

Trading Insight

Tuesday March 26 2013

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Currencies in the combat zone

Finding a strategy is vital as increasing volatility provides profit opportunities **Page 6**

Inside »

Silver lining
Industrial versatility gives a new edge to poor man's gold
Pages 5-6

Binary bonus
A simple approach that claims to cut back on risk
Page 7

On FT.com »



Spotlight on learning
Education is seen as the way forward

Multiple strategies

Broad approach gives insight into global market movements

Index	Value	Change
FTSE	6385.3	6386.3
Wall Street	14484.1	14485.9
EUR/USD	12911.9	12912.7
Vodafone Group	183.02	183.48
HSBC	704	705.3

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Movement and volume return to reinforce an air of optimism

Gains are to be had as stock markets worldwide continue an upward march, fuelled by better economic prospects and central bank action, says *Jonathan Eley*

For much of 2012, the UK's FTSE 100 index traded in a 500-point range. Many traders complained that such relatively directionless markets limited their scope for gains. Spread betting firms and interdealer brokers bemoaned the lack of volatility and volume. There are fewer such complaints now. Stock markets in particular seem to be heading inexorably higher. Most of the world's developed markets have put on around 10 per cent in the past three months, building on a rally that began last autumn.

The Dow Jones Industrial Average has set a new all-time high, as has the UK's mid-cap index. Fiscal cliffs, sequesters and ambiguous election results have not succeeded in delaying the upward march of share prices.

These rallies are partly based on an improving economic backdrop, with recent US economic data in particular coming in better than expected. But mostly, they are driven by central banks.

The US Federal Reserve is buying up to \$85bn of Treasuries and mortgage-backed securities each month, the Bank of England is making dovish comments regarding its asset purchase programmes, and the European Central Bank stands ready to do "whatever it takes" to stabilise European markets.

David Jones, chief market strategist at IG, says the impact of central bank cash is driving the market far more than any improvement in economic or corporate fundamentals. "Safe havens are offering very little yield at the moment."

Theo Papatthasiou, head of trading at Saxo Markets, thinks stock markets are in a sweet spot, with a combination of low interest rates and high profit margins making equities attractive. "Plus, there is a lot of new cash coming into the market."

Nowhere is the link between central bank action – or at least, the prospect of it – and

rising stock markets more evident than in Japan. Long the laggard among developed-world indices, the Nikkei has gained close to 30 per cent (in local currency terms) over the past three months, as new prime minister Shinzo Abe signalled his intention to help exporters and combat deflation.

Nor are clear short-term trends confined to equity markets. In foreign exchange, Abe's election has resulted in a sharp fall in the yen compared with the dollar, while weak economic data and talk of more monetary stimulus has caused another downward lurch in sterling.

What could stop the equity market juggernaut? Some sceptics point to corporate earnings, saying that at US companies in particular, profits margins cannot remain at such elevated levels for long.

But others contend that equities are still good value. David Coombs, head of multi-asset investments at Rathbones, a wealth manager, says that with home prices rising, energy costs falling and productivity improving, the US is still fair value. Mr Papatthasiou agrees.

"When economies come out of downturns, the US tends to be first out the hole. It's the fastest and most efficient market." He adds that internal data suggests clients are reallocating capital to the US and away from the UK and Europe.

Ben Gutteridge, divisional director of research at Brewin Dolphin, a UK stock broker, notes that after the technology bubble burst, the FTSE 100 offered a dividend yield broadly similar to today's despite being over 3,000 points lower. On a price to book basis, "equities are actually cheaper now than 10 years ago".

The rising tide of central bank cash has not floated all boats, though. Emerging markets have generally underperformed during the latest rally; Russia's RTS index is up just over 2 per cent over the past three months while Brazil and India have both fallen slightly. IG's Mr Jones is not



Changing fortunes: opportunities have increased in rising equity markets, such as the London Stock Exchange
Reuters

sure whether this is an opportunity or a warning. "I would question why, if the world and his wife are rallying hard, emerging markets are not doing so, too."

"It suggests that investors are prepared to take some risk, but not too much."

Mr Papatthasiou, at Saxo Markets, remains very wary of China. "Personally I think China has overdone it over the past 10-12 years... I'm not sure the time is right to be going there." He adds subdued global demand – and renewed competition from Japan, courtesy of its weaker currency – is making life difficult for China's exporters.

Most trading commentators feel that the market is due a break soon, and is perhaps looking for an opportunity to correct. "It has felt frothy now for some time, but it just keeps on coming," says Mr Jones. He and others agree that any correction is likely to be shortlived, and surveys of IG clients suggest most would welcome it as an opportunity to enter new positions.

"A short term correction is likely and it is in many cases hoped for. But once a pull back is complete we would expect the market to continue rising," adds Mr Papatthasiou.

That might well be bad news for gold, an asset class that has been left trailing in equities' wake since the summer of 2012. Coveted as a "safe haven" asset during the uncertainty of 2008 and 2011, it seems

'When economies come out of downturns, the US tends to be first out the hole. It's the fastest and most efficient'

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**Bond volatility
Sovereign debt
problems draw in
more traders**

By Tanya Powley

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Trading Insight

Silver's industrial versatility adds to its attractions

Precious metals The poor man's gold, which many investors see as being undervalued, is starting to look like a good bet, reports *Lucy Warwick-Ching*

Spread betters have turned to silver in recent months in the hope that "the poor man's gold" will experience a price rise soon. Capital Spreads said in February that the percentage of buy positions placed on silver far outweighed those placed in gold. "Our clients believe that silver is the one to bet on," says Angus Campbell, head of market analysis at Capital Spreads. "Clients are seeing far more

potential upside from the minor relation." Experts believe the renewed interest in silver is partly due to the fact that the precious metal has many industrial purposes, alongside the fact that it is yet to really catch up with gold. "It's been an ongoing claim by many a bull of the price of silver that it is vastly undervalued when you consider just how strong the price of gold has been in recent years," says Mr Campbell. "The argument

is that gold's poorer cousin has not enjoyed the same rally in recent years and, as an asset, it serves many more purposes, such as industrial uses, as well as being an important store of value." Silver's high electrical and thermal conductivity means it can be used for things like power generation, so it is a global demand and recovery play just as other industrial metals are, like platinum and palladium.

According to Shai Heffetz, managing director of InterTrader, 46 per cent of demand for silver is industrial, compared to just 9 per cent for gold. This means that silver is more correlated to macro economic growth, especially in the electronics market, which drives 21 per cent of global demand, says Mr Heffetz. Kathleen Brooks, research director at Forex.com, backs this up. "Silver has a key attribute that gold is missing: it is useful,"



Precious moments: gold's poor cousin is popular with traders who believe the metal could be heading for a strong rally Reuters

she says. "This makes us think that a bottom in silver could be in view." The silver price has followed gold lower in recent months and is now back at August lows. But if the global economic recovery continues to pick up this year, the silver bulls believe it could prove to be a turning point for silver as demand for metals with industrial uses pick up. "Later this year, we could see the relationship between gold and silver break down, with silver pulling away from the yellow metal as gold struggles to gain traction when inflation pressures remain low and people move into riskier asset classes," says Ms Brooks.

Traders can bet on silver either through spread betting or via contracts for difference (CFDs) using spot and "future bets". Spot bets reflect the cash price and are typically used for short-term views. Futures are more suited to trade longer-term views and will typically attract sophisticated investors happy to use leverage for big gains.

Another way to play silver is to look at the gold/silver ratio. On the whole, the price of gold and silver tend to move in the same direction but the ratio between the two can change from one extreme to the other and it is in these extremes where experts say investors can make money.

This is done when investors make a call to say that one asset is overpriced and the other is underpriced. If an investor holds the overpriced asset then they are likely to sell it and increase their holding in the undervalued asset.

'We could see . . . silver pulling away from the yellow metal as gold struggles to gain traction'

Trading Insight

"Silver remains undervalued compared to gold and has the potential to embark on a strong rally," says Fawad Razaqada, technical analyst at GFT Markets. "The historical gold/silver price ratio has been around 16:1 and, given the prices of \$1,665 and \$31.50 respectively, the ratio is currently 53:1. This means that, if prices move back towards their historic levels, silver would have a lot of ground to make up, even if we were to see a marked sell off in gold."

Others warn that, when investing in silver, traders must apply caution because it can be even more volatile than gold. Mr Heffetz says investors should focus on the main attraction of silver, which is that, in today's highly correlated markets, silver stands out. "Its correlation with the S&P 500 is just -0.49 which is considered a medium negative correlation," he says.

"On the other side there is a high correlation between silver and money supply, which means that silver may be a very valid hedge against the current printing frenzy of central banks."

Others argue that silver is not as useful as some might think and could be headed for a fall. "Silver distribution has been steadily declining since October," says Colin Cieszynski, senior market analyst at CMC Markets. "With the decline of photography demand and resurgence of precious metals over the past decade, silver has increasingly traded more on its currency status than industrial supply and demand."

He says that benign inflation has also reduced some of the demand for precious metals as an inflation hedge, although he admits this could return in future years.

"This suggests that just as silver had benefited from increased fear in recent years, it now could struggle as economic and political fears ease."

European periphery Growth opportunities

Traders looking to take advantage of any recovery in the global economy could place bets on peripheral European indices, but growth is unlikely in the short term, writes *Tanya Powley*.



"The obvious answer is the peripheral indices like Spain's Ibx, the Portuguese market and the Irish stock market," says Kathleen Brooks, research director at Forex.com.

She notes that one of the best performers has been the Athens stock exchange, which is up 120 per cent since July 2012 and is outperforming other global indices since the start of the year.

"Because the bar is so low, if growth in Europe picks up this year we could see further flows into some of the most damaged markets in Europe," says Ms Brooks.

Matt Basi, senior premium client manager at CMC Markets, agrees that if Europe returns to long term growth then these indices would be probable outperformers.

Any return to growth in peripheral Europe could also benefit eastern European indices, such as Turkey, according to Ms Brooks.

However, as economic data of these countries remains weak, traders are likely to find UK indices a safer bet on growth in the short term.

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Volatility provides profit opportunity

Currency wars Identifying the big movers and their motivation is key to success, says *Lucy Warwick-Ching*

Traders are seeking ways to profit from currency volatility amid renewed speculation that governments will continue to implement fresh money-printing measures to stimulate their economies.

Currency trading volumes have almost doubled in the past few months, say spread betting firms, among clients hoping to profit from what some say has the makings of a fresh round of global currency wars. Economic uncertainty and interventions from governments to stimulate recovery have triggered sharp movements in the dollar, euro, sterling and yen in recent months.

Spread betting firms report that buying the euro and selling the yen has become one of the most popular trades in the foreign exchange market, with currency traders more bullish on the euro than at any time since July 2011.

"Even if the G20 failed to mention the term currency war, it doesn't mean that it isn't going ahead," says Kathleen Brooks, research director at Forex.com. "In the current environment having a weak currency is economically advantageous, as strong currencies can shave percentage points off growth; hence we could see currency wars by stealth, rather than public battles."

The way to profit from exchange-rate movements is to "short" the market and speculate that a currency will continue to fall, or rise against another currency. Investors can buy at the upper end of a spread – if, say, they thought that the pound would strengthen – or sell at the lower end if they thought it would weaken.

Ms Brooks says the obvious choice at the moment is to short the yen as the government and the Bank of Japan are employing expansionary fiscal and monetary policies respectively, which traditionally tend to be currency negative.

"However, after falling nearly 20 per cent versus the dollar since November 2012, a lot of this "accommodative" policy could already be priced in," she says. "The yen might be the obvious choice to short during a currency war but it might not be the most expedient choice."

Others say that to find the opportunities with the best profit potential, traders should first decide who the major players are in this currency war and what their motivation is.

Shai Heffetz, managing director of InterTrader, an online trading platform for spread betting, CFDs and foreign exchange, says: "The initiators of devaluation [of currency] are indebted countries, led by the US, Europe and Japan. On the other side we have big debtors including China, Brazil and Russia. These debtors are also net exporters of commodities or goods so they want a weak currency as it will allow them to devalue their debt."

The first sets of currency pairs that InterTrader expects to see activity on are those within the indebted countries, where no central bank wants to stay behind the trend. "We expect to see cyclical patterns in the euro against the US dollar, sterling against the US dollar, US dollar versus the yen and the euro against the yen," he says.

Another opportunity, "only for the strong hearted", he adds, arises from taking advantage of potentially dramatic changes that arise from the pairing up of currencies such as the US dollar, euro and yen against the Brazilian real, the Chinese renminbi and the Russian rouble.



Price watch: a shopper at an electronics store in Caracas before the Venezuelan government devalued the currency

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A recent example of dramatic movements in currency linked to government intervention is the Venezuelan government's move to protect its economy that devalued its currency by 46 per cent overnight.

"These sudden sharp movements often arise over a weekend or overnight," warns Mr Heffetz.

"They are considered 'grey swans' as they are somewhat predictable but no one knows which one will happen, when it will occur and the magnitude of the action taken, but there is a market understanding that the grey swan is lurking."

Mr Heffetz, says: "In spite of this instability, we expect the currency wars will not get out of hand, due in part to the efforts of international forums where world leaders act to coordinate action. This 'war' will remain contained with spurts of volatility

'This [currency] "war" will remain contained with spurts of volatility rather than an all-out battle'

rather than an all-out battle which would destabilise the already very fragile world economy."

As with most financial investments, the popularity of currency pairs changes over time, and there are other currency pairs that could potentially offer further scope for profit such as the Australian dollar with the euro.

Michael Hewson, senior market analyst at CMC Markets, says that since 2008 the Australian dollar has risen sharply against the euro and is well overdue a pullback. He adds that traders could profit from this movement.

"In recent weeks we have seen evidence that these Aussie gains could well be about to reverse with a recent technical breakout showing that we could potentially see the euro gain 10 per cent over the course of the next 12 months."

System of risk and reward offers a simple alternative

Binary trading

Interest in an option that claims to reduce uncertainty is rising, writes *Lucy Warwick-Ching*

The number of traders using binary options in the UK has risen by more than eight times since 2011, driven by an increase in risk-averse investors.

Banc De Binary, the binary options trading company, says new investors in this sector are attracted to the straightforward decision making required by binary options trading compared with more technical betting structures.

"The spread betting industry in the UK generates nearly £1bn in revenues per year, but its appeal is limited by its complexity," says Oren Laurent, chief executive of

Banc De Binary. "Binary options are a simpler, fast-growing form of online options trading. They allow investors to benefit from making a straightforward choice; whether the price of a share, commodity or index will go up or down. Since there are only two possible outcomes, risk and reward are transparent for the investor."

Binary betting allows traders to bet with limited risk on a wide range of assets, including individual shares, equity indices, commodities and exchange rates.

These types of bet typically appeal to traders with limited experience, or appetite for risk, because the maximum profit and loss is known from the outset. Investors in binary options receive a payout if they correctly predict the direction of change in an asset's value in a set period of time. The payout is a percentage of the original investment, usually

between 70 per cent and 90 per cent. If the prediction is wrong, the original investment is lost.

It does not matter if the value of the asset changes by 1 basis point or 100 – the result is the same for the investor. Experts say one advantage of binary trading is that it removes the most difficult aspect of options trading – the precise movement of an asset.

In a similar way to betting on sport events, financial binary betting lets traders stake a certain amount on an event happening or not happening. As soon as the bet is placed, investors can see the maximum they stand to gain or lose.

"Many private investors have a view on the direction of an asset – the FTSE 100 is going to rise, Facebook is going to fall – but predicting exactly the degree of movement is close to impossible," explains Mr Laurent. "Binary options make that uncertainty irrelevant."

David Jones at IG Index, agrees. "Your view may be that the FTSE 100 is going to rise, and you buy a binary bet for the FTSE to end the day positive at, for example 50, at £1 per point. Even if you get the direction completely wrong and the FTSE ends the day 150 points lower, the most you can lose is 50 points as the binary never goes below zero."

IG offers clients a host of different ways to trade markets using these products, from short-term bets covering the next few minutes, to a more medium-term view over the next week or so. It also offers custom bets allowing clients to tailor

Binary betting lets traders stake a certain amount on an event happening or not happening



Base points: the FTSE 100 index, the Dow and the euro/dollar currency pairs are popular for binary bets

Getty

risk. For example, a client may want to set up a bet that makes £100 if the FTSE is 2 points higher than it is now, in 90 minutes.

Binaries also allow the more experienced trader the opportunity to take a view on future levels of volatility rather than just directional movements. Using a binary, a trader can back the FTSE to move 50 points in either direction and make money whichever way it moves – but, with a more traditional spread bet, the trader would have to get the direction right.

The most popular markets for binary bets tend to be the FTSE, Dow and the euro/dollar currency pair. But, Shai Heffetz, managing director of InterTrader, an

online trading platform for spread betting, CFDs and forex, warns that binary bets can sometimes be even harder to predict than other forms of investing.

"There is one very important factor that must be taken into account before entering into a binary bet; in small timeframes, markets tend to perform randomly and, therefore, being on the right side of a binary bet is as likely as calling the toss of a coin," he says.

"With average binary bet payouts typically at around 80 per cent, the probability of profiting from binary betting is always against the gambler and those who partake are more likely to run out of money than succeed."

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Trading Insight

Steady nerves and a lot of research count

Advice

Some tips – and warnings – for the novice from *Lucy Warwick-Ching*

Financial spread betting provides a tax-free way to make a profit from rising and falling prices on a range of different markets from foreign exchange, to shares or commodities.

But experts warn that, while profits can be big, so too can losses, so it is

important to approach spread betting sensibly and put some rules in place before you start. Here we list a few key ways traders can start to build financial spread betting careers.

Start small

The reality is that most beginners lose money. But you do not have to join

them. With most companies, the minimum trade is £1 a point, but there are others, such as finspreads.com, that let beginners trade 10p a point for the first few weeks.

Stagger your entry

Instead of aiming to enter at one specific price, experienced traders tend

to use an approximate entry range and then adapt to a short-term timeframe chart for exact entry points. This allows traders to develop a low-risk, staggered entry. Remember, there are no commissions payable with spread betting, unlike with share trading.

Stick to a plan

Once you have made your decision on a bet – unless there is some information that invalidates your original analysis – stick to your plan, no matter how ambitious you are on the position.

“To be a successful trader, you need to focus on a smallish range of investments and really get to know what forces make the price move,” says Stephen Walsh, product manager at Selftrade, “The most simple examples being company news and reports impacting individual stocks or changes in interest rates impacting FX pairs.”

Once you have done this, he says, set a trading plan – at what price should you make a trade, what is your target exit price and when should you cut your losses. “And, most importantly, stick to it.”

Similarly, if you decide on an exit position, say, at a set percentage from the entry price, hold yourself to it. Having any form of plan, even the most basic one, is better than no plan.

Back trends

If the market is going down then experts suggest you do not buy that sector thinking it will come back up. Wait until the market starts to bottom out and turn your way before you get behind it and start betting.

Read the news as well as the charts

While technical analysis will provide the inspiration and structure for trades, you should also do some light fundamental research before taking positions. This could include looking up forthcoming dividend dates, timetables for annual meetings, analyst recommendations and reporting updates.

There can be clear correlations between share prices in some sectors, such

as supermarkets, high-street retailers and builders. Poor performance from one company can point towards negative developments for companies in the same sector.

Limit losses

Experts suggest traders put a lid on potential losses by including a stop loss.

This is the mark at which investors can instruct their spread betting company to close the trade. This will enforce and help to protect capital.

Some spread betting firms adopt a policy whereby, if someone has lost more than a certain amount on a position, their bet will be closed automatically.

Place stop losses carefully

Putting a stop loss as close as possible to a bet may sound like a secure way to reduce risk, but if it is set too close then it will trigger just through regular intraday movements. Experts recommend traders look at how much the market has moved day-to-day, using the charting software provided by the spread betting firm, and set a stop loss that is reasonable for the sector.

Don't get carried away

Novice traders should beware of getting swept up in market rumours. Trades should be based on research you do yourself – after all, it is your money that is at risk.

“Fear and hope play on the trader's mind, but it is important to remove emotion. It is all too easy to fear losing any paper profit you have made and cut a winning position early or, more importantly, live in the vain hope that a loss will turn itself round,” says Mr Walsh.

Don't be afraid to admit defeat

One of the biggest errors traders make is thinking the market will move back so they double or triple their investment and lose a fortune. Traders should not be afraid to close out a trade early for a loss.

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