Standard

Online Share Trading

Education newsletter

Issue # 22
2nd June 2008

Obviously the thing to do was to be bullish in a bull market and bearish in a bear market.

Jesse Livermore

The Buffett Way with Alec Hogg

Alec Hogg of Moneyweb once again attended the Berkshire Hathaway AGM in Omaha, Nebraska. Known as the "the Woodstock of capitalism", some 30,000 shareholders attend and listen to Warren Buffett and Charlie Munger for four and a half hours as the duo answer questions on investment-related issues.

Alec will now be doing a 60 minute presentation to Standard Online Share Trading clients on the experience and views from his trip. Seats are limited, so be sure to RSVP online.

Cities/Dates;

- Cape Town 10 June
- Durban 12 June
- Johannesburg 23 June

To book log onto the website and on the menu under Help and education ➔ face to face classes.

Client courses for the next few weeks

These courses are *exclusively for Online Share clients* and all are free. To book for one of these courses log onto Online Share Trading and go to; Help & Education ➔ Face to face classes

Johannesburg

- Understanding company financials and announcements (21 June)

Durban

- Understanding company financials and announcements (07 June)
- A practical guide on how to effectively use the website (11 Jun)

Pretoria

- Intro to technical analysis (part 2) (07 Jun)

Cape Town

- A practical guide on how to effectively use the website (04 Jun)
- Truths of the Market and Trading Skills (05 Jun)

TALK
From the editor

Commodities continue the run as they keep the local market bobbing along at record highs (or just off those highs as I write this). With this in mind we have a review of an excellent book for traders and an article on mechanical trading.

There is also a couple of JSE/AltX presentation and we're heading off to PE next week and we've got the Buffett Way with Alec Hogg. In all cases seats are as always limited so please book early if you wish to attend.

All the best
Simon Brown
Head: Education & Media
Online Share Trading

WEBSITE – NEW FEATURE
Transfer cash

Last week we launched the latest feature on the website, the ability to transfer cash between accounts.

You will find the function on the menu; My account ➔ transfer cash.

Importantly you can only transfer between your own accounts or accounts you have power of attorney over and that are under your own log in.

Online Share Trading

TRADER
Benefits of Mechanical trading

From an early age, we are told to think that losing is bad. We live in a competitive society where we are conditioned in our business, sporting and social environments to think that we must win at each and every endeavour. As we grow older the 'competing to win' mindset becomes hard-wired into our thoughts, resonating through all facets of life. It has a profound influence on us each day, both consciously and subconsciously.

We are conditioned throughout our lives by our parents, peers, media and other environmental and social stimuli to feel negative emotions such as anger, embarrassment, disappointment and frustration when we lose or are wrong.

When we lose we think we have failed. We worry what others will think and how society will view us because of the loss. We know the winners are praised for their accomplishments.

In share trading, negative reactions to loss trades are no different. The same pressures, beliefs, expectations and disappointments are evident. Unskilled traders see losses and drawdown as failures. Resultant inconsistent trading often leads to complete withdrawal or avoiding a trade for fear of more disappointments, not to mention poor results, and diminishing cash reserves.

People in this position are different from a skilled trader who looks at the market objectively and consistently. Both have experienced the same conditioning from their environments. However, skilled traders have learned to think differently.

To become consistently successful in the share market, sophisticated traders have learned to think from the market's perspective in terms of probabilities—not in terms of winning and losing on individual trades.

Winning, losing, new portfolio equity highs and portfolio drawdown are seen by the skilled traders as the probabilities playing themselves out in the market. These are normal occurrences for the skilled trader—in fact, he or she expects them to happen.

To make the transition from a novice trader's perspective to that of a skilled trader who thinks from the market's perspective means changing ingrained beliefs and re-programming our mindset to a new understanding.

So what do we mean by probabilities, and what is the source of these probabilities? I mean that you must understand what your probabilities of success/failure are from the way that you trade the market. These probabilities are determined by the number of times that you win from all your trades and how large your winning trades are compared to how large your losing trades are.

When this is measured through research over a large sample of trading events, through different types of markets, you can determine the probabilities of success, or edge, that you have for the way that you trade. If you cannot understand or define your probability of success, then you are gambling and should not commence trading until you do understand your probabilities of success.

Researching a mechanical trading system will uncover your probabilities of success for a defined set of unambiguous entry and exit criteria. This is how you can determine whether you will have an edge in your chosen market and trading timeframe before you place a single trade. The next step is to take the mechanical trading system into paper trading and then into live trading.

Many novice traders draw rash, subjective and impulsive conclusions from small samples and brief experience. Immediate success is craved, if only for building confidence and self determination. This is another trait learned from modern society, instant rather than delayed gratification. It is normal to want to win as many times as possible, especially early in a new enterprise. The confidence gained from success leads to an expectation of future success. However, sophisticated traders define their edge precisely, know the probability of success that it represents, know the term over which it delivers success, and know an adequate sample size is required for long-term results.

Mechanical traders learn to think from the markets perspective because executing the mechanical system's rules, which emanate from the market, helps the trader transition their thinking from that of a societal paradigm, which causes the trader to execute according to society's rules, to that of a market paradigm. The old paradigm shift! I'm sure you've heard of that before. You see, a carpenter sees everything in terms of hammers and nails. Hammers and nails thinking doesn't work in the market.

Thinking from the market's perspective means that you will no longer think in terms of 'right' or 'wrong' or 'win' or 'loss' on the trades that you buy, hold and sell. Taking new trades and closing trades based on your edge simply means you accept the probabilities of your edge. Whatever the result of individual trades, you can be at peace knowing that the overall outcome will reflect the statistical probability of the system over a large sample of trades. Thinking from the market's perspective means that you expect to have winners, losers, new portfolio equity highs and portfolio drawdown.

Most traders do not understand, or fully accept, this concept. Many dismiss it as unimportant—but most of these traders are destined to failure. I suggest that thinking from the market's perspective is an absolutely essential component in the make-up of every successful trader.

Take time to seriously consider how you think and feel about each trade you execute. Critically analyse your feelings and actions to determine what you need to do to better align yourself with thinking from the market's perspective. In order to embark on this path I suggest that you seriously consider either acquiring or developing a mechanical trading system with a positive mathematical expectation and trade it to help you transition from a societal paradigm to a market paradigm.

Understanding that you need to learn to think from the market's perspective is an important foundation in becoming a consistently successful trader.

Gary Stone
intelledgence.com

COLUMNIST
Mr Big!

Trading, like dating, is counter-intuitive. There's something about money, or lust, that makes people lose their minds.

How else do you explain the endurance of the Jane Austen fantasy that men like women for their mind, character and wit? An Alpine profile, legs to China and the virtue of a Russian arms-dealer would tick the boxes for most blokes.

Right now, the market is going through a similar Austenesque phase. With the exception of the heavyweight commodity shares, a whole whack of blue-chips are looking cheap. Many retailers, banks, and property stocks are at five-year lows.

For an investor, maybe, buying low is smart. Over time, a good share will have its day. But investors are old and remember the First World War. They bought Sasol when it was R2 a share, a house in Plett before the place had plumbing, when nature's call was answered in a shack out back, a copy of the Sunday Times close to hand. Investing is long term, and takes patience, careful planning - and the luck to live long enough to spend it.

Trading is entirely different; trading is to investing as a fruit fly is to a baobab. It's short term. It is survives about as long as it takes to drown in a glass of red wine.
Skilled traders understand this, and are content to follow the price action, long or short, regardless of quality of the underlying equity.

And yet the chick-flick mentality persists. The romance of it, the belief that Big, or whatever the guy with the chin is called, will close the deal with Carrie. McDreamy will put knife in, and the ladies of Wisteria Lane will have their edges clipped.

Traders know that a happy ending requires a whole different plot. It's not Julia Roberts and Richard Gere. It's Divine Brown and Hugh Grant.

Right now, looking for love in the markets is a dangerous thing. There are many, tempting shares, skirts hitched, waiting for the window to roll down and negotiations to begin. SBK looks especially fetching; I'd wave my wallet at WHL too, and Massmart. And sooner or later, SHF will have its day. So will INL, the little darling, and who knows, even the pimply Simmers could be worth a second look.

The trouble is, there's just no way of telling when, or why, the recovery will begin. To trade them based on nothing more than their underlying quality, with a leveraged instrument, is to court disaster. The time frame is unknown, and frankly, unknowable. Because leveraged instruments are time sensitive, trades need to be tactically sound; a planned entry level, and a planned exit. The entry level should, I'd say, be rooted in technical analysis. So should the exit point. And of course, the traders penicillin - a stop loss, so that when things go wrong, you get out of a losing position with a small loss.

It's not to say there's no room for moonlight and roses. A good trader has an old fart portfolio. The steady investments that will accrue value over time, to fund retirement, pay for a heart bypass and the bottle of blue pills. Here it pays to seek out good companies, with sound fundamentals.

I know all this. But you know how it is. You wake up, roll over to find a yourself face to face with a woman whose name you couldn't remember if your life depended on it, looking back at you with vodka-tinted eyes, trying to figure out who you are and how the heck she can get rid of you before you ask her to make breakfast.

It's just so darned tempting to forget the rules and jump right in. Short the market because it's run too hard too fast; going long because it seems to have bottomed.

I reckon there's never a perfect time to trade. There's no match made in heaven. Each trade succeeds or fails based on its own technical merits. There is really no bottom or top; there's just the trend.

Now, having said that; do you come here often?

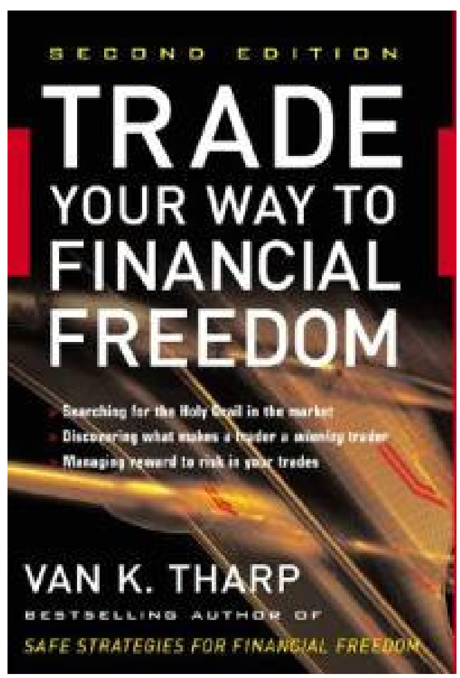
Peter Principle
(a non du plume to protect future earning prospects)

REVIEW - BOOK
Trade your way to financial freedom

Trade your way to financial freedom
by Van K. Tharp

This is a great book, even a brilliant book — but nobody will read it. The problem is that Tharp looks at trading from a deeply theoretical perspective, offering no quick fixes or solutions, and, while this is exactly what makes it great, it is also why most won't read it. People want instant answers, they want secrets, not effort.

Tharp is the acknowledge authority on positioning sizing; however, this book tackles the entire ambit of trading, from start to finish, and he significantly expands on Elder's book "Come into my trading room" which we reviewed in Issue 10*. However, the highly enjoyable Elder book does try to play to those looking for instant answers; hence, Tharp's book is by far the better one for traders.



The reality is that trading relatively easy and very rewarding, but, like anything else, one has to learn the ropes. Trading requires learning and acquiring skills. The process of opening a trading account "doth not a trader make".

Delving into the book, two lessons really hit home. First is that Tharp proves that a random-entry system (throwing a dart or tossing a coin) can produce a profit if one has excellent exit rules and trade size (Tharp calls this "position sizing"). The second major lesson follows on from the first; ask a trader what's the most important part of trading, and they'll say "the entry". However, I have long held this to be a false belief, as I believe the random system proves. So, what is the most important part of trading? Selling! Think on it for a moment; it is the selling that determines the profit or the loss, not the buying. Profits can flow only from selling.

Tharp also spends a lot of time dealing with the various biases we have to deal with in order to be successful. A bias is something which you believe to be true, but for which you have no proof, or, worse, which is not actually true. This is issue I have long spoken on in my seminars; biases can only be obstructive — and traders should earn to identify them, and eliminate them.

Other issues covered include: different entry systems, exit strategies, understanding risk and how it affects profits, managing position sizing. Tharp covers every aspect of trading, albeit from a theoretical angle.

Aspirant (and experienced) traders should read this book — but do not expect it to be an easy journey.

** Back issues of the newsletter are on the website under help and education ➔ educational newsletter.*

Simon Brown

JARGON BUSTING
Trade balance

A country's trade balance reflects the difference between exports and imports of goods and services. The trade balance is one of the biggest components of the Balance of Payment, giving valuable insight into pressures on country's currency.

Surpluses and Deficits
A positive Trade Balance (surplus) indicates that exports are greater than imports. When imports exceed exports, the country experiences a trade deficit. Because foreign goods are usually purchased using foreign currency, trade deficits usually reflect currency leaking out of the country. Such currency outflows may lead to a natural depreciation unless countered by comparable capital inflows (inflows in the form of investments, FDI - where foreigners investing in local equity, bond or real estates markets). At a bare minimum, deficits fundamentally weigh down the value of the currency.

Ramifications of Trade Balance on Markets
There are a number of factors that work to diminish the market impact of Trade Balance upon immediate release. The report is not very timely, coming some time after the reporting period. Developments in many of the figure's components are also typically anticipated well beforehand. Lastly, since the report reflects data for a specific reporting month or quarter, any significant changes in the Trade Balance should plausibly have already been felt during that period - and not during the release of data.

However, because of the overall significance of Trade Balance data in forecasting trends in the Forex Market, the release has historically been one of the more important reports out of the any country.

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ROAD SHOWS
JSE property showcase

You are invited to attend the JSE Property Showcase on Tuesday 3rd June 2008 at BMW Pavilion, cnr Portswood and Beach Roads, V&A Waterfront, Cape Town. Senior executives of JSE listed companies in the Property sector will present their businesses to you. Thereafter you will be able to meet them face to face. If you are interested in Property, this is a great investment opportunity.

Book soon if you would like to attend. Places are limited. There is no charge to attend this event.

Tuesday 3 June 2008, 17h30 for 18h00
VENUE: BMW Pavilion, cnr Portswood and Beach Roads, V&A Waterfront, Cape Town
PARKING: Parking available at the Granger Bay parking

PROGRAMME
- Fountainhead Property Trust (Anton Raubenheimer - CEO)
- Apexhi Properties (Gerald Leissner - CEO)
- Growthpoint Property Ltd (Norbet Sasse - CEO)

- Redefine Income Fund (Brian Azizollahoff - CEO)
- Hyprop Investments Ltd (Pieter Prinsloo - CEO)
- Capital Property Fund (Andrew Texeira - CEO)

To book please log onto the website ad you'll see the link under the special announcement section.

ROAD SHOWS
AltX construction showcase

AltX, the board for small, medium and growing companies at the JSE, invites you to learn more about the companies listed on AltX so you can decide whether to invest in them.

AltX now has a market capitalisation in excess of R28 billion, has listed 81 companies, and more are on the way. If you had invested in the AltX index since inception your portfolio would be up by 111%!

You will hear from AltX, as well as from the CEOs of some of the AltX listed companies, who will present their businesses to you. Thereafter, you will meet the senior leadership of these companies face-to-face. All these companies operate in the most popular sector on AltX: construction and infrastructure.

We look forward to seeing you there. There is no charge to attend.

Wednesday, 11 June 2008, 17h00 for 17h30
VENUE: The JSE Auditorium,

PROGRAMME

- Introduction to AltX, Ranjini Pillay, Marketing and Business Development – JSE
- Esor, Bernie Krone, CEO
- W G Wearne, John Wearne, CEO
- Sanyati Holdings, Rick Jackson, CEO
- Topfix Holdings Ltd, Webber Marais, CEO
- abe Construction Chemicals Ltd, Stan Stacey, CEO
- African Brick Centre, Beno van Graan, CEO
- Racec Group Ltd, Charles Harrod, CEO
- Wescoal, Andre Boje, CEO

To book please log onto the website ad you'll see the link under the special announcement section.

ROAD SHOWS
Getting started in shares

Online Share Trading and the JSE host a free one and a half hour educational seminars to the public. The seminars are designed to get you started on how to invest in shares and are open to the general public.

By attending one of the seminars, you will learn:

- Investing and returns
- Why invest in the share market
- How to develop an investment strategy
- Understanding the share market
- What determines the share price
- How to make money in the market
- How to choose companies to invest in
- How do you buy shares
- Next steps

Tell your friends and family and help them get started on the path to creating wealth.

Dates & cities

- **Port Elizabeth – 11 June**
- Johannesburg – 17 June & 02 July
- Pretoria – 24 June & 10 July
- Cape Town – 19 June & 30 July
- Durban – 12 June & 31 July

To book go to http://courses.standardbank.co.za

All venues are central and start at 6.00pm unless otherwise stated.
