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Questioning Market Leaders For Long Term Investors

SPECIAL INTERVIEW JEFF PIERCE

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J E F F P I E R C E



TWST: Why don't we start with you telling us about yourself and how you got into investing in the first place?

Mr. Pierce: I was first exposed to the stock market in my junior year of high school in an economics class. We had a stock contest where you would pick a basket of stocks and track them over 3 months

with the goal to be the top performer. You were only allowed to make changes to your portfolio each Friday, and our teacher would talk a little about the current events that drove the markets higher or lower. It was very basic, but it opened up my eyes to the idea of using money to make money. This is something I could get on board with because I've always believed in the concept of "working smarter, not harder."

After I completed a few years in college and entered the workforce, I had saved up some money and decided to test my luck in the Stock Market. Everyone seemed to be talking about the spectacular gains that can be made by investing in the Internet stocks, which were rising 5-10% each day. So I started watching Lou Dobbs each night and Bloomberg in the mornings before work to familiarize myself with the markets, opened an account with Ameritrade and began learning how to trade. I didn't even own a computer when I first started, so I had to do my research at my local library. Luckily for me, I began investing at a time when you could basically toss a dart at the financial section and buy that stock and it would go up, or I probably wouldn't be where I'm at today.

TWST: How did that progress or you were doing quite well with the dart-throwing picks?

Mr. Pierce: Oh I never utilized the dart approach, but I'm sure it would have yielded nice gains given the environment. I did however devise a stock picking strategy that I felt comfortable with. I subscribed to a few newsletters: Michael Murphy's Technology, and John Dessauer's Investor's World, that way I had growth and value investing approaches both covered, as I was trying to discover what type of trader I was. And what I hoped to learn from these newsletters was how they chose stocks and their logic behind those reasons. What types of targets were their buys and sells, and when a stock such as Dell was a buy under 40, I would observe the chart and try to grab it as far under 40 as possible, then cash

out a few points on the upside. I'll never forget my very first trade in Iomega, a data storage company. I made \$364 in 90 minutes and I was hooked.

During these initial stages of my learning curve, I found myself gravitating towards a more trader mentality than a long-term value oriented investor. I could never wrap my head around holding something after it's moved up 20 percent, knowing full well it was likely to decline, only to watch those gains disappear. I felt more comfortable in taking my profit and looking to get in at lower prices. This was basically how I traded the markets right up until the dot.com crash.

TWST: That didn't scare you off?

Mr. Pierce: I almost didn't survive the fallout from that crash. When stocks were going parabolic on the upside, being new to trading, I didn't make the huge gains that many seasoned vets did as I was afraid to buy stocks breaking out to new highs. I tripled my account during that period as investing really seemed simple, that is until the market rolled over and the air was let out of the .dot com bubble. That dropped my account to almost where I started, and I realized trading wasn't as easy as it seemed. I quickly learned that if I was going to continue trading, I had better get some new tools that enabled me to find my edge. From there I subscribed to IBD and bought a stock analysis software program called Vector Vest. These two tools really opened many doors regarding buying stocks with high relative timing, industry groups, creating scans, back testing, etc.

TWST: Tell us then about the next big crash, which just happened last month. Where you able to protect yourself somewhat?

Mr. Pierce: One of my biggest fears as a trader is being heavily long on a day when the market experiences an extreme correction, such as 9/11. I was holding many positions during that tragic event which caused me to head to the sidelines and regroup after a significant draw down in my account. This occurred again last February when the overall market was zooming higher and I had many momentum trades on and the Asian markets tanked in overnight trading, which caused a 350 point gap down the next day causing serious damage to my account. After that incident, I decided that I needed to devise a market timing system that tells me when it's safe to be long or short, or simply when a trend may be at a crossroads and about to reverse. I use a number of different moving averages spread out on different time frames and mix in a few obscure market indicators such as the Vix and CBOE Put/Call ratios that help me gauge sentiment. It has been very effective at keeping me out of all the major market drops this year and had me out of the markets

for most of August and September, which at that time I started going short. It hasn't been completely perfect, but given that I'm up for the year, I'm pretty happy with my portfolio's performance. This has been a brutal market for position traders any way you look at it. The key to surviving today's markets is to keep your position sizes small and don't really over commit on either side of the market right now. There is a big debate going on between the bulls and the bears as to whether we've hit bottom or whether we have further to fall. In my view it's really too early to be making any large bets either way.

TWST: You said that small sizes, does that mean you believe in diversification?

Mr. Pierce: One thing I've learned about myself is that whenever I have more than 8-10 stocks in my portfolio bad things tend to happen. Those are the times that my bias towards a particular trend begins to run my trading. A mistake can come in the form of a missed chance to take profits on stocks I own or miss potential trade opportunities because I'm distracted with my growing portfolio. I think it's important for each investor to find that perfect number of equities to own that they feel comfortable with.

The idea of small sizes comes into play with how much of a stake I begin my initial purchase with. When I've correctly identified a trend in the market and deem it safe to buy stocks on the long side, normally I'll buy half a position and add to it as it rises. If it doesn't move the way I anticipated it would, I'll cut my losses and move on. Given all the volatility in today's markets, I've scaled down my initial entry to a quarter of a full position size to keep my risks small. While it's true you limit your potential profit by starting with such a small initial investment, you also limit your potential losses. I read somewhere that amateurs assess potential, while professionals assess risk.

TWST: Do you still focus on the technology stocks that you started with? Is that the area that you like the best?

Mr. Pierce: I'll trade any stock that fits my trading criteria regardless of the sector or capitalization. I would say most of the stocks that show up on my scans are small caps, but earlier this year I noticed many large caps showing up. If the stock is breaking out to new highs or lows on big volume, meets my volume requirements, and it fits my certain chart patterns I'll trade it.

TWST: You live in Canada. Do you invest in Canadian or US stocks or a mix?

Mr. Pierce: I primarily invest in US stocks because they have more liquidity than Canadian stocks. When commodities turn around I'll be focusing a little more on Canadian issues, as the TSX is a commodity-based index. I have a few Canadian scans that will let me know when the time is right to look there for opportunities.

TWST: Would you describe yourself as a swing trader?

Mr. Pierce: I would because my typical holding period is anywhere from a day to a month. It really depends on how fast the stock moves after I buy it. If a stock goes up 10% the same day I purchase it, typically I'll take partial profits and let the rest run. If it slowly grinds higher, I'll hold it longer. It really depends on each individual issue to determine when momentum may be exhausting itself. You also have to pay attention to the overall market for signs of strength or weakness.

TWST: Tell us about your sell process and do you set targets?

Mr. Pierce: I've never really been one to use hard stops because whenever I do I tend to get shaken out of a stock. I invest in momentum stocks and have to factor in an extra degree of volatility that I counter that with mental stops. If I weren't able to be in front on my computer all day I would have a totally different approach. Over the years a trader develops many ways to take profits and it really comes down to training your eye to look for certain overbought patterns. One of the ways I can take profits is a close outside the upper or lower bollinger band if the stock has been on a nice run and the overall market is getting extended. I'm also a big fan of scaling out of positions to maximize the move. If I'm holding a stock and it moves 8-10%, I'll take a certain amount off the table and set a hard stop at my purchase price. I do this based on Mark Douglas's principle of "paying myself as the market makes money available to me." That way if the stock goes all the way back to my original purchase price, I avoid turning a gain into a loss and I will at least have some profit to show for it. This helps my mindset greatly from become frustrated because at least I've made something. Keeping your confidence high is very important in trading.

TWST: You have a Blog and it's called Zentrader, what does that mean to you?

Mr. Pierce: Yes, I started Zentrader.ca in July as a way to share what I've learned through the years and also provide market analysis with various trade ideas. Being a trader can be a lonely profession, so it's nice to journal my thoughts and receive feedback from other traders. I think it's also a way to reinforce your own rules and be held accountable in your trading.

The concept of Zen trading is to control your emotions at all time and never let them alter your trade plan while eliminating as much stress as possible from your daily trading routine. This entails having a very specific trading plan and having the discipline to follow through. Having the proper mindset is half the battle of trading, because the moment you lose control, you begin trading based on fear and greed and that's a recipe for disaster. Every trader has made a mistake, gotten scared out of a stock too early, or bought a stock because they felt like they were going to miss out on

some big move, only to regret it. It's OK to make a bad trade, but you have to realize what you did wrong, correct it, and implement a game plan so it doesn't happen again.

Earlier this month I had someone leave a comment that really made me grateful that I started blogging. This investor was about to give up on trading because of a large loss he had incurred due to an imprudent trading plan. Since he discovered my blog he credits me to helping him find his rhythm again in these trying times. It was a great feeling to know that my blog could have that kind of an effect on other traders.

TWST: That brings us to Covestor. Has that helped you by feeling that you are not alone out there, but there are people to contact or watch their progress?

Mr. Pierce: Covestor is an ingenious idea in my view. Over the last decade, I've had numerous people ask me how I think they should invest their money and there really isn't anything I can tell them. If I tell Bob to buy a stock because I just bought it and I think it's going to go up, then I have to tell him exactly when to sell it. If I'm unable to reach him at the exact time I sell, then it could drop and Bob's return would be drastically different than mine. And that's where Covestor enters the picture as an amazing resource for people who have capital, but don't have the time or resources to be a trader. They can register with your site and start following traders within the community and learn about people's ideologies on the market and can basically piggy back any trader they've deemed to be successful based on that trader's track record. The great part about being a trader is that you don't have the weight of managing a multi-million dollar portfolio and the stress that comes with that. You just trade your account and Covestor takes care of managing the funds.

I registered with Covestor as a way to give credibility to my blog by validating all of my trades. If I am talking about the Stock Market, how do people have any idea that I know what I'm talking about? I have to admit that after I signed up and all of my trades were out in the open, I did feel a little naked. Covestor has provided me with a way to compare my performance with traders just like myself in a non-competitive manner and to learn from them and share my experiences while receiving feedback about my trading. It has been very useful to get trading ideas from other successful traders and it's great to have a community to fall back on during challenging investing climates. When I first got started with Covestor, I reached out and contacted Don Bartell as he seems to be one of the most active participants in the community. I don't know where he finds the time to be so actively engaged, but people like him are what make websites like Covestor thrive and prosper.

TWST: Is there anyway that you think Covestor could help you more, do you have any suggestions?

Mr. Pierce: I do have a couple of suggestions with one being a more accurate representation of position size and percent-

age gain. What I mean by that is when I own one stock, Covestor states my portfolio as being 100% in that stock, which isn't true. It makes up a much smaller percentage and it would be useful for fellow traders to see when other traders are underweight or overweight particular stocks. The other thing I would like to see is have options being reflected in one's annualized gains and losses.

TWST: Do you have any books that you've read that you could pass on to our readers?

Mr. Pierce: I believe it's important to continually educate yourself and I've read a number of books on trading but there are three that really stand out and that I reference quite a bit. The first is Mark Douglas's Trading in the Zone, and this is for learning about market psychology and how your beliefs can effect your trading. Another is the bible of technical analysis, The Technical Analysis of Stock Trends by Edwards and McGee. That book will give you a very thorough understanding of the many different chart patterns and you can kind of pick and choose which ones that suit you the best. And the third is Reminiscences of a Stock Operator by Edwin LeFevre which includes many valuable lessons on speculation. Even though it was written over a hundred years ago, it's so applicable today because investing is all about human emotions and those never change. Two other non-trading books I've found incredibly useful for learning how the subconscious mind works, the power of visualization and autosuggestion, and goal setting are Think and Grow Rich by Napoleon Hill and The Power of Your Subconscious Mind by Dr. Joseph Murphy.

TWST: Is there is any thing that you wish to add that we didn't touch on?

Mr. Pierce: I'd like to share with you something that took me years to understand and has to be with the large myth that Wall Street will have most self-investors believe. Everyone seems to start off believing that the way to make money investing is to buy low, sell high. There are two major problems with that statement. First, investing long-term is no longer the best option and I have proof. If I would have taken my initial stake and invested it 10 years ago, I probably would have a day job now, as the market is 1000 points lower than when I started. The second myth in that statement is that stocks that are hitting new lows will eventually turn around and reward patient investors. I like to test people who don't know much about investing by asking them if they would rather buy a stock at a 52 week high or a 52 week low. Ninety percent of the time they say that they would rather buy the stock hitting new lows because it's "bound to go up." I think most traders would agree that stocks hitting new lows are there for a reason and they aren't going to turn around anytime soon. The real secret to trading is to buy high and sell higher.

TWST: Thank you.

Mr. Pierce: Thank you.