

How do we select stocks to trade?

How do most of us select stocks to trade / invest?

Observations from a User Group

Robert Brain
August 2021

Share Market Toolbox

Price charts summarise the underlying opinions and emotions of the market participants. Every chart tells a story. It pays to understand the stories in the price charts.



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Introduction

What's the best way to choose stocks?

Should we:

- 1) Use either **technical analysis**, or **fundamental analysis** and nothing else?
- 2) Or a **mixture** of both?
- 3) Or should we focus on a preferred **market sector**? (eg, biotech, lithium,...)
- 4) Or perhaps choose a company that has a **"good story"** and hope they deliver?

eg. low PE, good PEG, rising ROE...

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Introduction

The national BullCharts User Group has been playing a **stock-picking game** this year.

About 20 people participating (they are users of charting software).

What are their stock-picking criteria?

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How do we select stocks to trade?

 **Introduction**

The results were very surprising!!

In this session Robert will divulge the many reasons for stock selection that are in use among our colleagues and peers.

Surprisingly this includes the use of both *technical analysis* and *fundamental analysis* to varying degrees.

It is assumed that these observations might be typical across many ATAA members.

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 **Introduction**

No statistics

The aim of this session is to **share the stock-picking observations.**

In this session we will not produce any statistics, nor nominate a "best method", nor judge the various stock picking methods.

There is no elaborate back-testing of methods.

But we will demonstrate some examples.
(sorry if we disappoint)

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 **Introduction**

Why is this useful?

Why is it important or useful to do this?

There are some key observations and some very useful lessons. You might be interested to hear **why** people do what they do.

This might help you feel more comfortable with what you are doing.

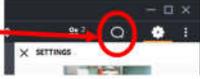
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How do we select stocks to trade?

Introduction

In this webinar we may take input...

- Feel free to ask questions via the G2M **Chat box** when prompted.



Any price charts herein were prepared using BullCharts software.

**Every chart tells a story.
It pays to understand the stories in the charts.**

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Introduction

Important Notice — No Advice!

- This presentation does not include any advice.
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- This presentation is pure education, only for your general awareness.
- There are no recommendations to take any action, or to invest any money in any way.
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How do we select stocks to trade?

Introduction

Important Notice



advice

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How to select stocks?

How to select stocks to trade*?

There are many, many ways:

- 1) Use 100% **technical analysis**;
- 2) Use 100% **fundamental analysis**;
- 3) Use a **mixture** of these two analysis types;
- 4) Focus on **tomorrow's market sector** (à la Nicolas Darvas's book);
- 5) Choose a company with **"good story"**;
- 6) And many combinations of these.



* to trade or invest

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How to select stocks?

Which method is most popular?

In our first stock-picking game – 16 players:-

- 4 players (25%) used **pure technical analysis**
- 3 players (19%) used a **combination** of technical analysis and "other"
- 9 players (56%) did not use TA at all.

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How do we select stocks to trade?

 **How to select stocks?**

Remember 4 things...

- 1) When trading/investing, there is not one right answer to stock-picking. There are many correct answers
- 2) If using technical analysis, remember it is not a 100% fool-proof science
- 3) Specific selection methods might work in *some cases* and not in other cases
- 4) Some methods might work with *some stocks* but not with others.

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 **How to select stocks?**

Some (misc) selection methods...

- 1) *"It is expected to be rising next month"*
- 2) *"Longer term, commodities likely to be strong"*
- 3) *"Platinum and palladium prices are rising" **

* – See price study shortly (ZIM)

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 **How to select stocks?**

Some (misc) selection methods...

- 1) *"It is expected to be rising next month"*
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If you do this, you are not alone. Some technical analysts might not believe it, but many people choose stocks using views such as these.


What do you think about these?
Are they useful methods?

* – See price study shortly (ZIM)

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How do we select stocks to trade?

 **How to select stocks?**

More (misc) selection methods...

- 1) "Good prospects in improving economy with more travel (post-COVID)"
- 2) "Looks good and good dividend announced today"
- 3) "Good prospects with local manufacturing and with overseas sales." *

* – See price study shortly (PNV)

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If you do this, you are not alone.
Some technical analysts might not believe it, but many people choose stocks using views such as these. *Comment?*

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 **How to select stocks?**

Some (FA) selection methods...

- 1) "Very undervalued (based on various fundamentals, eg. iron ore price)" 
- 2) "This stock has been heavily sold off and is now a Value Stock"
- 3) "Fundamentally – copper and silver prices are bullish" (so all related stocks ought to be bullish!)
- 4) "Fundamentally good with economy growing out of COVID lockdowns"

If you do this, you are not alone.
Some technical analysts might not believe it, but many people choose stocks using views such as these.

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How do we select stocks to trade?

How to select stocks?

Do these fundamental analysis based, or “assumption” based, stock selection methods actually work?



Comment?

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How to select stocks?

Do these work? – one example

In February, Bill (not real name) chose ZIM (Zimplat Holdings), a platinum producer “... in an industry expected to do well...”

How did the stock go?



Could we have spotted this with TA?

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How to select stocks?

This daily candle chart is more useful than the weekly in this instance

Increasing daily volume

Break above recent resistance

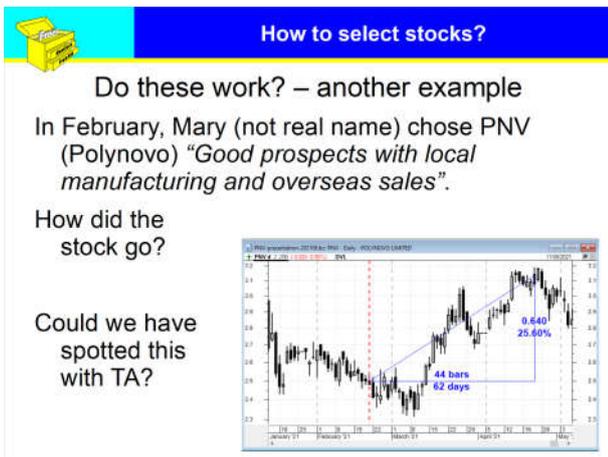


35 bars 48 days

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How do we select stocks to trade?

How to select stocks?

Longer term, this one not a good choice

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How to select stocks?

Misc/FA methods – Conclusion

1. Some people might think that these stock selection methods are somewhat hit/miss;
2. Don't forget that many “fund managers” use methods similar to all of these;
3. If the stock does not perform => opportunity cost;
4. Many retail investors are conditioned to accept losing positions;
5. Many investors “enjoy the *journey*”.

Comment?

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How to select stocks?

Technical analysis stock selection methods:

- (A) Based only on price*
- (B) Based on TA indicators

* – In his book(s), Leon Wilson refers to this as *Primary Analysis*

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Technical analysis methods

(A) Based **purely on price**:

- Price bottomed and now rising (uptrend)
- Rising Trend Channel
- Price chart "parabolic"
- Elliott Wave



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How to select stocks?

Technical analysis methods (p2)

(B) Based on TA **indicators**:

- Moving Average
- Moving Average cross-over
- MACD – "crossing Above"
- RSI oversold
- OBV (On Balance Volume)
- ADX/DM (Average Directional Index)
- more next slide...



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How to select stocks?

Technical analysis methods (p3)

More based on technical analysis **indicators**:

- Donchian Channel
- Jim Berg Volatility Profit Taker (Start signal)
- Price ROC (Rate of Change)
- Count Back Line (CBL)
- Heikin-Ashi indicator.



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How to select stocks?

Observations

1. Many/most of our traders actually use more than one of these technical analysis indicators for their stock selection (sometimes two, three or four)
2. They have observed the indicators over time, and understand them fairly well
3. And/or they have done some back-testing to confirm the approach, and gain some confidence in the method.

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How to select stocks?

How do these work?

The technical analysis indicators on the previous slides can be used for purchase/entry decisions:

1. Based on "bullish observations" (eg. a specific candle pattern, or "rising Moving Average", or "MACD cross Above from below zero"); and/or
2. One or more very specific trading/entry setups and signals.



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How to select stocks?

How do these work? – eg. MACD

Bullish observations: "MACD crosses Above from below zero"



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How to select stocks?

How do these work? – eg. RSI

Bullish observations:
"RSI rising when below 50"



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How to select stocks?

Observations

Why do people choose the stock-selection method that they use?

1. Enjoy the *journey*
2. Influenced by their own "belief system"
3. Influenced by *cognitive biases*.

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How to select stocks?

Observations

Why do people choose the stock-selection method that they use?

1. Enjoy the *journey*
2. Influenced by their own "belief system"
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**Why do you trade the way you do?
Do you have preferences?**



Comment?

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How do we select stocks to trade?

 **The journey**

The *journey*

This is a related and very interesting topic

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 **The journey**

The *journey*

When we look around at how other people trade the markets, and we notice their particular preferences, styles, methods, etc., we might wonder **why** they do it the way they do it:

- The activity might involve some sort of research, and they enjoy doing the research;
- They enjoy engaging in discussion with their friends and colleagues about their topic (ie. “talking shop”);
- It's the *enjoyment* of all this and more.

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 **The journey**

The *journey*

Think for a moment about people's favourite hobbies or sporting interests:

- Stamp collecting (or coins, etc.)
- Playing sports like: hockey, lacrosse, soccer, football, diving, marathon running, etc., etc.
- Power boat racing (expensive)
- Motor car racing (as a participant).

Surely they enjoy the experience.
It's one way to watch the time go by.

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How do we select stocks to trade?

 **The *journey***

The *journey* – for real estate investors

Think about this for a bit.

Consider the typical real estate investor (house, or commercial, retail, etc.).



This is an activity that can take a lot of research, discussions with friends and experts, and visiting locations.

Then making the purchase, perhaps by auction. Some people thrive on this activity.

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 **The *journey***

The *journey* – for commodities...

Think about this *journey*, and consider the research for commodities, miners, etc.

- Follow commodity prices (generally, or specific)
- Keep up to speed with some mining companies (explorers, miners, processors, producers);
- Read and absorb the reports;
- Visit special expos and conferences;
- Trained geologists would love this.

Some people really enjoy this activity.

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 **The *journey***

The *journey* – for travel industry

Think about this industry and consider the research for this:

- Airline stocks; railway stocks; tourist cos; cruise ship stocks; etc.
- The willingness of countries to have tourists
- The issues affecting tourism in specific countries

Some people really enjoy this research activity.

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 **The *journey***

The *journey* itself

All this applies to other industries and market segments:

- Biotech stocks
- Fintechs (eg. Afterpay, bnpl stocks, etc.)
- Technology stocks

Looking for opportunities in a field that we “like”
The research activity can be enjoyable
This might short-cut the search for the next stock.

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 **The *journey***

The *journey* can be fun and enjoyable

Looking for one particular market, industry, sector, whatever, and then following that choice can be: enjoyable, fun and possibly very rewarding

Many traders/investors learn about only a few specific companies and follow them diligently

Then, the choice of when to buy-in is another story.

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 **Summary & Wrap up**

Summary

In this session we:
shared the stock-picking observations from a share trading game.

Hopefully some of these observations and lessons were useful.

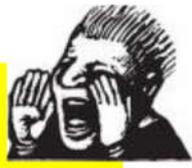
This might help you feel more comfortable with what you are doing.

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 **Summary & Wrap up**

Q & A ?

Any questions or comments? 

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 **Summary & Wrap up**

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- My contact details:
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 **Summary & Wrap up**

THE END

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