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# Pain and Loss Management

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***e*Research Corporation** is pleased to provide an article by Keith Richards of **VALUETREND**.

In this article, Mr. Richards views the 200-day Moving Average of the S&P 500 Index (SPX) as the key indicator to watch in order to gauge future market direction.

The article is reproduced below, beginning on the next page, or you can go directly to it at the following link: **https://www.valuetrend.ca/tear-down-the-wall/**

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Bob Weir, CFA
Contributing Analyst

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Friday, March 22, 2019

# Pain and Loss Management

By: Keith Richards (bio at end)

I have had some interesting conversations with a young business student who has taken up the study of Technical Analysis. One of the conversations we recently had surrounded the topic of selling a losing position.

My young friend has made a point of meeting various portfolio managers from different disciplines– me being one of them. One of his other portfolio manager contacts is a deep value investor with an excellent track record. However, as with most deep value managers – you have to take your lumps once in a while when your under-valued/under-loved stock becomes even more under-valued/under-loved.

Because of this problem, the manager in question does subscribe to a technical analysis research service to theoretically help him avoid too many chart break-downs. The manager in question was holding a stock that he had ridden down quite a ways. His technical analysis service had warned him to sell the stock near the beginning of this decline. The manger had declined to adhere to that advice, given that he felt the stock had far more fundamental potential than the technical advisory could see.

As the stock declined further and further, the manager felt more and more pressure to stay in the position. My young friend, who seems to be evolving into a pretty astute technical analyst, told me that he felt that this otherwise outstanding and incredibly successful manager was perhaps justifying staying in the position out of pride – as much as fundamental valuation.

The chart below is that of Kraft – which is NOT the stock this manager held—but it is a great example of the principle we are covering here. You can see the early signs of the trend rolling over from an uptrend, to a consolidation, then to a new downtrend. Lower highs, lower lows, break of the 200-day SMA. This chart tells a technical analyst everything she or he needs to know, and how to react.

Those of you who follow my blog with any regularity might know that I firmly believe that technical analysis tends to illustrate the psychology of market participants. Technical support and resistance, for example, result from past buying and selling points that stockholders pay attention to for future selling or buying opportunities. Sentiment studies provide insight on the confidence levels of the crowd – and often signal contrarian buy or sell signals based on irrational confidence or capitulation. Market breadth shows us if investors are acting irrationally by focusing too heavily on a concentrated group of stocks, rather than on a broader spectrum.

My friend currently manages his own portfolio. He must deal with his personal neurosis (we all must) when a stock fails to do what he thought it would do when he bought it. Dealing with your own neurosis is hard enough. Do you take the loss and move on, or do you hold and hope? The chart reflects the emotions and neurosis of all market participants trading that market.

Some stocks fall out of bed much more violently than Kraft did. SNC is a stock we own – our sell rules – applied to Kraft above, were not so easily deployed. But, generally, such situations are rare.


**<continued>**

CVS is a stock that we recently took a tight loss on. You can see the clear break in support, we waited 4 days to confirm it was not a head-fake, then we sold at a reasonable loss within an adequate time-frame. So far, that appears to be a good move—given the current price on the stock.


I mentioned to my young friend that, were he to eventually get into the management game, one of the things that he will eventually be faced with is dealing with his client's neurosis – in addition to his own.

Going back to our plummeting manager's stock – when a manager decides to take a loss after missing an early sell signal (and we all do this once in a while) – you must face up to your own questions of holding for a turnaround. If you don't sell, perhaps the stock continues to fall. If you sell, perhaps it rises immediately after that trade. It is tough! But you are not just looking at your trades in an isolated way. You are also a portfolio manager. And now, you have to make that call and face criticism as to your decision. If you sell, then the stock rebounds, perhaps you will get a call from a client asking why you sold it so low only to see it rise thereafter? Or, if you sell and it falls more, the same client might ask why you sold so late – couldn't you have caught this trade earlier? So, as a manager, you may be tempted to avoid the confrontation to begin with by telling clients the same story when you bought it – that is –" It is under-valued, and some day it will be a great story…"

Personally, I have made plenty of great calls and taken losses early. I have also made some lousy calls and waited too long. As I mature in this business, the early loss calls have become much better. One of the things that has afforded my ability to adhere to tighter loss control is, believe it or not, my interest in bicycle racing. When I moved out of cycling for fitness and made a serious commitment to trying to win races by dealing with a hard-core coach –I learned about pain management. Competitive athletes in many sports do intervals that replicate the pain of their event. By practicing pain management, you are ready for it when you are near the end of a race, exhausted, and still need to come up with a massive sprint or hill climb to meet the surges of your competitors.

The same goes for trading. Practice taking your losses on a system-based sell-strategy. Learn to live with the aftermath. Perhaps the stock rallies after you sell. Hopefully, you will not have that happen often if your system is logical. Nonetheless, it will happen.

By avoiding the pain of being wrong—you are going to be wrong more often than if you are willing to take logical losses. The idea is not to be perfect. It is to be more often right than wrong. I know I am still not perfect!

Hope that helps.  Have a great weekend!

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See **About The Author** below.

## ABOUT THE AUTHOR

ValueTrend Founder and Owner, Keith Richards, has been in the securities industry since 1990. ValueTrend manages over $100 million through a discretionary investment service for high-net-worth clients.

Keith Richards has been in the securities industry since 1990 and is a highly regarded member of the small, exclusive community of Chartered Market Technicians in Canada. Mr. Richard's articles appear regularly in INVESTORS DIGEST, MONEYLETTER, GLOBE AND MAIL, and the TORONTO STAR newspapers.

His appearances on BNN Television have inspired producers to acknowledge him as **"one of [our] most accurate technical analysts."** Mr. Richard's first book, SMARTBOUNCE: 3 ACTION STEPS TO PORTFOLIO RECOVERY, is available in bookstores and directly through his blog page **www.valuetrend.ca/blog/**. His second book, SIDEWAYS: USING THE POWER OF TECHNICAL ANALYSIS TO PROFIT IN UNCERTAIN TIMES was released in late 2011. He has been critical of the commission-based, follow-the-pack approach to investing – where brokers succeed regardless of performance.

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