So you want to be your own hedge fund manager?

BY TERRY NUGENT

"What you're doing is stupid." If you've been managing your own investments, that is not what you want to hear.

But hear it I did one day from an old friend.

I'd been managing my own money for my entire life with a modicum of success, not because I relished the task nor was overly qualified (my MBA is in marketing, not finance). But I learned early not to trust brokers and other commissioned financial salespeople when my post-college roomie sold me a load (heavily commissionable) mutual fund. The only thing that grew was his commissions! This tuition in the school of hard knocks was valuable.

Unfortunately banks, insurance companies, many investment advisors, and others merit caution. Perhaps Bernie Madoff's only socially redeeming value is forever disabusing people of the notion that they can trust anyone with their money.

So most of my life I felt pretty smug. I maxed my 401K, saved, invested in no-load (no commission) Vanguard mutual funds. Results: not spectacular, but steady growth. Then came the great recession. Investments dropped 30-40%. Business was down. Expenses rose. I wondered where the bottom was and realized it was zero. That's when my friend told me what I was doing was stupid. His timing was right. I had to step up my game.

My friend told me that there are ways to put a bottom well above zero in the market, to, in effect, insure your portfolio, and even to profit when stocks go down. In addition, there are tools you can use to employ leverage to profit from moves in the market for premiums that are a small fraction of the cost of buying stock outright.

KNOWLEDGE IS KEY

There's no free lunch and you have to know what you're doing. But the concept appealed to me. So I decided to enroll at the Chicago School of Trading. It was very challenging, but I learned a lot. Part of the course was "paper trading," which is using what you've learned to trade on paper, sort of a flight simulator experience. Once I demonstrated competence and gained confidence, I moved to the real thing.

How did I do? I'll tell you at the end (blatant tease as they say on CNBC).

So the first step is education. If you're going to be your own hedge fund manager, you *have* to be informed. My sources include CNBC (which is available online and via XM radio as well as cable, facilitating relatively constant exposure), *The Wall Street Journal*, *Business Week*, Morningstar online, and *Barron's*.

These can be fascinating. There are also synergies with the day job. Since healthcare represents such a big piece of the economy, it occupies much of the investment media. It's also an area where medical marketers have an edge.

Without making your eyes glaze over with technicals, one strategy that has a big payoff potential is a position that makes money when a stock makes a big move ("gap up" in the industry jargon) in either direction (up or down). This is a very profitable tool for FDA hearings on new drug applications (NDA), which I have used to generate fairly good profits on more than one occasion. One could also have used industry knowledge to capitalize on health reform—the market was far more worried about reform's impact on pharma than many of us in the business, who were confident that the public option would not prevail.

Here's what you should know about CNBC to use it efficiently. It's in the ratings biz, so beware the hype; many purported market movers are not in the event. There are only a couple of must-watch shows for traders, hosted by very bright Harvard grads—*Fast Money* (Melissa Lee) and *Mad Money* (Jim Cramer).

CNBC's MAD MONEY PEARLS

Yes, Cramer has substance beneath the bombastic style. Here are some pearls of wisdom from the Cramer investing dogma:

1). Buy individual stocks that meet a proven profile.

2.) Anticipate cycles. Big institutional investors rotate from sector to sector as predictable economic cycles transpire. Your job is to buy before they do. Buy banks before the institutions buy them. Sell banks shortly after. It can be done, and must be if you want to beat the market.

3.) Do your homework. Research each of your stocks at least an hour a week. Sounds tough, but how much time do you spend on hobbies? Make this your hobby and you'll have fun and profit too.

4.) As a function of (3) above, limit your portfolio to a relatively small number of stocks—at least five but no more than 20. You only have so much time—five stocks means five hours a week of homework. Twenty is a half-time job.

5.) Diversify. If you have five stocks, don't own five banks. Pick them in five different sectors. Pick the best company and the best stock in each sector (Cramer emphasizes that the company and the stock are two different things).

6.) Last, but not least, don't bet the farm. Trade with money you don't need for retirement or the kids' college. It should be a relatively small percentage of your assets. I would say no more than 10-20% for starters.

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BILL DIXON

Bill taught me about humility and availability. We met at a business conference, pre bits and bytes, and became very good friends. In our earlier days, Bill, a couple of years older than me, was always a call away to share his experience with marriage, travel, and business. We often travelled together and once, while in Washington D.C., he tearfully showed me the home his family lived in during WWII. Over the years, Bill became wildly successful and could easily do the money show for all to see, yet he remains humble. He lives a life that inspires and motivates. While he's the President of his company, he has always made time to be one of the most thoughtful dad's I know, offering thousands of hours coaching a high school track team. Whenever I see Bill, the conversation alone pulls up lessons in humility and helps me navigate that trait. Bill is one of a kind and I am very lucky to be part of his teaching.

JACK KEMNITZ

This is a bittersweet memory, as one of my best friends Jack passed away several years ago… Jack knew his priorities. We met in high school, started college together, married and raised families at the same time and even ran a successful, very fun, side business together. Jack lived life on this level—have fun, hang with your friends, and fit your family like a glove. His positive influence stays with me. Every day I can see Jack's smile, hear his storytelling, remember his upbeat phone calls and his pride when he became a grandpa. I will always see Jack moderating over feisty friend debates with a smile and cheerfulness that set it all straight.

Recently Jack's youngest son married and a bunch of old friends gathered. We felt his presence at the wedding and we all felt better for it.

Thanks Jack. Hope to catch up with you some day.

The Legions

Each "Pillar" I have singled out was part of my life at different times; each played a significant role in making me who I am both in my business and personal life. The lesson has been an easy one: You go nowhere and do nothing without PEOPLE. The people you know are the treasures you have and keep forever with you.

To that end I have listed others who were part of my roadmap. Pillars in their own right, they helped keep me focused and moving forward.

Michael Springer, John Sheehy, Etta Fielek, Alan Greenberg, Chris Whittle, Charlie Sicola, Paul Jaffe, Pres Williams, Dick Kiernan, Bill Kissinger, Retzie Gleeson, Al Kitchen, Lois Fisher, and more.

To all those who have been pillars supplying radar both active and passive, I owe a tremendous gratitude. It has been great to work and play amongst the best and emerge each day with the experience and memories of a lifetime.

The beauty of it all is there are always new pillars to keep the movement on task. Thanks to all.

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ON THE RIGHT PATH

So this has been my journey, from a mutual fund buy-and-hold guy, to a stock picking, home gamer hedge fund manager—an aspiring investor. I look at it as sort of a hobby/second job, and maybe a second career down the road. To use a medical education analogy, my options course was medical school, and the last few months are a residency. Hopefully, I'll become a competent practitioner. But even experienced investors are always learning the lessons the market teaches. So, believe me, the tuition for education and information that gives you the edge is a bargain by comparison to the school of hard knocks that is the market.

RESULTS

So how have I done? Well, compared to the Madoff victims, not bad. Seriously, at the time their article was written, I was up about 23% YTD which would be 70% annualized. Best of all, I've realized an 1100% return on my trading school tuition. But the real revelation is how well I could have done if I had known these techniques when the crash happened. I could have protected myself from the downturn and had the courage to bet on the upside all the way up. Fortunes were made in those days (read *The Big Short: Inside the Doosmday Machine* by Michael Lewis).

IS THIS FOR YOU?

It's not for everybody. It's hard work. It has to be done carefully. But you gain control over your financial destiny. You learn a lot and come to understand what's happening and why. Best of all, you don't have to worry about huge losses in downturns, or take the ultimate risk-investment risk of falling prey to Madoff-style fraud.

If you're interested in going down this road, I recommend Jim Cramer's books (*Getting Back to Even* is the latest one; *Real Money* outlines his cyclical theory, which I wholeheartedly endorse). His website, *thestreet.com*, has some great research (you can sign up for free; then you will get bombarded with marketing for paid content—the promotion is annoying but the content is actually quite good).

For options education, I highly recommend The Chicago School of Trading (*www.thechicagoschooloftrading.com*). There you will find the friend who got me started on my journey, Dan Keegan. Mention my name.

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