TUTORIALS IN APPLIED TECHNICAL ANALYSIS

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The Australian Internet Trading Weekly with independent analysis

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Edited by Daryl Guppy with contributions from J Mitchell, S Blair, R Harper, and P Rak
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Stocks mentioned in this issue

HIB, MAP, PBG, WES, XJO, MIG, STW, CTX.

Note. The more computer icons appearing after a section heading, the more advanced the material.

CONTENTS

EFFECTIVE REBOUND STRATEGIES

By Daryl Guppy

TRADERS GLOSSARY

WATCHLISTS

Watch lists are a fundamental tool for all traders. They are a list of stocks which the trader is interested in. They can be selected by many means, from hot tips, from eyeball scans, from complex technical explorations, from brokers tips and newspapers. The list contains a group of stocks which the trader watches over the following days or weeks.

Some lists include stocks that are currently held. Others include just speculative holdings, or investment sections of the portfolio. The list might include stocks that have good trading potential and we want to watch them, ready to jump when money becomes available.

Watch lists allow the trader to efficiently organize his analysis of the market and quickly keep up to date with stocks of interest to him. Stocks in a watch list are automatically up dated with each new days data.

Last week we jumped the gun by including an unnamed trading example designed to illustrate the conclusions discussed in the earnings trading strategy discussed in articles below. In a later article we look at the way traders develop a strategy to deal with the shortened reporting season and the increase in the number of earnings downgrades. By understanding how the market has reacted in recent similar periods we have a firmer basis to develop a trading strategy. We did not name this example for two reasons. First, we want to explain the strategy in full and this will not happen until part 2 of the article is published this week. Second, this is a developing trade and to preserve this as an educational example we feel that it is preferable to leave this example unidentified at the moment. Readers will be able to verify entry conditions next week.

We note the probability of success, but in this example we selected a developing example that used the wrong side of probability. The example did not rebound and this turns into a losing trade. This does not invalidate the strategy or our conclusions. It is simply part of the balance of probabilities that prevail in any trading strategy. That is acceptable for three reasons.

- It highlights the essential conditions of trading. Success is not guaranteed so we need to plan for failure.
- We can use the example to show how trading stop loss discipline protects the trader. The function of this newsletter is to educate, not to provide stock tips or investment advice. Traders need to learn how to handle success as well as failure.
- It also serves as a useful reminder of the integrity of these trading examples used in the notional case study portfolio. Occasionally we receive feedback that suggests the notional case study examples are ‘manipulated.’ If this were true then we would have taken steps to ‘delete’ this current failed example because of the adverse impact on case study portfolio returns. As with all case study examples, good or bad, we include it in the ongoing results. We do not expect to receive email complaining about this.

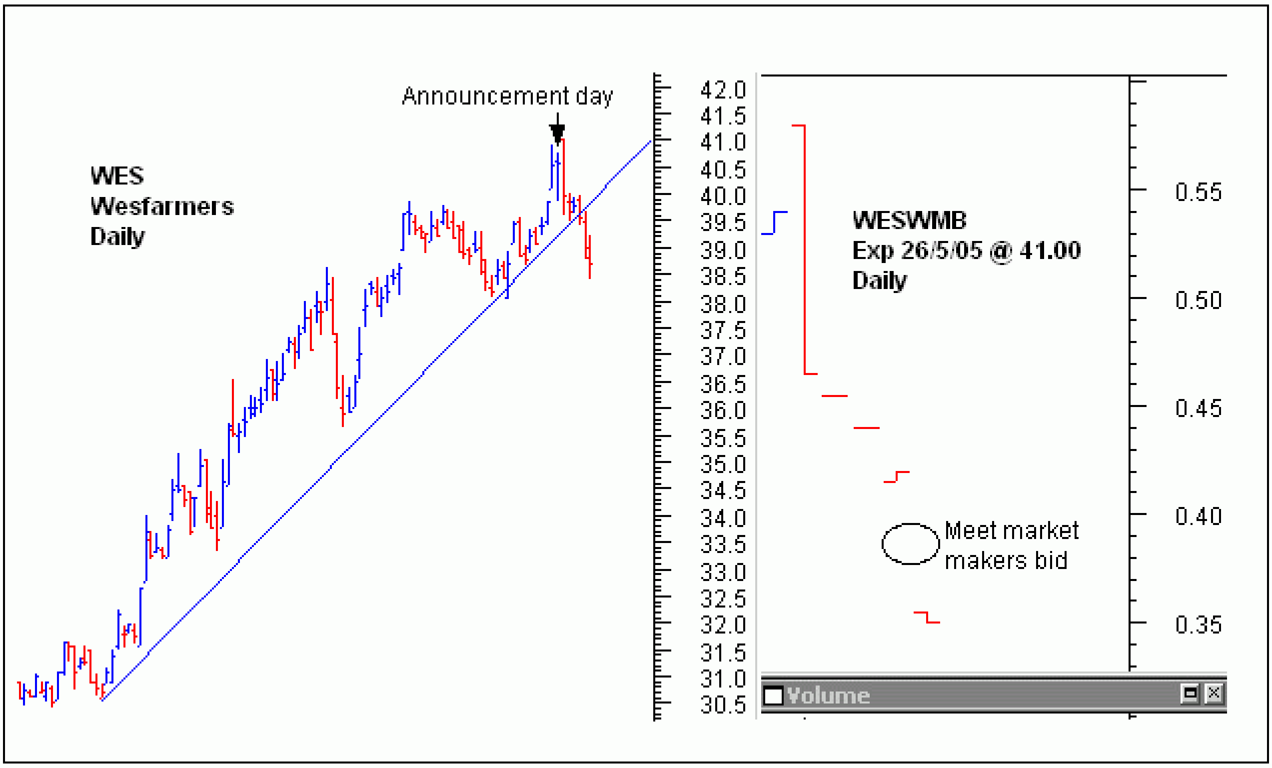
We also note an interesting developing situation in another unnamed stock example. This is also compatible with the earnings strategy under discussion and we want to flag it as a potential application for next week’s newsletter. We face the same educational restrains mentioned above, so this example also remains unnamed.

Type of trade – DIVIDEND EARNINGS STRATEGY

This is a rebound strategy based on the analysis notes discussed below. Full details of the trading plan and strategy are included in the second part of this article series printed below.

Trading plan

The trade plan assumes that the immediate reaction to the WES profit downgrade or earnings downgrade is similar to the reaction when a stock goes ex-dividend. On this basis, an entry is made during this period of emotional overreaction with the intention of benefiting from the short term rebound, or the longer term resumption of the trend.



- Uptrend defined by a straight edge trend line.
- **Prices are expected to rebound from this level. This did not happen, and this signalled an exit from the trade.**

- The price dips are still consistent with up trend. The dips carry price down to the trend line.
- **Move below the trend line, associated with a reaction to the earnings release, triggered an immediate exit.**
- Sell off after an earnings downgrade announcement is strong and position in the trend indicates a higher probability of a rebound.
- **This failed to hold. When prices fail to hold on a well defined trend level then a rapid exit is signalled.**
- Rebound advantage is maximised by the use of a leveraged trading instrument, in this case a warrant.
- **This also increases the risk in the face of strategy failure. Again, this emphasises the need for a rapid exit.**

Position size, stop loss and protect profit conditions

For tutorial purposes we add this WESWMB warrant at $0.455 as a notional case study illustrating the application of the earnings strategy based on the implied relationship emerging from the behaviour of stocks during the recent ex-dividend trading period.

The stop loss for the warrant trade uses the trend line on the underlying stock as the exit condition. Position size is reduced in the warrant. This reflects lower trading volume and also is a way of reducing the risk associated with a higher level of volatility. For case study purposes we add 22,000 warrants for a total cost of $10,010. (Although this is a notional trade, we note that this number is less than the total number traded on the entry day.) Warrants offer a higher level of leveraged return – and potential loss. **Reduction in trade size is one way to manage this risk**. **The financial stop loss on this trade reduces the exit point to $0.364. At this level this trade would lose $2,000 or 2% of our total portfolio trading capital. With an entry at $0.455, a fall to $0.364 is nearly equivalent to the warrant volatility range shown on the day prior to entry.**

The large gap in warrant prices underlines the importance of reducing trade size as a method of containing risk. 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.

For tutorial purposes we take an exit at $0.385, even though no trading is shown at this level. The warrant did not trade for the two days after the close below the WES trend line. However, the market issuer continued to post bid and ask prices during this period. The market reality is that no warrant holder decided to trade at these posted prices. However, the strategy we outlined in these trade notes calls for this trade to be quickly closed as soon as there is confirmation of a trend failure. When there is no rebound, the trading plan requires a rapid exit.

In these circumstances the warrant trader has no choice but to trade with the warrant issuer by taking the offered buy price. This issuer trades in 10,000 lots and we have 22,000 to sell. This provides an achievable average exit price of $0.385 as shown. The important feature here is the method that is used to manage this trade exit. The actual trading record shows no *traded* activity during this period. However, this does not mean an exit could not have been made. The warrant holder is always able to trade with the market maker or warrant issuer. It may not be at the trader's preferred price, but an exit is achievable even though other warrant traders do not want to do business.

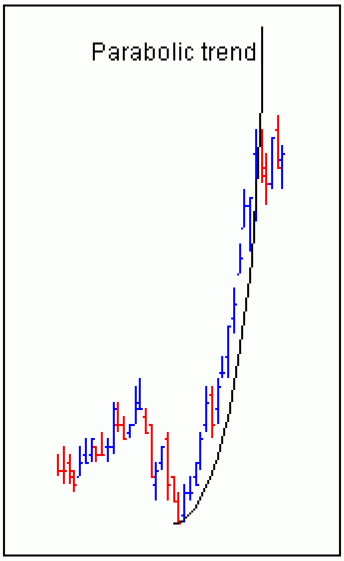
This case study trade is closed at $0.385 for a loss of $1,540, or 1.5% of total trading capital.

Current Status

Trade is closed.

Type of trade – PARABOLIC TRADE

We flag this example of a parabolic trend because the trend collapse provides an alternative way to implement the earnings strategy discussed elsewhere. The parabolic curve is plotted to get the best fit on the known low points of the trend. A characteristic of this type of trade is the rapid collapse of prices once the trend is broken when price moves to the left of the trend line. We leave this stock unidentified at this point.



Trading plan

The objective is to wait for the decline in the parabolic trend and use this as an entry point for a trade based on the earnings strategy analysis which starts this week. We provide full details of the trading plan next week.

The chart has been updated. The high probability parabolic decline has not yet developed. The trade remains unnamed, and under observation.

Position size, stop loss and protect profit conditions

Details next week if trade reaches entry conditions.

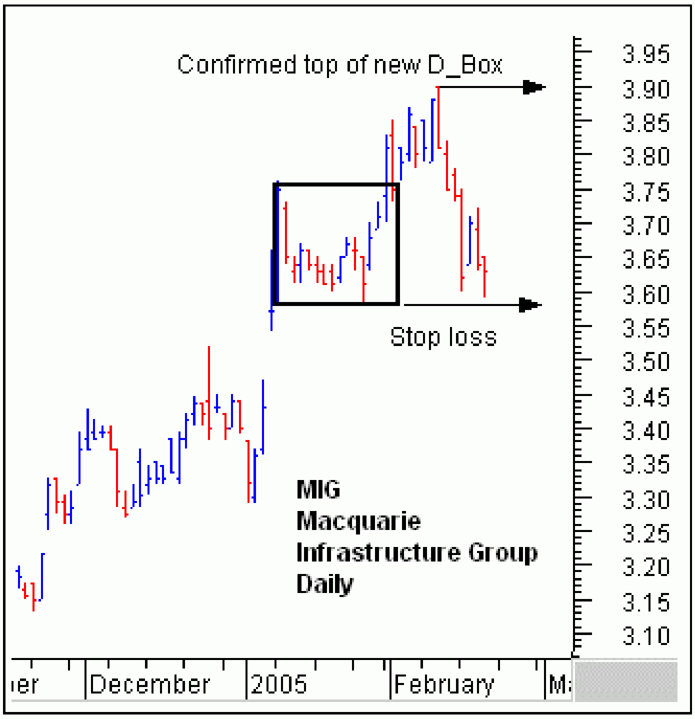
Current Status

Trade is placed on watch list.

Remains on watch list.

Type of trade – DARVAS TREND TRADE

This is a Darvas trend trade using a modern Darvas box for management. This means that no action is taken until there is a close above or below the edges of the Darvas box. Exit is made on the following day. Darvas trading is not suitable for all stocks. However, the method provides a very robust way of setting support and resistance levels that are consistent with trending behaviour, which allow for retreat and rebound activity and which set a resistance point based on a single new high. This case study is an example of the way traders anticipate pullbacks in the trend and use them as an entry opportunity.



Trading plan

The objective is to apply a modern Darvas trading approach and join an established trend at a point of temporary price weakness.

- For the trade to continue, prices must continue to close above the bottom of the Darvas box.
- **Trade remains open**.
- A close below the Darvas box triggers an exit in the next day.
- **No exit required. This example uses a modern Darvas approach so we look for a close below the current D_Box stop loss.**
- A breakout above the box uses a ghost box as a stop loss if no new Darvas box is created

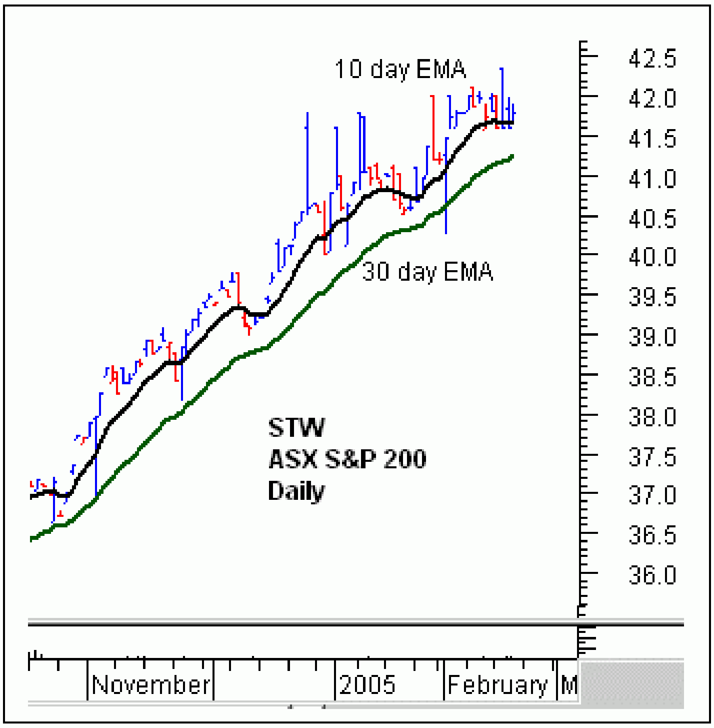
rapidly. Breakout, but no conditions for a ghost box. Stop loss remains unchanged.

- **The top of the next D_Box is confirmed.**
- There is no target for the trend. The objective in this style of trading is to stay with the trend until the Darvas box signals an exit.
- **No change**

Position size, stop loss and protect profit conditions
For tutorial purposes we add MIG as an example of this strategy. This is a low risk strategy because the amount at risk based on the stop loss point is $112. Entry for tutorial purposes is made at $3.60 with the bottom of the D_Box at $3.58. At this entry price we add 5,600 shares for a total cost of $20,160. 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.

Current Status

This case study trade remains open.



Exchange Traded Fund Strategy

There is no change in the management of the STW case study trade using an Exchange Traded Fund (ETF). As shown in the Market Outlook notes, traders are aware of the needs for caution in this extreme trend, but this does not prevent them from taking advantage of the profit opportunities offered by the trend. Having a cautious outlook on the market is not inconsistent with trading the rising 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.

SETTING PRICE OBJECTIVES FOR NON PATTERN BASED TRADING – PART 4

By Jason Mitchell

SUBJECT SUMMARY
PROBABILITY AND ODDS

The probability of an event occurring is the ratio of favourable outcomes to the total number of possible combinations. The odds of an event happening is the ratio of favourable outcomes to unfavourable outcomes.

In the market, these differences have important impacts. The total number of possible favourable outcomes in trade is finite. You can make a profit, break even, or lose money. The total number of possible outcomes – not combinations - is 3. There is only one favourable outcome, so the odds are against you in every trade. The ratio of favourable outcomes is always 1:2.

We offset the odds in trading by identifying the balance of probabilities – the total number of price combinations. The balance is most easily seen visually. We use a straight edge trend line. A stock that has been trending upwards for six weeks has a high probability of continuing to trend upwards tomorrow. The range of price combinations is skewed in an upwards direction. A stock that has been trending upwards for 3 days has a lower probability of this trend continuing.

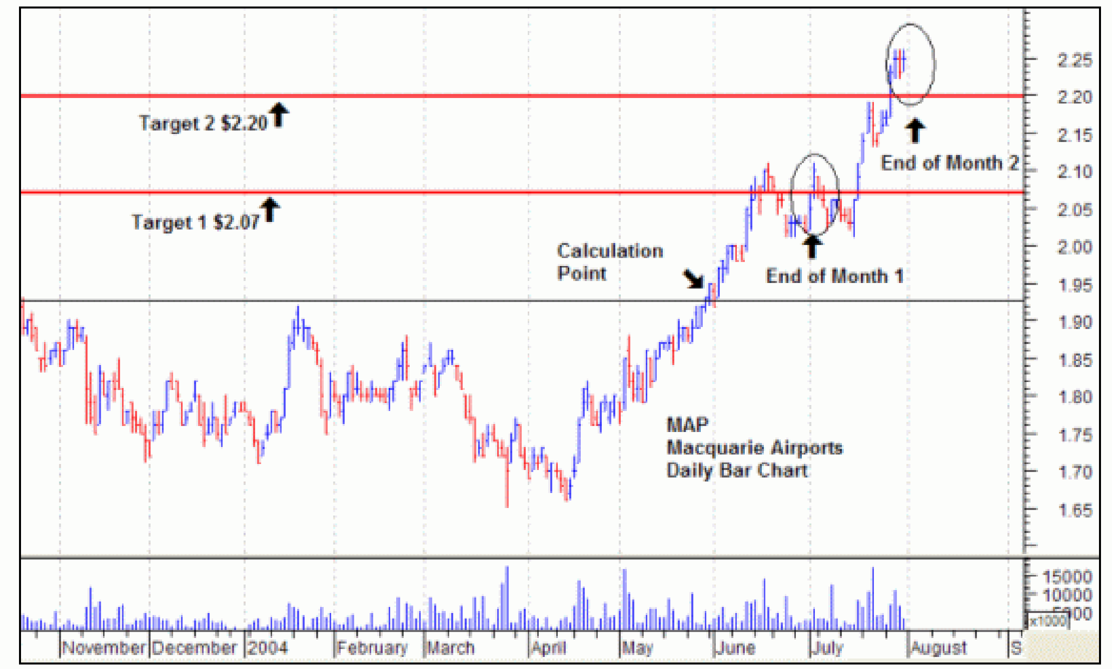
The price of a stock today is not independent of the price of the stock yesterday. This is why coin toss analogies and random walk theory are so irrelevant to the market. Prices are not independent events. When you buy a stock your decision is influenced by the price that it traded at yesterday. The event – you buying a stock – is not independent of the previous event – someone else bought or sold the stock.

Successful trading recognises the odds are stacked against us, so it looks for tools to identify situations where the balance of probability is tipped in our favour. When a trade is implemented, traders are alert for changes in the balance of probability, because they know the odds are still stacked against them.

Another method of using historical data to predict targets is to use indicators that attempt to calculate how far a share price is likely to move over a given period. I sometimes use an indicator I designed based on the Average Rate of Change. The drawback with this method is it only gives regional targets and not specific targets. What I mean by this is even though it may give a figure of $2.07, the reality of this figure ever being the exact point of a turnaround is slim.

The reason for this is they are not actually targets. They are calculations that tell us how far a stock is likely to move over a certain time frame given the previous movements. For trending situations, I usually calculate this over a month, but the formula can be adjusted for shorter and longer time frames.

The chart (again showing MAP) shows the break out and we use this as the calculation point for the indicator. The indicator then works out the likely average movement over one month and two months and projects these lines forward on the chart. The figure we used for calculation purposes was the high at $1.97. The lower red line on the chart at $2.07 shows the estimated target after one month and the second red line (top) shows the target for two months.



We can see this nice chart played along with me and by the end of month 1 the prices were oscillating around the mark at $2.07. By the time the second month came around prices had gotten above the second line and hit $2.25. The region of $2.20 was accurate. We can see the average movement over this period however has been stronger than expected when we calculated the line. This is Bullish behaviour. I personally only use the initial target and re-calculate the lines at the end of each period (in this case month). A second major issue with this method is that it assumes that prices will go up. This is why recalculating the lines at the end of the month or period is helpful.

This chart shows the target for the second month when calculated at the end of the first month. Note it has not changed greatly in this stock and again was reasonably accurate as a region. The formula for this indicator is contained at the end of the article.

Other traders have similar formulas and I'd say it is where I got the idea from originally. The ATR could also be used as well as a number of other calculations. The truth is, however, most, like mine, will be too inaccurate to use as an exit target. I usually use this method with a spreadsheet. I then work out my desired risk reward and combine the information to see how long a target may take to be hit.

There are other indicators that could be used for the same purpose of predicting limits into the future, such as speed resistance lines, Andrew's Pitchfork Method, Fibonacci & Gann Fans, as well as the simple old trendline or trend channel. These methods do not predict targets so much as give estimates of price behaviour over time. These should be used with caution and a deep understanding needs to be achieved. They are not simple purely because they can be subjective. Trying to learn the complexities of these methods takes a lot of patience and time, as they seem very unreliable (at least to me).

Fundamental Analysis

I know this newsletter is not involved directly in using fundamental analysis; however, I also do not think it would be an unbiased article if I did not at least briefly mention the possible use of this tool. I have put it last so and I promise it will be very brief & painless.

Fundamental analysis drives the majority of the market and these analysts make their decisions by judging the future value of a company. If prices reach the levels they are expecting, what is stopping them from selling at this point? If large numbers of stocks are being sold, prices tend to at least stall.

This target can come from research reports or a comparison of financial figures. Recently I had a target for the oil price of $55.00 a barrel. I had read and heard a number of analysts mention $55.00 and I felt it would be accurate as a self fulfilling prophecy if for no other reason. It turned out to be reasonably accurate, and it was not a surprise to me that oil fell back from these levels. The same analysts would have been recommending to funds and other large players to be selling at this price before I heard the information.

Using fundamental ratios could also be used to set price targets. As an example, people may set a target based on the % Yield a stock will offer at a given price. This may be an acceptable strategy, as many people are buying certain stocks purely for the yield. Should prices rise and the % yield figure becomes too low, fewer buyers enter the market. The use of fundamental ratios is beyond the scope of this article and the newsletter. I personally do not use this method, but I do acknowledge that it is a valid method that could be used with technical analysis to define targets.

Indicator Details

The indicator I used in this article is one I designed and called “ROC Prediction”. Basically, I have called it this as it uses the ROC to make a prediction. I used the word prediction in the title to remind me that it is a prediction and these by nature are often inaccurate. Please do not think this indicator will always work as well as I have shown it to in this article.

Metastock users can download the indicator from my website listed at the end, or use the formula:

Name: **JM - ROC Prediction**

```
I3:=Input("Starting Price",0.01,1000,1.00);
I1:=Input("# Periods in ROC",1,1000,30);
I2:=Input("# Periods in Average",1,1000,250);
V1:=ROC(C,I1,%);
V2:= Mov(V1,I2,S);
V4:=(100+V2)/100;
M1:=LastValue(I3*V4);
M2:=LastValue(M1*V4);
M1;M2;
```

For more information and variations on this formula please check out the relevant material at http://www.StarTraderReport.com or contact me by email at Jason@StarTraderReport.com .

TREND TRADING PBG

By Scott Blair

SUBJECT SUMMARY
TRADE MANAGEMENT(3)

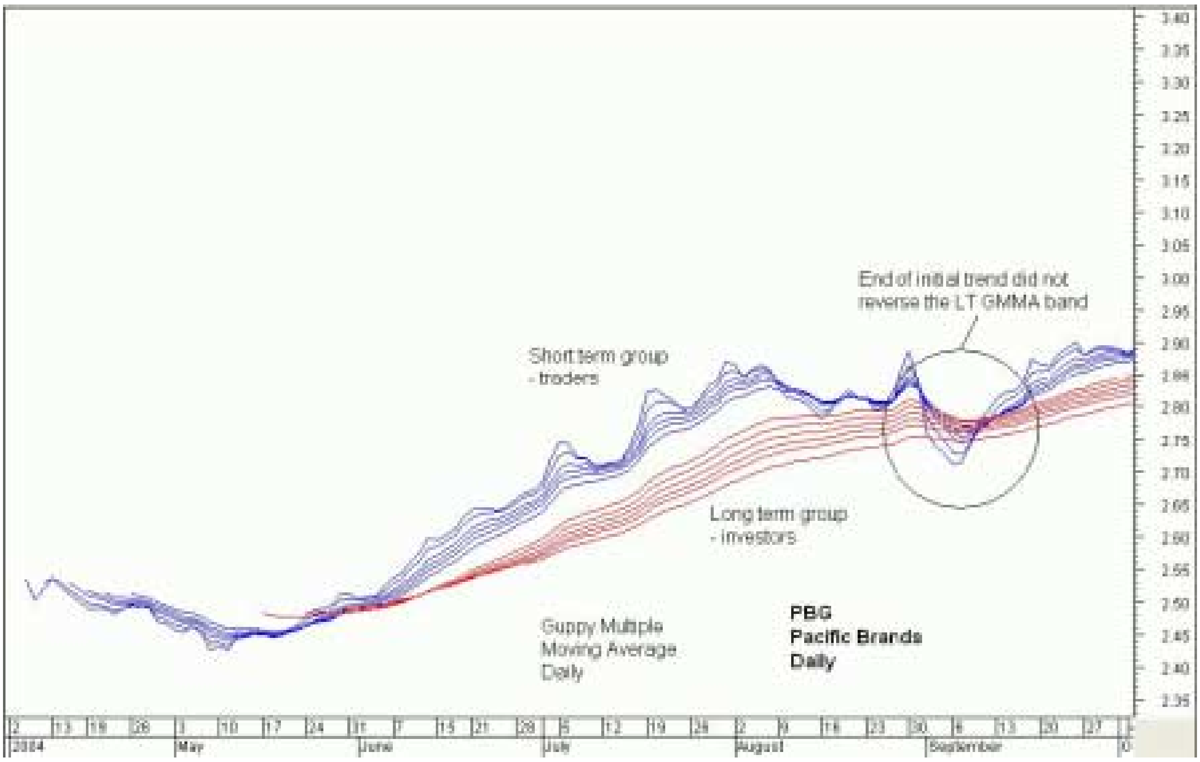
Trades have multiple exit conditions. On entry, the first exit conditions are based on the stop loss. This is designed to minimise loss should our entry be inappropriate. Once the trade starts to show a profit, our exit conditions focus on preserving that profit. We use a trailing stop loss to monitor this. A close below this level gets us out, protecting some, but not all of the profits possible from the trade. Sometimes an interim profit level is set, particularly if we expect prices to pause briefly at a level before moving on. If the move fails to develop, the pause allows us to collect some profits. The final exit condition is based on the initial profit calculations for the trade. This is the best outcome. It is also based on specific indicator signals decided upon before the trade is entered.

PBG (Pacific Brands Limited) was selected as a trend trade based on a simple MetaStock exploration that searches for all stocks with a positive long term GMMA band. The longer list of potentials is narrowed down to a handful of prime candidates based on a brief visual inspection of each chart.

A number of bullish signals make PBG stand out as a strong candidate. Price action has consolidated after a roughly 3 month, well defined, initial uptrend, and recovered steadily after a negative penetration of the long term GMMA band. The trend line is adjusted based on this new significant low to provide the context for a possible longer term trend. The crowding of price action over the past two weeks around the $2.90 resistance level while the long term GMMA band continues to rise and expand slightly indicates buying pressure that may push through the resistance area and continue the upward trend.

An entry is taken at $2.88 and the trade is managed using a combination of trendline and 3 day count back line. Entry is on a slight price pullback but still above the CBL based on the high of the most recent short term uptrend. Conservative traders could choose to wait for a clear penetration of the resistance with a close above the high of $2.93.

A protect capital stop is implemented using a CBL as a warning sign and a close below the adjusted trendline as a clear exit signal. The CBL point at $2.85 is very tight and inappropriate as a clear exit signal in the context of this trend trade. A close below the CBL would clearly indicate an end to the previous, short term uptrend that bounced off the trend line but that is not the trend we are trying to ride. The trend we are trading is defined by price action that penetrated the long term GMMA and recovered without turning the long term GMMA negative. We don't want to be shaken out



prematurely so our strategy allows for price action to bounce off the trend line again without risking too much capital if the trend line does not hold. Price has closed very near the trendline twice so a close below this signals a trend failure. A safety net is built by taking an appropriate position size that risks less than 2% of our total trading capital if the clear exit signal is triggered.

Once price action exceeds the break even point, the exit strategy is adjusted from capital protection to profit protection. As prices continue to rise and pull further away from the trend line, tighter stops become more appropriate. A fall back to the trend line would allow erosion of too much profit and, if the trend line did not provide support, a winning trade could turn sour. We now use a close below the CBL as an exit signal.

The wide ranging day on December 7 looks frightening, but does not close below the CBL – it is a warning, but no exit signal is generated. End of day traders who monitor intraday prices would need a great deal of discipline to stick with the trading plan in this situation, but assessment after the market closes shows this price action is consistent with previous wide ranging days on the down side in the trend. However, the warning cannot not be ignored, so price action is monitored closely the following day to achieve the best exit possible if necessary.

Prices open lower and below the CBL providing further confirmation of weakness and do not recover through the day, so an exit is managed at $3.21 for an 11% profit on the trade.

The PBG trend has now twice displayed behaviour of a clear intermediate trend followed by a retreat to the longer term trendline. PBG stays on the watch list for possible re-entry to catch this behaviour again if price action provides bullish signals as it approaches the longer term trendline.

This is a description of an actual trade. I no longer hold shares in PBG.

DEVELOPING DIVIDEND STRATEGIES FOR CURRENT MARKETS - PART 2

By Daryl Guppy

TRADING METHODS

DIVIDEND DATES

When dealing with dividends, there are four periods of interest to traders. The first is the announcement of the dividend amount. Prices often rise in expectation of the dividend announcement. If the dividend is below expectations then the price tends to fall very rapidly.

The second period is called the cum-dividend period. Although this really extends from the period starting as soon as the stock goes ex-dividend, other traders become aware of their entitlement to a dividend when the half yearly results are released. This means that all people who hold the shares are entitled to receive the dividend. This tends to keep the price up, because a $10.00 share with a $1.00 dividend is really 'worth' at least $11.00 ($10.00 plus $1.00 dividend). Any shares sold in this cum-dividend period transfers the right to receive the dividend to the new share holder. The old shareholder loses the right to collect the dividend.

The third period is when the shares go ex-dividend. From this time on all shares sold do not carry an entitlement to receive the current dividend. The old shareholder retains the right to collect the dividend, even though he has sold the shares, while the new shareholder does not have a right to collect the dividend. Using the example above, we would expect the share price to decline by the value of the 'lost' dividend. i.e. fall from $11.00 to $10.00.

The fourth period is the book closing date. This simply means that this is the final date by which all share transaction during the cum-dividend period should be registered. The objective is to make sure that every one who is entitled to the dividend receives it. This book closing date has no impact on the share price.

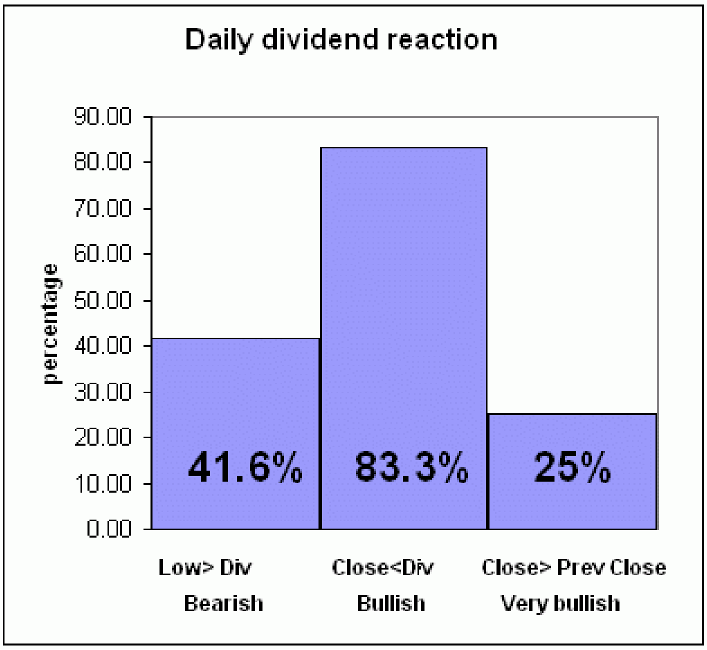
Over the next month, the Australian market moves into reporting season. The period for reporting has been reduced and many analysts are complaining that they will not have time to complete timely analysis. They worry that an 'ill-informed' market will overreact to company report releases. The immediate impact of this for traders is twofold. First, the overreaction may provide a trading opportunity if the price dip is temporary. These opportunities are best exploited using leveraged instruments such as warrants, options or CFD's. The second opportunity is a longer term resumption of the uptrend after this panic driven dip.

Last week we indicated how traders can anticipate and evaluate the most effective trading strategies for this period. Our analysis has three components.

- An understanding of the emotional content of dividend behaviour (last week's notes).
- A framework that compares both the daily reaction to ex-dividend days, and the reaction a week later (last week's notes).
- A statistical summary of the current reactions to ex-dividend trading and the development of appropriate strategies on an intraday and weekly basis.

Dividends for Bullish or Bearish Markets

Using this analysis framework we have explored these statistical relationships amongst the 24 stocks that have gone ex-dividend in the past 6 weeks. The small selection size does have an impact on the reliability of the results. It may turn out that the broad market ex-dividend behaviour is not a good guide to the way the market reacts to profit warnings and down grades in the coming reporting season. We will keep a record of this developing behaviour for comparison as the short reporting season proceeds. However, this analysis provides a logical framework for understanding the behaviour of the market in a broad sense. In a broad bullish market, profit downgrades are not a problem. In a market that is worried about the sustainability of the bull run, profit downgrades may cause a greater incidence of temporary emotional overreactions. In a bear market, a dividend cut is a signal to take profits and run quickly. This broad framework helps traders to fine tune strategies for individual stocks.



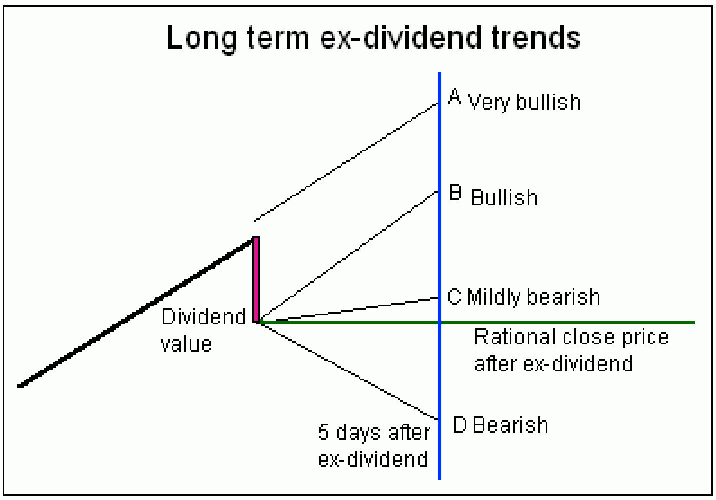
The ex-dividend analysis suggests that we remain in a strong bullish market. In 58.4% of recent cases the intraday low when a stock went ex-dividend was still higher than the rational ex-dividend price. Price dips did occur, but they did not exceed the value of the dividend. There are still 41.6% of cases where the intraday low was larger than the value of the dividend, but generally the market has a more bullish outlook.

This is confirmed when we examine the relationship of the ex-dividend close to the rational ex-dividend price. The theory suggests that the ex-dividend close ought to be the exact value as the previous close, less the value of the dividend. This did not happen in 83% of cases. Instead the close was above the rational ex-dividend price. This is the equivalent to the light blue bar on the previous daily dividend diagram. In 25% of cases the ex-dividend close was above the previous day's close. This is evidence of a very strong bullish market.

(It would be particularly useful to compare these relationships with a previous period so any change can be tracked. This will help to determine if bullishness is increasing or decreasing. We are undertaking this research and will bring you the results in coming newsletters.)

On this information traders may develop the following strategies.

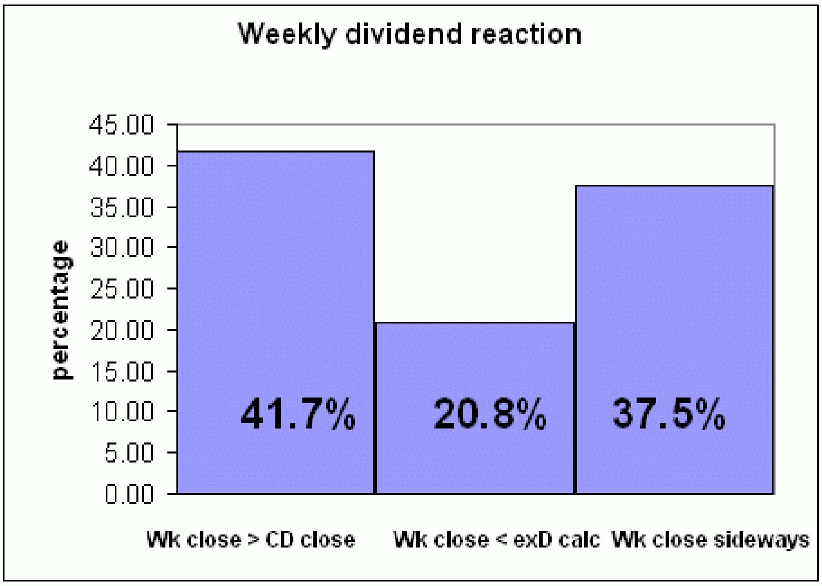
- Buy the intraday ex-dividend low because there is a high probability that price will close higher on the day, or even higher than the previous close. Leverage makes this a profitable strategy.
- Selling on the day prior to the stock going ex-dividend with the intention of re-entering the next day is a successful strategy in all but 25% of cases. However, the advantage is reduced as prices generally remain above the rational ex-dividend value.
- Traders who hold the stock prior to ex-dividend do not need to panic at a price dip below the rational ex-dividend price as the price is most likely to recover by the close.



Using this analysis as a guide, traders can watch for replication of this behaviour as profit and earnings announcements are made. Although ex-dividend behaviour is not directly comparable to behaviour relating to company announcements, we suspect there is a broad correlation.

Intraday reactions tend to be more greatly influenced by emotional behaviour. When deciding if we should react to this we need to consider the longer term impact on price development. We do this by comparing the close 5 days after the stock goes ex-dividend with the close on the day before the stock went ex-dividend. There are four outcomes as shown in the diagram.

- The most bullish result is when the trend continues after ex-dividend without any interruption. The ex-dividend prices close above the previous day's close and the trend powers on. We identify this by tracking those stocks that closed higher 5 days after ex-dividend than the close of the day prior to ex-dividend.
- The usual bullish result is for prices to drop by about the value of the dividend and for the trend to continue in the same way, but offset by the value of the dividend. We track these by stocks that close lower after 5 days than the close on the day prior to going ex-dividend.
- A mildly bearish result is when prices drift sideways after the ex-dividend day. These results are included in the usual bullish results as they are difficult to extract separately.
- The most bearish results are when prices close lower than the rational ex-dividend price after 5 days of trading.



Recent reactions are not strongly bullish. Currently 41.6% of stocks close higher after one week of trading than the close price on the day prior to going ex-dividend. This tells us that most stocks ***do not*** continue to trend strongly upwards. Traders who hold onto these stocks enjoy both the dividend value and continued capital appreciation.

Many stocks either move in an offset parallel trend, or sideways in 37.5% of examples. This is still a mildly bullish outcome. Traders who hold onto these stocks may recover the value of the dividend and enjoy capital growth. After a week of trading they have lost some capital growth, and the price rise has not yet fully compensated for the value of the dividend.

Changes in this value between periods, is the first warning of a weakening market. The bear delivers a warning with stocks that are trading lower than the rational ex-dividend price a week after the stock goes ex-dividend. Currently this happened in 20.8% of examples. This suggests that a bear attack is an unlikely reaction, but there is still a reasonable prospect that once prices have fallen below the rational ex-dividend value, that the previous uptrend has ended. Traders who hold these stocks lose both the value of the dividend and the capital value.

This analysis is a starting point, but it suggests that stocks that dip on profit warnings and recover during the day have a higher probability of continuing to trend upwards. This is true if the ex-dividend relationship carries across to the reporting season reactions. In the coming weeks we will watch the early reactions to company reports. If we find these broad market ex-dividend relationships continue to hold, then we will illustrate some intraday and longer term trend trading strategies based on this analysis.

Details of earnings announcements dates in previous years are available from http://www.justdata.com.au/Training/index.htm Follow the dividends link. This provides a guide to the likely date of announcements.

The actual date of announcements is available from http://www.egoli.com.au/clientservices/documents/generaldocuments/Reporting_Season_1H_2005_date_egoli.pdf

READERS' QUESTIONS – KANGAROO TAIL TRADING

By Rod Harper

TRADING METHODS

THE KANGAROO TAIL

The kangaroo tail is an intraday pattern of trading. It is triggered by a minor price fall that accelerates as stop loss orders are triggered. The pattern develops if the stop loss order structure sets a lower than market execution price. This means the stop may be triggered at $1.00, but the sell order is active within a buffer set 10% or 15% below the trigger price. A stock with multiple stop loss orders based on this buffer execution may experience a cascading effect. If there are not many orders in the bid stack, there is a high likelihood that traders who may not have specified a lower limit, or who are working with a 15% in-built buffer limit, may be sold down like a pack of falling dominos as their system sells through all levels queued to buy down to -15% below current levels.

Astute traders move into the market and buy the rebound, lifting prices rapidly back to their previous levels. This rebound creates the kangaroo tail. It is an intraday trading opportunity, but a hazard for those who want to use stop loss points as an effective management tool.

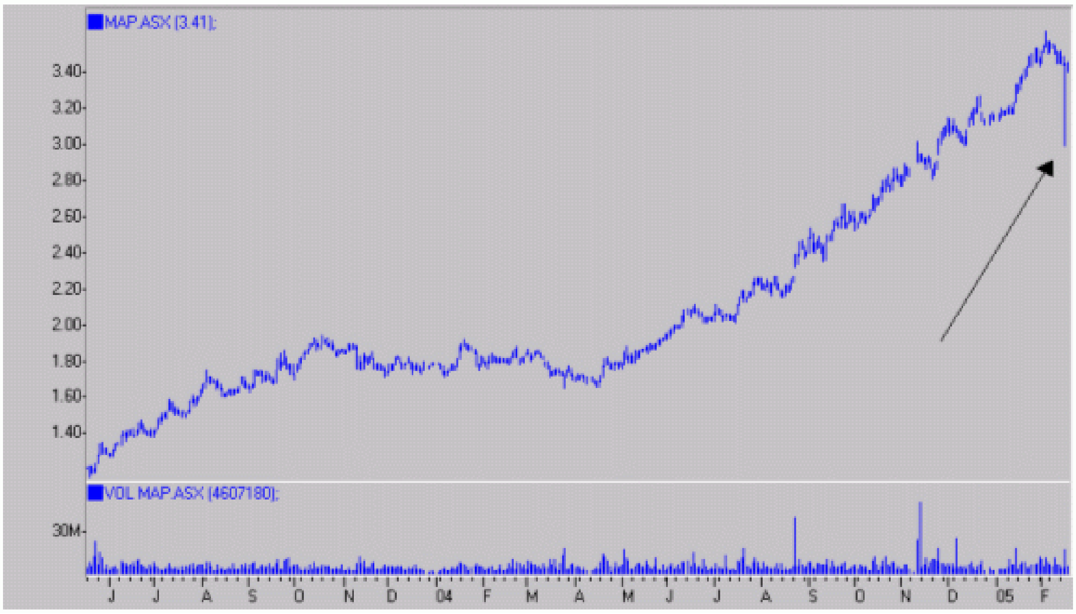
Kangaroo Tails, caused from online brokers using automated Stop-Loss systems, have shown up in a number of stocks this week.

It was about twelve months ago when Commsec and E*Trade first developed their automated systems that could accept Stop-Loss orders which would sell investors' stock into the market as soon as their required Stop-loss price was reached. The major problem with these automated systems is that they are very fast. They are so fast that one Stop-Loss order can trigger another Stop-Loss in the same stock, and if there isn't sufficient buying in the market, the stocks can fall rapidly within seconds.

One of the first examples of this was in Caltex on 11th December 2003. Its share price opened at $4.56 on the day, fell as low as $3.75 on automated Stop-Loss selling and recovered to close at $4.32.

Since then we have had a number of examples including: Record Investment, Colorado Group, McPherson's Limited, Fleetwood, Great Southern Plantations, GUD, ARB Corporation, Redflex Holdings, and many more. The stocks most vulnerable to these sell-offs tend to be high-turnover, outperforming blue-chips, where many investors have placed Stop-Losses to protected their gains.

This week we saw two major stocks affected by automated Stop-Loss selling; Macquarie Airports on Wednesday, and Great Southern Plantations on Thursday. Macquarie Airports was sold down, mainly by Commsec and their automated system, from $3.40 to $2.99 between 11:06am and 11:07am. That is almost 15% of its value wiped out in less than sixty seconds. A staggering $750 Million was wiped off its market capitalisation during this time. The bargain hunters quickly swooped on it and brought the price back up to the level where the Stop-Loss selling began.



It appears to be taking some time for investors to realise that these Automated Stop-Loss facilities do not work. The alternative is Operator-Assisted Stop Loss facilities, such as that offered by DataTech Financial Services, where a trained operator checks the market before executing. The brokerage is slightly higher than that of the automated systems, but there is no point trying to save $10 in brokerage on a trade that will end up costing you thousands of dollars in poor execution.

My condolences to the Commsec client who arrived home on Wednesday to find they had been sold out of Macquarie Airports at $2.99.

Rod Harper is a Senior Private Client Advisor at DataTech Financial Services and may be contacted on 02 9268 0250 or rharper@datatech.net.au .

CHART TECHNIQUE BRIEFS - HIB

By Petra Rak

INDICATOR REVISION

EQUILATERAL TRIANGLES

Some trends are ambiguous. Prices do make higher lows, setting the conditions for placing an uptrend line. Sometimes the price activity on the day also makes a lower high. More often, prices work their way above the uptrend line, but fail to make new highs. This trend meets the conditions for placing a downtrend line. Both lines are valid and define an equilateral triangle. The market is uncertain as to the correct pricing for the stock (this is not the same as valuation). Both sellers and buyers revise their valuations over time, but in opposite directions. Breakouts tend to be driven by external factors, hitching a ride with broader market conditions.

The daily chart of HIB shows a relatively young uptrend, which commenced in November and has progressed in a step-like fashion through rallies separated by two equilateral triangles. Prices moved from low, at $0.40 in November, to a high at $1.80, reached in late January. Since this point, HIB has retreated from this high, though prices are still some way above the upward straight edge trendline. The retreat has taken the form of an equilateral triangle, which is now reaching the last third of its development.

A few general notes on equilateral triangles: The pattern indicates indecision or uncertainty and commonly forms when news is expected, but buyers and sellers are balanced and uncertain whether upside or downside movement is more likely. Targets are set by projecting the height of the triangle (here $1.80 - $1.40 =$0.40) upward from the point of breakout, such that as the triangle develops, the triangle target moves downward parallel to the slope of the upper triangle boundary. The likelihood of achieving the target is lower than in up sloping triangles, and equilateral triangles may break either way.

UP CONDITIONS

These general pattern features have to be amended in HIB due to the price history, in which an equilateral triangle has previously developed as part of the overall uptrend. This history, together with a valid existing uptrend, indicates a higher than usual probability of both an upside breakout and ability to reach the upside target around $2.05.

Trend continuation and associated opportunities appear likely at this stage: the GMMAs indicate a strong trend, with very good support signaled by well spread and parallel long term GMMAs. This support continued throughout the development of both equilateral triangles, reinforcing trend strength (typically, equilateral triangles, as patterns of uncertainty, are accompanied by uncertainty in the GMMAs signaled by narrowing and flattening of both MMA groups).

DOWN CONDITIONS

A downside triangle breakout through the CBL and the trend line, or sideways movement through the tip of the triangle and the trend line, will signal the end of the uptrend. In this case, the triangle pattern can be used to set a potential downside target around $1.42, or below this at support/resistance levels around $1.30 and $1.15.

Possible continued upside movement and potential new opportunities will be signaled by the development of a strong support to any retreat and a CBL breakout.

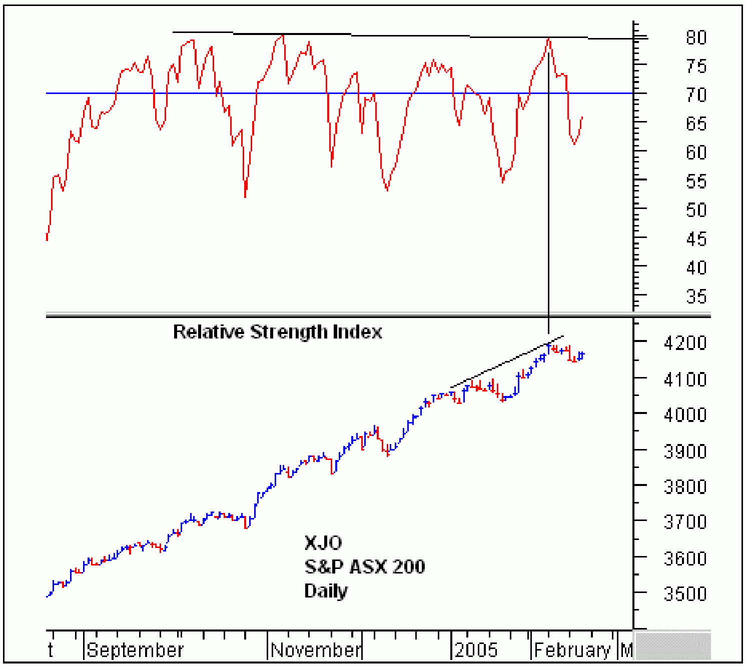
NEWSLETTER OUTLOOK – SUPPORT ON BAND

By Daryl Guppy

Updated notes are shown in blue.

The trading band discussed in previous weeks has acted as a support level around 4150. The dominant concern remains how far any pullback can go before it signals an end of the trend. Although traders continue to ride the rising trend, they are increasingly alert for index pullbacks. Hence the concentration of support levels and trend definition. Shorter term trades continue to help manage the risk of a sharp market decline, no matter how temporary.

We plot a minor support level at 4090.



The RSI divergence pattern that has been in place for several months remains a technical concern. The XJO rally does not invalidate the divergence pattern until the RSI makes a new peak. RSI values need to peak above 80 for the divergence to be invalidated. This failed to happen.

This remains a technical knockout and this indicator suggests caution. Traders remain alert for an interruption to the trend rather than a collapse of the trend.

This is 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.

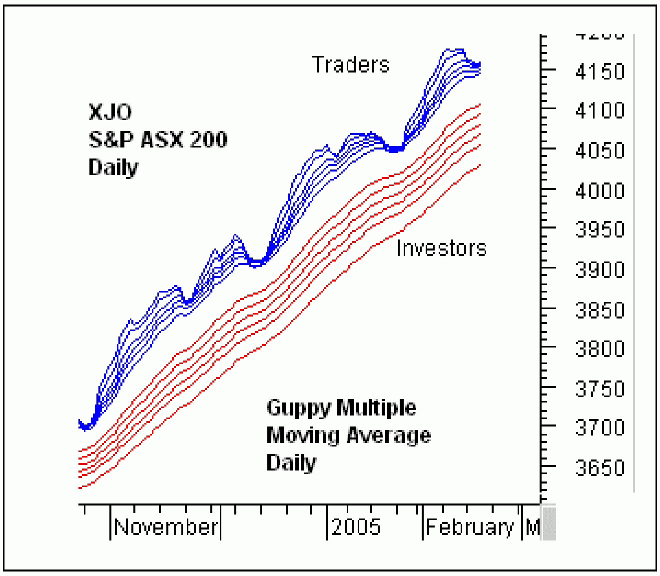
The ultimate support level is the long term uptrend, shown as the thick red line. **The value of this line has exceeded the value of support line 2. This is a significant bullish feature as it confirms multiple levels of support under any falling market.**

For bulls, the dominant concern is the ability of the market to rebound from the current up trend line shown in black. This concern has been eased with the rebound this week. For bears, the dominant

feature is the influence of support at level 2, and later at the 3820 level. Some traders will use a fall below the upper trend line as a signal to go short in anticipation of a sharp January sell off.

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. The retreat patterns discussed above remain consistent with this strong trend. 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. 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.



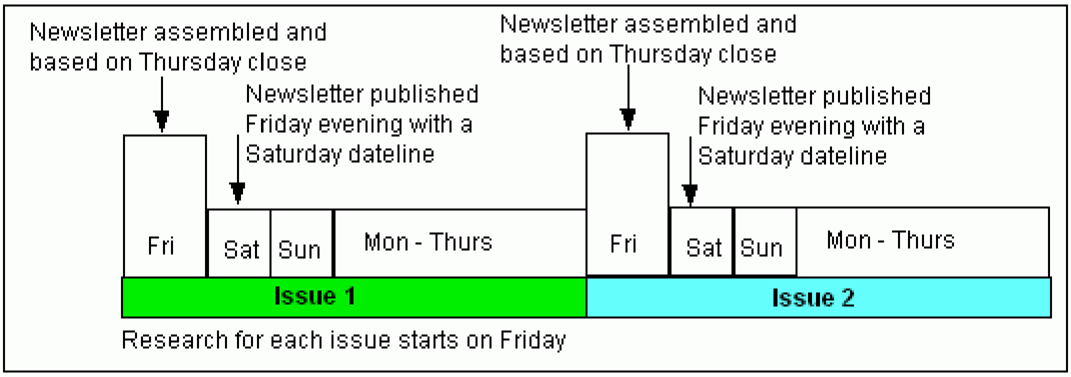
The indicator confirms that a substantial index retreat remains consistent with the long term underlying trend. The GMMA is not a stand alone indicator. Our preference is to use it in conjunction with other indicator tools. These include the support and resistance levels, and the trendlines discussed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

PUBLICATION SCHEDULES

We do not work on Saturdays and this simple decision has implications for the newsletter publication schedule. Each week material for the newsletter is researched and written. It takes five to seven days to write. It is not put together in a few hours after the market close and prior to distribution on Friday evening. Some notes are compiled over several days and detail the exact steps we have used in locating particular trading opportunities. We try to keep many of the notes as current as possible – but we don't work on Saturdays.



The newsletter takes one day to compile and assemble. We do this on Friday so we set the cut off point for market data on Thursday evening. Whatever happens on Friday is not discussed in the newsletter until the following week's issue. The dateline on the newsletter is the Saturday following the Friday compilation. However, as a service to our subscribers, we send the newsletter out on Friday evening for collection Saturday morning.

This publication schedule creates a lag and this has advantages and disadvantages. The two main advantages are:

- We do not have to work Saturday.
- The lag helps ensure that information in the newsletter does not constitute investment advice and ensures that articles are educational in nature.

There are several disadvantages of this lag. They include:

- We get to watch case study trades discussed in the newsletter as they develop on Friday. There are some instances where there would be a great advantage in using Friday's information to retrospectively exit the trade on Thursday, because prices collapse on Friday as we put the newsletter together. We do not yield to this temptation, and the newsletter includes a discussion of the disadvantaged exit in the following week's issue.
- We get to watch case study trades discussed in the newsletter as they develop on Friday. There are some instances where there would be a great advantage in using Friday's information to retrospectively enter the trade on Thursday, because prices race up as we put the newsletter together. This situation we handle slightly differently because readers are always more suspicious of profits than they are of losses.

  If the stock is subject to a brief article prepared during the week, we simply drop it from the newsletter. That's right; we drop it because we prefer to avoid the suggestion that the trade was picked retrospectively.

  If the stock has been selected after a selection process that is discussed across several articles appearing in the newsletter, we face a more difficult decision simply because thousands of words were written between Friday and Thursday about this technique. Where possible, we replace the stock with another that also passes the selection tests being discussed.

  If this is truly not possible, - and sometimes there is only one candidate – we stay with the selected example. And we wear the flak from a small number of readers who suggest the trade has been picked retrospectively. (Interestingly, we do not get the flak if the trade subsequently fails. Apparently only profits are suspicious)
- In certain market conditions our focus is on short term intraday and overnight, and 2 to 3 day techniques. It is quite difficult to find a case study trade that starts on Thursday and ends on Friday. And even if it does, we are in a bind as some readers still suggest the trade is selected retrospectively. Again, we do not hear this questions when the selected trade turns in a loss.

There is no solution to this problem – other than to work on Saturdays. On balance we are happy to live with the occasional question regarding retrospectivity. They often come from people who are more interested in stock tips than in education. This publication lag also ensures that the focus of the newsletter is on education and not on investment advice. The notional case study portfolio is used as a way to measure the effectiveness of the trading techniques discussed. Not all of them work, and not all of them work brilliantly. Many take just a small part of a long term trend. Use the articles and the case studies to learn about the market. Understand the losers and well as the winners and the newsletter will deliver its full educational value despite the lag in publication dates after the market close.

WELCOME DESPINA

We welcome Despina to the staff in our Australian office. Her proofing skills have had a favourable impact on the newsletter. She is responsible for the assembly and layout of the newsletter.

GUPPYTRADERS TOOL BOX – WE NO LONGER WORK WITH MARKET ANALYST ON TOOL DEVELOPMENT

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.

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. (Aiming for March release)

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.

In March Guppytraders.com will release a GTE Toolbox that can be used with Metastock data. Pricing will be under $100. We will also release a full GTE Charting package. We will offer an attractive upgrade path to those who wish to change 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 2005.**

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.

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.

PLEASE *DO NOT* USE THIS EMAIL ADDRESS TO CONTACT US

Our solution to separating virus mails masquerading as "postmaster' messages from genuine "fail to deliver" messages we direct all bounce back email to a <suport@guppy04.webzon" address. This is only used for dealing with bounce backs. This is our catch basket for junk mail. It is checked and emptied once a week. Please do not use this to contact us about support or subscription issues.

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	$ 41.80	$ 22,990
		Newsletter date		11-Sep	Open Profit	2,975.50
				dividend Jan 6		464.48
					profit	3,439.98
MA trend manage					Percentage	17.19

Stock	Price	Qty	Pur Value	Close	Cur Val
WESWMB	$0.455	22,000	$ 10,010	$ 0.3850	$ 8,470
		Newsletter date	12-Feb	Open Profit	-1,540.00
Earnings rebound				Percentage	-15.38

Stock	Price	Qty	Pur Value	Close	Cur Val
MIG	$3.600	5,600	$ 20,160	$ 3.6300	$ 20,328
		Newsletter date	22-Jan	Open Profit	168.00
Trend trade				Percentage	0.83

SUMMARY MONEY MANAGEMENT

Sell WESWMB for a loss of $1,540 or 15.38%

Overall profit to date since July 1, 2004 = $57,054 or 57.1% 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.

OFFICES; Head Office, 22 Hibernia Crescent, Brinkin, **Darwin, Australia**, Level 36, Menara Citibank, 165 Jalan Ampang, **Kuala Lumpur, Malaysia**, Penthouse Level, Suntec Tower Three, 8 Temasek Boulevard, **Singapore,** RmB 30G Majestic Garden, No 6 Middle of Beisihuan Road, **Beijing, China**