

TUTORIALS IN APPLIED TECHNICAL ANALYSIS

A publication of Guppytraders.com Pty Ltd since 1996 ACN 089941560

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The Australian Internet Trading Weekly with independent analysis

Weekly for Saturday March 26, 2005 Based on Wednesday's Close 19 pages

Edited by Daryl Guppy with contributions from J Dalton, T D'Angelo, G Hewitt, J Atkinson, J Mitchell and P Rak

Guppy Trading Essentials Chart pak, Metastock, Ezy Charts & SuperCharts. Data from JustData, Paritech, MarketCast & theNextView.

Stocks mentioned in this issue

APA, CCE, STW, CPU,
GUD, XJO, S&P ASX
200, AZR.

Note. The more computer icons



appearing after a section heading, the more advanced the material.

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MANAGING MARKET DIPS

By Daryl Guppy

TRADERS' GLOSSARY SHAKEOUTS

These happen when, on a single day, prices, usually on the open, spike dramatically below existing support level or trend line and on low volume. This is a false trend break because at the end of the day, prices close above the trend line or support level. These false signals are difficult to manage when traders use an intra-day stop loss to manage a trade based on end of day signals. There is no easy solution to this problem, as it is difficult to tell at the time if the down spike is a genuine trend break or just a false panic driven move on very low volume.

Traders using intra-day stops may have little choice but to rejoin the trend on the next day as prices return to their previous levels. These false breaks, or shakeouts, are most common in very nervous or weak markets.

When markets dip, traders turn to well developed trading plans to make their decisions. A good plan allows for market action and sets logical conditions for trade exits and management. The objective is to avoid being 'shaken out' by what turns out to be a temporary price dip. The objective is to also recognise a significant price dip and to take appropriate action. We show in the notes below how each of the open case study trades are managed in relation to the current Index dip, and in relation to anticipated events, such as upcoming ex-dividend days.

These notes are based on Wednesday's close for this early Easter edition of the newsletter.

TYPE OF TRADE – OFFSET TREND LINE

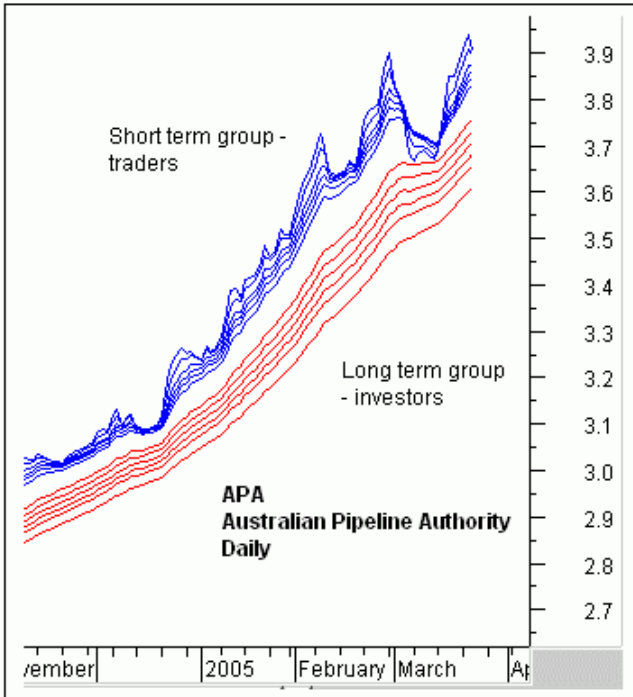
We use an offset trend line after a stock goes ex-dividend we start by using just a single point and project the line parallel to the previous line. We watch for future price action to confirm that the line has been correctly placed. In some developments the new trend is slightly steeper. In other, slightly more shallow. We cannot verify this until a second retreat and rebound point is created.

If the trend is more shallow, as with the APA example, then we assess the continuation of the trade on these factors:

1) What is the nature of the trend as shown by the GMMA? If it is still strong, then we can readjust the parallel trendline without fear that this lower price point is the start of a new downtrend.

2) What is the risk? In this example, the risk involved in lowering the trend line to take into account the new price action does not significantly increase the risk. It remains well within the parameters of the 2% rule. If the position of the new trend line had meant that risk grows to more than 2% then the trade is closed because this risk is unacceptable.

Plotting a parallel trend line provides a way to manage future price action. It does not provide a perfect solution, but it sets a framework against which we can assess developing price activity. Many of these trades are found using the peak to trough Metastock exploration covered in previous notes.

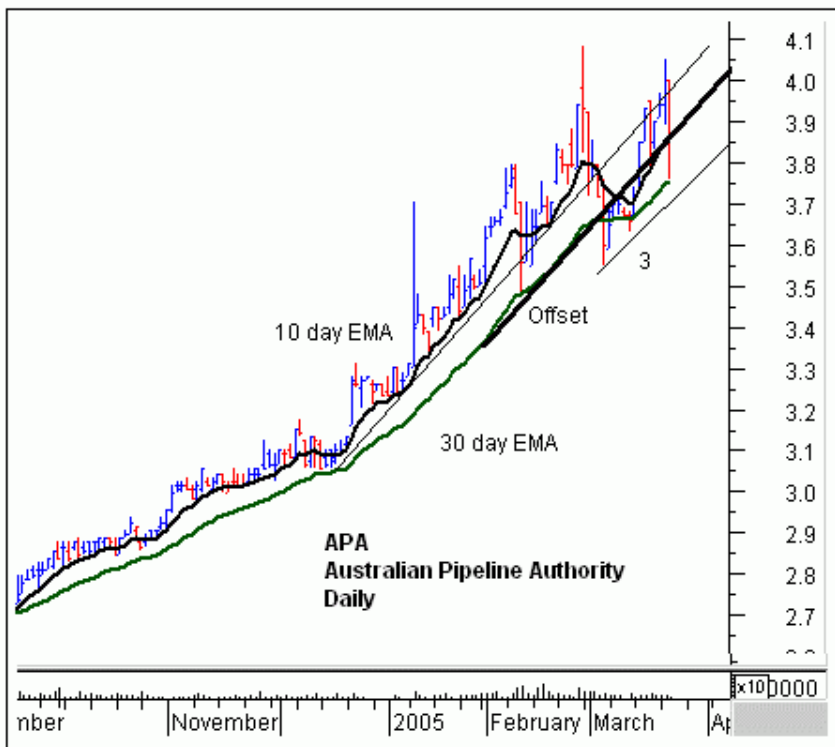


Trading plan

The objective is to use an offset trend line once an ex-dividend or earnings downgrade rebound is established. **Stop loss is based on the value of the offset trend line.**

- Trade identification starts with GMMA trend strength.
- **No change. GMMA trend relationship remains sound.**
- Substantial price pullback must already have taken place. This allows the trader to observe the strength of the trend. This is shown in area A on the GMMA chart.
- Trend behaviour is also confirmed with 10 and 30 day moving average relationships. This is a backup indicator. It is not the intention to use a moving average crossover signal in managing this trade.

No change. 10 and 30 day signals remain valid. There is a small dip, but not enough to cause any concern.



The offset trend line is plotted after the rebound has been proven. This may be adjusted as more of the emerging trend develops. Initially we use two points and plot the same slope as the original higher trend line. Entry is delayed until at least the second point is established. Traders wait for proof that the rebound is developing. The offset trendline is *initially* based on a single low point. This is similar to the way a lower trend line is plotted with a bullish flag.

The offset trend line is parallel to the original trend line

and uses a single starting point. Traders look for a rebound from the projected trend line to *confirm* the placement of the line and a continuation of the trend in a way similar to that which prevailed before.

This new trend line has been confirmed by two points. This means that any close below this trend line is treated as an absolute sell signal. The trend line is no longer a potential guide. It is now a verified plot. The emerging development of this offset trend retains the same slope as the original trend, but at a lower level. We show trend line 3 as a good emerging definition of the emerging trend. This is not relied upon by itself. It is combined with GMMA analysis.

No change in use of trend lines. Please note that this is not an Andrews Pitchfork construction. The resemblance is co-incidental. We will be running an article on constructing and using the Andrews Pitchfork in the newsletter after Easter.

- Stop loss is based on the value of the lower trend line.
Remains valid based on the new trend line plot.

Position size, stop loss and protect profit conditions

For tutorial purposes, we add APA as an example of this strategy. Entry for tutorial purposes is made at \$3.70 with the stop loss at \$3.65. This is a low risk strategy because the amount at risk based on the stop loss point is \$272. At this entry price we add 5,450 shares for a total cost of \$20,165. This keeps the trade at the same size as previous trades in the case study portfolio. We do this so all trades are easily comparable.

We added this trade as an example of the way to plot and use offset trend lines. The initial plot was based on an earnings release. Offset trend lines are typically used when a stock goes ex-dividend. This happens with APA on March 30. Dividend value is \$0.055. Using the techniques discussed in this case study example, we will drop the offset trend line and stop loss values by \$0.055 on the ex-dividend day to avoid generating a false stop loss exit.

Current Status

This case study remains open.

TYPE OF TRADE - COUNT BACK LINE TRADE MANAGEMENT

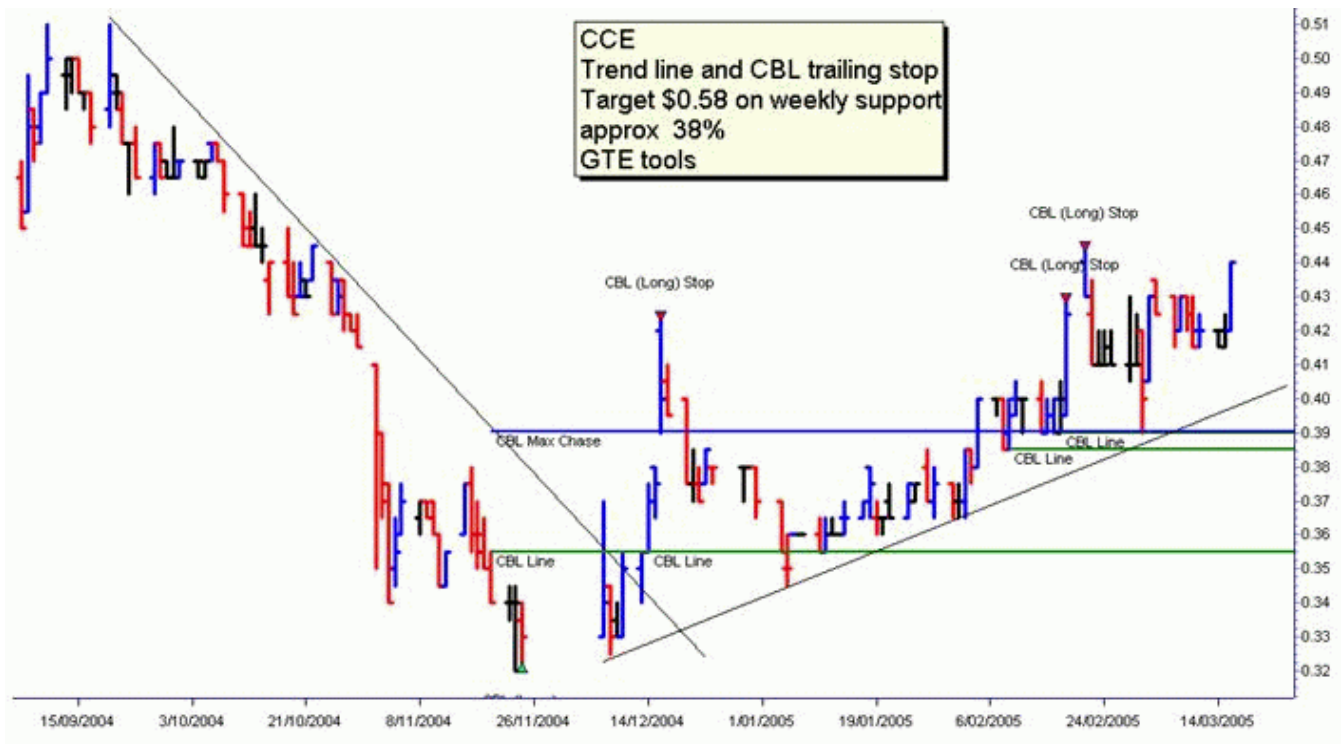


At the Continuing Professional Education module last week for the Society of Remisiers in Singapore, we used an example of a count back line trade available in the SGX link. We have added this to the case study newsletter portfolio, based on the details made at the presentations. We use the same screen shot of Clinical Cell CCE as the one used in the slide. The chart display is from the new Guppy Traders Essential Toolbox, which reads Metastock data. This small program is designed to work alongside Metastock and will be available for download within the next 2 to 3 weeks.

TRADING PLAN

The plan is to ride the trend using:

- A count back line as a stop loss and trend management tool.
- The straight edge trend line as the primary trend definition tool.
- As the trend develops, to use the Guppy Multiple Moving Average to understand the nature of the emerging trend and to verify exit signals once the trade is profitable.

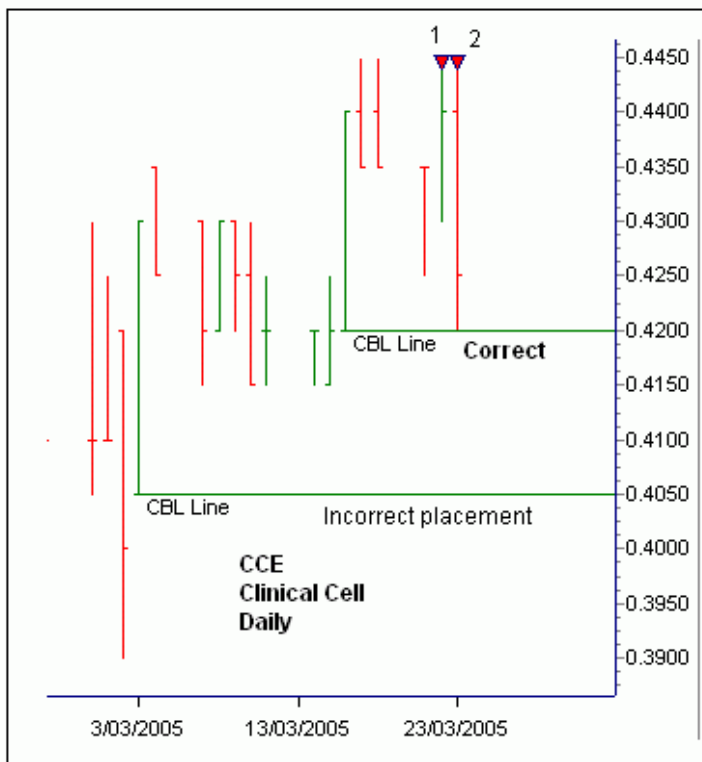


Position size, stop loss and protect profit conditions

For tutorial purposes, we buy an exact number of shares equal to \$20,000. Using the SGX link, we do not have to buy in lots. We buy 48,300 for a total cost of \$20,044. The stop loss is based on the count back line as shown at \$0.39. **Until the value of the CBL moves up beyond our entry point at \$0.415, then this trade remains unprofitable.** This trade puts at risk \$800 when initially entered.

Trade management

This trade is managed using the count back line as a trailing stop loss. There is no price objective, although a broad target is set at \$0.58 based on the resistance level on the weekly chart. The trade is also managed using the straight edge trend line. A close below either of these indicators is a signal to prepare for an exit.



- **Current stop loss is \$0.42. This is calculated from the second most recent equal high at \$0.445. This is shown as point 1. The CBL calculation based on the most recent equal high – point 2 – is not used. The placement of the line is a correct calculation, but the stop loss should not be lowered. The initial exit trigger in this trade remains at the higher value of the stop loss at \$0.42. This is slightly above our entry price, so technically this trade is now profitable.**

Trade status

Trade remains open.

TYPE OF TRADE - Exchange Traded Fund Strategy

No change. Trend trade remains open. Pullbacks are all consistent with the underlying trend.

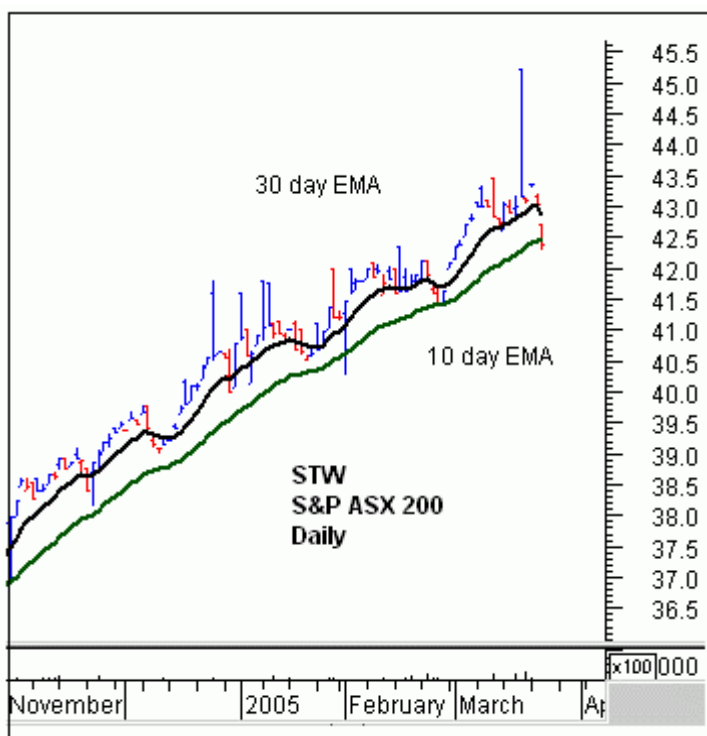
This remains a profoundly boring trade. It simply keeps going up. The main challenge with this type of trade is to develop the discipline to sit back and do nothing. Many traders have observed that trading, when implemented successfully, is quite boring. This is a good example of that observation.

The market offers a lower rate of return than that available from trading individual stocks, so why use an ETF strategy? This strategy offers two main advantages.

- Ease of management for exposure to the broad market.
- Access to dividends from the top 200 companies.

We note several points of market inefficiency in this fund. These spikes do not match the XJO performance. This market inefficiency can be helpful in making better than expected exits and entries. The danger is that as the XJO continues to stall there may be sudden STW dips. This is also market inefficiency at work.

Rather than repeat XJO analysis, we refer readers to the Market Outlook notes below as this



underpins the management of these types of associated trades. The objective is to use the ETF as a proxy for the XJO. The trade is closed whenever the first crossover signal is generated on either the XJO or the STW.

This technique uses a simple trend analysis tool to confirm when a trend change has taken place. As the conditions develop, we use defensive techniques to fine tune our decision making so that when the time comes, we can take the appropriate defensive action. The purpose of the newsletter is to educate. Part of that education process means giving readers the opportunity to examine a range of strategies as they develop and unfold in real time. Equipped with this information, readers are more informed and can make a better choice about how appropriate a selected strategy is for their particular circumstances.

Management notes layout.

These management notes provide an ongoing record of how a trade was identified, how it was entered, the management decisions made during the life of the trade, and finally the exit and evaluation of the trading strategy. We use colour highlights to make it easier for readers to select either the updated notes, or examine the decisions during the life of the trade example. **Each week the new notes are added and highlighted in bold blue.** The notes from the previous week are summarised and added to the existing notes in plain text. In some weeks we want to highlight an advance trading trigger mentioned in the previous week and acted upon in the current week. In this case we highlight the **relevant sections in bold green.**

To avoid crowded confusion on charts, we may delete the earlier chart comments from the latest version of the chart. Sometimes the text management notes may refer to a feature, ie circle A, that is not seen on the current chart. Readers will need to look at past issues to find the relevant management notes and chart with that feature.

We believe this layout method develops a useful reference of ongoing management of each case study trade. Readers can quickly see the new management notes while still having access to the previous management decisions.

GOT A QUESTION YOU WOULD LIKE TO ASK?

This is the only chat room where you will find Daryl Guppy and other recognised traders and authors. Post a question and get quality answers. Just visit and browse the discussion boards for educational information on trading techniques, using Metastock, and the questions that we all need to ask. This chat room has an international audience.



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TRADING DISCIPLINE: A KEY INGREDIENT TO TRADING SUCCESS

By J.Dalton

TRADERS' GLOSSARY

TRADING SYSTEMS

We all use trading systems. It is the methodical identification and development of trading opportunities and methods to trade them successfully that are at the core of all successful trading. Most traders do not trade well intuitively, so we always look for clear entry and exit signals. In developing a trading system, we have a choice. We can do it ourselves from the ground up. We can decide a particular approach suits our style and select a software program that will enable us to implement this trading style more effectively. These are light grey boxes. Or we can surrender all the decision making to another person, looking just for results and not reasons. In this case, we buy a black box. The prime determinant of success of any of these approaches is the discipline the trader brings to the system. This discipline impacts on his money management, and directly affects the long term outcome of his trading career.

After such a significant rise in the value of the ASX 200 since March 2003, many would say that we are approaching (if not already in) an extreme in prices. In these market conditions, the emphasis is on looking to lock in profits and tightening our stops. As we approach the inevitable top in the market, trading discipline will become a key factor in maintaining profitability. For those of you who have joined the market in the last two years, you are yet to see any real volatility and are yet to be tested.

The last two years have provided a fairly safe environment for the amateur trader, but it is likely that bad habits have been encouraged. Have you made good money from a trade that has gone against you by ignoring the stop and giving the trade more room? As strange as this sounds, this is one of the worst things that could ever happen to you. It reinforces the dangerous habit of ignoring stop losses and giving the trade more room. Ignoring stops is the most common form of poor discipline and will eventually lead to financial ruin.

Discipline is an aspect of trading that is often overlooked, yet it is just as important as a trading strategy and money management. Discipline is what helps you to follow your plan and keeps your emotions in check. It helps you stay in good trades and exit the bad ones quickly without fuss. Unlike our institutional peers, we do not have the luxury of someone supervising our trading and making us act.

The following two examples demonstrate the problems with poor trading discipline and shows why it does not make sense not to act on your stops. They are both trend trades and utilise a CBL (count back line) as a 'soft' stop and a trendline as a 'hard' stop. The first of these trades is CPU (chart 1), which was trending along quite strongly before its half yearly report was released. On the day of release, price immediately opened below both the CBL and trendline

and never recovered. This is quite a frustrating event, especially if you entered on the most recent bounce off the trendline at around \$6.00 and all open profits were ripped from you at the open of trade.



The second trade is something we may see more of when individual stocks no longer have the support of the entire market. In the stock GUD (chart 2), some weakness was signalled prior to the trendline break and those running tight stops would have exited on the violation of the CBL. Traders who wanted more confirmation of the trends conclusion would have been caught in the severe correction that gapped through the trendline.



Once again this is a frustrating event as a large chunk of profit is surrendered at the open.

TRADING METHODS

DISCRETIONARY TRADING

This trading style puts the trader in the driving seat. The trader assembles a collection of his preferred indicators, assigns a level of importance to each, and then makes a decision based on his understanding of the indicator readings and trading signals. This inevitably involves some subjective judgment, and this opens the room for error. The trade is managed in the same way, and this requires a high level of confidence.

Mechanical Trading seeks to remove human intervention - and hence subjective behaviour - as much as possible from the trading equation. Typically such systems rely purely on mathematical relationships, although in establishing many systems there is subjective human input to determine the most desirable outcomes. Trade management requires discipline and a great deal of faith in the system. The temptation is to second guess the trading signals.

Intuitive Trading develops from experience, and should not be confused with the gut feelings used by novices. Experienced traders are subconsciously aware of certain patterns and market set-ups. When they see them they act intuitively drawing on many years of trading experience. This requires a high level of confidence and skill and trades are managed with certainty. These trading processes are difficult to explain. The Intuitive Trader by Koppel examines these issues in detail.

In this newsletter our emphasis is on developing discretionary trading approaches.

However, it is a good idea to adhere to a statement from Edwin Lefevre's fictionalised biography of Jesse Livermore, **Reminiscences of a Stock Operator**: 'You've got to have less hope and more fear when a position moves against you'. The loss of profit may seem bad at the time, but looking back you would have been grateful for your quick exit as GUD continued to plummet. Giving up profit is one thing, but turning a highly profitable trade into a losing one is a lot harder to take and is more emotionally damaging. Staying disciplined and following your plan will increase your chances of being successful and also help you avoid many sleepless nights.

A FINAL WORD ON MEASURING TRADING EMOTION

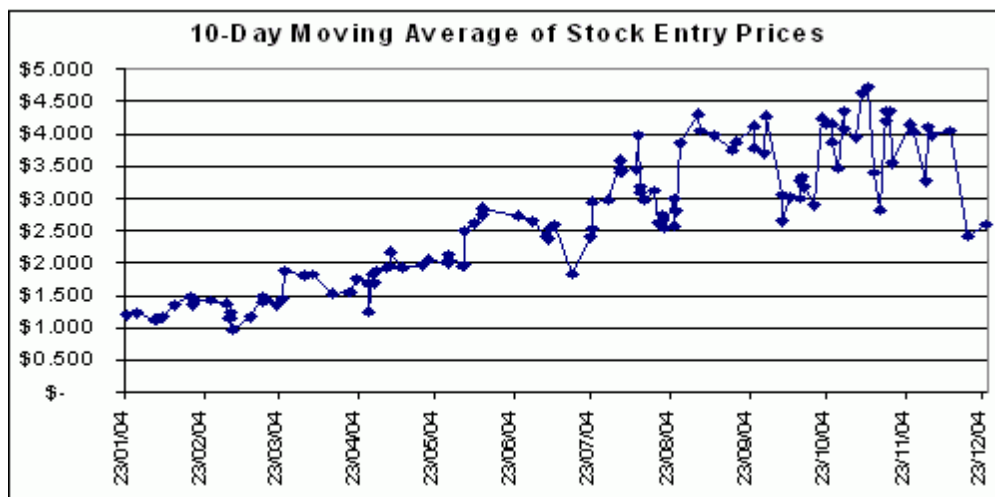
By Gavin Hewitt

These trading emotion articles have explored a number of topics regarding how our psychology affects trading, and the mechanisms we can put in place to measure these. Almost every good trading book I've read acknowledges the significant effect our psychology and emotions have on our trading. However, there is scant advice on practical ways to measure and monitor the psychological aspects of our performance, with Dr Van Tharp being a notable exception. These articles have shown how the information can be compiled and measured.

The diagram introduced last week shows the 10-day moving average of the entry prices of stocks I bought during 2004. I had done a lot of research into trending stocks in 2003 and my trade plan called for purchasing trending stocks around the \$1.20 entry price, and with a price not exceeding \$2.60. However, what I found in buying stocks priced below \$1.00 was that the volatility of price movements was more than my emotions could comfortably handle. I was getting scared at the first sign of selling and exiting too early, as well as constantly feeling uncomfortable during the trade.

And so, without ever making this conscious decision, I began to find increasingly higher priced stocks that still fit my other trend-following entry criteria. These higher-priced stocks performed well, as most stocks did, in the current trending market. And my subconscious selection methodology of buying more expensive stocks was further reinforced as I felt more comfortable in the trade. This was not necessarily a bad thing as my trade results improved as my stress was reduced and I was able to let trade profits run.

While you would think that the process of increasing stock entry prices would be obvious during trading, it is really only during my review of entry prices that the relationship shown in the diagram below was demonstrated so clearly. Given my realisation of this, I relaxed my trading plan assumptions about "best" entry prices to take into account not only the ideal price range from a performance point of view, but also to account for my personal psychology. Interestingly, since having performed well in the price range I now trade in, it has given me the confidence to make a number of smaller trades in lower priced stocks.



A similar situation occurred when I examined the tables below of the type of trades I made in the last two quarters of 2004. Each trade I made is initially categorised as either: a trend trade, a breakout from a range, or a channel trade (which is just one leg of a trend from a higher low to a higher high).

Q3 2004	Trend	Channel	Breakout	Average
Win-to-loss ratio	9 to 11 = 45%	100%	4 to 7 = 36%	14 to 18 = 44%
Return %	1.27%	1.03%	1.96%	1.50%
Return \$/trade	\$126	\$123	\$257	\$171
Occurrences (%)	20 (61%)	1 (3%)	11 (33%)	32 (100%)
Q4 2004	Trend	Channel	Breakout	Average
Win-to-loss ratio	6 to 3 = 67%	5 to 6 = 45%	12 to 2 = 86%	23 to 11 = 68%
Return %	4.25%	-1.03%	2.44%	1.80%
Return \$/trade	\$741	\$-162	\$240	\$242
Occurrences (%)	9 (26%)	11 (32%)	14 (41%)	34 (100%)

From this data, I can see that breakout trades are fairly consistent in their average returns across quarters, even though the win/loss ratio is very varied. What is most notable, however, is that

in the 4th quarter of 2004 the market trended stronger than ever, and was ideal for trend trading. Reflecting this, my average return per trend trade soared from \$126 to \$741. However, only 26% of my trades were trend trades in Q4 compared with 61% in Q3. The reason was the large increase in channel trades, from almost non-existent, to 32% of my trades in Q4.

During the strong bull run in 2004, I was constantly watching for any signs of a turnaround in the market. Knowing it had extended itself beyond its long-term average growth rate, I was concerned about the downside of entering long- to medium-term trades. As such, I focused on "taking bites" out of trends with the channel trades. This had two consequences. Firstly, that I did not optimise the market strength that was available. And secondly, my psychology when entering a channel trade was that "I am doing this because I *feel* like the market could drop", even when I had no evidence for it. This pessimistic feeling hampered my trade management by making me fearful. I took profits early at the first sign of weakness. Hence I had a negative average return on the channel trades when they too should have been profitable in a bull market. Let me be clear about this, this was not a problem with my stock selection, entries, target setting or any other trade plan construction activity. It was my psychology during execution that was turning potential winners into losers. And this was happening even while I was winning big on the trend trades. What an amazing capacity we have to blind ourselves.

As I always note in these articles, the conclusions you reach about your trading will reflect your own unique psychology, and so my conclusions won't necessarily be directly applicable to you. But again, it is surprising and depressing how often people follow similar psychological patterns and have to deal with the same emotional issues. We need to ensure that we are fostering the right emotional and psychological platform for peak trading performance, and to keep monitoring our psychological as well as our financial performance to ensure that if we do develop a behaviour we don't like, then we minimise its impact.

A PROFESSIONAL AND DISCIPLINED MONEY MANAGEMENT METHODOLOGY

By Tom D'Angelo

SUBJECT SUMMARY

THE BUSINESS OF TRADING

Trading is a business. The trader deals in buy and sell contracts and has an inventory of shares that are the same as the 'stock' in a retail shop. His customers do not walk in the door. They are found throughout the country and are connected by a broker and an exchange which facilities the sale of 'shares'. Every business has its profitable and less profitable sections. Trading is no different and our profits come from particular techniques and processes. Successful traders create a professional trading environment to manage their trading activities similar to a successful business.

Good software assists in this process. These articles explain how ManusRisco money management software is used to improve the business control and management of trading.

Failure to adopt a professional, disciplined businesslike approach towards speculation and investment will significantly decrease your chances of achieving long term profitability in today's volatile trading arena. These articles are designed to teach you how to create a professional trading environment so you can manage your trading activities similar to a successful business and make confident, disciplined trading decisions.

Over the next few weeks we will cover these topics:

- Introduction - How successful businesses are organised
- The Profit Centre business model applied to trading
- **A professional, disciplined money management methodology**
- Positive and negative expectation games
- Drawdown
- Return on Investment
- PTR / UTR
- Breakeven Analysis
- The edge: Who has it and how to get it.

In previous articles, we discussed the Profit Centre Structure of a successful business organisation. In this article, we will define the components of a professional and disciplined money management methodology.

The following methodology provides the information required to trade confidently and profitably:

- Create a Business Organisation which segregates trading performance into meaningful

“businesslike” enterprises which reflect your trading methodology.

- Update the Business Organisation with each day’s completed trades.
- Produce Analysis Reports which contain key money management statistics for the Business Organisation.
- Use the Analysis Reports to:
 - Identify positive and negative expectation situations, as well as their trend.
 - Capitalise on trading strengths and strive to eliminate trading weaknesses.
 - Establish and manage the Reward/Risk profile for new trades
 - Utilise a professional and structured money management methodology to engender confidence, foster trading discipline and increase the probability of achieving long term profitability.
 - Return to the second step (Update the Business Organisation) and start the process over again.

For those of you who have any type of business experience, you will probably recognise that the above steps are performed by every successful business, whether it’s a large corporation or small mum and dad corner grocery store. In essence, our money management methodology is the framework for the operation and management of your trading activities as a successful business.

The above methodology organises your trading results so that Analysis Reports can be created to answer important money management questions, such as:

- Which trading methods are profitable and which are unprofitable?
- What are my trading strengths and what are my weaknesses?
- What will be my Reward/Risk Profile for tomorrow’s trading day?
- What is my current drawdown situation?
- Where am I becoming more profitable and where am I becoming less profitable?
- Do I have an edge in any particular situation, and if so, is the edge increasing or decreasing?
- How many contracts or shares should I trade tomorrow and how many points should I risk on each trade?
- What is my Trading Plan for tomorrow and how does the Trading Plan compare to my past trading performance?
- What is my breakeven profile?

The above questions are the same questions that every business manager is confronted with on a daily basis, such as an auto manufacturer: Which cars are selling and which cars are not? Which cars have the highest profit margin? Which have the lowest profit margin? Which cars are unprofitable? Which cars should I produce more of and which cars should I discontinue? What is the profitability trend? Am I becoming more profitable or less profitable?

Without a structured Business Organisation designed to provide informative and practical Analysis Reports, it is impossible to answer these questions, and your business, whether it is selling cars, shoes, televisions or day trading the E Minis, will suffer the consequences.

The above methodology also reveals where you have the edge and where you don’t, where you have a positive expectation and where you don’t, where you are playing as the customer and where you are playing as the casino, and that will be the subject of our next article.

Tom D’Angelo is the CEO of ManusRisco Inc. The money management methodology described in these articles is used by ManusRisco money management software which can be found at www.manusrisco.com. This software adds an important business dimension to the business of share trading.

READERS’ QUESTIONS: DIFFICULTY IN TAKING STOP LOSSES



By John Atkinson, Jason Mitchell and Daryl Guppy

TRADING METHODS

STOP LOSS

A stop loss is a pre-determined exit point. When a trade is first planned, the stop loss is designed to protect the trader's capital. The exact price of the stop loss is the result of a relationship between the maximum level of risk as determined by the 2% rule, the logical support levels on the chart, and the amount of capital the trader wants to allocate to the trade. By varying these three figures, the trader is able to reach an ideal trading solution that controls risk effectively.

A stop loss order should always be constructed at the same time that any trade is planned or entered. Disciplined stop loss sell orders are the key to long term trading success.

The new chat room www.Stockmeetingplace.com is operated by a group in Singapore and their objective is to provide an independent forum for the discussion of financial market trading issues. This chat room has an educational bias, where traders from around the world come to exchange ideas, swap exploration formulas and discuss trading techniques. There are many solutions to any question and this new forum StockMeetingPlace taps into a wide range of trading experience.

I am active in several sections. If you want to ask me a specific question, this is the best place to go. You will receive a reply from me, and also additional information from StockMeetingPlace regulars.

This site is developing into a premier educational chat room, which is attracting a quality group of people who genuinely want to learn about the market and assist others. Many topics are covered and for the benefit of readers who may not have read the following, this article is based on four posts on Stockmeetingplace, which were recently provided by two regular contributors to this newsletter and myself on the subject of the difficulty in taking stop losses.

This topic was introduced by a new trader Jim, who wrote:

Okay I'm going to admit it, "I find it hard to act on stop losses". I know I'm not the only one.

Many possible reasons - I'm comfortably ahead this year anyway, the companies are fundamentally sound with good prospects, the price decline defies common sense (this is a common thought). I've pondered on this for some time now.

Anyway, I know I've got a problem that could bite me hard if the market turned nasty. For those of you that have been here but overcame it, please share your thoughts on how you did it.

In response, John Atkinson replied:

In Daryl's first book, **Share Trading**, he uses the analogy for wannabe traders of learning to put down notes on the footpath and have someone pick them up and walk away with your money. During the tech stock run, traders worldwide felt they were invincible as stocks soared at an incredibly fast pace. During those times, we found it easy to sell out at losses when you were making up for it on other profitable trades.

Then one week the party was over - and all of a sudden it's not any fun anymore as you see red on any screen you look at - and no more green up days.

First of all regret hits you - wishing you hadn't listened to that broker who told you to hold - regret you hadn't got out sooner - regret you hadn't acted on your stop (if you set one in the first place) or not bought such a large position or too many positions or had actually taken the time to get some education on technical analysis, psychology and risk management in the first place.

This then moves to hope - the BHP approach - Buy, Hope and Pray - you find yourself looking at the charts or screen hoping the share will turn around - believe me the share can't hear you - it doesn't care about you or your hope - it always did and always will respond to supply and demand and if no-one wants it, it's headed South.

Then fear really hits - gut wrenching fear as you see your capital decimated - 20 years of working multiple jobs to get ahead and most of it all gone in months; sleepless nights for weeks, then months, and you still have to try and function at work by day when you've been pacing the house night after night - your mind goes, your memory goes, your reasoning goes, and our waterfront home went.

And all of that can be traced back months previously to a series of small decisions that evolve around getting the right education and developing discipline for correct position sizing, capital allocation, setting your initial stop, moving up trailing stops and exiting your stops when they're triggered.

Hope this helps you in what you consider now to be a dilemma. I also hope this helps you decide whether trading is actually for you or not and please realise it's okay to say no and seek your fortune in other endeavours, in which case we applaud you for your decision.

I mean this with sincere conviction - trading is not for everyone and sorry to be appearing tough on you, but acting on stops is tough, and the alternative is much tougher, believe me.

To this, Jason Mitchell added:

Well done on being honest. I think, as you say, many people do have trouble acting on stops. I would like to tell you there is a nice simple way, but I think for many people it takes losing money. It did for me anyway. This is because of our beliefs.

I noticed in your post you wrote "the companies are fundamentally sound with good prospects, the price decline defies common sense (this is a common thought)".

I am assuming these are your thought processes. Thought processes are generally underpinned by our beliefs. I have no trouble acting on stop losses because I have lost money in the past not doing it. My belief is that working on fundamentals and common sense loses me money while acting on stops helps make me money. Your belief, however, may be that the fundamental opinion of a company is meaningful and that price will come back.

I am not saying you are wrong and the others are right. Everybody has a different way of trading. Many fundamental analysts have no time for technical views - if they make it work that is fine. I believe using technical analysis is a numbers game. Minimise losses and put the balance of probability on your side. In order to do this, stops are generally needed.

Changing beliefs for the most part (I think) comes from our experiences. For example, I love dogs, but if I got mauled tomorrow by a pit bull, I may be less caring next time I see one running across the road. Maybe this answer is not what you are looking for, but while someone is trying to adhere to another person's belief when it doesn't seem right to them, there will always be trouble maintaining discipline.

The only suggestion I can make is extensive research on your approach. Seeing factual results can be hard to deny, especially when there is a repeated pattern that becomes visible. This could be done through back testing, but this is more difficult with fundamental and technical combined. Hope this helps in some small way. I admire your honesty.

I added my perspective on this subject with the following:

Consistently exercising stop loss discipline is the greatest challenge and barrier to successful long term trading. Our desire to avoid experiencing the pain of losing is hardwired.

Once you have created a discipline to take a series of losses, you tend to find that another set of inhibiting factors start to creep in. At first they are special cases, later they become the 'normal' reason for not acting on stop losses and the losses grow.

I do not think there is a single, or simple, solution. The solutions we use to force ourselves to act on stops change over time. We need to be alert for the need to change and the more we can read about the different ways that others resolve this problem, then the better the chance we give ourselves of finding a solution that will work for us.

The foundation is accurate trade planning and good records showing how a trade failed. Look for the patterns as Jason suggests, and then develop strategies to block the losing behaviours. This may mean not taking particular types of trades because they always 'blow up.'

Jim's response to these replies may be read at <http://www.stockmeetingplace.com/forum/viewthread.php?tid=471&page=1#pid2132>

*Jason Mitchell is a full time trader working from the Gold Coast Australia. His tools and strategies are developed to be easily applied in the markets and he is the founder of the popular trading newsletter and short list, the **StarTrader Report**. For more information go to www.StarTraderReport.com.*

John Atkinson is the author of '10 Ways Not to Lose Your Home in the Stock Market'; In Home Study Courses and Portfolio Management Tools, which are due for release in 2005.

*His new E-book, the **Atkinson-Guppy Articles**, is a collation of articles he has written for this newsletter, which focuses on exit strategies; money & risk management and provides original material on trading strategies for Share Purchase Plans, rights issues, avalanche selling and much more. It's now available from www.sharetradingeducation.com with a special promotional savings of 30%. A **free sample chapter** may be downloaded by registering in the Free Downloads section at that site.*

By registering at these sites, readers will also have access to fully automated affiliate programs to be launched next month which will allow traders to develop additional income streams.

CHART TECHNIQUE BRIEFS: AZTEC MINING (AZR)

By Petra Rak

SUBJECT SUMMARY

TREND TRADING

Trend trades are designed to capture the capital appreciation that comes from a steady rise in price. Trends can be fast or slow. They can also be short term, lasting days or weeks, or medium term, lasting weeks or months. Long term trends persist for months and sometimes years. A stable trend shows a steady rise with low volatility. The moves up and down are not very great. When the volatility starts to expand, it is an early sign that the trend is becoming unstable.

Trend trades are usually defined by the way that the current short term average price is consistently greater than the long term average price. This defines the general direction of the price movement. Trend trading delivers very good returns, but the weakness is in the delayed entry and exit. This costs potential profits and depletes actual profits when compared with the very start and end of the trend.

The daily chart of AZR shows an accelerating uptrend.

In detail, for most of the second half of 2004, AZR traded in a sideways channel between a \$0.10 support and a \$0.14 resistance. In November, a breakout above the \$0.14 resistance pushed prices into a higher consolidation, between \$0.14 and \$0.165. This breakout indicated potential future upside movement, but was still within a long term trading band (see weekly chart) below \$0.175. The current uptrend commenced in January on a breakout from the consolidation, and has since developed in two stages, a shallower stage and a more recent steeper stage which has progressed relatively smoothly, and recently reached a new historical high at \$0.31.

UP CONDITIONS

The primary question when analysing a stock in blue sky territory is how persistent the trend is. Once we determine trend persistence, the second question becomes how to manage trade entry.

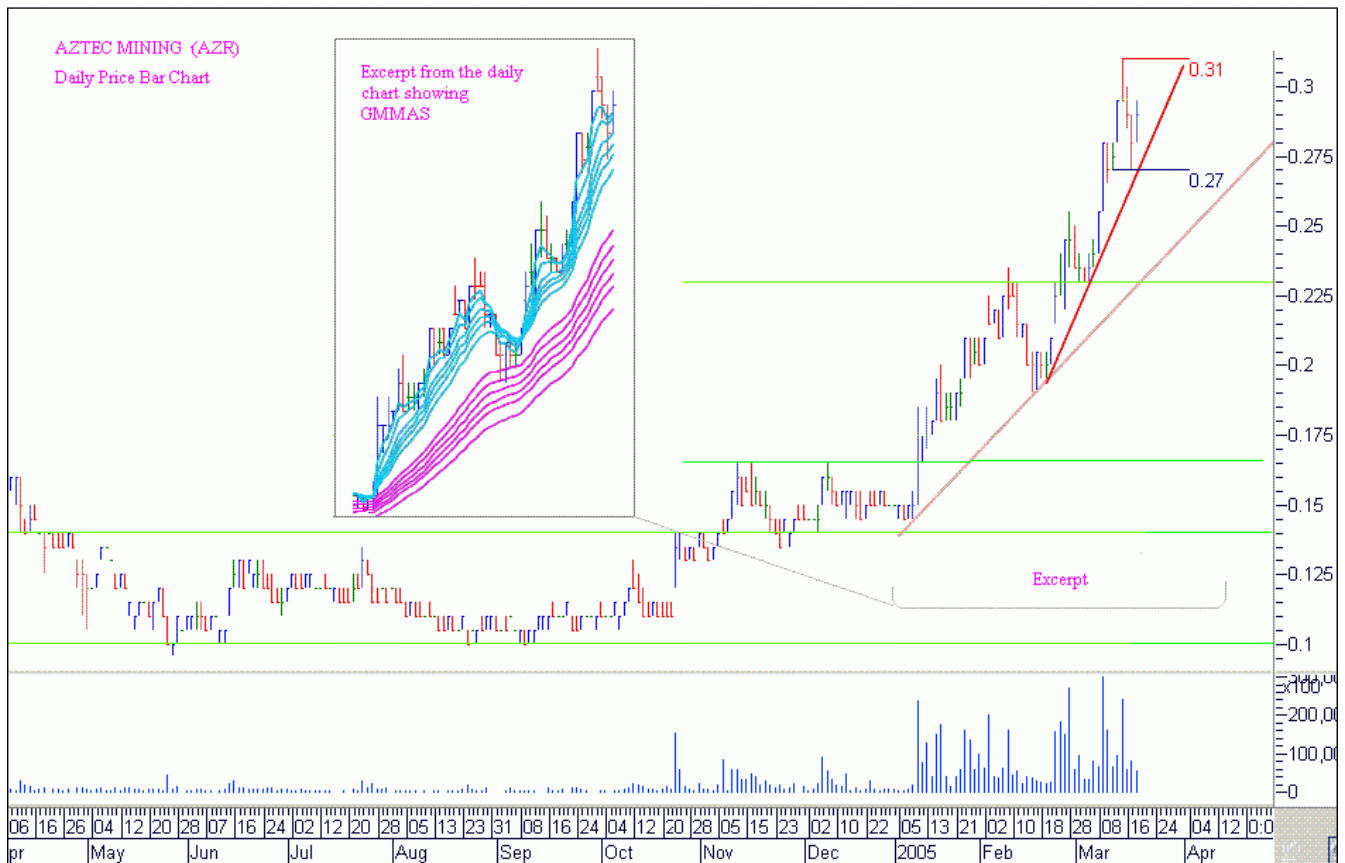
Even at first glance, the overall AZR trend appears strong, though we may question the persistence of the steeper segment as trend accelerations tend to be shorter term developments. However, at present, good trend strength is indicated for the steeper up trend by the GMMAs, which show strong and steady investors support through a very well spread and upward trending long term group. A constant distance between the GMMA groups confirms trend stability.

Determining an appropriate trade entry point requires analysis of short term price behaviour within the trend. In AZR as is usual in ongoing uptrends, a potential entry point is just above the upward

trend line. Traders interested in AZR will watch for such a development in the next few days. A bounce away from the trend line will re-confirm the steeper trend and signal trend continuation.

Targets in blue sky stocks are generally not predetermined, and trades are managed in accordance with entry parameters, such as continuing validity of the initial and trailing CBL stop losses and of the trend line, together with strength in the GMMAs. The presence of an accelerating uptrend alerts traders about the possibility of parabolic trend development.

Key management tools in any trades are likely to be the steep trend line together with CBL stop loss signals and the GMMAs for monitoring trend strength and continuation together with market depth.



DOWN CONDITIONS

Failure of the trend line and CBL stop loss (currently at \$0.27) will signal the end of the current stage of the trend and any trades based on it. Historically, the CBL stop loss has been very useful in AZR, as none of the retreats have triggered the stop loss and thrown traders out of the ongoing uptrend.

If the trend line and CBL stop loss are broken, traders will look for the shallower trend line to provide a support for any retreat. A rebound from this shallower trend line will confirm the validity of the shallower uptrend. In contrast, failure of the shallower trend line would increase the probability of a trend reversal. In this case, traders still interested in AZR will look for the development of a strong support (possibly around \$0.23 or \$0.165), and potential opportunities created by a bounce away from this support and breakout through the CBL breakout line.

Our Asia newsletter will cover Cape Range Gold, which was one of the companies featured at the Singapore Australian Mining Conference last week.

NEWSLETTER OUTLOOK – FINDING TREND SUPPORT

By Daryl Guppy

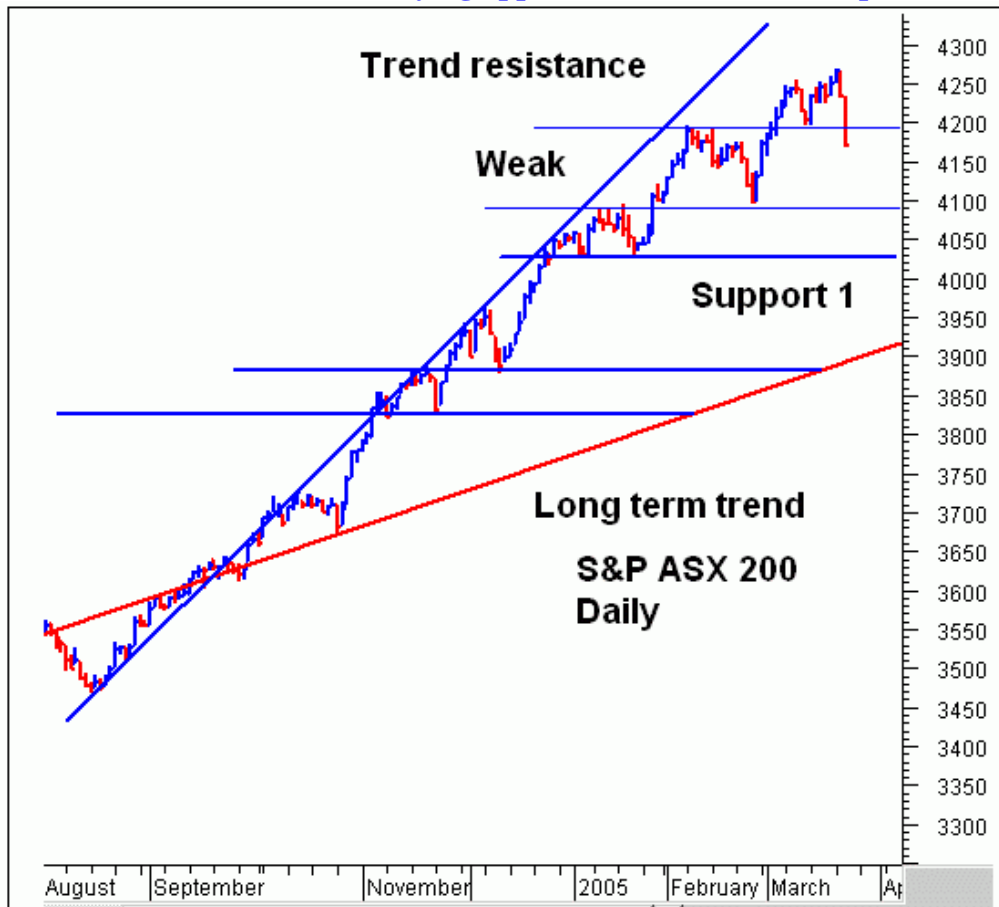
The support level at 4190 failed to hold on the second rests this week. This underlines the primary technical problems with these market conditions. This is blue sky charting. The support levels we identify are based on very little information. They provide a potential support level, but they must be tested and retested successfully several times before we can have confidence that they are genuine and effective. We have shown these two upper levels as weak and until there are successful re-tests, we will continue to treat these as potential support areas.

A continued market fall will use the 4090-4100 level as the next support base. This is a little stronger, but it has not been seriously tested on a pullback. We have to move back to 4030 to

find a support area that has been tested more often. This sets our lowest figure for an index retracement based on support.

The market can retrace as far as 3900, based on the current long term trend line values, and still remain consistent with a long term uptrend. A retreat to these levels will cause serious pain for any investors, however, it is not inconsistent with the trend.

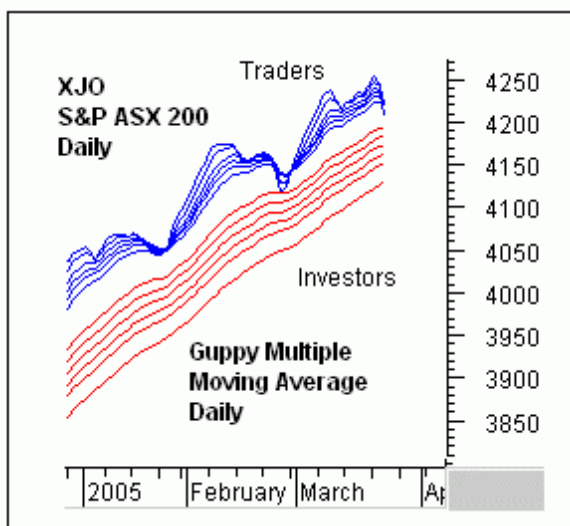
Traders will look for buying opportunities if the market probes towards support at 4030.



We will continue to plot new support levels as the trend develops because we need to establish potential pullback areas. When the trend stalls, declines, or retreats, it is important to have a defined method of distinguishing between a temporary retreat and a major trend change. Just as a mountain climber uses pitons to secure each new step before advancing, so we use this support areas as a way of defining the potential damage from any slip.

This remains an incredibly robust trend. In an ordinary stock we would be less concerned about potential trend weakness. In an index that represents the broad market, we are more concerned because the index represents 200 stocks. The money flow required to keep hitting new highs is much more substantial than that needed to propel an individual stock. This makes these longer, sharp broad market trends more difficult to sustain. Hence, we remain more cautious.

To put this shorter term analysis into perspective, we turn to the Guppy Multiple Moving Average display. We use the Guppy Multiple Moving Average as one of our primary trend analysis tools. A substantial retracement could take place and still remain consistent with the trend.



The GMMA continues to show the strength of this trend. The long term group continues to maintain a consistent parallel separation. The strength of the trend is confirmed by the reaction of the long term group of averages as the index drops or retreats. Traders are alert for significant compression in this group. The degree of penetration by the short term group is a leading indication of trend strength. The rebound behaviour provides important clues about the potential for the trend to continue. The pattern of

rebound and retreat is crucial. Lower retreats signal significant trend weakness. The rebound confirmed the strength of this very robust trend.

A strong bullish trend is suggested when the long term group of averages does not compress. It tells us investors are actively moving into the market and buying stocks as they fall in price because they believe that these are still good value. Traders may want to take short term profits, but investors take a longer view. Their reaction to price retreats creates the conditions for trend continuation.

The indicator continues to confirm that a substantial index retreat remains consistent with the long term underlying trend. The GMMA is not a stand alone indicator. Our preference is to use it in conjunction with other indicator tools. These include the support and resistance levels, and the trendlines discussed above.

Each week we make a choice about the material we include and the subjects we cover. The selection is based on our outlook for the current and coming market. Our objective is to illustrate effective trading strategies that readers can apply to current market conditions. We do not identify recommended individual stocks. We identify opportunities and appropriate trading methods for them. Our outlook is not a forecast. It is a probability framework. Use it as just one part of the other information you are reading about the market. Our summary outlook will be included each week.

NEWSLETTER NOTES

WHAT TRADING EDGE?

While I was working in Singapore during the week, I attended a number of market presentations. One was from a market research group that provides independent fundamental analysis. They made a point of noting their success rate in making correct calls on stocks. Their rate at 56% was “world class”. The accepted financial industry average is 52%. This is not much better than a coin toss. The presenter suggested that any fund manager who is able to achieve consistently more than 60% correct calls is at the top of the world rankings.

Personally, I found this astounding. We regard 50% as a no-brainer, and certainly a no-pay situation. With even the most simple of trend analysis, a trader can get the call correct at least 60% of the time. We believe the real challenge is to lift success rates from 60% to around 70%. Over the past 10 years of the newsletter publication, our success rate has been around 72%. World class is 80% success rates.

However, it is also important to note that the success rate in making correct calls is only part of the solution for trading success. The second, and more important part, is how you handle those calls that are unsuccessful. This is where risk management and money management play the most significant role. Even at a 52% success rate, it is possible to deliver excellent returns – but only if losing positions are cut quickly. Unfortunately, the very fund managers who average a 52% success rate, apply a money management method of risk control that allows losing positions to continue to grow on the grounds that their fundamental analysis is ‘correct’ in the long run. Perhaps this explains why so many funds have difficulty in even matching the market index performance.

Food for thought and a confirmation that even simple charting analysis provides a significant trading edge.

REASONS FOR NOT SUBSCRIBING TO THE NEWSLETTER #3

You have to be a trader or chart expert to read it

A misconception about the Tutorial newsletter is that you have to be a trader to read it. This is simply not true. Our subscribers include investors, fund managers, brokers, position traders, day traders, financial advisors and those who just want to improve their results from the market.

We aim to provide a tutorial that shows what works and does not work in current markets. Some strategies are suitable for readers who are just beginning their foray into the markets. These are marked with a single computer icon. Others are advanced strategies suited to experienced traders who are trying to hone their trading edge. These are shown with 3 computer icons.

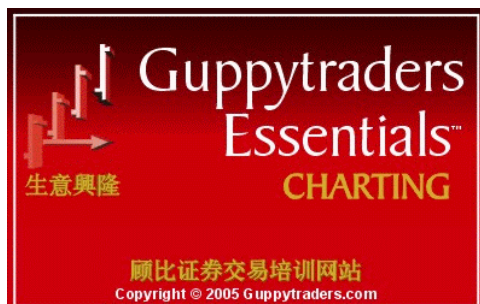
Many people in many different professions subscribe to the newsletter. They know the newsletter gives them the insight they need to get ahead of their market competition. They know we give them the tools and combinations that they can apply to their own market approaches. This work is harder than just simply following a tip sheet, but it develops the skills necessary for market survival. Our sample portfolio models the types of returns possible in current markets when good trading discipline is observed.

In short, the newsletter gives you a wider view of the financial markets so you can make a more informed decision about the things that affect you and your market exposure – be it investment, trading, or somewhere in between.

GUPPYTRADERS TOOL BOX – RELEASE ON SCHEDULE

The new GuppyTraders Essentials Toolbox and charting program is in final testing stages. Toolbox pricing will be under \$100. We will also release a GTE Charting package. We will offer an attractive changeover path to those who wish to *changeover* from the original Market Analyst version of the GTE charting package or toolbox. We own the licensing and

copyright to these products and they are no longer associated with Market Analyst. The new version of the GTE Toolbox produced by Guppytraders will be available early in April 2005.



Features include:

- Full count back line capability. This is CBL for long side trading, and for short side trading
- GMMA display
- Parabolic trend line plots – including long side and short side plots. Also includes convex plots as shown in Leon Wilson books.
- Symmetrical and a-symmetrical saucer plotting
- Pattern price projection tools
- Darvas boxes including:
 - Modern
 - Classic
 - Ghost boxes – just click and add.
- An effective ATR plot that operates as a stop loss display as well as a standard indicator display option.
- ATR stop loss configured for both long side and short side trading.
- One click display of 1, 2 and 3 moving average combinations.

The GTE Toolbox is designed to work with a variety of data formats. It is a small utility application that gives traders access to a selection of Guppy tools and indicators that might not be included in the charting program they are currently using. We are currently upgrading the GTE Toolbox and adding some new indicators and other enhancements.

If you want first access and leading development, then this is available through our weekly newsletter and the Guppytraders version of Guppy TradersEssentials toolbox and charting program. Some readers will have received an offer from Market Analyst to upgrade to Market Analyst Guppy Traders Edition Version 4. Please note that Market Analyst stopped working with GuppyTraders.com in mid-2004 as they made a decision to stop producing the GTE toolbox and the GTE Charting package. They rebadged the charting package as a Market Analyst Guppytraders Edition that included the tools found in the original GTE charting they produced for us. We no longer provide them with access to updated tools and techniques. Market Analyst, like every other software developer, such as Bull Charts, Ezy Charts, Metastock etc, have access to our tools and techniques only AFTER they are in the public domain and published in books or articles.

12 MONTH SUBSCRIPTION RENEWAL OFFER OPEN TO RESUBSCRIPTION AT ANY TIME

With every 12 month subscription renewal, we are including a free copy of either Martin Pring's, **Breaking the Black Box** (rrp \$45.95) or Robert Prechter's, **Conquer the Crash** (rrp \$39.95). We do have limited numbers of these books and once they are used, this 12 month subscription renewal offer will end. This offer is made each week to all those readers whose subscription periods are currently coming to an end. However, this offer is available to any subscriber who resubscribes for a 12 month period. If your subscription is due to end in May, then if you resubscribe now for 12 months, we will send you your choice of free book. Just note your preferred book in the Comments section on the order page.

TRADING STRATEGIES WITH METASTOCK BY JIM BERG



This is a comprehensive guide that takes you step by step through a 2 day trading strategies workshop using Metastock software. This is excellent value and quality work.

The workbook is well set out with clear screen shots of the processes under discussion. The trading strategies include the Berg Volatility Indicator which has been featured in Technical Analysis of Stocks and Commodities magazine. The full coding steps for all indicators are included, along with detailed explanation of how the strategies are implemented. This guide is now available through our Guppytraders store at

<http://www.guppytraders.com/gup240.htm>

ASK YOUR QUESTIONS IN THE CHAT ROOM

Thank you to newsletter readers who have participated in the new chat room. www.Stockmeetingplace.com is operated by a group in Singapore and their objective is to provide an independent forum, for the discussion of financial market trading issues. I have agreed to work with them exclusively. If you wish to ask me a question, discuss issues raised in the newsletter, or follow up on issues in my books, then post your question on www.stockmeetingplace.com

I am confident that www.stockmeetingplace.com will develop into a premier educational chat room which will attract a quality group of people who genuinely want to learn about the market and assist others. That is why I have agreed to exclusively participate in this chat room. This chat room has an educational bias where traders from around the world come to exchange ideas, swap exploration formulas and discuss trading techniques. I am active in several sections. If you want to ask me a specific question, this is the best place to go. You will receive a reply from me, and also additional information from StockMeetingPlace regulars. There are many solutions to any question and StockMeetingPlace taps into a wide range of trading experience.

NEWSLETTER DELIVERY

If you have a question about delivery of the newsletter, the progress of an order, or your subscription details, please email support@guppytraders.com. We will respond within 24 hours (a little longer over weekends).

WHICH GUPPY BOOK?

Many people have asked this question. Here is a summary guide.

Want to know more about trading?	Share Trading	Beginner to experienced
Want to know more about charts?	Chart Trading	Beginner to experienced
Want to know more about tactics?	Trading Tactics	Beginner to experienced
Want to improve your trading results?	Better Trading	Experienced to professional
Want to master simple but powerful techniques?	Trend Trading	Beginner to experienced
Want to understand short term trading?	Snapshot Trading	Experienced to professional
Want to survive difficult markets?	Bear Trading	Beginner to experienced

PORTFOLIO CASE STUDIES- MONEY MANAGEMENT

PORTFOLIO CASE STUDIES - MONEY MANAGEMENT

Starting cash position \$100,000 - no brokerage or slippage 2% of risk = \$2,000

NOTE Entered date is the *newsletter date* which contains the case study discussion.

Stock	Price	Qty	Pur Value	Close	Cur Val
STW	\$36.390	550	\$ 20,015	\$ 42.37	\$ 23,304
	Newsletter date	11-Sep		Open Profit	3,289.00
		dividend Jan 6			464.48
				profit	3,753.48
MA trend manage				Percentage	18.75

Stock	Price	Qty	Pur Value	Close	Cur Val
APA	\$3.700	5,450	\$ 20,165	\$ 3.8700	\$ 21,092
	Newsletter date	26-Feb		Open Profit	926.50
Trend trade				Percentage	4.59

Security/Counter/Stock	Price	Qty	Pur Value	Close	Cur Val
CCE	\$0.420	48,300.00	20,286.00	0.425	20,527.50
	Newsletter date	26-Mar		Open Profit	241.50
CBL trade				Percentage	1.19

SUMMARY MONEY MANAGEMENT

Overall profit to date since July 1, 2004 = \$56,774 or 56.7% return on trade equity.

Profit 2003/04 = 48.7% return on trade equity. Profit 2002/03 = 75.9% return on trade equity.

Profit 2001/02 = 71.3% return on trade equity. Profit 2000/01 = 59.2% return on trade equity.

Profit 99/00 = 111.2% return on trade equity. Profit 98/99 = 102% return on trade equity.

Profit 97/98 = 94% return on trade equity. Profit 96/97 = 66.5% return on trade equity.

Direct investing in the stock market can result in financial loss. Historical results are no guarantee of future returns. Results reflect absolute trading stop loss discipline. Case study trades are monitored and managed in real time, and management reports are delivered every week in the newsletter. Except where noted, all case study trades are notional examples using reasonably attainable entry and exit points.

Unlike an actual performance record, simulated results do not represent actual trading. Also, since the trades have not actually been executed, the results may have over or under compensated for impact, if any,

of

certain market factors, such as lack of liquidity. No representation is being made that any account will or is likely to achieve profits or losses similar to those shown. Full trade summaries, with charts, are provided every six months.

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