

FINANCIAL STANDARD GUIDE TO CONTRACTS FOR DIFFERENCE (CFDs)



GUIDE SERIES 3

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CFDs can be risky and are not suitable for all investors. You should consider whether CFDs are suitable for you. CMC Markets' Shield Account Product Disclosure Statement is available at www.cmcmarkets.com.au/shield. Please consider it in deciding whether to acquire, or continue to hold, CFDs. CMC Markets Asia Pacific Pty Ltd (ACN 100 058 213, AFSL No. 238054). *53% of Australian CFD traders trade with us – source: Investment Trends May 2007. [^]Shield Stop Loss orders are accepted at the discretion of CMC Markets. CMC0043/GUARD/FSM

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A close-up photograph of a person's hand holding a silver pen, signing a document. The document is white with black text, and the signature is being written in silver ink. The background is blurred, showing a blue surface and some papers.

CFD providers are joining forces with financial planners, stockbrokers and fund managers to design products that adapt CFDs for a bigger group of investors, including wealth accumulators.

INDUSTRY SNAPSHOT

INVESTING IN CONTRACTS FOR DIFFERENCE (CFDs) is a relatively recent development in the Australian retail investment market. The number of CFD providers has grown from a couple of pioneers early in the decade to around 20 today.

Because providers operate independently of a securities exchange, there are no hard figures on the number of active CFD traders in Australia, nor the volume of transactions. But a survey of the CFD market by market research company Investment Trends puts the number of active CFD traders at about 30,000. Contract size is between \$30,000 and \$40,000. Investors trade twice a week and hold their positions from three to five days.

Some estimates of the United Kingdom market, where CFDs have been established much longer, show that CFD traders account for 20 per cent or more of turnover on the London Stock Exchange. In Australia, the current industry estimate is that 10 to 15 per cent of the daily transactions on the Australian Securities Exchange (ASX) are due to CFD trades.

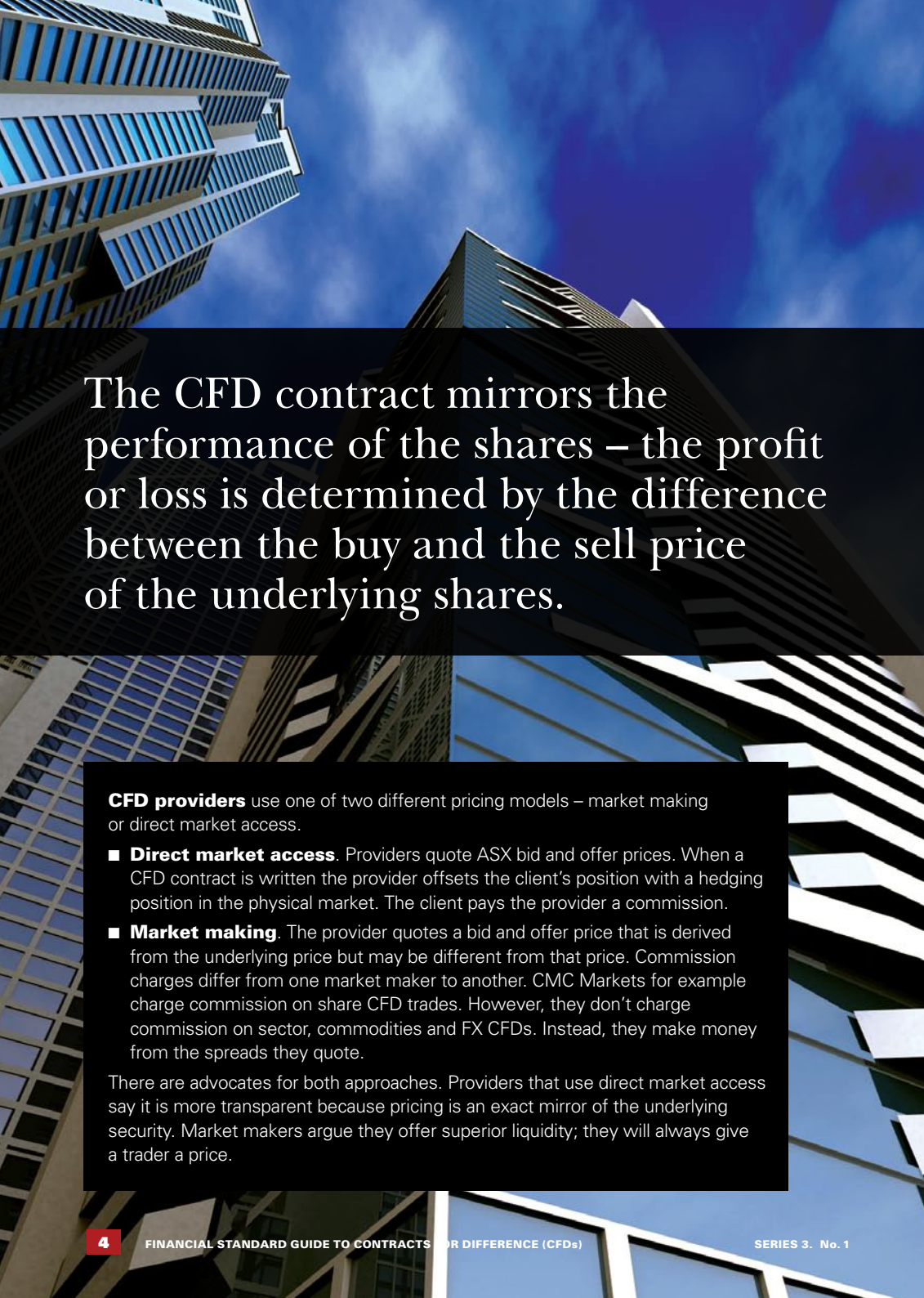
CFD providers range from specialists such as CMC Markets, IGMarkets and MF Global to big groups such as CommSec. Last year the ASX entered the market with exchange-traded CFDs.

In its early days the market was largely the domain of professional traders looking for a leveraged product for share trading that was simpler and more efficient than options and warrants. These traders held short-term positions and could go long or short.

By the middle of the decade, the range of products available through CFD providers had broadened to include overseas share markets, currencies, commodities, indices and sectors.

As providers built more sophisticated risk management tools, such as guaranteed stop loss facilities, CFDs started to attract a wider range of investors. In recent times, short-term traders have been joined by long-term investors who have come to see them as an efficient way of investing and as a way to hedge established holdings.

The most recent trend on the market is the development of structured investment products that combine CFDs with capital protection. CFD providers are joining forces with financial planners, stockbrokers and fund managers to design products that adapt CFDs for a bigger group of investors, including wealth accumulators.



The CFD contract mirrors the performance of the shares – the profit or loss is determined by the difference between the buy and the sell price of the underlying shares.

CFD providers use one of two different pricing models – market making or direct market access.

- **Direct market access.** Providers quote ASX bid and offer prices. When a CFD contract is written the provider offsets the client's position with a hedging position in the physical market. The client pays the provider a commission.
- **Market making.** The provider quotes a bid and offer price that is derived from the underlying price but may be different from that price. Commission charges differ from one market maker to another. CMC Markets for example charge commission on share CFD trades. However, they don't charge commission on sector, commodities and FX CFDs. Instead, they make money from the spreads they quote.

There are advocates for both approaches. Providers that use direct market access say it is more transparent because pricing is an exact mirror of the underlying security. Market makers argue they offer superior liquidity; they will always give a trader a price.

WHAT IS A CFD?

A CONTRACT FOR DIFFERENCE (CFD) is a form of derivative that involves a contract between an investor and a CFD provider to exchange the difference between the value of a security at the time the contract is opened and the time it is closed.

The underlying security might be a stock on a local or overseas share market, a local or overseas stock index, a currency, a commodity, an interest rate or a debt security.

Rather than owning shares or other securities, the investor is buying and selling the price movement of the security. The contract represents a theoretical order to buy or sell a security. When the position is closed, the profit or loss is set by the difference between the opening and closing price.

In practice it works like a margin loan in giving investors leverage. When an investor opens a CFD position they put down a deposit on the value of the shares, which can be as little as 5 per cent. The CFD contract mirrors the performance of the shares – the profit or loss is determined by the difference between the buy and the sell price of the underlying shares.

CFD providers report that popular trades include the top local stocks and some big Wall Street stocks, the S&P/ASX 200 index, gold and the Australian dollar against the US dollar.

One of the attractions of CFDs is that they give an investor the ability to trade long or short. An investor who takes a view that a stock is going to fall can sell it (short it) using a CFD contract.

Conventional trading instruments can make short selling costly and complicated. A stockbroker must borrow stock to cover the investor's position and this adds substantial cost to the transaction. CFD providers allow their clients to enter a short position at the same cost as a long position.

Compared to other derivative instruments, CFDs are simple. Options and warrants have a pricing structure that incorporates some arcane financial concepts such as time decay, but the price movement of a CFD contract is directly linked to the change in the value of the underlying security. This is what CFD providers are talking about when they say the contract mirrors the underlying asset.

The emergence of CFDs is due, in part, to the development of the internet as an information and trading resource. Retail investors have access to sophisticated trading platforms that were once the preserve of institutional investors.

Clients watch their stocks being traded in real time, with bids and offers on display. When they place an order they can see their trading account being debited and, if they make a profit on a transaction, their account being credited instantly. A lot of the competition between CFD providers is about who has the best platform.

FEATURES AND BENEFITS OF CFDs

CFDs ARE FAMILIAR TO TRADERS who want cost-effective, leveraged access to markets where they can use short-term trading techniques to take advantage of market volatility.

They are less familiar as a tool for people accumulating wealth through private portfolio or self-managed funds, and for retirees who are looking for an efficient risk management tools.

One big difference between CFDs and other derivative trading instruments is that CFDs, unlike options and warrants, have no expiry date. Investors can keep their CFD contracts open for as long as they like.

This gives CFDs a great deal of flexibility; they are not just short-term trading tools. CFD providers have been developing their products to cater to investors who want leverage and hedging as part of their longer term strategies.

One example is CMC Markets' Shield Account, which allows trustees of self-managed funds and other investors to trade in the ASX200, other indices and currencies. The product has a built-in stop loss facility that covers the investor if the market moves against their contract position.

Long-term investors can use CFDs of this type in a number of ways:

- **HEDGING.** To protect a portfolio against adverse market movements, an investor can take a CFD position that is opposite to the portfolio position. If the portfolio is long Australian shares, which is a typical exposure for self-managed super funds, the trustee can use a CFD contract to short the ASX 200. If the market falls the gains on the short position will offset the losses in the physical portfolio.
- **DEFER CAPITAL GAINS.** An investor may have built up an overweight position in a stock that has performed very well. The investor wants to diversify away from what has become a high-risk exposure but does not want to sell down the stock and create a capital gains tax liability. CFDs can be used to sell against that stock position. The sale of a contract has the effect of locking in a selling price and frees up cash for other investment.
- **LEVERAGE.** Many investors approach retirement with less in their retirement savings portfolios than they would like. CFDs can be used in the same way as a margin loan to gain greater market exposure with limited exposure. With a stop loss in place, losses can be controlled.

A stop loss operates like an insurance premium. A guaranteed stop loss provides an additional layer of protection by providing a guarantee that the contract will be closed out at the set price. For example, an investor takes out a CFD contract on a stock at \$17 and places a guaranteed stop loss at \$16.50. It is possible that the stock will hit \$16 without trading at \$16.50. A guaranteed stop loss will get the trader out at \$16.50 but a stop loss won't. Some CFD providers charge a premium for that level of protection.

It is important to remember that the liability for a holder of a CFD contract is not limited to the deposit paid. In the case of some derivatives, such as warrants, if the underlying share price moves against the investor the derivative will expire worthless. All that is lost is the money invested in the warrant.

In the case of a CFD contract, if the market moves against a position the holder of that position may be called upon to pay additional funds. That is where the stop loss and guaranteed stop loss facilities come in; they unwind contracts once a certain loss level has been reached.

If a portfolio is long Australian shares, which is a typical exposure for self-managed super funds, the trustee can use a CFD contract to short the ASX200. If the market falls, the gains on the short position will offset the losses in the physical portfolio.



CFDs offer a great deal of flexibility; they are not just short-term trading tools. They cater to investors who want leverage and hedging as part of their longer term strategies.

THE COST OF USING CFDs

CFD PROVIDERS charge commission on transactions, interest on the leveraged-up amount of the portfolio and, in some cases, monthly account fees.

■ **COMMISSION** is charged on the initial deposit. Some providers have flat commission rates, regardless of the size of the transaction. The most commonly occurring flat commission rate is 0.10 per cent. On a \$10,000 initial deposit, the commission would be \$10. Providers that charge commissions on a sliding scale have rates that are as low as 0.05 per cent and as high as 0.2 per cent. A commonly occurring scale is 0.125 per cent for small transactions down to 0.08 per cent for initial deposits of \$100,000 or more. Some brokers have different rates for online and phone transactions, with higher charges for phone services.

■ **FINANCING COSTS** are charged on the portfolio balance above the initial deposit. Securities can be traded by putting up as little as three per cent of the value of the underlying asset. The investor gains exposure to the whole amount of the transaction; the CFD provider offers exposure to the balance. The provider protects its own exposure to the underlying asset by taking out a hedge and the cost of that hedge is passed on to the investor as a financing charge.

The cost of financing is calculated as a margin over the cash rate. Margins vary from 1.25 to 2 per cent. Interest is calculated daily and the investor's account is rebalanced daily. When the investor takes a short contract, the CFD provider pays interest.

■ **MONTHLY FEES** vary widely. Some providers have no monthly fee and no fee for live market feeds. Other have no monthly fee but charge separately if the client wants a live feed. Some charge a monthly account fee, with a charge of around \$40 the norm, but will waive it for frequent traders.

MINIMUM OPENING BALANCE requirements vary from nil, in the case of a couple of providers, and up to \$5,000. The most commonly occurring minimum opening balance is \$5,000.

HOW CFDs WORK

A step-by-step guide

MOST SUCCESSFUL CFD traders have a few things in common. They have a well-developed trading strategy, they have a risk management plan and they are prepared to commit time every day to monitor the market and their trading positions. This is as true of the investor who lets a CFD contract run for months or years as it is of the trader who opens and closes multiple contracts in a day.

There is no single trading strategy that works best. Traders use a variety of techniques: straightforward fundamental analysis that allows them to look for cheap stocks; momentum indicators that track the market's support for a stock through price movement and volume; and technical and quantitative trading systems.

Traders set aside a certain amount of time each day. They set up watch lists and have a list of criteria for taking action. Traders also keep a diary of their trading activity; this allows them to keep track of what works for them and what doesn't.

Investment guidelines should include the types of assets that will go into the CFD portfolio, the degree of leverage, target returns and risk tolerance. The guidelines might stipulate only trading in Australian shares with daily volume greater than \$350,000 (volume is important to ensure the investor can get out of the position). Is the investor going to trade long only or go short? How much capital is the investor prepared to put at risk?

Investors who are planning to trade a variety of different assets should look at the trading platforms offered by CFD providers to make sure they can monitor their positions in share CFDs, index CFDs and currency CFDs with a single view.

Traders allocate a set amount of their trading portfolio to each trade. This is an important element of the risk management process. Small exposures of one or two per cent reduce risk for two reasons: if the contract results in a loss it is only a small loss; and it is easier to get out of a small position. Many small positions with limited risk are better than one big position. Most CFD traders allocate around two per cent of capital to a contract.

Investors have different levels of risk tolerance. To assess their level they need to ask certain questions. How much is at risk on each trade? How much is at risk across the whole portfolio? How much are you making for each dollar at risk?

Some traders set a level at which they will take profits to ensure they make a return on their investments. Other traders oppose this approach, arguing that the market should decide when the trend is over. These traders prefer to use a stop-loss. A stop-loss order is an order you place either online or by calling the provider, to close your position when it reaches a certain point.

Stop-loss orders are trading insurance. The investor will be taken out of a trade when the nominated stop-loss level is reached. The key is to use the stop-loss to keep losses small and under control.

Stop-loss positions can be adjusted as the price of the underlying security rises. If the shares are worth \$30 when they are purchased the stop-loss might be set at \$25. If the share price goes up to \$40 the stop-loss can be adjusted up to \$35. This is called a trailing stop.

It is important for investors to understand that with CFDs, they are trading on margin. Stocks can be traded by putting up as little as three per cent of the value of the shares. This leverage allows investors to take big positions with small outlays but it is important to note that the investor is exposed to the whole amount of the transaction. The investor puts up three per cent and the CFD provider offers exposure to the balance supported by derivative contracts. If the contract results in a loss, the investor is liable for the whole amount.

That is why it is so important to have a strong risk management strategy in place before trading. Many seasoned traders do not trade unless they have set a stop-loss position first.

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CFD ONLINE

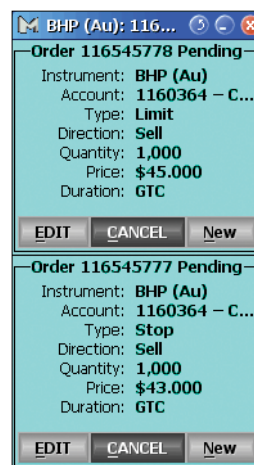
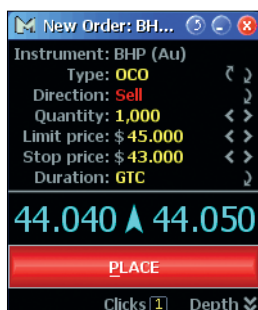
Different CFD providers will have different products but the principles are fundamentally the same. Here are some screenshots* using the CMC Markets platform that illustrate a classic CFD portfolio.

1. Buy order execution screen 5000 Oxiana at market price \$2.74



2. One cancels the other order – sell 1000 BHP at limit price of \$45 or stop (loss) sell at \$43

The two screens show placement and order going into pending execution status (light blue).



* Screenshots were provided by CMC Markets as at June 2008.

3. Pending orders blotter (order pad)

First two lines are the one cancels the other orders in BHP.



Order ID	Instrument	Quantity	Ccy	Order Price	Market Time	Local Order Time	Order Type	Valid	Link ID	Order Action
116545778	BHP (Au)	1,000.00	AUD	45.000	Jun 16, 2008 5:12:3...	Jun 16, 2008 2:12:3...	Limit	GTC	116545777	OCO
116545777	BHP (Au)	1,000.00	AUD	43.000	Jun 16, 2008 5:12:3...	Jun 16, 2008 2:12:3...	Stop	GTC	116545778	OCO
116545646	BHP (Au)	3,000.00	AUD	44.081	Jun 16, 2008 5:10:2...	Jun 16, 2008 2:10:2...	Stop	GTC		None
115289783	XAUUSD Spot	200.00	XAU	756.99	Jun 5, 2008 5:55:00...	Jun 5, 2008 2:55:00...	Limit	GTC		None
115097876	IPL (Au)	999.00	AUD	192.410	Jun 4, 2008 3:41:04...	Jun 4, 2008 12:41:0...	Limit	GTC		None

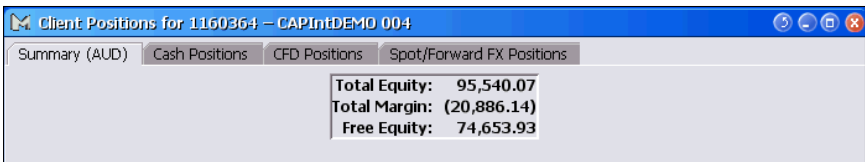
4. Client positions summary screen

Total equity equals the money you have deposited in your **account** plus dealings conducted on your account and the positions you hold.

During the trading day, your account balance is constantly calculated in line with movements in CMC Markets' prices using CMC Markets' Mid Price. The account balance is also calculated at the end of the day using CMC Markets' Mid Price closing rates (or CMC Markets' last dealing price).

Your total equity balance is used to assess your available margin against current positions, and any potential new positions you may wish to take. The **total equity** balance is used to establish if there is a requirement for additional margin to be paid in respect of your account.

To assist clients monitor equity balances, we summarise **total equity** and **free equity** together with total margin requirements at the end of the day (using CMC Markets' Mid Price closing rates or CMC Markets' last dealing prices) in a daily statement.



Client Positions for 1160364 – CAPIntDEMO 004	
Summary (AUD)	
Total Equity:	95,540.07
Total Margin:	(20,886.14)
Free Equity:	74,653.93

5. CFD positions tab

This screen lists daily **profits** and **loss** in real time.

Client Positions for 1160364 - CAPIntDEMO 004										
Summary (AUD) Cash Positions CFD Positions Spot/Forward FX Positions										
CFD Equities										
Instrument	Ccy	L/S	Qty	Value	Mkt	Reval	P/(L) (AUD)	Margin (AUD)	Margin %	Liq %
BHP (Au)	AUD	Long	1,000.00	44,020.00	44,045	1	25.00	(440.45)	1.00	20.00
CSR (Au)	AUD	Long	15,000.00	39,750.00	2,695	1	675.00	(2,021.25)	5.00	20.00
FMG (Au)	AUD	Long	0.00	1,850.00	10.295	1	1,850.00	0.00	5.00	20.00
IAG (Au)	AUD	Long	5,000.00	18,750.00	3,795	1	225.00	(569.25)	3.00	20.00
MQG (Au)	AUD	Short	2,000.00	98,340.00	49,175	1	(10.00)	(2,950.50)	3.00	20.00
QGC (Au)	AUD	Long	13,000.00	66,950.00	5,115	1	(455.00)	(6,649.50)	10.00	20.00
WTF (Au)	AUD	Long	5,000.00	17,000.00	3,355	1	(225.00)	(1,677.50)	10.00	20.00
CNE (UK)	GBP	Long	10.00	328.30	3,291.50	2.0779	1.77	(34.20)	5.00	20.00
DHI (US)	USD	Long	100.00	1,190.00	11.90	0.9993	0.00	(63.35)	5.00	20.00
YHOO (US)	USD	Long	1,000.00	23,470.00	23.46	0.9993	(15.97)	(1,248.54)	5.00	20.00
							2,070.80			

The ATO's view of gains made on CFD trades is that they are income not capital gains and are assessable for income tax purposes. Losses may be used to reduce taxable income.

TAX AND COMPLIANCE

End of year accounting

There are no tax advantages to holding a CFD. Trading is done on margin, which means that stocks and other securities can be bought and sold by putting up as little as three per cent of their value. The investor puts up the initial amount and the CFD provider offers exposure to the balance. No party ever owns the securities.

The provider takes out a hedge to cover its exposure to the underlying shares, indices or currencies, and the investor pays the provider a funding charge to cover the cost of the hedge.

The Australian Tax Office position is that the funding charge is not a loan and is not a deductible expense.

The ATO's view of gains made on CFD trades is that they are income not capital gains and are assessable for income tax purposes. Losses may be used to reduce taxable income.

Compliance

Broadly speaking, the requirements on planners if they want to offer CFDs to clients are:

- The planner's AFS Licence must allow the planner to provide advice on CFDs.
- The planner must have studied optional derivatives units as part of their professional education.
- The planner will have to go through an accreditation process with the CFD provider.

DISPELLING THE MYTHS ON CFDs

An adviser's guide

Sponsored statement

Nic Blakemore, Head of Distribution, CMC Markets Asia Pacific

CONTRACTS FOR DIFFERENCE (CFDs) have been around and available to Australian investors since 2001. There's no question that this innovative financial instrument is gaining popularity among a wide range of self-directed investors who want more control of their finances and wealth creation. The latest survey on the CFD industry shows that the number of people using CFDs in their portfolio has been doubling every year.



Nic Blakemore
CMC Markets Asia Pacific

However, despite its popularity and growing use, there is still a misconception among some people that CFDs are too risky and complex. On the contrary, many people who have included CFDs in their portfolio said they did so because of the myriad of benefits that come with it including ease of trading, the leverage component and risk management tools.

Financial advisers are in the best position to highlight the benefits of CFDs which may not be readily obvious to their clients. Here, we've outlined some of the common myths about CFDs and how advisers can dispel them for their clients' benefit.

MYTH 1

CFDs are complex

CFDs are much simpler and relatively easy to understand compared to other derivatives. If you have any experience with share investing, you will find it very easy to include CFDs in your portfolio. This is because share CFDs are very similar to investing in physical shares. Whatever knowledge you have about shares – how to buy and sell, what to buy and sell – will be useful when you use share CFDs because the price of CFDs moves in line with the price of the underlying shares. For example, if BHP Billiton's share price goes up by 25 cents, the price of the BHP Billiton share CFD will also go up by 25 cents. The same way you make money in shares – by buying low and selling high or selling high



CFDs are much simpler
and relatively easy to
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and buying low – applies with CFDs. Some people have actually described CFD trading as very similar to share trading/investing with the added benefit of leverage.

As more and more people realise the benefits and potential of CFDs in their portfolio, there is also a continuing effort from many CFD providers to offer education and training sessions to a wide range of traders and investors. Whether you're new to CFDs or have been investing for the long term or wanting to expand into new innovative products that will enhance your portfolio, there are many CFD specific education and training materials that will help you and your clients to fully grasp the potential of the product. Consult any of the major and reputable CFD providers for education materials including:

- Getting started in CFD trading
- Trading Australian and international CFDs
- Trading psychology
- Short-term trading strategies
- Trading FX (currency pairs) CFDs
- Risk management strategies

MYTH 2

CFDs are risky

Like any other investment vehicle, CFDs carry their own risks. However, there are also risk management tools that are readily available to those who want to include CFDs in their portfolio. Some of these risk management tools are not available to other investment vehicles such as shares, properties or other derivatives. In a sense you and your clients can manage the risk on the overall portfolio with CFDs better than with other products because of the built-in risk management tools.

At the same time there are literally thousands of CFDs that can be traded over shares, indices, sectors, commodities and even currency pairs. CFDs are available on Australian as well as international markets including the US, UK, Europe and Asia. This means you have a wide range of instruments and markets to choose from so you are not limited to a single market or instrument. In the overall context of your portfolio, you don't have to put all your eggs in one basket. With CFDs you can diversify as much or as little as you see fit.

MYTH 3

CFDs are only for traders

If you look and consider the growth and lifecycle of financial products and investment vehicles, you would see a similar pattern with CFDs. That means when it was first introduced in the country, there were early adopters who took advantage of its benefits. Then another group of investors came along and today we are seeing the next wave of investors who see and appreciate the various features and potential of the product. Today, there are many long-term investors, DIY Super administrators and other self-directed individuals who are using CFDs in their portfolios. It is interesting to note that the longer CFDs are in the market, the better people's understanding and appreciation of this innovative investment vehicle's role in the overall wealth creation program become – and that, you can include it in your overall wealth protection and wealth building program.

While CFDs are still relatively new in Australia, they are enjoying a healthy level of growth because of their versatility. Every year there are new instruments and new products available providing access to a growing list of tradeable CFDs to suit investors and traders alike.

CASE STUDIES

Case study 1

Hamish Thompson, trader

From the day he started investing, Hamish has been a trader. He started trading options but gave them up for CFDs. Some of his gains have been impressive; in one 12-week period, he turned \$12,400 into \$62,000. In one quarter, he made a 102 per cent return. But he has made plenty of losses as well.

At age 17, Hamish took over the management of the family cattle and sheep farm with his older brother, when his father died. Over the years he developed other business interests, including a bottle shop and a petrol station. He is also a property investor.

About 10 years ago, his brother bought him out of the farm and he sold the service station. He found himself looking for a new venture.

That's when he got into options trading. He had his ups and downs in the options markets and decided to give CFDs a try.

Thompson uses a mechanical trading system with predefined entry and exit points. The system is largely based on a charting principle called moving averages; he will buy into a position that closes on a high above the previous peak on a rising moving average.

Thompson says, "You really have to spend time on it. I think if you want to make something decent you should devote time to it."

He trades shares and indices. An example of a trade was a long position in Paladin Resources on August 31, 2005 at \$1.75 a share. He closed his position on October 12 at \$2.10 a share. The percentage gain was 19.65 in 31 days.

"A lot of people wait for the perfect entry. In the meantime they are missing out on what could be a good trade. No one knows how a trade will turn out."

Thompson says he was "surprised and a bit shocked" when he made his first loss early on in his trading career. He says, "I did not think about what would happen if I lost or I had losses with my trades. I had a few sleepless nights.

"You have to accept that losses are part of trading and I've learned how to deal with them. You just have to move on. Just accept it as part of the business. It's like any other form of business losses. Learn from your mistakes and see what you can improve on."

Case study 2

Jim Smith*, accountant

Jim has been investing in the Australian sharemarket for a long time. He doesn't consider himself much of a stock picker but he feels confident picking the trends. Index funds suit his style and when he has a strong view on the direction of the market, he is prepared to back his judgement by using the leverage that a CFD offers.

Jim first became interested in CFDs towards the end of 2002, when the CFD market was still new to Australian investors. It was the end of the second year of a bear market and Jim was concerned about the erosion of the value of his portfolio. He decided to use a CFD contract to hedge his stock position.

Jim set up a hedge by shorting the ASX Top 20 using CFD contracts. With an initial deposit of \$50,000 he established a portfolio of \$500,000. As a short seller he received interest from the CFD provider and as the market fell through the first quarter of 2003 the hedge made a profit. When he closed out his contract at the end of the first quarter 2003 the CFD position produced a return of \$23,728.

Towards the end of 2006, Jim came to the view that the Australian sharemarket would have another strong year in 2007. He decided to double his exposure to Aussie equities using CFDs. Jim knows he is no stock picker, so he decided to use an ASX 200 index CFD for leverage.

His \$50,000 initial deposit gave him exposure to a \$500,000 portfolio. Over the six months he held the position he paid interest of a little over \$18,000, received dividends worth \$7,000 and produced a return of \$53,000 on his position. When he closed out the contact at the end of June 2007, his \$50,000 initial deposit had increased to a balance of more than \$91,000.

* Not his real name.



EASY GUIDE

A comparison of CFD vs margin lending vs options and warrants.

FEATURE	CFDs	MARGIN LENDING	OPTIONS/ WARRANTS
Leverage	✓	✓	✓
FX, commodities	✓	✗	✗
Tight spreads	✓	na	✗
No establishment fees	✓	varies	✓
no account minimum	✓	✗	✗
Go short	✓	limited	✓
Liquidity	✓	✓	✗
No expiry date	✓	✓	✗
Use within super	✓	✗	✓
Assessable for income, CGT	✓	✓	✓

Source: CMC Markets

GLOSSARY

Contract for difference	A contract for difference or CFD is an agreement which allows you to make a profit or loss from fluctuations in the price of the underlying instrument.
Over the counter	Over the Counter ("OTC") means that you do not trade in a CFD through an exchange or market; rather, it is a transaction between you and the CFD provider.
Long and short positions	When you buy a financial instrument, you have a long position. When you sell a financial instrument, you have a short position.
Market maker	A firm who quotes both a buy and a sell price in a financial instrument or commodity, hoping to make a profit on the turn or the bid/offer spread.
Margin call	A demand for payment on a leveraged instrument.
Stop-loss order	A stop-loss order is an order you place either online or by calling the provider to close your position when it reaches a certain point.
Total equity	The money you deposited in your account plus dealings conducted on your account and the positions you hold. The total equity balance is used to establish if there is a requirement for additional margin to be paid in respect of your account.
Trailing stop	Stop-loss positions can be adjusted as the price of the underlying security rises. If the shares are worth \$30 when they are purchased the stop loss might be set at \$25. If the share price goes up to \$40 the stop loss can be adjusted up to \$35.

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