TAKING LOSSES

I came across the piece below a few months ago and, whilst it's specifically about stock, rather than currency, trading, the principles are still applicable to our business. I read this each week to drill it into my subconsciousness in an attempt to make taking losses easier – it seems to be working though it's still a difficult thing to do. I hope it helps you as well.

This article comes courtesy of Marcus Padley who writes a daily Australian stockmarket newsletter call MARCUS TODAY – you can sign up for a free two week trial on www.marcustoday.com.au

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Losses have three times the emotional impact of a gain. It is three times harder to sell a stock at a loss than a profit. The tech wreck taught us how to adjust for this… use stop losses. This is the only way to take the emotion out of trading. You have to have a rule… if the stock falls 10% from the top, I'll sell. If I'm down a grand, I'll sell. You just need something to short circuit your emotional response (close to impossible). Consider this though… when you are physically sweating at your loss, when you are concerned that this one is so bad you can't tell your spouse, are you in any fit state to be making a decision? No, so you need a rule or a mechanism so you have no confusion about what decision to make and when. You will find that loss taking is very cleansing.

It is one of the hardest things for brokers to convince themselves of, let alone persuade a novice trader to take a loss. We have developed arguments to persuade you (they don't seem to work on ourselves). They include the following. If ever you are having trouble taking a loss, if ever you are not enjoying your trading, or getting emotional and still hold the stock… read this list. You will have put the sell order on before you get to the end:

- If a stock is going down, it is far more likely to continue going down than it is to turn on a sixpence to suit you.
- The further a stock falls, the more intense the selling becomes as higher losses cause more selling decisions. So sell early… an early loss is the smallest loss.
- If you sell 10 falling stocks, as any technical trader will tell you, it will be the right thing to do in 9 cases… but you will only remember the other one.
- If you sell now, you are no longer exposed… all you have to do is come to terms with the loss.
- If you sell now, you can always buy it back… and who knows, you might buy it back lower than you sold it.
- If you sell now, you enter the eye of the storm. All becomes calm. You have a moment to think. You can watch from a distance and think. You can always choose to enter the storm again and if you do, you will be thinking more clearly and be armed with a plan.

- If you are making a loss on a stock, think to yourself… if I had cash, would I buy this stock now at this price… no?... then why are you holding it? Sell it. (Most people begin to 'hate' the stocks they lose money in… so this argument always works).
- Your state of mind has a value. What would your spouse pay (or you pay) to have you carefree at the weekend instead of ripping the heads off the kids.
- Look after yourself… there are not that many weekends in the year or your life… don't ruin too many of them by keeping risky loss making positions until Monday because you didn't have the guts to sell them on Friday.
- Averaging down is a mug's game. If you have money to invest, you should be putting it in the best investment in the whole world. Do you really think that that is going to be the very same stock you have already bought at a higher price and that is falling at the moment… very, very unlikely. You already have an exposure as well… why do you need more of something that has already proved itself to be a dog.
- Averaging down is what broker's advise you to do to distract you from the fact hat they have put you in something that has lost you money. Do you really want to turn a short term trade into a long term loss. Every day you see it in your portfolio. Every day it will be flashing "you idiot". There is a value to avoiding that.
- The quickest way to become a long term investor is to make a short term trade and get it wrong.
- There is no logic in being emotional about losses. Do what most brokers do with their own shareholdings. They have an excel spreadsheet linked to live prices monitoring all their holdings and what they are worth. At the bottom of the page is a total of what all the holdings are worth now. That clicks over every second all day. Up $500, down $500. This figure is the only truth. This is what the shares are worth. What you paid for the shares is irrelevant… so why care about whether it is a profit or a loss. It is an amount of money. If it's gone, it's gone, period… it is no more likely to come back because you paid a higher price. (There are still clients who will tell you they have $50,000 in Telstra when the holding is worth $25,000. You do not have $50,000 in Telstra, you have $25,000).
- Most clients who have loss making stocks will tell you that they "hate XYZ". So why hold it? Far better to put the cash in something that you want to wake up to in the morning than something that depresses you.
- If in doubt, sell it… it crystallises a capital loss and you can always buy it back.
- If you have paid capital gains tax whilst having unrealised capital losses (because you couldn't sell at a loss), then you really are a mug. Take them.