



THE WILEY TRADING GUIDE

VOLUME II



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THE
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Ray Barros is a professional trader, fund manager, author and educator. Ray closed his private hedge fund in December 2010. In 1990, he started with A\$20 million, and by the time the fund closed it had grown to A\$943 million. The December 2010 result was the best in his trading history, securing a 137 per cent return.

Ray is also the author of two books: *The Nature of Trends* and *The Ray Wave*. Ray has been regularly featured in regional newspapers and publications such as the *Singapore Strait Times*, the *Sydney Morning Herald*, *Your Trading Edge* magazine, *Singapore Business Times* and *AFR Smart Investor*. He has also been featured on BBC (Asia), CNBC, Bloomberg, Channel News Asia and a number of Indian TV stations; for example, Channel 18 (CNBC Indian Affiliate) and UtV-Bloomberg. In addition, Ray has given public and in-house seminars in Sydney, Singapore, Bombay, Shanghai, London, Tokyo and Taiwan.

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Many of the long-term social, political and economic forecasts Bernstein has published in the last two decades have come to pass. These include the interest rate top of the early 1980s; the deflation of the 1980s and early 1990s; the Japanese economic peak; the explosion in genetic engineering technology; the interest rate lows of the mid to late 1990s; the Gulf War; and many more.

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Jeff has educated tens of thousands of people in Australia and New Zealand about trading and investing through presentations for E*TRADE, CMC Markets, Cube Financial, Trading and Investing Expo and Pavilion Securities.

Over the last 10 years of being involved in the financial markets Jeff has been featured in and written articles for the *Sydney Morning Herald*, *Brisbane Daily Mail*, *Your Trading Edge* magazine, *Smarter*

Investor, Wealth Creator magazine and the Compare Shares website. Jeff and Ashley Jessen have created the website <www.learnCFDs.com>.

Jeff implements a wide variety of investment strategies that include investments in property, stocks, commodities, currencies and CFDs both in Australia and in global markets. Jeff is one of Australia's leading experts in trading chart patterns.

John Christian

John Christian is an internet entrepreneur with a focus on the Australian investment industry. John founded TopStocks.com.au <www.topstocks.com.au> in 2005 and built it to one of Australia's largest stock discussion and research websites and a HitWise™ top 50 website for the Australian financial sector (including banks and brokers). In 2006, John founded StockScan <www.stockscan.com.au>, a popular online stock scanning website, and in 2011 John founded SPOTMEX <www.spotmex.com>, an online physical gold and silver trading platform.

In addition to his technical skills, John is a seasoned trader with over a decade of experience in the international currency and commodity markets. More recently, John has been focused on the precious metals market as both a long-term investor and short-term trader. His work in this market has been referenced by the titans in the industry, such as Ted Butler, David Morgan and Bob Chapman. John offers exclusive commentary to thousands of precious metal investors via YouTube.

John has a bachelor of Information Technology majoring in Software Engineering from Queensland University of Technology.

David Hunt

David Hunt has been trading and advising for over 26 years. His experience includes corporate treasury, funds management, private trading and bank proprietary trading in foreign exchange, futures, shares and commodities, including work for Qantas and Macquarie Bank.

With a passion for trader education, David has trained with many of the best in the world and brought many of them to Australia.

He is a popular guest on the Business Channel and a *Smart Investor* magazine contributor. The *Australian Financial Review* calls him the Bellringer.

He is a past president and co-founder of the Australian Professional Technical Analysts Association (APTA), and co-founded the Australian Technical Analysts Association (ATAA). David co-created the Finsia/Kaplan/SIA Technical Analysis course.

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Since 2009 he has market calls on ASX forex, commodities, world and US indices and shares for the Profit Hunter Group of financial planners, funds managers, bank traders, stockbrokers, private traders and investors. His market calls incorporate his 26 years' experience in risk management, price projections, market timing, trade management and trading psychology for his Profit Hunter group <profithunters.com.au>.

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Ashley Jessen

Ashley Jessen was one of the first 10 traders to open a CFD account when they first launched in Australia, having originally traded stocks and options. Ashley is an experienced and successful trader with specialised knowledge in the trading and educational fields.

Ashley is an expert teacher, having taught tens of thousands of everyday traders how to plan, construct and implement winning trading systems and get back to the basics. He has also personally coached over 400 traders, one on one, on how to get the most out of their trading methods and mindset.

Making the transition to CFDs and trading full time was simple, and together with three trading colleagues Ashley set up and managed a trading office in Bondi Junction overlooking picturesque Sydney Harbour. It was at this stage that Ashley learnt what it's like to eat, sleep, breathe and live the markets on a full-time basis.

When not trading, Ashley has been instrumental in helping grow some of Australia's largest education and trading companies, including Metashare International, HomeTrader, CMC Markets and MF Global, from sales and marketing manager all the way up to running a state office.

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Dr Kacher is the co-author and publisher of *The Virtue of Selfish Investing* <www.selfishinvesting.com>. Dr Kacher launched one of the first internet-based stock advisory services in 1995. He then went on to generate triple-digit percentage returns for six years in a row during the 1995–2000 period, before moving to cash for most of the 2000–2002 bear market, one of the worst in history. From 1996 to 2001, Dr Kacher served as stock market research analyst for William O'Neil + Company. During this period, William O'Neil

hand-picked Dr Kacher to manage a portion of the firm's proprietary capital, whereupon Dr Kacher became a top-performing internal portfolio manager at the company. Along with Mr Gil Morales, Dr Kacher is currently a Managing Director of MoKa Investors, LLC, a registered investment advisory firm.

Dr Kacher received his BS in Chemistry and PhD in Nuclear Physics from University of California at Berkeley, where he was awarded the Berkeley Graduate Fellowship Award and the American Chemical Society award for excellence in undergraduate research. He co-discovered element 110 on the periodic table of elements and confirmed the existence of element 106, which his team named Seaborgium after Dr Glenn Seaborg who supervised Dr Kacher's work as a doctoral student at UC Berkeley.

Roger Kinsky

Roger graduated from the University of NSW with a bachelor's degree in engineering at the age of 20, and after working for few years in Australia decided to 'see the world'. After a stopover in the South Pacific, Roger worked for five years in Great Britain and the United States. On returning to Australia Roger adopted a career in management, then joined the Department of Technical and Further Education (TAFE). Roger obtained a master's degree from Sydney University, and he remained with TAFE for 27 years before retiring to the south coast of New South Wales, where he's active trading shares and managing his extensive share portfolio, as well as writing books and organising and conducting training courses. He's been a tutor with Sydney University of Technology and Sydney University, a consultant for industry, a guest speaker at investor conferences and has appeared on ABC radio discussing shares and share investing. Roger has been investing and trading shares for about 40 years and is a successful author of 14 books on a variety of topics, including share investing and trading, engineering mechanics, thermodynamics, fluid mechanics and management. Four of his books have been published by John Wiley & Sons: *Online Investing on the Australian Sharemarket*, the best-selling *Teach Yourself About Shares*, *Shares Made Simple* and most recently *Charting Made Simple*.

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Delia Langdon is Chief Analyst at The Inside Trader, one of Australia's largest and most well respected online share research companies. She has been at The Inside Trader since 2002, and, together with Keith Nielsen, has expanded the company from a small research firm to one of Australia's leading online share market advisory services. She has a practical, commonsense approach to share trading and has a particular interest in following company director's trades. She shares this knowledge with clients on a daily basis and is often called upon by various Australian journalists to comment on this topic and others. Delia is particularly passionate about supporting people new to share trading, providing them with support and simplifying what can be quite a daunting task: understanding the concept of share trading. Delia has a Diploma of Financial Services from FINSIA and is currently completing a Graduate Diploma in Applied Finance.

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Mark graduated from King's College London in Special Physics. He was awarded the Bronwen Wood Memorial Prize in Technical Analysis by the Society of Technical Analysis (UK) in 2007. He also holds the CFTe designation from IFTA (USA). Mark's expertise includes stocks, CFDs, futures and options. He conducts a range of technical analysis and proprietary trading masterclasses and live webinars on intermediate to advanced profit extraction methodologies for directional and non-directional trading, some of which include vibrational, bidirectional, reactional, formational, exclusional and transformational techniques. He is the author of *The Profitable Art and Science of Vibratrading* under the Wiley Trading series. Mark also teaches traders how to profit from pure randomness via his stochastic maximisation techniques.

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Internationally accredited as a Certified Financial Technician, Regina is president of Australian Professional Technical Analysts, is a former director of the Australian Technical Analysts Association, a 30-year member of the STA (British Society) and is a director and immediate past journal director for the International Federation of Technical Analysts.

Her freelance consultancy work includes report writing for research companies and broking houses and regular columns in the financial press, notably *The Financial Review*, the 'Smart Investor' section of the *Sun Herald*, the *Sunday Age* and *Australian Resources and Investment* magazine. She is also the author of *Charting, An Australian Investor's Guide* (Wrightbooks, 1999).

Regina's company, Your Technical Analyst, provides private tutoring and larger seminars, training investors and traders in market psychology, CFD and share trading and technical analysis. She runs webinars for traders and investors on stocks and current market trends.

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2100 per cent over eight years in the firm account, and manager of the O'Neil Institutional Services group responsible for advising over 500 of the largest and most successful institutional investors in the world, including mutual fund, pension fund and hedge fund clients. Mr Morales also co-authored with William J O'Neil a book on short selling, *How to Make Money Selling Stocks Short*, published by John Wiley & Sons in 2004. Also in 2004 Mr Morales was appointed chief market strategist for William O'Neil + Company, Inc. Along with Dr Chris Kacher, Mr Morales is currently a Managing Director of MoKa Investors, LLC, a registered investment advisory firm. Mr Morales received his BA in economics from Stanford University.

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Keith Nielsen is the founder and CEO of The Inside Trader, one of the very first online stock market research companies in Australia. His main strength is looking at the market from new perspectives to achieve above average results. He is the inventor of the now famous Nielsen supply demand indicator and smart money indicator. Over the last 12 years he has published books, hosted his own radio program, written regular columns for major magazines and newspapers as well as continuing to develop new tools for The Inside Trader.

Over the last four years he has moved his attention to automated trading and has dedicated his time to perfecting hands-free, profitable trading systems in the forex market. He is now one of the world leaders in this new field and is a member of an exclusive team of developers with the same aim.

It's the challenge that excites Keith, and the stock market and forex markets give him plenty of challenges. They are his passion.

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Colin Nicholson BEc, SF Fin has traded and invested in the Australian stock market since the mid 1960s. He created one, and wrote most of a second, technical analysis subject for the Graduate Diploma in Applied Finance and Investment with what is now the Financial Services Institute of Australia (FINSIA). He subsequently

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Colin is a past president and honorary life member of the Australian Technical Analysts Association (ATAA) and remains active on the council of the Sydney chapter. He is also an active member of the Australian Investors Association (AIA). He has been a frequent presenter at national conferences for the ATAA and AIA and their meetings around the country. He has been invited as guest instructor at four of Dr Alexander Elder's Traders' Camps.

Colin has written five books. He has also written hundreds of articles and columns for *Shares* magazine, *Smart Investor* magazine, *BRW*, the *Australian Financial Review* and the *ATAA Journal* among others.

Colin is now an investor, but his techniques and ideas are readily applicable to trading and he has taught them to traders ranging from beginners to experienced.

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John Person is a 32-year veteran of the futures and options trading industry. He started on the floor of the Chicago Mercantile Exchange in 1979. This was the premier exchange which launched foreign currency trading. He then had the privilege of working with George Lane, the innovator of the stochastic indicator. John has worked his way through the industry as an independent trader, broker, analyst and branch manager for one of Chicago's largest discount/full service firms under the direct supervision of a former chairman of the Chicago Board of Trade. He is the former owner and president of First National Futures Group, Inc. and is continuing his work as a registered Commodity Trading Adviser. John has shared his wealth of knowledge in the field of technical analysis, his trading style and system development and has taught thousands of traders, including members of the largest exchanges. He is the author of three nationally and internationally popular trading books as well as two trading courses and a DVD seminar series. John is widely quoted by CBS Market Watch, Reuters and Dow Jones Newswires, and appears regularly on CNBC. He is a sought-after speaker for

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Chris Shea

Chris Shea has over a decade of experience as a coach of traders. As a coach Chris uses his experience as a cash flow trader and as a success therapist.

His emphasis is on assisting clients not only to overcome their internal barriers but also to develop and implement their own successful probability-based approach to achieve consistent superior returns.

While Chris has worked with institutional and hedge fund traders, he has in the last few years focused on his internship program whereby he expands private traders into successful professional traders. Chris has a unique incentive arrangement whereby his payment is a share of the profit generated by his client. If the trader doesn't profit, neither does Chris.

Chris's goal is not to be the best-known trading coach; rather his goal is to be the highest paid trading coach. This will be achieved through the expanding success of his team of clients.

Chris is the author of *Licensed to Profit by Trading in Financial Markets* (Wrightbooks, 2007) and is a contributor to *Your Trading Edge* magazine.

Chris holds a Bachelor of Education, Master of Science as well as a Diploma of Professional Counselling.

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Preface

The Wiley Trading Guide Volume I has become a valuable resource for traders of all levels of skill and experience. In fact, it's proven so popular that we've decided to do it again. In *The Wiley Trading Guide* Volume II you will once again find contributions from 17 of the finest traders and market educators from around the world. These authors have a range of different skills, experience and areas of expertise, and have all developed their own methods for succeeding in the markets over many years. In this book they share with you their techniques, wisdom and invaluable insights, helping you along the road to becoming a consistently profitable trader.

No matter what your trading interest you are sure to find valuable information in these pages. Equities, derivatives, small caps, currencies and commodities are all examined; trading strategies, day trading, position sizing, psychology and plans are addressed; and a range of analysis methods are considered.

Achieving success in the markets requires learning from those who have been there before, who have faced the many challenges that the markets can offer and emerged battle-tested and profitable. It can be a perilous journey, and the uneducated trader will not succeed.

We feel privileged to again be able to share the experiences of skilled and inspiring traders with you, and sincerely hope that *The Wiley Trading Guide* Volume II becomes a source of education, motivation and guidance for you on your own trading journey.

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Planning to succeed

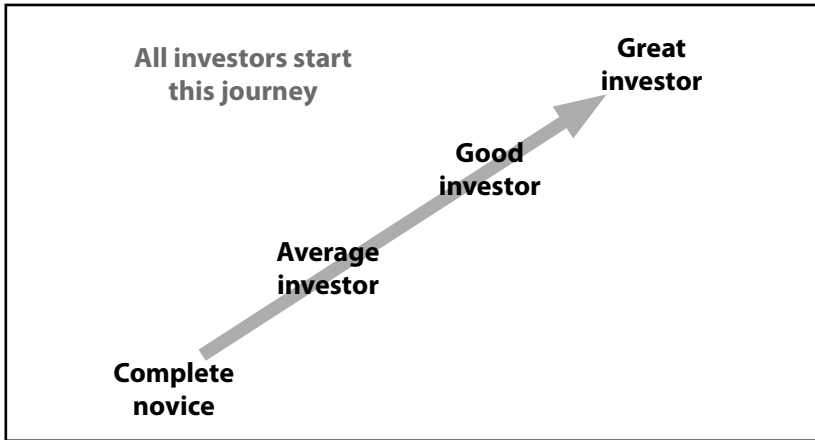
Your journey from novice to great investor

Colin Nicholson

As investors, we all start one day on a journey. At the beginning, we are complete novices. Many of us will be overwhelmed by the enormity of the learning process ahead of us. However, some of us will persist. If we stick at it, we will make the difficult transition into average investors. Then, with the application of more time and effort, a smaller number of us will progress to being good investors. From that point, the going becomes very difficult, as a small minority of good investors apply themselves to the necessary disciplines to one day become great investors. At this level making money is no longer an objective, it is simply a way of keeping score of our ability to beat the market. Figure 1.1 (overleaf) shows the journey.

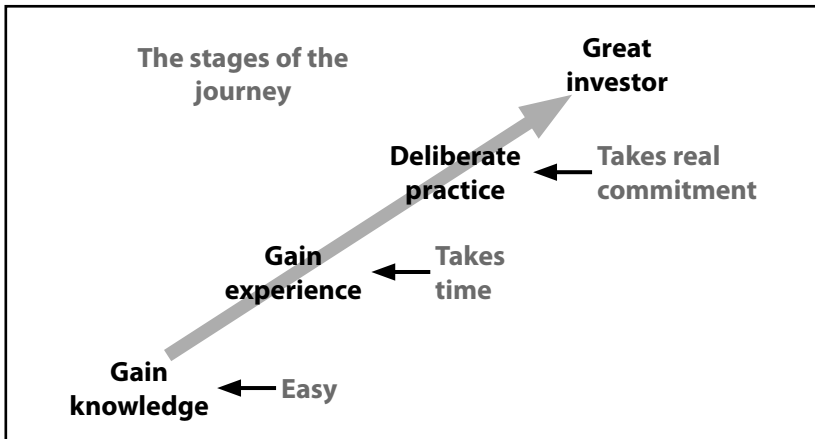
From wherever we are on the journey as we read this chapter, there is a path to greatness if we are prepared to devote the time and to make the effort. It will be a long and demanding journey in terms of thinking through the issues and being prepared to change the way we think and do things.

Figure 1.1: the investor journey



Very few of us will follow the path right to the end. However, going as far as we wish to go is beneficial. Figure 1.2 is another way to see what is involved.

Figure 1.2: what's involved in the journey



In my experience there are eight steps to becoming a great investor:

- 1 Learn how markets work and how to assess investment opportunities.
- 2 Create a written investment plan.

- 3 Gain experience by putting the plan into action and modifying it as necessary.
- 4 Track results against the objective of the investment plan.
- 5 Record investment reasoning in a journal at the time that each decision is made.
- 6 Evaluate decisions made in the investment process against the investment plan.
- 7 Identify aspects of the investment process that require improvement.
- 8 Devise and carry out a program of deliberate practice of these aspects.

Novices are only starting out: they achieve poor results

Novices are investors who are just beginning their investment journey. We all start out with the idea that investing must be easy. This is often because we hear friends talk about their successful investments. These are what we call *war stories*. They are always about successful investments and are designed to boost the reputation of the storyteller. This gives novices a completely unbalanced picture of investing because hardly anyone will willingly talk about the many other investments they have made that resulted in losses. Moreover, novices will never hear others tell what their overall portfolio return has been over the years, because most people do not calculate it.

As soon as we step onto the investing path as novices, we slowly begin to appreciate just how much we need to learn. Our first step might be to read one book. This will usually have been written to tell us what we want to hear, which is that investing is simple and easy if we just follow the methods of the author. Nothing could be further from the truth. However, as we start investing we soon begin to wake up to the real world of investing, which can be very complex and is far from easy. We may read more books and become more and more confused as different methods are proposed. Many of us will decide that we are not prepared to put in the time and

effort to move along the path to the next stage. Those who give up completely at the novice level will turn to professionals to guide their investing decisions. This is a smart choice.

Average investors are well on their way: they achieve average results

Those of us who persist will realise at some point that we are setting out to learn a new profession. This will take us at least 10 years, as we gain the knowledge and develop the experience needed to make effective progress on our investment journey. This is the usual time to learn any similar profession. It took me much longer because I could not devote myself to it full time as a student would do. Ideally, we will undertake some formal education, avoiding expensive seminars and trading software. If we try to teach ourselves, it is likely to take even longer than a decade. Our goal is to reach the next stage on the investment journey, which is to become average investors.

As average investors, we will have begun to deepen our knowledge about how to assess investment opportunities. This should involve basic fundamental analysis and the elements of charting and technical analysis, both of which will have been integrated into our investment plan. Most of us will start investing before we have formulated an investment plan, which will evolve as we go along. The best of us will progress to the point where we have written down a complete investment plan. Our final step will be to start consciously putting our plan into action.

Good investors go a lot further: they achieve superior results

Good investors who have a strong desire to improve their investment performance will have formulated a written investment plan that is complete in every respect, suits their unique temperament and life experience and has been tested in the market over at least one complete bull–bear cycle. At this point, we will be ready to begin the more challenging part of the investment journey into becoming good investors.

To become good investors we need to integrate three further steps into our investing. At this stage of the journey, we will typically not know how our investing has panned out until we do our tax return at the end of the financial year. To move to the good investor level we need to be tracking our investment performance accurately against our investment plan throughout the year. This is the easy part of this section of the journey.

The tougher steps are to begin recording our analysis and thinking behind decisions at the time that we make them. This must be done at the time we make the decisions to avoid hindsight blurring our memory, which is what happens if our journal is written up after the event.

Our final test in this stage of the investment journey is even more of a challenge. We need to begin to evaluate our investment decisions from our investment journal against what we planned to do in our investment plan. This will prompt a lot of deep reflection and ongoing modification of our plan.

Great investors go all the way: they achieve outstanding results

Very few good investors among us will have the desire to attempt the climb to the summit. Typically, we will have come to the realisation that the problem is no longer that our investment plan was wrong. In fact it will already be very strong if we have climbed this far up the mountain. What we now need to face up to is that the last leg of our ascent to greatness in investing is all about working on the way we perform in trying to follow our plan. The final part of the previous stage in our journey will have exposed that we do not always follow our investment plan faultlessly. Now we must come to terms with how to change our own investment behaviour.

To do this and reach the summit involves the supreme effort for us as investors. From our evaluation of our investment performance against our plan we will start to identify those aspects where we need to improve. From this we will devise a series of programs aimed at working on these problem behaviours. Having done that, we engage in ongoing deliberate practice to develop and embed those skills.

Like all elite performers in any field this will be an ongoing effort for the rest of our investing lives.

Not everyone will have the desire and dedication to try to reach the summit of investing skills. However, these ideas are still useful if we aim for lower levels and decide not to try to go beyond them.

At this point I will declare that I believe I have reached the level of a good investor. I am starting out towards the summit of great investing. I have studied what I think I need to do. During the remainder of this chapter I will discuss the key steps to becoming a good investor and outline what I think needs to be done to become a great investor.

Step 1: Learn how markets work and how to assess investment opportunities

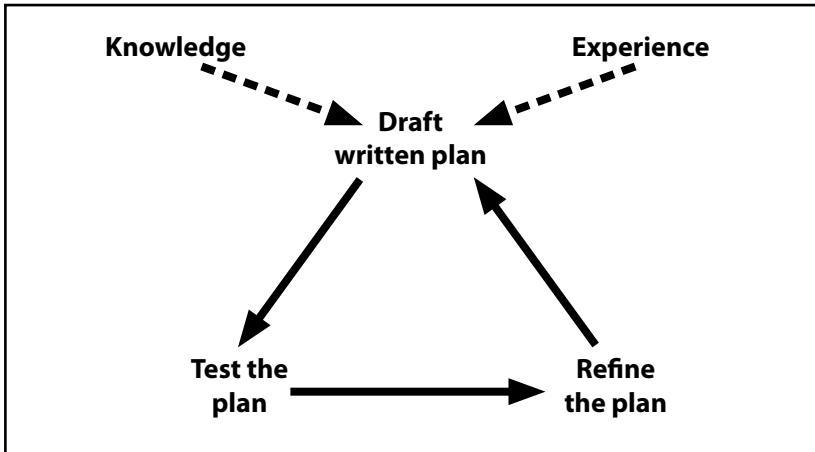
I am going to assume that, as novices, we have begun to educate ourselves about the kinds of securities we might invest in, the way the relevant investment markets work and the basics of analysis. This is ideally done in a formal setting, starting with the free resources provided by the Australian Securities Exchange. This should move on into industry education, avoiding expensive seminars and trading software. Personally, I completed my formal education at post graduate level through what is now the Financial Services Institute of Australia (FINSIA), whose courses are now provided externally by Kaplan. After completing the qualification, I went on to devise two courses for FINSIA and to teach both fundamental and technical analysis. This was immensely valuable and underlines my experience that if we wish to deeply understand something we should teach it, at which point we will find out how little we truly and deeply understand.

Step 2: Create a written investment plan

Creating an investment plan will require that we have achieved some level of knowledge and have some experience in investing. Those ingredients are essential to drawing up the initial draft of

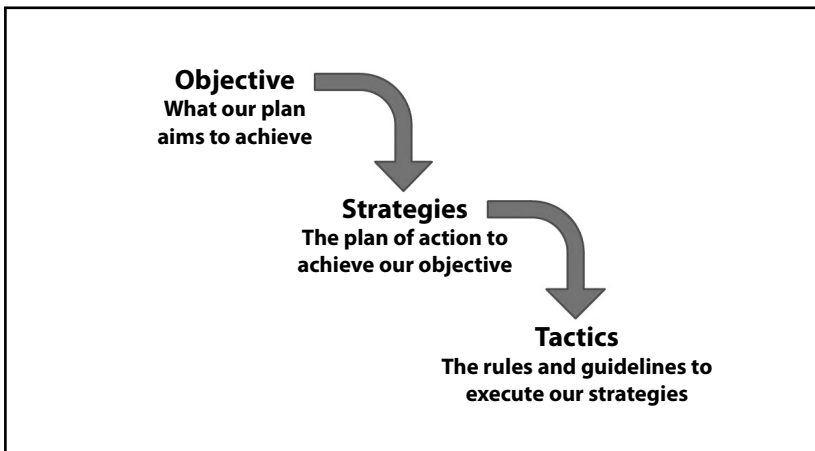
our plan. Once the plan is drafted, there will be an ongoing process, probably over several years. We will test our plan in the market. We will use this experience and our studies to think through how our plan might be refined, as shown in figure 1.3.

Figure 1.3: refining a plan



My preference for structuring an investment plan is that it would consist of three overall sections, as shown in figure 1.4.

Figure 1.4: structure of an investment plan



The detailed headings within the sections of our plan will be:

Objective: Our required level of saving and the rate of return on capital that we need.

Strategies: The risks to be managed and our chosen methods for doing so:

- economic cycle or market risk
- specific risk
- financial risk
- liquidity risk.

Tactics: How we will select and manage our investments. This will be in two sections:

Selecting investments:

- asset allocation
- security selection
- analysis methodology
- valuation matrix
- timing models.

Managing investments:

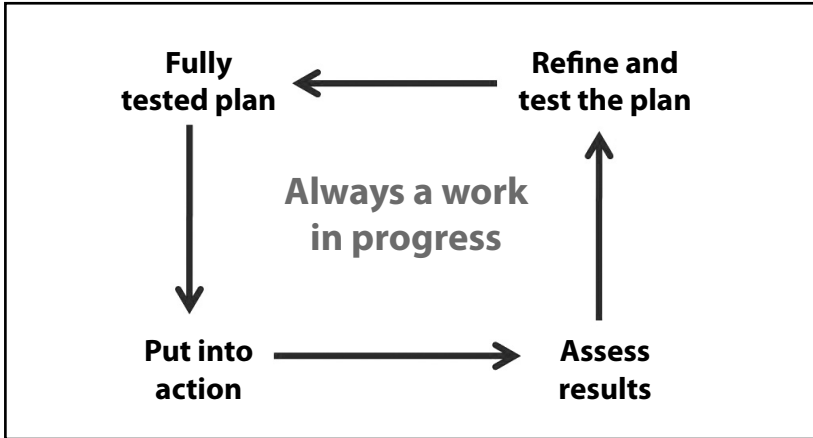
- stop-loss levels
- position size
- building positions
- closing/switching investments.

For an explanation of these various elements in an investment plan, my book *Building Wealth in the Stock Market* (Wrightbooks, 2009) sets out my own complete investment plan as a model for investors to use in developing a plan to suit their own temperaments and level of experience.

Step 3: Put the plan into action

The process here is best seen as a feedback loop, as shown in figure 1.5.

Figure 1.5: feedback loop



The key idea here is that our plan will never be completed in one attempt. It will be an ongoing effort over many years and will involve us in deep and ongoing contemplation. We will usually do this in parallel with, and influenced by, our ongoing reading and learning.

Most of us who stick at it will get at least part of the way through this step and then stop growing further as investors. That is why we call this large group the *average investors*.

Step 4: Track investment results against the objective of the investment plan

To start on the road to being a good investor, rather than an average one, we need to tackle this obstacle in our path. It stands to reason that, if our investment plan calls for a target rate of return, we should be tracking how we are going. I do this myself by valuing my investments at the market price at the end of every trading day. All income is included as it is received. From this I can calculate a rate of return for the year to date. I compare my return with the market index return and my average annual investment plan target return

of 12.5 per cent. For the market, I use the S&P/ASX All Ordinaries Accumulation index because it assumes reinvestment of dividends, making it the most applicable index to track investment returns. On my spreadsheet these three returns look as shown in figure 1.6 for 30 March 2011.

Figure 1.6: returns for 30 March 2011

Accum. Index 30.06.10	30 415.2
Accum. Index now	35 713.2
Market return year to date	17.42
My average annual target return	12.50
Portfolio rate of return year to date	16.24

My rate of return for the year to date is calculated from this summary of my portfolio (figure 1.7), which is in dollars.

Figure 1.7: portfolio summary

Portfolio value	1 350 092
Cash reserve	748 995
Total capital	2 099 087
Capital gain	207 867
Dividends	52 967
Interest	12 553
Franking credits	21 563
Total return	294 950
TWAC	1 816 513

My rate of return for the year to date is the total return amount expressed as a percentage of the time weighted average capital (TWAC), which takes account of movements out of my investment capital during the year, primarily administration expenses and pensions as this is a self managed superannuation fund (SMSF) portfolio. It should be noted that dividends are notionally reinvested in the Accumulation index on the ex-dividend date, but I only take them into my calculations on the date they are paid. This means