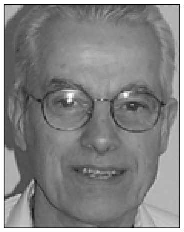
Trading dos and don'ts that have helped me

By Peter Degraaf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Did you hear about the woodsman who, when asked by a friend how long it had been since he had his axe sharpened, replied: "I just don't have the time for that."

No matter how good a trader we may have become, we're still not perfect. Yet, perfection must always be our aim, and we must never be too busy to improve.

This essay is meant to help the reader become an even better trader than he or she is today, and as part of it, I'd like to present you with a few dos and don'ts that have worked for me over the years.

As a starting point, allow me to introduce you to an excellent way to sharpen your skills. There is a mutual fund company in California that has come up with a brilliant idea: Marketocracy, founded by Ken Kam. He has introduced a novel plan to attract talented traders and investors for his investment funds.

As part of this concept, Mr. Kam has built a website, *www .marketocracy.com*, that offers an open invitation to traders and investors to open a "cyber account" at his site. Everyone who registers at the website is issued $1,000,000 in "cyber dollars." (They will issue up to $15M - $1M for each of 15 model funds). With these accounts comes the challenge to outperform some 100,000 other traders at the site.

Marketocracy has an excellent staff that keeps meticulous track of the performance of each of those traders. At the end of the day, there is an accounting, complete with a chart of your performance, as measured against the Dow Jones industrials, S&P and Nasdaq.

Once you have outperformed the mainstream averages, your next goal is to move into the top- 100 model funds at Marketocracy called the M100. In that select group you are entitled to a number of special privileges that will help you to become even more proficient, (and Marketocracy signs a research contract with you with a short-term and long-term compensation program that is based on assets under management).

Traders from the M100 group may be asked to assist with selecting stocks for Marketocracy's "real money fund" the Marketocracy Masters 100 Fund MOFQX.

By picking the brains of the M100, and using some of the funds from within the M100, the MOFQX fund since inception Nov 5, 2001, has returned profits of 86.23 per cent, versus 46.08 per cent return for the S&P 500. This rate of return is almost double that of the S&P 500. Marketocracy is thus a "farm system" for MOFQX, and for several other funds that Marketocracy operates. This farm system has developed into the most extensive system of gathering investing talent in the world.

Put all your eggs in one basket, then watch the basket

Thus, your benefits while trading at Marketocracy are two-fold:

Sharpening trading skills without risk, and the possibility of becoming a fund manager.

Marketocracy has a set of rules that must be obeyed. These rules are similar to the rules that fund managers on Wall St. or Bay St. have to adhere to.

I have personally enjoyed the experience of cyber trading at Marketocracy since May 2005, and watched my "cyber" fund there increase by 75 per cent in 26 months, or three per cent per month. This roughly parallels the returns in my own stock portfolio.

I feel that the experience has been a real benefit, and it enables me to constantly stay "in tune" with the markets.

Here then are some dos and don'ts for your consideration:

- Trade only in paid positions, avoiding margin; sectors that are rising; stocks that have experienced management; stocks that have "net asset value."
- Put all your eggs in one basket, then watch the basket.
- Diversify exclusively within the sector you are interested in.
- Do not put more than 10 per cent (five per cent is even better), of your available capital into one stock, unless you're just starting out with limited capital. In that case make 10 per cent your goal as your portfolio grows.

Buy stocks when price is near the 200-day moving average, as long as the it is rising. (*www-.bigcharts.com* and *www-.stockcharts.com* both include the 200-day moving average in all of their charts, making this very simple. In my early days, I had to do all this with pen, paper and calculator).

- Take partial or full profits when your stock trades too far above the 200-day moving average. The simplest way to do this is to put in a "good till cancelled" order when your stock nears your target price.

Ideally, if you buy 2,000 shares of XYZ at $1, and the price goes to $2, by selling 1,000 shares, the rest are free, and you can let them ride.

Some traders like to use protective sell stops. If you decide to employ them, use the moving average for that.

You can sell once price closes below the moving average or upon the close once the price closes two per cent below. Once your stop is in place, do not change it. Stick with your plan.

Avoid getting caught up in the hype. The old adage Buy Low — Sell High is still effective, but it only works for those who buy low. Ideally, when a sector reaches a temporary top, you should be 25 per cent to 50 per cent into cash.

Avoid looking at your stocks too often. Discipline yourself to ride out the minor ups and downs, they are part of the game.

If you're new to stock trading, do some paper trading first. See how you make out on paper. Or, better yet, open a cyber account at Marketocracy.

Read all you can about the sector, and about the stocks in that sector. Visit *www.google.com,* and see what has been written about the stock. Then spend time at the company website.

If you decide to follow the advice of an analyst, check out his or her record. Keep track of their advice, to see how accurate they are. Look at previous newsletters in the archived section for guidance.

There are many other trading rules, and over time you will add some, and drop some, till you have a system that is right for you.

We end this essay with a quote from Richard Russell, now in his 80s, he still sends out a regular newsletter to his subscribers: "A successful investor is someone who buys the dips and rides the waves".

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