Global Financial Crisis?

10 Key Lessons from the Financial Crisis

for investors and traders

Robert Brain

May 2012

Brainy's Share Market Toolbox — www.robertbrain.com

V 2012-01.b

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10 Key Lessons

Background

The *"Financial Crisis"*

- Global Financial Crisis (GFC)
- Euro financial crisis → austerity measures
- US sub-prime mortgages
- CDOs (Collateralised Debt Obligations)
- "Toxic" debt
- Bear markets in world stock markets
- Recessions in many countries

BUT, are there any lessons to be learnt?

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10 Key Lessons

Background

How bad was/is it in Australia?

A lot of people suffering
2008, 2009, 2010, 2011, 2012...?

- Property values fell.
- Superannuation investments fell in value.
- Retrenchments.
- Unemployment increased.
- Some investments lost as much as 90% or more of their value.
- Some investments were liquidated completely.
- Inappropriate lending - margin loans, etc.
- Issues with over-borrowing that had been encouraged by some lenders.
- Some questionable advice from some "experts".

10 Key Lessons

Background

Are there any lessons to be learnt?

10 Key Lessons

Introduction

About this presentation

The original material was prepared in late 2008 in response to questions from saddened investors regarding their losses in that year from the GFC.

Then expanded into a presentation:
"Beware the Share Market Bears (they are never far away)".

And now with more time and continued losses behind us, it is time to reflect and update the material.

10 Key Lessons

Introduction

About... Robert Brain

Consultant, educator and part-time* share trader
Web-based sharemarket-support business

- Many years experience as trainer, presenter, conference facilitator (*Scouts*)
- Share market analyst – active 13+ years*
- Chartist ie. technical analyst (ATAA member and national director)
- Provide tuition and support to traders and investors ***Brainy's Share Market Toolbox***
- Engineering Degree (structured thinking with an eye for charts and diagrams)
- 30+ years – professional experience (IT and management)
- **Do not hold AFS license! (Can't give advice)**
- BullCharts software (convenor Australian BullCharts User Group and authorised reseller (with special pricing)
- Member Mensa

* - Not yet enough capital to live off the proceeds of trading (after trading as a hobby until a career change in 2008).

10 Key Lessons | Introduction

Important Notice — No Advice!

1. This presentation does not include any advice.
2. For proper advice, your personal financial situation needs to be considered.
3. This presentation is pure education, only for your general awareness.
4. There are no recommendations to take any action, or to invest any money in any way.
5. Always consult a properly licensed advisor before making investment decisions.

10 Key Lessons | Introduction

Important Notice

10 Key Lessons | The TEN Lessons!

The 10 KEY LESSONS for investors and traders...

10 Key Lessons

The TEN Lessons!

Ten lessons for investors?

Any idea
what these lessons
might be?

10 Key Lessons

The TEN Lessons!

The 10 Key Lessons...

1. Buy-and-Hold? — This strategy has expired!
2. Priority 1 — Preserve the capital
3. The Big Picture — Maintain perspective and reality
4. Cycles — Markets, stocks, property all run in cycles
5. Corrections — Stock market corrections? — How long?
6. Timing the market — We ***can*** "time the market"!
7. Advisors — Financial advisors, brokers, bankers
8. Leverage — Leveraged instruments and methods
9. Chart reading? — Can be useful Here's how...
10. Risk / Reward — Understand and respect it

10 Key Lessons

The TEN Lessons!

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10 Key Lessons

#1 — Buy and Hold is dead!

Lesson #1

The age-old and respected ***Buy-and-Hold*** strategy

10 Key Lessons

#1 — Buy and Hold is dead!

Multiple choice:... (a) or (b)?

The old ***buy-and-hold*** strategy is:

(a) alive and well?

or

(b) best forgotten?

10 Key Lessons

#1 — Buy and Hold is dead!

Really?

- Can investments really fall 90%?
- Can blue chip stocks disappoint?

Details follow: . . .

10 Key Lessons

#1 — Buy and Hold is dead!

Going...Going...Gone

The following companies had significant share price falls from the bull market peak of October 2007, and are now GONE:-

- AFG (Allco Finance) -99% gone Aug 2009
- BNB (Babcock & Brown) -99% gone June 2009
- TIM (Timbercorp) -97% gone May 2009
- NLX (Nylex) -97% gone Feb 2009
- GTP (Great Southern Ltd) -96% gone May 2009
- CDR (Commander Comms) -95% gone Aug 2009
- ABS (A.B.C.Learning) -92% gone Aug 2009
- BJT (Babcock and Brown Japan) -92% gone Jul 2009
- MFS (renamed Octaviar OCV) -74% gone Aug 2009

10 Key Lessons

#1 — Buy and Hold is dead!

Fell > 60% **

- CNP (Centro Prop) -99%
- CER (Centro Retail) -99%
- BKN (Bradken) -93%
- ABP (Abacus Prop) -91%
- ALZ (Australand) -91%
- AAX (Ausenco) -89%
- AWC (Alumina) -89%
- AGO (Atlas Iron) -88%
- FLT (Flight Centre) -88%
- CGF (Challenger Fin) -84%
- APN News Media -83%
- BSL (Blue Scope) -82%
- FXJ (Fairfax Media) -82%
- HIL (Hills Indust.) -82%
- CTX (Caltex) -77%
- CEY (Centennial Coal) -76%
- LEI* (Leighton) -74%
- HVN (Harvey Norm) -72%
- PRY (Primary Health) -66%
- AXA -69%
- CRG (Crane Group) -67%
- BBG (Billabong) -66%
- ABC (Adel Brighton) -63%
- NAB* -63%
- ANZ* -62%

** — lowest price (until March 2009)
* — Blue Chip stocks

10 Key Lessons

#1 — Buy and Hold is dead!

Fell between 50% and 60% **

- CAB (Cabcharge) -65%
- ASX -58%
- CBA* -58%
- DJS* (David Jones) -57%
- QBE* -57%
- AWE (Australian Worldwide Exploration) -57%
- CPA (Commonwealth Property) -59%
- BHP* -55%
- JBH (JB-HiFi) -58%

Do you recognise many of these names?

** — lowest price (until March 2009)
* — Blue Chip stocks

10 Key Lessons

#1 — Buy and Hold is dead!

Fell < 50% **

- AMC (Amcor) -48%
- ANN (Ansell) -42%
- COH (Cochlear) -40%
- HSP (Healthscope) -42%
- * TLS (Telstra) -40%
- * WOW (Woolworths) -34%

** — Until March 2009
* — Blue Chip stocks

BTW:- What does "blue chip" mean?

10 Key Lessons

#1 — Buy and Hold is dead!

Blue Chip Stocks — definition?

BTW

Current definition*:

Larger companies with a long history of profitability and stability.

Former definition*:

Shares, usually highly valued, in a major company known for its ability to make profits in good times or in bad, and with reduced risk of default.

* Source: www.asx.com.au/glossary/

10 Key Lessons

#1 — Buy and Hold is dead!

Even ***Blue Chip*** stocks can disappoint.

See Robert's examples:
www.robertbrain.com/share-market/blue-chip.html

10 Key Lessons

#1 — Buy and Hold is dead!

The set-and-forget approach

- Tends to work in a bull market.
- Many people have used this approach along with a margin loan, and pre-paid 12 months of interest expense.
- Can this approach ride out the downs of the market? (*not in 2007-2012!*)
- Is this a *sensible approach* to investing?

10 Key Lessons

#1 — Buy and Hold is dead!

- Share prices can fall
- Share prices can stay depressed for long periods
- Why hold shares in these companies?
- This is "capital destruction".

10 Key Lessons

#1 — Buy and Hold is dead!

The lesson:

The Buy-and-Hold investing strategy...

Has expired!

10 Key Lessons | #2 — Priority one — the Capital!

Lesson #2

Priority one is: *preserve the capital*

Back to the list of 10 Key Lessons

10 Key Lessons | #2 — Priority one — the Capital!

How can we protect our capital?

(a) Blue chips — they are "safe havens" — yes?

(b) Buy capital-protected products?

(c) Sell a losing product?

Let's look at these: …

10 Key Lessons | #2 — Priority one — the Capital!

Blue chips can disappoint

- We saw earlier that blue chips are:
  - larger companies
  - with a long history of:
    - profitability and
    - stability

- But there are no guarantees regarding the share price
- That is, they are not a "safe haven"
- So, should we hold them for ever?

10 Key Lessons

#2 — Priority one — the Capital!

There are times when shares in some companies could be converted to cold hard cash to ***preserve capital***. Even blue chip stocks

Actively monitor the portfolio (weekly).

10 Key Lessons

#2 — Priority one — the Capital!

"But... my dividend income stream..."

Some people buy (blue chip) shares and hold long-term for the steady dividend income stream.

- It can be shown that some portfolios can perform better by realising capital gains, and protecting the capital (and paying capital gains tax).

See Robert's $100,000 hypothetical portfolio performance in another slide presentation.

10 Key Lessons

#2 — Priority one — the Capital!

Consider the *opportunity costs*

Investing for income, at the expense of capital protection, is an often-used "excuse".

- This approach might be okay... but it does depend on your:
  - strategy, and
  - investment timeframe / horizon
- Recommend to do the sums.
- Reality:- It might be best to preserve capital, and forego income in the short term.

10 Key Lessons

#2 — Priority one — the Capital!

Even Blue Chip stocks
can disappoint,
so consider
selling the bad performers
(using a clear strategy).

See Robert's examples:
www.robertbrain.com/share-market/blue-chip.html

10 Key Lessons

#2 — Priority one — the Capital!

"Capital protected" products?

Are your investments really *"capital protected"*?

- Your superannuation?
- Capital-protected products and schemes
  - ALPS, etc. (and knockout events)
  - Beware the "knockout" events!
  - Important to read the fine print and understand exactly what we are buying
- Buy some form of insurance against a fall in capital?
- Buy share *options*?

10 Key Lessons

#2 — Priority one — the Capital!

How can we protect capital?

What options are available
to protect our hard-earned capital?

10 Key Lessons | #2 — Priority one — the Capital!

How to protect share-invested capital?

Use a Stop Loss strategy:-

- For a share holding;
- Identify a price level
  below which the shares should not be trading
  — if they do, it suggests that
  share price support is gone and
  further falls are possible;
- So, sell it!

10 Key Lessons | #2 — Priority one — the Capital!

The Stop Loss strategy

- This is NOT a haphazard approach to liquidating stocks at arbitrary price levels whenever we perceive price weakness
- It IS a carefully designed strategy to pre-determine the threshold price level below which the stock is to be sold.
- BUT, there is a little more detail to it than this
  eg. to sell on "trading below" or "close below"?
  and sell immediately or on next open?

10 Key Lessons | #2 — Priority one — the Capital!

The lesson:

Priority one: Preserve the capital

Consider selling a falling investment
in order to protect
the investment capital.

10 Key Lessons

#3 — The Big Picture

Lesson #3

The BIG Picture
to maintain perspective

Back to the list of 10 Key Lessons

10 Key Lessons

#3 — The Big Picture

Remember the BIG picture

- Too many people spend too much time focusing on the very short term.
- The ***noise*** of daily announcements and daily spikes on price charts is distracting.
- It is useful to look at weekly and monthly price charts, and over several years.

It all helps to maintain "perspective".

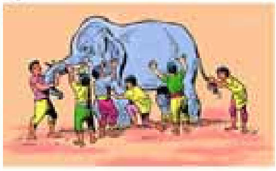
10 Key Lessons

#3 — The Big Picture

"The market is like an elephant!" *

- We should "zoom out" to get a bigger-picture understanding of the beast; and
- If we try to stand in the way, we might get "trampled".

So, remember the BIG picture.



More Share Market *GEMS** in the Toolbox: www.robertbrain.com/gems/

10 Key Lessons

#3 — The Big Picture

"Stay invested for years..."

- The professionals tell us:
  "Stay invested for years..."
  "we are in it for the long term..."
- But, what if we don't have years?
- It might be true that over the very long term the returns from the share market are better than other forms of investment.
- But that doesn't help us *today*.

10 Key Lessons

#3 — The Big Picture

Share market down 5% !

- The share market might be down 5% in recent days; but it might be up 10% in recent weeks.
- Don't let the short term news scare us.
- Don't focus only on the short term.

So, remember the BIG picture.

10 Key Lessons

#3 — The Big Picture

Shares are up 40%

The news this week said that **shares are up 40%!**

How can that be?

10 Key Lessons

#3 — The Big Picture

Shares are up 40%

The news this week said that shares are up 40%! How can that be?

- We could consider:
  - Month-to-date performance
  - Year-to-date performance
  - Financial year-to-date performance
  - Performance since April Fool's day last year!
  - etc., etc.,
- Beware the ***arbitrary baseline date***.

10 Key Lessons

#3 — The Big Picture

Here's another trick

- The highest "High" price in a period can be different to the highest "Close" in the period
- And the highest "Close" on a monthly chart can be a different value to the highest "Close" in any one week.
- So, be aware of the differences in the data (daily, weekly, monthly)

10 Key Lessons

#3 — The Big Picture

XJO October 2007 (Top 200)

Highest Weekly Close = 6749 for the week comm 8 Oct 2007 (the blue line)

Highest Daily Close = 6829 on 1 November 2007 (the black line)

Highest Monthly Close = 6754 for the month of October (the red candle)

10 Key Lessons

#3 — The Big Picture

Daily candlesticks

10 Key Lessons

#3 — The Big Picture

The lesson:

Remember the

BIG picture

to maintain perspective

10 Key Lessons

#3 — The Big Picture

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10 Key Lessons

#4 — Cycles

Lesson #4

Markets, stocks, property all run in cycles

Back to the list of 10 Key Lessons

10 Key Lessons

#4 — Cycles

Some of the more common cycles

- 10-year investment clock
- Generic investment clock
- Property / real estate cycle (~18 years)
- US Presidential cycle

10 Key Lessons

#4 — Cycles

The 10-year Investment Clock

10 Key Lessons

#4 — Cycles

The generic Investment Clock

Source: Citigroup and AFR

10 Key Lessons

#4 — Cycles

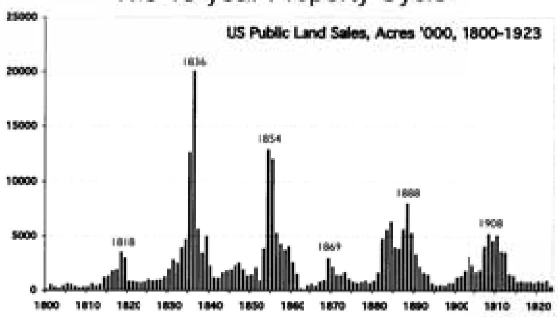
Property values — rise and fall

- Cycles of 17 to 21 years (about 18 on average)
- Phil Anderson (Economic Indicator Services) www.businesscycles.biz
- The Savings and Loan crisis (late 1980s) en.wikipedia.org/wiki/Savings_and_loan_crisis
- The CDO debacle (2008) (Collateralised Debt Obligations)
- Clever manipulation of the law and regs by "innovative" (unscrupulous?) people.

10 Key Lessons

#4 — Cycles

The 18-year Property Cycle

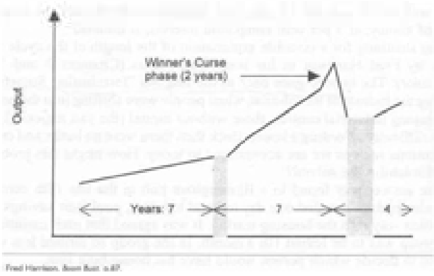


Source: Phillip J. Anderson, "*The Secret Life of Real Estate*", p. vii.

10 Key Lessons

#4 — Cycles

Profile of the 18-year Real Estate cycle

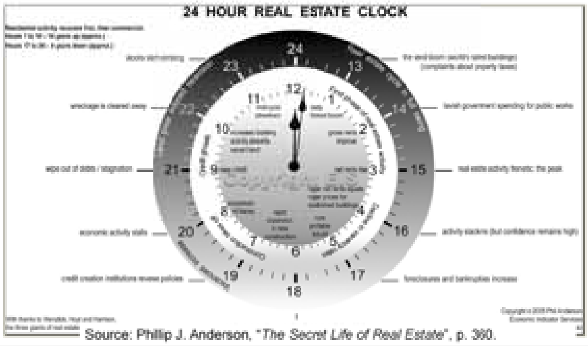


Source: Phillip J. Anderson, "*The Secret Life of Real Estate*", p. 340.
Original source: Fred Harrison, "*Boom and Bust*", p. 87.

10 Key Lessons

#4 — Cycles

The 24-hour Real Estate Clock



Source: Phillip J. Anderson, "*The Secret Life of Real Estate*", p. 360.

10 Key Lessons

#4 — Cycles

Several other cycles

- 30-year commodity price cycle
- Seasonal cycles
- 80-year New Economy cycle
- Kondratieff cycle (58-60 years)
- US Presidential cycle — 4-years (details over)
- Decennial cycle (details over)
- 40-year generational spending cycles

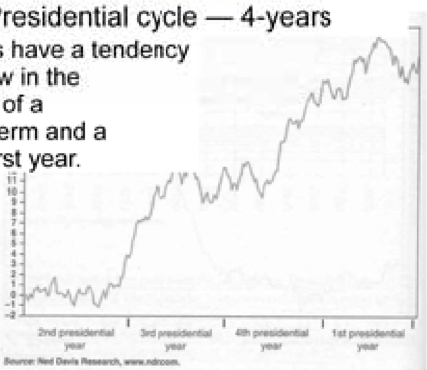
More details, refer:
"*The Great Depression Ahead*", Harry S. Dent, www.hsdent.com

10 Key Lessons

#4 — Cycles

US Presidential cycle — 4-years

U.S. markets have a tendency to make a low in the second year of a President's term and a high in the first year.



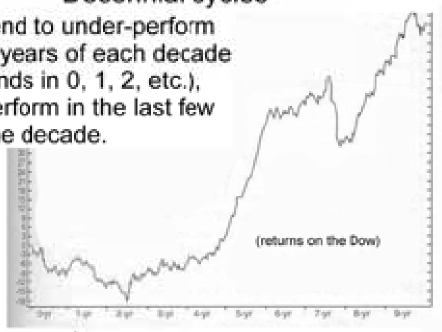
Source: www.ndr.com
Ack: Harry S. Dent Jr, "*The Great Depression Ahead*", p. 94.

10 Key Lessons

#4 — Cycles

Decennial cycles

Markets tend to under-perform in the first years of each decade (ie. year ends in 0, 1, 2, etc.), and out-perform in the last few years of the decade.



Source: www.ndr.com
Ack: Harry S. Dent Jr, "*The Great Depression Ahead*", p. 93.

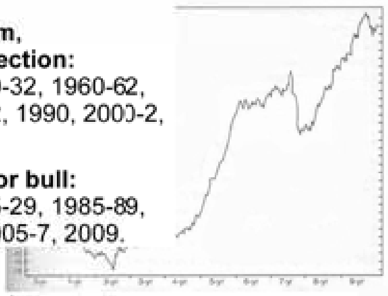
10 Key Lessons

#4 — Cycles

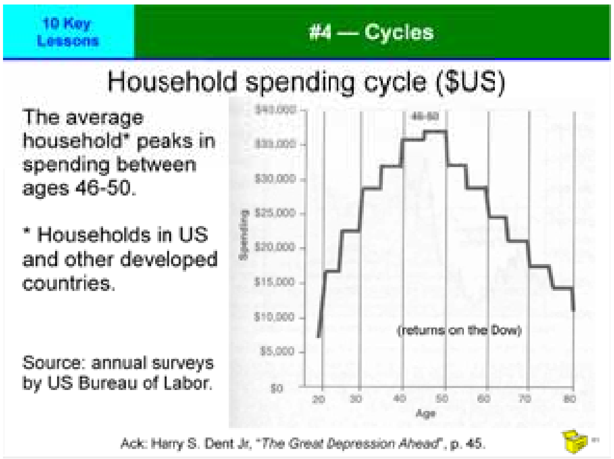
Decennial cycles

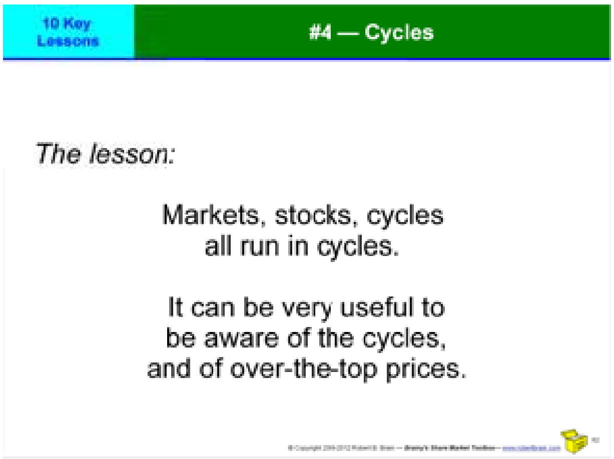
For example:

- **Under-perform, crash or correction:** 1920-22, 1930-32, 1960-62, 1970, 1980-82, 1990, 2000-2, 2010-2012.
- **Out-perform or bull:** 1914-19, 1925-29, 1985-89, 1995-2000, 2005-7, 2009.

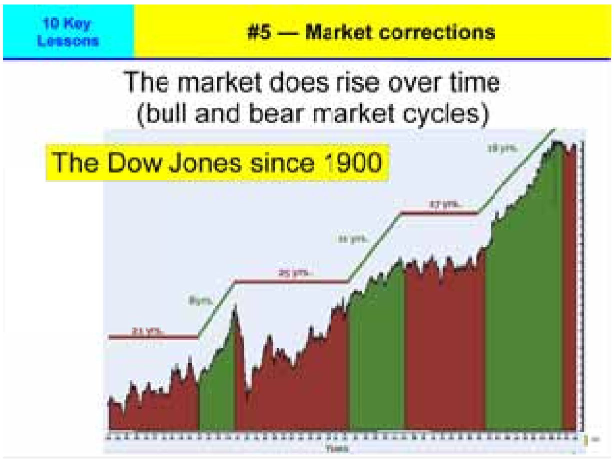


Source: www.ndr.com
Ack: Harry S. Dent Jr, "*The Great Depression Ahead*", p. 93.


10 Key Lessons
#4 — Cycles
Household spending cycle ($US)
The average household* peaks in spending between ages 46-50.
* Households in US and other developed countries.
Source: annual surveys by US Bureau of Labor.
$40,000
$35,000
$30,000
$25,000
$20,000
$15,000
$10,000
$5,000
$0
Spending
46-50
(returns on the Dow)
20
30
40
50
60
70
80
Age
Ack: Harry S. Dent Jr, "The Great Depression Ahead", p. 45.

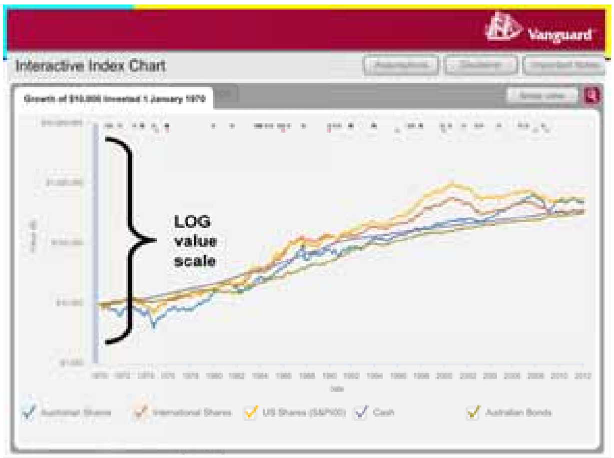

10 Key Lessons
#4 — Cycles
The lesson:
Markets, stocks, cycles all run in cycles.
It can be very useful to be aware of the cycles, and of over-the-top prices.


10 Key Lessons
#5 — Market corrections
Lesson # 5
Market "Corrections".
They happen.
How often? How long?
Back to the list of 10 Key Lessons


10 Key Lessons
#5 — Market corrections
The market does rise over time
(bull and bear market cycles)
The Dow Jones since 1900


10 Key Lessons
#5 — Market corrections
The market rises (over time)
Market returns from June 1970
This web-based interactive chart is useful to view performance of different asset classes, and to readily zoom the chart in/out.
See active web link below.
Click to view this interactive chart on the web:
www.vanguard.com.au/personal_investors/knowledge-centre/indexing/interactive-index-chart.cfm


Vanguard
Interactive Index Chart
linear
value
scale



10 Key Lessons

#5 — Market corrections

BTW — Aussie market history?

- We can see a chart of the Dow back to 1900?
- But, how far back does the Australian market go? (see next slide)

BTW

10 Key Lessons

#5 — Market corrections

Ancient history

1861 - The Melbourne exchange commences.
1871 - The Sydney exchange commences.
1882 - The Hobart exchange commences.
1884 - The Brisbane exchange commences.
1887 - The Adelaide exchange commences.
1889 - The Perth exchange commences.

$\}$ **Separate state-based exchanges**

1903 - The first interstate conference meeting of representatives from the state-based exchanges.

1937 - The Australian Associated Stock Exchanges (AASE) established.

10 Key Lessons

#5 — Market corrections

Stock exchange amalgamation

- 1980 – The Australian Stock Exchange (ASX) replaced the Sydney and Melbourne exchanges.
- 1980 - The separate Melbourne and Sydney stock exchange indexes were replaced by the Australian Stock Exchange indexes.
- 2000 - The S&P/ASX 200 (XJO) index established (and other index changes).

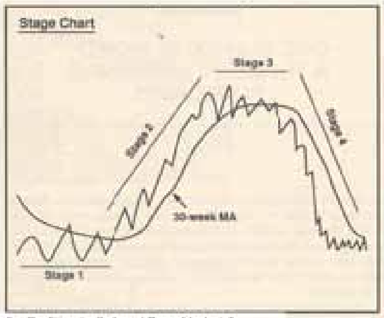
10 Key Lessons

#5 — Market corrections

Stan Weinstein's Stage Analysis

"Any stock (or index) has to be in one of four market stages."

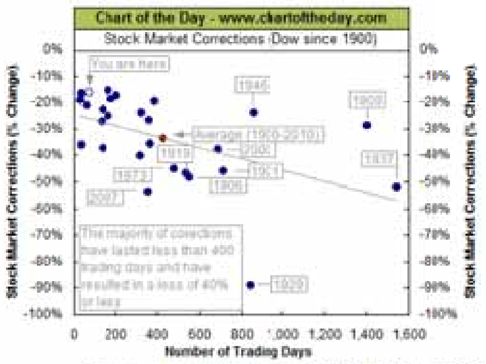
And they don't have to follow in sequence.



Source: "*Secrets for Profiting in Bull and Bear Markets*", Stan Weinstein (1988). McGraw-Hill.

10 Key Lessons

#5 — Market corrections



Source — www.chartoftheday.com/20110812.htm 12 August 2011

10 Key Lessons

#5 — Market corrections

Notes for the chart

Explanatory text for the chart on the previous slide,
from: http://www.chartoftheday.com/20110812.htm

The stock market remains highly volatile and currently trades significantly lower than where it did three short weeks ago -- investors are concerned. For some perspective on the current correction, today's chart illustrates all major stock market corrections (15% loss or greater) of the last 111 years.

Each dot represents a major correction as measured by the Dow.

For example, the bear market that began in 1973 lasted 481 trading days and ended after the Dow declined 45%.

There are a few items of interest... Since 1900, the Dow has undergone a major correction 26 times or **one major correction every 4.3 years**.

Second, most major corrections since 1900 (62%) have resulted in a drop of less than 40% while lasting less than 400 trading days. Since 1950, the percentage of major market corrections that were less than 40% and 400 trading days increased to 78%. As it stands right now, the current stock market correction (April 2011 peak to most recent low) would measure below average in both magnitude and duration.

10 Key Lessons

#5 — Market corrections

Australian Bear Market Durations

Start Date	End Date	Duration (weeks)	Fall %
Jan 1970	Nov 1971	98	-39.0
Jan 1973	Sep 1974	89	-59.2
Nov 1980	Jul 1982	85	-40.6
Aug 1989	Jan 1991	72	-28.0
Jun 2001	Mar 2003	89	-19.0

Source:- UBS

10 Key Lessons

#5 — Market corrections

Recent history — 1986 to 2012

10 Key Lessons

#5 — Market corrections

Recent history — 1987 to 2012

Bear Markets and Corrections — 1987 to 2012

Start Date	From Point	Bear Market or Correction	Amount (%)	Time to recover to past high: Months	Time to recover to past high: Years
Sept 1987	A	Bear market	-44	106	8.8
Aug 1989	C	Bear market	-28	46	3.8
Oct 1991	D2	Correction	-15	18	1.5
Jan 1994	F	Bear market	-21	32	2.7
Sept 1997	J	Correction	-11	14	1.2
June 2001	O	Correction	-21	35	2.9
Oct 2007 *	S2	Bear market	-54	48	4.0
Apr 2010 *	U	Correction	-15	21	~2
Apr 2011 *	U2	Bear market	-21	TBA	TBA

Note: The letters in the "From Point" column refer to points on next slides.

10 Key Lessons

#5 — Market corrections

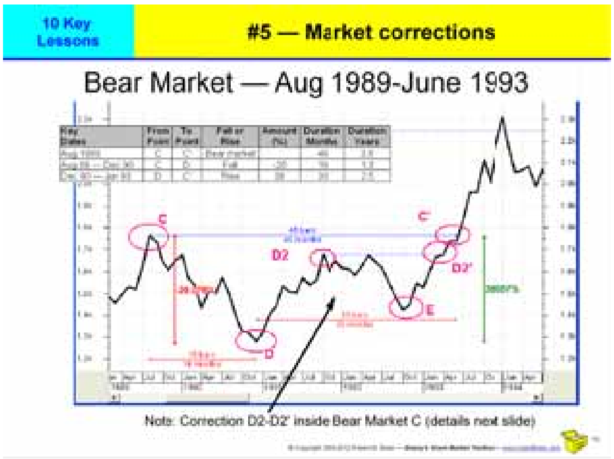
1987 to 1996

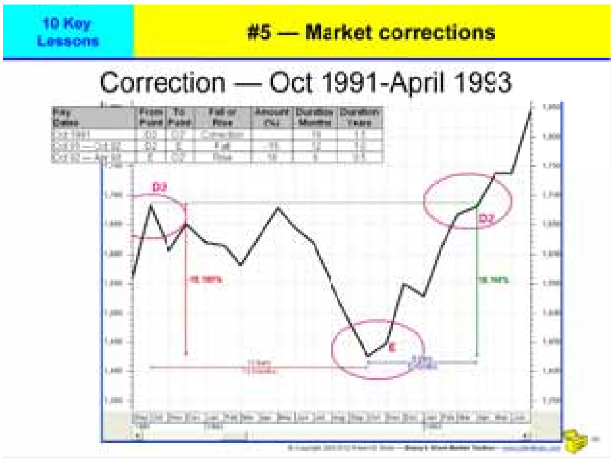
Based on monthly close prices

10 Key Lessons

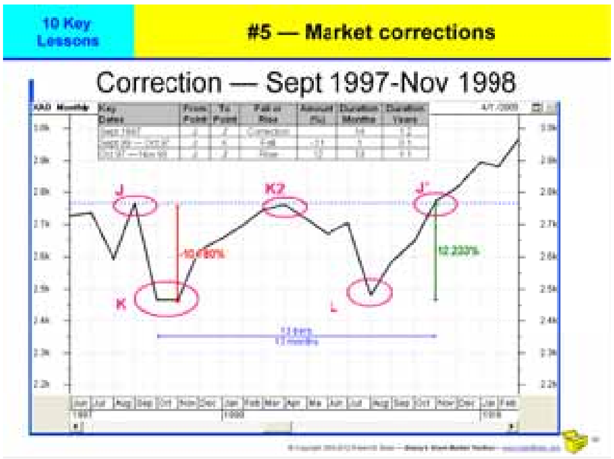
#5 — Market corrections

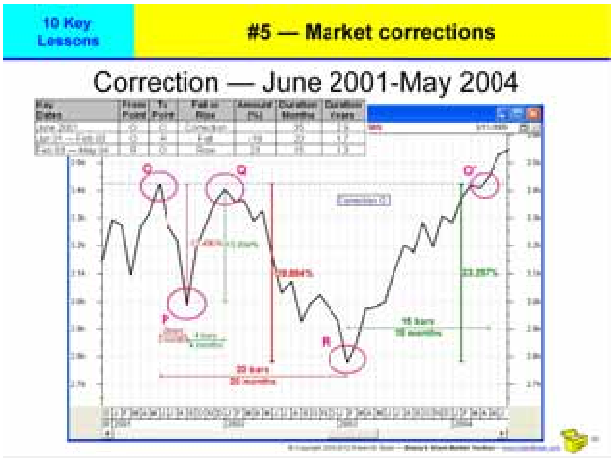
Bear Market — Sept 1987-July 1996


10 Key Lessons
#5 — Market corrections
Bear Market — Aug 1989-June 1993
C
D2
C'
D2'
E
D
Note: Correction D2-D2' inside Bear Market C (details next slide)


10 Key Lessons
#5 — Market corrections
Correction — Oct 1991-April 1993
D2
D2'
E


10 Key Lessons
#5 — Market corrections
Bear Market — Jan 1994-Sept 1996
F
H
G
F'
A'


10 Key Lessons
#5 — Market corrections
Correction — Sept 1997-Nov 1998
J
K2
J'
K
L
-10.480%
12.233%


10 Key Lessons
#5 — Market corrections
Correction — June 2001-May 2004
O
Q
Q'
P
R
19.864%
23.287%
15 bars
15 months
20 bars
20 months


10 Key Lessons
#5 — Market corrections
BEAR MARKET — Oct 2007-May 2012
S
T
41.277%
this?

10 Key Lessons

#5 — Market corrections

BEAR MARKET — These charts

The charts on the previous slides are already posted on the web.

Visit:

www.robertbrain.com/bearmarkets

10 Key Lessons

#5 — Market corrections

Bear Market + Correction

- Bear Market — 1989 to 1993 (3.7 years)
  - Correction — late 1991-1992 (1.5 years)
- Bear Market — 2007 to 2012+ (4+ years)
  - Correction — April 2010-? (? years)

10 Key Lessons

#5 — Market corrections

The lesson:

Stock market "corrections" do happen,
too often than we would like,
and the bears can demolish investments.

Be prepared to protect your investments.

10 Key Lessons

#5 — Market corrections

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10 Key Lessons

#6 — We *can* time the market!

Lesson #6

Can we “time the market”?

Back to the list of 10 Key Lessons

10 Key Lessons

#6 — We *can* time the market!

Multiple choice:... (a) or (b)?

Is it possible to
“time the market”?

(a) Yes, we can time the market.

(b) No, we can't do this.

10 Key Lessons

#6 — We *can* time the market!

"Timing"? or "Time in"?

Many professionals in the finance industry say:

"It is not possible to ***time the market***, it is ***time in the market*** that is important."

What do you think?

10 Key Lessons

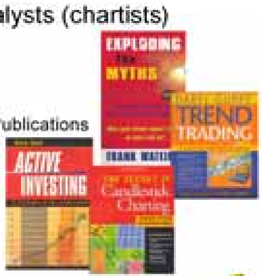
#6 — We *can* time the market!

"Timing"? or "Time in"?

It is possible to "time" the market!!

Thousands of Technical Analysts (chartists) think so, including:

- Frank Watkins
  "Exploding the Myths", Vocational Education & Training Publications
- Alan Hull, Daryl Guppy, Louise Bedford, Leon Wilson, Jim Berg, Stan Weinstein, etc., etc...



10 Key Lessons

#6 — We *can* time the market!

The lesson:

Many people do successfully "time the market". It can be done.

10 Key Lessons

#6 — We *can* time the market!

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10 Key Lessons

#7 — Advisors...

Lesson #7

Financial advisors, brokers & bankers

Back to the list of 10 Key Lessons

10 Key Lessons

#7 — Advisors...

Observations

In the finance industry, ***some*** professionals:-

- rely on commissions
- are "serial innovators"
- don't really "care" about their clients
- will trot out the same old spiel to keep clients invested in their products — eg:
  - *"It's time in the market, not timing"*
  - *"Over the long term, the market does rise."*

10 Key Lessons

#7 — Advisors...

Might not be right all the time

- 100% accurate?
- *"Your investments are safe for the long haul..."*
- *"...don't worry, they will recover (eventually)"*
- What about the "experts" and "advisors" (and the innovative bankers) who created and contributed to the melt-down in 2008-09?
- Question their remuneration methods?

10 Key Lessons

#7 — Advisors...

The lesson:

Don't believe absolutely everything that you hear.

Healthy scepticism is healthy.

Seek a second opinion?

10 Key Lessons

#8 — Beware of leverage

Lesson #8

Leverage — beware!
(margin loans, CFDs)

Back to the list of 10 Key Lessons

10 Key Lessons

#8 — Beware of leverage

Margin Lending — Example

Consider this example:

- You own $50k worth of shares
- Borrow another $50k "at the margin":
  - So, buy another $50k worth of shares
  - In this case the LVR = 50%
  - Interest rate might be 10%pa (ie. pay $5k pa interest)
- You now own $100k worth of shares

10 Key Lessons

#8 — Beware of leverage

Example (cont)

- You own $100k worth of shares ($50k your funds + $50k from the bank).
- Annual dividends might average to 7%: 7% of $100k = $7k
- The annual interest bill = $5k
- So, $2k in front.

10 Key Lessons

#8 — Beware of leverage

Example (cont)

- Let's say a bear market hits, and shares drop in value by 20% for 3 years.
- Your portfolio value is now $80k, and you still owe the bank $50k, so you have $30k left.
- That is, your $50k original portfolio is now worth only $30k
- You are down $20k.

QUESTION: In this example, is margin lending beneficial to anyone?

10 Key Lessons

#8 — Beware of leverage

Margin Lending — Can it be safe?

Recent history (~2008):

- Directors' borrowings for own shares
- Excessive LVR (Loan to Valuation Ratio)
- ABS (ABC Learning), AFG (Allco Finance), plus others...
- Share values plummeted,
  Margin calls were placed,
  lenders could not stump up more funds
  shares were sold out from under them
- Result:- massive personal debts.

10 Key Lessons

#8 — Beware of leverage

Derivatives, CFDs

CFD = Contract for Difference

- Can be safe; can be very dangerous!
- It is possible to lose a lot more than the initial deposit.
- Under the right circumstances, and in the right hands, can be powerful.

10 Key Lessons

#8 — Beware of leverage

The lessons:

Leverage — beware!
(eg. margin lending)
It might work well in a *bull market*.
If you don't understand
the rules of the game,
then don't play the game.

10 Key Lessons | #8 — Beware of leverage

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10 Key Lessons | #9 — Chart reading — very useful

Lesson #9

Chart reading
can be very useful

Back to the list of 10 Key Lessons

10 Key Lessons | #9 — Chart reading — very useful

How to anticipate the next bear?

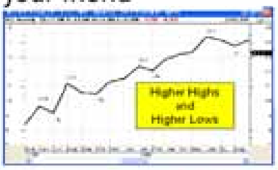
- Find some useful price charts
- Watch the market (eg. market index — XAO)
- Use useful technical indicator tools:
  - Moving Average (30-week, GMMA)
  - Coppock indicator
  - Momentum (and search for divergence)
  - Money Flow (and search for divergence)
- View good quality charts

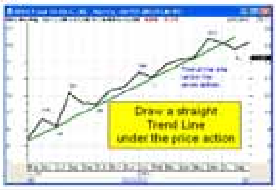
10 Key Lessons

#9 — Chart reading — very useful

The trend is your friend

- HH = Higher Highs
- HL = Higher Lows
- A trend is in place until it is confirmed to no longer be in place
- Applies to Up trend, and Down trend.





10 Key Lessons

#9 — Chart reading — very useful

Sample charts

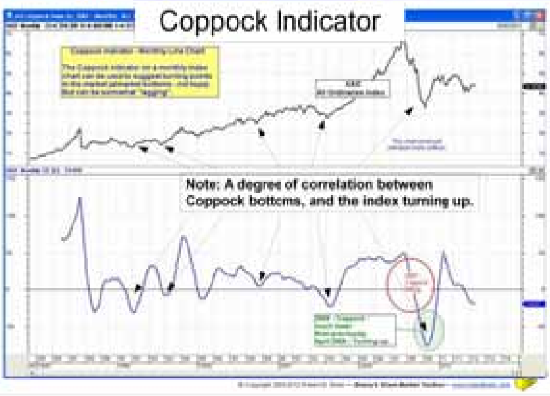
Some sample and useful price charts follow...

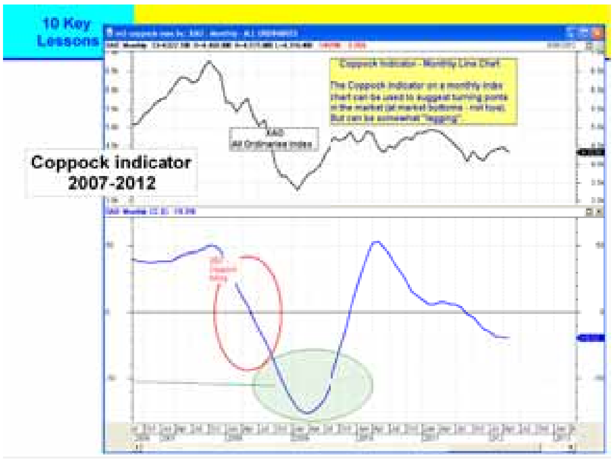
With latest (zoomed in) updates included (as at 8 May 2012)

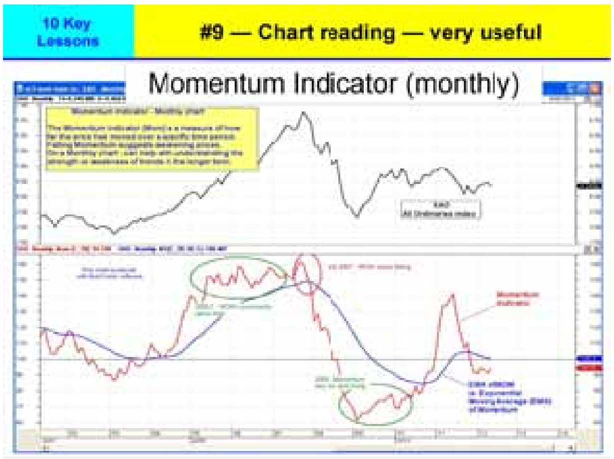
10 Key Lessons

#9 — Chart reading — very useful

Coppock Indicator




10 Key Lessons
Coppock indicator
2007-2012


10 Key Lessons
#9 — Chart reading — very useful
Momentum Indicator (monthly)


10 Key Lessons
Momentum Indicator
2009-2012


10 Key Lessons
#9 — Chart reading — very useful
Stan Weinstein
Stage Analysis Ribbon

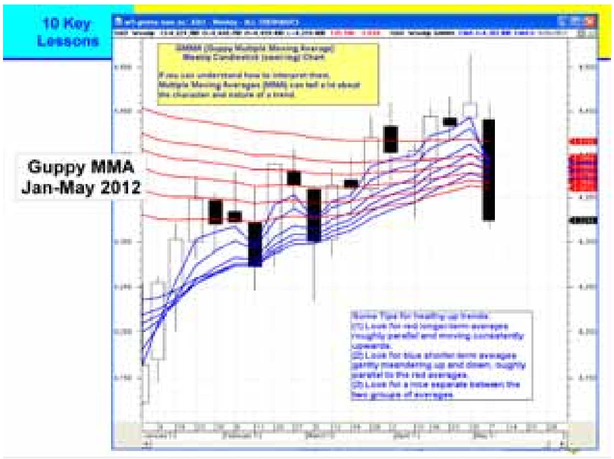

10 Key Lessons
Weinstein's chart
30-week SMA
Oct 2011-May2012


10 Key Lessons
#9 — Chart reading — very useful
Momentum divergence


10 Key Lessons
Momentum (weekly)
July 2011-May 2012


10 Key Lessons
#9 — Chart reading — very useful
Twiggs Money Flow indicator


10 Key Lessons
Twiggs Money Flow indicator
Oct 2011 — May 2012



10 Key Lessons

#9 — Chart reading — very useful

These charts...

The charts on the previous slides
are already posted on the web
and updated weekly

Visit:

www.robertbrain.com/weekly

10 Key Lessons

#9 — Chart reading — very useful

Candlesticks

- Don't forget, candlestick charts can tell a whole story:
  - the presence or absence of buyers and sellers
  - testing of higher (or lower) prices
  - indicates the underlying mood and sentiment of the market participants

see chart.../

10 Key Lessons

#9 — Chart reading — very useful

Volume is important

- In a healthy rising trend:
  - Rising prices should be supported by rising volumes, and
  - Falling prices will see lower volumes.
- If we see rising volumes with falling prices, it shows weakness and possible further falls.

see chart.../

10 Key Lessons

#9 — Chart reading — very useful

The lesson:

Charts
and Technical Analysis
can be very useful.

Back to the list of 10 Key Lessons

10 Key Lessons

#10 — Risk versus reward

Lesson #10

Risk / Reward
Understand and respect it

10 Key Lessons

#10 — Risk versus reward

To help us sleep at night:

- Keep the amount of money "at risk" with any one position to a small amount.
- Keep the portion of our total portfolio in any one position to a small amount.

10 Key Lessons

#10 — Risk versus reward

For example

With $10,000 of investment capital:

- Commit no more than 20% to any one investment position (ie. up to $2,000).
- If any one investment position might go 'bad", then be prepared to sell it after losing about 2% of the total capital (ie. up to $200)
  This is the "amount at risk".
  [Implement this approach using a Stop Loss.]

10 Key Lessons

#10 — Risk versus reward

Other considerations

- In a bear market => be more "careful";
- Spread investments across asset classes (understand the GICS codes and sectors);

10 Key Lessons

#10 — Risk versus reward

Optimise position size

- A small position size is difficult (eg. $500) because brokerage puts a hole in it.
- A very large position size might be too large a portion of the total investment capital.
- Need to strike an "optimal" position size:
  - At least about $2,000-3,000
  - Maybe $5,000 to $10,000+

10 Key Lessons

#10 — Risk versus reward

Reward to Risk ratio

For any one investment,
the amount of money we put "at risk"
might be able to reap a tiny reward, or
a large reward.

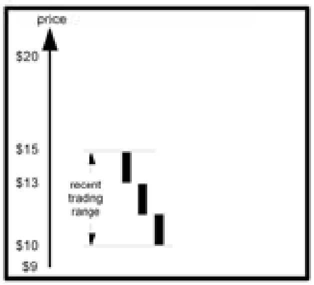
- eg. BHP is unlikely to experience significant share price rise.
  So, would the dividends suffice?
- Perhaps consider a more volatile stock, with the possibility of a significant price rise eg. Fortescue Metals (FMG)

10 Key Lessons

#10 — Risk versus reward

On the chart (example):

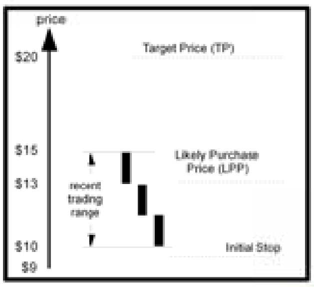
- Recent trading range $10-$15
- Anticipate a rising trend.



10 Key Lessons

#10 — Risk versus reward

1) Determine three key price points:
- Target price = $20
- Likely purchase price = $13
- Initial stop = $9.50



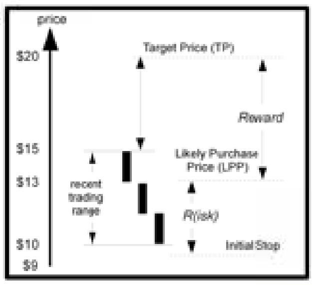
10 Key Lessons

#10 — Risk versus reward

2) Calculate:
- Reward amount
- Risk amount

3) Calculate:
- Reward/Risk Ratio

4) Ideally:
- greater than 2



10 Key Lessons

#10 — Risk versus reward

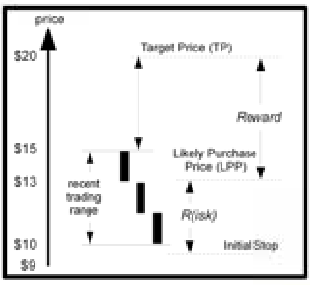
Reward/Risk Ratio

= $7 / $3.50

= 2

The greater the reward, the better the ratio.

Great if 3, 4 or 5+



10 Key Lessons

#10 — Risk versus reward

The lesson:

Risk / Reward
Understand and respect it

10 Key Lessons

#10 — Risk versus reward

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10 Key Lessons

Summary & Wrap up

SUMMARY

- Whatever has happened before, could happen again.
- There are lessons to be learnt from past "financial crises".
- Here is the list of Ten Key Lessons again.../