

Trading Insights 1a - What to Trade?

Trading Insights

A series of workshop sessions
for ATAA members

Session 1(a) What to trade?

Material provided by Mark Umansky
Slides prepared and presented by Robert Brain



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Version 2b

About this material

This set of presentation slides was prepared for a presentation/workshop at the ATAA Melb meeting in March 2020.

With the large number of slides herein, the presentation and discussion was cut shorter than the planned 20 minutes. With a knowledgeable and involved audience, this presentation could take around 40 minutes.

The basic set of slides is intended to be available to ATAA members on the ATAA website www.ataa.asn.au

If we run out of time to go through this material, audience members are encouraged to re-visit the set of slides.

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Trading Insights — About

This series of sessions entitled “Trading Insights” comprises 12 topics, to be covered two at a time in an ATAA chapter meeting.

Two topics will be covered for about 20 minutes each in any one session.

The session presenter might not be a subject matter expert, and might rely on experienced audience members to supplement the discussion.

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Trading Insights — Who is this for?

- This Trading Insights series is intended for:
- (a) Newbies to trading/investing, and
 - (b) Intermediate and advanced traders/investors;
 - (c) ATAA members and prospective members.

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Trading Insights — Purpose

- (a) To help provide a head-start into trading/investing for “newbies”.
- (b) To help intermediate and advanced traders/investors to tweak their approach and strategies by sharing their own knowledge and experience, and picking up some clues and re-thinking their approach.
- (c) To educate the “newbies” to trading and investing about HOW to go about it.
- (d) To provide ideas and considerations about trading/investing, to help progress their journey.
- (e) To highlight the traps and pitfalls.

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In this insights session...

- (a) “What to trade?” (Mark Umansky)
- (b) “How much money do I need?” (Robert B)

The following slides will provide some information and discussion-starting comments on the above topics.

The presenter might be more a *moderator* and not a *subject matter expert*, so **your input** will be greatly appreciated for the benefit of everyone present.

On the following slides, this is your prompt to contribute to the discussion...



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Trading Insights 1a - What to Trade?

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What to trade? (Mark)

What to trade?

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What to trade? (Mark)

Whether a newbie to trading/investing, or an old-hand, a good question is:

“What should I trade / invest in?”

There are a number of *instruments*, *markets* and *asset classes* that are often mentioned, including:

- Shares
- Currencies
- Commodities
- CFDs
- Options
- Futures
- Warrants

Let's help to clarify all this...

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Why important?

By knowing:

- 1) What **instruments** and **markets** are available?
- 2) How these instruments are created and function?
- 3) Their **risk and benefit parameters**, and
- 4) Their **capital requirements** per instruments

Individual traders / investors can decide how to best utilise the available instrument in their pursuit of profit from the prevailing market conditions.

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For example...

During bull markets you can either:

- Purchase company shares
- Purchase index ETFs
- Purchase forex (foreign currency)
- Purchase futures contracts
- Purchase call options
- Sell put options
- Purchase CFDs
- etc.

For:
capital growth
and/or
income

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So you can see...

There are **plenty of instruments** available if you wish to profit from prevailing market conditions; BUT:

- Which instrument to use?
- How much money will I need?
- How much risk does each instrument carry?
- What are the advantages of using a particular instruments compared to the others available?
- What are the disadvantages of using a particular instruments compared to the others available?
- etc...

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What to trade?

All of these questions are important, as most traders will overlook the opportunities available to them simply because of lack of knowledge and understanding of the best type of instruments to be used within a particular strategy or scenario.

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Summary list

Summary list of **instruments** and their **markets**:

- Share / equities / stock markets*
- ETPs / ETFs (Exchange Traded Products)
- Options market
- Futures market
- Forex market
- CFDs market

* – Often interchangeable names for same thing

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Equity markets

Equity markets
Share markets
Stock markets

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Trading Insights 1a - What to Trade?

Equities markets

- Most (ATAA) traders investors participate in share markets, so it's well understood;
- Different equities markets:
 - ASX ~ 2200 shares/companies
 - NYSE ~ 2800
 - NASDAQ ~ 3300
 - FTSE ~ 2000
 - etc...

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Stock exchanges

Stock exchanges, market cap, numbers...

Rank	Stock Exchange	Short Name	Region	Market cap (USD bn)	Number of Companies Listed
1	New York Stock Exchange	NYSE	United States	22,923	2,800
2	Nasdaq	NASDAQ	United States	10,857	3,300
3	Japan Exchange Group	JPX	Japan	5,679	2,200
4	Shanghai Stock Exchange	SSX	China	4,026	1,041
5	Hong Kong Stock Exchange	SEHK	Hong Kong	3,936	2,118
6	Euronext	EUORNEXT	European Union	3,927	1,400
7	London Stock Exchange	LSE	United Kingdom	3,787	2,600
8	Shenzhen Stock Exchange	SZSE	China	2,504	2,209
9	TMX Group	TSX	Canada	2,095	2,231
10	Bombay Stock Exchange	BSE	India	2,056	5,000
11	Natbnal Stock Exchange	NSE	India	2,030	1,600
16	Australian Securities Exchange	ASX	Australia	1,328	2,185

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About Shares

- By investing in shares you are buying part ownership of a listed company.
- If the company performs well, you can benefit from share price growth and/or income paid as dividends.
- If the company performs poorly, your shares might decrease in value and/or the company may pay no dividends.
- Shares are issued by listed companies and traded by investors on the share market, either on their local or foreign market.
- You can trade shares by using a licensed broker to buy and sell shares on your behalf.

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Shares – features, pros/cons

A number of features and pros/cons:

- **Capital growth** — share price up (or down)
- **Dividends** — a slice of the profit
- **Buying and Selling** — is easy
- **Spread your risk** — across several companies and sectors
- **Shareholder rights** — get information and vote and receive rights issues.

Details over.../

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Shares – features, pros/cons

Capital growth:

- Share price can go up — building wealth
- Share price can go down, even to zilch, so you could lose all your money. Even “blue chip” stocks can go belly-up.
- Monitor share price performance using various tools (eg. ASX Watchlist tool).



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Shares – features, pros/cons

Get dividends — a slice of the profit

- This is paid by **some** companies, usually from a share of the company profits.
- Some pay regularly, and some not so.
- Some companies allow you to “re-invest” the dividends — known as DRP.
- Some investors might also get tax benefits (eg. franking credits).
- ✔ • No guarantee of continuity of dividends.

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Shares – features, pros/cons

Shareholder rights:

- Receive company information
- Vote at the company AGM
- Participate in “rights issues”, etc.



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Shares – features, pros/cons

Winning when you’re losing (and vice versa):

- Negative gearing — if you have borrowed in order to fund the share purchase, your borrowing costs might outweigh the capital growth + dividends.

Losing when you’re losing:

- Losing money might seem to be clever (for tax purposes), but the emotions can be stressful, and we really want to be ahead.

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Shares – features, pros/cons

Buying and Selling — is easy:

- Via an online broker — very easy.
- Via full-service broker — not hard.
- Easier than: unlisted shares, property, term deposits.
- Brokerage fees for executing a trade, vary from broker to broker.
- The size of the share parcel is important.

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Shares – features, pros/cons

Lots of choice:

- Buy shares in Australian companies, or overseas companies, large blue chips, or small Aussie businesses with promise.
- Invest in exciting start-ups or established cos.
- Invest in: banks, miners, telecoms, retailers, tech companies, media firms, biotechs, energy providers, software companies, etc.
- Beware! of the many, many choices and the many risks.

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Shares – features, pros/cons

Easy or hard to transact?

- Buying and selling listed shares can be easy and quick (for heavily traded shares).
- Much easier and quicker than trying to buy or sell real estate.
- Beware of the share trading brokerage costs.

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Shares – features, pros/cons

There are risks:

- Spread your risk across several companies, and across sectors.
- Liquidity risks? — Stick to the companies that trade heavily on the market.
- Small position size? — Can make it hard to achieve a profit.
- Money risks — eg. slippage, brokerage.

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ETPs and ETFs

Exchange Traded Products and Exchange Traded Funds

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ETPs and ETFs

- Exchange-traded products (ETPs) is the family name for the group of products comprising exchange-traded funds (ETFs), managed funds (MF) and structured products (SPs). There are over 100 ETPs accessible through ASX.
- Funds representing all sorts of sectors, industries, currencies and commodities.
- Trading similar to stocks, these funds can be bought and sold rapidly or held long term.

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ETPs and ETFs

Different types:

- Most ETPs generally seek to track the performance of a specified index or benchmark (eg. S&P/ASX 200 index) or a currency such as the USD or a commodity such as gold.
- Single asset products that track the performance of a specific security, bond or debenture are also available.

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ETPs and ETFs

ETPs are open-ended:

- The number of units on issue is not fixed but can increase or decrease in response to demand and supply from investors. This assists in ensuring that the ETPs trade at or near their net asset value (NAV).
- ETPs trade, clear and settle in the same way as shares on the ASX.

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ETPs and ETFs

ETPs can offer exposures across a range of asset classes including:-

- Australian shares ETPs
- International shares ETPs
- Commodity ETPs
- Fixed income ETPs
- Currency ETPs
- Cash ETPs.

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ETPs and ETFs

Why trade in these?

- They provide access to many securities and indices, and sectors, and groups of securities, and types of risks.
- Many are listed and can be easily traded on the regular exchange.

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Options market

Options market

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Options market

- A market which allows participants to undertake positions in the **underlying asset**;
- Therefore, the option itself is **not ownership** of the underlying asset (though rights and obligations do exist).

Ref: [https://en.wikipedia.org/wiki/Option_\(finance\)](https://en.wikipedia.org/wiki/Option_(finance))

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Options market

An option is a **contract** that gives the buyer the **right**, but not the **obligation**, to buy/sell the underlying asset or instrument at a specified **strike** price prior to, or on, a specified date.

Ref: [https://en.wikipedia.org/wiki/Option_\(finance\)](https://en.wikipedia.org/wiki/Option_(finance))

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Options market

- The option price (along with other inputs) fluctuates with the value of (or lack of value of) the underlying asset.
- Options can be traded on shares; and options on futures contracts; etc.

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Options market

Why trade options?

- To hedge against various risks (eg. bear market)
- For income (by selling an option)
- Can be less risky than shares
- Less capital needed than shares
- But can lose all of your capital.

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Futures markets

Futures markets

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Futures markets

A **futures contract** is:

- A **legal agreement** to buy or sell a particular commodity asset, or security, at a predetermined price, at a specified time in the future.
- Futures contracts are standardised for quality and quantity to facilitate trading on a futures exchange.

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Futures market

Futures markets for:

- Foreign Currency
- Metals
- Indices
- Bonds
- Energy
- Meats
- Commodities
- Softs
- Grains
- etc.,...

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Futures — Pros and Cons

Pros:

- Futures trading involves an extremely liquid market.
- Costs are fixed in advance.
- Cost of Entry is based on margin % requirements.
- The greater the leverage, typically, the greater your potential gains.

Cons:

- Futures are considered riskier than trading stocks, primarily because of leverage and the amount of leverage allowed.
- The potential for loss could be substantial.
- No industry standard for commission and fee structure through brokers.

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Options and Futures market

What is the difference between options and futures?

- Options contract — The right to buy/sell the underlying asset/instrument.
- Futures contract — A contract to exchange the real asset at a specific future date for an agreed price.

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Futures market

Why trade futures?

- A fast, cost effective way to trade various markets
- The contracts to buy or sell are standardised
- To reduce risks
- To seek profits.

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Forex market

Forex market

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Forex market

- Forex = Foreign Exchange = Currency market
- The international currency market is the largest financial market in the world.
- The forex market facilitates the exchange of one currency for another currency.
- Currencies are always traded in pairs, with many potential combinations available, but only some of which are very liquid.
- Types: Spot market, Futures market, Forward market, Options market, Swaps market

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Forex market — Pros and Cons

Pros:

- Sizeable leverage can turn a lot of money into a major profit.
- The forex market is extremely liquid and accessible.
- There's no central exchange, and it is decentralised and deregulated, all good things for traders who like consistency.

Cons:

- Sizeable leverage can turn into a major loss, losing more than you wanted.
- Extreme volatility can occur in the foreign exchange market.
- There can be less regulatory control.
- Price determination can be tough to discern, particularly regarding foreign economies and global politics.

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Forex v Stocks — Key diffs

FOREX MARKET	STOCK MARKET
Large volume around \$5 trillion per day	Less volume roughly \$0.2 trillion per day
Highly liquid	Less liquid
24 hour markets	8 hour markets (in local time zones)
Minimal or no commissions	Commissions / brokerage
Narrow focus (currencies)	Wide focus (multi-sectors)

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Forex market

Why trade forex?

- A very large and liquid market.
- Can make a lot of money quickly; but can lose a lot of money very quickly.
- The **journey** — enjoy the research to understand the drivers of currency prices, or just trade for profit (hopefully), and maybe just use technical analysis for decisions.

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CFD markets

CFDs

**Contracts for
Difference**

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CFD markets

A Contract For Difference is:

A contract between two parties specifying that one party will pay the other party **the difference in the price** of an asset

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CFD markets

- A hybrid of the stock, forex, futures & options markets;
- Allow participants to place trades on a **derivative** product based on an underlying asset;
- Generally the CFD does not have an expiry date, premium or commission (see broker's terms and conditions);
- Generally requires the participant to pay a larger **bid/ask spread** than what would be seen in the actual physical market for a product.

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CFD markets

CFD markets exist for:

- Equities
- Indices
- Bonds
- Commodities
- Forex
- Crypto currencies
- etc...

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CFD markets

How?

- Access a CFD market through a **CFD service provider**
(eg. CMC, IG, FP Markets, Plus500, XTB, AvaTrade, IC Markets, etc....)
- The service provider is a **market-maker**, and they have some control over the buy/sell prices, and the **spread** between the buy and sell prices.

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CFD markets

Why trade CFDs?

- Can trade CFD contracts on almost anything, including:
shares, commodities, indices, etc., etc.
- Leverage is inherent.
- Can make a lot of money quickly, but can lose a lot of money very quickly.

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Summary comparisons

	PROS	CONS
Shares	<ul style="list-style-type: none"> • Lots of people participate • Easy to talk about in networks 	<ul style="list-style-type: none"> • Liquidity risk • Company and Market risk
ETPs, ETFs	<ul style="list-style-type: none"> • Many can be easily traded 	<ul style="list-style-type: none"> • Liquidity risk
Options	<ul style="list-style-type: none"> • Less capital required • Can be used for hedging or for income 	<ul style="list-style-type: none"> • Can lose all the capital
Futures	<ul style="list-style-type: none"> • To reduce risks and to hedge. • Participate in the markets (ie. the journey) 	<ul style="list-style-type: none"> • TBA
Forex (currencies)	<ul style="list-style-type: none"> • Very large, liquid market • Minimal commissions • Leverage => large profits 	<ul style="list-style-type: none"> • Narrow focus (currency pairs) • Leverage => large losses
CFDs	<ul style="list-style-type: none"> • Leverage — can gain a lot 	<ul style="list-style-type: none"> • Leverage — can lost a lot
Commodities		

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How to get started?

For information about how to get started, or the steps to go forward, including clues on trading strategies see later sessions in this TRADING INSIGHTS series.

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What to trade? — SUMMARY

- There are several different instruments, markets and variations available to trade or invest in.
- Take care.
- Be knowledgeable.
- Watch out for the risks.

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Trading Insights

Stay tuned for discussions on:

- | | |
|--------------------------|----------------------------------|
| (a) Stock universe | (a) Brokers and their fees |
| (b) Other instruments | (b) Position sizing |
| (c) Buy signals | (c) Initial stop loss |
| (d) Trend trading (more) | (d) Risk management |
| (e) Other strategies | (e) Trading plans and strategies |

“Trading Insights” segments in Melbourne Chapter meetings in 2020

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About this material

This set of presentation slides was used in a workshop in the ATAA Melbourne meeting in March 2020.

The basic set of slides is intended to be available to ATAA members on the ATAA website www.ataa.asn.au

The members of Brainy's Share Market Toolbox can also download these slides plus the more detailed Speaker Notes from the Share Market Toolbox www.robertbrain.com/presentations/

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