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Mark Minervini

Meet one of Wall Street's most remarkable success stories – YTE's **Ben Power** speaks with market wizard, **Mark Minervini**.

A former musician, Minervini began trading stocks in 1983 and faced a number of years of losses. But he persisted. His breakthrough came when he read Richard Love's little-known book, 'Superperformance Stocks', which outlined the characteristics of the market's biggest winners.

Minervini honed his strategy and – as highlighted in Jack Schwager's 'Stock Market Wizards' – in a five-and-a-half-year period generated an average annual compound return of 220 per cent. To put that in perspective, a $10,000 account would explode to $3.3 million with those returns. Even more impressive was his risk – Minervini had only one losing quarter, when he was down just a fraction of one per cent.

Minervini also won the 1997 US Investing Championship with a 155 per cent return, and went on to run a successful investment advisor firm, Quantech, which worked with some of Wall Street's leading hedge funds and investors.

But it has not just been spectacular returns that have distinguished Minervini. He has also made a series of prescient market calls and protected his account with defensive moves. In August 1998, he publicly said the market was showing similarities to the 1987 crash. The next day the market slumped 508 points. Minervini then turned bullish a month later and rode several stocks to huge gains. In May 2000 Minervini successfully called the bear market in internet stocks and put most of his account in cash.

The core of Minervini's strategy is SEPA (Specific Entry Point Analysis), a proprietary computer-driven technology based on models derived from historic winners. SEPA combines quantitative screening, fundamental research and qualitative analysis to identify stocks with the potential for significant price appreciation.

In addition to his own trading, Minervini has turned to educating traders with Minervini Private Access. Members gain access to live stock selections and even a live trading room, where a moderator reviews and explains the rationale of, and analyses, Minervini's trades.

Mark Minervini spoke with YTE's Ben Power

You started your career as a drummer. How did you shift into trading?

I simply opened a brokerage account and started trading my own money. I saw the stock market as the ultimate financial opportunity without prejudice. That's the beauty of the stock market, it's just you and the market; you don't need anyone's permission. The market doesn't care about pedigree, it treats everyone equally. It doesn't care if you're a drummer or a plumber. It gives you pure, instant feedback, and it never lies to you. Each night, you get an honest assessment or 'report card' – your account balance. I began investing in stocks in 1983. I started with a small amount of capital that I earned working as a musician. For about five or six years I didn't make any money. In fact, I lost money. It wasn't easy to stick with it through those difficult years, but my love of speculation kept me going. Eventually, I acquired the necessary skill to succeed. Over time, I grew my trading account. The rest is history.

How did being profiled in 'Stock Market Wizards' change your career?

It didn't really change my career very much. My career had consisted mainly of trading my own money. Although I sold research to institutional clients for a time, 95 per cent of my wealth has been created trading my

own account. By the time I was interviewed in 'Stock Market Wizards', I had pretty much accomplished my financial goals. I have never been very interested in managing other people's money, so I didn't leverage the book as much as I could have.

In your Market Wizards interview you cited Richard Love's book, 'Superperformance Stocks' as a major influence. His book is long out of print. How exactly did Love define a 'superperformance' stock'?

A stock that advances 300 per cent or more within a two-year period.

Believers in the efficient markets hypothesis, who say it's almost impossible to beat the market, concede that momentum stocks are one strategy that can deliver above-market gains. Would you describe your trading as momentum?

I don't really like labels, but I guess I fall into the trend-following/momentum camp. I definitely have a bias toward growth.

You call your strategy Specific Entry Point Analysis (SEPA). Can you explain it a little?

SEPA® is a strategy of precision. Timing is a key component. The objective of SEPA® is to take all the pertinent information available, and pinpoint, in terms of reward versus risk, the precise spot at which to enter a high-probability trade. This is achieved by taking into account what we know influences institutional buyers. The key is convergence. SEPA® employs a method of stacking supporting probabilities. For example, if one variable is present, you may have a certain theoretical probability of a particular outcome, while a different variable may have a certain other probability; and so forth. The probability from combining the variables is not as simple as just an average. By stacking supporting probabilities, the cumulative probability can increase exponentially as each variable is added to the equation. We take into account all sorts of data, including fundamental and technical. Once the supporting criteria are met, we look for a low-risk entry point.

What fundamentals are you looking for in a stock?

Optimally, I want to own companies that are delivering the goods; strong earnings, sales and margin growth. I'm looking for those that have something really great going on, which translates into bottom line success. It's not much different from what any good growth manager would look for.

You've said you enter when a stock breaks out of a constructive consolidation. How do you define a constructive consolidation?

A constructive consolidation is one that has gone through the proper supply/demand dynamics, which sets the stock up for a line of least resistance. If the stock is under accumulation, the consolidation will represent a period where strong holders ultimately absorb weaker ones. Once the 'weak hands' have been eliminated, lack of supply allows the stock to move higher because even a small demand will overwhelm the small supply. Stocks that are under institutional accumulation will rest and consolidate within the context of a long-term uptrend and then continue higher. Most of these situations will show telltale signs.

You've said you stick to your system even when it's not performing well. Does your system perform best in a trending market?

Yes. As defined by our Trend Template qualifier, I require a stock to be in a confirmed uptrend prior to my purchase. So, by definition, a trending market is the best environment for my style.

How did your system perform during the recent bear market?

With the exception of some short positions, I was in cash during most of the decline. I'm not likely to be caught in a major decline, because our stop-loss discipline gets us out fairly early. You won't get too far off track, if you allow the market to guide you. However, if you argue with the market, eventually you will suffer a major setback. For a strategy like the one I employ, a back-and-forth volatile market is actually riskier and potentially more destructive than a declining market. If the market breaks down and trends, I'm out and that's the end of it. However, in a whipsaw environment, the risk in using relatively tight stops is getting repeatedly stopped-out and suffering a large loss as a result of a bunch of small losses.

We have seen big gains lately in the US stock market particularly, but those gains were led by many stocks with poor fundamentals. Is that changing? And how have you played this bull market?

I don't think I would necessarily categorise this bull market as being led by stocks with poor fundamentals. Many of the leaders during this bull run sported excellent fundamentals. NFLX, AAPL, BIDU, CMG, FFIV, RVBD, PAY, LULU, TIBX, GMCR are all examples of leaders that had great fundamentals.

Do you have an example of a recent winning trade and chart?

Body Central Corp. (BODY) – Stock went IPO in October 2010. I bought it on 5 January 2011 and sold it just five days later, on 11 January 2011 (figure 1). The stock rallied almost 50 per cent in six days. This is the type of situation I look for.

You've said you often sell too early. What would trigger your exit from a winner?

I may simply sell when I have a big gain that I'm satisfied with. I'm not really concerned with getting the highest price, I'm concerned with making more than I risk and repeating that consistently. The five- or ten-bagger is not something I need to achieve to make big returns. When I make a very good gain, generally when it reaches a multiple of my risk, I look to protect what I've made, and at some point sell the stock. If the stock is really strong, I may stay with it, unless I think it's too far ahead of itself and it appears vulnerable. The key is to make more than you risk, do it consistently, and avoid large losses. Once you can do that, you can work on optimising your trading.

Where do you set your stop-loss points?

Depending upon my position size and the liquidity of the stock, my stops generally range between low-to-mid single-digit. My 'Uncle Point' is 10 per cent maximum. I never want to lose more than that

FIGURE 1: BODY CENTRAL – BODY

on any one trade. I will also sell if I think the trade has technically or fundamentally gone sour, often before my stop is hit. I back into risk; position size is based on where the stop-loss is.

SEPA looks for trades with high potential reward/risk ratio. How do you determine reward/risk?

After trading tens of thousands of stocks, I have a pretty good idea of what I can expect from my trades on average; intuitively and scientifically. That's because the buys are made under very consistent, reliable conditions (the set-up). I also rely upon our Leadership Profile® of past stock market winners as a guide. This is in addition to in-depth post-analysis of my own trades. The estimated profit is a very important consideration when deciding the amount of risk I'm going to take. I back into risk according to what I expect to gain. From that perspective, the stop is a mathematical calculation. However, the price action of the stock is also very important and telling. I enter trades at very specific points using charts. So, it's a balancing act between math and technical analysis.

How long do you tend to hold stocks for?

On average, maybe 20 trading days. However, much of that is due to high turnover as a result of loss cutting, which generally occurs quickly, within the first five to ten days on average. It's not uncommon to hold a winner for several quarters. I rarely hold for long-term capital gains (a year or more).

Are you still shorting stocks?

Yes, but I do relatively less shorting in a bull market than in a bear market.

Many traders say the biggest challenge is when markets change and their system starts underperforming. Do you thing markets change, and have changed? Or do you think they cycle? (The former implies the need to reinvent new systems constantly; the latter implies sitting out rough patches.)

Stocks today rise and fall for the same basic reasons as before: people drive stock prices, and people stay basically the same. Fads come and go. Businesses grow by doing things better, more cheaply, and more effectively. Has the way you throw a baseball, a football or a basketball changed very much? Has the way you throw a punch in boxing changed much over time? I certainly strive to improve my techniques, but there are certain fundamentals that, for the most part, are timeless. Very little has changed in the market except more information moves faster than before. I try to approach trading through timeless truths. If you base your approach on timeless principles, you have the best chance for longevity, and you won't have to constantly reinvent your method. I'm doing the same things I've done for several decades, and the results are consistent.

You've recommended new traders get a mentor. Do you have one yourself?

I never had the luxury of a personal mentor, other than reading books. Back in the day, during my first six or seven years trading, I spent most of my time in libraries because I didn't have much money to buy books. However, you don't have to go it alone these days. Today, we have access to all sorts of information and talent through the internet and technology. Take advantage of it. The learning curve is shorter than ever.

In 'Stock Market Wizards' you said you rarely took a holiday from the market. Does trading success require that kind of obsession and focus?

I think to be outstanding at anything requires a major commitment. In order to be great at something, you must be focused and somewhat unbalanced and maybe even obsessed. Champions don't have balanced lives; they are laser-focused and obsessed with winning. Passion is unbridled.

Finally, what is one thing traders can start doing now to improve their performance?

Know the truth about your trading. Find out where you're going wrong and what areas need improvement. Look for common denominators and your emotional tendencies. Understand why you do what you do. Improve your weaknesses until you have no weaknesses. Believe it or not, few traders really take the time to analyse their results and truly understand their trading. It takes time and attention to detail; big success is not going to happen overnight, and it's definitely not going to be easy. However, the rewards are well worth the effort. The bottom line is that those who can weather the learning curve and those who can handle the truth about their trading make it, and those who can't, find another line of work. And then, there are those who are oblivious; they eventually self-destruct. As Gordon Gekko put it: "A fool and his money are lucky enough to get together in the first place." YTE

Ben Power *is a writer, journalist and trader. He has written on politics, economics and finance for numerous publications.*