Active Trading

Online Manual

by Alan Hull

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Contents.......

Introduction

The Active Trading strategy uses a weight of evidence approach. This simply means that we're looking at 'evidence' from a range of different indicators and sources from which to draw our conclusion(s). In fact Active Trading takes trend trading to the extreme as I'm looking for trends within trends within trends within trends. That's four layers of trends to be precise!

I'm looking for a rising market, then a rising sector, then a rising share and finally, a rising week. Now I'm going to explain each of these four layers and then in I'll introduce the tools I use to measure each one of them. The logical place to start of course is with the top layer; the state of the entire Australian Stockmarket.

Rising Market Indexes

The Active Trading strategy analyses the broader market using both the All Ordinaries and the Small Ordinaries indexes. My first layer of evidence is to make sure that the broad market represented by the All Ordinaries index is rising. I then also need to make sure that the particular index that represents the small to medium capitalisation shares such as the Small Ordinaries is, is also rising.

This is my first layer of evidence…rising market indexes. The following weekly charts are examples of these two indexes, showing a time when they were both trending up together. Of course this would have been an ideal time for short term trend traders to be in the market.

Weekly Candlestick chart of the All Ordinaries index

Weekly Candlestick chart of the Small Ordinaries index

Rising Sector

The next layer is the rising sector. What I am looking for here is a sector or sectors that are rising the fastest. Thus I want to hunt for shares in the fastest rising sectors, providing they have an acceptably low level of volatility. Of course I'll employ sector risk to balance out my portfolio and make sure that I limit my total exposure to each particular sector.

This means that I will need to look at trading shares from about three or four different sectors in order to spread the risk far enough. However this shouldn't prove too much of a problem as there are a total of 22 individual GICS Industry Group Sectors to choose from. These 22 different sectors form the backdrop for my rising sector analysis and the following charts show some examples of these sectors....

**Line-on-close charts of some GICS Industry Group Sectors**

Rising Share

My third layer of evidence is that of a rising share. The shares that are going to be part of my Active Trading portfolio will firstly need to be shares that are trending upwards in the short term with low volatility. Secondly, they will also need to be rising at an acceptable rate and we'll look into this in more detail shortly.

Suffice to say that not only do we want upward trending shares, we also want them to be going up nice and quickly! Here is an example of a relatively smooth, yet rapidly upward trending share that we would consider acceptable…

Candlestick Chart of a rising share
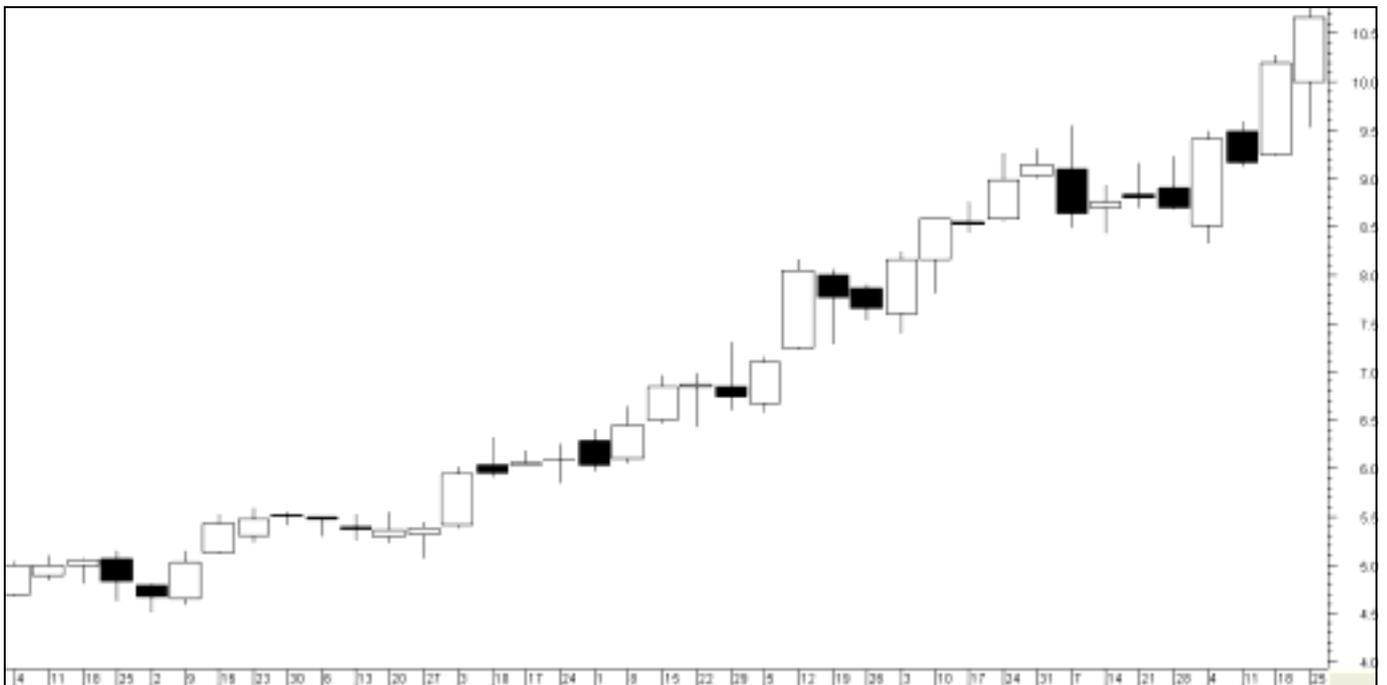
Rising Week or Upweek

This is my last layer of evidence…that of a rising week. After getting through the previous three layers and having identified a particular share or shares, I will now only enter the market when a share has been rising for at least the last week. I'm doing this because I don't want to buy a share when it is falling in the very short term.

I want a share that is showing immediate strength and so I want to witness what we call 'buyer support'. Thus, one obvious way in which buyer support is evident is when a share closes at the end of the week higher than it closed at the end of the previous week, ie. an 'upweek'. See the chart at the top of the next page.

Candlestick chart showing an upweek
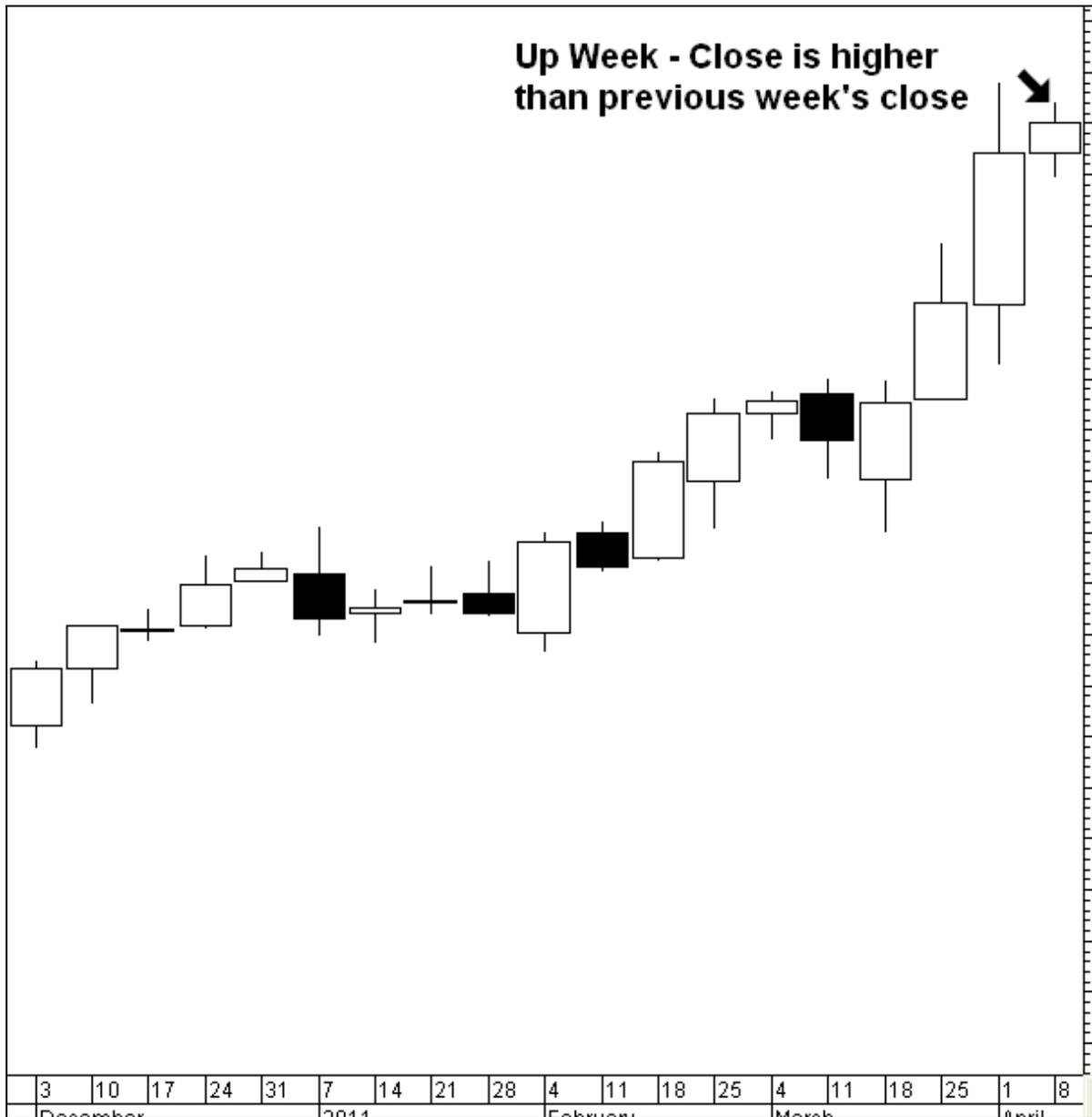
Putting this altogether and to summarise, with my Active Trading system I'm seeking :

1. a rising market as indicated by both the All Ords and Small Ords

2. a rising sector or sectors that are trending up with relatively low volatility

3. a rising share that is trending up very rapidly but with relatively low volatility

4. an upweek where the closing price is higher than the previous week's closing price

The Active Trading strategy is very much a top down approach to trading where we start off with the big picture and then work our way down from there. So there we have the four layers that form the basis of my Active Trading system. Now we'll take a look at the tools I use to assess each of these layers.

The Active Trading Toolbox

Now I'm going to explain how I measure each of the four 'trends' that make up the system. Thus, we will examine all of the tools I'm going to employ in detail, which are as follows :

Rising Indexes – we'll use moving average crossover charts, namely 10 and 30 day EMAs

Rising Sector – we'll use sector MMA Charts and my Rate of Return (RoR) indicator

Rising Share - we'll use share MMA Charts and my Rate of Return (RoR) indicator

Up Week – we'll simply analyse weekly price data to determine this condition

These are the indicators and tools I'm going to use although I'll also be introducing my Range indicator a little later on when we get to the discussion on trade management. So once again we'll start at the upper or outer most layer, being the analysis of the All Ords and Small Ords indexes.

Rising Index

What I need here is a way to determine the direction of the trend of both the All Ords and the Small Ords, the two indexes relevant to this strategy. My tool of choice is the simple yet very effective Crossover Chart and shown below are the Crossover charts for the two indexes. Note that I have turned the index itself off in each case so you can only see the two moving averages…

All Ords Crossover chart

Small Ords Crossover Chart

10 day exponential moving average (grey)
30 day exponential moving average (black)
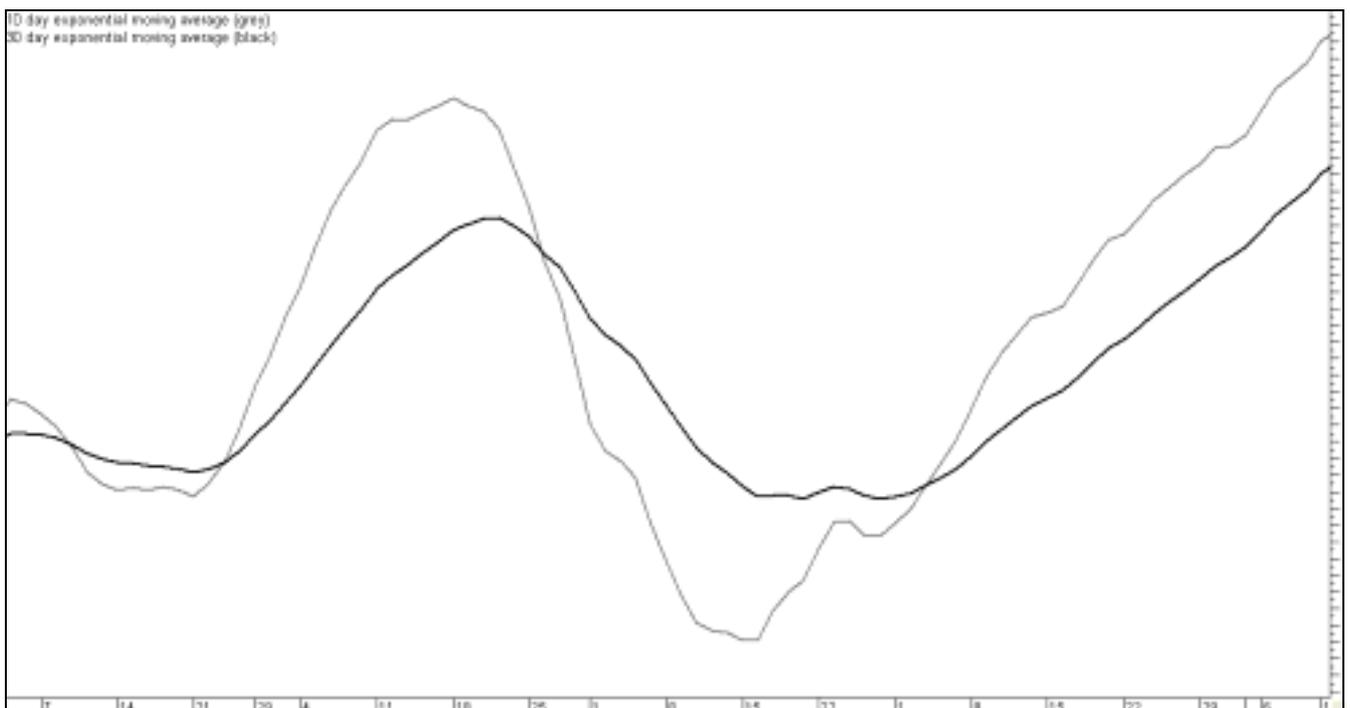
Here I'm looking at two short term moving averages applied to daily charts of the All Ords and the Small Ords. The lighter of the two lines (the fast moving average of the two) is a 10 day Exponential Moving Average (EMA) and the black line (the slower moving average) is a 30 day Exponential Moving Average.

I chose these moving averages and particular periods because I have determined through many years of trialing different combi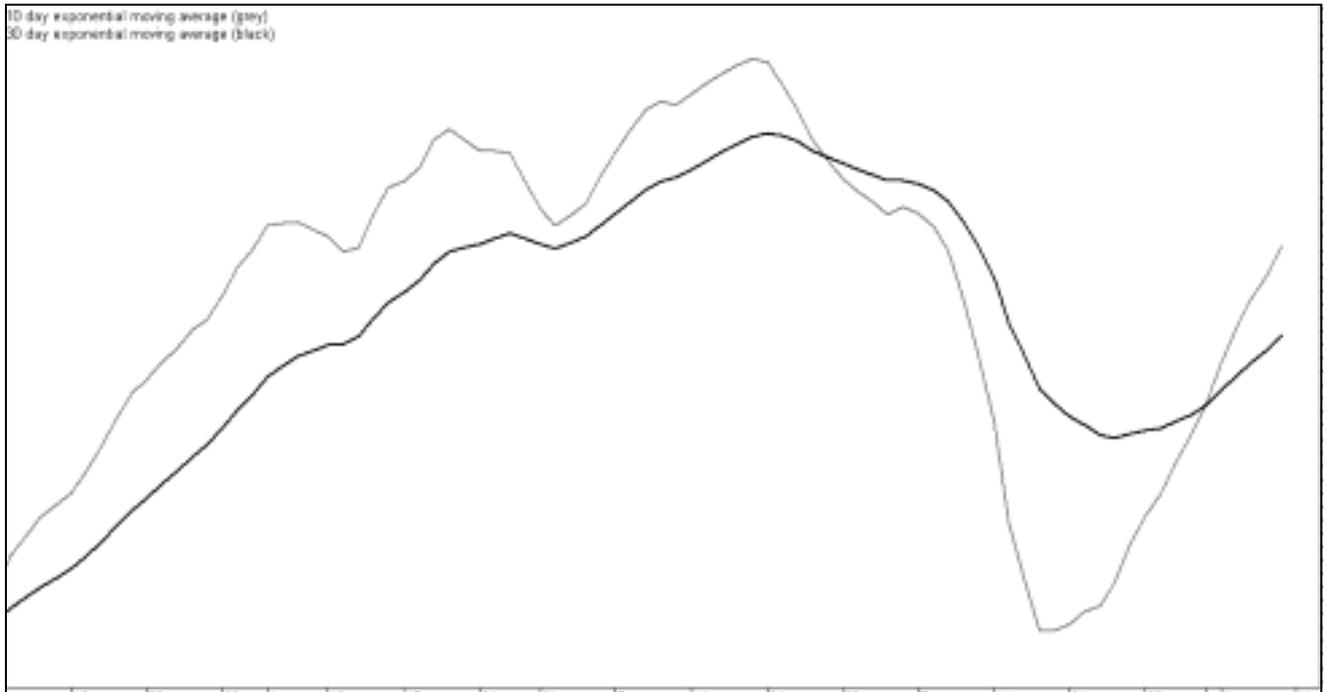nations that this is most suitable combination for assessing the direction of the Australian Stockmarket, for my given timeframe. The rules for interpreting the Cross Over Charts are VERY simple :

> *BOTH of the charts must be crossed to the upside, ie. the grey line must be above the black line at the right hand leading edge of the chart, in both cases.*

So a chart is 'crossed' in a particular direction when the grey line (the shorter of the two moving averages) is ABOVE or BELOW the black line at the right hand leading edge of the chart. So if you can see the grey line above the black line, then the chart is crossed to the upside. If the grey line is below the black line, the chart is crossed to the downside. If the two lines are sitting right on top of each other at the right hand leading edge then they are not crossed in either direction.

These charts are my starting point and so we need to be very clear on their interpretation. Although that doesn't stop us *trying* to make them say what we want them to say; one might even zoom in on the chart for a better look! Of course even if you do utilise that sort of functionality from your computer software….if it's still not crossed to the upside…then it's NOT crossed to the upside!

If I can look at BOTH charts and see a grey line above the black line and I am looking to buy shares, I know that the indicator is telling me that I have the green light for go.

This is the first stage of the system and is a vital step because if we attempt to countertrend the broad market by trading against it we will surely fail. So the crossover charts provide us with clear unambiguous signals. However, in the next stage we will see some discretion start to come into the trading process.

Rising Sector

To help pick which sectors I'm going to look at, I actually use two tools. The first tool is an MMA chart which will let me pick sectors with suitable trends. The second tool is a Rate of Return indicator or RoR. This will show me which of the sectors are rising or falling at the fastest rates. Let's look at these two tools one at a time.

Multiple Moving Averages

Multiple moving averages, as the name implies, are a series of moving averages all drawn on the same chart with different but usually evenly spaced periods. And when creating an MMA chart it is a common practice to hide the underlying financial instrument as I have done in the following chart (ie. the actual price activity isn't displayed, only the MMAs)…

MMA chart created using 10 evenly spaced periods
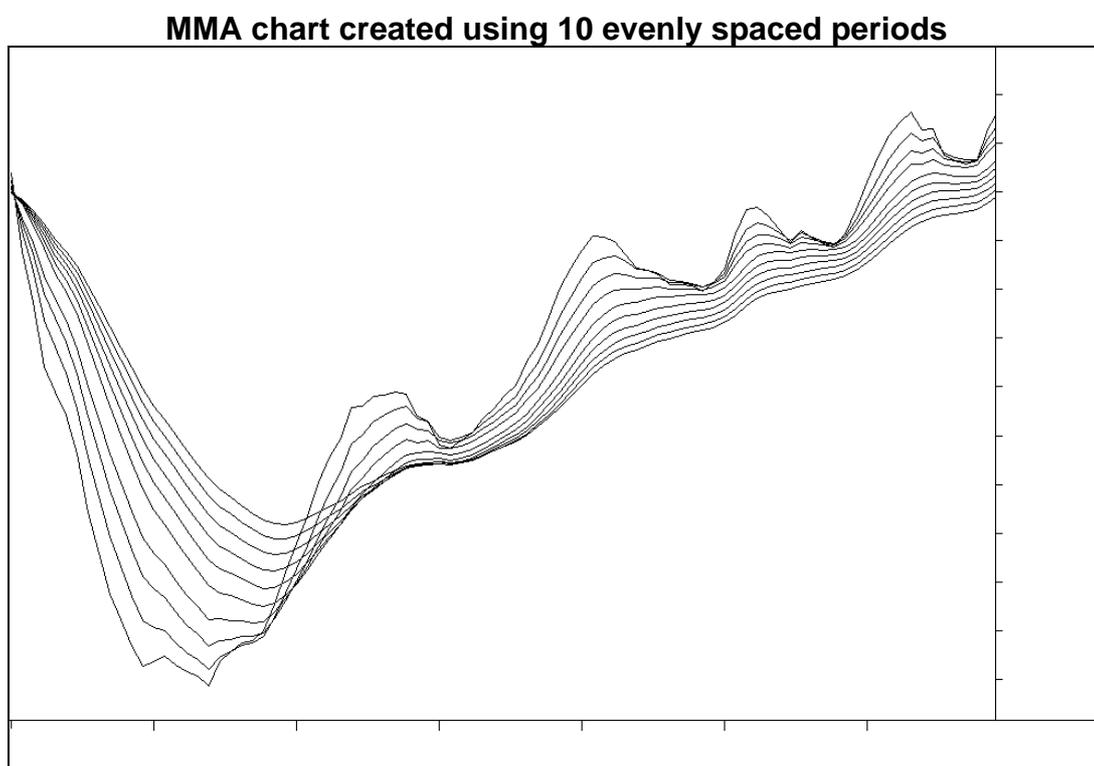
As you can see by placing a series of moving averages on the same chart with evenly spaced period values, it forms a ribbon that filters out the short term price movements but highlights the underlying trend. This technique was adopted several decades ago by Daryl Guppy, an internationally renowned share trader and best selling author, who came up with the idea of splitting the ribbon into two distinct groups.

Thus the shorter term group of averages would represent the shorter term traders in the market whilst the longer term group would represent the more conservative, longer term traders and investors. Daryl prefers using exponential moving averages and employs MMA charts in a variety of different ways but principally for trend analysis.

However the one way in which Daryl and I differ is that he trades with daily charts whilst I use weekly charts. Because of this we invariably use different periods for our EMAs.

Weekly MMA chart created using EMAs, with the shorter term group in grey and the longer term group in black
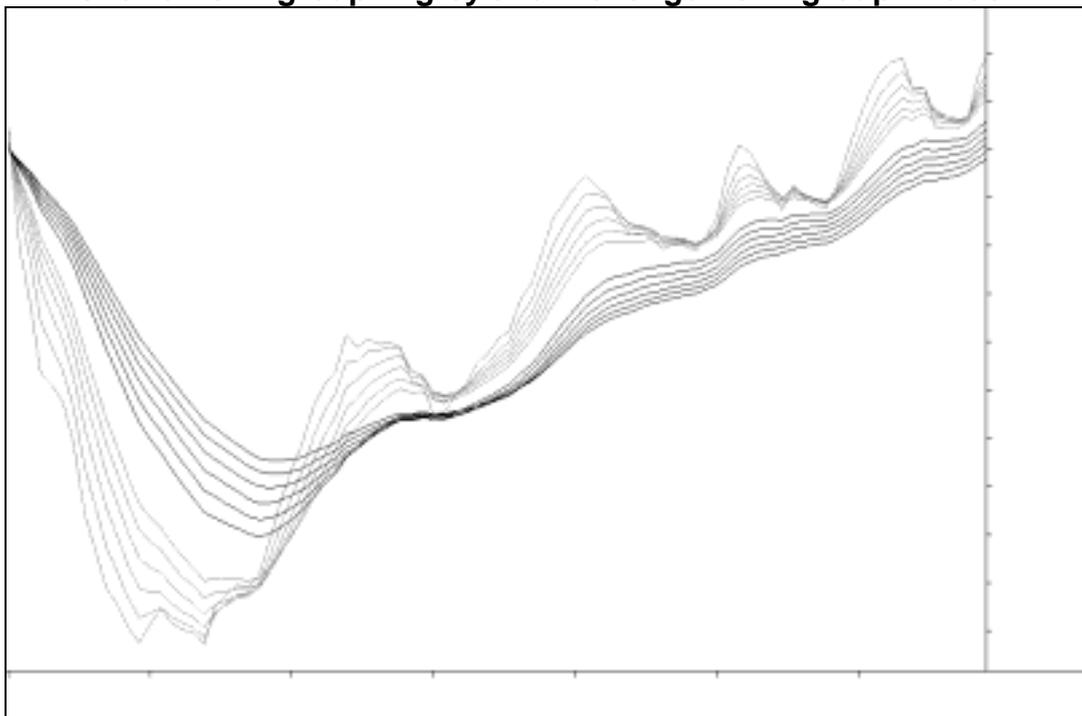
Now that I've covered how they are constructed, let's now turn our attention to their application which is qualitative as opposed to quantitative. Essentially I use MMA charts to judge the quality of a trend, my principle concern being the degree of volatility in the price behaviour. Let's start by looking at an ideal trend where there is a little bit of short term volatility but all the longer term lines on the chart are remaining relatively straight, evenly spread out and parallel to each other.

MMA chart showing an ideal trend with very low volatility
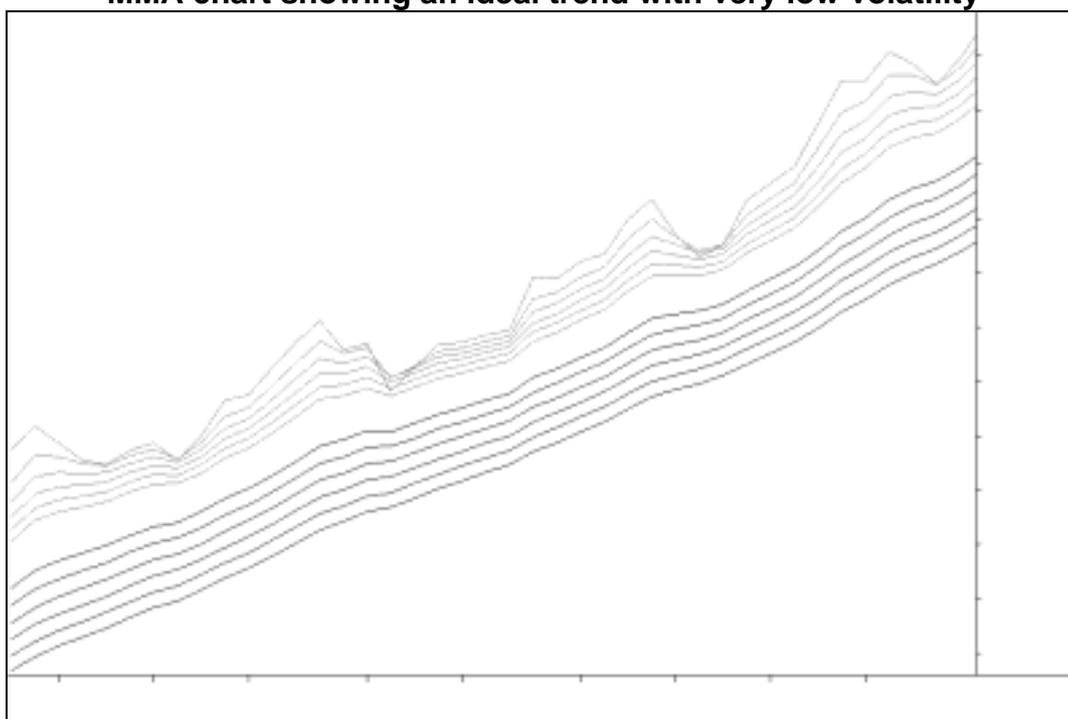
Looking at the short term group of averages, you can see how the market runs and then pulls back, over and over again. This is normal trending behaviour as markets constantly rally and then rest, repeatedly. But it should be a nice even and regular pattern that isn't too violent.

If it is very aggressive then it indicates that the very short term traders have a strong influence over the market and, as a result, the trend is inherently unstable. So let's look at this type of situation where the price activity has far too much short term volatility and would therefore be considered as unstable.

MMA chart showing an unstable trend
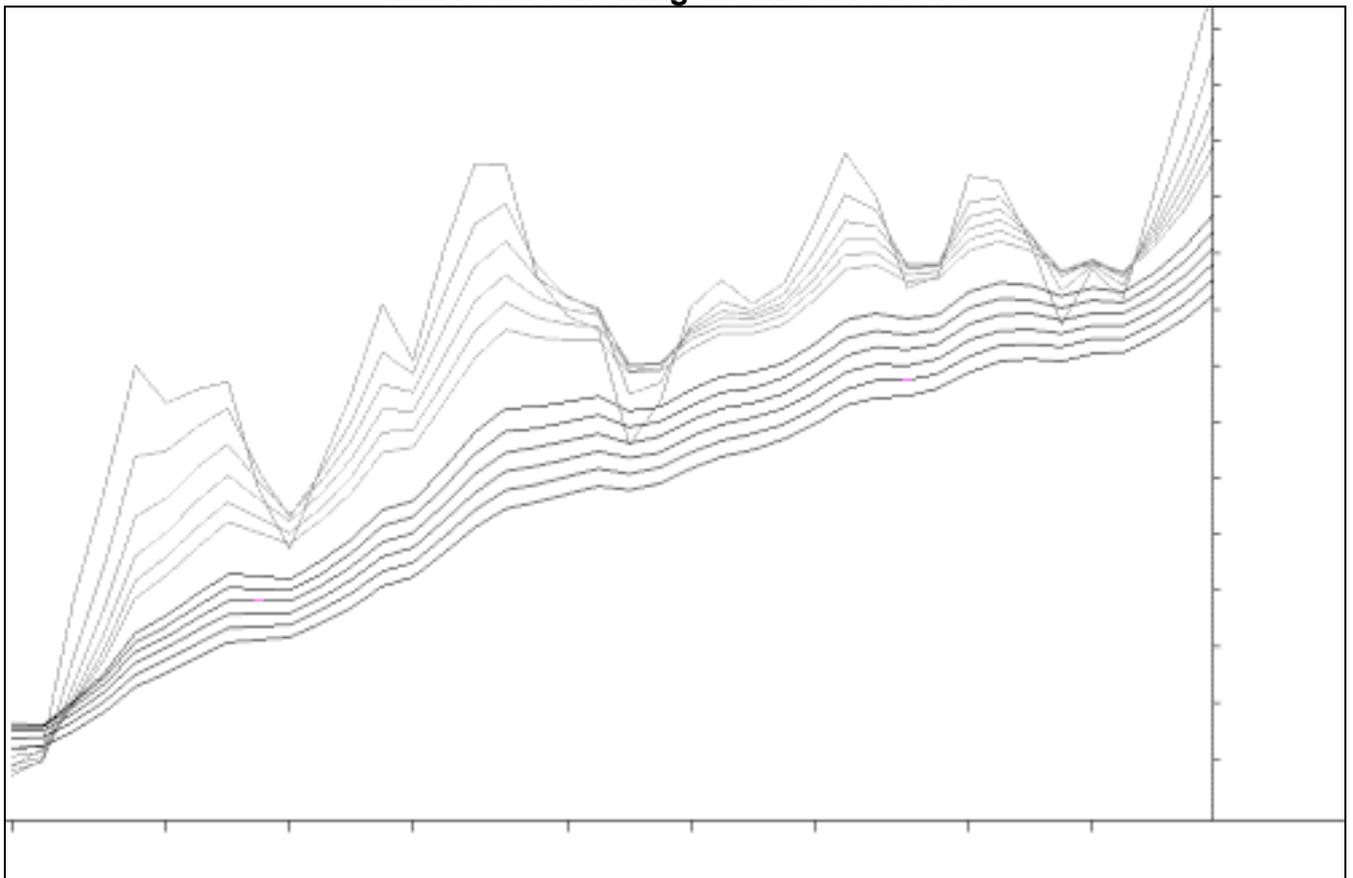
In this instance you can see how the long term group of lines aren't straight and look like their being pushed around by the shorter term group. So I would buy into the ideal trend but not into the unstable one as it is far less likely to survive, in my opinion. And there's the kicker…in my opinion.

Analysing MMA charts is entirely discretionary and requires a considerable amount of practice if you want to do it well. Hence MMA chart interpretation is more akin to an art than a science.

Sector MMAs

I'm using the GICS Standard and Poors Industry Group sectors as the basis of my sector analysis. My indicator of choice, as I've just explained, are the Multiple Moving Averages for assessing the quality of trends. Let's have a look at what they look like;

S&P GICS Industry Group sectors with Multiple Moving Averages
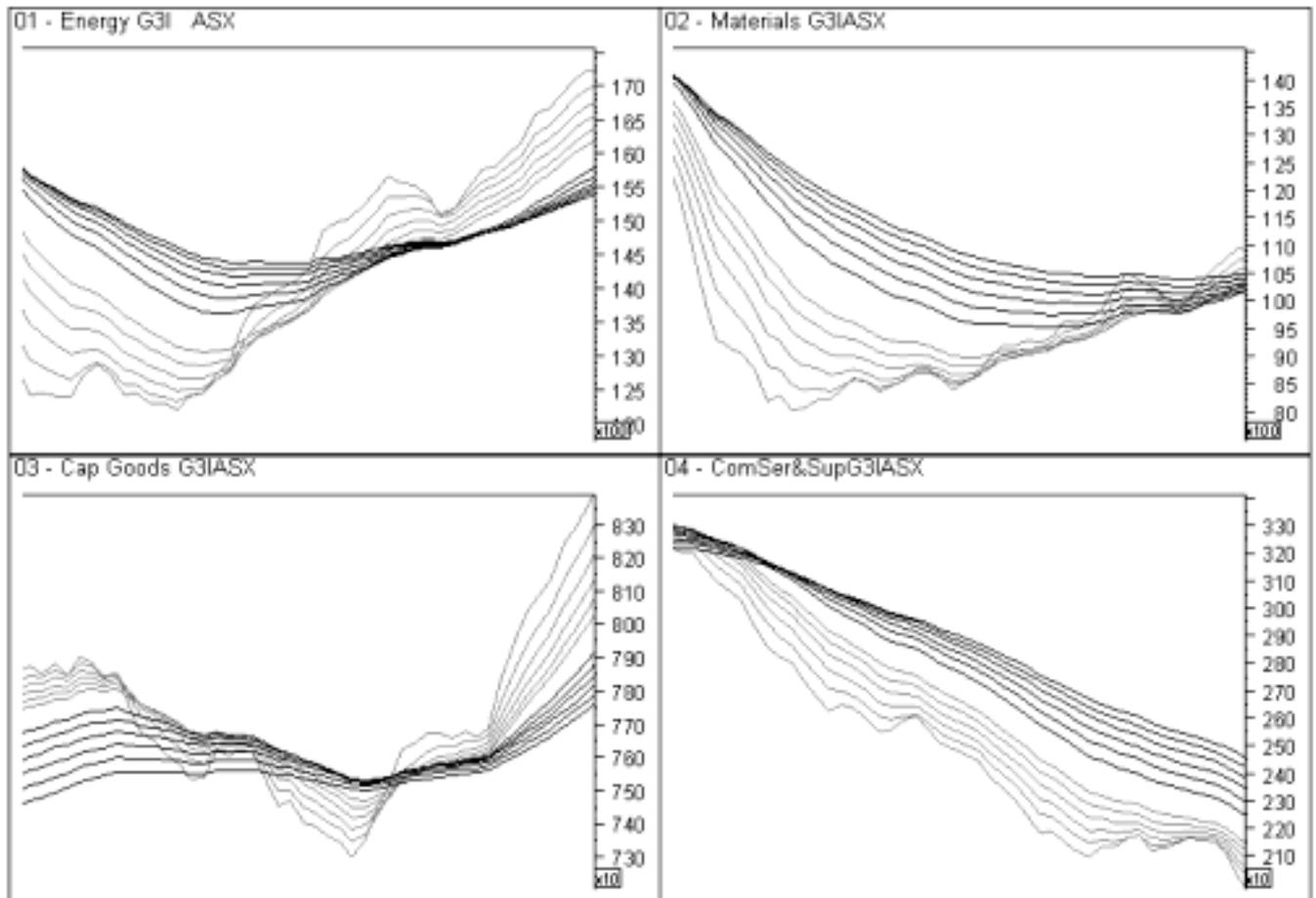
Here we can see 4 of the 22 main sectors over about a 30 week period. The shorter term group of averages (the grey lines) are 3, 5, 7, 9, 11 and 13 periods and the longer term group (black lines) are 21, 24, 27, 30, 33 and 36 periods. All moving averages are of the Exponential type and the periodicity used is weekly. Again, I've hidden the price activity for ease of reading.

This is a discretionary part of the analysis, but the MMAs will show me which sectors have the valid trends I'm looking for as part of this stage of the process. These charts do a great job at filtering out the short term noise of the market so I can focus on what the actual underlying trend is doing.

I'm looking for nice trends, those that have been rising for at least two months and have an acceptable low level of volatility. And note that we use the same type of analysis here that we are going to use when we look at the MMA charts of individual shares. Thus it is very important that we are as discerning with our analysis of the MMA charts for the sectors as we are with the shares. The following is a list of critical points to consider then interpreting the MMA charts…

- The long term group must be pointing upwards.
- The long term group must be spreading apart or running parallel with each other.
- The straighter the long term group of lines are, the less volatile the trend is.
- The short term group can pullback (ie. compress together) but they shouldn't come into contact with the long term group of averages and preferably the pullbacks are regular

So I have narrowed it down to the sectors with valid trends, now I have to narrow it down further to those that are rising the fastest. To do this I'm going to introduce a new indicator, the Rate of Return indicator.

Rate of Return Indicator (RoR)

The Rate of Return Indicator is used to calculate the annual rate of return of a share or an index (such as a sector index), given its current rate of climb or fall. In simple terms; we take the annual change of the share or sector and then divide it by the current value of the share or sector and multiply by one hundred to convert the figure to a percentage. For example:

- We'll assume a sector is rising at a rate of 120 points per year, ie. the change in value over 12 months is 120 points.
- The current value of the sector index is 1,980 points.
- Hence the annual Rate of Return would be 0.061 (ie. 120 divided by 1980)
- To convert this to a percentage we multiply by 100 and get 6% (rounded off!)

If we apply this measurement to all the sectors with valid trends, then we can see which ones are moving the fastest…these, of course, being the ones we want. Now let's get a little more specific about the design of the RoR indicator; rather than use the change in value over 1 year, which is a little blunt, we actually take a 3 month sample and then annualise the result.

And to provide a degree of smoothing, our values are actually taken from a 26 week Hull Moving Average, rather than the actual price activity itself. The following charts show the sector MMAs and also the rate of return (RoR) values at the top of each chart window.

Sector MMA charts with their Rate of Return at the top
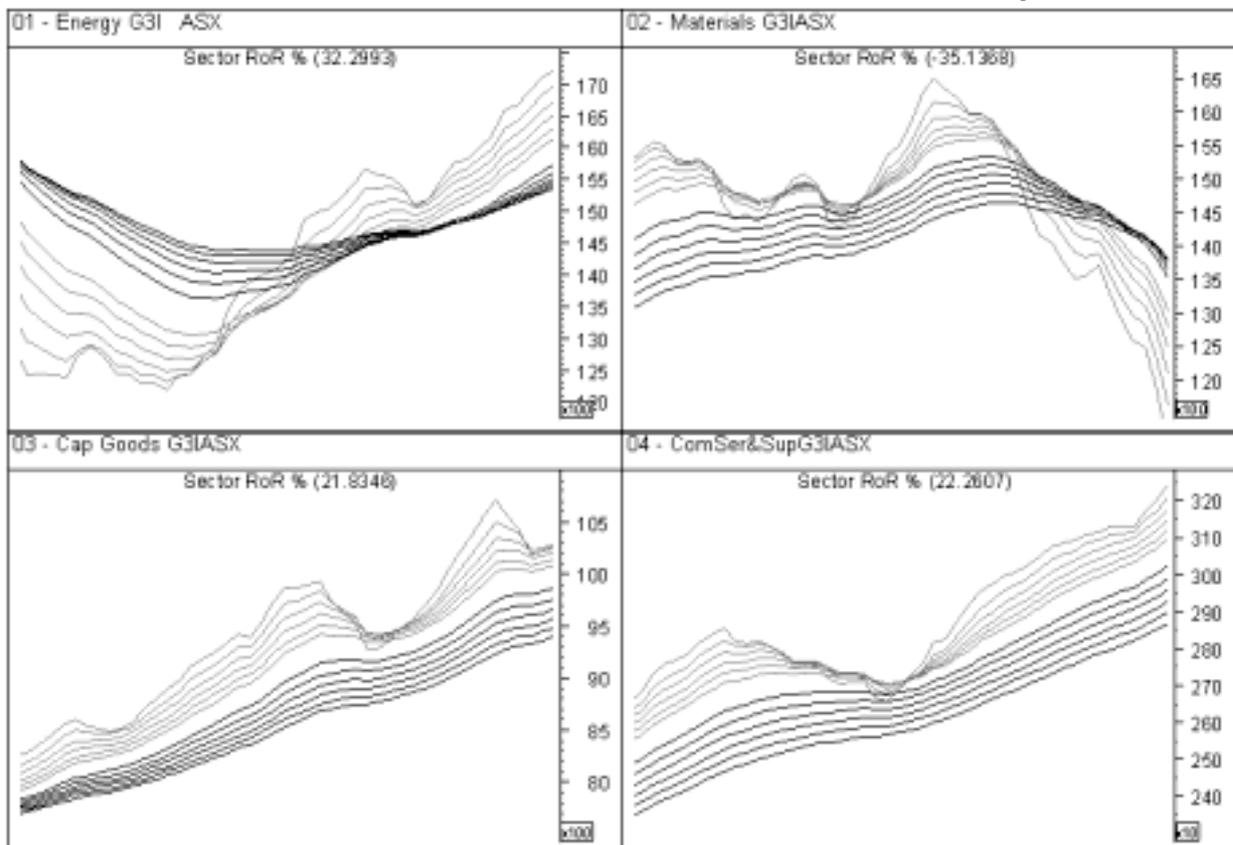
And I'll just add a little foot note here; if the RoR is negative it means that the sector is falling.

At this point, I will usually pick out the top 3 or 4 sectors, providing there is that many acceptable ones. I have to consider my sector risk management rules (more on this later on) and therefore I will need to spread my portfolio over at least 3 sectors. If I can't find enough acceptable sectors then I might be forced to leave some of my money in the Bank.

So now I have the tools to not only find the sectors with valid trends, but I can also find the ones that are rising the fastest. So what's next? Well now we getting down to the sharp end of the process because its time to look for those rising shares that are in the rising sectors.

Rising Share

The process for identifying rising shares is very similar to that used to identify the rising sectors. Again the two tools to be used will be MMA charts and the RoR indicator. At this point I'm trying to find the most suitable shares in the sectors I've identified in the previous step. The MMA charts will show me the shares with the valid trends and the RoR will let me know which ones are rising the fastest. First, let's take a look at some share MMA charts….

Share Charts with Multiple Moving Averages
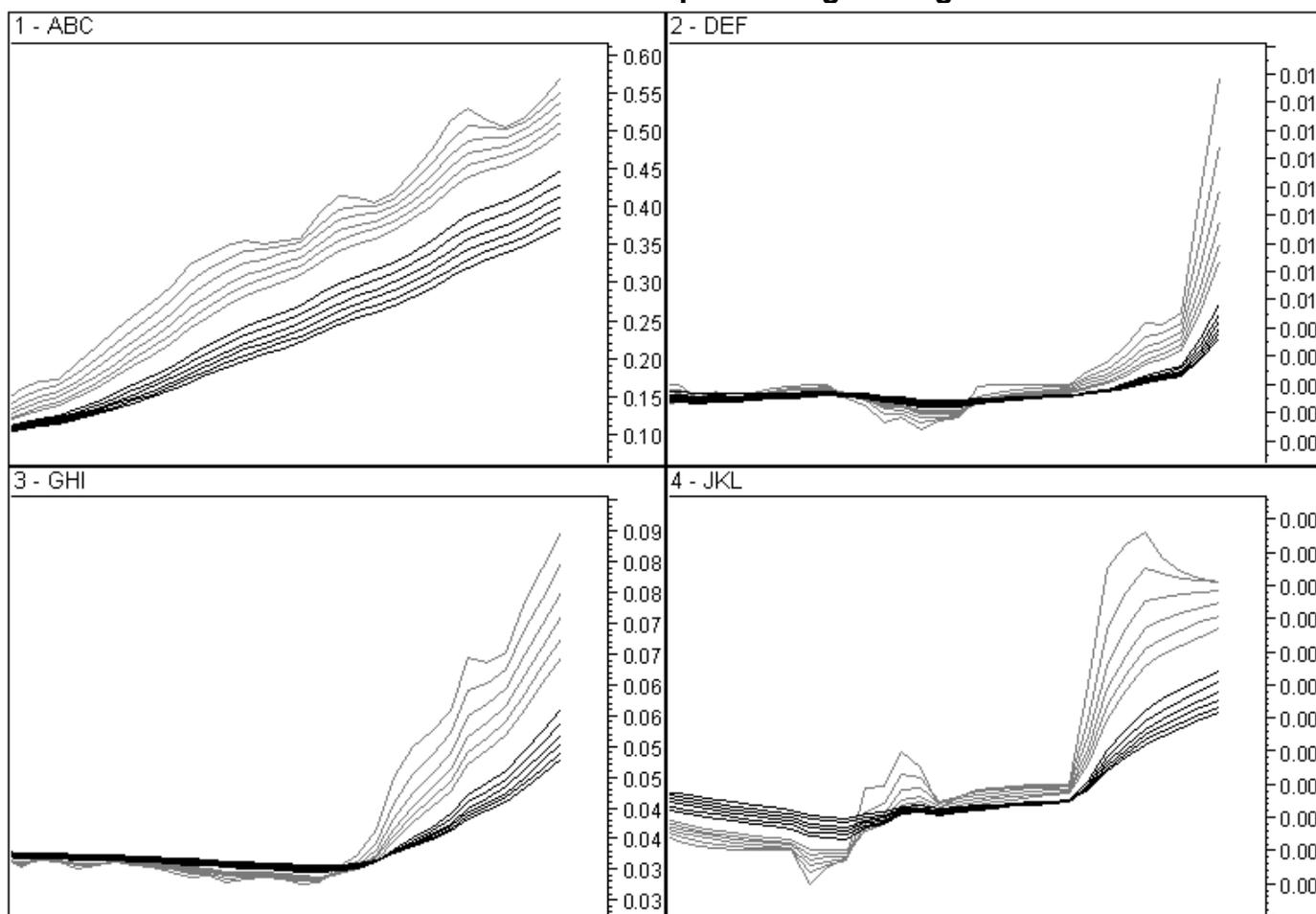
Again I'm using weekly charts with the following exponential moving averages :

- Short term group (grey lines) are 3, 5, 7, 9, 11 and 13
- Long term group (black lines) are 21, 24, 27, 30, 33 and 36

We use the same rules for interpreting the share MMA charts that we used for the sector MMA charts and making sure we remember the critical points listed previously. Here's a few examples of the good, the bad and the ugly!

Sample of various Share MMA charts with appropriate titles!
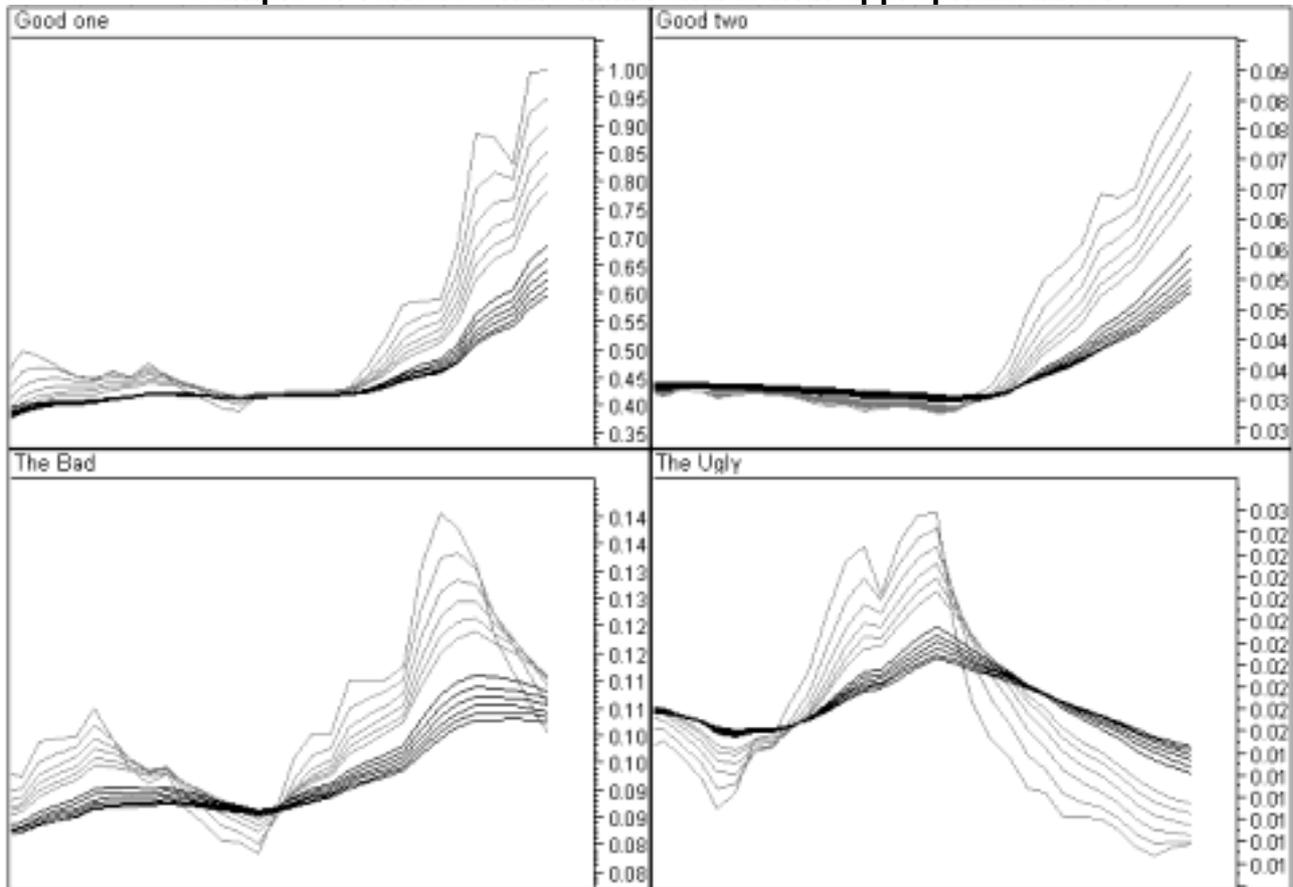
And just like we did with the sectors, we apply the RoR indicator to the shares to make sure the trends are rising fast enough. Because this is a short term system, we want fast moving shares with high Rates of Return.

Thus, my minimum Rate of Return is set at 80%. This means that if I check the weekly value of a shares RoR and it is below 80%, I'll sell that share and replace it with another one, if there's a suitable opportunity.

This ensures that my money is always working hard for me and I'm not holding onto shares that are just drifting sideways. Now one further thing I need is a minimum entry RoR to ensure that I'm not whipsawed in and out of the market if a share's RoR hovers just above and below 80%. Thus my minimum entry RoR is set a comfortable distance away at 120%.

Having a minimum entry RoR of 120% provides a buffer zone of 40% (120% - 80%). Here's a chart of a share with the RoR indicator (in the uppermost window) so you can see how it changes over time…

Candlestick chart of Share and Rate of Return Indicator (RoR scaled by 10)
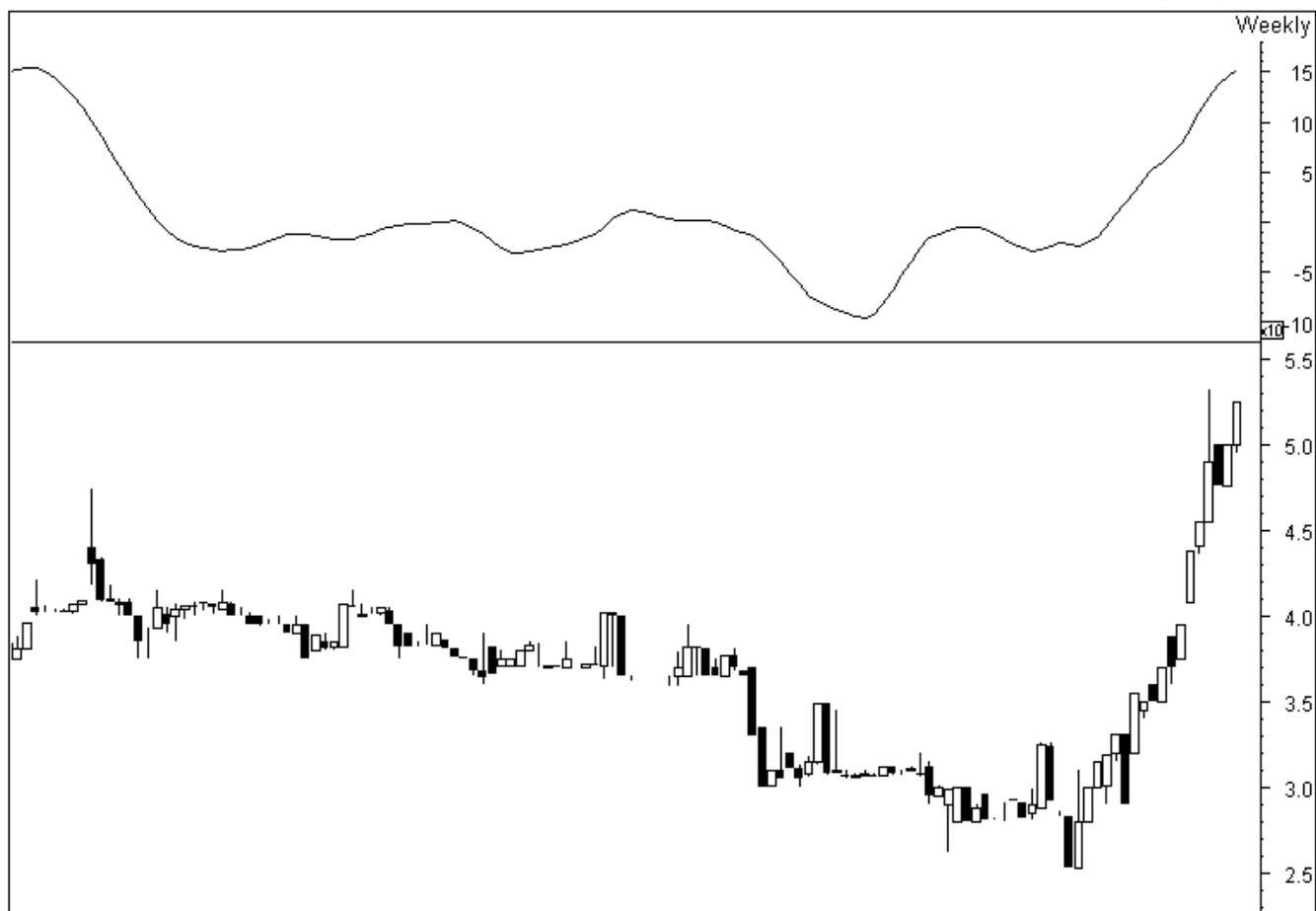
Applying the RoR to the shares with valid trends will give me a list of the best possible candidates for my portfolio. Once we've narrowed the search down to this degree, we're ready to complete the last step in the process and find the shares with rising weeks or upweeks. Once we've done that, we can fine tune our entry and call the broker!

Rising Week or Upweek

And, very shortly, I'm going to introduce another tool…the Range Indicator. The Range indicator, along with plain old end of week closing prices, will enable us to find the shares with a valid entry.

Finding if a share has had an upweek is really very simple. All we need to do is look at the current end of week closing price (remember our analysis is weekly) and then look at the closing price from last week.

If this week's closing price is greater than last week's closing price, then this week is an upweek. And please note; if the prices are the same, then it is not an up week!

Anyway, I've listed a few examples at the top of the next page, so see if you can pick out the shares with an upweek…

Table of Shares showing this week and last weeks closing price

Share Code	This weeks Closing Price ($)	Last weeks Closing Price ($)
MNO	3.220	3.000
PQR	0.230	0.310
STU	0.355	0.354
VWX	0.625	0.625
YZA	1.135	1.250

Yes…there were only two (MNO and STU), the others are either down or neutral. Once we've sorted out which ones have had an upweek then we can then use the Range Indicator to find out if we have a valid entry.

Range Indicator

The Range indicator provides us with a series of price ranges that tell us when to buy, sell, hold or take profit. Although simple in construction, it tells us when the price activity is pulling back, rallying up or the trend is reversing. And like the RoR indicator, its construction is based on the Hull Moving Average, referred to in this context as the central cord.

We then use Average True Range (which measures price volatility) to position upper and lower lines based on the central cord. These lines are referred to as the upper deviation line and lower deviation line. These two lines create an envelope that defines our tolerance towards price volatility.

The central cord, upper deviation and lower deviation lines create four distinct price zones that tell us when to buy, hold, profit take or sell. The following chart illustrates how the Range indicator is used to set buy, hold & sell zones.

Share chart showing Range Indicator
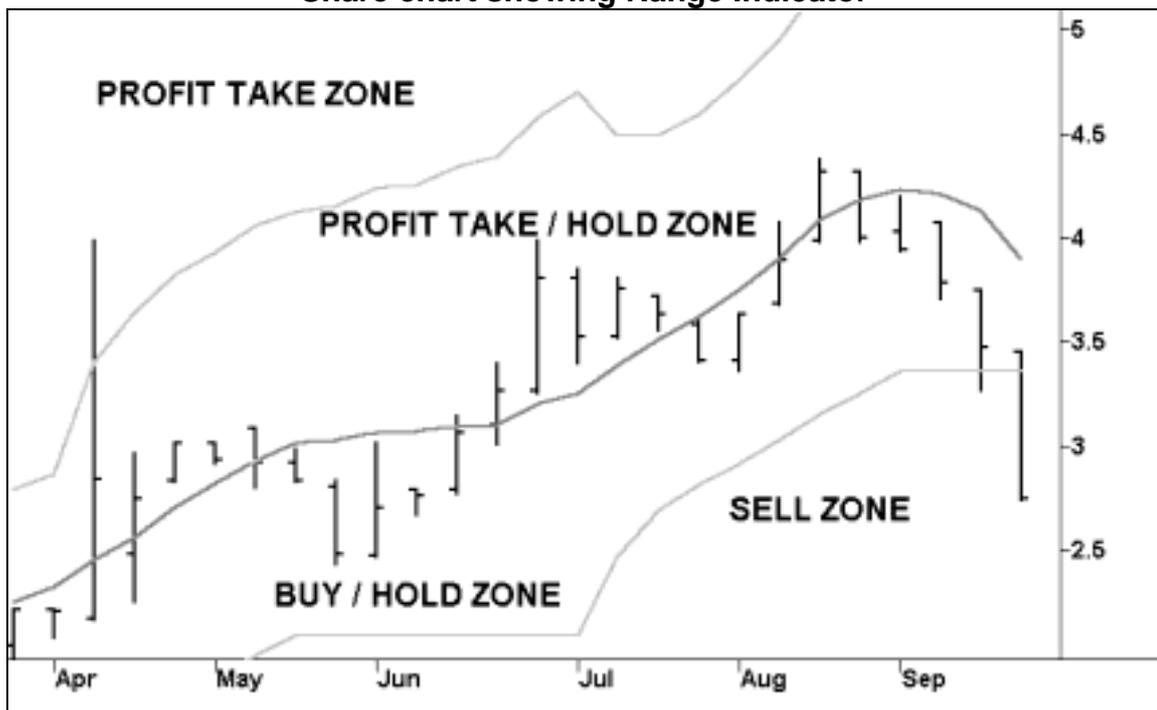
Rules for the Zones

Sell Zone   Sell if the share closes at the end of the day in this zone.

Buy/Hold Zone   Buy the share if it has closed at the end of the week in this zone and the price is higher than the previous week's closing price. The share must be purchased at a price between the lower deviation and the central cord. Hold if already owned.

Profit Take   Hold if the share price is in this zone or take profits if the position is up
/Hold Zone   strongly from its initial purchase price (eg. maybe sell half the position)

Profit Take   Mandatory - Take profits if the share price closes at the end of the week
Zone   in this zone. (in this instance sell the entire position)

                        Optional - Take profits if the share price is in this zone at any time.

By using the range indicator to control our entry and exits we can avoid buying overpriced shares and sell when a trend reversal occurs. Although the Range Indicator is applied to weekly charts (ie. weekly analysis), the buy and sell signals are applied on a day-to-day basis (ie. daily execution).

Here's a list of shares where you can see whether or not they have had an upweek by looking at the third column from the left. It also shows the Range and RoR indicator values and so we can work out which ones have a valid entry and which ones don't. Note that the RoR indicator measures a share's 'rate of annual return' which I refer to in the table as the ROAR value.

List of shares showing weekly direction, Range indicator and RoR indicator values

Share Code	Closing Price($)		Central Cord($)	Upper($) Deviation	Lower($) Deviation	ROAR (%)
AAA	0.255	Up	0.258	0.266	0.244	184
BBB	0.670	Dn	0.791	0.923	0.579	157
CCC	3.610		3.688	3.922	3.309	110
DDD	0.096	Up	0.102	0.120	0.074	137
EEE	0.620	Up	0.748	0.860	0.568	116
FFF	0.435	Up	0.516	0.607	0.370	174
GGG	0.715	Dn	0.821	1.009	0.517	248
HHH	3.220	Up	3.350	3.508	3.094	81
III	0.230	Dn	0.256	0.305	0.175	137
JJJ	0.355		0.462	0.555	0.311	204
KKK	0.625	Up	0.822	0.978	0.569	231

Share FFF, among others, is a valid entry as long as we purchase it at a price between the lower deviation and the central cord. Unfortunately the share price may suddenly take off and we may not be able to purchase it in the 'buy zone' and therefore we will have to wait for another opportunity. Hence, it is quite normal to spend several weeks or more waiting for entry signals to completely fill an Active Trading portfolio.

Trade management

And once you've found a share you want to buy then you need to work out your position size. To do this you will need to know your buy price and your initial stop loss in order to apply risk management (more on this shortly). Of course the lower deviation will be your stop loss.

Now we already know that if a share's RoR drops below 80% then it has to be sold. But there are other times when we will have to sell a share too. And as you saw a little earlier, the Range Indicator has a 'Sell' zone. Thus, if a share has an END OF DAY close below the lower deviation then we must sell that share. And there is no negotiating with this rule!

So that's the Active Trading system; the hows and whys behind it and the tools needed to implement the system. Of course I appreciate there's a lot to digest and so it probably take multiple readings of this manual to fully grasp all the workings of the strategy.

Now, we'll look at the risk management requirements before taking you for a test drive of the strategy using some historical *ActTrade* newsletters.

Risk Management

Share Traders can only manage the risks involved in share trading if they use clearly defined entry and exit prices. As Active Traders these are defined for us by the Range Indicator.

Position Risk

The potential loss in owning each share is referred to as position risk. Traders normally use the 2% risk rule that states;

'The total loss for any single trade must not exceed 2% of total capital'

Your total capital is the current value of all shares held plus the total amount of cash on hand. By risking only 2% of our total capital on each trade it would take well in excess of 150 consecutive losses to lose all of our money.

Statistics from the U.S. indicate that 20% of Traders use risk management which coincides with the fact that only 20% of Traders survive.

An Example of the 2% Risk Rule

- We are trading with $20,000 total capital and using the 2% risk rule
- Assume that the closing price of a share is 12 cents & the stop loss is set at 10 cents. (It is assumed in this example that the closing price is the probable entry price.)
- The potential loss per share is 12 - 10 = 2 cents and 2% of $20,000 = $400
- Divide $400 by 2 cents to get the number of shares we can buy = 20,000 shares
- Multiply 20,000 by the closing price of 12 cents to get the position size = $2,400
- Divide $2,400 by $20,000 and multiply by 100 to get the percentage of total capital that can be spent on this position = 12% (This is the maximum position size)

The 'Port. Weighting for the 2% risk' column in the ActTrade Newsletter is calculated using the Range indicator's lower deviation value as the stop loss. The amounts shown are the maximum weightings for your total capital, ie. a 10 in this column means 10% of your total capital. This column will display a maximum value of 20 because the largest allowable position size is 20%.

Sector Risk (Also referred to as Industry Risk)

We want to be able to capitalise on strong sectors without being overly exposed to sector 'Fads'. To limit our exposure we will only allocate a maximum of 40% of our total capital per sector and a maximum of 6% position risk per sector, ie. 3 positions/sector (3 x 2% = 6%).

Portfolio Risk

Portfolio risk is the sum total of our position risk. Therefore we must limit our maximum number of positions at any given time in order to control our total exposure to the market. A maximum of 20% portfolio risk will yield a maximum of 10 positions (10 x 2%). In fact it is a good idea to operate well within this limit at say a total of 5 positions. This is because most of us will find even just 5 positions difficult to manage on a day to day basis if the market suddenly turns volatile. An example of such an event was the impact on markets by S11.

Capital Allocation

The Active Trading strategy is a short term, medium risk approach that often identifies relatively low liquidity shares. It has been designed to work alongside and compliment well proven Trend Trading strategies such as the *ActVest* Newsletter and the Blue Chip Report.

The following guidelines are strongly recommended to investors/traders for capital allocation. Within these guidelines the Active Trading strategy would fit in as medium risk strategy.

Guidelines

☑ 60% Blue Chip shares   (the Blue Chip Report and the *ActVest* Newsletter)
☑ 30% Medium risk strategy   (the *ActTrade* and the Breakout Trading Newsletters)
☑ 10% Speculative strategy   (leveraged instruments; CFD's, Forex, Futures, etc.)

Using the *ActTrade* Newsletter

This section is written by Simon Sherwood who assists with the weekly production of both my ActVest and ActTrade Newsletters.

Now that we've read all about the theory of Active Trading, it's time to see it work in real time. To simulate how the strategy works, we are going to use the ActTrade Newsletter for all the charts and data and the ActVest Trade Recorder to track our portfolio. The ActVest Trade Recorder is a simple Excel based spreadsheet tool that contains all the information we need to track our portfolio without distracting us with too much clutter!

This is an outline of the process we will be following :

1. Check the Stop Losses for all our open positions (very important, this should be the FIRST thing we do each week)
2. Check the Cross Over charts
3. Select suitable Sector MMA charts with the highest rates of return
4. Select suitable Share MMA charts
5. Check Share Data Tables for valid entries
6. Calculate purchase details and position size
7. Update records

We'll be doing this over a period of about four weeks and we're starting on the 2nd of February 2007.

Week One

As this is the very beginning of the simulation, the first thing we need to do is to set up our ActVest Trade Recorder. We're going to start with a $100,000 cash and as the first newsletter we are looking at is AT070202 (where the numbers reference the date – YYMMDD), we'll set up our Trade Recorder so it looks like this :

ActVest Trade Recorder showing Cash and Newsletter reference

When we get to the stage of clicking the 'New Week' button, the macros in the spreadsheet will save the file under the name of the newsletter reference, ie AT070202.xls. This way we can easily match up the appropriate spreadsheet with the corresponding newsletter. Of course the other benefit of the ActVest Trade Recorder is that it contains only the information we actually need – Cash on Hand, the Share codes and the number of shares. Of course, as we progress through this simulation you'll get a much better idea of how the spreadsheet works.

Moving on and normally the first step would be to check our stop losses but because this is week one, we don't have any open positions. Our second step is to check the Cross Over charts. For this we're looking at the All Ords and the Small Ords to get the green light to go shopping. We need BOTH of them crossed to the upside (as explained earlier). Here's the two charts from our first newsletter:

All Ords Cross Over Chart
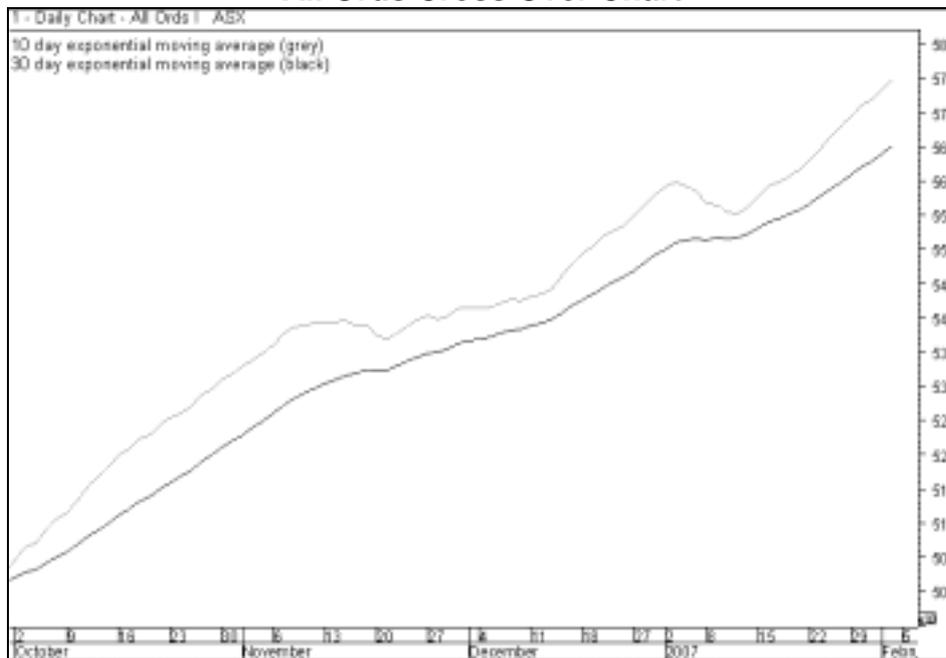
Small Ords Cross Over Chart
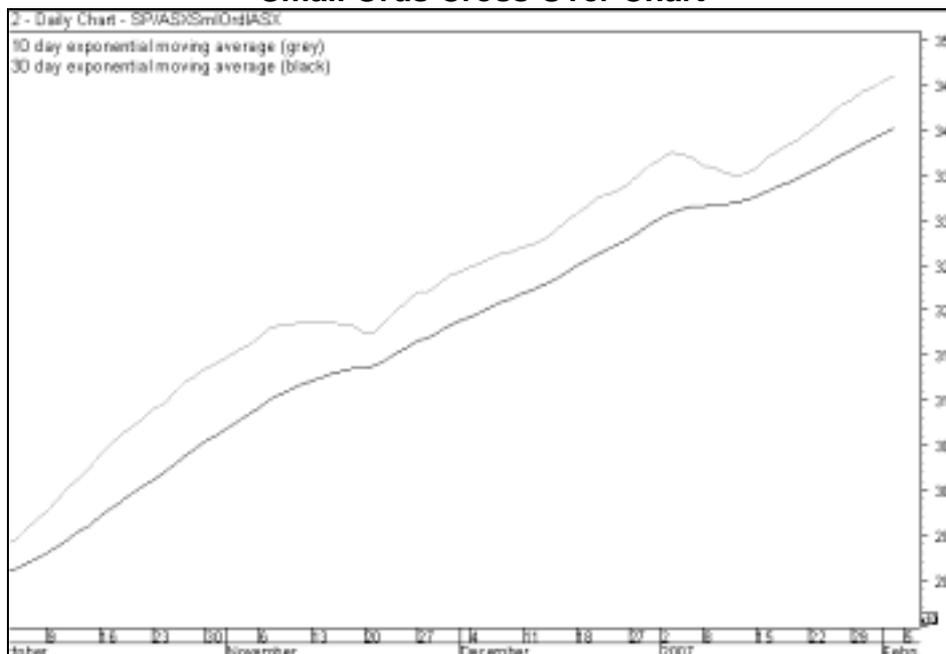
As we can see, BOTH of these charts are crossed to the upside as the grey line is above the black line for both charts….as Alan says…let's go shopping! Well, almost….now we have to look at our next level, which is the Sector MMA charts.

Here we are looking for suitable rising sectors and this is what they look like (all 22 of the GICS Industry Group MMA charts). Remember that suitable MMA charts are those that have been rising for at least two months and have an acceptable low level of volatility.

GICS Industry Group Analysis Charts

09 - Media G3I ASX — Sector ROR (43.6078)

10 - RetailingG3I ASX — Sector ROR (36.8594)

11 - Food&DrugG3I ASX — Sector ROR (24.0810)

12 - FoodBev&TG3I ASX — Sector ROR (31.8405)

13 - HealthE&SG3I ASX — Sector ROR (51.1326)

14 - InsuranceG3I ASX — Sector ROR (54.3967)

15 - Banks G3I ASX — Sector ROR (19.9202)

16 - DiverseFinG3IASX — Sector ROR (36.4699)
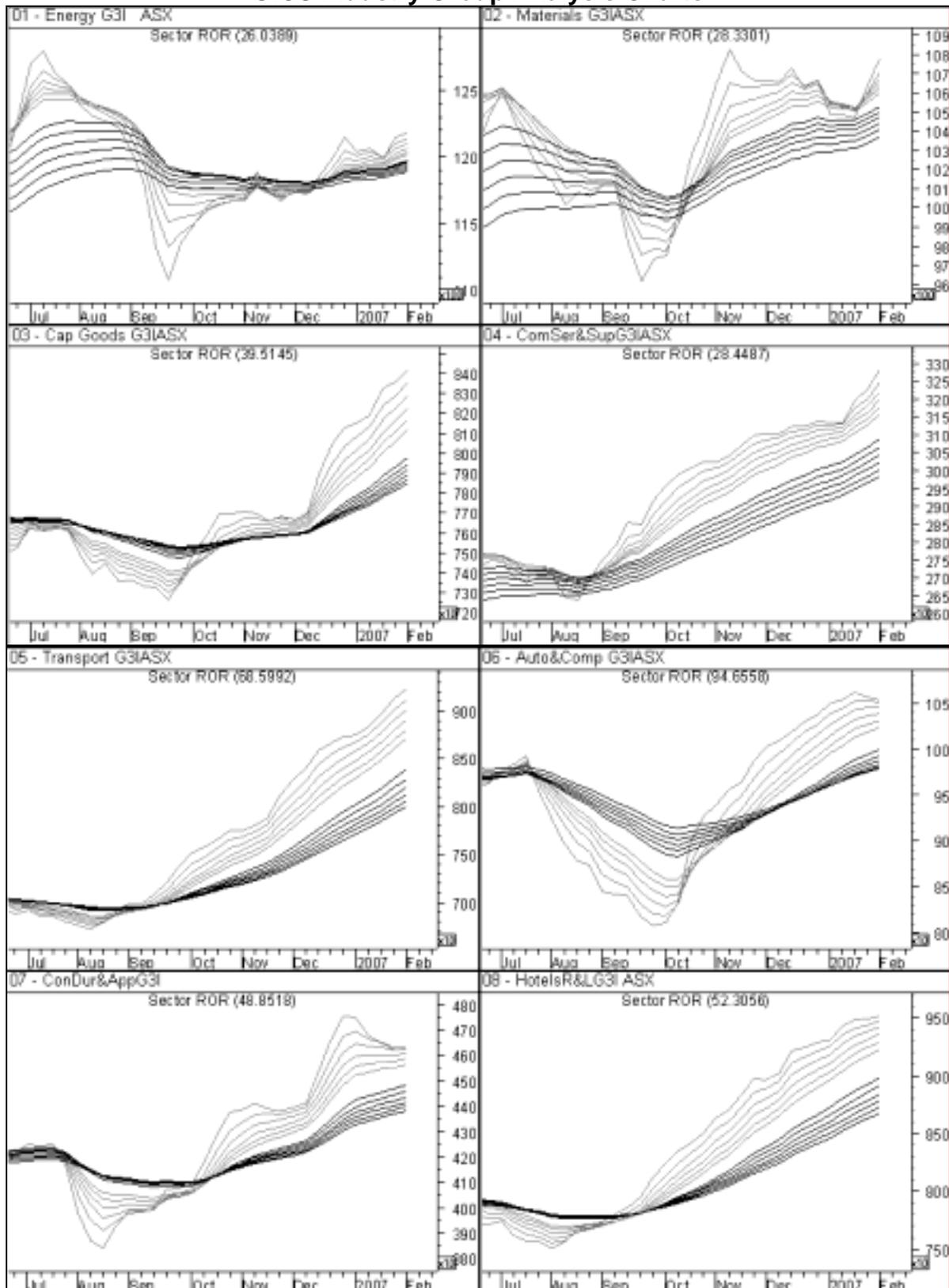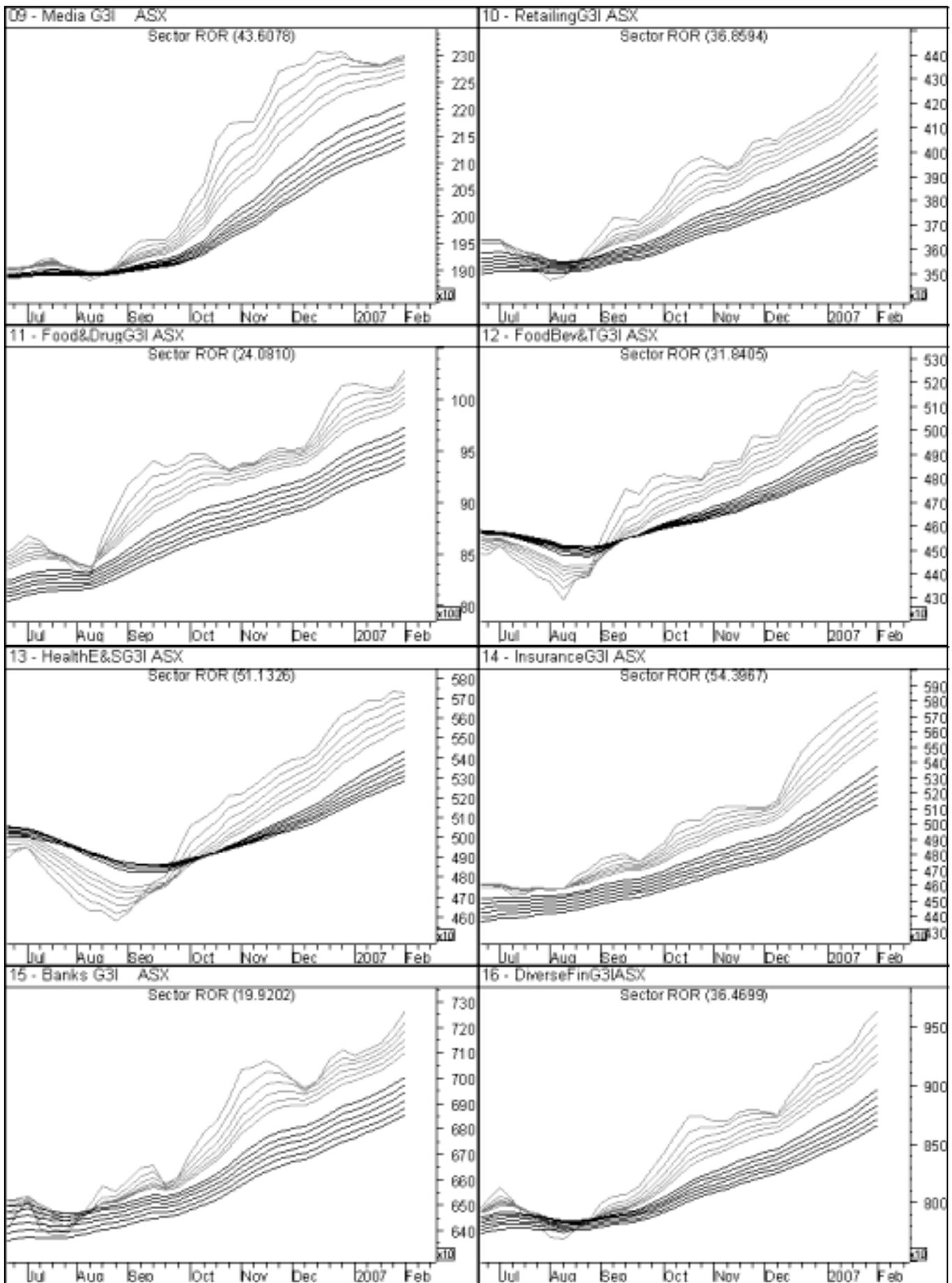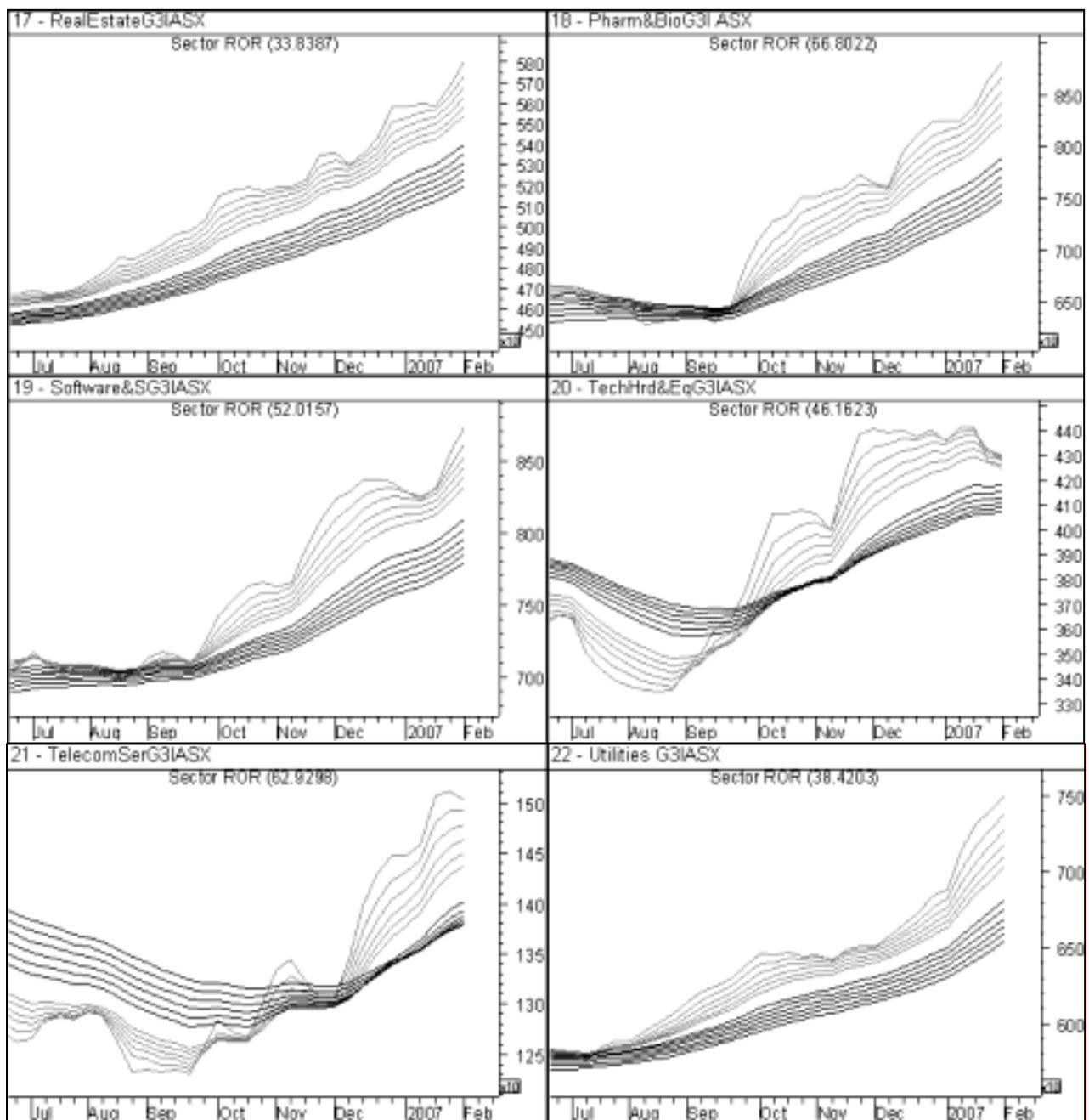
From looking at the MMA charts and using the rules previously stated, we can come up with the following list of suitable sectors (and their respective Rates of Return - rounded off) And note that ROR and ROAR values are in fact the same thing but a different notation is used when referring to a sector's rate of return (ROR) and a shares rate of return (ROAR):

GICS Industry Group	ROR %
Transport	69
Pharm&Biotech	67
Insurance	54
Software&Services	52
Utilities	38
Retailing	37
DiverseFinancials	36
Real Estate	34
FoodBev&Tobacco	32

So that's the end of step 3 and now we need to select the best shares in the best sectors.

For this particular week, there are over 170 charts…so we'll just look at a sample of them here and then we'll move on to the shares I've selected for the simulation. Of course if you want to see a recent sample of an Active Trading (ActTrade) newsletter with all its charts and data then please send a request to us at **enquiries@alanhull.com**

Sample of Weekly MMA Charts from the ActTrade Newsletter
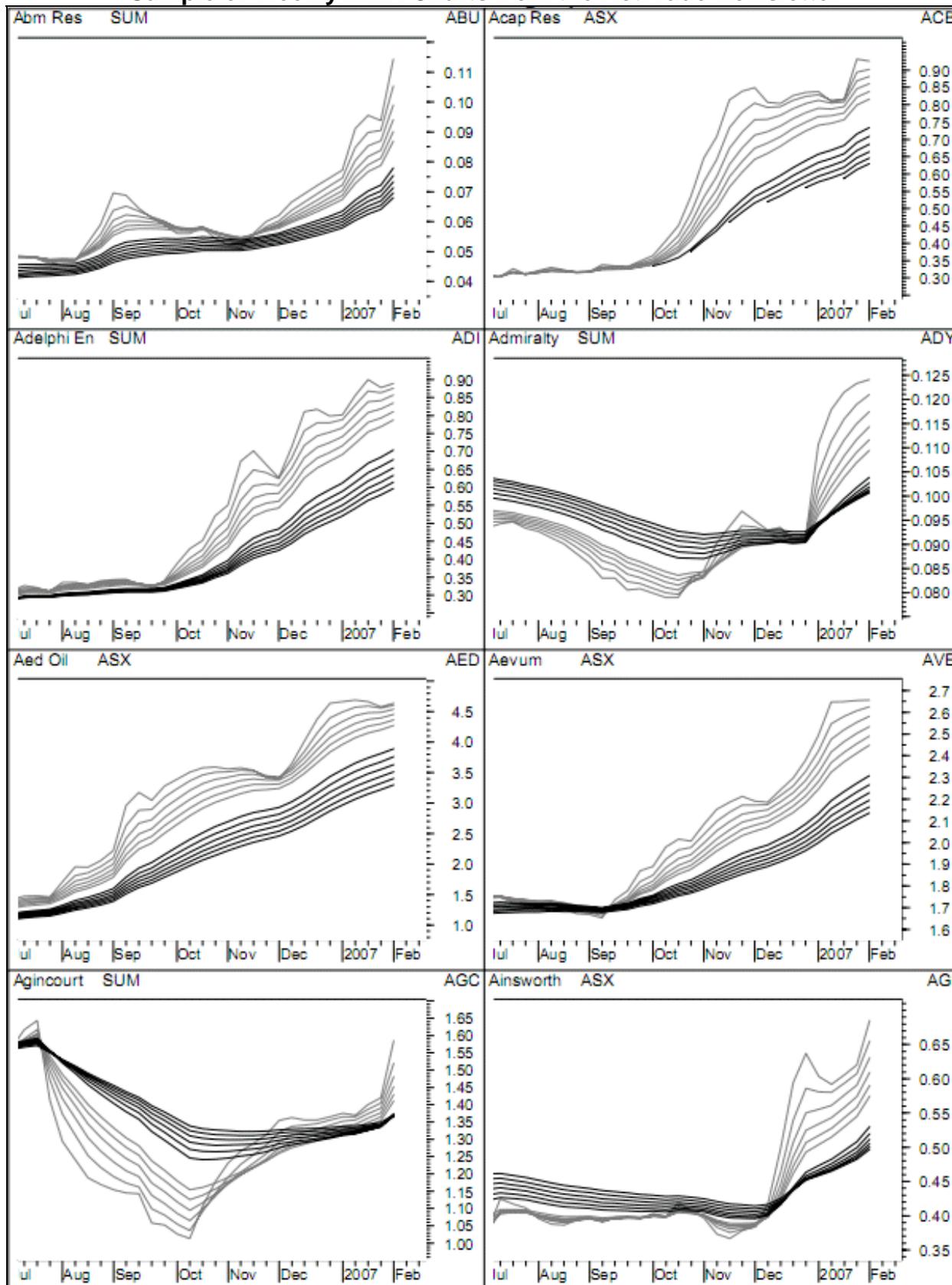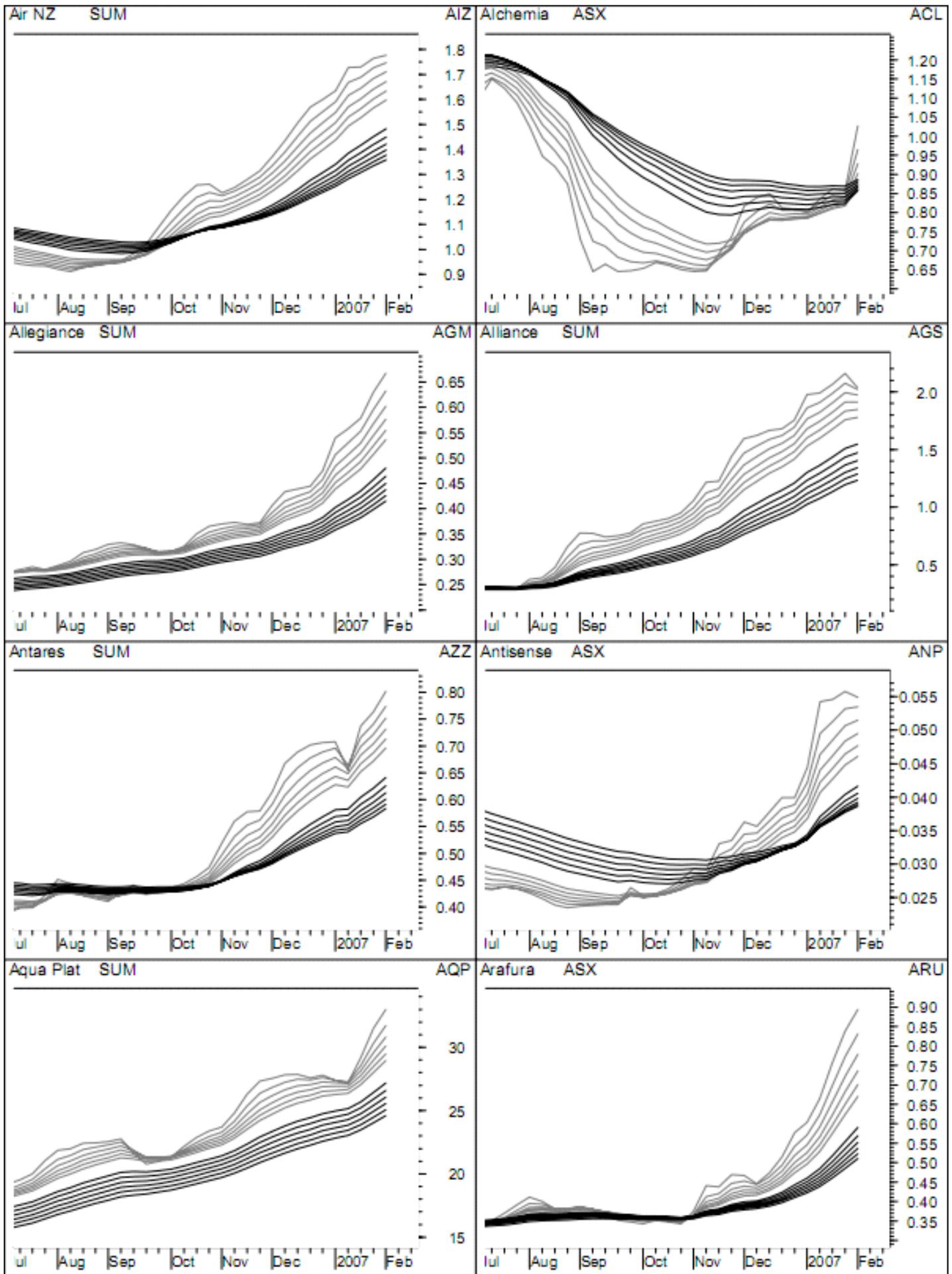
From examining all 177 MMA charts, we've come up with the following short list of suitable shares:

SHARE	GICS Industry Group
MRM	Transportation
REX	Transportation
TOL	Transportation
VBA	Transportation
CUV	Pharmaceuticals & Biotechnology
PWT	Software & Services
UXC	Software & Services
HGI	Diversified Financials
GPN	Real Estate
SDG	Real Estate
TGR	Food Beverage & Tobacco

We've narrowed our search down to those sectors that we listed earlier, so now we have a short list of upward trending shares in the upward trending sectors.

From this short list, we can move onto the next step which is to check for valid entries. For this we will be referring to the weekly ActTrade Data Tables and following is a sample :

Sample of ActTrade Newsletter Data Tables

ActTrade **Rising Equities**

Share Code	Closing Price ($)	Central Cord ($)	Upper ($) Deviation	Lower ($) Deviation	ROAR (%)	Port. Weighting for the 2% risk
AAX	4.880	4.878	5.550	3.790	108	9
ABU	0.135	0.138	0.165	0.094	149	6
ACB	0.920	1.017	1.064	0.940	158	20
ACL	1.195	1.191	1.327	0.971	97	11
ADI	0.900	1.013	1.118	0.842	166	18
ADY	0.125	0.140	0.158	0.111	106	11
AED	4.700	5.502	6.191	4.387	91	17
AEE	0.690	0.721	0.892	0.445	234	5
AGC	1.750	1.901	2.039	1.678	87	20
AGI	0.750	0.967	1.145	0.679	131	11
AGM	0.705	0.766	0.906	0.538	153	8
AGS	1.910	2.349	2.688	1.801	184	11
AIZ	1.790	1.960	2.206	1.562	112	13
AKK	0.820	1.025	1.206	0.733	217	9
ANG	1.370	1.538	1.750	1.195	168	11
ANP	0.054	0.066	0.078	0.047	168	9
AOE	1.220	1.249	1.338	1.106	116	18

Please note that the Data Tables also include two additional columns which show the GICS Industry Group and also the weekly direction; 'up' if this weeks closing price is higher than last weeks closing price or 'dn' if it is lower and a blank if there is no change. Given the restricted amount of space available here in the manual I've left these two columns out and I'm also going to be taking a closer look at both of them anyway.

So now we'll sort our prospects by their ROAR value to see which are the best candidates and make sure they pass all the entry criteria which is :

- An 'UP' week
- ROAR >= 120%
- Closing price in the Buy Zone – which means it must be less than or equal to the value of the Central Cord and greater than or equal to the value of the Lower Deviation.

Our list of prospects now looks like this :

List of prospects showing entry criteria

Share	GICS Industry Group		ROAR%	Buy Zone
REX	Transportation	Up	129	in
MRM	Transportation	Up	128	in
VBA	Transportation	-	98	
TOL	Transportation	Up	80	
CUV	Pharmaceuticals & Biotechnology	Up	156	in
PWT	Software & Services	Up	152	in
UXC	Software & Services	Up	93	
HGI	Diversified Financials	Up	98	
GPN	Real Estate	Up	202	in
SDG	Real Estate	Dn		
TGR	Food Beverage & Tobacco	Up	86	

If we then eliminate the shares that don't meet our criteria, those where the ROAR is less than 120%, or the weekly direction is NOT up, or the weekly closing price is NOT in the Buy Zone, we are left with our final list :

**Final list of prospects that meet all our criteria**

Share	GICS Industry Group		ROAR%	Buy Zone
REX	Transportation	Up	129	in
MRM	Transportation	Up	128	in
CUV	Pharmaceuticals & Biotechnology	Up	156	in
PWT	Software & Services	Up	152	in
GPN	Real Estate	Up	202	in

Here are the respective entries in the Data Tables :

Share Code	Closing Price ($)	Central Cord ($)	Upper ($) Deviation	Lower ($) Deviation	ROAR (%)	Port. Weighting for the 2% risk
CUV	0.895	1.012	1.195	0.716	156	8
GPN	0.053	0.053	0.066	0.033	202	5
MRM	1.200	1.270	1.451	0.978	128	10
PWT	2.270	2.438	2.778	1.888	152	10
REX	2.070	2.282	2.646	1.694	129	9

And these are their MMA charts that we found earlier :

Weekly MMA Charts from the ActTrade Newsletter
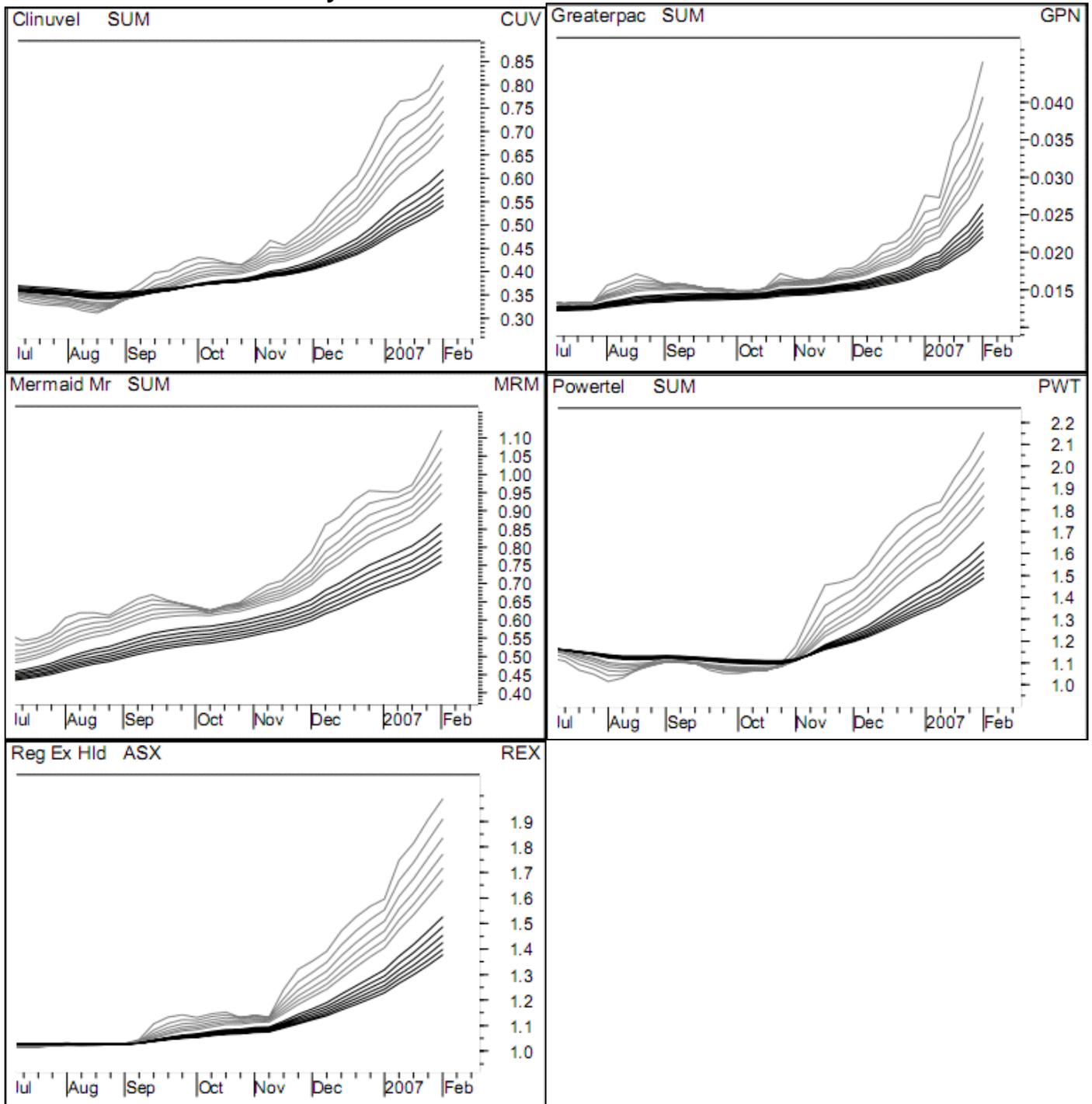
We're now ready to work out our position sizes and enter our trades in the Trade Recorder. And to keep this exercise reasonable simple, we are going to use the weekly closing price listed in the Newsletter Data Tables as our actual buy price.

You'll also note the column on the far right hand side of the data tables with the heading 'Port. Weighting for 2% risk' which stands for 'Portfolio Weighting for the 2% risk rule'.

What we've done here is calculate the percentage of your total capital that you can allocate to each share in order to only risk 2% of your total capital. Also note that this figure is never greater than 20% which is the maximum position size allowable.

Anyway, we'll start with the best performing share in the best performing sector and work our way down from there. Utilising the BUY calculator in the Trade Recorder and the figures from the Data Tables, you can see that we can purchase 4,347 shares of REX.

Trade Recorder Buy Calculator

Buy	Clear BUY
Cash on Hand	100,000
Total Capital	100,000
Portfolio Weighting	9
Share Price	2.07
Position Size	9,000
Maximum Number	4,347
Cash on Hand - AFTER	91,001

Please take your time to understand what we've done here by looking back at our final list of prospects and the Data Tables to see where we got the information for the calculator. Now we'll go ahead and do the calculations for the rest of the shares, so we end up with the following:

Trade Recorder showing all our positions for week one

Newsletter	AT070202
Cash on Hand	$58,001
Total Capital	$99,998

New Week

ActVest Trade Recorder
For buying shares

Share	Number	Price	Value
REX	4,347	2.07	8,998.29
MRM	8,333	1.20	9,999.60
CUV	8,938	0.90	7,999.51
PWT	4,405	2.27	9,999.35
GPN	94,337	0.05	4,999.86
			0.00
			0.00
			0.00
			0.00
			0.00
			0.00
			0.00
			0.00
			0.00
			0.00
			0.00

Buy	Clear BUY
Cash on Hand	
Total Capital	
Portfolio Weighting	
Share Price	
Position Size	
Maximum Number	
Cash on Hand - AFTER	

Sell	Clear SELL
Cash on Hand	
Number	
Share Price	
Cash on Hand - AFTER	

Action for Week
Bought REX 4347 @ 2.07
Bought MRM 8333 @ 1.20
Bought CUV 8938 @ .895
Bought PWT 4405 @ 2.27
Bought GPN 94337 @ .053

We've allocated about 42% of our cash to these five positions and our 'Total Capital' hasn't changed (we've just lost $2 because there's just been some rounding in the calculations).

That's a fairly busy week one….now time to save the Trade Recorder and move on to week two! And when we save week one, the Trade Recorder only retains the information that we absolutely need to carry forward.

Week Two

So this is what our Trade Recorder looks like at the start of week two….

Trade Recorder at the start of week 2

Newsletter				New Week
Cash on Hand	$58,001			*ActVest Trade Recorder*
Total Capital				*For buying shares*

| Share	Number	Price	Value
CUV	8,938		0.00
GPN	94,337		0.00
MRM	8,333		0.00
PWT	4,405		0.00
REX	4,347		0.00
			0.00

It shows ONLY the information we need.

Now the first thing to do this week is to check our Stop Losses. To do this we refer to the ActTrade Data Tables and see if any of our open positions have closed below the Lower Deviation. For this exercise I'm using an end of week stop loss, but in real time, you would be checking your stop losses at the end of each day.

Stop Losses checked! All our shares have had a weekly close above the Lower Deviation and they are all still in the Data Tables, meaning that their RoR is above 80%. Note that if their ROAR was less than 80% then they would simply be removed from the list. If this occurs then it is also a stop loss condition where we have to immediately sell the share.

Now it's time to see if we can purchase any more shares as we still have cash to spend.

We check the Cross Over charts and see that both the All Ords and the Small Ords are still crossed to the upside, ie. the grey line is ABOVE the black line at the right hand edge of the chart. (see charts on the next page)
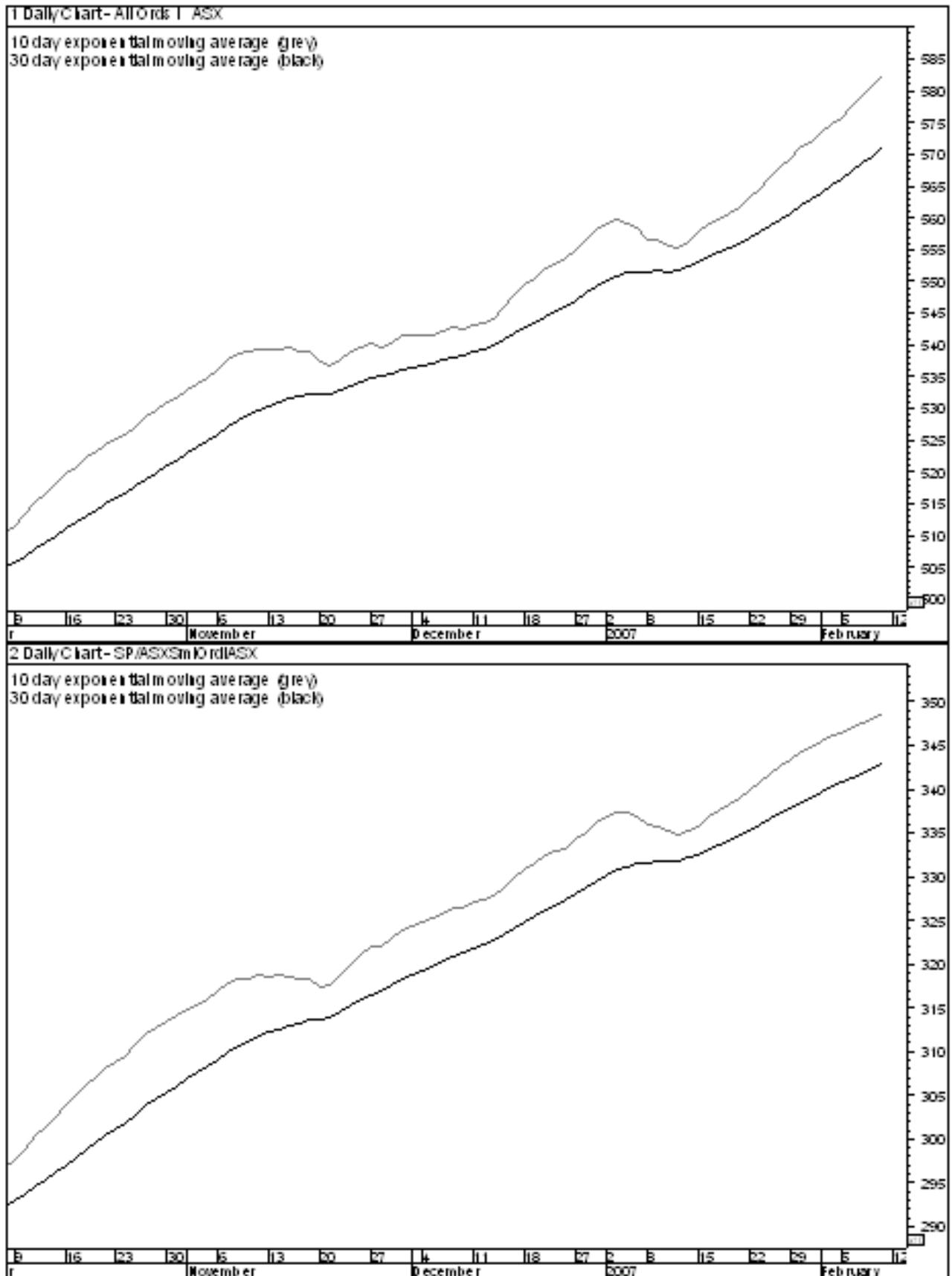
And they are still crossed to the upside. So the next thing to do is to check the Sector MMA charts and compile a list of the best rising sectors. Getting a feeling of *déjà vu*?

GICS Industry Group Analysis Charts
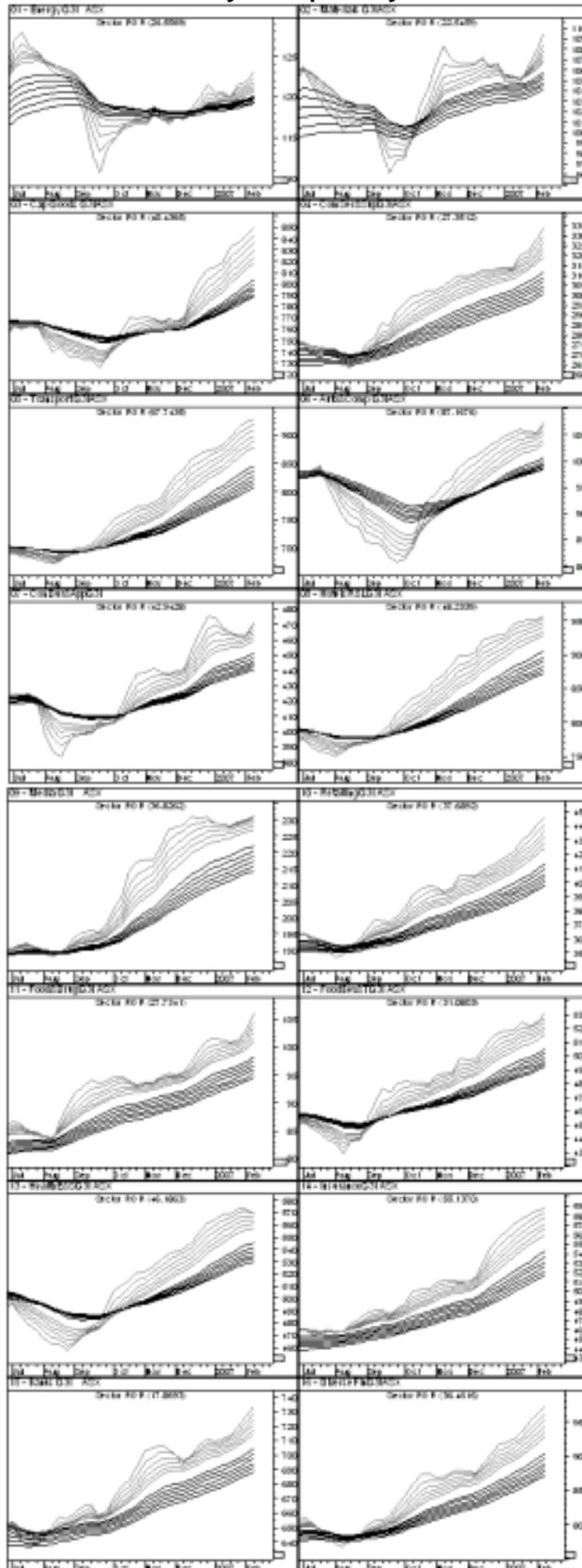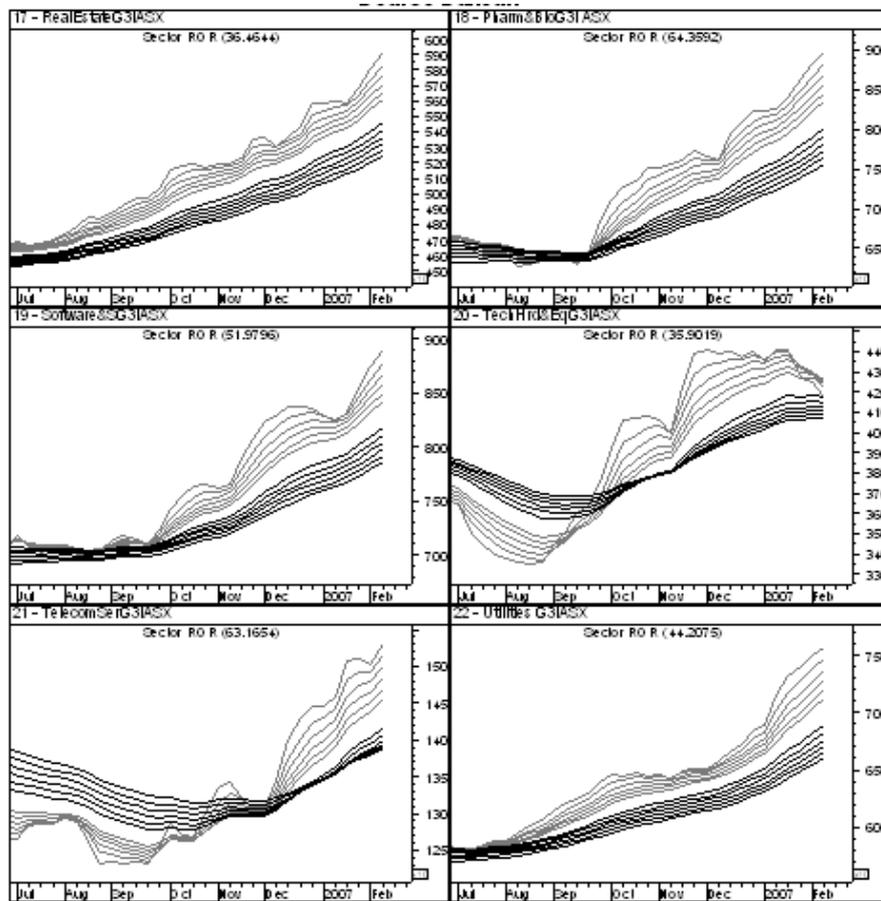
After examining the Sector MMA charts we can compile our list of rising sectors and their respective ROR values :

GICS Industry Group	ROR %
Transport	67
Pharm&Biotech	64
Software&Services	52
Utilities	44
Retailing	37
DiverseFinancials	36
Real Estate	36
FoodBev&Tobacco	31

The only change here is the Insurance Sector; we've had a close look its MMA chart and have decided to wait as the short term moving averages have just started to roll over. Only a little, but we will err on the side of caution in this case.

Looking at the share MMA charts we find that there are two candidates this week :

List of prospects showing entry criteria

Share	GICS Industry Group		ROAR%	Buy Zone
MBA	Software & Services	Up	190	in
SMY	Software & Services	Dn	147	in

We'll knock out SMY because it hasn't met all our buy criteria as it has had a down week. We'll just stick with MBA now and this is what MBA's MMA chart looks like and its values in the Data Table :
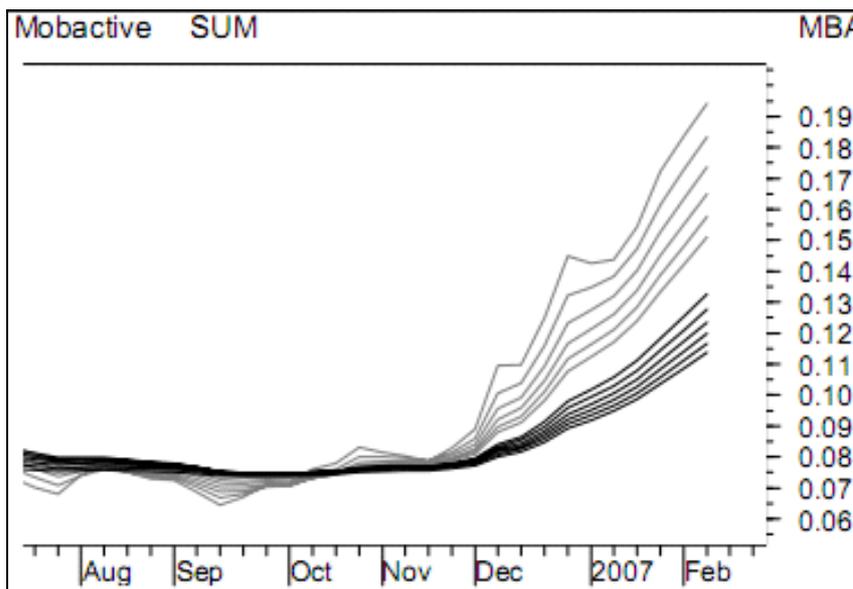
Share Code	Closing Price ($)	Central Cord ($)	Upper ($) Deviation	Lower ($) Deviation	ROAR (%)	Port. Weighting for the 2% risk
MBA	0.205	0.231	0.278	0.153	190	6

We can now go ahead and add MBA to our portfolio and to do this we need to go back to the Trade Recorder. To work out our current Total Capital, we have to enter the current values of all our open positions and we'll use the closing price in the Data Tables for this exercise.

Here's what our Trade Recorder looks like now we are ready to purchase MBA :

Using the Buy Calculator we can work out our position size and see how many shares to purchase. Once this is done, we can add MBA to our list of open positions and click the 'New week' button to save the spreadsheet. Our Trade Recorder now looks like this :

Newsletter			New Week
Cash on Hand	$52,018		*ActVest Trade Recorder*
Total Capital			*For buying shares*

| Share	Number	Price	Value
CUV	8,938		0.00
GPN	94,337		0.00
MBA	29,184		0.00
MRM	8,333		0.00
PWT	4,405		0.00
REX	4,347		0.00
			0.00

That's the end of week two, six shares in our portfolio and approximately 50% of our funds committed to the market. Now on to week 3….

Week Three

First things first as usual….check our stop losses. Again we'll make sure the weekly close is above the Lower Deviation and that the shares are actually still in the Data Tables – which means that their ROAR is greater than 80%.

All our shares are above the Lower Deviation and are indeed in the Data Tables, so our next step is to check the Cross Over charts…again. Both the All Ords and the Small Ords are crossed to the upside so we can move onto the Sectors.

We've narrowed the Sectors down quite a bit further this week. Again we've been tough on the MMA charts and this time we've ruled out the Transport, Real Estate, Pharm&Biotech and the Utilities sector as the short term moving averages are showing some early signs of weakness. Here's the MMA chart of the Transport sector where the short term moving averages are starting to roll over…just little a bit :

05 - Transport G3IASX
Sector ROR (66.4511)
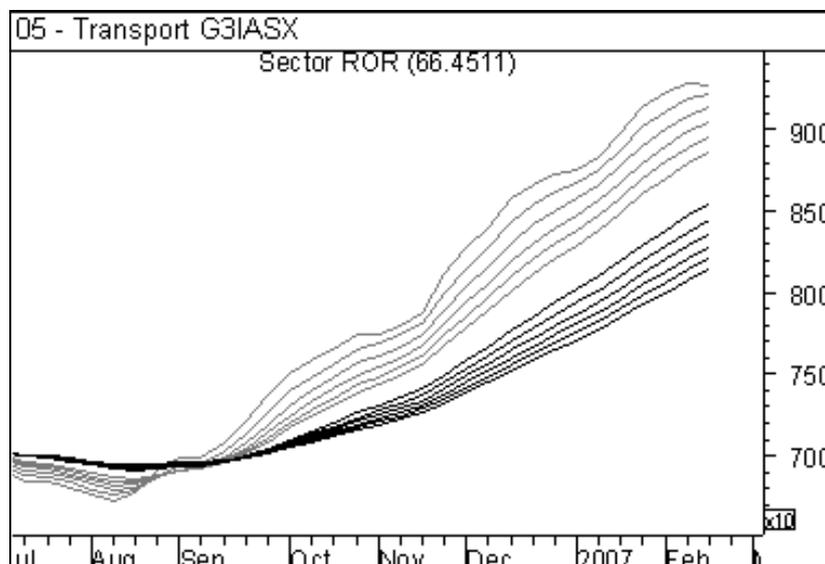
So our final list of Sectors is as follows :

GICS Industry Group	ROR %
Software&Services	52
Retailing	40
DiverseFinancials	37
FoodBev&Tobacco	31

Once we've gone through the Share MMA charts we're left with the following share...SMY:
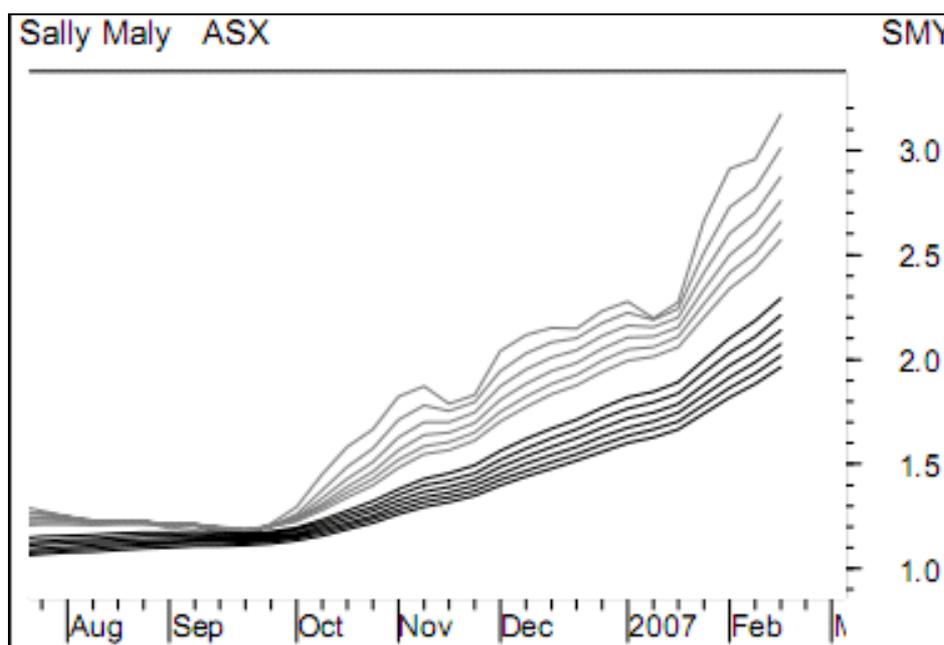
And the details for SMY are :

Share	GICS Industry Group		ROAR%	Buy Zone
SMY	Software & Services	*Up*	146	in

Here's SMY's entry in the Data Table :

Share Code	Closing Price ($)	Central Cord ($)	Upper ($) Deviation	Lower ($) Deviation	ROAR (%)	Port. Weighting for the 2% risk
SMY	3.390	3.666	4.244	2.731	146	9

Time to update the Trade Recorder with the values of our open positions so we can work out our Total Capital and then buy SMY. This is what our Trade Recorder looks like once we've added SMY and before we've cleared the Buy Calculator :

Newsletter	AT070216						Buy	Clear BUY	

Top section:

Newsletter	AT070216
Cash on Hand	$42,912
Total Capital	$101,199

New Week

ActVest Trade Recorder
For buying shares

Buy	Clear BUY	
Cash on Hand		52,018
Total Capital		101,199
Portfolio Weighting		9
Share Price		3.39
Position Size		9,108
Maximum Number		2,686
Cash on Hand - AFTER		42,912

Share	Number	Price	Value
CUV	8,938	0.85	7,597.30
GPN	94,337	0.06	5,565.88
MBA	29,184	0.22	6,274.56
MRM	8,333	1.30	10,832.90
PWT	4,405	2.27	9,999.35
REX	4,347	2.05	8,911.35
SMY	2,686	3.39	9,105.54
			0.00
			0.00
			0.00
			0.00

Sell	Clear SELL	
Cash on Hand		
Number		
Share Price		
Cash on Hand - AFTER		

Action for Week
Bought SMY 2686 @ 3.39

That's the end of Week 3. We have 7 shares in our portfolio and nearly 58% of our capital allocated to the market. Anyway, I would think by now that you're getting a good idea of what using the Active Trading strategy with the ActVest Trade Recorder is really like…

Week Four

We'll finish off this week by just checking the stop losses of our open positions and then look at the final value of our portfolio. Thus the first thing to do is to check the stop losses and we've done this and all our shares are still above the Lower Deviation and in the Data Tables.

Next, we'll use the weekly closing prices from the Data Tables to work out the value of our portfolio in the Trade Recorder. And so it looks like this :

Newsletter	AT070223
Cash on Hand	$42,912
Total Capital	$102,802

New Week

ActVest Trade Recorder
For buying shares

Share	Number	Price	Value
CUV	8,938	0.98	8,759.24
GPN	94,337	0.06	5,282.87
MBA	29,184	0.19	5,399.04
MRM	8,333	1.27	10,582.91
PWT	4,405	2.28	10,043.40
REX	4,347	2.07	8,998.29
SMY	2,686	4.03	10,824.58
			0.00

That concludes our four week trading simulation using the Active Trading (ActTrade) newsletter and so just to re-cap the process…

1. Check the stop losses for all open positions
2. Check the All Ords and Small Ords cross over charts
3. Select suitable rising sectors (using sector MMA charts and ROR values)
4. Select suitable rising shares in the rising sectors
5. Check for valid entries

Of course if you wish to subscribe to the ActTrade newsletter service then you'll find a subscription form on the last page of this manual.

General Considerations

The following points, whilst not critical for success, will undoubtedly enhance your performance as an Active Trader.

Don't 'Make the Market'

The ROAR indicator used to generate the weekly ActTrade newsletter tests market liquidity by testing money flow. The benchmark used by the ROAR indicator equates to an average daily minimum of $150,000.

However it doesn't ensure that you won't 'Make the Market' by buying or selling too many shares, thus moving share prices significantly up or down. A good rule of thumb is to ensure that your daily transactions in any market don't exceed 10% of the total volume of shares being traded.

Different Market Segments

Different market segments (ie. Blue Chip shares, small capitalisation shares, etc) represent differing degrees of risk and reward. They also have non-correlating performance which means that while large capitalisation shares are enjoying a strong rally, usually in unison with their offshore cousins, small capitalisation shares may be suffering a general decline.

So to ensure exposure to the entire market it is a wise idea to allocate capital to several market strategies that are targeted at different market segments, ie. Active Trading for small to medium capitalisation shares and Active Investing for Blue Chip shares. Furthermore, the capital allocation guidelines outlined on page 21 should always be strictly adhered to.

Fundamentals

Whilst 'Active Trading' is a technical approach (analysis of price activity), it certainly doesn't hurt to analyse a company's fundamentals as well. Our objective is to shift the balance of probability as far as possible in our favour and seeking good fundamentals as well as rising share prices will only assist us in this endeavour. Thus there is no reason why we can't analyse the market using a top-down approach and a bottom-up approach at the same time.

ActTrade Newsletter Subscription Form

The ActTrade Newsletter is updated every week and can be downloaded from:

www.acttrade.net

Subscribers also have access to the Active Trading Course Notes (which can be downloaded from the above site)

Please print all details clearly, tick where appropriate, sign, date and fax or post to:
(Signed forms can also be scanned and sent by email)

ActVest P/L
53 Grange Drive
Lysterfield
Victoria, 3156

Fax 03 9778 7062
Email : enquiries@alanhull.com

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- I, the above signed, acknowledge that I have read and understand the above.

- I acknowledge that I will at all times in the future indemnify Alan Hull and his servants and/or agents against all actions, liabilities, proceedings, claims, costs and expenses which I may suffer, incur, or sustain in connection with, or arising in any way whatsoever in reliance upon any material, information or opinions provided by Alan Hull and his servants and/or agents.

- I acknowledge that any future dealings I may undertake in any securities will be entered into freely and voluntarily and without inducement or encouragement from Alan Hull and his servants and/or agents.