

How I lost \$100,000 Trading

(SO YOU DON'T HAVE TO)



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Introduction

I would like to clarify that although the title of the book mentions my trading losses, I didn't enter into trading in the same way that some would enter into a casino. I sought professional training and mentorship.

One of my favourite mentors Jim Rohn (Who passed away as I wrote this book) said that if losers gave seminars he would attend and take good notes. He was the driving force behind me writing this book.

The trading world (despite what some may say) is not a case of one size fits all.

There are some good books out there that chronicle a diary of someone's trading (e.g. making money from CFD trading by Catherine Davey).

The period which I accumulated my losses spans approximately four years. For brevity this book is not going to be plot my progress over the whole four years.

There were some difficult times (including the breakup of my marriage) and I am a firm believer in getting to the crux of the info so I have attempted to make this book as frank as possible whilst providing as many useful kernels of information as possible (that there is something for all levels of traders).

I first became aware of Options Trading from a friend who had attended an Anthony Robbins weekend. Robert Kiyosaki mentions Options in some of his Rich Dad books but it was a friend's recommendation that set me on the Options Track.

As fate would have it was a couple of years after the recommendation that I was next exposed to Options

I was glancing through the paper one day and I saw an article about a mentor that had visited Christchurch, the New Zealand city which I was living in (but I had missed his intro evening). I saw that he was running a three day course in another city so I contacted his company.

The course was about \$3000 - \$4000 at the time and I jumped in feet first.

When I booked the course I actually asked for a hotel as I had to fly into the city for the course.

I did start the course with little due diligence but I have no regrets looking back.

I believe that when you go into a venture as long as you learn from any setbacks the setbacks (financial or otherwise) are just the training costs.

The people I met and the friends I have made during my trading life are people that I can't put a price on.

At this weekend I subscribed to a text "elert" system (that was designed to help me monitor the market from a distance), this system was supposed to send me a text when a specific option or stock reached a set price but worked to various degrees of success.

After an initial period of trading for approx three months I then enrolled for a six month mentoring program (with a trading group).

Although the book isn't aimed specifically at people who are first starting out in trading I have included a bit more detail in some areas of the book in order to enable a more

comprehensive explanation.

Layout of the book

I am a firm believer in reducing padding and as such I have tried to avoid filling the book with pictures and other memory intensive items.

Rather than just go straight into my mistakes each chapter covers some useful information followed by a section in how I used this information.

Not all of the chapters are a list of my mistakes and the losses of over \$100,000.00 are the result of failing to follow the route I should have as opposed to not knowing the route.

From October 2004 to June 2008 my trading cost me approximately \$100,000 New Zealand.

I have uses the term “Losses” for simplification (in both the title of the book and in several of the chapters) but as I have stated earlier in this section these funds have been exchanged for experiences and friendships that I may never have received had I not traded.

The main purpose of this book is to allow you to benefit from my learning’s so that you don’t have to lose \$100k.

Unfortunately no matter how many mentors and books that we experience, some of us need to make the mistakes ourselves.

The most I can hope is that if you are ever in a similar position my results will nudge you back onto the right path.

I'd like to clarify that I wasn't reckless in demolishing \$100,000 by out and out gambling.

I actually went through processes and systems to learn my craft and I hope that this comes out in this book

NB:

The figures in this book are primarily Australian or New Zealand dollars. All trade values (& brokerage) are in Australian dollars

How to use this book

Although this book is not designed to be a comprehensive course in trading I am assuming that the readers will be at various levels and as such I have tried to provide enough insight to make it accessible to all.

I have attempted to provide a layout that represents a logical progression in my initial trading.

My aim is to provide honesty and insight into the mistakes I made along the way in order that you the reader can avoid these expensive training lessons.

I have spent several years trading and would like to believe that I would have wiped out the cash a lot faster if I hadn' been doing something right.

Dependant on your current level of trading you can read this from start to finish or just dip into the relevant section that you feel useful.

I know there are traders out there with a lot more experience than myself but as some

of my errors are common trading mistakes I hope the chapters serve as a reminder to the experienced trader not to go down this road (or retrace their previous steps down this road).

Although I have highlighted some of my learning's through the chapters I hope that there are other useful snippets here.

At the rear of the book is a consolidated list of my learning's

For those that really want a condensed book and are too impatient to use the (Table of Contents) I have put my six top tips below.

My 6 Top Trading Tips

- 1. know yourself Well before you risk money trading** (Psychology is an essential key for every successful trader).
- 2. Practice good Money Management techniques** (Of the 80% + Traders that fail in the market a high percentage fail because they run out of money).
- 3. Choose your Mentors or instructors Carefully** (You need to think the same way as them to adopt their systems).
- 4. Have a set of Trading Rules and stick to them** (You don't need as many as I have in Chapter 4).
- 5. Understand the time Commitments that you will require to learn to trade successfully** (Trading is an art ,a skill and a trade).
- 6. To be a successful trader you need to consistently make profits.** (A few good trades are not enough)

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Chapter 1 Basic Call & Put Options

There is a vast variety of options trading strategies available but the basic Call and Put Options provide their basis in one combination or another.

CALLS

Purchasing a Call Option on a stock provides a binding contract that gives the buyer the Option (But not the obligation) to purchase a set quantity of a stock at a set price until a set date.

If you believed that a stock was going to go up in value but did not want to risk the full purchase price of the stock a Call option gives you leverage. You can tie in the price you want to pay for a stock without risking the whole purchase price of the stock.

PUTS

Purchasing a Put option on a stock provides a binding contract that gives the buyer the Option (But not the obligation) to sell a set quantity of a stock at a set price until a set date.

If you believed that a stock was going to go down in value and wanted to profit from this move you could buy a Put option on the stock. Once the stock goes down you can buy the stock at the new lower price and your Put option allows you to sell the stock at the earlier higher price.

Option's in Layman's Terms

I believe the analogy of a house purchase as a way of a simplified explanation of how options work is one of the best so I will use this basic premise here.

NB: The cash values are only for simplification and this will obviously work for different option and stock prices.

Case Study 1: Buying a Call Option

We see a house that is currently selling for \$100,000.

We can't afford the cash this month but think the house will go up in price so we approach the vendor with a Contract (proposal).

Our Contract states that we will give the Vendor \$1000 dollars for the option (the right but not the obligation) to purchase the house at the list price of \$100,000.

The contract is valid for 30 days and if we don't purchase the house within that period the vendor will keep the \$1000 and there is no further commitment on either of our behalf.

We have in fact purchased the equivalent of a one month Call option on the property.

If the housing market soars (in the next 30 days) and the house is now valued at \$110,000 we can exercise our option and buy the house for \$100,000.

$\$110,000$ (Current Value) – $\$1000$ (Option Price) - $\$100,000$ (Purchase Price) = $\$9000$ (Our Savings).

If the housing market crashes (in the next 30 days) and the house is now valued at \$90,000 we let our option expire worthless and buy the house for \$90,000.

$\$100,000$ (Initial Value) – $\$1000$ (Option Price) - $\$90,000$ (Purchase Price) = $\$9000$ (Our Savings).

Case Study 2: Buying a Put Option

We have a house that we are currently selling for $\$100,000$.

We think the house prices may fall but don't want to sell the house this month, we approach a purchaser with a Contract (proposal).

Our Contract states that we will give the purchaser $\$1000$ dollars for the option (the right but not the obligation) to sell the house at the list price of $\$100,000$.

The contract is valid for 30 days and if we don't sell the house within that period the purchaser will keep the $\$1000$ and there is no further commitment on either of our behalf.

We have in fact purchased the equivalent of a one month Put option on the property.

If the housing market soars (in the next 30 days) and the house is now valued at $\$110,000$ we let our option expire worthless and we can sell the house for $\$110,000$.

$\$110,000$ (Current Value) – $\$1000$ (Option Price) - $\$100,000$ (Initial Price) = $\$9000$ (Our Profits).

LEARNING 1.1 – Choose the correct option for your view of the market

Chapter 2 Training & Mentors

Initial Training

My Initial training involved an intensive three day course that left me with a comprehensive set of notes, a set of audio CD's (of the course) and a group of great friends.

I must compliment the course presenter who later became a mentor. For the great resources and training

It is interesting to note that (Just as many people pay out good money for other self development courses and do not use what they have learnt) the group that attended the weekend training consisted of approximately 50 or 60 people yet only a dozen or so traded for more than a short time. Some of the attendees never traded at all.

As my initial training had covered basic Long Call and Long Put strategies, this is what I stuck with in the early days of learning my craft.

My first trading arena was trading the Australian Stock Exchange (ASX) and there were only around seventy to eighty stocks that had exchange traded options available. Living in New Zealand meant that the time difference gave me the benefits of late starts

Of the Stocks available I only looked in depth at twenty or so stocks and actually predominantly traded only around a dozen.

There are two schools of thought in regard to restricting your trading to a small group of stocks

For:

With a smaller group of stocks it is easier to keep a track of the fundamental factors that may influence the stock price.

Limiting your trades means you concentrate in high probability returns and this can reduce your losses.

Against:

If you are restricting your trading pool with basic strategies this may limit the quantity of trades you can find that meet your entry signals.

Limited trading means limited revenue and if you are trading for a living you may not survive.

After the course the next stage of my training was paper (virtually) trading where I carried out the processes of analysis of the market for entry signals exactly as I intended to with cash trading.

Basic Entry Signal Criteria

My entry signals confirmations consisted of analyzing my chosen stocks (using OHLC charts) to look for the following:

For Call Options I wanted it to have a Higher High and a Higher Low than the day before.

For Put Options I wanted it to have a Lower High and a Lower Low than the day before.

I wanted the Open and Close to be in opposite thirds (dividing the time bar into thirds).

I wanted the trend to be a Bullish for Call Options or Bearish for Put Options

I drew in all the necessary Support, Resistance and trend lines and ask myself

Was the Bullish Higher day close to a support line or the bearish low day close to resistance? (I only proceed with the trade if the answer was YES)

(For more detailed info see my trading rules in chapter four)

I paper traded for two months before I put any money into trading. Unfortunately I made the mistake of not being a (consistent) successful virtual trader before I put skin in the game.

I made myself believe that paper trading was boring and that to get the real experience required to become a successful trader I needed to make those early cash losses that the elite traders make.

Whether or not I was trying to create a self fulfilling prophecy I succeeded in transferring my virtual losses into real losses.

LEARNING 2.1 -Ensure that you are trading successfully on paper before you switch to cash trading.

I remember my first cash trade- January 6th 2005 I bought 4 BHP \$15.00 Call Contracts

Total cost including Brokerage and ACH Fees \$1964.08

January 7th 2005 I sold the 4 BHP \$15.00 Call Contracts

Total returns less Brokerage and ACH Fees \$2215.92

Profit overnight of \$251.64 (almost 13%)

My next trade was a 40% loss with WOW so potentially I had become a victim of my earlier success.

Trading Logs

When you initially begin to trade you may have just one position open at a time but as you progress there will be times that you are still in one trade when you enter another.

Remembering that Paper (Virtual) trading is designed to be as close to cash trading as possible I ensured that I used the same systems when paper trading as I would in Cash Trading.

In my early days of trading I found trading logs a good way of keeping a track of the positions I had open as well as ensuring that I took the time to verify that I was trading by my rules.

I used a basic excel spreadsheet that I completed prior to entering a trade.

My mental arithmetic is pretty good but I ensured some checks and balances by having a few simple formulas in a spreadsheet. The formulas automatically gave me the figures for my profit and losses and also helped me to decide if a trade was worth entering.

An example of one of my trading logs

Date	03/01/08	20% Loss	\$0.23
Stock	LGL1W	10%Profit	\$0.32
Current Share Price	\$3.64	15%Profit	\$0.33
Strike Price	\$3.54	20%Profit	\$0.35
Option Type	Call	25%Profit	\$0.36
Exp Date	Feb-08	30%Profit	\$0.38
Bid	\$0.28	Resistance	\$3.84
Ask	\$0.33	Move	\$0.20
Buy	\$0.29	Delta	0.606
No Cont	6.5	Potential Profit \$	\$0.12
OI	1946	Potential Profit %	43
Amount Avail trade	\$2,000.00	Amount Per Trade	\$307.400
10% Loss	\$0.26		

Trading Logs explained

Cell	Date	The date of entering the trade. This allowed me review my trades and see not just how long I had been in a trade but back test entry signals during my trading life.
A	Stock	The Stock code of the specific option that I was purchasing of selling
B	Current Share Price	The exact price that the stock had last traded at on the market
C	Strike	The strike price for the specific stock option that I was

	Price	purchasing or selling
D	Option Type	This was either a Call or PUT (an important factor depending on the market direction).
E	Exp Date	The Expiry date of the option (A good check to ensure the trade has time)
F	Bid	The price that the market is willing to pay for the option
G	Ask	The price that the market is willing to sell the option for
H	Buy	Before the trade is placed this will be the middle of the Bid and Ask to give a rough idea of entry costs. After the trade is entered this is changed to the price paid for the option to allow exit values to be accurately assessed
I	No Cont	The number of contracts that I am purchasing or selling to enter the trade (allows estimation of trade entry costs). This will be rounded down to a whole number
J	OI	The (Markets) Open interest in the specific option
K	Amount avail trade	The amount of cash available to place in the trade as calculated as a percentage of the trading bank (In relation to the percentages allowed on our trading rules.
L	20% Loss	The value of the option when it has reached a 20% loss
M	10% Profit	The value of the option when it has reached a 10% Profit
N	15% Profit	The value of the option when it has reached a 15% Profit
O	20% Profit	The value of the option when it has reached a 20% Profit
P	25% Profit	The value of the option when it has reached a 25% Profit
Q	30% Profit	The value of the option when it has reached a 30% Profit
R	Resistance	The next price level (above the current stock price) where the stock price has consolidated. If trading puts this becomes a support level.
S	Move	The potential movement in price between the current stock price and the price at the estimated resistance level.
T	Delta	The current delta value of the option.
U	Potential Profit \$	The potential profit as a cash value

V	Potential Profit %	The potential profit as a percentage of the trade
W	Amount per trade	The cash amount required to enter a trade. If this figure exceeds the amount of cash available from the trading bank (and that meets the rules) either the number of contracts needs adjusting or the trade is off.
X	10% Loss	The value of the option when it has reached a 10% loss

NB if the price of the bid/ask/buy is \$0.28 that has to be multiplied by the number of stocks the option contract underwrites (e.g.1000) so the actual cost of the trade would be \$280 per contract

Formulas for trading Logs

My trading log is normally in a simple excel spreadsheet, I have allocated each cell a letter above and duplicated that below to clarify the formulas I have completed in each template.

Calculation	Cell	Formula
20% Loss	L	$H \times 0.8$
10%Profit	M	$H \times 1.1$
15%Profit	N	$H \times 1.15$
20%Profit	O	$H \times 1.2$
25%Profit	P	$H \times 1.25$
30%Profit	Q	$H \times 1.3$
Potential Profit \$	U	$S \times T$
Potential Profit %	V	$U/H \times 100$
Amount Per Trade	W	$H \times 1000$
10% Loss	X	$H \times 0.9$

Mentoring and Advanced Trading

After trading basic strategies for several months I decided that I would have more flexibility in my trading if I could utilize more advanced strategies.

The Mentor who I had initially trained with had a six month mentoring program which entailed learning advanced strategies, one on one mentoring and direct access to him (So I subscribed).

I could now trade advanced and basic techniques. (See chapter 12)

I realised that my psychology, wealth and risk profiles were not necessarily the same as my mentors.

This is no reflection on the skills of my mentor but a further realisation that psychology plays a large part in trading (see chapter three).

The next stage of my training involved a more intimate group that met once a month and traded live under the mentoring of our initial instructor.

We learnt advanced strategies designed to build on our initial training and also had access to our mentor on a one to one basis where required.

LEARNING 2.2 - Choose your Mentor not just on their results but also on their compatibility with your personality and profile.

It was during my six months mentoring that my mentor launched a company that provided a recommended trade service.

The system involved trades being sent out via email and text to tell you when to enter and exit a trade (The trades being chosen for us by our mentor).

What I didn't realize initially was that the way to make money was to trade all of their trades (This became apparent when the company results for the service showed a profit but I did not)

Unfortunately with a limited trading bank I wasn't able to trade all the recommendations.

Another problem was that although the service told you when to enter it were not always as ready to exit a trade.

Unfortunately we all have different risk profiles and unless someone is actually doing the trading for you it is dangerous to have someone lead you into a trade if they are not going to exit the trade under your rules.

The monthly fees for the service retailed around \$400 which meant that with a trading bank of \$10,000 I needed to make a profit of 4% a month just to cover the fees. When you add brokerage and the frequent losses a limited trading bank made the service untenable.

The recommendation service I used had no track record which limited my due diligence.

LEARNING 2.3 - If you choose to use a service that recommends entry and exit points for trades ensure that you know their track record in detail.