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Building wealth through shares

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Email Newsletter No 10

This email newsletter is published free from time to time to people who have previously contacted me about technical analysis and trading. If you would prefer not to receive it again, please let me know.

I do not allow anyone else to use my list.

If you have friends who you think would like to receive the newsletter, please feel free to email it on to them and invite them to contact me to add their address to the list.

It has been some time since the last newsletter. Partly, this has been because of the holiday season. However, it also because I have been busy with other things. One of them has been development of a web site.....

Web Site

Please visit my web site, which was launched between Christmas and New Year. It is still under development, but already there is much useful information available. Over the next few months there will be constant improvements. The address is www.bwts.com.au

Pacific Traders Camp

The rooms are starting to go at our Pacific Camp in March. We had started out with 30, and now we are down to 19 vacancies. Last year's Pacific Camp in Fiji was magic, and we will try to repeat and exceed that magic in Vanuatu. The main teacher will be my great friend Dr Alexander Elder, whose book ***Trading for a Living*** is still a best seller eight years after publication. He is writing a new book and will be teaching its contents at the camp. Helping Dr Elder with the teaching will be Chuck Le Beau and myself.

People come to our Camps to become better traders, to study in close personal contact with the best experts in the world. I would like to introduce one of the assistant teachers at the March Camp, Chuck LeBeau. Chuck, with over 30 years experience in the markets, is the author of a highly important book, ***Computer Analysis of the Futures Markets***. In recent years he has become active in the stock market and runs a website www.streakingstocks.com. He had taught at the January 1999 Camp in the Dominican Republic where he was one of the top-rated speakers in the history of Dr Elder's Camps. I have read Chuck's work, but not heard him in person, so I am also excited at the prospect of hearing him first-hand at the camp.

While Chuck can cover all aspects of system design, his revolutionary contributions are in the area of exits from trades. Some snippets of his discoveries, such as his famous Chandelier Exit, are starting to percolate through the trading community. It is very frustrating that his book on exits keeps getting postponed again and again. With no book out, the only way to learn Chuck's revolutionary techniques is to learn from him face-to-face. There is no plan for him to come as far from home as Australia, so this is a unique opportunity to hear him.

Already there are a range of interesting people from the US and Australia who have booked for Vanuatu. There are both professional traders and some who are just starting out on the road to trading success. All the material presented will be accessible to you, even if you have only a little experience. Having brought you up to speed on the important concepts we will then take you with us through more advanced ideas, many not yet available in books or videos. One of the advantages of the camp format is that there is time to sit and discuss

trading topics with fellow campers and instructors. If anything is over your head in class, your instructors can quickly rectify that in extra sessions.

I invite you to come to our Camp to learn from the best experts, ask your important questions, become a better and more confident trader. Time is ticking away to book. We have been warned that seats on the available flights to Vanuatu will get very tight soon. If you are thinking of coming, now is the time to act! The essential details for Australian campers are on www.bwts.com.au and there is further information and details for New Zealand and US campers on www.elder.com

Confusion of Roles

The role of the analyst and the trader are different. However, many market participants do not clearly distinguish the process of analysis from the process of applying that analysis. This may be because of a lack of appreciation of the special skills involved in trading. There is a widespread belief that to trade markets, all you need is a good analysis. Then you just buy and sell at a profit. However, this ignores the essential role of money management and the different psychology that is required for trading. Indeed, some good analysts find it difficult to become good traders and vice versa. For this reason institutions usually separate the roles by employing both specialist analysts, or strategists, and specialised traders.

The best way to deal with this problem is to be aware of which role or roles you are playing. Where you are only performing the role of analyst and giving advice to a trader, there is not usually a problem, since only one process is involved. However, if you are analysing markets as part of a trading plan, the difficulties are much greater. All traders should have a written trading plan. This should be divided into sections dealing in turn with money management, analysis methodology and trading strategy. A conscious effort must be made to shift the mind set to trading mode once the analysis is completed. Remember that trade management is far more important than stock selection and entry price in determining trading results.

Most traders solve the conflict of roles problem by keeping the analysis very simple. They look for a set-up in the market and trade it, concentrating their focus on the trading process. They know that it really does not matter whether the analysis is right in any one situation, because their focus is on the outcome of a series of trades over a period.

Building Wealth Through Shares Seminars

Many readers have asked me when I will be running more of my weekend seminars. I have just worked out a timetable for 2001 and the dates are up on www.bwts.com.au The bad news is that writing and travel commitments preclude me running more seminars before the middle of the year. However, this does not mean you need to wait that long to access my seminar material. Last year I taught the essentials of my approach in an intensive seminar in New York titled *How to Design a Trading Plan*. This was videotaped and is now available in PAL format as two 2 hour tapes accompanied by 80 pages of notes. For more information and how to order it, go to www.bwts.com.au

Time Horizons

One of the most important challenges for technical analysis lies in the realisation that trends unfold simultaneously in many time frames and it is difficult to separate them out with any certainty. At any one time, there are participants trading minute by minute fluctuations on the floor of an exchange, others day trading intra-day trends on a screen, others speculating on an imminent company result or news announcement, position traders looking for trades that will work out over weeks or months and portfolio managers investing with a view to a three, five or ten year performance. So, at that time, some of them will be seeing the market to be rising in their time frame, while others see it to be falling in theirs. If this were not so, it would be difficult for markets to operate efficiently.

There is another perspective to this problem of trends in different time frames. Not only are there all these trends laid one on top of the other, but the longer term trend affects the shorter term trends. It is therefore important that the analyst not only identify and study the trend for

the time frame of the analysis, but also consider the effect of longer term trends upon this trend. If I had to identify one of the most common errors I see traders making it is that they have not started with the long-term picture and worked down to the time frame they are trading.

This is not an easy problem to deal with. However, it is the way the real world is, so the technical analyst must learn to handle it. What is required first is, of course, an appreciation that there is a problem. The problem is not immediately obvious and we will encounter many people trying to use technical analysis with no appreciation at all of this phenomenon. Once we appreciate that there is a problem, we need to make it a part of all of our analysis.

Stop-Loss Orders

In the US all brokers accept stop-loss orders. Most textbooks on analysis and trading that emanate from that market assume that this facility is available. It is most important, of course, in highly leveraged markets. Australian share brokers have never offered a stop-loss facility, perhaps because there is little trading on margin in this country. However, there is a constant demand from private traders for such a facility, that is generally going unheeded. I pointed this out in the last newsletter and asked any readers who had a broker who accepted stop-loss orders to let me know. The result was that such brokers are difficult to find and what they offer seems quite limited compared to what is available to US traders. These are the brokers with whom you should make further enquiry if you seek a stop-loss facility:

CSFB (Credit Suisse First Boston)
E-Star/Barton Securities (maybe still in development)
Hartley Poynton (now HP JDV)
Intersuisse
Tricom
William Noall

It was not entirely clear from some of the responses I got whether these brokers offer the facility on the Internet. Readers should make their own enquiry on this point.

I had an email from MetaShare International saying that the first three only offer this to MetaShare clients. However, a friend at CSFB seemed not to know about such a restriction. I have not followed up this aspect personally.

Readers are warned that they should ascertain the price of these facilities. It may be reasonable that there is some additional charge for the service. Even more importantly, they should make sure they understand exactly how the stop-loss facility operates before using it. Do not assume anything. Ask questions and pose examples until you clearly understand the mechanics or rules of the service you are considering.

An alternative to stop-loss order is to use a pager or email alert system, which warns you if price has crossed your stop threshold. The Sanford service seems to be of this type. There is also a service by www.stoploss.com.au. However, I heard that the business was for sale before Christmas, so I am not sure what has happened to it.

Subjectivity

There is an element of subjectivity in all technical analysis. We can reduce it to a minimum using mathematical techniques that seem to give clear rules. However, close inspection finds elements of subjectivity even here in selection of parameters, time periods, etc.

Many people unfairly compare technical analysis to fundamental analysis on this point, claiming fundamental analysis is objective because it is based on facts. However, again, close inspection shows many 'facts' to be estimates subject to revision, or samples and so on. Moreover, there are many assumptions made, often without the analyst realising they are being made. The more you look at it, the more you realise that all analysis is, to some extent, subjective.

The danger in subjectivity is that the analyst will see in the chart what he wants to find. We are all prone to the desire to be right and will subconsciously filter out information that does not support our view. Good analysts make a practice of looking at both sides of any situation. They determine what evidence is in favour of the prevailing view. Then they turn “devil’s advocate” and determine the evidence contrary to the prevailing view. Good analysts tend to be very suspicious of any strongly held view, even their own, and never cease to question every assertion.

Those who have a difficulty with subjective analysis look for rules that seem to provide clear signals, say by one line on the chart crossing another. There are two problems with this as a solution to the challenge of subjectivity. Firstly, there are often quite subjective assumptions underlying the construction of the lines. They are just hidden from view. Secondly, this sort of approach is trying to simplify markets, when the reality is that markets exhibit great variation and subtlety.

Instead, we should see the challenge of subjectivity as an opportunity for experienced analysts to obtain an edge in the market by developing a better insight into the reaction of buyers and sellers to what is happening in the market. This is directly analogous to the skilled fundamental analyst, who can see beneath the surface of information to the dynamics of a company or commodity market. Yes, this will require a great deal of hard work and application.

Notice Board

Readers have asked me to seek response from my email list on these two matters:

Melbourne Discussion Group

An experienced, end of day, near full time, stock and derivatives trader is seeking to establish an informal discussion group in Melbourne. The aim is to share experiences and discuss available resources rather than for trading advice. Contact pvalentine@one.net.au if you are interested.

Managed Funds Data

If anyone knows a vendor of end of day prices for managed funds that is downloadable into Metastock, please let me know at colin@bwts.com.au

Back Issues of the Newsletter

One of the more important functions of my web site is making back issues of the email newsletters available for downloading. This is much faster than email attachments and very flexible by allowing readers to only download what they want.

Newsletters will generally be posted to the web site when the following issue is sent out, so my email list is still the fastest way to get to see it.

The Coppock Indicator spreadsheets may also be downloaded from the Newsletters page.

There are instructions on how to download the files at the top of the Newsletters page.

I wish you all the best for 2001. We are trading in dangerous times. Make sure you have a strategy for dealing with market risk.