people it will violate market symmetry.”

they simply go bust, then why would you get in? However in most market circumstances there is a pattern which evolves over time.

In good markets or bad a company normally falls because of bad news. It will then fall a certain percentage, say 15 per cent in a bull market, perhaps 40 per cent in a bad one. Then there is a pause, perhaps two days in a bull market or a week in a bad market, before a rebound. This is the pattern you are looking for. Once it is established you need to refine your candidates.

For example, I discard companies that crash, which might go bust through debt or

have a mighty valuation before the bad news. As such, I will not buy Apple when it falls 10 per cent or more in due course.

Once you have filtered out companies you do not like on other criteria, you are left with a plan of attack.

A company has some bad news and collapses; you can then follow the established pattern of previous cases and buy in.

Of course this can be easily paper traded at first to get a feel for it and like all high volatility trades, is best started small.

Conclusion

The current dead cat bounce pattern in the UK market has been changing in the last month and a chart of the archetypes is illustrated here. In time this will change and a new form will be tradable.

Yet until the advice in general stops being, 'do not catch a falling knife' there will be a fat profit for trading jugglers prepared to become skilled in doing just that. Then the rule will again be: 'buy the dips' and it will be time to sell them.



F3) HMV GROUP



The third example is part way through the cycle, with a Dead Cat bounce (1) already occurring. The trader should then follow the progress of the cycle to look for early signs of a recovery. The recovery is not guaranteed but its likelihood coupled with other criteria will produce a high probability trade.

Source: www.advfn.com

Technical Analysis & the Age of the Algorithm

Has Algorithmic Trading Rendered Technical Analysis Ineffective?

Professional and retail traders alike have long relied on technical analysis to deliver insights into market behaviour. But now that computers are increasingly making the trading decisions, can technical analysis really provide the same value it once did? After all, does it not reflect the human behavioural patterns behind trading activity?

According to veteran technical analyst and president of Gramza Capital Management, Inc. Daniel Gramza, technical analysis is just as relevant as ever. In fact, he argues, it may even be more so. “As long as there are people involved in the decision process, we will see their footprints. The fact that an algorithm may trigger a signal and possibly execute it does not change the underlying premise that a human created the algorithm and it is their actions that we are seeing reflected in technical analysis.”

And that is good news for retail traders because mastering technical analysis is something that an individual investor can certainly achieve – without massive amounts of capital investment. John Netto, President of One Shot One Kill Trading and popular market commentator believes that retail investors should embrace technical analysis

perhaps even to a greater extent than in the past. In his opinion “The secret of the successful trader, retail or professional, is the drive to improve his or her game. Staying abreast of the latest developments, whether in technical analysis or technology, is key. In my opinion, technical analysis can only help traders decode market movement.”

Interest from the Algo Players

A positive development for technical analysis is a rise in interest on the part of sophisticated trading firms looking to supplement their mathematical models. As with every strategy since the dawn of trading, when the crowd catches up, the edge is gone. And it is of course no



Daniel Gramza

Gramza Capital Management

different in the case of algorithmic trading. The algorithmic space is becoming increasingly crowded and as many firms are trying to do the same thing the challenge at hand is to build a better mousetrap.

In the search for unique sources of edge in the algorithmic trading world, technical analysis



John Netto

One Shot One Kill Trading

systematically develop and hone new strategies. “Now whether technical analysis needs to be part of a winning trading strategy is another story. However, firms or traders that aggressively search out ways to create edge – which certainly may include technical analysis – are in my mind ahead in the race for survival of the fittest.”

Gramza has witnessed first hand this search for new inputs to models, noting that the matriculation of sophisticated players in his courses is up. “What

I have experienced around the globe is that more and more algorithmic institutional and prop trading firms are expanding how they view and trade the markets and are becoming interested in technical analysis. Technical analysis trading tools are beginning to be implemented by these organisations in ways that has not occurred in the past.”

Special Considerations in the Algorithmic Age

So if the patterns made by algorithms are arguably no different than those made by any other trader, are there any differences in the age of the algorithm? Netto argues that at

least one important difference exists. “Today, we are seeing that the market moves at an incredibly rapid pace. And when trading decisions are taken in milliseconds, technical indicators have to keep up. In my personal trading, I have reduced the timeframes that I look at and invested in technology to ensure that my charts and studies are delivered via larger, higher-capacity lines.”

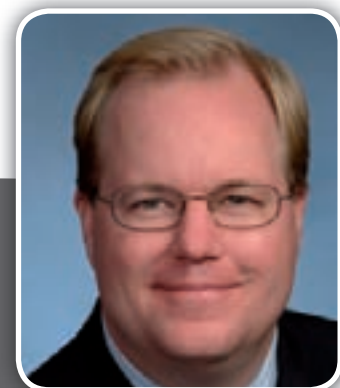
No Holy Grail

Experts agree that a common problem for retail and professional traders alike may be that they are looking for a holy grail in technical analysis. They caution against asking something from the technical indicator that the technical indicator is not capable of providing. Gramza has his own laundry list of common mistakes when it comes to explaining why a given technical analysis method falls short. “Typically, it is because the trader has not taken the time or does not have the understanding to make critical inquiries into the specific market characteristics, the strengths and weaknesses of the trading strategy, identification of specific targets and stops,

etc. The second major issue is knowing when and when not to trade. Investors and traders often fail to identify this aspect of trading.”

Conclusion

While technical indicators can offer value, it is essential to ask questions that look beyond the typical output information. Potentially profitable trading strategies are often not identified because traders fail to ask the right questions regarding the analysis of signals. So while technical analysis summarises human behaviour and perception regarding a particular market, this recording of behaviour is not affected by algorithmic



Ben Van Vliet

Illinois Institute of Technology

presents a powerful resource, as traditionally it has not played a major role in algorithms. On a global basis, the application of technical trading strategies is often limited to a few basic techniques. This limited application may just provide an opportunity upon which others in the industry are not currently capitalising.

Ben Van Vliet, Lecturer and Associate Director of the Illinois Institute of Technology's MS in Finance program has made a name for himself identifying the next challenges in algorithmic developments. Van Vliet's argues that tomorrow's leaders are the ones that proactively and

trading. That is good news for traders everywhere, as it means that they can continue to rely on technical analysis for clues into market movements.



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Going Green

Trading on Sports Exchanges – Part 2

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In a previous article we examined how trading works on a betting exchange. While we discussed that trading on a sports exchange was similar to spread betting on financial markets, there are some important differences to examine and explain. Most of these curiosities relate to the way in which the exchange was set up to deal with settlement or a sports market rather than a financial market and this should influence how you choose to trade them.

How to Make a Loss, but Not Lose any Money

On the financial markets there is the traditional saying that you should “let your profits run and cut your losses”. While that mantra is true, in general, for trading on most markets, it is not strictly true for betting exchanges. One of the real oddities about trading on betting exchanges is that it is possible to get your trade wrong and make a loss, but still not lose money! The reason for this strange situation is due to the unique way in which

markets are settled. When you place a bet on a betting exchange you will either win or lose, that is fairly obvious. In a horse race there can be many runners, but only one winner. Therefore betting exchanges only settle a market on whoever wins that market. That is a fairly logical way to settle a market, but when trading, this aspect takes on a whole new characteristic.

In Figure 1 you can see we have made a bit of a mess of this trade. We backed Thundering Home at 3.50 for £200 and his



Peter Webb

Former City Trader Peter Webb was one of the very first people to use Betfair, back in June 2000. In 2005 he launched Bet Angel (www.betangel.com), a comprehensive software solution for sports exchange trading. Peter has run regular seminars on advanced sports trading techniques since 2004 and regularly writes for the Racing Post on the subject.

odds drifted out, got bigger, so we had to close for a loss of £25. Our loss occurred because, to be profitable, we needed to lay at a lower price than we backed at and we have not on this occasion, so we have incurred a loss.

But, because the market is settled on the eventual winner of this race we may still not lose any money. Our loss on “Thundering Home” will only be recognised as a loss if “Thundering Home” actually thunders home! To clarify my point, only if that horse wins we will make a £25 loss, if this horse fails to win then we will lose nothing.

The reason for this is that none of the other horses have a loss on them. None of them have a winning amount on them either, so if any horse other than “Thundering Home” goes on to win we will win nothing; but we will also lose nothing! In this particular case the horse did not win, which is less likely anyhow as it was not the favourite. Therefore our £25 loss did not mature. Despite losing £25 on this trade we actually ended up losing nothing on the race, strange but true.

It is at this point that I can flip things the other way. If we traded this well and correctly predicted the price movement, we would win some money. In Figure 2 you can see that I have successfully done this earlier in

the same race. I have traded and realised a £5 profit. Unfortunately, in the same manner in which we would only make a loss if the horse with our losing position goes on to win, the same applies in reverse to our profit. We will only make a profit on this horse, if we have traded it correctly and the horse goes on to win. However, there is a neat solution to this problem which allows you to win regardless of who goes on to win the event.

Win Whatever the Result

I coined the phrase ‘greening up’ many years ago. The nickname “greening up” comes from the status of your profit and loss display on the betting exchange after you have successfully completed this transaction. When you ‘green up’, your entire profit and loss displayed for this event will be green, in profit, rather than red. This means you will win money whatever happens in the actual event, hence the name. It is a marvellous feeling looking at an event and seeing it all green and knowing you cannot lose whatever happens in the underlying sport. What you are effectively doing is hedging your traded profit to ensure a win. But how is that achieved?

When you hedge, what you are effectively doing is transferring profit from one selection to the rest of the field. You do this by

F1) Making a Loss, but Not Losing any Money

Selections (5)	Back	Starting Price (Projected SP)	Lay
Keeney Royale (3)	2.38 (234)	2.42 (242)	SP (2.42)
Thundering Home (4)	3.65 (365)	3.75 (375)	SP (3.75)
Temple Fair (5)	5.4 (54)	5.5 (55)	SP (5.5)
Kathind (1)	9.8 (98)	9.2 (92)	SP (9.2)
Rock Of Fire (2)	26 (26)	27 (27)	SP (27)

This section of the screen shows our trading position on a race on the 19.40 at Kempton. We backed Thundering Home at 3.50, but had to close for a loss of £25 when the price drifted out. However, we will only lose if the horse wins the race.

Source: www.betfair.com

F2) Correct Trade Only Pays if Your Horse Wins

Selections (5)	Back	Starting Price (Projected SP)	Lay
Keeney Royale (3)	2.46 (246)	2.5 (25)	SP (2.5)
Thundering Home (4)	3.3 (33)	3.4 (34)	SP (3.4)
Temple Fair (5)	5.4 (54)	5.5 (55)	SP (5.5)
Kathind (1)	9.8 (98)	9.2 (92)	SP (9.2)
Rock Of Fire (2)	26 (26)	27 (27)	SP (27)

On the same horse, we now stand to make a £5 profit (this is actually at an earlier point than depicted in Figure 1). Likewise, we will only see our winnings materialise if Thundering Home crosses the line first.

Source: www.betfair.com

laying off some of your profit on your profitable traded position. If we had £100 traded profit at odds of 2.00, we would lay £50 at 2.00. This would mean that the profit on the eventual winner will be lower at £50, but you would also win £50 if any of the other runners won the race. The benefit of doing this is that the result of the event, from a profit perspective, becomes irrelevant. It does not matter who wins from this point onwards, you would win £50.

The criteria for greening up is very simple, all you need to do is make a profit on something in that event. Then it is best to use software to perform the greening transaction. We could talk about the actual maths of how it is achieved, but that is irrelevant if you use software like Bet Angel. All you need to do is click a button on the screen and it will instantly spread the profit out across all selections. You can choose not to hedge, but your profit then becomes dependant on the result of the underlying event and that means that most people typically hedge all the time.

Leveraging Your Capital
Another key factor that works well in your favour if you trade

on betting exchanges is instant settlement. On a betting exchange there is no concept of delayed settlement or result dependant settlement when initially trading. When your trade is complete, your stake is returned to you immediately and

“**We made £48.20 for only ever risking £100 at any one time.**”

you can put that back through the market. If you have just £100 in your account you can open a trade and close it seconds later, hopefully for a profit, and immediately put the same £100 back through the market again for another turn. Taking advantage of this characteristic allows you to put through significant sums, while only using a small bank. By turning the same capital repeatedly you can effectively leverage up quite small stakes into a potentially very large traded sums.

In the final illustration (Figure 3) you can see we have combined all the elements we have talked about into one neat profit. First we traded “Thundering Home” with £100. The first trade went well and made us £5 but the

next trade did not work and we took a £25 loss. We let this loss stand and then decided to trade “Keenes Royale”. We did better on this horse and managed to put through five trades of £100 each making a total of £500 traded on the back and lay side.

In total we managed to put fourteen trades through the market. The final bet was a ‘greening up’ bet and this ensured we won whoever went on to win the race. The favourite “Keenes Royale” went on

to win, so we made £48.20 for only ever risking £100 at any one time. All this was done just a few minutes before the start of the race. I recorded this live to capture the illustrations, so a video of this is available on our website (www.betangel.com) for you.

Conclusion
There is no doubt that some of the characteristics of exchanges are unusual if you are used to traditional spread betting. But if you are aware of them you can incorporate them in your trading strategy and use them to your advantage.



F3) Ensuring a Profit, Whatever the Outcome

We have now managed to get trade Keenes Royale to the tune of £500, on the back and lay side, only risking £100 at a time. We have ‘greened up’ – ssee green figures on the left hand side – meaning the worst outcome of this race is a £30 profit if either Temple Fair, Kathindi or Rock of Eire win. If Keenes Royale wins, we will pocket £48.20. See a video of this process at www.betangel.com.

Source: www.betfair.com

optionsXpress offers a series of technology upgrades to its proprietary streaming charts. Upgrades, free to optionsXpress customers, include a customisable grid view allowing traders to see a variety of charts simultaneously, then save and reload charts for use during future sessions. Traders can use tab or grid views to alternate between multiple full-sized charts for use during future sessions. Traders can display recent earnings information with details on their charts. The integration of the charts into the optionsXpress platform allows customers to launch an entire watchlist or positions into the grid or tab view with a single click. It allows customers to trade multiple asset classes from one platform and one account. For further information, please visit www.optionsxpress.com

Interactive Data Mobile, a companion offering to the Interactive Data suite of desktop and web-based solutions for financial professionals, has been released. The application uses the latest technology, delivers streaming financial data and tools. It is available on Apple's iPhone through Apple's iTunes App Store. Interactive Data Mobile, formerly known

as QuoTrek, gives financial professionals and traders access to real-time streaming data on their mobile devices anytime and anywhere and can be used



in conjunction with Interactive Data's desktop and web-based products. Users can create their own portfolios to obtain detailed data on an issue, view charts, follow markets or stocks, and monitor the market. It is also available for the BlackBerry and other mobile devices. Two versions are available for the iPhone: a free delayed version and a paid real-time version. Additional details can be found at www.InteractiveDataMobile.com

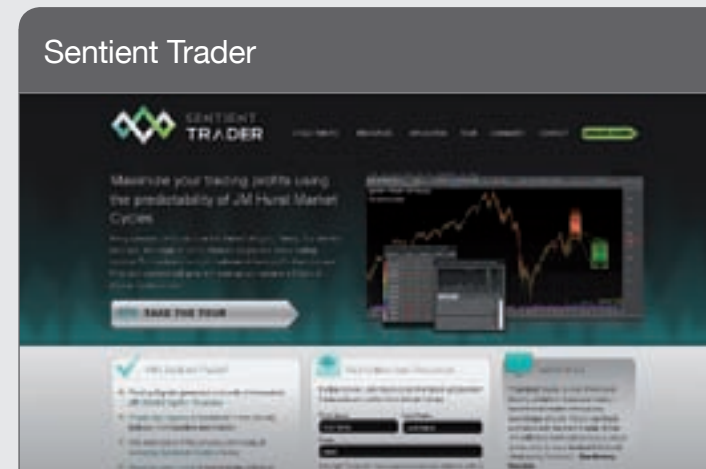
CQG announced Chicago-based Continuum, a new enterprise solutions business division. The Continuum suite includes: Continuum Connect, Development Library, FIX Connect, FIX/FAST Direct, and

an Historic Data Hub. Continuum has recently partnered with several major organisations to provide customised solutions for their platforms. CQG also said it had partnered with ADVFN to provide global order routing connectivity to offer trade execution functionality to ADVFN's client base. ADVFN customers can now connect to CQG's global infrastructure using Continuum's FIX Connect. ADVFN customers will be able to trade global markets through CQG's gateways. With a presence in Europe and North and South America, ADVFN provides market data from exchanges worldwide. Firms can take advantage of Continuum's API offerings to realise low-latency order routing execution



and real-time and historical market data delivery objectives. For more information, please visit www.cqg.com

SunGard has launched an ultra low-latency direct market access (DMA) service for pan-European equity markets through its European broker-



dealer, Valdi Execution Services. Valdi addresses the ultra low-latency requirements of high-velocity traders, providing a broker-managed solution that includes clearing and settlement. The demand for ultra low-latency market access continues to grow. Initially, the new DMA offering will connect to the BATS and Chi-X MTFs and then extend its connectivity to Turquoise and the London Stock Exchange. For further information, please visit www.sungard.com

Sentient Trader has interpreted and developed the cyclic theories of JM Hurst into a modern computer trading

system, the company said. The Hurst Trading System captures all the theories published by Hurst in his book, Profit Magic Of Stock Transaction Timing, and in the more complex theories in his course (available from Traders Press). Sentient Trader added that it had refined the theories with innovations designed to improve performance for traders specialising in technical analysis. The Sentient Trader community has access to a range of regularly updated support materials including training videos and webinars, and participation in a user forum. Further details can be found at www.sentienttrader.com

FXDD, an online forex broker, now provides forex trading accounts using the yen as a base margin currency in addition to the US dollar. FXDD expects to offer similar options in other major currencies including the euro, British pound, as well as others shortly. FXDD offers 24-hours forex trading worldwide via its trading platforms powered by Currenex and FXDDAuto. For more details, please visit www.fxdd.com

The Street-Smart Trader

An insider's guide to the City

by Ian Lyall

To the outsider the City is still something of a mystery. Independent traders and investors like you may study the financial pages and log on to websites to read about the markets, yet what you find there will generally give you little concept of the realities of City business. The hard truth is that independent traders are up against dealers with more information, professional investors with greater financial clout, and investment banks and hedge funds with more powerful systems, all of which can leave the odds stacked against you and puts you a few crucial steps behind in their trades.

Ian Lyall's new book *The Street-Smart Trader* aims to level this playing field, giving an insider's view on the big issues from press coverage of the markets through to the reports of financial analysts. Formerly a financial journalist for the Daily Mail, Lyall takes a look inside the City and encourages readers to question what they think they know and

shows how his insights can turn you into a more profitable trader.

The book begins with a look at the history of the stock market, from the coffee houses of the 1680s right through to the Big Bang in the 1980s and the financial crisis of 2007-2009. Lyall comments that despite the advances in technology and the reforms that came about in the late 80s, the market is still 'centered around the institutions that dominate the City of London', and as such still operates largely for those professional traders who do most of the business. However, Lyall argues that the street-smart trader must not be down heartened about this, and must just always bear it in mind when entering the markets.

Chapter 2 'If you don't know the rules, don't play the markets' features seven trading commandments from a City dealer that will show exactly what you're up against and how individual traders can improve their trading performance. As Lyall says 'If this was a

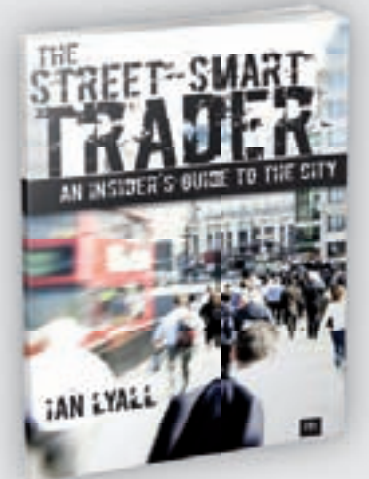
newspaper I'd dub Chapter 2 your cut-out-and-keep guide to surviving the stock market' - this section is key to how you approach your trading. Rule One, 'The information available is not evenly shared' is an important one to note. Professional traders will sit in front of a bank of screens, all continuously updating the latest prices, they will have access to a wide network of analysts, fund managers and journalists that they can call up, gaining seconds, maybe even minutes over an independent trader waiting for the internet page to reload. Rule Five 'Be dispassionate' examines how professional traders 'inhabit a surreal world where million-pound transactions are distilled down to ticks and bars...the pros have perfected a way to insulate themselves mentally from the trades they make.' Now obviously, this is more difficult for a private trader or investor, but Lyall's tip is to act like the professionals. This means not taking the ups and downs of the markets personally, and not getting greedy - take a profit, cut a loss.

Chapter 4 'The City Spin Game and How It Is Played' looks between the lines of company statements and reports in the press to find out what is really being said. Lyall writes that the spin machine from the City today is a sophisticated one, and is

mainly about control, run by a small but influential band of advisors who decide what the financial press and traders are told. Using the Cadbury takeover as an example, Lyall examines how the press coverage of a story is manipulated. He argues 'As a street-smart trader, it is important to probe behind the smokescreen thrown up by the spinners' and concentrate on the facts, to make sure you're seeing the fuller picture and not just what the PR advisors want you to see. As Lyall rightly says, there is no substitute for original research and performing your own due diligence on a company. Lyall's book highlights the hard truth that independent traders are up against professionals with more information, more access and more powerful systems, but he argues that this doesn't have to mean that the independent traders can't win. Concluding *The Street-Smart Trader*, Lyall suggests readers remember two questions - does the story really make sense and can I trust the source? Using these two questions and the book's insights into the City, Lyall shows how you can make more successful and more profitable trades in the future.



BOOKREVIEW



Title: The Street-Smart Trader

Subtitle: An insider's guide to the City

Author: Ian Lyall

ISBN: 9781906659073

Price: £12.99

Publisher: Harriman House

About the author:

Ian Lyall is the editor of 'Proactive Investors', a champion of the independent stock market trader. Before that he was the investment editor and City news editor at the Daily Mail, where he directed the coverage of some of the biggest stories to ever emerge from the Square Mile as it struggled in the grip of the credit crunch and subsequent banking crisis. In his 15 years as a business reporter and editor, Ian has worked for Dow Jones, writing stories for the international news wire, and the Wall Street Journal. He also led the London company coverage for AFX News, now part of Reuters. His specialist areas are pharmaceuticals, biotechnology and growth stocks.

A Modern Take on What Interactive Data's eSignal Does Best

eSignal 11

Interactive Data has made a bold move with eSignal 11. Completely rewriting an already successful trading application is a large investment, but given how long eSignal has been around and the changes in the markets, it was certainly time for a change that would take the best of the old and give it, not just a modern, new look and feel, but added features that meet the demands of today's markets. The all-new eSignal has mostly hit that mark.

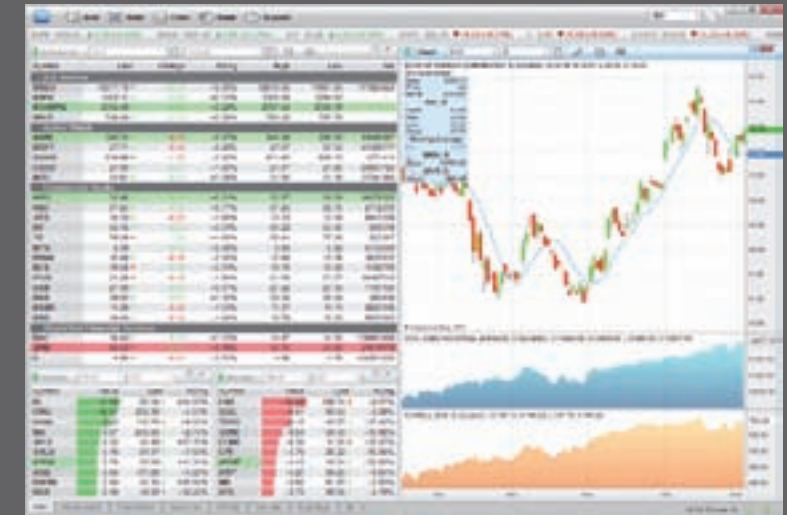
New Look and Feel

Even before you open eSignal, it is clear from the splash screen that version 11 is different from previous releases. Not just the sleek new look but the improvements to the interface tell you that this version was re-designed by traders, for traders. The real-time data immediately flows, and the default portfolios light up with each trade.

One of the striking differences is the lack of toolbars. Previous versions of eSignal layered numerous buttons and icons along the top of the screen. In version 11, the clutter has been replaced with a scrolling ticker and toolbars that tuck

themselves into the windows' title bars to save space. It is an elegant approach that saves space. Along the bottom, eSignal now has tabs for switching between pages – a welcome addition to the application for those who need fast access to pre-set layouts. In fact, many of the tools a trader needs to perform efficiently are easier to get to and manipulate in the new version. Everything from creating pages to moving windows and charting components is simpler and faster. One clear absence is the ability to bring in pages from 10.6. A quick web chat with an eSignal sales person confirmed that this is something coming in the future. Multiple language

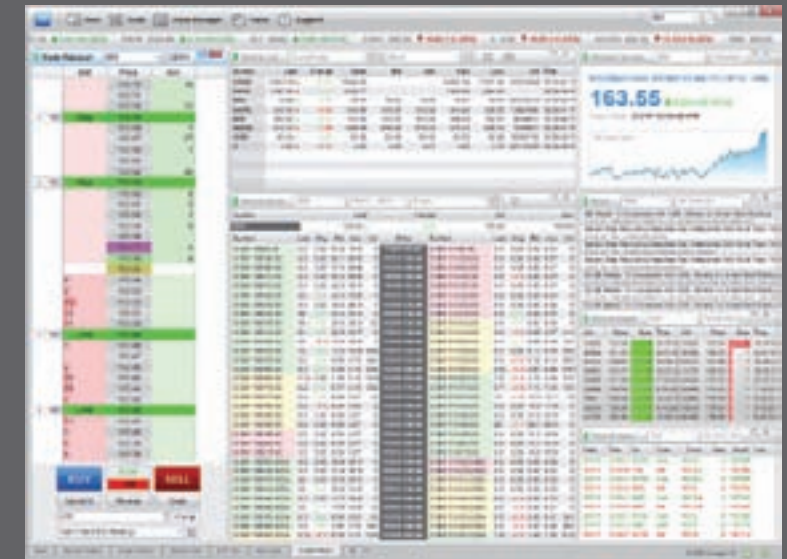
F1) eSignal 11's Main Page



One of the default pages with the software includes a candlestick chart of BAC on the right with sub-charts of the Dow Industrials and Russell 2000 indices.

Source: eSignal 11

F2) Trading with eSignal 11



Placing trades is easy to do with eSignal 11's Trade Manager (on left). Tiered limit and stop orders are automatically placed with customisable exit strategies.

Source: eSignal 11

support now includes German, Spanish, French, Italian, Russian, Chinese and Japanese. Although the German translation was not perfect, it is certainly great to see eSignal moving in this direction.

Trading in eSignal 11

One of the more flexible aspects of the eSignal platform is the way it works with a variety of brokers and service providers (more than 25 are supported). This enables you to shop around to find the best broker and still be able to trade right from within the application.

eSignal 11 really shines here. With large Buy and Sell buttons and an easy-to-use price ladder, using the re-designed Trade Manager feels like riding a familiar bicycle around the block. It is especially useful not having to download and install plug-ins separately although having to re-establish the trade defaults was something of an annoyance.

The new Trade Manager shares many commonalities with other DOME applications: single-click order entry, drag-and-drop order modification, and a heads-up display. What differentiates these features in eSignal is that they are inserted into a clean view within the eSignal work area. And, mousing-over the price ladder “holds” the display for you so that you can place orders without the

prices moving underneath your mouse...a nice touch.

What is really enjoyable is exploring the new Money Management Planner to set up different exit strategies. For instance, with a default size of five contracts, once you enter a trade, multi-tiered stops and profit targets are automatically entered at the levels you specify, with ways to add trailing stops and other advanced order types.

Charting

eSignal has always had strong charting capabilities, and for the most part, this has not changed in eSignal 11. All the built-in studies and formulas are present. However, it does seem to require manually moving over the formulas you may have used in eSignal 10.6. Adding studies to the chart is easy, as is drawing lines; not much departure from 10.6 in that regard. Double clicking a moving average to edit it is certainly an improvement, as well as the ability to edit studies on the fly (i.e., a change in parameters immediately took effect on the chart).

One missing item in this category is the ability to save chart settings and apply them to another window. It was confirmed by a company representative that this was not yet possible but is coming in the next version (11.1) in the form of “Study Templates”.

Overall, the charting was easy to use, but some improvements would make it as strong its predecessor. Interactive Data does seem to be financially committed to improving eSignal 11.

Watch List

Acting as a central hub for baskets of stocks and futures, the Watch List is thoroughly integrated into eSignal 11. Combining the best 10.6 features from the Quote, Summary and Portfolio windows, the new Watch List is easy to use and multi-featured.

The ability to insert Comment Rows was a handy feature in eSignal 10.6. In version 11, this feature is brought to a whole new level with the ability to roll symbols up underneath these rows for later use. In combination with one another, the ability to insert symbols from a specific sector, industry, or one of eSignal’s Hot Lists and this roll-up feature allow for simple creation of powerful U.S. market scans that can then be sorted on various columns. Furthering the usefulness of these scans was the new ability to add technical studies to the Watch List. In eSignal 11, you can add all your charting favourites right into your symbol lists. Sortable study columns mean that you can dig into the technicals efficiently without

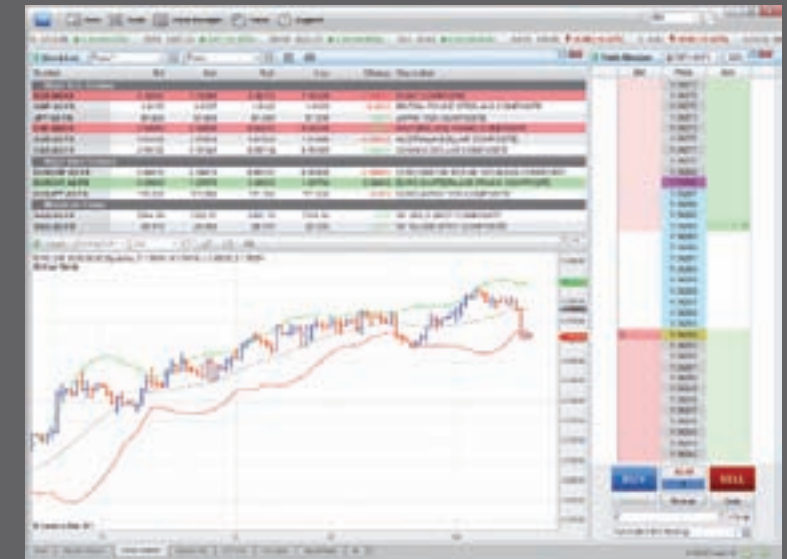
F3) Advanced Charting



Charting is easy to do in eSignal 11, yet powerful enough for the advanced trader. Here is a daily chart of Apple with three Volume-Weighted Moving Averages, a MACD, Stochastic and Directional Movement. The Fibonacci retracement shows potential support levels based on the recent trend.

Source: eSignal 11

F4) Tracking Forex in a Watch List



Popular Forex currency pairs and metal spot prices are listed in a Watch List. Clicking on a symbol updates the symbol in the integrated bar chart and Trade Manager for easy analysis and trading.

Source: eSignal 11

having to look at chart after chart after chart.

Price

eSignal 11 comes with a 30-day trial in multiple pricing packages, depending on your needs. eSignal OnDemand starts at \$34.95 per month and provides delayed data across nearly all global exchanges. For an additional \$20, you can add real-time E-mini data to the OnDemand version if you use one of the supported brokers. eSignal Premier is the recommended package for real-time stock and futures traders and has a base price of \$129 per month while

Premier Plus adds options for a \$199-per-month base price.

Also available on eSignal 11 is the Advanced GET Edition, a proprietary set of strategies and studies, complete with personalised training and mentoring. Priced for a one-time purchase at \$3,995, this full-service trading suite based on Gann and Elliott Wave theory has many potential benefits for the novice and professional trader alike.

System Requirements

eSignal 11 is fully compatible with Windows 7, Windows Vista, Windows XP and

2000 and has 32- and 64-bit versions. The following are the "Recommended" and "Power User" system requirements:

Recommended

- Intel® Core™ 2 Duo, 2.0 GHz or faster
- 2 GB RAM
- 40 MB available disk space
- DSL or cable modem

Power User*

- Intel® Core™ i5 / i7, 3.2 GHz or faster
- 64-bit Operating System
- 3 GB RAM or more
- 40 MB available disk space
- DSL or cable modem

*A "Power User" is someone who uses one or more of the following:

- five or more tick charts
- ten or more interval charts
- 15 or more drawn objects on a chart (through eSignal's formula language, EFS, or the line toolbar)
- CPU-intensive EFS or back testing studies (using multiple loops, global variables, etc.)
- Tracking of a high number of active symbols
- Tracking of E-minis in a chart or in a Market Depth window

Conclusion

eSignal 11 is a new product from a proven company. eSignal has been

known for its high quality financial information and charting for the active trader, and the latest offering is no break from that. Although not yet as fully featured as its predecessor, eSignal 11 is built on a strong foundation, making it attractive to prospective users for a long time to come. New traders should definitely take advantage of the 30-day trial. Existing eSignal traders may choose not to upgrade right away, but they would be wise to keep a close eye on eSignal 11's development.





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Real World Trading Signals for Active Traders

There are plenty of proprietary trading systems out there hoping to impress you with their historical performance results. StockSpotter.com is unique in that it provides daily short-term trading signals in advance and tracks its own performance for each and every trade.

Structure and Mode of Operation

StockSpotter.com locates daily short-term trading opportunities from a basket of 3000 listed U.S. stocks. Algorithmic buy/sell trading signals are published on the website each evening for intended execution at the next market open. StockSpotter gives an entry signal the night before and then simulates trade entry at the next open. Open trades are monitored with profits updated as each trade progresses from entry to exit.

Exit signals are specified for each open trade. StockSpotter is a short-term (swing) trading system that gives an exit signal within ten market days of entry. As with entry signals, exit signals

are published on the site the night before for execution at the next open. The website provides a convenient watch list feature allowing you to follow open trades of interest and be alerted to their exit signals in advance.

The Algorithm

StockSpotter's trading signals are algorithmic with no human intervention or consideration given to fundamental analysis, earnings reports, or news events. StockSpotter uses a proprietary algorithm developed by veteran trader and author John F. Ehlers, pioneer of the MESA trading technique. The same robust algorithm is used for all tickers at all times. Ehlers is well known for his 20+ years of work

involving the use of digital signal processing (DSP) to analyse market cycles and trends. StockSpotter's approach is based on Ehlers' technique for detecting the dominant cycle of daily price fluctuations and advancing the phase to buy on cycle troughs and sell on crests when the signal strength is optimal.

Signal Ratings

Each new entry signal is published along with a signal rating ranging from two to five stars. The signal rating represents an estimated signal quality based on statistical data mining techniques. By including the signal rating, StockSpotter permits historical performance results to be viewed by signal

rating. Ehlers points out that the signal rating is statistical thus it should be taken with a grain of salt with regard to any individual trade. Says Ehlers "Neils Bohr said 'Prediction is difficult, especially about the future'. This is the nature of prediction. It is difficult enough to forecast the correct direction, yet alone assign a confidence level. None the less we have found StockSpotter's signal rating to be a useful metric and have included it in our approach".

Performance Results

Once a trade closes the details are retained in StockSpotter's internal database. The website provides several convenient methods of viewing performance.

Historical and open-trade performance can be viewed for both individual ticker symbols and aggregated by signal rating. If you want a more detailed analysis, a CSV file can be downloaded containing trade-by-trade details for import into Microsoft Excel or other analysis software.

You can view performance results summary information containing metrics you would expect including profit factor and percent wins, average profit per trade, and others. StockSpotter also includes an equity growth chart and a detailed trade-by-trade grid that provides a chronological listing of each trade's entry and exit dates and prices along with percentage gain and signal rating.

Ease of Use

The StockSpotter system is intended for several types of active short-term traders including: (1) those that do not have time to do their own detailed analysis, (2) those that have not been successful with their own analysis techniques and (3) those who wish to use the trading signals as a starting point for their own further analysis. We found the website to be very easy to understand and navigate. There are no backtesting tasks to perform, no technical charts to interpret, and there is no coding involved.

Monte Carlo Simulation

The StockSpotter trading system performs a daily analysis for each ticker symbol. A typical day might produce several to a dozen or more new trading signals. As a result, the number simultaneous open trades can vary considerably at any given time. An individual trader or small fund could not possibly take all the trades all the time. This makes overall system performance measurements difficult. To accommodate this, StockSpotter includes a Monte Carlo simulation tool to estimate profit based on a single \$5000 investment always in the market. The Monte Carlo tool also gives you an estimated drawdown based on this same \$5000 investment. Although no method based on historical performance can be counted on for future performance, the Monte Carlo simulation technique is generally well-regarded and superior to other risk estimation methods such as the risk of ruin.

Options Strategies

StockSpotter is a statistical edge equity trading system that attempts to achieve moderate gains with holding times of two weeks or less. This suggests a couple of options strategies. One is to buy a call (or put in the case of short signals) near the money with a month or two until

expiration. Since the expectation is for a small gain within a short period of time, a slightly more complicated but typically less risky strategy would be to execute a bull call spread (or bear call spread in the case of short signals), buying the bullish leg at the money and selling the bearish leg one or two strikes out of the money.

Conclusion

StockSpotter.com can be a valuable tool for active short-term traders. The service costs \$120 USD per month and offers an initial \$30 for 30 days evaluation period.

We found the website to be very open and realistic about its performance. Unlike some black-box systems, StockSpotter provides 100 per cent of all trading signal results. The website publishes all entry and exit signals in advance effectively making each simulated trade out-of-sample and independently verifiable. Since all trade entries and exits are taken at the next market open without stops or limits, the simulated trading results should typically be very close to what you could have expected to achieve in the real world.



F1) Entry Signals



Figure 1 shows an example of StockSpotter's daily entry signals for the next open. The system produces both long and short trading signals.

Source: www.stockspotter.com

F2) Equity Growth Chart



Figure 2 shows the equity growth chart resulting from StockSpotter's simulated trades.

Source: www.stockspotter.com

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Last year the WhichWayToday LIVE trading made 8000 pips. Each day between 0630 and 1100 GMT two experienced financial traders operate the live trading room which specialises in making money from short term trades in stock indices and Forex.

The room is run by Tom Hougaard and David Paul. The room has a one year, transparent profit history, which is clearly displayed on the www.whichwaytoday.com website. Each trade is relayed to each room member instantaneously and is complete with stop loss level and profit target.

In the room the trades are classified into two main categories. These are intraday and swing trades. When a new customer signs up for the service, they are immediately sent a document which details the money management principles upon which all winning traders agree, that success is built. During the trading sessions, this concept is reinforced and many have concluded that the WhichWayToday

live room is like going on a course in trading in each day that someone else (the markets) pay for.

In the last week of each month WhichWayToday run a two day workshop. Here the emphasis is on quickly explaining the various setups and applying them to real markets WHEN the market is open.

The setups are simple, but unique. They are taught in an open and friendly environment by two excellent speakers who trade each day themselves. Although many setups are taught the aspiring trader just needs one to be successful. Each seminar student is allowed to repeat the seminar at a nominal cost if it is required.

In summary the WhichWayToday seminar teaches the setups and techniques necessary for success in short term trading. The WhichWayToday live trading room shows how to apply these techniques each and every morning as the market is moving. It is an unequalled learning experienced.



One Way of Surviving All Market Conditions

Trading for Sure Profits

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Rule-based discretionary traders are among the best traders on this planet. The trading strategy explained here is a rule-based discretionary system. Similarly, the fact that the majority of traders fail does not mean that trading is a dead end activity. Traders who are successful prove otherwise. Occasional losses leading to transient drawdowns are inevitable but not insurmountable challenges in trading. The secret to success lies in developing a deep love for trading and a willingness to apply trading principles that work. Trading principles that work are non-market specific. For a strategy to survive all market conditions, it must have three ingredients incorporated into it: aborting losers and capitalizing on winners, very low risk, and rock-solid discipline. These are the secrets of trading masters – trading success has nothing to do with your ability to predict the markets accurately. If you give yourself a sensible reward-to-risk ratio, you will survive the markets in the long run. For instance, it does not make sense to risk \$20 in an effort to gain \$2. These secrets are what make the difference between financial freedom and financial disaster – the difference between solvency and bankruptcy.



Mustapha Azeez

Mustapha Azeez is a professional Forex trader, Forex signals strategist, funds manager, researcher and coach. He is a senior analyst at FX Instructor, LLC. He is also a content contributor at Fxstreet.com, plus his numerous articles are posted at Forexpeacearmy.com, Ituglobal-forex.com, Trade2win.com, and Elitetrader.com.

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The Pedigree of a Good Strategy

It is very disturbing that so many traders find it difficult to survive on the markets. Many top market speculators are perplexed by a new generation of traders who do not seem to have a clue about the skills necessary to preserve their trading portfolios. The issue is: even if you are disciplined, it would be difficult for you to survive with a worse expectancy system, i.e. a system whose risk is greater than the reward. And checking complex data ad infinitum is not so sensible for simple markets either. Good trading strategies are the ones that survive all market conditions. This kind of strategy must be effective in sustaining minimal drawdowns when the market conditions are not favorable – while making a decent profit during favorable market conditions. Whether a strategy is trend-following or counter-

trend or scalping, it will survive all market conditions provided that those simple but effective principles are incorporated into it. The markets eventually reward those who show an earnest quest for trading mastery.

The trading strategy described in this article is very good for all market conditions. This strategy is useful for gaining some pips during trending and volatile markets. It can take advantage of breakouts, while sustaining easily tolerable drawdowns in very bad and choppy sideways markets. The worst drawdown so far was four per cent (despite many losses in a row), and this is easily recoverable. This strategy is very simple to use and it would make life easier for you. The ability to survive has been proven, especially considering the recent difficult market conditions. An average of 50 pips per trade is taken; sometimes only 30 pips are taken in order to prevent a

T1) Breakdown of the Strategy

Timeframe:	30-minute charts
Trading style:	Short-term
Indicators parameters:	EMA period 21 & ADX period 14
Buy rule:	Buy when price closes above the EMA, and +DI has just crossed –DI to the upside.
Sell Rule:	Sell when price closes below the EMA, and –DI has just crossed +DI to the upside.
Position sizing:	0.01 lots for each \$500 (thus making it 0.1 lots for \$5000)
Stop loss:	30 pips
Take profit:	50 pips
Trailing stop:	Optional
Risk per trade:	0.6%
Potential reward per trade:	1%
Max. weekly drawdown:	3%
Safety rule:	Trading is stopped for the week if drawdown reaches 3%
Filter rule:	You may not enter a position if the ADX line itself is above 35 or below 20
Instruments names:	AUDUSD, EURUSD, GBPUSD, USDCHF, USDCAD, GBPUSD, EURJPY and EURGBP
Average orders per week:	35-55
Orders type:	Mostly pending orders
Signals generation periods:	4-9 am GMT, 12-3 pm GMT, and 10 pm - 12 am GMT

profitable trade from turning into a losing trade. Losses are limited in that they are not allowed to run (they are truncated). But it is no Golden Goose strategy, because if you do not follow the rules that are revealed below, it may not work for you.

Strategy Parameters

In Table 1 you see a breakdown of the strategy. One problem with this strategy is that it is easy to miss many trading signals if you are away from your PC. It has the problem of generating 'too many signals' per week, since more trades don't necessarily mean more profits. Late signals

should not be traded. Although good signals can be missed quickly, other signals will soon form. Certain signals would therefore need to be cherry-picked. You may also have noted that pending orders are mainly used for this strategy. This does not mean that instant execution of orders is useless. If you want to enter some orders instantly, it should not be more than 20 per cent of the total orders, while the remaining orders would be 80 per cent pending. Pending orders, apart from filtering potentially bad trades, prevent the intraday trader from chasing the markets. There is also a benefit of allowing

beneficiaries enough time to enter orders before live trading takes place. Also take special note of the safety rule: If you have accumulated a profit of 20 per cent over time, you may stop trading in the week that your profit is reduced to 17 per cent. This ensures that you avoid further drawdown in a bad week. But as long as there are winnings, trading continues in a week.

Effects on Other Timeframes

This strategy was originally designed to be used on 30-minute charts, but it can also work on higher timeframes. For those who may want to try the

strategy on higher timeframes, say hourly charts or 4-hour charts, there is a need to increase the amount of pips at stake while also increasing the amount of pips targeted. If you would like to experiment with a higher timeframe other than 30 minutes, you are advised to practice consistently for at least two months. You might even come out with your own modified rules. But I do not think that the inclusion of additional indicators can improve the trading results – it may even make things harder while useful trading setups are unnecessarily constrained. After consistent practice, the system

could make you feel as though you are playing some electronics games. Trading should be made as simple as possible. The simpler an effective trading system is, the easier the life for the trader.

I personally try to have as much fun as possible while trading (my trainees and clients are aware of this). Once you know the truth about trading, you have taken a giant leap forward in your personal evolution as a trader. Few things would be more fascinating than making some profit while trading as if playing Nintendo games. You need to know that you are

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playing the game of speculation in order to survive in the long run and come home with some profit – not because you want to impress your sweetheart with huge profits.

Trade Examples

There is a need to show some trading examples from recent movements of prices. For the sake of simplicity and clarity, four examples are shown. Three examples are of winning trades, and the last example would be of a losing trade. The second example explains how profit is made when prices decline, whereas the third example shows how a winning trade could be prevented from becoming a losing trade. Each example has a purpose. On the accompanying charts, the

red line along the price is the EMA. The ADX is below. Its green line stands for the ADX line, the blue line stands for the +DI line and the red line stands for the -DI line. On the charts, the first vertical red line shows where a trade is entered while the second vertical line shows where it is exited.

Example 1

In Figure 1 the EURUSD closed above the Exponential Moving Average. The ADX +DI crossed its -DI counterpart northwards, and the Buy Stop order was placed around ten pips above the current price. Please note that the ADX line showed that the strength of the current trend was in the middle of our optimised parameters. The trade was profitable.

The Tools Used

The trading tools used to determine when to enter and exit are the EMA (Exponential Moving Average) and the ADX (Average Directional Movement Index).

The simplest way to spot a trend is to use the EMA. As the name suggests, this is simply the average closing price of a given pair over a specified period of time. The rule is that when the next price closes above its Moving Average it is in a positive trend and vice versa. Moving averages are trend following indicators. As such, they will only work well in trending markets – not when the market is trapped in a trading range.

The ADX is an oscillator which is good for determining the direction of the trend, as well as the strength of the trend. It also acts as a good filter for potentially bad trades. The ADX plots a positive DI line (+DI) measuring buying pressure and a negative DI line (-DI) measuring selling pressure. The simplest way of using this information is to take the cross as the signal to trade, so that when +DI goes above -DI traders should go long and when it drops back below they should switch to a short position. Generally a reading below 20 suggests a trendless market while a reading above 30 shows a considerable trend.

Instrument: EURUSD

Order: Buy Stop

Entry date: December 29, 2010

Entry price: 1.3170

Initial stop: 1.3140

Exit date: December 29, 2010

Exit price: 1.3220

Profit/loss: 50 pips

Example 2

In Figure 2 the USDCHF was winding its way down. An opportunity to enter a short-term 'sell' signal emerged when the price closed below the EMA and the -DI moved above the +DI.

Instrument: USDCHF

Order: Sell Stop

Entry date: December 29, 2010

Entry price: 0.9470

Initial stop: 0.9500

Exit date: December 30, 2010

Exit price: 0.9420

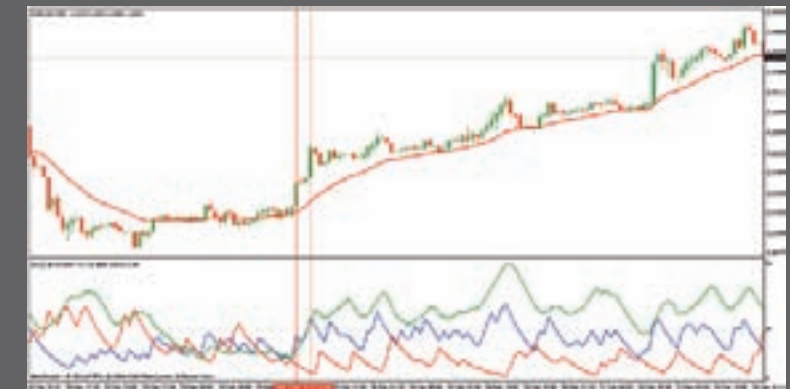
Profit/loss: 50 pips

By the way, recently the Swiss Franc proved to be too strong for the Greenback. Occasional losses in the bearish momentum were invariably an opportunity for a smart market speculator to go short. It is one way of selling a rally in price. This is much better than any game you would ever play in Las Vegas. Indeed, you can make money both in bull and bear markets.

Example 3

Figure 3 shows an interesting example of how a profitable trade

F1) Bullish EURUSD, 30-Minute Chart



The EURUSD closes above the moving average. The ADX +DI crossed its -DI counterpart to the upside, and the Buy Stop order was placed around ten pips above the current price. The trade was profitable.

Source: www.metaquotes.net

F2) USDCHF in Bearish Momentum



An opportunity to enter a short-term 'sell' trade emerged when the price closed below the EMA and the -DI moved above the +DI. Recently the Swiss Franc proved to be too strong for the Greenback: occasional losses in the bearish momentum were invariably an opportunity for a smart market speculator to go short.

Source: www.metaquotes.net

can reverse; trying to turn into a loss, and how this might be handled. The entry criteria were met and a long position was opened; with a nice profit. But the price retraced before the 50-pip target was hit. The retracement took the price from over 40 pips to around 30 pips, and therefore the position was exited quickly at 30 pips. Not that bad. Here, the proper use of a Trailing Stop could also handle this typical scenario, because the price can turn more quickly than the trader may have envisaged. During my novice years, it was not uncommon for me to sprint from my trading room into the toilet

whenever this 'crazy' pair showed me its true color. You should not call yourself a hero until you have faced the fiercest of battles and survived them all.

Instrument: GBPUSD
Order: Buy (instant execution)
Entry date: December 20, 2010
Entry price: 1.5530
Initial stop: 1.5500
Exit date: December 20, 2010
Exit price: 1.5560
Profit/loss: 30 pips

Example 4:
 Figure 4 depicts a losing trade. A 'sell' order was opened, but the price soon reversed and

eventually hit the stop. Please note that this losing trade occurred after a small gap down in the price. This is really interesting! Losing trades are a blessing in disguise; they have made me become the type of trader I wanted to be.

Instrument: EUR/GBP
Order: Sell Stop
Entry date: December 13, 2010
Entry price: 0.8355
Initial stop: 0.8385
Exit date: December 13, 2010
Exit price: 0.8385
Profit/loss: -30 pips

Conclusion

As you can see, it is mandatory for you to stick to the strategy rules, no matter what. By doing this, you can move ahead regardless of a few certain transitory losing trades. A period of losses can be an unnerving event.

However, having realistic expectations, while using good risk management technique may help you get through it better. But more importantly than that, you can always look forward to times when the markets conditions are favourable to you, and you will be so happy that you are trading.



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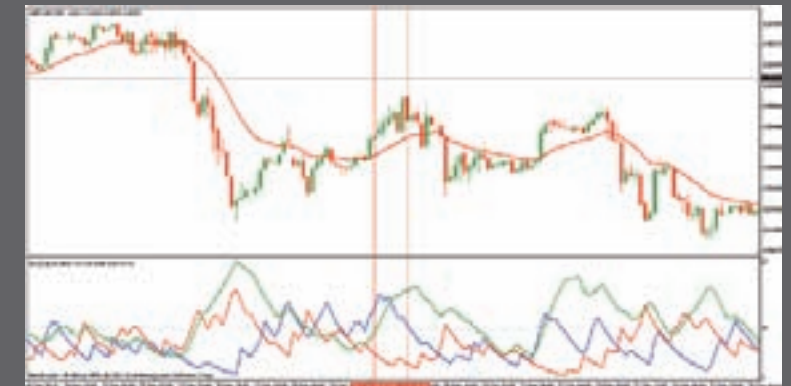
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F3) GBPUSD Moved Up but Reversed Quickly



On this chart, the trade was prevented from turning into a loser with an ultimate win to loss ratio of 1:1. The entry criteria were met and a long position was opened; with a nice profit. But the price retraced before the 50-pip target was hit. The retracement took the price from over 40 pips to around 30 pips, and therefore the position was exited quickly at 30 pips.

Source: www.metaquotes.net

F4) EURGBP, an Example of a Losing Trade



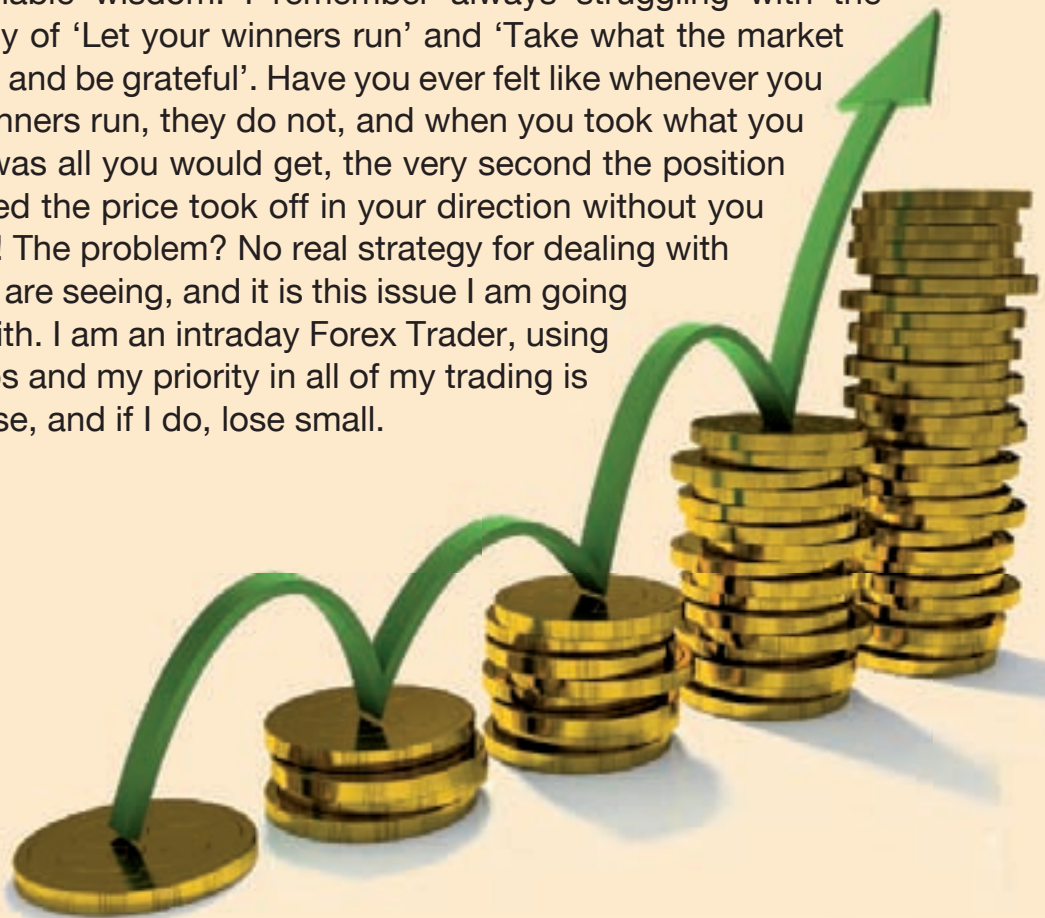
This example of a losing trade was on EURGBP. A 'sell' order was opened, but the price soon rallied and eventually hit the stop. Please note that this losing trade occurred after a small gap down in the price. Losing trades are a blessing in disguise.

Source: www.metaquotes.net

Identifying High Probability Turning Points in Pullbacks

Getting the Intraday Trend

The trend is your friend... till the bend at the end! In trading there are so many well quoted phrases, all designed to suit a particular market occurrence. The problem for all of us is to identify when to apply that single piece of undeniable wisdom. I remember always struggling with the dichotomy of 'Let your winners run' and 'Take what the market gives you and be grateful'. Have you ever felt like whenever you let the winners run, they do not, and when you took what you thought was all you would get, the very second the position was closed the price took off in your direction without you on board! The problem? No real strategy for dealing with what you are seeing, and it is this issue I am going to deal with. I am an intraday Forex Trader, using tight stops and my priority in all of my trading is do not lose, and if I do, lose small.



The Strategy

Capturing an intraday trend requires the buying of pullbacks in an uptrend or selling them in a down trend. Identifying the turning point at the end of the pullback is the difficult part, and if not identified accurately will result in losers or excessive risk at entry. If you cannot find a good high probability entry but are confident of the trend, you will probably take a large stop risk to 'let the trade breath'. Trading intraday means taking small momentum based moves which you can live on, whilst seeking to stay in a move which gains strength and momentum. Therefore the risk needs to encompass the smaller higher probability move and not hope for a bigger move! You can also use this strategy to add to a position in the trend. Trading EUR/USD I would use a seven pip stop or less with a target of 30 pips.

The strategy uses two momentum indicators simultaneously on a 5 minute chart, not something normally recommended as they are likely to show the same thing in Overbought or Oversold terms,

and therefore acting in unison. This is primarily because most of these indicators use a measure of current price strength and compare previous periods of price averages. The greater the differential in the latest close to the average, however calculated, creates a stronger movement in the indicator.

Use a Slow Stochastic with the settings of 5,2,4. The slow stochastic is created using the original fast stochastic calculation and smoothing it. By changing the observation periods to 5, this results in the emphasis being placed upon the recent price action and therefore the momentum in the pullback. The %K line in the original fast stochastic calculation is smoothed with a simple moving average (SMA) to produce the %K line in the slow stochastic (this is in fact the %D in the fast stochastic) and this is further smoothed with another SMA to produce the %D line. By using the 5,2,4 settings the fast %K is given a 2 SMA to produce the slow stochastic %K and this is given a 4 SMA to produce the %D. In this strategy only the

%D is used as it is the position and structure of this line that is important.

Simultaneously using the RSI (Relative Strength Index) can give you a fixed signal point. Traditionally the 30 per cent and 70 per cent areas of the RSI are used as indications of oversold and overbought respectively. In this strategy the 30 and 70 are not used and instead a line is placed at the 50 per cent as this will be the signal point.

Using the Set up

Using the example of a trend move up on the 5 minute chart, after a period of consolidation or downward movement, we will see the RSI starting from a low area into a high area and the stochastic %D moving into the high area and probably remaining there through some cycles. See the highlighted areas in Figure 1. This indicates a trend with some momentum and one that will be of interest. When the pullback occurs this will cause the RSI to turn down towards the 50 per cent line and the Stochastic to turn and head lower, indicating momentum direction is changing.



Steve Beaumont

Steve Beaumont was trained by Online Trading Academy beginning in September 2006. He has studied Stocks, Forex and Futures and utilised many of the Academy's extensive support programs. He opened his first trading account in March 2007 and produced astonishing results. Since March 2008 he has lived off of his trading and joined Online Trading Academy as an instructor.

You now need to look for three things:

1. A point of resistance in the up move that was significant, that may become a support area (significant will be explained later).
2. The RSI to be at or near the 50 per cent line.
3. The Stochastic in its low area about to turn up but not at an extreme.

This indicates the potential to join the existing trend, and a trade should be taken. It is important at this point in any strategy that you consider what the ideal picture would like. It should be so good that you would not hesitate to take the trade! Once that is done rules can be written around the use of the strategy to ensure only high probability trades are taken consistently, and therefore the statistical analysis of results is accurate and objective. The best case scenario for this strategy based upon EURUSD is as follows:

1. Daily chart showing a trend with the probability of continuation.
2. Intraday movement at London open (7am London, Midday New York) starts intraday trend in direction of daily trend.
3. Stochastic shows strong momentum with trend, being

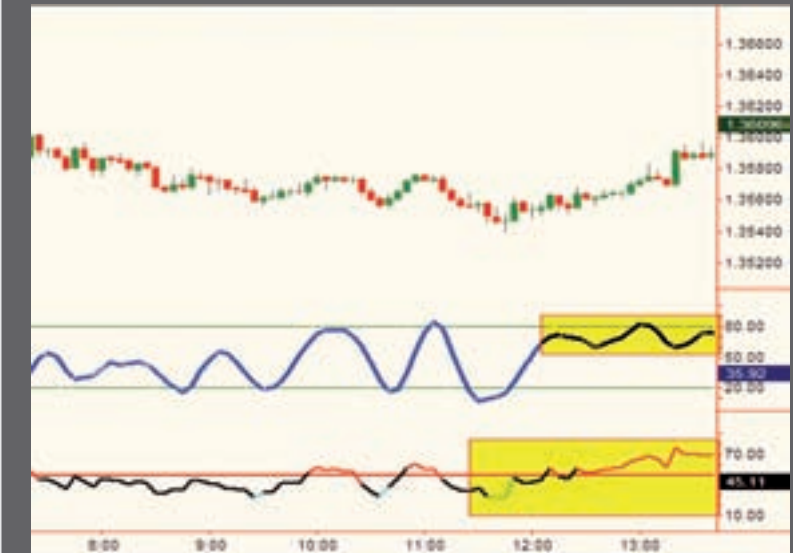
biased toward the high range in an uptrend or low range in downtrend.

4. RSI moves from one end of range to the other with trend momentum.
5. The intraday trend hesitates at a known area of Support or Resistance, which when breached shows a significant increase in speed of price change.
6. Pullback identified after the breach, with Stochastic and RSI reversing.
7. Pullback reaches level identified in No 4 above, with Stochastic reversing to opposite level and RSI at 50 per cent.

In the example Figure 2, three potential trades are shown;

T1 (Trade 1): After a sell off in the Asian session the move into the London open was going with the daily trend, with a hesitation at 1.3490 a previous area of resistance, which once breached was followed by a faster change in price. The pullback consisted of a slower decline in price, to the identified level at 1.3490. The RSI had reached 50 per cent, and the Stochastic was declining but had only reached the halfway, significantly the 50 EMA (Exponential Moving Average) was also at the support level. To summarise, this set up looks good, but ideally the stochastic

F1) The Transition into a Potential Trend



After a slow sell off in the Asian session, price begins to resume the uptrend. The stochastic moves to its upper area and remains there through two cycles, the RSI begins in its low area and climbs steadily into the higher area showing continued strength (highlighted areas).

Source: www.tradestation.com

F2) Three Potential Trades



These trades with potential have differing characteristics, identifying the best trade and defining rules to capture these will increase profitability.

Source: www.tradestation.com

would have been lower. Total range from low to high before next pullback = 43 pips. Duration 15 minutes.

T2: After the first pullback price rallied strongly initially, but then consolidated, before declining again. The pullback reached slightly above 1.3490, using the upper line confirmed as a small range of hesitation previously at around 5am London. The RSI has returned to the 50 per cent, and the stochastic is now more than halfway back and has started to turn. Again the 50 EMA is acting as another support. This set up looks better than T1, with better fulfilment of the 'ideal' image. Total range from low to high before next pullback = 63 pips. Duration 20 minutes.

T3: From around 9am, the energy in the trend starts to decline, however a pullback again to a previous area of resistance and the 50 EMA, with the stochastic in its low area gives the potential for a trade. The RSI has breached the 50 per cent line and this with the stochastic being so low it shows that the potential for the momentum to change direction exists. Subsequently, a period of consolidation occurs with no real direction showing its hand; equilibrium in the buy and sell activity is occurring.

The Ideal Set up

In Figure 3 you can see which trades became an ideal set up.

T1: A steady slow decline in price through the London session is against the Daily trend, and eventually strength is then seen just prior to the New York session opening, and some consolidation leading into the NYSE opening at 2.30pm London. The price pulls back to a known resistance area and the 50 EMA. The RSI has come from a low area to a high area and back to 50 per cent, with the stochastic just below halfway. This now looks like our ideal, and the trade potential is good. Total range from low to high before next pullback = 78 pips. Duration 25 minutes.

T2: The price has rallied from the London session nearly 140 pips and a pullback is likely, and it is late in the afternoon or lunchtime in New York. The price has returned to a known previous resistance area but not the 50EMA, the stochastic is very low and the RSI has breached the 50 per cent line, the potential for the momentum to change direction now exists. This is followed by a weak upward move followed by a stronger lower low down move.

The Trade

Using the example trades shown, we are using a previously identified

area as the potential for a pullback to return to. If our rules state that it must come to this point before we consider a trade, then that logically should be our entry. For an intraday momentum trade, the target of 20 per cent of the Average Daily Range is a good benchmark, and you could use a 100 period ATR (Average True Range) on the daily chart to measure this. By using 100 periods a smoothing of volatile weeks and holiday periods occurs, giving a more reliable average (see Figure 4). Currently this would give a measure of 160 pips, so our initial target would be 32 pips. Using a 1:3, Risk/Reward ratio a maximum stop of ten pips including spread would be used. The target of 30 pips was achievable in all of the identified 'ideal' set up trades, and the ten pip stop was never threatened.

Conclusion

Taking things forward, you could apply this strategy to your 5 minute chart in the background of your normal trading and monitor the results. It will not produce numerous signals but will however produce, when using the criteria, a number of reliable signals. If you are swing trading, this strategy could be used to add to a profitable position by finding an accurate entry.



F3) The Ideal Set up



The first trade meets all required criteria and results in capturing a strong move. The second potential trade outcome demonstrates the need to wait for the ideal.

Source: www.tradestation.com

F4) Average Daily Range



Taking this strategy further, you could use a two part position, taking profit on the first part at the 30 pip target and allowing the remainder of the position to run. Exit strategies could utilise the 5 minute chart, raising the exit stop to the low of each pull back, thus generating greater reward sacrificing the pullback reward at exit. Remember that the second part of the position must have the 30 pips locked in to preserve good entry risk/reward criteria!

Source: www.tradestation.com

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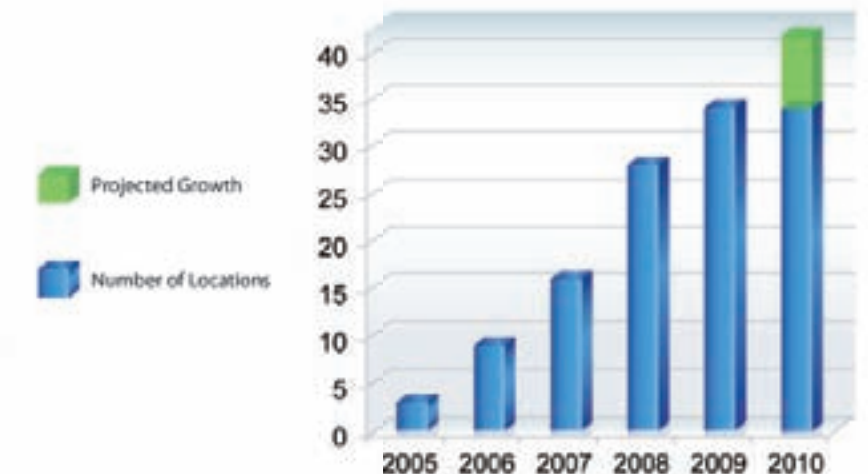
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NASDAQ Ultrashares and Ultrashort ETFs

ETF Swing Trading

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In this article we investigate a strategy based on swing trades that take advantage of a new breed of ETFs: the leveraged ETFs. We will explore swing trading with long and short entry opportunities using the NASDAQ Ultrashares (QLD) and the NASDAQ Ultrashorts (QID); and will compare its return performance versus a passive buy-and-hold strategy using the benchmark index QQQQ (NASDAQ-100 ETF).



Fabio De Castro

Fabio De Castro, an engineer with an MBA, teaches Investments at Webster University in Geneva. He has been an independent trader since 2004 with particular interest in the US financial markets and special focus on options trading strategies and ETFs.
Contact: itrader.fab@gmail.com

Traders are always looking for new and creative ways to beat the passive buy-and-hold (BAH) trading strategies usually applied to benchmark indexes such as the S&P 500. The typical strategy used to time the market is swing trading. It employs a set of objective rules defined by technical analysis for buying and selling decisions on stocks and/or indexes. It allows a trader to identify the best conditions to enter (and also to exit) positions because these rules are intended to eliminate the subjectivity, emotional aspects, and labour intensive analysis. These trading systems are usually rooted in combinations of price trend indicators (e.g. Moving Average, Bollinger Bands, and others); price oscillators (e.g. MACD, Stochastics, RSI and others) to identify high probability trades in a predefined timeframe.

In this article, we will analyse and compare the risk and return when applying swing trading that would take advantage of long and short trading signals versus a traditional BAH strategy during a period of three years –

from December 2007 to end of November 2010.

This is an interesting timeframe to analyse due to the increased volatility seen in the markets. And because volatility is an important aspect that favourable to swing trades, this strategy backtest will be conducted on the NASDAQ-100 index and their leveraged ETFs (QLD and QID).

Logic of the Swing Trading System on the Leveraged ETFs

The swing trading strategy adopted in this example will be simple and straightforward. We suggest using the price ratio between the two NASDAQ leveraged ETFs – QLD and QID; and the trigger signal for long and short entry positions will be given by the simple moving average of this price ratio. This will be explained in further detail later.

This strategy works better when the price momentum emerges after the trigger signal, i.e. when a price trend takes place over a certain period of time. The longer the better. On the other hand, range bound prices can trigger false trade signals that can

increase losses – increased by the transaction costs. This turns out to be the major weakness of any swing trading strategy.

The Trading Vehicles

As mentioned above the swing trading strategy will adopt the leveraged ETFs on the NASDAQ-100 (symbol: QQQQ). So, let us introduce them to understand how they work in terms of price action:

- QLD (ETF NASDAQ Ultrashares x 2): This leveraged ETF

moves twice the QQQQ price move. For each one US\$ price upmove on the QQQQ, the QLD will gain \$2; and vice-versa when QQQQ moves one US\$ down. Thus, it provides a leveraged double performance on bullish trend moves of the NASDAQ-100.

- QID (ETF NASDAQ Ultrashort x 2): This leveraged inverse ETF moves two US\$ up for each one US\$ down on the QQQQ price. Thus, it provides a higher performance when the NASDAQ-100 shows

Strategy Snapshot

Strategy name:	Swing Trading on Leveraged NASDAQ ETFs
Strategy Type:	Indicator based; Simple Moving Average of QLD:QID price ratio
Trade Horizon:	Based on the weekly chart
Setup:	QLD:QID price ratio crossover of its ten week SMA generates the confirmation signals
Entry/Exit:	When the QLD:QID price ratio crosses above its ten week SMA it triggers a buy signal on QLD and a simultaneous sell signal on QID; and when it crosses below its ten week SMA a sell signal confirmation on QLD and a simultaneous buy signal confirmation on QID are triggered.
Stop-Loss:	None
Risk and Money Management:	Allocation of a fixed amount of capital per trade (\$100,000 used in this example)
Average Number of Signals:	Six per year
Profit to Loss ratio:	2.4:1

bearish price trends. It is like playing short trades on the NASDAQ-100 with a leveraged effect 2:1.

Furthermore, instead of following the price action of each leveraged ETF independently and looking for entry and exit signals on bullish and bearish trends, the idea here is to create a “ratio” of QLD:QID prices. Explained in more detail in the trading rules below.

Since all trading strategies need a parameter for comparison to analyse and to validate their results, the one chosen here will be the NASDAQ-100 benchmark (QQQQ).

The Swing Trading Rules: How It Works

1. The pricing dashboard is the price ratio QLD:QID using weekly data. The objective is to detect the major trade signals instead of using daily signals where a larger number of trade signals are more frequently obtained; and then generating a higher number of bad or false signals.
2. The trading signal indicator is the ten week Simple Moving Average of the QLD:QID ratio of prices. The confirmation signal

appears when the crossover of the QLD:QID ratio price above or below their ten weeks SMA occurs; triggering at the same time the buy and sell signals of each leveraged ETF (QLD and QID).

Let us see in Figure 1 how it works. Every time the QLD:QID ratio price cross “above” the ten weeks SMA, a buy signal on QLD

always be one, and only one position, in place with either QLD or QID after each confirmation signal. Trades are held until the next crossover signal of the QLD:QID price ratio is confirmed on its ten week SMA.

The trade execution after each confirmation signal is done on Mondays (using the opening prices of QLD and QID) due the fact the system uses a weekly moving average of price. The blue arrows in Figure 1 display all trade entries.

The initial investment capital considered for this exercise is \$100,000 to facilitate the comparisons. It is important to stress

that the swing trading system takes into account a constant amount of \$100,000 for each position purchased, and this is done in this matter to reduce the risk of important impact of losses on compounded capital. Please refer to the comments of this capital allocation decision on the summary of this article.

Strategy Performance Analysis

Figure 2 summarises the comparative returns between the swing trading strategy using QLD and QID versus the buy-and-hold strategy with the benchmark,

“Swing trading presented a much higher cumulative return over three years.”

(the bullish leveraged ETF) is triggered. A blue arrow pointing up in the chart will help the reader to identify these bullish entry signals on the price ratio chart.

On the other hand, a QLD:QID ratio price crossover “below” the ten weeks SMA will trigger a buy signal on QID (the bearish ETF).

In the case of a trade already being in place with one of these two ETFs, the triggered buy signal in one of them will translate into an instantaneous sell signal on the other one; which means, a trade shift from QLD to QID or vice-versa. Hence, there will

F1) Weekly Chart of the QLD:QID Price Ratio



This is a three years chart, from December 2007 to December 2010. The blue line represents the ten week moving average of the ratio QLD:QID. The blue arrows indicate the trades' trigger. The horizontal blue line indicates the ratio parity (QLD:QID = 1.00). The horizontal green line (QLD:QID = 2.50) shows the key level of support and resistance during the period.

Source: www.stockcharts.com

F2) Cumulative Return QLD/QID vs. QQQQ

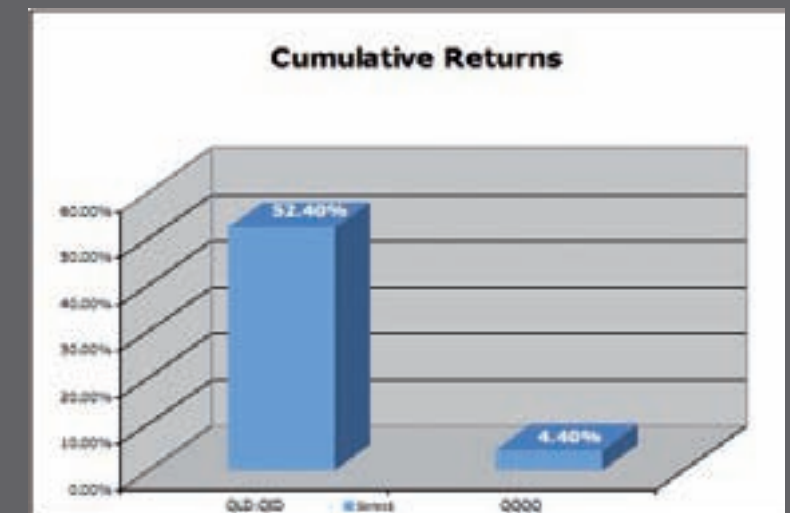


Figure 2 shows the comparison of the cumulative return on the initial capital investment over three years.

Source: Microsoft Excel

QQQQ. Swing trading presented a much higher cumulative return over three years (+52.4 per cent) versus the benchmark (only +4.4 per cent).

In Table 1 the reader can see that the swing strategy has triggered a total of 19 trades over three years, with a breakdown of around 50 per cent of trades on each leveraged ETF. However, QLD has produced a much better winner to loser trade rate versus the ultrashort ETF QID resulting at the end in a higher contribution to the final return of this strategy. In addition, when comparing levels of risk between the swing strategy to the BAH on the benchmark QQQQ measured by the drawdown (the peak-to-trough decline during the period of investment); the swing trading presented 22.5 per cent vs. 41 per cent of the benchmark.

On the chart of the comparative equity curves between the swing strategy and the BAH of the benchmark index QQQQ – please refer to Figure 3 – we can observe the dominance of returns displayed by the QLD/QID from December 2007 up to end of November 2010. This strategy outperformed the buy-and-hold from the beginning. The two major market corrections which occurred in 2008 triggered buy signals on the ultrashort NASDAQ ETF (QID) which resulted in immediate positive returns for the swing strategy – please refer to

Figure 1 and look at the “first” and “third” arrows pointing down.

At the same time, the benchmark QQQQ down move caused constant losses to its investment equity. Also interesting to point out is that at the lowest point of this massive market correction occurred in March 2009, the equity curve of QLD/QID swing trading reached \$117,113 (+17.1 per cent) versus \$56,641 (-43.4 per cent) for the QQQQ; i.e. a very respectable 60 per cent investment return difference between them – please refer to Figure 3.

And as a final point, we could illustrate how two potential investors following each of these strategies could have experienced different levels of stress brought on by the high level of uncertainty dictated by these volatile times. The swing trader would have seen his or her equity curve in the positive territory since the beginning while the BAH investors would have stayed on the opposite side of returns – under water – until December 2010; and above all, sitting tight trying not sell his or her position when the investment equity was dropping month after month from the end of 2008 to March 2009.

Final Comments and Conclusions

Using a timing system with leveraged and inverse ETFs of

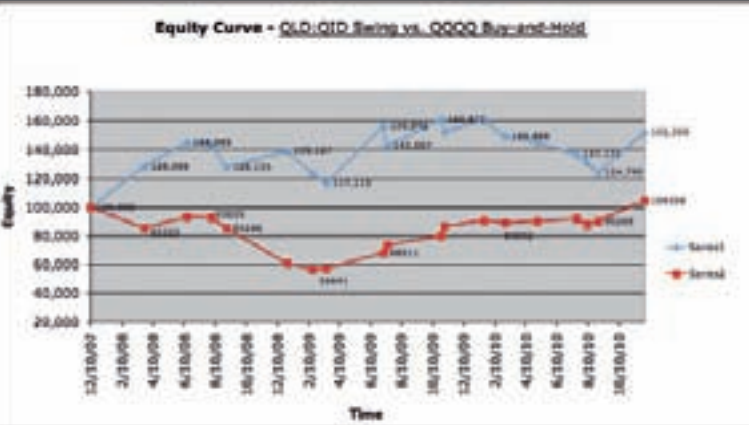
the NASDAQ resulted in bringing solid positive returns over the three year period. Unfortunately we are not able to confirm whether or not the same strategy would have the ability to provide the same good returns over a longer period of time because these two leveraged ETFs have only been available for traders since December 2007.

Swing trading strategies have a higher probability of outperforming the BAH ones in periods in which market volatility becomes important and large amplitudes of price swings are present. Swing trading provided in this example, a way to profit from rising and falling markets while the BAH strategy could be seriously damaged during bear markets.

In conclusion, backtesting swing trading strategies – along with their set of rules – turns out to be an essential exercise for traders, allowing them to check the strategy strengths and weaknesses in different market conditions in the past. And above all, to provide the necessary confidence and discipline to follow the trading rules while reducing the effect of emotions when making the trade decisions.



F3) Equity Curve QLD/QID vs. QQQQ



This graphic shows the comparative performance between the QLD:QID swing trading strategy on the equity curve of \$100,000 (blue line) versus the buy-and-hold strategy using the QQQQ benchmark (red line). From December 2007 to December 2010.

Source: Microsoft Excel

T1) Overview QLD/QID vs. QQQQ

	Total Trades	Winners/Loosers	Maxi Drawdown	CAGR*
QLD : QID	19	7/12 (13% / 63%)	22.5%	+ 15,2%
QID	9	2/7 (29% / 71%)		
QLD	10	5/5 (50%/50%)		
QQQQ bench-mark	-	-	41%	+1.2%

This table shows the number of trades occurred during the three years, with the number of winner and loser trades by leveraged ETF (QLD and QID). Also, the maximum drawdown of the swing strategy compared to the BAH using the benchmark QQQQ. (*CAGR: Cumulative Annual Growth Return)



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A Successful Position Trading Approach

Buy like a Trader and Hold like an Investor

Judging from the trading platform providers' marketing literature, you would think that a spread betting account, Contracts for Difference (CFD), or other trading account obliges you to engage in the rapid day trading of four-digit indices, commodities and forex currency pairs. There is no place in a trading account for holding a diverse set of individual equity positions in the form of a longer-term portfolio. Or is there? If we take spread betting as an example, there is actually nothing inherent in spread betting that mandates it as a vehicle for short-term trading. It is possible to run a portfolio of spread bets with a longer term perspective using the trading-cum-investing approach known as position trading.

What Is Position Trading?

Definitions of position trading vary, but a good working definition for the purposes of this article would be: Establishing a portfolio comprising a diverse set of competing equity positions which are bought like a trader (with a view of letting go quickly if they perform badly) and held like an investor (maybe even 'forever' if they perform well).

You can think of a position trading portfolio as a long distance horse race in which the various runners and riders jostle for position. But in this horse race you can:

- Place bets on any or all of the racers.
- Alter those bets at any time during the race, increasing your stakes on those racers that are running ahead of the pack.
- Take back some or all of your stakes from those racers that are falling behind.

Buy like a Trader and Hold like an Investor

Successful position trading is not analogous with the investors' preferred "Long-Term Buy and Hold" or (even worse) "Long-Term Buy and Forget" philosophies. If

one of your exploratory positions performs badly, you will not be shy of letting it go with the help of a tight initial stop order, and you will not lose too much money thanks to your small initial position size. Make a note of this stock and its last stop-out price, with a view to buying in again in the future if – and only if – you can do so at a lower price.

You will hold on to any positions that perform well and will trail your stop orders cautiously, trying not to get stopped out of a profitable position. Along the way you might increase your stakes by pyramiding your successful positions, and – just like an 'investor' – you will collect dividends which may go some way to offsetting the overnight financing charges on your 'rolling' spread bets. When a profitable position eventually stops out, note its stop-out price with a view to buying in again at a lower price and with your smaller exploratory position size.

The Seven Pillars of Position Trading

Some traders and most if not all investors tend to think it is all about stock picking. While

clever stock picking is important to you as a position trader, it will not save you if you have not first mastered the essential arts of money and risk management. So in addition to stock picking, the other six pillars of an effective position trading strategy are:

- Diversification; which allows you to spread your risk across instruments and over time, so that no single bad trade or price gap can wipe you out.
- Stop Orders; which allow you to cut your losses or (even better) to lock-in your profits without crystallising them prematurely.
- Position Sizing; which ensures that you do not risk too much money too soon on positions that may not perform well.
- Pyramiding; which helps you ‘back the winners’ rather than averaging down the losers.
- Leverage; which provides greater scope for diversification, even in a small account, and which allows you to make big gains from small stakes.
- Dividends; which can help offset overnight financing charges on rolling spread bets.

Example Position Trade
Table 1 shows the progress of an example position-trade in Severfield-Rowen that you could have run over the five months between 28 August 2010

and 17 January 2011; and the corresponding price chart for the period is given in Figure 1.

An initial £1-per-point position was established at a price of 203.1 on 28 August 2010, with a potential profit of -£17.10 (i.e. a loss) locked-in by a stop order at 186. The stop order was raised gradually so as to lock in a profit of £25.90 by 28 October 2010. On 29 October an additional £1-per-point stake was pyramided

into the position thus reducing the secured profit – but note, still a profit – down to £16.10. Thereafter, the stop orders on both stakes were raised gradually so as to secure a combined locked-in profit of £136.10 by 20 December 2010. On 24 December 2010 some profit was taken off the table by banking the £65.80 generated by the second pyramided position, and by 17 January 2011 the original position

has stopped out for an additional banked profit of £95.90.

Having stopped out entirely at a price of 299 on 17 January, you could have begun the whole cycle again by re-purchasing at the massively gapped-down price of 215 on 27 January – with the exploratory £1-per-point initial position size and a tight stop order, of course. You should note that this example ignores the bid-ask spread which would



Tony Loton

Tony Loton is a prolific private trader and writer, and author of the book “Position Trading” (Second Edition), published by LOTONtech.

T1) Position Trade in Severfield-Rowen						
Date	Transaction	Price	Position Size	Stop	Locked-In Profit	Banked Profit
28.08.10	Buy £1-per-point	203.1	1	186	-17.1	
20.10.10	Raise stop to 190		1	190	-13.1	
21.10.10	Raise stop to 204		1	194	-9.1	
25.10.10	Raise stop to 208		1	208	4.9	
26.10.10	Raise stop to 215		1	215	11.9	
27.10.10	Raise stop to 219		1	219	15.9	
28.10.10	Raise stop to 229		1	229	25.9	
29.10.10	Buy £1-per-point	238.8	2	229	16.1	
11.11.10	Raise stop to 234		2	234	26.1	
18.11.10	Raise stop to 239		2	239	36.1	
24.11.10	Raise stop to 241		2	242	42.1	
30.11.10	Raise stop to 245		2	245	48.1	
06.12.10	Raise stop to 249		2	249	56.1	
08.12.10	Raise stop to 257		2	257	72.1	
14.12.10	Raise stop to 276		2	276	110.1	
20.12.10	Raise stop to 289		2	289	136.1	
24.12.10	Sell £1-per-point	304.6	1	289	85.9	65.8
10.01.10	Raise stop to 292		1	292	88.9	
12.01.10	Raise stop to 299		1	299	95.9	
17.01.10	STOP OUT		0	299	95.9	95.9
					Trade Profit	161.7

Table 1 shows a five-month position trade combining pyramiding with raising stop orders.

have dragged down the overall profit by about £6, and also ignores the ongoing spread bet 'rolling charges' which over five months would have amounted to approximately £3. On some positions the receipt of dividend adjustments might go some way to offsetting the rolling charges.

This example was based on a nominal £1-per-point initial position size, so if you find the resulting £156 profit over five months not rich enough for your tastes you can scale up to a £10-per-point initial position size which would have been pyramided to £20-per-point en route to your £1560 profit. Do keep in mind, however, that the idea is to run many such positions simultaneously in parallel rather than one position at a time in series; so make sure you are sufficiently well capitalised to be able to realise your edge before you run out of cash. Not all positions will perform as nicely as this one. It appears to work on this carefully selected (but real) position trade, but does it work in real life over a large number of trades?

Does It Work?

Having tried my hand at every trading and investment strategy over the years, I finally settled on Position Trading as the approach that best suited me. And having transitioned from being a consistently losing trader to being a predominantly winning trader, in 2009 I started keeping more comprehensive performance records which I made public first in a book and then in a year-long trading blog.

In a good year for this strategy (2009) I made a spectacular 3000 per cent return in as little as six months using a very small initial stake, and in a not-so-good year (2010) I ended the year almost 40 per cent down. While alternating between +3000 per cent and -40 per cent would be perfectly acceptable, the good news is that the 40 per cent drawdown was from a new small initial stake rather than from the entire previous accumulated profit – which means that over the two-year cycle my accumulated profit had hardly been dented at all. It might not work out like this for you, or me for that matter in the future, but the aim of this strategy is to make as much as possible in a good year and to lose as little as possible in a bad year.

Strategy Snapshot

Strategy name:	Position Trading
Strategy type:	Trend Following Diverse Equity Portfolio
Time horizon:	Intraday to (potentially) Forever
Setup:	Buy only on downward correction and at lower price than last stop-out.
Entry:	Ideally as a live trade rather than a GTC order.
Stop-Loss:	Initially very tight within 1% of trading funds and below most recent support.
Take Profit:	Usually only by stopping out.
Trailing-Stop:	Let initial tight stop widen to 15%-20% below current price, before trailing manually while respecting support prices.
Exit:	Usually only by stopping out.
Risk and Money Management:	1% risk per trade initially, pyramided by another 1% when previous risk is (more than) covered by the trailed stop order.
Average number of signals:	Typically 1-10 opportunities each day to enter a new position or pyramid an existing position.
Average hit rate/profit to loss/return per month etc.:	Total portfolio return ranging from +3000% to -50% experienced over six month periods.



F1) Severfield-Rowen, Aug 2010 to Jan 2011



Here you can see the chart on which the example position trade is based.

Source: www.tradesignalonline.com

How to Trade Short-term Turnarounds Using Gaps

Gaptrading – Part 3

Gaps are among the best-known phenomena in trading. Many different qualities are attributed to gaps – for example, they can reverse entire trends. In Part 3 of our series on gap trading we will endeavour to find these particularly strong gaps. In addition, the article will describe a setup designed to profit from these gaps. Besides intraday trading, reversal gaps also loom large on the overarching time horizon since they indicate which way things are headed on subsequent days.

First of all, it is important to clarify which qualities gaps must have to be of any significance to a trade. This is where entry management is called for most with the principal focus being on the trading done prior to the opening of the market. Stocks must be found that feature relative strength and relative weakness vis-à-vis the overall market. Furthermore, when looking for the right stocks care must be taken to ensure that there is little support ahead in the case of a potential short trade. Similarly, there should be little resistance ahead on the long side. So the stock ought to be able to break out upwards or downwards with a great deal of momentum.

Origin and Impact of the Gaps

For the long side:

It is important that the market is in an intact downward trend and that the gap is above the previous

day’s high. That way, you have already eliminated the first few resistance lines at the opening, which simplifies trading on the long side. Psychologically, it must be kept in mind that as a result of the market opening above the previous day’s high, the market participants are forced to cover their short positions. As a rule, such covering purchases cause a major bullish momentum to develop.

For the short side:

Everything is a little faster here. Most market participants are still orientated long and the market opens below the previous day’s low with a downgap. This opening will force most market participants to part with their positions. As a rule, this brings a great deal of bearish momentum to the market and the following days are highly likely to see a continuation in the direction of the gap.



Peter Soodt

Peter Soodt has been a full-time day trader since 2001. He learned about the principles of trading from his father and later attended various seminars at renowned institutions. In 2005 he founded "PS Trading Seminars", an online-education school. In early 2009 Mr Soodt won the trading competition of www.termintrader.com with flying colours.

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Which Prerequisites Are Required?

Here the pre-market needs to be watched closely. The time from 1 pm to 3.29 pm CET is an important indicator of the US market helping you to orientate yourself. As a rule, what happens after the opening is that the market continues to trade in the direction of the pre-market phase. Following the opening, the five-minute chart will become the main trigger point. If the market opens with a downgap and the first five-minute candle closes red, the short setup will be the first five-minute low. The same is true of the long side: If the market opens with an upgap and the first five-minute candle closes green, the high of the first five-minute candle will be the long trigger.

How Can You Find such Stocks?

Owing to the large number of underlyings, it is obviously difficult to filter out the suitable stocks from the nearly 10,000 issues. However, even here, devices such as market scanners exist that can considerably simplify life in day-to-day market trading. Care should be taken to make sure that you create a pre-market scanner. The following components should be included in the scanner:

For the long side:

- Pre-Market Highs
- New Highs

- Minimum position in today's range: 95 per cent
- Minimum holding period of the high: ten seconds
- Approaching new high: 0.10 dollars

What is important about these scanning adjustments is that the highs are held for at least ten seconds. For many traders, this is rather irrelevant, but the holding of the highs makes it possible for Relative Strength to be recognised. The next important item in this scanner is approaching the new high. Here you ought to see to it that sufficient time is taken to put this scan on the desk and watch the stock. A gap of 0.10 dollars ought to be sufficient for approaching the new high. The minimum position in the current trading margin should be at 95 per cent. That means that the stock must be in the 95 per cent range when a new high is formed. This allows you to see how much upward momentum there is in the market.

For the short side:

- Pre-Market Lows
- New Lows
- Minimum position in today's range: five per cent
- Minimum holding period of the lows: ten seconds
- Approaching new low: 0.15 dollars

F1) Model of a DownGap



The market is in an intact upward trend forming a bullish candle. Then a large downgap materialises below the last candle. The sales cause further bearish follow-through to develop. Normally, after such a downgap the underlying has three to five days' space to continue the movement initiated. The long position can be completely disregarded and only short opportunities be sought.

Source: TRADERS' graphic

F2) Model of an UpGap



Most market participants are still bearish here when they are caught off-guard by the bulls at the opening of the market. During the first five-minute candle a maximum of concentration is called for to achieve the best entry. After the upward break the underlying moves into a lengthy sideways phase. In this situation a good stop management is called for. As soon as the market forms a higher low, the stop will be placed from the negative to the positive.

Source: TRADERS' graphic

Just as is the case on the long side, here too the holding period of the lows and approaching new lows are the most important characteristic. Pre-market, the stock must be in the lower five per cent range, which indicates momentum on the short side. These are three of the most important items to consider when trading these gaps. After all, you need to remember that at this moment trading is done totally anti-cyclically.

The Psychology behind It

Imagine there is an intact upward trend and the market opening below the previous day's low with a downgap (Figure 1). Those traders who have held their positions overnight are now completely in the loss area with their positions. That means that they are forced to liquidate their trades as soon as possible causing enormous pressure to sell.

The same is true of the long side (Figure 2). The market had previously been trading ever lower, and traders were feeling relatively secure in their short positions. Now the underlying is opening with an upgap. Consequently, the market participants are forced to part

with their short commitment, causing considerable momentum to develop on the long side. Should the stock develop any strength on the long side, you can expect each correction to represent a new buying offer

“Remember that at this moment trading is done totally anti-cyclically.”

on the ensuing days – just as you can on the short side. If the market builds up a short momentum, each rally is a new sale offer on the ensuing days. This means that you have an indication of what the direction is going to be on the next few trading days following the development of the gaps, and this is true irrespective of the long or the short side. And that direction will be one that you can then focus on.

Stop and Trade Management For the short side:

As soon as the five-minute low was triggered, the stop will be placed 0.05 Dollars above the first five-minute highs. After the underlying has developed new lows, the stop will be placed at breakeven. Now what it is

required is to pay attention to where the distinctive support points are (points, for example, that have previously led to new highs). As a rule, those points are approached very strongly and very quickly on the short side, and the stock will initially move into the sideways consolidation. The stop will remain at breakeven until the stock breaks downwards through this sideways consolidation,

causing a strong momentum to enter the stock very quickly. From now on, the stop can be placed from breakeven to the lower high of the sideways consolidation.

For the long side:

Here things are a little different from the short side. After the five-minute high was triggered, the stop is placed 0.05 dollars below the five-minute low. As a rule, the stock breaks through upwards in one fell swoop (by approximately 4 pm CET) and then moves into the sideways phase. Under normal circumstances the position here is already very much in the profit zone. Now the question arises whether to take part of the profit (which normally is the better solution) or to hedge the position completely. Normally, the stock starts to continue this

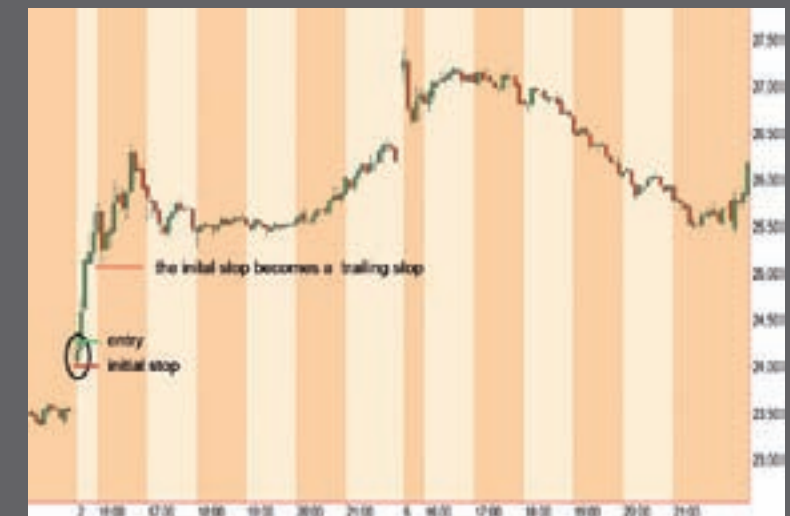
F3) Upgap with Thor Industries (THO)



After a two-month sell-off the THO stock opens with an upgap. This is so strong that several resistance lines were broken in the daily chart. To be able to participate in such gaps, you need to have the stock on your watch list during the pre-market phase. At the opening the five-minute-high must be paid attention to.

Source: www.tradesignalonline.com

F4) Intraday Trading with THO



Here you can see THO in intraday trading. The stock opens with a large upgap and is free of resistance from the five-minute chart perspective. The entry point is the five-minute high with the stop being placed 0.05 dollars below the five-minute low.

Source: www.tradesignalonline.com

upward movement after 8 pm CET. Here you can then move the stop from breakeven to the higher low of the long sideways movement.

Notes on the Examples

Figure 3 and Figure 4:

The example given here is that of the Thor Industries stock (code: THO). After a strong two-month sell-off THO opens with a gap of 0.60 dollars above the previous day's high. This up-gap caused any of the previous day's resistance to be removed, the stock is upwardly free. Now exactly five minutes remain after the opening to find the stock primarily via the scanner and prepare it for trading. After completing the first five-minute candle (Figure 4) a stop-buy is placed at the high of the first five-minute candle. Following the triggering the stop is placed 0.05 dollars below. No more resistance can be seen on the five-minute chart. This in turn one needs to find out from the larger time frame, the daily chart.

As mentioned at the beginning of the article, the market moves upwards within a very short period of time after an upgap above the resistance. This provides enough scope to look for a good stop which is found in the lower range of the first red candle. The market then breaks out once more towards a new

high and subsequently moves into a long sideways phase. This very sideways phase is needed for the next stop adjustment and for finding possible partial exits.

Figure 5 and Figure 6:

After a very bullish previous day's candle the Apple stock (code: AAPL) opens with a downgap of 4.18 dollars. This alone has already had a devastating effect on the underlying. Most market participants are forced to close their long positions. Using the existing knowledge you change to the five-minute chart. There the stock starts building a short momentum, and you get ready with your short order to short the stock below the five-minute low at 263.33 dollars.

After the order was triggered, the safety stop will be placed 0.05 dollars above the five-minute high at 264.44 dollars. The stock immediately starts to break away sharply downwards. The stop continues to remain in negative territory. As soon as the first lower high is formed in the stock and momentum again develops on the short side, you wait for the stock to form a new low. Now you can place the stop on the lower high.

This means that it is possible to either consider a limit or to leave the position enough space to develop. It must be borne in mind that this is a short-term trend

reversal (five days at the most) which leaves enough space for a sufficient target in the case of a big stock like Apple. On the daily chart you can see the first strong support area at 244.84 dollars. This target would make a very good risk-reward ratio. As a rule, the market overshoots such marks and one can try to achieve a smooth target of 20 dollars. However, please note that positions held overnight are exposed to very high risk. To certainly be on the safe side, you should close the position in the course of the day and as close as possible to the closing price.

Conclusion

The gaps described here are certainly among the most aggressive ones and should only be used by experienced traders. Professional traders go even further down into the smaller time frames. That means they use a minute chart or tick chart to further reduce risk. Neophytes ought to trade these kinds of gaps cautiously and do so with demonstration accounts or in paper trading. This way crucial experience can be gained first before the setup is used in real trading.



F5) Downgap with Apple (AAPL)



After an extremely bullish previous day's candle Apple forms a downgap that you can again see enlarged in Figure 6. The downgap alone is devastating as it is. The subsequent bearish follow-through allows a short trade with a very good risk-reward ratio. When managing your trade previous lows are distinctive points for placing a stop.

Source: www.tradesignalonline.com

F6) Intraday Trading with Apple (AAPL)



Following the downgap of 4.18 dollars at the opening, you will be waiting for your chance in the five-minute chart. Here Apple forms a red candle in the first five minutes. After briefly testing the opening price the stock will implode. As soon as the stock moves into a correction and forms new lows after that correction, the stop will be placed on the lower high.

Source: www.tradesignalonline.de

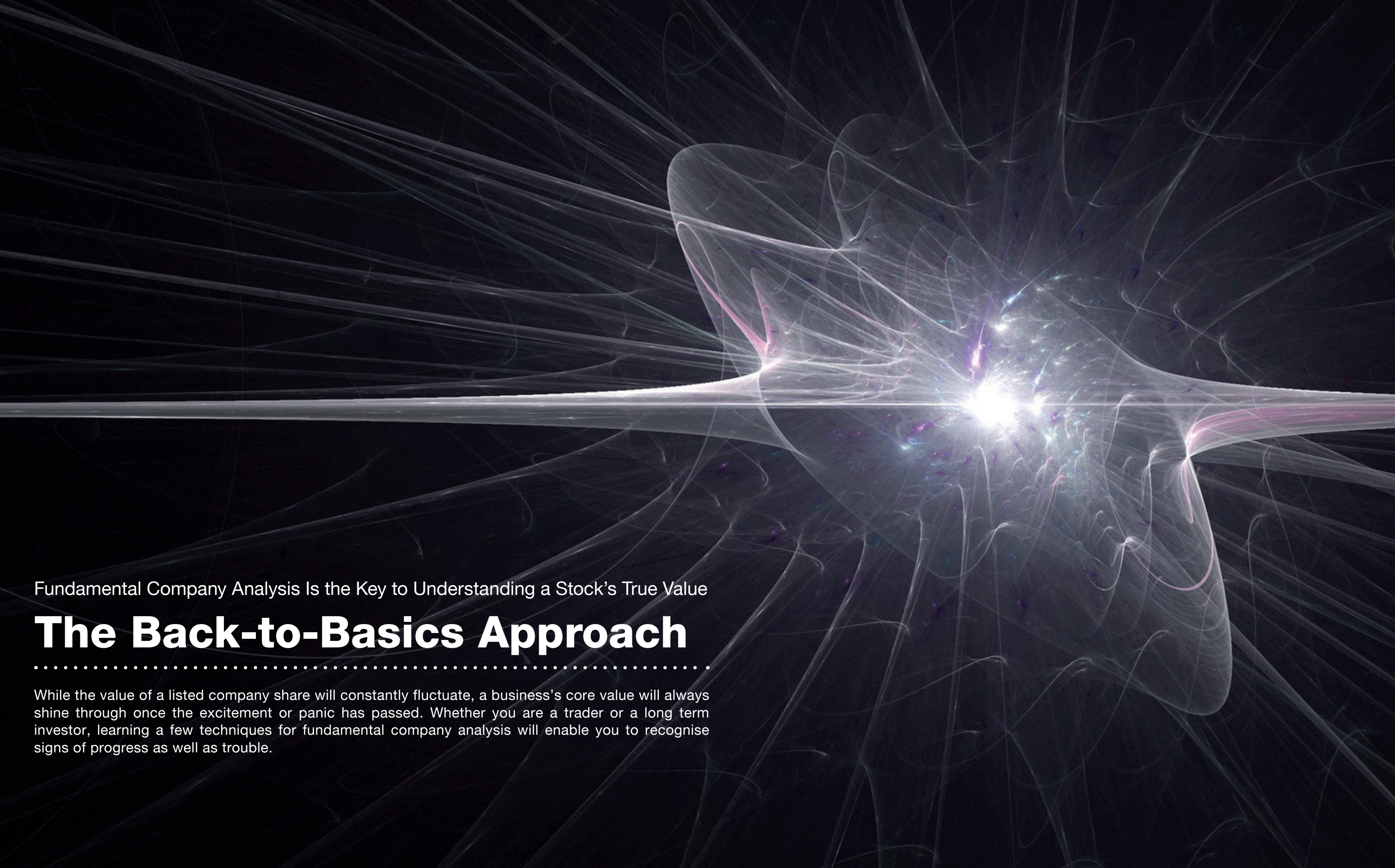


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The background is a dark, almost black, space filled with a complex network of thin, glowing lines. These lines are primarily white and light grey, but some have a soft pink or magenta hue. They radiate from a central, intensely bright white point, creating a starburst or nebula-like effect. The lines are mostly horizontal and vertical, with some diagonal and curved paths, giving a sense of dynamic energy and depth.

Fundamental Company Analysis Is the Key to Understanding a Stock's True Value

The Back-to-Basics Approach

.....

While the value of a listed company share will constantly fluctuate, a business's core value will always shine through once the excitement or panic has passed. Whether you are a trader or a long term investor, learning a few techniques for fundamental company analysis will enable you to recognise signs of progress as well as trouble.



Jessica Furseth

Jessica Furseth is a London-based investment journalist specialising in the technology, telecommunications and renewable energy sectors. For contact details, see: www.jessicafurseth.wordpress.com

For better or worse, it is the components of real life business which drives a company's share price over time. The basic rules presented in this article will enable you to recognise the markers of a company in good health, as well as help you to pick up warning signs that should make you think twice before investing. The ability to conduct a thorough analysis is also vital in terms of judging whether a rising stock is losing touch with its fundamentals. This is also a key tool for those looking to unearth hidden gems, as it may help to identify an under-appreciated growth story just set to take off.

Five Questions to Ask

While fundamental analysis takes a little time, you may find it reassuring to hear that it often comes down to common sense. With annual company reports and regulatory announcements now available on the internet, it has never been easier to get your head around a company's operations, opportunities and potential problems. To get started, we will start with these five basic questions:

1. What Does the Company Do?

Always ask this first when looking at a new company, and make sure you understand the answer. Do not be afraid of sounding stupid if the company's role

seems confusing, as it is their job to explain this in clear terms and if they cannot that should be a red flag. A prime example of this is software companies, which often use jargon so look for those who are able to explain their business in layman's terms.

2. Is the Company Making Money?

It is not the profit figure but the cash flow statement that best indicates a company's financial health. Reported earnings can be distorted by accounting practices, but cash is cash. The cash balance is crucial because it determines whether the company can pay dividends and service its debts, as well as how much working capital is available to run the business. If investing in a pre-profit company, consider how long you might have to wait to get a return, as businesses can survive for decades without actually making any money.

3. What Are the Growth Prospects?

A company with a steady track record of increasing its earnings-per-share (EPS) every year is an investors' dream, as you could theoretically sit back and watch your investment grow in value.

Mature technology hardware companies are ideal examples of this, as a foothold in a rapid renewal industry means constant customer upgrades. Cautious investors should also look to a company's dividend policy for signs of stability; utilities will often set these out years in advance and this will support the shares even in turbulent times. Consult the dividend cover for further reassurance, as if this starts to creep downwards a cut may be in the cards.

Reported earnings can be distorted by accounting practices.

4. What Is the Market Position?

Ask yourself, what advantages does the company have compared to its competitors? Is its market share growing or shrinking? Take the pharmaceutical sector - a good, mature company should ideally have a strong position and a growing market. Also consider pricing power, as a dominant position is worthless if anyone can swoop in and take over. Airlines can be vulnerable on this point, however pharmaceuticals often enjoy strong pricing power

from patented medications, not to mention a steady stream of new products from ongoing research and development. In contrast, a start-up company, would score very low on all these points, as there is significant risk associated with any product launch, especially in medical sciences or technologies.

5. Special Circumstances?

Every company will have its own set of circumstances making it slightly different even to its closest peers. Mature companies may have underfunded pension obligations, and an necessity to plug this gap will limit its ability to make investments in itself. A company undergoing a

restructuring could be a diamond in the rough, although this can turn into a test of patience. When considering whether to invest in a turnaround story, look to the management's standing and experience for turning things around. Frequent acquisitions can add value to a company, but look for concrete statements from management on exactly how it plans to extract value from the new pairing. Also, make sure enough time is left to integrate each purchase before a new deal is announced.

Red Flags

Large pension liabilities and overly aggressive acquisition programmes are two issues which may make you think twice about buying shares. Excessive leverage is another, as the recession proved how over-reliance on borrowings made some ships unsteady in the storm. Companies with cash on hand, such as many of the large software groups, benefited

significantly from being able to carry on with business as usual during the recession. Solid cash generation, as is often the case at large telecommunications groups, means some companies can carry debt reasonably well. However, a will among management to pay down money owed is a good sign, especially for small- and medium-sized companies. While securing a contract with a large customer

can often pull a start-up company up from the doldrums, over-reliance on a single customer can also be a danger sign. That customer might change its mind, so look for efforts to diversify. Familiarising yourself with the company's customers, even those further away in the food chain, could prove to be worth your while. For example, the effects of an industrial expansion freeze will trickle not only through to construction companies, but also to component manufacturers, material analysis firms, down to the providers of enterprise software. The same mechanisms could also let you spot opportunities; now, following last year's oil rig mishap in the Gulf of Mexico, US lawmakers are pushing for tougher regulation for oil companies to prevent future incidents. Perhaps bad news for industries associated with oil and gas exploration and extraction but good news for companies making security sensors and other analysis equipment.

While the effect of market psychology on a stock is more of an issue for valuation than for fundamentals, it pays to remember that if the sector is hopelessly out of favour, it does not matter how good the company is. After all, no one wants to buy a good house in a bad neighbourhood. But if your analysis convinces you the

Case Study NCC Group

Company activities

NCC backs-up business data in case of damage or theft. NCC also tests IT security systems to ensure customers are adequately protected from fraud attempts.

Financial position

NCC delivered a 25% growth in earnings per share (EPS) in the year to May 2010, and even during the recession (the year to May 2009) the group's EPS grew by 8.6%. Indicative of a healthy balance sheet: cash flow per share was 43p per share in 2010, up from 41p in 2009.

Growth prospects

Reassuring double-digit dividend growth over the past five years, but the dividend remains highly sustainable at 2.9% covered (as of the year to May 2010). 2010's final results, reported on 5 July, showed £11.9 million in net debt, modest for a company whose operating cash conversion stood at 139% of operating profits. Further growth from acquisitions; 14 October's purchase of iSEC followed the takeover of SDLG on 23 April 2010.

Market position

Solid market leadership position in software backup (escrow) services. While smaller, the company's testing division enjoys strong customer relationships and acquisitions are adding to its size and geographical reach.

Special circumstances

Solid growth also during the recession demonstrates the strength of its business offerings, and customer loyalty. Expansion is supported by a reassuring, market-leading software escrow business.

F1) Case Study NCC Group



Figure 1 shows the share price performance for NCC Group, the London-listed IT escrow and software assurance company.

Source: www.tradesignalonline.com

company is in good nick, this could be a buying opportunity before the company comes back into favour.

When Bad News Could Be Good

As companies are legally required to alert the market if their results are likely to be materially different than what is expected, you will very handily be informed if things are not going well. The trick is to understand how bad the news is, as what sounds negative may not always be so. A start-up company telling you it is having difficulty perfecting a new design is usually a bad sign, but a missed earnings forecast needs further examination. Sometimes companies miss targets because analysts get overly ambitious, and this is not always a reflection on the core business. Look to the wording in the company's statement - a key contract closed a week after cut-off, causing an analysts' target to be missed is not a sign of disease.

However, if a company's management tells you in no uncertain terms they are not doing well, you should believe them. Profit warnings do not usually come as isolated incidents, especially if the explanation points to external events. Any variation on the phrase 'end-market uncertainty' is usually a warning; the one thing the market hates above all else is

uncertainty, so it is only when all the bad news is out in the open that the share price can start to recover. Wait to hear terms such as 'cautious optimism' before expecting improvement.

A dividend cut is never popular, but sometimes it can pave the way for new growth. A company paying out excessively high dividends could arguably put this cash to better use by funding growth, meaning shareholders may be better off in the long term if the management made the cut. However, a reduced dividend may also become necessary to decrease debt, meaning while the balance sheet will be healthier as a result, it will take longer for the shareholders to feel the benefits.

On the heels of long-term poor performance, a restructuring announcement is usually a good sign. You should, however, be aware that this may not be as straightforward as it may first seem - there will be unexpected changes and it is almost certain to take longer than expected. A newly arrived chief executive officer with a solid track record of turning things around can be reassuring, although keep an eye on the progress as the world changes - what worked once is not guaranteed to work again.

Cost cutting is usually seen as a positive sign, however make sure this does not come at the expense of growth. Technology

companies will often justify large research and development spending on the grounds that innovation is the lifeblood of this industry, and the same sentiment will, to varying extents carry over to other sectors as well. Consider how a company is trying to save money, whether it be outsourcing, automation, department closures or pay cuts. For example, one large component manufacturer weathered the recession by having its staff agree to pay-cuts to avoid lay-offs in the hope that normal wages could be restored when business picked up again.

Value versus Price

While the hopes and fears of the market will continue to distort a company's value to some extent, a fundamental analysis is key to determining the true value. This means if you take the time to look at the business fundamentals you are less likely to be taken for a ride when valuations lose touch with reality. While there is often a reason why a stock is cheap, if you understand the business you may be able to identify the signs of change up ahead, and buy at a good price. It is only when you understand the true value that you can form an opinion of whether it is worth what the market is asking.



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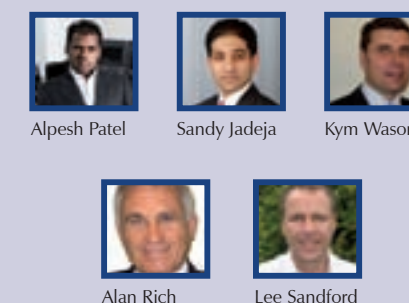


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It Is the Little Foxes which Spoil the Grapes

Ten Key Points to Trading

.....

Many traders have a list of things they have done which they later regret with regards to trading and then swear never to do them again. Not to be outdone, I submit to you my list of ten things to keep in mind during your trading career. Keep in mind, whenever I use the word ‘trading,’ it does not mean that you are in front of your computer all day placing 100s of trades: rather it is a mentality. You need to have what I call a ‘trader’s mentality,’ which means that you will never enter a trade, leave it alone and then hope for the best. Instead, you will properly manage the trade – realising that this is in fact your business and not a hobby. This list could easily be two to three times as long, but in the interest of time and space, I have condensed it to ten in no particular order. So, whether you are in a position for a few minutes or a few months, consider the following as some helpful advice.



Eric Waddell

Eric Waddell has been trading for over ten years and teaches with Online Trading Academy. He has developed various strategies in the equities and Forex markets, which he has shared with students in various parts of the world. Eric truly considers it an honor to instruct with Online Trading Academy and encourages his students to stay in touch with him.

Law #1: Losses Are a Part of Trading

No, it cannot be...all of our trades are supposed to be profitable, right? However, as anyone who has been trading for any length of time knows, that is simply unrealistic. Repeat after me: "Losses are a part of trading." The sooner you come to terms with that the better. What do we call people who always buy at the exact bottom and sell at the exact top every single trade and thus never incur losses? Well, they are either extremely lucky or lying... with the latter being the probable explanation. Why is it important to realise that you will take losses trading? Well, the way I look at it, you will be more inclined to place a 'stop' on your trade to mitigate your downside as opposed to entering a trade and simply focusing on all the money you are going to make.

Have you ever entered a trade, disregarded placing a stop, and then watched as it went against you? Why did you not close it out or place a stop to begin with? Probably because you were just focusing on your profit potential instead of the downside (which we will discuss later). You want to avoid big losses – but losses will occur. The key is entering a trade at a logical location and placing your stop at a logical location – in other words, where would whatever it is you are trading have

to go for you to conclude that there is no longer justification for being in the trade? Get rid of this mindset that you just cannot take a loss. Why? Because if you do not, your trading career will be very short-lived.

Law #2: Be Aware of the Potential for 'Price Shock'

Price Shock is when there is a dramatic move in the price of a trading instrument which is sudden and usually unexpected. For example, Bear Stearns closes around \$30.00 per share and then opens around \$2.50 the next day: that is price shock. How can you protect yourself against price shock? Well, there are some option strategies we could discuss – but that would be an article in and of itself. I will just say this with regards to price shock: always think 'worst case scenario.' If you are spending sleepless nights worried about your stock positions, then you probably need to reduce your holding to a more manageable amount in which your lifestyle will not be affected should there be a sudden drop in the price. Rather than holding that 1000 share position of XYZ, perhaps you should only be holding 300 shares, for example. You never know when the CEO is going to be led away in handcuffs and the price of your stock will be significantly reduced. Even as

F1) Price Shock



Here is an example of price shock. If you were long Amylin (AMLN), you woke up on October 20, 2010 to see that it had lost half its value when the market opened. Price shock can ruin your day or destroy your account if you are over-leveraged.

Source: www.tradestation.com

an 'active' trader (day trader), as we witnessed in May, 2010, price shock can occur during the trading day such as when the 'flash crash' occurred. Now, fortunately, the examples of price shock I have mentioned do not happen every day and are rare for the most part, but my point is: always consider the worst case scenario and do not trade with too large a position size.

Law #3: Trading Is All about Odds

Trading is not gambling, but we must always put the odds in our favour. Here are a couple of examples: let us say that the ADR (Average Daily Range) of XYZ is \$1.60 and it has already moved more than that with about an hour to go in the trading day. You have decided to enter a long position in the hopes that it could move even higher. Could it continue higher? Absolutely. What you have to ask yourself is: "What are the odds it will continue to move higher if it has already exceeded its average daily range?" It is something to take into consideration prior to placing the trade.

Would it make sense to enter a long position on XYZ right under an area of resistance? It might work out, but what are the odds that it will? Chances are it will hit that area of resistance and at a minimum stall prior to deciding

which way it wants to go. It is not guaranteed to happen that way – but the odds are that it would. So, bottom line, make sure you put the odds in your favour prior to entering the trade.

Law #4: Be Aware of Climactic Volume

An example of 'climactic volume' is when there is an abnormal or greater than average increase in the amount of shares being traded. This may be indicative of a potential reversal in the market as we can see from the illustration (Figure 2). The volume was moving along pretty steadily and then what happened? A huge spike in the volume which corresponded with a reversal in the stock. Just be advised, that whenever you see a large increase in the volume of whatever you are trading, something big might be getting ready to happen. It may not happen right away all the time, but there is a chance that a reversal could potentially being set up. It is not guaranteed to reverse – sometimes the original move just winds up continuing... but you never know, I have seen many instances when a stock was moving distinctly down or up and all of a sudden there was a huge spike in the volume coupled with a candlestick formation such as a 'hammer' or 'shooting star' and sure enough

– it began to reverse. This is just something to keep in mind.

Law #5: Do Not Fall Victim to 'Revenge Trading'

A 'revenge trade' basically goes down like this: you trade XYZ, it goes against you, you take a loss and now XYZ 'owes you some money.' The reality is, XYZ does not care about you. The market is going to do what the market is going to do – and without any emotion. The problem is, traders are human and are thus susceptible to emotions – which is why people have been doing this for years: lose money on a stock (or any financial instrument) and then they trade it again over and over until they finally either make a profit on it or go broke in the process. Always ask yourself why you are entering a trade. If the best reason you can come up with is: "Well, I will show XYZ who is boss..." I might then suggest an alternative and less costly method of spending your time and money? Perhaps consider a stamp or butterfly collection.

Law #6: Do Not 'Average down'

So, you bought 500 shares of ABCD at \$50 and it is now trading at \$40 (of course, you did not place a stop) but you are convinced this thing is going up. What do you do? Of course, you buy more – another 500 shares.

F2) Climactic Volume



Midway through this chart we can see an upward move and then a dramatic increase in volume which signaled a potential reversal.

Source: www.tradestation.com

Makes sense, right? (Can you sense the sarcasm?) Now your average cost is only \$45, but you own twice as many shares. And what happens next? You guessed it...it tanks even further.

Two things I will say about 'averaging down':

- Again, always ask why you are entering a trade. Is it due to some clear-cut analysis you have done? If the best you can come up with is: "Uh, it will lower my cost basis," – then you may just need to close out that original position altogether or at least take some of the shares off the table. Adding to a bad decision is rarely a good idea.
- Would you have been in this situation to begin with if you had placed a stop? I think you know the answer to that. Place a stop in a logical location immediately after entering the trade and move on. If you get stopped out, so be it; it is a part of trading...at least you lived to trade another day.

Law #7: **Look for Clear, Definitive Moves One Way or Another**

This sounds very elementary but you would be surprised how many people enter trades when there is not a clear trend and they really cannot tell which direction it might go. What they

are doing, in effect, is trading off of gut instinct as opposed to treating trading like a business. One of the worst things which can happen to a trader is that he/she does the wrong thing and then it works out. Why? Because they will do the same thing again. Unfortunately, trading off of gut instinct or placing a trade without using a stop will catch up with you over the long run (assuming there winds up being a 'long run' for you).

Law #8: Ask Yourself "How much Can I Lose on this Trade?"

This goes against the conventional wisdom of the novice trader...focus on your risk. This is paramount to longevity in this business. When I first started trading, I did what most people do – I focused on how much I could potentially make on each trade without giving much thought to the downside. I felt that each trade was going to be the one. You know what I am talking about. Again, the issue is that if you are focusing simply on the profit and not your risk – it will be detrimental to your equity. Make a plan and follow it. If the plan is viable, which should include the use of a stop order to mitigate your downside, the 'making money' part should

take care of itself. I remember Paul Tudor Jones stating in an interview many years ago, something to this effect, "If the investing public would focus more on their risk instead of some pie in the sky – they would be a lot better off." How true. Yet most look at their brokerage account as an cash machine where every

“Capital preservation is the name of the game.”

trade will bring them riches. If that happens – then great – but focus on the downside first. Capital preservation is the name of the game.

Law #9: You Are Not Infallible

Just as with 'loss being a part of trading,' this is something else you need to come to terms with. There is an old saying on Wall Street: "the market has a paddle big enough to give anyone a spanking." Just when you think you are infallible – you know it all – whatever you touch turns to gold – is typically right before a catastrophe. (Pride goes before a fall). If you feel you are infallible, you are more likely to break your rules and trade out of emotion as opposed to adhering to a clear-cut business plan.

When you entered that trade without a stop and held it forever because it was "going to come back"...what made you do that? Speaking from experience, when I first started trading, I did not place stops. I did my 'analysis' if you can call it that, placed the trade and then hoped for the best. Some of you can relate to this. I would hold the losing position forever because deep down I could not come to terms with being wrong. Thankfully, things have changed and now I always

think about the worst case scenario and place my stop. Even if there is a 90 per cent chance of a trade working out, there is a ten per cent chance it will not. It is that ten per cent which prompts me to place a stop and realise that I am not infallible and it may in fact go against me. Which is fine, it is all a part of trading.

Law #10: **Always Educate Yourself**

Since we have established that trading is a constant learning process, would you agree that it makes sense to always try to make yourself a better trader? Regardless of your profession, whether you are an attorney, M.D., fill in the blank, you have to hone your skills and stay current with new trends and

technologies. Does an athlete, once he turns pro, forego practicing? Of course not. He has a coach and continues to practice and to better himself. When he becomes lazy and no longer keeps himself in shape – his career comes to an end. It is the same with our trading business. I am always purchasing books on trading, technical analysis, the psychology of trading, the lot...Why? Because this is my business. I hunger to learn more – even after all these years – I never want to lose my curiosity. (And since this is our business, there may be tax advantages to these expenses). Many times, you can listen to someone speak for an entire day on trading topics or read an entire book on trading and it is that one little nugget which you remember – the simple little thing that you take away which changes your life.

Conclusion

This is certainly not an exhaustive list of do's and do nots and some of it might even sound somewhat basic, but many times it is the simple things which can mess us up. As the old proverb reminds us, "It is the little foxes which spoil the grapes."





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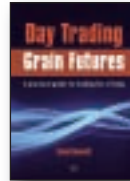
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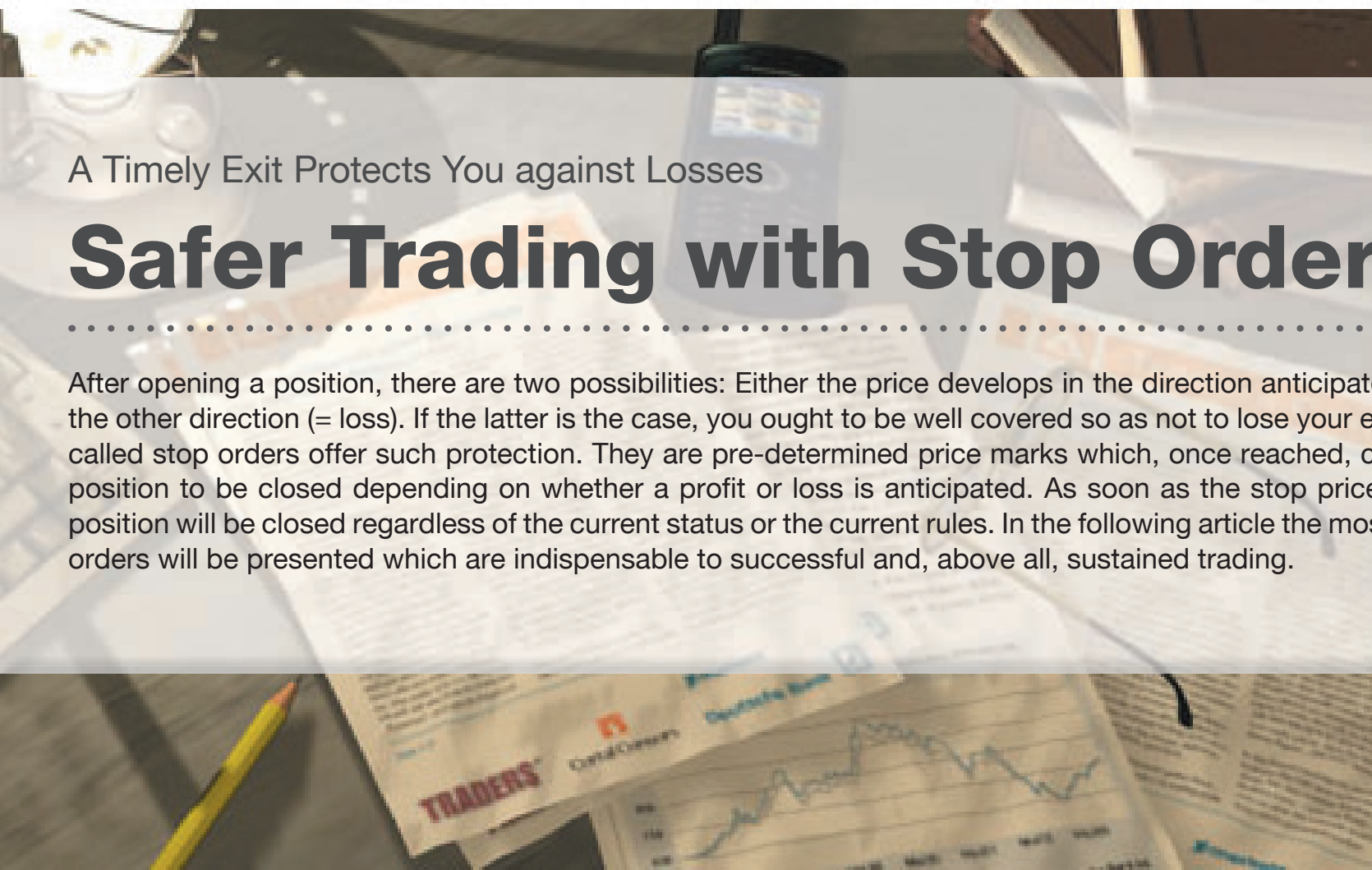
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A Timely Exit Protects You against Losses

Safer Trading with Stop Orders

After opening a position, there are two possibilities: Either the price develops in the direction anticipated (= profit) or in the other direction (= loss). If the latter is the case, you ought to be well covered so as not to lose your entire capital. So-called stop orders offer such protection. They are pre-determined price marks which, once reached, cause an existing position to be closed depending on whether a profit or loss is anticipated. As soon as the stop price is reached, the position will be closed regardless of the current status or the current rules. In the following article the most important stop orders will be presented which are indispensable to successful and, above all, sustained trading.



Initial Risk Stop

The initial risk stop is the fundamental stop on which all other stops are based. As the name suggests, a stop is determined prior to opening a position that sets the maximum risk of loss. For that reason it is also known as a maximum loss stop. This stop will close an open position if the losses of the trade exceed a specific amount. Primarily, this serves to preserve capital and enables the risk of the respective trades to be balanced against the available capital.

Breakeven Stop

The breakeven stop will be placed after opening a position as soon as the price has moved in the anticipated direction by a specific amount. The position will therefore be closed if its value were to fall below the price that would be tantamount to a loss. This means that you will maintain your opening balance plus expenses. This stop is designed to make sure that the positions entered that have already become part of the profit by a specific amount will no longer result in losses.

Trailing Stop

Trailing rather precisely describes the function of the trailing stop. If a position develops in the direction anticipated, it will continuously be adjusted to or

trailed, in the direction of a profit. However, if the price moves in the opposite direction, the trailing stop will remain unchanged. It will close an open position as soon as a pre-determined amount of the resultant book profit is lost again. Every time the profits from a position reach a new high the trailing stop will be placed at a certain spot where a certain part of the profits are allowed to be lost. This loss is specified as a profit risk. On the one hand, trailing stops are meant to reduce the risk of loss and on the other hand, they are designed to partially and consistently protect profits (Figure 1).

Profit Target Stop

The profit target stop is used to determine an upside target which, if reached, causes an existing position to be closed. The upside target is based on one's individual assessment which may be based either on the (technical) situation of the underlying security or on the profit target for opening a new trade (Figure 2). Since this stop only serves to take profits, the risk of loss is rather high. That is why one should also always determine one of the other types of stop in order to limit losses. For example, an initial risk stop could be placed alongside the profit target stop in case the price does not develop in the direction anticipated.

Inactivity Stop

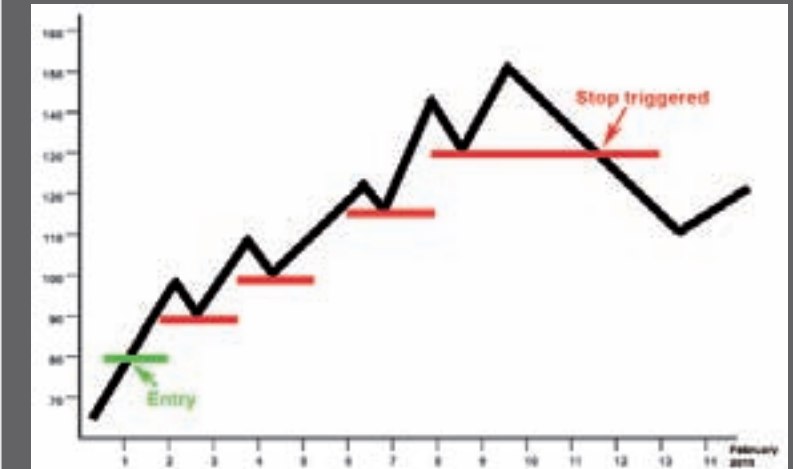
The inactivity stop will close a position if the price has not developed in the direction anticipated during a specific period of time. What is special about the inactivity stop is the time factor. Once the pre-determined upside target is reached, the inactivity stop will be inoperative. However, if the respective value during this period of time is quoted below the upside target, the position will be smoothed. This stop neither limits losses nor does it secure partial profits or take profits. It is only designed to serve as a reminder of the exit in order to keep one's portfolio adjusted thus making it more efficient, or not to tie up liquid funds in immobile positions.

Conclusion

Stop orders are indispensable to any trader since they protect against extreme losses and thus secure one's trading livelihood. Thanks to stop orders, there is still enough money available even in case of a series of loss trades to continue pursuing a trading plan. Not only do they serve a protective function, stops may also secure profits and allow for profit-taking.



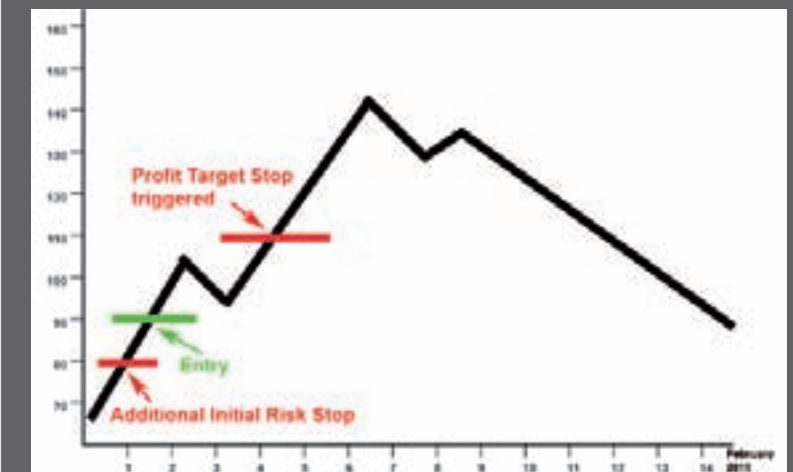
F1) Trailing Stop



On 1st February we enter at 80 points (green). We place our trailing stop at 90 points (red). After the price has developed upwards we trail our stop further and further in this direction (red), securing partial profits for us. However, after 10th February 2011 there is a trend reversal. In that case our stop remains unchanged at 130 points, closing our position on 12th February.

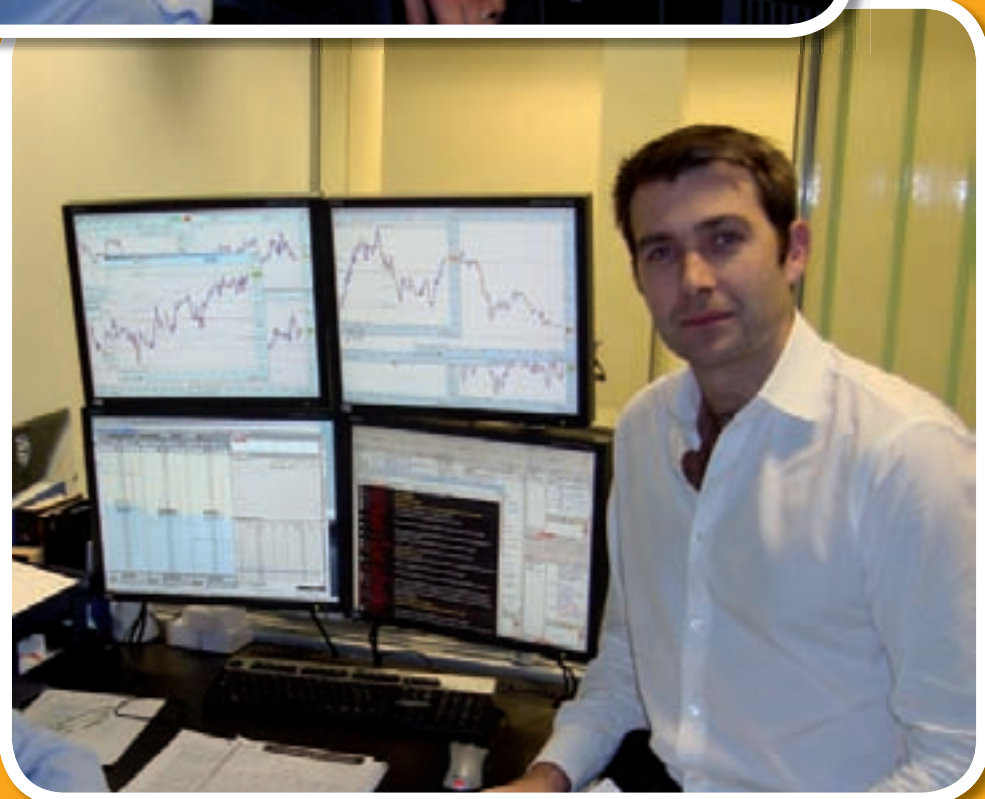
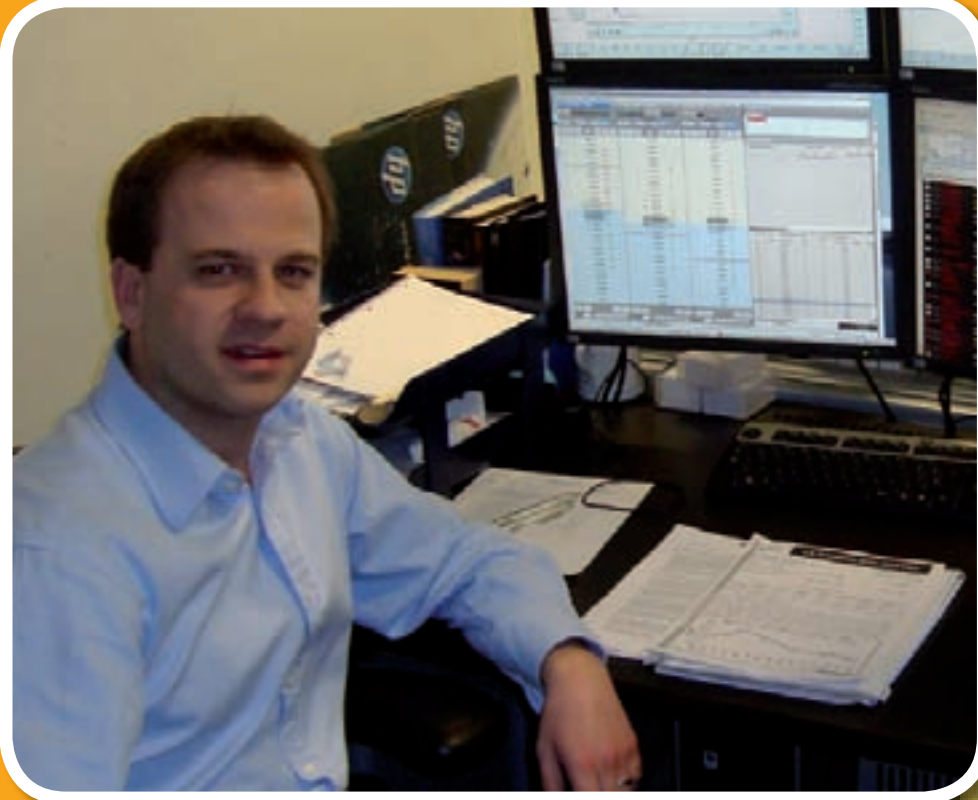
Source: TRADERS' graphic

F2) Profit Target Stop



On 1st February we enter at 90 points (green). For profit-taking purposes we place a profit target stop at 110 (red). In order to protect ourselves against losses, we place an additional initial risk stop at 80 points. However, our upside target is reached at 110 on 4th February 2011, smoothing the position.

Source: TRADERS' graphic



Will de Lucy and Piers Curran

Experience Is Key

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In the middle of the credit crunch, Will de Lucy and Piers Curran jointly founded their proprietary trading & training company Amplify Trading in London. Prior to that, they both worked for several years in proprietary trading at Goldenberg Hehmyer, and before that Piers had already done a stint in HSBC Asset Management's strategy department. In the course of their careers, both have predominantly traded Fixed Income Spreads (combined strategies with two (bond) futures of different maturities), currencies, commodities and share-index futures. Piers' focus was on Euro Schatz futures while Will specialised in the S&P E-mini. Today they both continue to trade in these asset categories with their focus changing depending on the market environment. Several times Piers has been a guest on CNBC as an expert analyst. In addition, his contributions have been published in various financial publications. Will and Piers work with their own money as traders and are mentors for young talented traders some of whom trade right there in the trading room at London's Canary Wharf. Most of them, however, participate in the trading sessions from everywhere in the world by remote link. In addition, Will and Piers cooperate with the prestigious BPP Business School by making it possible for the students to gain trading-related experience alongside their more theoretical studies. Marko Graenitz visited both of them in their trading room and conducted an extensive interview that we would like to share with you in this issue of TRADERS'.

Can you remember how you came into contact with the stock market for the first time?

Piers Curran: At a very early age I knew that there was something like the stock market. The reason for that was that my father had some investments and would tell me about them now and then.

However, I was not particularly interested in that when I was an adolescent. Actually, all I thought about was football (laughs). I went on to study engineering – and found out that that was not what I really wanted to do. It was during that time that I discovered trading and the

stock-market business and really got involved with it. Following my graduation, I applied for the HSBC trainee programme and went into asset management there. Most of the time, I was busy building portfolios and developing various investment strategies.

Will de Lucy: It was pretty much the same with me. While at university, I still was not sure what career I was going to pursue. I then was at the San Francisco office of Bank of America for six months working in customer support. During that time I realised that trading was much more interesting for me than the rather boring work in the back office. So after graduation I applied for a job at Goldenberg Hehmyer and went on to work there as a proprietary trader.

Overall then, from the very beginning your education and training was very professional and you did not do any experimenting with a private account first. Can either of you remember your first trade?

Piers Curran: No, not really. But since my focus was on the Schatz future for a long time, it must have been a Schatz trade with a small position size.

Will de Lucy: I believe that my first trade was a spread between the Schatz and Bobl future. But I cannot exactly remember that.

How have the markets changed over the years?

Will de Lucy: Everything has changed a lot. Today the market is really quite unlike the market ten years ago when I started. At that time I traded the Bobl-Bund

spread, which allowed me to take advantage of the upward and downward relative movements. There were, if you like, better patterns then. Besides, the markets were a lot slower. Back then what occasionally happened was that for a few seconds there existed opportunities to make virtually no-risk profits (arbitrage). Nowadays, such opportunities have very nearly disappeared.

So the market has become more efficient?

Will de Lucy: Yes, definitely! It is much more difficult now to identify an opportunity on the markets now and take advantage of it. In my opinion, the reason for that is the considerable growth of algorithmic trading.

Piers Curran: Exactly. Algo trading has caused many trading opportunities that used to exist to disappear. That is just one of the technological advances making the markets more and more efficient. While arbitrage opportunities and price-reaction slippages have not completely disappeared, "safe" trades only exist now in a matter of milliseconds. The computer just is a lot faster than human beings are.

Will de Lucy: That reminds me of the way staff levels have developed in proprietary-trading

companies. For example, when I started out there were around 125 traders at Goldenberg Hehmyer but today there are only about seven or eight left. The "new associates" are now algo trading computer programs.

What do these changes look like in everyday trading?

Piers Curran: To make a long story short: In the old days, there were relatively few ticks with a lot of volume each. Today we have many more and much faster ticks with significantly lower volume each. Overall volume has increased, but average volume per tick has decreased. That is it.

What is the advantage you have then as a day trader on the markets?

Piers Curran: While computers are fast and cannot be beaten in terms of computing and automatic execution, they are by no means suitable yet for every kind of trading. Above all, we have the edge when it comes to interpreting information. For example, I have a look at technical and fundamental data and then relate that information and those assessments of the current market action. Depending on price action and sentiment, the market may, for example, anticipate very good or very bad news – and that may be decisive as can be seen on the EUR/USD

F1) Anticipation in the Case of EUR/USD



In early January the Euro was down significantly, anticipating major problems on the periphery of the Euro-club nations. When the actual news turned out to be not quite so bad, the market shot upwards. Behaviour resulting from a market expectation is hard to teach a computer.

Source: www.cqg.com

chart (Figure 1). Ultimately, such considerations are also based on one's experience as a trader.

Will de Lucy: Generally speaking, I would see our advantage vis-à-vis the computer in the way we respond to events discretionarily. Again, that has to do with experience.

Piers Curran: What we should also consider is that inefficiencies may again increase in the meantime. For example, after many investment banks reduced their proprietary departments during the financial crisis, distributing the "loot" was more favourable to the remaining players. However, efficiency will rise in the long run, and that is obviously a challenge.

What were the most important insights you gained during your trading careers?

Will de Lucy: My most important insight was that I need to know myself. At first sight, that seems to be far removed from the subject of trading, but in the final analysis all the decisions will invariably hark back to that.

What have you learned from that then?

Will de Lucy: For example, it helps to know how to react to feelings of frustration or anger – and whether that behaviour

is perfect. Most of the time it is not, of course. You have to be in a position to objectify your subjective feelings and to reflect and look at yourself from the outside, as it were. More often than not, it is a lot easier to make the right decision by being a neutral observer of yourself. Imagine, for example, what your imaginary mentor would advise you to do in this situation if he were to stand right next to you monitoring the trade.

Could you please illustrate this by way of an example?

Will de Lucy: Sure. Big losses provide the best example. Obviously, nobody likes making big losses, but that is what is going to happen in a trading career sooner or later. You have to be aware of your emotions and see yourself as an outsider when it happens, and then draw the right conclusions from it. Quite clearly, the objective is risk management, i.e. avoiding big losses. To achieve this aim, it may be necessary to smooth losing positions against your own convictions and analyses (the price may move this way or that way). If the risk is too great, we cannot make the best trade because risk control is the number one issue. If you look at yourself and your rules objectively from the outside, that state of affairs will be perfectly clear but

our emotions may thwart our efforts, which is something that simply must not be allowed to happen.

Speaking of big losses: How did you experience the Flash Crash of 6th May 2010?

Will de Lucy: A day like that is a real test of any companies risk management strategies. On that day I had my hands full keeping all my risks under control, but overall, things went pretty well. It was on that day that one of our traders traded for us for the last time, but another one made a nice bit of profit. Apart from these two "outliers", our performance was essentially balanced.

Piers Curran: Once you manage to avoid the big losses, you are already half way through to lasting trading success. On the other hand, that obviously also means being humble – since excessive position sizes with astronomical profits are impossible in the first place. However, that is exactly what most people want.

Can you tell us about a particularly extraordinary trade in your careers?

Will de Lucy: Yes, that always reminds me of a trade that resembled a ride on a roller coaster. It was one of those days when the non-farm payroll data

Info

Euro Schatz Future:

Future contract for short-term German government bonds (maturity 1.75 to 2.25 years).

Euro Bobl Future:

Future contract for medium-term German government bonds (maturity five years).

Euro Bund Future:

Future contract for long-term German government bonds (maturity 8.5 to 10.5 years).

Spread Trade:

Combined strategy with two (bond) futures of different maturities. Example: Long Bobl future and short Bund future if the spread between the two contracts is above average and the trader expects a return of the size of the spread.

Non-Farm Payrolls:

The economic data arguably given most attention. The US Bureau of Labor Statistics publishes, among other things, data concerning the number of employed people (excluding some areas such as agriculture). Publication is always on the first Friday of each month.

Squawk Box:

Loudspeaker announcing the most important news.

were made public. I was a little impatient and promptly jumped into the market much too soon. After the briefest of periods I was a whopping 30,000 euros on the losing side and I already heard the heavy steps of our risk manager on the trading floor making his way to my desk. The funny thing about that was that at the very time that he looked at my screen ready to confront me, the market had done a U-turn and my position was again back at around zero. That meant that I was spared the worst. In the end, I was even able to achieve a nice profit on that “volatile” day.

Piers Curran: I remember something as well. One year almost to the day after the devastating tsunami in Asia in late December 2004, the news came over our squawk box that there had been an earthquake in California that might lead to a tsunami. Since the terrible tsunami had happened almost exactly one year earlier, the issue was very much alive in the media and therefore in the minds of all the traders. I immediately responded to this information and went long on 2000 contracts of Schatz futures. The reason for that was my assumption that this news of a catastrophe would cause a flight to quality such as safe types investments like German government bonds. And

that is exactly what happened. Suddenly, though, what came out of the squawk box was that the earthquake had probably been no more than a minor tremor and would never ever be followed by a tsunami. Thereupon I immediately smoothed my positions – as it turned out PRECISELY at the high. That was the perfect trade – the kind you like drawing into a chart after the event. Buy low, sell high (laughs). That is the kind of thing that really happens rarely, but when it does it is simply awesome! Especially when you are in on this trade with a decent position size as I was.

Can you remember the profit you made on this trade?

Piers Curran: Must have been about 125,000 euros. And all that money in about 20 minutes – that is how long it took after my entry – before the news of the significantly less serious extent of the quake went over the squawk box. If you like, it was also a type of inefficiency that an automated computer program can probably not exploit as well as a human being can.

What do your concepts of technical and fundamental analysis look like?

Piers Curran: First of all, I have to say that we have not developed any completely new concepts. Instead, we put

together the existing things in such a way that it works for us. That obviously also means that the whole thing needs to adjust flexibly to market conditions and cannot remain constant over a longer period of time. I first look at the fundamentals because that is what ultimately moves prices sustainably. Technical constellations will then show me the most favourable entry and exit points. On the fundamental side, I incorporate macro-information such as the statements made by central banks and politicians but also factors such as terrorist attacks or other extreme events. The key thing is then to put these things into the right context and draw a conclusion for your trading. A nice example of the fact that technical factors alone are clearly less meaningful, is provided by the EUR/USD chart (Figure 2). Those who go against the market by way of divergence analyses have been caught off-guard several times.

Will de Lucy: Of course, we nevertheless incorporate technical factors – for timing purposes, as I said before. For example, I especially enjoy using fibonacci retracements for my entries and long-term trend lines such as the 200-day moving average to determine the overall market movement.

F2) Isolated Technical Patterns



A mere consideration of technical factors may be a double-edged sword. Here you can see multiple divergences between the relative strength index (RSI) and the price development of the EUR/USD that did not trigger any correction. Instead, the strength of the initial, fundamentally based impulse (explanation in Figure 1) was the driving force.

Source: www.cqg.com

F3) Long Trade EURO STOXX 50 Future



On the morning of 21st January we entered the EURO STOXX 50 Future long. This area corresponded to a previous double top as well as some other intermediate lows. In addition, since 20th January several successive higher lows and higher highs have been marked so that we had a relatively low-risk entry at this point. At the blue line we have smoothed the position by way of a profit target.

Source: www.cqg.com

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Which markets do you trade and where do you see your strengths compared to other traders?

Piers Curran: Essentially, we trade whatever currently promises good opportunities. So we basically proceed selectively and take a look at different markets. In January we mostly traded EURO STOXX 50, S&P 500, EUR/USD, the Bund and oil. As I said earlier, we rely on our fundamental and technical evaluations and make discretionary decisions on the basis of our experience. And experience is what a lot of all the trading is all about.

Will de Lucy: One of our strengths is the combination of analysis and data based on experience. In trading, the latter above all means being selective. So do not just jump on the bandwagon of each minor movement but make an average of five to ten trades a day. Obviously, my chart adjustments do vary, but I would not look at very short-time charts such as 1 or 2-minute charts since there is virtually only random noise to be seen there.

Piers Curran: I believe the crucial word is “adaptive”. In trading you need to adjust to market conditions, and that does not work with a rigid methodology. The market behaves irrationally every so often and you need to be prepared for that. We cannot

trade all that in a “controlled” way by using firm rules, but we need to readjust time and again. So there is no such thing as a target system, but there is only lifelong learning and changing.

Do you position yourselves prior to any news?

Piers Curran: No, certainly not. It is important to us never to have a large open position right before the publication of key data or even to open one first. The data may differ very considerably from expectations – in both directions. Usually, we take all our positions out of the market before the publication of important data and smooth at least portions of the open trades in the case of less important data.

What is the benefit of the squawk box here in the office?

Piers Curran: Some trading desks have Reuters or Bloomberg with all their information but frankly, we do not want to have that much input. All the important news comes to us from the squawk box, and the uninteresting things are filtered out. Besides, it is good not to have everything on the screen but also to take something in acoustically, which complements our trading perfectly.

Is there any restriction to intraday trades?

Will de Lucy: We trade intraday nearly exclusively, but now and then there are trades that we hold longer, i.e. for several days, in extreme cases even for one to two weeks. A nice example of that is the short trade in the Bund future following the rally in August 2010 which in my opinion was totally excessive (Figure 4).

What are the fundamental rules of your risk management?

Piers Curran: Here, too, we leave ourselves – and also our junior traders – some discretionary scope. Of course, there is no question that there is an overall risk management. If, for example, one of our traders has a risk limit of 1000 euros a day, he may risk a maximum of 50 per cent of that amount, i.e. 500 euros, for one single trade. Normally, of course, the risk ought to be significantly lower in order that there may be a few trades in there every day if things go badly. But as I said before, the decision is that of each individual trader as long as the overall risk management is adhered to.

Do you pay any attention to the risk-reward ratio (RRR) before entering a trade?

Piers Curran: In general I do, yes. For example, I would not risk 1000 euros for the potential profit of 100. Apart from that, though, I do not do a lot of calculating

F4) “Long-term” Short Trade in Bund Future



Here we have shorted the bund future following the massive August rally. The previous day was the first day of the rally which saw considerable pressure to sell. Hence we started the short trade below the previous day's low. After the position was in the profit zone, the market again turned upwards. The third upward day was very painful to us, and we debated for a long time whether we were able to continue to hold the position overnight. Only slightly higher prices would have triggered our fixed risk limit since our discretionary possibilities had been exhausted. The market subsequently plummeted, and we exited this (to us very long-term) trade at 130.30 by stopping above the previous day's high.

Source: www.cqg.com

there. Some traders set a target as soon as they have earned their risk but I take a very dim view of that. So if I enter at 100 and my stop is at 95, why then should I exit at 105 (RRR of 1.0)? This I would never arrive at on the basis of pure mathematics but on the basis of the chart and the way prices behave. If there are good reasons for the trade and my target is at 103, I would make the trade even at a ratio of less than 1.0. Obviously, a high RRR is nice when it happens. But depending on market behaviour, I can still increase my original target and optimise the whole thing on the basis of the data gained by experience.

What types of orders do you actually use?

Will de Lucy: I use market orders nearly exclusively. If a trade is good, then it is good and I want to enter the position. Period. I will not go on to haggle with the market about each and every penny because that would cause me to risk missing the movement. However, in volatile markets I also place limit orders when the market oscillates and it looks as though I will probably get into the trade more favourably that way. In other words: In that case I use the short-term random fluctuations

of the market for optimisation purposes.

Piers Curran: I would estimate that I use 60 per cent market orders and 40 per cent limit and stop orders.

Do you do any scaling in or scaling out?

Piers Curran: I frequently scale out of trades. I think it makes sense to at least partially realise the profit from a good trade by way of target. By contrast, I scale in less often. But when I do, I put several grouped orders, for

The whole thing must happen at strategic points and always needs to be in sync with risk management.

Do you also look at the behaviour of markets and positions among yourselves?

Piers Curran: Yes, every so often we look at correlations. Since we trade in a highly discretionary manner and we can also coordinate our activities at all times, there is hardly any risk of the two of us holding the same or a similar position twice, which would necessarily increase overall risk.

“We hedge our trading on the basis of our risk management.”

Have you examined what conditions trigger the biggest drawdowns in your strategy?

Piers Curran: Since we hedge our trading on the basis of our risk management,

that will ultimately be connected to market conditions. Whenever we have high market volatility, things usually run optimally. As short-term traders we live on the movement of prices. But when markets are very quiet, there is little money to be made. During such phases of the market, a drawdown may occur now and then since we may make the occasional trade that in the end does not have the necessary potential. Otherwise there is, of

example, around a resistance area. So if the resistance level is at 100, I spread my entry order evenly at 99, 99.50, 100, 100.50, and 101. If the resistance level is not quite reached then and the market turns downwards early, I will at least be in it with a portion of the planned position size.

Will de Lucy: I proceed similarly. Obviously it is important not to turn the scaling in into a systematic “cheapening” (laughs).

F5) False News about Microsoft & S&P Spike



On 27th January, the day of the interview, the squawk box in the trading room carried the news that Microsoft had already published its results before the close and they had turned out to be far better than expected. Thereupon its stock as well as the Dow and S&P future shot upwards. Shortly afterwards the news turned out to be false (again via the squawk box) triggering the opposite reaction. Such events, too, never fail to “enrich” the day of an intraday trader since it is possible to make (and lose) money on the basis of totally false information.

Source: www.cqg.com

course, the classic period of “bad weeks” during which we have a number of losing trades that add up to a hefty drawdown.

Which software do you use and how are your trades cleared?

Piers Curran: Our entire software, i.e. the data feeds and all the tools, come from CQG. Our trades are cleared via Chicago-based Penson Futures.

You not only trade your own money, but also train new traders at the same time. Most of them do that from other locations by remote link. What benefits does that have?

Will de Lucy: Obviously, we also have traders right here who have been with us for some time. But most of our traders actually do trade by remote link, and they do so for a simple reason: Fixed costs are significantly lower. If you rent a trading booth here in London, then that will cost an average of 3000 to 3500 pounds a month. In addition, you will then have to live in London, which not everybody can do either. A remote access lowers these costs by a factor of ten and offers especially neophytes a good alternative. Conversely, we can profit from the network effect since every so often

good ideas develop from the permanent online discussions. In particular, the chance to discuss positions and setups is a benefit that should not be underestimated. The remote variant we also use in order to train the students at the BPP Business School, albeit with a simulated account.

What difficulties are there?

Will de Lucy: Depending on the market environment I have to vary my attention to the development of our new traders. I have to be careful to manage my mentoring and risk management duties in line with

the opportunities I have to trade. At times this means I am taking the new guys through a live trade whilst I am in the position which certainly adds to the pressure of managing correctly. On average, however, the combination works pretty well.

What advice would you give to novice traders?

Will de Lucy: Besides all those things like risk management and self-perception that we have already discussed, I would recommend that novices begin to develop a consistent trading style in the course of their trading. I specifically mean this in the

sense of a goal, i.e. a challenge. It is not important to make a lot of money but to work consistently and in doing so, use a strategy that systematically generates reproducible trades – in contrast to the well-known “random hits”. To achieve this aim, you obviously need discipline. But expectations of achievable returns ought to be realistic, i.e. rather low.

Piers Curran: I would definitely recommend paper trading. By now virtually any trading software comes with a simulator which allows you to engage in some “dry practice” and try out various things. Obviously, you must not

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fool yourself and play with “what if” positions, but you should make a note in real time of all the positions entered and evaluate them in a trading diary. That much discipline is indispensable. Of course, it is even better for you to have professional support, i.e. a mentor who is by your side ready to advise you and ideally monitor your risk management. Only this will make many a trader conscious of the fact that they are possibly just doing the opposite of what actually is meant to correspond to the strategy they had devised earlier.

Which trading rules are indispensable?

Will de Lucy: There are quite a few of them, and nevertheless everybody has broken them at one point in their careers, including me (laughs). It is important to say that it is not the worst eventuality to break these rules when you first start trading, risking a small size. The reason for this is that hopefully the pain you feel by breaking the rules will prevent you from making the same mistake when you are trading on a larger size. The key word is discipline, if you do not have this you will have no control over your trading in the long run.

When has a professional level been reached in your opinion?

Will de Lucy: It is all a work in progress whose transitions are in flux. But speaking from my own experience, you are professional when over longer periods of time profits are made constantly and steadily. Obviously, the size of these profits depends on the base capital and the position sizes. What counts ultimately is the long-term development, the big picture. I think that as a trader making a consistent profit of 3000 to 5000 pounds a day you have reached a level that is definitely highly professional.

Piers Curran: But even professionals make mistakes, that much I can confirm. Just think of the classic “fat finger” (inadvertently oversize order by pressing several keys on the keypad). Reminds me of a nice story: A trader I knew at Goldenberg Hehmyer was once eating a sandwich at his workplace around noon when a crumb dropped into one of the interstices of his keyboard. While trying to extract that crumb, he somehow sold Schatz futures causing a loss of 5000 euros.

You hold seminars at BPP Business School. What can you give your students there to take along for their trading careers?

Will de Lucy: The event opens most students' eyes to the fact that besides all the indepth academic economic theory there is also the more basic realities of the market. I do not want this to mean that success in trading is easy but only that the basic principle of supply and demand is simple and yet the resulting development of a price works so well. At university, they keep discussing market efficiency but in practice everybody knows that there is no such thing. We said at the beginning that the markets have become more efficient as a result of computer trading – they certainly have. But that does not mean that no more money can be made with trading. Just look at the last ten years, what movements there were and how high volatility was. Perhaps in the future the upward and downward cycles will be even faster and shorter, who knows? There are always some imbalances and no central bank in the world is reactive enough to quickly adjust conditions to them. In any event, the markets will continue to present profit-making opportunities.

The interview was conducted by Marko Graenitz



F6) Loss Trades with Oil

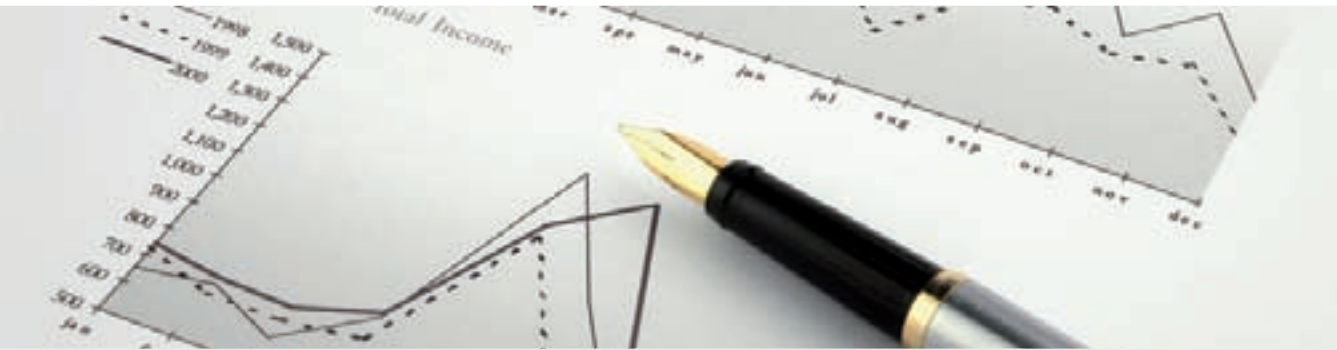


In the case of oil there was a long-term overall upward trend that cannot be seen here. We started our first long attempt at 91.32 dollars, but were stopped out at 90.52. During the following consolidation, we again went long at 89.87 dollars only to be stopped out again at 89.37. This example is an illustration of the fact that the stops are our life insurance policy.

Source: www.cqg.com

SEMINARS

Date	Seminar	Firm	Location	Website
25.02.2011	The London Investor Show	Investor Conferences Ltd	London	www.londoninvestorshow.com
26.02.2011	An Introduction to CFD market strategies with David Land	CMC Markets	Sydney	www.cmcmarkets.com.au
26.02.2011	Learn to trade CFDs and FX with CMC Markets	CMC Markets	Auckland	www.cmcmarkets.co.nz
26.02.2011	Stock Market Training	WIN Investing	Newcastle	www.wininvesting.co.uk
28.02.2011	Trading With Charts Seminar	IG Markets	London	www.igmarkets.co.uk
28.02.2011	Stock Market Training	WIN Investing	London	www.wininvesting.co.uk
29.02.2011	Trading Options for Greater Profits	eSignal	USA	www.esignallearning.com
01.03.2011	Stock Market Training	WIN Investing	Brighton	www.wininvesting.co.uk
01.03.2011	Discover the Secrets to Winning Trades	eSignal	UK	www.esignallearning.com
02.03.2011	Stock Market Training	WIN Investing	Reading	www.wininvesting.co.uk
02.03.2011	Discover the Secrets to Winning Trades	eSignal	Australia	www.wininvesting.co.uk
03.03.2011	Discover the Secrets to Winning Trades	eSignal	USA	www.wininvesting.co.uk
10.03.2011	Stock Market Training	WIN Investing	Swansea	www.wininvesting.co.uk
10.03.2011	Discover the Secrets to Winning Trades	eSignal	USA	www.esignallearning.com
11.03.2011	Stock Market Training	WIN Investing	Cardiff	www.wininvesting.co.uk
12.03.2011	Trading Stocks for Greater Profits	eSignal	USA	www.esignallearning.com
16.03.2011	Stock Market Training	WIN Investing	Tunbridge Wells	www.wininvesting.co.uk
16.03.2011	Discover the Secrets to Winning Trades	eSignal	Australia	www.esignallearning.com
17.03.2011	Stock Market Training	WIN Investing	Milton Keynes	www.wininvesting.co.uk
17.03.2011	Discover the Secrets to Winning Trades	eSignal	USA	www.esignallearning.com
22.03.2011	Stock Market Training	WIN Investing	Leicester	www.wininvesting.co.uk
23.03.2011	Discover the Secrets to Winning Trades	eSignal	Singapore	www.esingallelearning.com
24.03.2011	Trading the Worlds Financial Markets	Gann Management Ltd.	London	www.gann.co.uk
24.03.2011	Stock Market Training	WIN Investing	Gravesend	www.wininvesting.co.uk
26.03.2011	Stock Market Training	WIN Investing	Heathrow	www.wininvesting.co.uk
26.03.2011	Stock Market Seminar	Knowledge To Action Ltd.	London Victoria	www.knowledgetoaction.co.uk
27.03.2011	Stock Market Training	WIN Investing	Gatwick	www.wininvesting.co.uk
27.03.2011	Stock Market Seminar	Knowledge To Action Ltd.	Surrey Richmond	www.knowledgetoaction.co.uk
29.03.2011	Discover the Secrets to Winning Trades	eSignal	UK	www.esignallearning.com
30.03.2011	Discover the Secrets to Winning Trades	eSignal	Australia	www.esignallearning.com
31.03.2011	Workshop Day Trading and Swing Trading	Trader Tom	London	www.whichwaytoday.com
31.03.2011	Discover the Secrets to Winning Trades	eSignal	US	www.esignallearning.com



When Is the Fed Going to Raise Interest Rates?



Jochen Steffens

Jochen has been working as an independent trader for more than twelve years, specialising in trading with futures, derivatives, and high risk warrants. In addition, he has developed several highly profitable strategies for short to long-term speculative trading, one of which is the target-trend method presented here. Since 2008 he has been running Stockstreet GmbH (www.stockstreet.de), editing Steffens-Daily and other market newsletters.

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One of the most important questions of 2011 is: When is the Fed going to end its zero interest-rate policy? Time and again past experience has suggested that rising interest rates may put an end to a rally or may at least seriously weaken the dynamism of the economy. For the current rally of the US indices this means that it will continue until key US interest rates are raised or such a decision is in the offing. In an environment of rising interest rates the markets are going to move sideways. However, should interest rates be raised to too high a level, for example to counter the risk of high inflation, we will have to expect a major consolidation. And this means that the question of when the Fed is going to raise key US

interest rates will be of crucial importance to the subsequent development of the markets.

Until the great crash of 2000 to 2003 there was a simple rule: Whenever the ISM index of the manufacturing sector exceeds a

sustained level of 55 points, the Fed will initiate a period of interest-rate hikes. However, the Fed broke this rule right after the crash of 2000. It did not even raise

key interest rates when the ISM index exceeded the 60-point mark. The underlying cause of this inactivity was the extent of the crash and its economic impact. There was simply too much of a danger of a premature interest-rate hike killing off the recovery of the US economy just as it had started.

Even in the current situation we still have not seen a reaction from the Fed although the ISM index has already broken the 55-point barrier significantly and consistently. Obviously, the Fed's current caution is again related to the drama and impact of the crisis in the financial markets. The very weak US labour market especially hinders the US Federal Reserve in responding. – although experts are still debating whether in the current situation low interest rates will actually

result in stimulating the US labour market. There is furthermore a danger of a bubble developing in a new asset class that resembles the one experienced by the US property market after the end of the crash of 2000. Yet the Fed has decided to ignore the ISM index as a bellwether until further notice, making the erstwhile rule finally obsolete.

Consequently, finding an answer to the question of when exactly is the Fed going to raise interest rates, has been made considerably more difficult. The current crisis – bearing a resemblance to the crash of 2000 – must therefore be seen as a special case whose outcome is equally difficult to predict. This is not exactly a favourable environment for medium and long-term investors waiting for a relatively clear exit signal.

However, a different kind of development might force the US Federal Reserve to respond by raising interest rates. While the Fed is still fighting the deflationary effects of the crisis, there have recently been more and more signs of the inflationary effects of the low interest-rate policy asserting itself. For example, consumer and producer price indices have again reached the same excessively high levels which were seen prior to the crash in the financial markets. Meanwhile,

this impression has also been corroborated by other US economic data. If these signals are confirmed, the Fed would be forced to raise interest rates in order to check inflation. In that case, it could no longer make any allowances either for the US economy or the US labour market.

The development of price indices in the US is an early indicator of the possible beginning of the end of the zero interest-rate policy perhaps as early as this year. However, since unemployment in the US is still too high to guarantee sustained growth, the first inflationary tendencies may yet be ignored by the Fed for a while. But if prices continue to rise strongly, the US Federal Reserve will have to respond. After all, the destructive nature of galloping inflation is similar to that of deflation. Since the Fed cannot raise interest rates significantly in one fell swoop, it needs to react as soon as price developments indicate inflation risks that are visible to everybody. So as early as late this year you can expect the first few interest-rate hikes, the result of which is that the rally will turn into sideways movement.





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