

# Warning

Warning: All content provided in this guidebook is protected by copyright law and international treaties. Unauthorized reproduction or distribution of this information, or any portion of it, may result in severe civil and criminal penalties, and will be prosecuted to the maximum extent possible under the law.

EASY GUIDE  
TO  
PENNY STOCK  
PROFITS

## PENNY STOCK PROFITS

---

© Copyright, ALL RIGHTS RESERVED

All rights reserved under the laws of the United States and provisions of the Pan-American and International Copyright Conventions. This book may not be reproduced, in whole or in part, in any form or by any means, electronic or mechanical — including photocopying, recording or by any information storage and retrieval system now known or hereafter invented — without express written permission from the publisher. This report is for information purposes only and is not intended as an offer to sell nor a solicitation to buy securities.

### IMPORTANT NOTICE

NOTICE: This publication is designed to provide valuable information. It is sold with the understanding that the publisher or author is not engaged in rendering legal, accounting, or other professional service. If legal advice or other assistance is required, the service of a competent professional should be sought.

The author and publishers disclaim any personal loss or liability caused by utilization of any information presented in this book. Claims of liability, if any, shall be limited to the amount paid for the book less the amount paid for postage and handling.

All content provided in this guidebook is protected by copyright law and international treaties. Unauthorized reproduction or distribution of this information, or any portion of it, may result in severe civil and criminal penalties, and will be prosecuted to the maximum extent possible under the law

## **Table of Contents**

Introduction.....	3
Selecting A Stock Broker.....	8
What Are Penny Stocks.....	15
What Makes Penny Stocks Different.....	21
Penny Stock Selection Secrets.....	24
Learning How To Place Your Orders.....	31
Paper Trading Is The Best Trading Education.....	37
Rules For Paper Trading.....	39
12 Rules For Penny Stock Investing.....	41
Stocks To Avoid.....	43
Cheat Sheet Check List For Penny Stock Selection.....	44
Paper Trading Records.....	47

# **EASY GUIDE TO GETTING RICH IN PENNY STOCKS**

## **Introduction**

Welcome to the fascinating world of penny stocks. By sending for this guide you have already demonstrated one of the chief characteristics of the successful penny stock investor - the ability to think on your own.

The economy and the investment markets are seeing more changes more rapidly than at any time in our history. If you have taken the plunge and purchased a personal computer in the past few years you know how very quickly that industry has come to be a dominate factor in the our personal and professional lives. It was just a few years ago that only the very largest businesses were able to afford computers because not only was the computer equipment expensive but it took a whole specially trained staff to operate and maintain it.

Five years ago the Internet was a vague concept to most of us. Yet today it is one of the most important elements in the success of many companies. Billions of dollars of business is transacted on the Internet everyday. It was a marketplace that did not even exist a few short years ago.

Today cell phones are everywhere. When I watch movies that are only a couple years old, I find myself wondering why people in trouble don't simply pull out their cell phones and call for help. Then it occurs to me, that the cell phone revolution is literally only a couple years old.

## **TIMES ARE CHANGING AND TECHNOLOGY IS THE KEY**

My how the times are changing. And those rapid changes are one of the factors that makes penny stock investing such exciting prospect. Small, often only one or two person companies can and do develop unique products which

## **PENNY STOCK PROFITS**

---

can revolutionize the business world overnight. The Palm Pilot and other handheld computer devices are ubiquitous in the business world already! Yet who would have believed the rapid advances that miniaturization in the technology world would usher in.

You don't have to be one of those geniuses who managed to envision some product or service that quickly becomes indispensable to virtually all consumers. Elantec (ELAN) manufactures analog integrated circuits (ICs) for commercial applications in markets where technology plays a major role in rapid growth. These include things like video/multimedia, communications, data processing, and instrumentation. The stock sold under \$5 (and often under \$2) for many months in 1998 and 1999. As late as Oct 22, 1999 it sold for about \$7 a share. It exploded upward reaching a high of \$123 in less than a year!! And that is only one of many high tech companies that exploded on the market making many people very rich even as the naysayers were telling people never to buy stocks below \$5 because they were too risky!!

Consider the world of technology stocks just in the last couple years. This pattern has been repeated many times as one small company after another finds a better way of doing something, or finds a niche market that proves lucrative. In only the last two years (1999 and 2000) there are many technology companies which belied the notion that penny stocks are nothing but scams.

You didn't need to understand what the heck ICs were or how they worked. But by learning what we teach you in this manual and by carefully employing the research and insights we provide in our monthly newsletter, Penny Stock Profits, you can put yourself in a position to catch some moves of this size. And it won't take many of that size of price move to make you very wealthy.

## **PENNY STOCKS OFFER GREAT OPPORTUNITIES**

But don't get us wrong. We believe that penny stocks offer outstanding opportunities. But at the same time they present very high risks, especially for those people who do not understand what to look for. The penny stock market is rife with liars, cheats, and thieves who make plenty of money. Unfortunately they do not make those huge sums by helping their clients make money. They make it by essentially stealing from their clients.

If you have a chance, take a look at the recent movie, BOILER ROOM. It is a scary and all too accurate picture of the very successful high pressure techniques employed by the sophisticated stockbroker con artists who lurk in the penny stock world. One of the most important things you will learn in this guide, is how to spot the cons and how to avoid them.

Information on penny stocks is not as widely available as on listed stocks. Much of what exists is often produced by interested parties with strong conflicts of interest. A classic example is the proliferation of chat rooms on the Internet.

## PENNY STOCK PROFITS

---

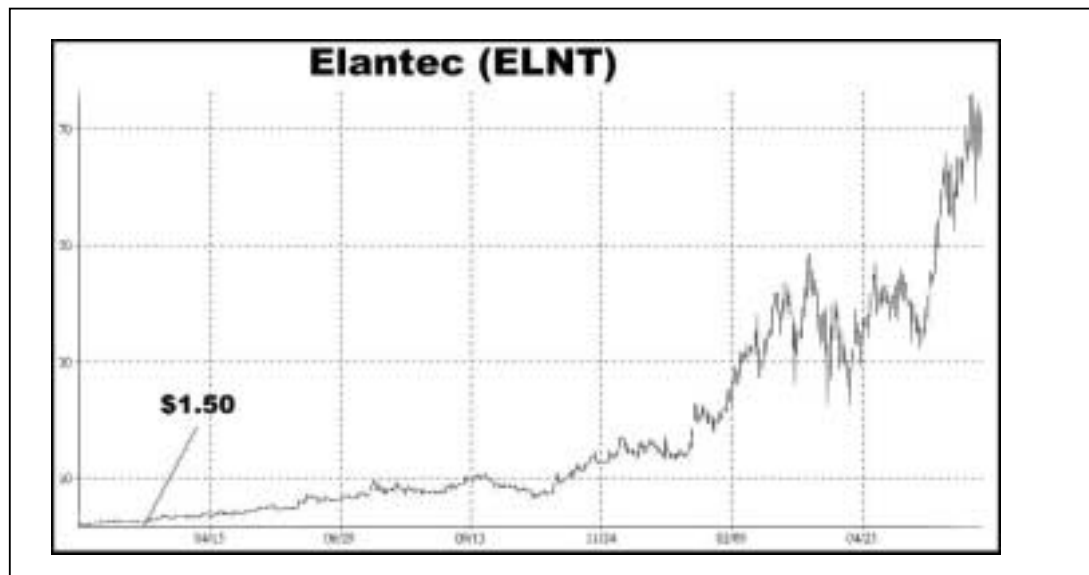
You can go to these chat rooms and read 100s of "tips" about every piece of garbage imaginable.

You should never use money that you cannot afford to lose when investing in penny stocks. In fact, you should never invest money that you cannot afford to lose in any type of stocks.

Far more penny stocks wind up dropping to zero as the companies go broke, than higher priced stocks. It is a fact of life in this sector of the stock market. If you can't deal with that then penny stocks are not for you. We teach you methods to minimize that danger. But no one can honestly tell you that investing in penny stocks is a no risk proposition. But frankly, that is one of its attractions. High rewards come from high risk. If you can't handle risk, put your money in the bank or government bonds. But you will never get rich that way!! If you can afford to set money aside for high risk speculation then the penny stock market is one area you should seriously consider.

## THE KEY TO SUCCESS IN PENNY STOCKS IS PROPER CAREFUL SELECTION

In the pages that follow we outline our approach to selecting and investing in penny stocks. But the one thing that is most important of all, is that you must employ an approach that is comfortable for you. We cover many different ideas here. Don't fee that you have to use all of them. In fact, that would be most unwise. Select the things that make sense to you and you will be far ahead of most investors who are continually trying to force fit their personalities into an approach that they do not really believe in. You must be committed to make money. A half-hearted approach will not work.



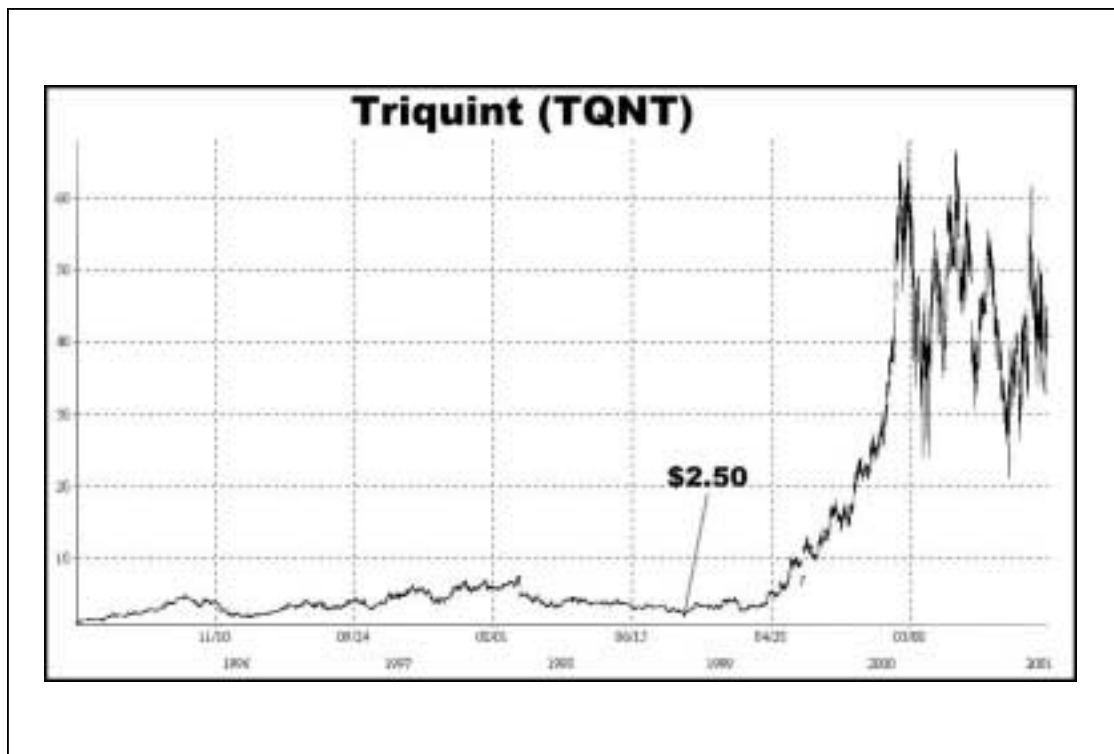
## PENNY STOCK PROFITS

---

When to buy is easy. And strangely enough that is what most investors spend most of their time doing. About 95% of the average investors time is spent researching, analyzing, and finally determining what to buy. Yet the far more important decision is when to sell. Once you buy you are already committed. You cannot change that fact.

The buy decision does not make you any money! Only when you sell will you finally determine if you made money. Your selling decision determines if you make a little money (sold too quickly), a lot money (let your profits run). But your selling decision also will determine if you lose a little money (cut your losses short) or if you lose a lot of money (stubbornly refuse to admit you're wrong) and perhaps lose any chance to make it back. After all you can no longer play the game if you lose all your chips. If you lose all your money, you cannot make it back because you can't buy anything else! We teach you our own approach for knowing our selling plan before we buy.

We welcome you to the exciting world of penny stocks. We will do our very best to help you in every way we know to profit in this wild and exciting investment world.



## **SELECTING A STOCK BROKER**

The very first step you must take before you can ever invest in penny stocks is to select a broker. This is an important decision because broker's fees, services, customer service, ease of use, method of operation, and willingness to accept penny stock business all can play a very big role in your ultimate success.

As we mention in the very first section of this report, there are many different definitions of penny stocks. While we use the simple "everything below \$5 is a penny stock," you will find a wide range of definitions among brokers. It is important to understand primarily because some firms tack on additional charges for penny stock business.

Most brokerage firms do everything they can to discourage penny stock trading, especially for those issues trading for less than \$1. For example, WYSE Securities charges a flat rate of \$15.45 for stocks selling for more than \$1. However, for stocks selling at \$1 or less, the commission jumps to a base of \$29.50 PLUS 2.75% of the amount of the trade.

Watch how the brokers define penny stocks because some, like InvesTrade define a penny stock as anything sell at \$2 or less. InvesTrade's basic commission rates jumps from \$11.95 to \$29 for stocks selling at \$2 or less.

Typically OTC:BB and pink sheet stocks are considered penny stocks by most firms, regardless of price. Expect to pay higher fees to transact business in these stocks.

## **BETTER QUALITY PENNY STOCKS ON NYSE, ASE, AND NASDAQ**

Since our penny stock selections are limited to the NYSE, ASE, and NASDAQ this is normally not a problem though some firms still assess higher fees even for stocks listed on exchanges. This is because the exchanges assess "per share fees" which mount up quickly with penny stocks because a small investment can still buy a lot of shares. However, if you do plan to ferret out bargains in the high risk OCT:BB or pink sheet stocks, you should be prepared to search for brokers willing to take the trades. And if you find a firm that is anxious for your below \$1 stock business, be careful, be very careful!!

There are a number of reasons for brokers discouraging penny stock business. The primary one is that the regulatory agencies make life very miserable for brokers transacting penny stock business. Imagine have some government bureaucrat with the power to close you down looking over your

## **PENNY STOCK PROFITS**

---

shoulder every minute. Not a pleasant thought!

### **SOME BROKERS CHARGE EXCESSIVE FEES FOR STOCKS UNDER \$1**

Most of the examples below of excess and additional charges are for purchasing stock that sells for \$1 or less. However, it is important that you check out a number of firms. Company policies and commission rates constantly change. The information provided below is obtained from sources we consider reliable but there is no guarantee that these policies will be in place by the time you act to get your own broker.

Some firms such as Castle Securities simply refuse to handle any trades for OTC:Bulletin Board or pink sheet stocks. They explained that "we are just not interested in that business. [There is simply too much] insurmountable red tape." [see the SEC Schedule 15G requirements for Disclosure Document to be Distributed Pursuant to Rule 15g-2].

Other firms that flat out refuse to deal with OTC:BB and pink sheet penny stocks include Trading Direct and Freetrade.com. Others that add substantial fees to their normal commission rates include Scottdale and Firstrade.

Some firms limit the number of shares you can order per trade. For example, Datek limits you to 5000 shares. So if you want to order 20,000 shares you have to break it into 4 separate orders, paying a separate commission for each. So instead of paying the \$9.99 standard commission charge for a 20,000 share non-penny stock order, you would wind up paying 4 times the regular commission for penny stocks under \$1. Charles Schwab is another firm which charges high fees for transacting sub-\$1 stock buys and sells.

Another technique to discourage trade in penny stocks is to charge exorbitant fees once a set limited number of shares are purchased. For example, Suretrade charges a mere \$14.95 to buy 5000 shares of a penny stock, but buy 5001 and the commission jumps to \$65!!

### **ORDER CHARGES: MORE FOR LIMIT ORDERS**

Keep in mind that most brokers do charge more for limit orders than market orders. Since we recommend that most of your order be limit orders, this is yet another consideration in your decision making process.



## **PENNY STOCK PROFITS**

---

**Financial CafE      [www.financialcafe.com](http://www.financialcafe.com)      (1-877-600-6410)**

Account minimum: None; \$20,000 account gets \$4.95 commission rate.

Commissions: website makes not mention of penny stocks. Check with the firm prior to opening account. \$14.95 for limit orders.

Check with the company for current rates and policies.

Inexpensive rates listed on the website but there is no mention of penny or low priced stocks whatsoever.

**Ameritrade      [www.ameritrade.com](http://www.ameritrade.com)      (1-800-454-9272)**

Account minimum: \$2000

Commissions: online \$13 for limit orders. No online market orders for penny stocks.

Touchtone phone: \$17.

Check with the company for current rates and policies

Ameritrade is one of the big boys on the Internet.

Their dramatic growth as a result of aggressive advertising campaign engendered some dissatisfaction but things appear to have been ironed out in recent months.

**R. J. Thompson      [www.rjt.com](http://www.rjt.com)      (1-800-934-4448)**

Account minimum: \$2000

Commissions: \$8 per trade limit or market orders any number of shares (online).

\$10 per trade limit or market orders for their touchtone phone service.

\$15 per trade limit or market for broker assisted trades.

## **PENNY STOCK PROFITS**

---

Check with the company for current rates and policies.

The pricing is VERY cheap. The website is appealing and has a demonstration of the whole process. Definitely worth looking into. Offers real time streaming quotes for nominal fee.

### **America First Securities [www.aftrader.com](http://www.aftrader.com) (1-888-588-0400)**

Account minimum: none

Commissions: online \$9.95 for limit and market orders.

Touchtone: \$19.95 for limit and market orders.

Broker assisted: \$30 per trade.

Nice easy to navigate website. Demo for order entry on the website so you can see how complicated it may be.

### **Web Street Securities [www.webstreet.com](http://www.webstreet.com) (1-800-932-8723)**

Account minimum: no minimum

Commissions: \$14.95 online limit or market orders for any trade.

Broker-assisted: \$24.95 for any trade.

Check with the company for current rates and policies.

Nice website with free real time quotes available for customers. Free NASDAQ trades of 1000 shares or more (only for stocks over \$2). Worth checking out.

### **Patagon.com [www.patagon.com](http://www.patagon.com) (1-902-365-366)**

Account minimum: no minimum

Commissions: online for NASDAQ only \$12 per trade

## **PENNY STOCK PROFITS**

---

any number of shares.

Pink sheet and OTC:BB are available only as broker assisted: \$25.00.

Check with the company for current rates and policies.

Website features education from basic to advanced. Prices not good for listed penny stocks but very competitive for NASDAQ. We had a little problem loading the website the first time we tried.

**InvestTrade      [www.investrade.com](http://www.investrade.com)      (1-800-498-7120)**

Account minimum: \$2000

Commissions: \$29 for penny stocks under \$2 any number of shares.

OCT:BB and pink sheet stocks: \$2 and higher): online for \$11.95 (limit orders) and \$7.95 (market orders); otherwise \$27.95 per trade.

Check with the company for current rates and policies.

Trading demo on the website. Quick loading site. Not a lot of bells and whistles. Check it out.

**NetVest      [www.netvest.com](http://www.netvest.com)      (1-800-961-1500)**

Minimum Account: \$2000

Commissions: penny stocks limit orders: \$29; market orders: \$24.00.

Broker assisted: \$39 and \$34 respectively.

Check with the company for current rates and policies.

One of the better websites we've seen. Features a stock screener, java based interactive charting from the makers of MetaStock, and plenty of other investment tools.

**Share Builders [www.sharebuilder.com](http://www.sharebuilder.com) (1-866-747-2537)**

Minimum Account: no minimum

Buy or Sell for as little as \$4.00 on the web.

\$25.00 per year fee.

Real time trades from \$11.95.

Auto investments 20 free.

Check with the company for current rates and policies.

### **SELECTING A GOOD BROKER IS BIG STEP IN THE RIGHT DIRECTION**

So that is a starting point. As you can see many of these deep discount brokers do offer broker assisted trading. An interesting sidelight is the number who offer touchtone order entry that will save you money from the broker assisted rates. We assume that while you may not want to tackle a computer, handling a phone is right up your alley.

If none of these firms trip your trigger, don't despair. Go to a good search engine on the Internet. We like [www.hotbot.com](http://www.hotbot.com). Type in discount stock brokers. It will generate a huge list of brokers for you to check out. There are literally hundreds of these outfits fighting for your investing dollars.

Take your time to select the right one for your particular circumstances.

# **WHAT ARE PENNY STOCKS**

## **WHY DO THEY SAY SUCH TERRIBLE THINGS ABOUT THEM?**

There are many different definitions of penny stocks. To some it means any stock that sells below \$1. To other the cutoff is \$2. But for most (and the definition we use here) a penny stock is one which sells for \$5 or less. This is the general definition of the government watchdog agency, the SEC. Of course, as you would expect with any government proclamation, there are innumerable exceptions. But one reason we use the \$5 cut off figure is that you cannot margin (borrow against) stock unless it is more than \$5.

## **PENNY STOCKS ARE THOSE THAT SELL UNDER \$5**

Penny stocks by this definition trade on the New York Stock Exchange (NYSE), the American Stock Exchange (ASE), NASDAQ, as well as less well known sectors of the OTC (Over the Counter) market including the OTC Bulletin Board and the infamous pink sheet stocks.

Usually when people refer to penny stocks they are thinking of OTC issues. The NASDAQ (National Association of Securities Dealers Automated Quotation) system has certain listing standards that companies must meet in order for their stock to be quoted on the system. Many NASDAQ issues are quoted regularly in newspapers.

The next level of OTC stocks is the OTC Bulletin Board (OTC:BB). The OTC:BB is a regulated quotation service that displays real-time quotes, last sale prices, and volume information for OTC issues that are not included in the NASDAQ system. Note that the NASD (the National Association of Securities Dealers) the industry's self-regulatory agency, has NO regulatory authority over OCT BB issuers.

The NASD's responsibilities include establishing rules governing its broker/dealer members' business conduct; setting qualification standards for securities industry professionals, examining members for their financial and operational condition as

## **PENNY STOCK PROFITS**

---

well as their compliance with appropriate rules and regulations; investigating alleged violations of securities laws, disciplining violators of applicable rules and regulations; and responding to inquiries and complaints from investors and members.

The third segment of the OTC market is that National Quotation Bureau's (NQB) service. This is most commonly referred to as the "pink sheets." The NQB's service list securities and prices on long narrow pads of pink paper. The issuers in the pink sheets have no meaningful listing standards. Reliable up to the minute price information is often difficult to impossible for small investors to independently obtain for these issues. Broker-dealers obtain their price information by calling the trading desks of three other companies who are market-makers in the particular stock. Small investors then find that they must rely on their stock broker for timely price information. This is a situation fraught with possibilities for fraud.

## **THE FIRST STEP: STAY AWAY FROM OTC:BULLETIN BOARD AND PINK SHEET STOCKS**

Due to the difficulty of obtaining objective accurate price, volume, and company information for most OTC:BB and pink sheet stocks, we recommend that you stay away from those stocks. These are the issues that are most often hawked by aggressive stockbrokers who cold call unwary investors by phone with great stories of "guaranteed" profits in companies you never heard of nor can find any information on.

### **RULE NO. 1**

Never buy a penny stock from a stockbroker who phones you out of the blue with an unbelievable deal. Penny stocks that are being hawked by cold calling stockbrokers are never the good deals that they seem. The brokers are being paid handsomely to help distribute the stock at inflated price from the few insiders to the gullible public.

### **RULE NO. 2**

Never buy a penny stock from a high pressure salesperson. Investment in a legitimate emerging growth company is a long term proposition. A good little company is not likely to skyrocket in the next 24 hours no matter what your salesperson may say. It will take time even if it is the most legitimate company in

## **PENNY STOCK PROFITS**

---

the world. You certainly have time to research the matter on your own. If the salesperson doesn't want to provide you with sufficient information to check things out on your own, that is evidence enough that you do not want to buy that stock or deal with that broker.

### **RULE NO 3**

Never buy into blind pools. Sometimes scam artists will call with a pitch about putting together a few "qualified select" investors (and boy are you lucky to be one of the few chosen) in a pool that will invest in the next Microsoft and Cisco. Of course no details about how the money is going to actually be invested and what fees are going to be charged for this one-in-a-million opportunity are ever disclosed. Know exactly what you are buying and how you can independently check its value.

### **RULE NO 4**

Always carefully check your trade confirmations. On every trade you make, the law requires that the brokerage firm provide you with a detailed record of the transaction. The trade confirmation will indicate whether the trade was unsolicited (you initiated the trade) or solicited (the broker brought the trade idea to you). Devious penny stock broker will often mark trades "unsolicited" to avoid stringent registration and disclosure laws pertaining to penny stocks.

### **RULE NO. 5**

Buy only those penny stocks which are listed on the NYSE, ASE, or NASDAQ. Accurate timely price and volume information is available from many sources other than your broker. The Internet has literally thousands of sites which provide this information free. Company information on these stocks is readily available again from hundreds of sources. Each of these exchanges require that timely reports are filed with the SEC. The annual and quarterly reports of financial condition are available to the public from the SEC directly.

## **UNDERSTANDING THE PRICING OF PENNY STOCKS**

When you buy a stock from the NYSE or ASE, typically there is a single

## **PENNY STOCK PROFITS**

---

price quoted. For example you may ask your broker what IBM is trading at. He or she will come back with a single number.

Note that the symbols for stocks on a listed exchanges are 1,2, or 3 letters. For example, the symbol for U.S. Steel is X. The symbol for General Motors is GM. The symbol for IBM is IBM.

The symbols for OTC issues are usually 4 letters. 5 letter symbols are for foreign OTC issues. For example, the symbol for Microsoft is MSFT. When you see a 4 letter symbol you understand that that is an OTC stock.

When you buy an OTC stock, the prices are typically given as a "bid and ask." The bid price is the price that someone is willing to buy a minimum of 100 shares at. The ask price is the price that someone is will to sell a minimum of 100 shares for. For example, if you ask about Priceline (PCLN) you may be told 2 by 2 1/4 . If you wanted to buy PCLN at the current market price you would pay the asking price (\$2.25) per share (plus commission. If instead you wanted to sell 100 shares of PCLN you would receive the bid price or \$2 per share (minus commission).

So you can see that as soon as you buy an OTC stock you are already at a loss. The difference between the bid and ask is the "spread." Now in reality the exchange listed stocks are also traded on a bid/ask basis. However, one of the alleged advantages of the exchange system is that the spread is theoretically kept very small by the specialists. There is no doubt, that in many cases, the spread on OTC issues can get quite a bit larger than would ever happen on the exchanges. That is one of the dangers you must watch out for.

## **PRINCIPAL VERSUS AGENCY TRANSACTIONS**

Most stock transactions (and all exchange listed stocks) are handled on an agency basis. This simply means that your broker acts as your agent by arranging a transaction between you and a third party for a fee (the commission).

However, in the case of OTC stocks, if your broker is also a dealer, it may have the security you want to buy in its inventory. It may want to purchase the stock you want to sell for its inventory. If your broker-dealer buys or sells for or from its inventory, it is acting as a principal, not as an agent. The trade confirmation will indicate that. The broker-dealer is not paid a commission on a principal trade. Rather it makes its money on the spread between the bid and ask or by having wisely bought or sold the stock previously like any investor.

## **BEWARE OF CONFLICT OF INTEREST IN PRINCIPAL TRADES**

## **PENNY STOCK PROFITS**

---

There is an inherent conflict of interest in principal trades. After all the broker-dealer wants to get the highest price it can, while you want to pay the lowest price possible. We recommend that you try to stick with agency trades whenever possible. See the section on selecting a stock broker.

A sizable portion of OTC penny stock trades, especially those solicited by penny stock brokers, are principal transactions. The typical spread for actively traded stocks should be 1/8 point (12.5 cents or less per share). However, the spread for spreads for OTC penny stocks are often 25-33%, and sometimes as over 100%.

### **RULE NO. 6**

Never buy a stock with an inordinately wide spread. A wide spread presents unscrupulous broker-dealers with too many opportunities to profit from its trading with customers. It also indicates a thinly traded, easily manipulated stock. Stay away from them.

### **MARK-UPS OR ANOTHER FEE BROKER-DEALERS WILL TRY TO SLIP BY YOU**

A broker-dealer who has held a stock in its account and as a result is subject to the risk of market fluctuation, may mark up the price of the security it sells you by a certain percentage on top of the spread! Yee ow! Be sure to check your confirmation. If your broker-dealer is socking you with all these fees, that makes it all the more difficult to make money. Insist on agency transactions where you know and can control the cost of your transactions.

### **MARKET MAKERS: KEY TO LIQUIDITY**

Market makers are broker-dealers who stand ready to buy 100 shares of the stocks in which it makes a market. When a transaction is proposed, the market maker gives a price at which it would be willing to make the transaction. The one thing you as a penny stock investor should understand about market makers, is that the more market makers there are in a given stock means the more true the market price (the narrower the spread) because of the competition among the market makers.

The more market makers there are in a stock, the less susceptible that stock is to manipulation. If there is only a single market maker it can accumulate a large block of stock, then use a high pressure sales force to hype the stock and drive the price up. But after selling all its stock to the public, the demand dries up and the price falls sharply.

## **PENNY STOCK PROFITS**

---

### **RULE NO. 7**

Never buy a penny stock with less than 3 market makers. This is never a problem with the NYSE, ASE, and NASDAQ penny stocks that we work with in our newsletter.

### **TRADE CONFIRMATIONS PROVIDE A WORLD OF INFORMATION**

To avoid the penny stock scams you must be diligent in reviewing all your sources of information. One of the most valuable pieces of information you have is your trade confirmation. The trade confirmation by law must include the following information: number of shares and price, whether the transaction was agency or principal, was solicited or unsolicited, in the case of pink sheet and non-NASDAQ OTC trades, the bid and ask at the time of execution.

# **WHAT MAKES PENNY STOCKS DIFFERENT**

You can hardly ever read anything in the financial press about penny stocks except negative stories. There is no doubt that this particular arena has been inundated with scam artists and scum who have stolen millions of dollars from the unsuspecting public. But if you understand that there is no such thing as risk free millions. That a sure thing would never be offered to you. The person making the offer would have no reason to give up a sure thing for a few measly dollars. People calling you at home at all hours of the night with the greatest opportunity to make you wealthy should take those offers themselves so they wouldn't have to be bothering decent working people at dinner!! But we suspect that they know better than to invest their own money in such nonsense!

That said you should know that penny stocks have certain characteristics that make them appealing to serious investors will to do a little work to understand what is worthwhile and what is junk. Because in the penny stock world, about 90% is junk, but the remaining 10% can be solid gold!

## **INFORMATION MORE LIMITED FOR PENNY STOCKS**

Old line companies like IBM, Procter and Gamble, or General Motors have many years of information and history that analysts can pore over. They have years of detailed price history that can be analyzed to ascertain anomalies and trends. There are mounds of corporate financial data.

Small companies on the other hand, have limited operating histories. There is usually very limited price history for the stock. There is only a limited amount of financial data available.

What would not be of interest to the hordes of financial analysts peopling the major Wall Street brokerage firms and multi-billion dollar institutions may be just the ticket for the diligent investor bent on ferreting out the undiscovered jewel with the product or service that may change the way business is done. Would you ever have thought that a company with a name like Yahoo, and a business plan of giving away its service, would be worth hundreds of millions of dollars? Well some investors saw the potential and are millionaires today!!

## **PENNY STOCK PROFITS**

---

### **GROWTH CAN BE SPECTACULAR FOR RIGHT PENNY STOCKS**

Established companies may trade market share back and forth, but it is unlikely that Xerox (XRC) will ever again completely dominate the copier business. Mature business and industries are fairly stable.

But a new company with a new idea, can set the world on its ear. Microsoft (MSFT) was not the first company to develop an operating system for personal computers. There were others before it. But it managed to do it better and grew to dominate the software market for PCs.

International Paper (IP) is unlikely to develop a product that will revolutionize the way business is done. But Cisco (CSCO) did in fact build better products to make the Internet an unstoppable reality.

Merck (MRK) or Pfizer (PFE) spends hundreds of millions of dollars developing drugs. But the hottest sector in the medical field is biotech. There are many companies which are developing products that may reverse or halt the aging process, that may cure cancer, that may cure AIDs, that may change the world as we know it. Some are mere penny stocks only one discovery away from changing the world for the better.

### **VOLATILITY IS AN UNDENIABLE CHARACTERISTIC OF PENNY STOCKS**

A stock with 200 million shares outstanding, largely in the hands of institutions, e.g., Coca Cola (KO), can very well run up in price. But it is unlikely that there will develop enough buying power to move the stock up hundreds of percentage points. How much money is there in the world?

But a small company with a float of only a few hundred thousand shares or even a million, can and most likely will see huge volatility. Volatility is only bad when you are on the wrong side. But frequent huge price swings offer the smaller investor the chance to multiply his or her capital quickly. But of course, much like Las Vegas, it works both ways. High volatility can diminish one's capital quickly.

It is not at all unusual for a penny stock to gyrate back and forth over a relatively large price range considering the price of the stock. For example, ZAPP went from as low as \$3.50 on 5/24/00 to a high of \$7.31 on 6/15/00 (more than a 100% move) back to a low of \$4.25 on August 18 only to jump to a high of \$9 on 9/6/00 (another 100% plus move). All that occurred in less than 3 months trading. Fasten your seatbelts!

That is where experienced trading advice can make a difference. No one knows what is going to happen tomorrow. However, by being prepared for all

## **PENNY STOCK PROFITS**

---

eventualities, you can maximize your profit potential while minimizing your risk by following the steps we outline in the section on How to Buy Penny Stocks.

## **REVENUES FOR PENNY STOCKS ARE LIKELY TO BE SMALL OR NEGATIVE**

When General Motors (GM) reports earnings growth it is typically a few per cent. If the economy has been good, the rate of growth may go up 10%.

But a small company with negligible or even negative earnings, can turn things around dramatically with a minor change in fortunes. If the company has been on the edge for a couple years, but suddenly its product or service catches on, the turnaround can be surprising (a necessary ingredient to dramatic price moves) and dramatic. Going from negative to positive is a change of many degrees. It can't be measured in terms of a few per cent. It is a major change. It could be reflected in a major price change.

## **IT DOESN'T TAKE AS MUCH VOLUME TO MOVE PENNY STOCKS**

It may take hundreds of millions of dollars to make any kind of difference in a stocks which trades millions of shares a day with a float of 500 million shares and a price in the 100s.

But small companies have small floats with small volume. If someone takes an interest, it doesn't take much buying to dramatically change a companies prices. To move Citibank (C) it take billions of dollars from many huge institutions. To move a penny stock it can take one committed buyer with reasonable resources who buys the story. Paul Allen, one of the founders of Microsoft (MSFT), is worth billions. To this day he actively invests in small developing technology companies looking for the next Microsoft (MSFT) or Cisco (CSCO) or Sun Micro (SUNW). Wouldn't you like to be there just ahead of him? It can happen. But it won't just fall in your lap. Do the necessary homework and improve your odds.

# PENNY STOCK SELECTION SECRETS FOR THE AGES

Most people tend to think of all penny stocks as speculative high risk, no assets, no earnings, new companies. Indeed most penny stocks fall into that category. In fact some 90% of all penny stocks can accurately be termed junk. But that remaining 10% is where the gems of tomorrow may very well come. That remaining 10% may be the foundation for your penny stock trading fortune.

Anyone who tells you that making a fortune investing is "easy" is pulling your leg. It is easy in the sense that if you apply proven tested techniques you can and will ferret out the winners. But these do not just fall out of the sky. Good ole Uncle Billy's hot tip is more likely to turn up a total loss than a read hot fortune maker.

## **BEWARE OF "HOT TIPS"**

It is time to face the facts. When someone who barely has two nickels to rub together suddenly shows up with a "hot tip" it is most likely neither hot nor useful. It is the same with that high pressure hard sell broker who somehow manages to catch you eating dinner every time. But he knows that his latest hot tip is ready to explode and it may just do it tomorrow. In fact if you don't buy today you will just lose out.

Well if this was such a sure thing fortune maker why doesn't Mr. Slick Stockbroker just invest his own money and his family's money in, make a fortune and give up working 12 hours a day harassing vulnerable potential victims hour after hour, day after day. Is that anyway for a rich person to operate? Not likely.

## **THERE ARE SOME PROVEN SOLID COMPANIES AMONG PENNY STOCKS**

We have found after years of experience in this business that there are a few solid, proven, growing companies even in the penny stock sector. There are penny stocks with good financials. But it does require work. We don't make a dime when clients buy the stocks we recommend. We make our living solely from selling our research. And frankly, if it didn't turn up candidates that grew then nobody would subscribe would they?

Below we have detailed a list of the things that we carefully check for each and every penny stock candidate. As you will see, there is nothing particularly difficult. There is not magic involved. You don't need us to do the work. You can do it yourself. We will teach you exactly what to do. We happen to love what we do, and think that that gives us an advantage. Some of you will decide to pursue

things on your own with the solid base of information that we have give you in this guide. Some of you will use our advisory service as a starting point, but will do plenty of work on your own. Finally some of your will rely almost totally on the nuggets we are able to mine and report on in our monthly newsletter because you have other lives to attend to.

## CHECKLIST FOR STOCK SELECTION

**1) FIND NEW DEVELOPING TECHNOLOGIES.** Often small companies own new patented technologies that can shape the future. Just think of Qualcomm (QCOM), it developed the technology that powers many cell phones. In 1999 QCOM went up over 166% in a single year. This stock at one time sold for well under \$20 and went to almost \$600 based solely on one technological patent.

There are many ways to ferret out new technologies. Keep an ear to the technology world. Check out the websites for technology magazines. They will always feature the latest toys. Some of these things are made by very small companies. Use your common sense. Does it make sense to you?

Most people did not see the potential of the Internet. But those who did made fortunes. What is the next step? One of the things we know for sure is that everyone wants Internet access to go faster. There is a huge demand to make it more secure. To protect privacy.

The major developments will come from small companies. A Microsoft or an IBM are too bureaucratized to be able to move quickly. But you can bet that when the next hot technological advance is made, that Microsoft or IBM will be there with bags of money to buy it out. Many entrepreneurs made millions by selling their little companies to the big boys.

We monitor the technology services on a daily basis. We use every waking moment for research. Do you see someone using an interesting new piece of equipment. Find out about it. Think of the Palm Pilot. There were many handheld computers and calculators around long before the Palm Pilot. What made it different. Would you have liked to have caught that rocket ship to the moon?

They are out there. And you do not have to be an engineer. In fact, with a

## **PENNY STOCK PROFITS**

---

little common sense and vision, it is far more likely that you can spot the next big wave than an engineer who is tied in to the old ways and technology.

**2) TAKE A LOOK AT A COMPANY'S EARNINGS.** There are few penny stock companies that actually make money. Those that do don't stay penny stock for long. But there are trends that can help you pick out a winner. Are earnings, though negative, improving on a steady basis. Take a look at sales as a leading indicator for earnings. Are sales going up even as earnings remain negative. Not a problem. If there is a demand for a product or service, and sales are increasing, eventually even a new company will be able to pay off its debt and operating expenses and move into profit country. And that is where the big moves are often made. That shift from negative to positive territory is the fundamental change that could signal a glowing future.

**3) A KEY ELEMENT TO THE SUCCESS OF ANY SMALL COMPANY IS ITS MANAGEMENT.** Take a close look at who is running the show. Does the management team have previous experience turning a small money losing company into a money maker? With the Internet you can easily check out virtually any manager. Who is the CEO? What is his or her background and track record? Who are the other chief players? What companies were they with before? How did those companies do? All this information is available from the company itself in the annual report. You can check out many of these things on the Internet at no cost. A successful manager of turnaround situations understands what is necessary to do it again. In fact, it is not too much to say that the management team may be the single most important factor in determining the success of a budding operation.

**4) CHECK OUT THE FINANCIAL STATEMENTS.** Below we detail some of the key things to look for in the financial statements. As above be sure to check out the quality of the earnings and its leading indicator, sales. But also take a look at debt levels. One of the biggest advantages of a small company is the flexibility that its small size gives it for reacting to market changes. However, if a company is saddled with debt, that limits what it can do. It limits what it buy. It limits the attractiveness of itself to potential buyers. It limits its options. All other things being equal we would prefer as little debt as possible.

**5) LOOK FOR COMPANIES IN INDUSTRIES THAT ARE DIFFICULT TO ENTER.** If a company is doing well in an industry that has high barriers to entry they have less competition, and a small change can mean a big difference on the bottom line.

**6) WHAT IS THE CUSTOMER BASE?** Does the company's products or service

## PENNY STOCK PROFITS

---

target a growing dynamic segment of the population? You don't want to be targeting the horse buggy crowd. In other words, focus on where the company's growth will come from.

**7) KEEP AN EYE ON DEVELOPING TRENDS.** In the past few years there have been 2 very hot industry groups that featured a number of huge winners from the penny stock sector. Remember the Internet dot.com craze? The biotech craze as everyone and their uncle were going to profit from genome research project. What is the next hot industry. A hot sector is often easier to detect early than a hot stock. Find the industry then focus on the company.

**8) EVALUATE THE INSIDER ACTIVITY.** You don't want to be buying into a company where the insiders are dumping stock. Heck they ought to know something. But it is important to remember that it is the trend that is important not any single transaction. People have to sell stock for a variety of reasons. College education for the kids. A new house. Etc. The strongest most reliable insider signals are buys. When an insider steps up and buys more stock that is a strong statement. There are not many motivations other than to make money when someone buys a stock.

**9) WATCH VOLUME FOR TIP OFFS.** Sometimes penny stocks' volume will shrivel up to practically nothing. Days may go by without a trade. Try to avoid low volume stocks. Before buying any penny stock get a chart or observe it for some time but look not only at price action but at volume activity as well.

One obvious advantage of higher volume issues is that the bid/ask spread tends to be much smaller. Also the volume is a vital tool for assessing potential bottoms and tops. For example, if a stock is rising but the volume is shrinking, that is a warning signal that the upside move is running out of gas. If you are familiar with the volume pattern of a particular stock you will recognize when unusual volume activity takes place. Often volume will increase prior to a big move as insiders and other people in the know move in to take advantage of the low priced stock before it explodes.

Volume is a good lead indicator to price. Watch it carefully. Try to focus on stocks with a good daily volume that will enable you to move 1000 to 2000 shares easily. The good volume indicates a consistent underlying interest in the company. If that interest gets stoked by a news development the volume will increase, but the liquidity will prove useful for trading.

Higher volume penny stocks will tend to have more solid support and resistance levels. A support level is a price zone at which buying historically comes into a stock. A resistance level is a price zone where selling historically arises, arresting any upward price move. Volume is a great tip off at both of these

## **PENNY STOCK PROFITS**

---

levels. If prices have dropped to what is historically a support zone take a close look at volume. If the volume fell and is lower than usual at it nears the support zone you can buy with greater confidence. If volume is shrinking as prices reach a resistance zone, then it signals you to sell. Take your profits.

**10) UNDERSTAND THE BASICS OF FINANCIAL STATEMENTS.** Financial statements can seem very daunting to the average non-accountant. But there are really only a few things that you need to know to gain an upper hand in analyzing financial statements.

**THE BALANCE SHEET SHOWS THE COMPANY'S FINANCIAL CONDITION AT ONE SPECIFIC DATE**, usually the last day of the company's fiscal year. On one side of the balance sheet are listed the company's assets, i.e. what it owns. The other side is the company's liabilities, i.e., what it owes. Now if the company's assets exceed the company's liabilities, the difference is shown on the liabilities side as shareholder's equity. That is if the company was liquidated, the shareholders equity would be what is left to distribute to the shareholders. Shareholders equity is also known as book value.

Total assets equal total liabilities plus total shareholder's equity. The Balance Sheet should be used to determine the value of the company, its debt load, and its cash position.

**THE INCOME STATEMENT (ALSO CALLED THE EARNINGS STATEMENT OR PROFIT AND LOSS STATEMENT SHOWS A COMPANY'S REVENUE RECEIVED FOR SALE OF ITS PRODUCTS OR SERVICES OVER THE PAST YEAR.** It also details the expenses incurred for things like wages, operating costs (rent, supplies, office equipment etc). The difference between the revenue and expenses is the company's profit for the year. The amount left over after taxes are paid is the net earnings.

**NET EARNINGS TELLS YOU HOW MUCH THE COMPANY REALLY MADE -** after all everyone must pay the taxman. Some companies can have low earnings but be good prospects if they used the revenues for research and development, to acquire other companies, expand product line or into new markets and so on. The quality of the earnings is more important than the absolute numbers. You want to invest in companies which are aggressively pursuing growth.

Beware of one time earnings boosts or losses. You are looking for fundamental underlying trends. The fact that a company got a one time windfall from winning a lawsuit should not be too heavily counted. After all, it won't happen every year.

## **PENNY STOCK PROFITS**

---

**THE STATEMENT OF FINANCIAL REPORTS (ALSO CALLED THE CASH FLOW STATEMENT) SHOWS HOW THE COMPANY'S FINANCIAL CONDITION CHANGED FROM ONE YEAR TO THE NEXT.** It details how the company generated and spent its money during the year.

The Statement of Financial Reports is valuable for evaluating the liquidity and solvency of a company. It can help you assess the ability of the company to generate cash internally, to repay debts, to reinvest and so on.

**THE NUMBERS YOU WANT TO RELY ON HAVE BEEN AUDITED.** The fine print at the bottom of the reports will tell you. Don't rely on company estimates or unverified results. You want audited and the bigger the name of the auditing firm the better.

Beware when reading a report of the tendency to preface the data with glowing interpretations and positive news. Don't quite early. Read the entire report. Many times a glowing beginning gives way to a dismal reality of numbers. Remember Mark Twain's saying: "Figures never lie, but liars always figure."

You can obtain a company's financial reports direct from the companies themselves. Most will mail out their latest quarterly and annual reports.

You can go to the Internet and obtain the latest reports much faster. One source is the SEC Edgar repots ([www.sec.gov/edgarhp.htm](http://www.sec.gov/edgarhp.htm)) or the ever handy [www.freeedgar.com](http://www.freeedgar.com) . Other websites such as the very popular Yahoo (<http://biz.yahoo.com/reports/edgar.html>) feature access to the Edgar database of filed financial reports from public companies.

**11) USE THE INFORMATION GLEANED FROM FINANCIAL STATEMENT TO COMPARE VARIOUS COMPANIES THAT YOU ARE INVESTIGATING.** See how the company you are interested in compares to others in the industry. For example, when looking at the Balance Sheet, how does the debt load compare? How are current liabilities in relation to current assets (that will tell you if your company has sufficient cash on hand). How does the share price compare to the book value?

**COMPARE THE INCOME STATEMENTS.** Are revenues growing from year to year and quarter to quarter? Is the growth rate increasing or decreasing.

And with the Statement of Changes you can tell at a glance which companies' debt load is increasing or decreasing. Are there any unusual expense items that might distort the numbers?

Keep in mind that the numbers in the financial reports correlate with long term price movements. They are not very good indicators of short term price

## PENNY STOCK PROFITS

---

movements. To evaluate the short term prospects of a company it is more useful to examine technical factors such as recent price history and volume.

Fundamental analysts tend to view the financial data as the only important consideration for stock selection. They fail to recognize that there are many non-numerical factors that go into making up the price of a company.

You need to go back no further than the last few years when the dot.com mania hit the market. Companies with no earnings, no sales, no assets, with inexperienced management saw their stock prices double, triple, and more as a buying frenzy hit the Internet sector. If all you watched was the financial statements you would have missed one of the most explosive moves in history.

**SO USE THE INPUT FROM FINANCIAL REPORTS AS ONE PART OF THE OVERALL PUZZLE.** But don't limit yourself to only those numbers. We have given you many tips on using volume as a leading indicator of price action.

**12) DON'T LIMIT YOURSELF TO COMPANY BY COMPANY ANALYSIS.** Take a look at the industry group that your company is in. Much of a stock's price movement is generated by the movement of its industry group. When the Internet stocks were running, the cats and dogs ran right along with the better quality issues.

One of the best websites for analysis of industry sector performance is Wall Street Research Net ([www.wsrn.com](http://www.wsrn.com)). Another good site for sector information is Wall Street City ([www.wallstreetcity.com](http://www.wallstreetcity.com)). The weekly Barron's and daily Investor's Business Daily, and the Wall Street Journal also feature data on industry sector strength. Buying stock in a strong sector improves your odds of success.

# LEARNING HOW TO PLACE YOUR ORDERS FOR PENNY STOCKS

As we discuss in our section on selecting a broker, that is the first critical step on your way to becoming an independent investor. In recent years with the advent of the Internet there has been a strong move toward online discount brokers. But if you do not have a computer, you won't be able to take advantage of that. However, most discount firms now make it possible to place orders by touch tone phone over toll free 800 lines.

Once you have selected a broker or two, it is important that you understand the terminology used by the brokerage industry for placing orders. If you are an experienced stock investor this section please bear with us. For new stock traders knowing the language for properly placing your orders will make a huge difference in confidence, and it can make the difference in getting good prices on your orders.

## ESSENTIAL INFORMATION FOR EVERY ORDER

**When placing orders you will need to provide the following information.**

**TICKER SYMBOL:** The ticker symbol is the 1, 2, 3, 4, or 5 letter combination that represents a specific stock. For example, the symbol of Priceline is PCLN. The symbol for Moore Corp is MCL. These ARE NOT the same as the abbreviations that you see in the daily newspaper. You can get the symbols from many different sites on the Internet. Our favorite is [www.pcquote.com](http://www.pcquote.com). Simply type in the name of the company, or even part of the name, and this site, like most, will provide you with a list of potential stocks and their symbols. Or you can get the symbol from your broker. Finally, any publication on stocks such as those published by Standard and Poors or Moody's feature the ticker symbols.

**QUANTITY:** You must be very clear in detailing exactly how many shares you want to buy. You can buy any number of shares. Typically most investors trade in lots of 100. A typical order for penny stocks may be 500 or 1000 shares. As we detail in the chapter on picking a stock broker, some firms have limits to how many penny stocks you can buy before penalizing you with extra fees. Be sure to know this information before placing an order. It can make a big difference in your costs.

## **PENNY STOCK PROFITS**

---

Be sure that you know how many shares you have in your account prior to placing sell orders. Big problems can occur if you accidentally sell more shares than you own.

### **SCALE IN WHEN BUYING**

Many neophyte traders tend to be all in or all out with their positions. In other words if they intend to own 1000 shares, they buy it all at once. When the sell they sell all at once.

Experienced traders know that there is nothing special about any one price. The more experienced and successful traders tend to scale in over time when they buy. For example, if they plan to own 1000 shares of Priceline (PCLN) when it is quoted with an ask price of \$2.25, they may buy 400 shares at \$2.25. At the same time they are prepared to buy more if it drops to \$2.00 (and all other things stay the same). Or they may want to buy more if it starts to move higher. The point is that they will accumulate the position over time rather than committing all their funds in one pop. This is another reason why experienced traders will not be conned into buying something immediately by some high pressure salesperson. They know that successful trades, the really big money makers, will develop over time.

### **SCALE OUT WHEN SELLING**

Just as it is unwise to buy your entire position at a single price, it is far smarter to unwind your position on a scale out basis. Say you bought 1000 shares of PCLN over a 2 week period at an average price of \$2.50 with the expectation that the price could move to \$7. Say that in 3 months the price moved to \$7. You could sell your entire position and take a nice profit. But one thing that you will learn with experience is that prices tend to go much higher than anyone expects (and vice versa, tend to go far lower than most people expect). A wiser approach may be to sell 500 shares at \$7, and place a sell stop to sell the balance if it drops to \$6.50. If the price continues to move higher, move your sell stop with the price. If the stock spikes then to \$15 or so, you will still participate in the bigger move.

Remember, some stocks have run from only pennies to over \$100! We encourage you to take profits as it moves in your favor, but don't limit your potential profits by exiting too soon. You are in penny stocks looking for home run. Don't exit every time you get a single.

## **PENNY STOCK PROFITS**

---

### **RULE NO. 8**

When you buy into a stock, decide in advance how many shares you plan to own. Then scale in your buying over time. Do not put your entire position on all at once.

### **RULE NO 9**

When you sell a stock, scale out of the position. Scale out of your positions over time. You do not have to be all in or all out when buying and selling stock.

**TYPES OF ORDERS:** When buying or selling stock you should know what the price is and have an idea what price you expect. There are two main types of trade entry orders for penny stocks: market and limit.

A **MARKET** order is an order to buy the stock immediately at the best price available. This will typically be the "ask" price of the price quote you are given at the time of order entry.

### **A MARKET ORDER IS A HIGH RISK ORDER IN THE THINLY TRADED PENNY STOCK MARKET.**

As we told you above, one characteristic of penny stocks is the tendency for a wide spread between the bid and ask. For example, if the quote for XYZ stock is \$3 by \$3.50 the spread is 50 cents per share. If you buy 1000 shares of XYZ at market you will pay \$500 more than you can get if you turned around and sold it immediately ( $1000 \times \$0.50 = \$500$ ). You would pay \$3500 but could only sell it on a market order for \$3000.

Active floor traders or traders with sophisticated quote equipment on their desks who trade is very liquid stocks with high volume often trade very successfully with market orders because the spread between the bid and ask is very small.

But in most cases, it is financial suicide for penny stock investors to use market orders. A market order guarantees you immediate execution of the trade, but the price may come as a surprise.

## **PENNY STOCK PROFITS**

---

A LIMIT ORDER IS AN ORDER WHICH SPECIFIES A SPECIFIC PRICE TO BUY OR SELL THE SHARES. For example, in the example above you may think that 50 cents is much too wide a spread. You think correctly, that once you buy the stock you are immediately at a 17% loss. It is tough enough to make money consistently as a trader without putting yourself behind 17% at the beginning.

However, you may decide to "split the spread." In this case, you would enter a limit order to buy 500 shares of XYZ stock at \$3.25. The limit order means that you are willing to buy the stock at the specified limit (in this case \$3.25) or lower, ONLY. You will not pay any more than \$3.25 per share. You will only buy the stock if someone steps up who is willing to drop their sell price to \$3.25 or lower.

It works the same way for a sell order. If you own XYZ stock at \$1.50 per share and the current bid/ask is \$3.00 to \$3.50 you may want to try to get a bit more by placing a sell limit order at \$3.25. This specifies that you will not take less than \$3.25 per share for your stock. If you have 1000 shares, the difference between a limit order of \$3.25 and a market order that would be filled at \$3 is \$250. That is a lot of money to leave on the table.

## **THE DRAWBACK TO LIMIT ORDERS: NO GUARANTEE OF EXECUTION**

However, be aware of a very important drawback of limit orders. You are not guaranteed an execution (or fill in broker lingo). If no one is willing to come down to \$3.25 per share you will not buy any shares of XYZ at your limit price. With a market order you are guaranteed an execution if the stock is available. However, you are not guaranteed a execution of your whole order if it is more than 100 shares at a single price.

The same works on the sell side. Unless someone is willing to pay the \$3.25 you specify in your limit order, you will not be able to sell any shares.

If you feel you must buy or as is more often the case you must sell MUST sell, then use market orders.

## **RULE NO. 10**

When entering positions in penny stocks always use limit orders to specify your maximum buying price. When exiting positions a market order may be appropriate if you want to get out immediately.

## PENNY STOCK PROFITS

---

### DAY OR GTC ORDERS

When you place a limit order you need to decide how long you want that order to sit on the books. As we explained above, with a limit order there is no guarantee of execution.

You would place a "Day" order if you want the order cancelled at the end of the trading day.

If you want the order to stay on the books for a few days, use a GTC (Good Til Cancel) order. Different brokerage firms have different terms for GTC. Some will cancel all GTC orders at the end of every month. Others cancel the orders after 30 days. Some firms allow you to place a GTC order to the end of the week.

But the important point is that a GTC order stays on the books and does not have to be renewed everyday like a Day order.

If you use GTC orders, be sure to have a good record keeping system. You don't want to forget about an old order on the books that may get filled when you are committed fully elsewhere.

### A Sample Buy Order

**Buy 1000 shares of PCLN at \$2.25 per share, good till Friday.**

This order is a limit buy order. It specifies that you want to buy 1000 shares of PCLN at \$2.25 or lower. You will not pay more than \$2.25 per share. If the order is not filled immediately it will stay on the books until the close of business the first Friday after the order. It will be cancelled at the close of business on Friday if not filled.

There are only a few things which can happen with this order. If no one steps up willing to sell PCLN for \$2.25 or lower nothing will be done. You will not buy any stock and the order will expire on Friday. No commission will be charged if the order is not filled, though there may be an order charge by your broker.

Someone may be willing to sell some PCLN at \$2.25 but not 1000 shares. So you may wind up buying fewer shares than you ordered with your limit order. A seller can always fill part of your order unless you specify the rarely used condition "AON" (all or none) and your brokerage firm allows you to use an AON order. You will be charged a commission for the stock you buy. If the order is partially filled over 3 days you will pay a commission each time.

## **PENNY STOCK PROFITS**

---

Finally, you may buy 1000 shares at \$2.25 or lower. Naturally you will pay a commission over and above the price of the stock.

## **A SAMPLE SELL ORDER**

**Sell 1500 shares of PCLN at the market.**

Be sure that you have 1500 shares in your account first! This order will be filled immediately at the best price available when you place the order. But with a market order it WILL be filled.

The fill price may be all 1500 shares at a single price. However, if there may also be 2 or more sellers to fill your whole order. You may get \$2 for 1000 shares, \$1.75 per share for 300 shares and \$1.50 per share for the remaining 200 shares. With a market order there is not guarantee of a specific price, though there is a guarantee of an execution.

At any one time, there are typically a number of buy and sell orders that are outstanding for the various market makers for your stock. That is why a market order may not be filled all at once or even with just one market maker. That is also why the fills on market orders may cover a wide range, not just a single price.

Remember what we told you above. The more market makers there are the better more true the price is. A single market maker can really take advantage of a sizable market order by scaling down the prices it is willing to pay or scaling up quickly the prices it is willing to sell for.

## **UNFILLED AND PARTIAL FILLS**

As we explain above, limit orders may not be filled at all. If no one is willing to pay what you want for your stock (the limit price), the order will not be filled. In very thinly traded stocks, a common characteristic of penny stocks, there may be no trades for days at a time.

Sometimes you may only get part of your order filled, because there was no one willing to meet your full quantity with the price you wanted in your limit order. Partial orders may be higher commissions because you have to place another order to get the full quantity you want.

You can always adjust your order during the market day or before trading begins the next day. Simply cancel the existing order, and replace it with a new order specifying new limit prices.

# **PAPER TRADING IS THE BEST TRADING EDUCATION YOU WILL EVER GET**

Properly understood and implemented, paper trading is not a game. It is a very real test of your investment approach. The problem that arises is that when people paper trade they take great liberties since their own money is not really on the line. For example, positions will be held despite an exit plan that was clearly spelled out as a critical part of your investment strategy.

When you paper trade, the more realistic, the more accurate, the more rigorous you make the exercise, the more valuable it will be for you. For example, one of the things that your editor learned many years ago was the critical importance of having an exit strategy in place BEFORE actually placing an order. A successful investor will know in advance how he or she intends to exit a position before buying it.

Most investors have some idea of how much money they expect to make. You always hear price projections. You think that XYZ will double based upon your knowledge of the stock, its business, and the market as a whole. Let's assume that XYZ is selling for \$4 per share. A doubling would mean a move to \$8 per share. Certainly a hearty profit that any investor would love to pocket.

## **HAVE A PROFIT TARGET IN MIND**

Hopefully you have considered what you are expecting in terms of profits. After all if you buy a stock simply because you think it may go up, you have no idea when to sell to pocket some of that profit. Watching a stock fluctuate between \$4 and \$8 year after year does you absolutely no good, unless you buy at \$4 and sell at \$8. You have to take some profit sometime. That is half of your exit strategy. You know what profit you are expecting. When it gets close to that profit zone, you should be selling at least a portion of your position to lock in some of that profit.

## **HAVE A RISK MANAGEMENT PLAN IN PLACE WHEN YOU START**

But a key question that few investors ever address is how much are you going to risk to make that \$10 per share rise? If the stock is selling for \$4, and

## **PENNY STOCK PROFITS**

---

you expect it to double, how much are you willing to risk? Do you want to risk \$4 to make \$4? That is not a very good trade off. In fact, if you risk as much as you expect to gain it is unlikely that you will ever make much money.

What you want to do is to set your system up so that you will profit handsomely even if you are only correct 50% of the time. In other words, if you design your system to make money when you are right no more than you would be simply flipping a coin, you are on the right track.

In our example, XYZ stock is at \$4. Let's assume that you are not willing to risk more than \$1 to make \$4. That simply means that if the stock drops to \$3 before it double, you are going to sell the stock and take that money to take another try. But that is the beauty of this approach. You save some of your chips so you can make another play. If you risked 100% of your money to make 100%, if you are wrong only once you are knocked out of the game. You don't have any money to try again.

But if you risk \$1 to make \$4 and get knocked out, you at least have \$3 left to try the same thing 3 more times. Let us say you are only right 1 measly time out of 4. That one trade will make you \$4 plus the \$1 you started with. You have a total of \$5 which is a 25% gain even though you were wrong 3 out of 4 times. Remember you made \$4 profit and you had \$1 to start with so you are up slightly.

Now imagine the number if you are right only half the time. Well paper trading is designed to let you see how the market actually works in the real world. You can read all the books and study all the theory in the world and still not have the slightest clue how it works in the real world. Many brilliant theorists have worked out their complicated theorems and then decided to show the great uneducated unwashed how to make money. And they failed miserably. The real world has surprises, pressures, and human input that no computer can figure properly.

## **MAKE PAPER TRADING AND EFFECTIVE TOOL FOR YOU!**

Paper trading can be an effective tool for investors. The problem is that all too often it is approached in a sloppy haphazard manner. You must be a diligent in your paper trading as you will be in your actual investing. Unless you treat every paper trade as though you have your own money riding on the results, you are doomed to disappointment because you will fail to learn a thing.

Paper trading properly done will serve to validate or discredit your investment approach. Use it wisely. Lose money on paper to make money in the real world.

## RULES FOR PAPER TRADING

**1) PROPERLY DONE PAPER TRADING IS A VERY GOOD METHOD FOR TESTING YOUR INVESTMENT APPROACH.** Many experienced investors use paper trading techniques to fine tune their investment strategies.

**2) ENTER YOUR ORDERS AHEAD OF TIME.** In other words, if you are planning to buy PCLN, then write it down on your paper trading worksheet that you will enter an order tomorrow to buy it at \$2.25 or better. Be specific. Be exact. Note the number of shares, the price and the type of order.

If you enter a limit order, then you will need to check the next day's high and lows to see if it would have been filled. Look also at the volume. If there was no trading in your stock, you would not have been filled. Treat it just like it was a trade with a broker. You are trying for realism here, not profits or losses.

Most people make the mistake of looking at the paper or Internet price quote today and saying why I think I'll buy at the closing price. Too late. The market has already closed. You cannot buy once it is closed. You must put the order in and see if the market fills it for you before you can start calculating how much money you are making. Once you decide you want to buy, you must enter the order and wait to see if you get a fill before entering it on your worksheet.

**3) KEEP COMPLETE ACCURATE AND DETAILED RECORDS.** Be sure to include the costs that you will incur with your broker. Commissions, and fees add up. That can make a big difference in your trading success. Don't delude yourself. You WILL pay commissions on every trade. Add or subtract them on your day trade logs.

**4) CONSIDER EVERY DETAIL: VOLUME, PRICE, ETC.** For example, if you put an order to buy 5000 shares in and it only trades 1000 shares, you should not figure that you were filled on your whole position. Partial fills - say 1000 out of 3000 - are charged a full commission. And when the balance is filled, you are charged another commission. Figure those numbers into your data.

**5) KEEP IN MIND THAT WHEN YOU HAVE YOUR OWN MONEY ON THE**

## PENNY STOCK PROFITS

---

**LINE THAT FEAR AND GREED WILL BECOME MUCH STRONGER EMOTIONS.** Many analysts believe that they are the driving force in the market. And they are difficult to deal with. You need a detailed plan in advance to successfully ward off the deadly duo.

**6) SET UP YOUR PAPER TRADING ACCOUNT AS THOUGH IT WAS REAL TO YOU.** If you plan to invest \$1000, then set the paper trading account up with a beginning balance of \$1000. Then keep a very accurate running total of profits and losses on a daily basis. Only then will you learn what the risk really is.

**7) WRITE OUT THE DETAILS OF YOUR INVESTMENT PLAN.** What are the criteria for the stocks you will be buying? What are the exact details of your exit strategy for each and every position? How are you going to allocate your funds? Are you going to limit how much money you can invest in any one position? A good rule of thumb is to never invest more than 10% in any one position at the beginning. When you have a big winner, that will inevitably grow to far more than 10% of your investment portfolio.

# **12 RULES FOR PENNY STOCK INVESTMENT**

## **RULE NO. 1**

Never buy a penny stock from a stockbroker who phones you out of the blue with an unbelievable deal. Penny stocks that are being hawked by cold calling stockbrokers are never the good deals that they seem. The brokers are being paid handsomely to help distribute the stock at inflated price from the few insiders to the gullible public.

## **RULE NO. 2**

Never buy a penny stock from a high pressure salesperson. Investment in a legitimate emerging growth company is a long term proposition. A good little company is not likely to skyrocket in the next 24 hours no matter what your salesperson may say. It will take time even if it is the most legitimate company in the world. You certainly have time to research the matter on your own. If the salesperson doesn't want to provide you with sufficient information to check things out on your own, that is evidence enough that you do not want to buy that stock or deal with that broker.

## **RULE NO 3**

Never buy into blind pools. Sometimes scam artists will call with a pitch about putting together a few "qualified select" investors (and boy are you lucky to be one of the few chosen) in a pool that will invest in the next Microsoft and Cisco. Of course no details about how the money is going to actually be invested and what fees are going to be charged for this one-in-a-million opportunity are ever disclosed. Know exactly what you are buying and how you can independently check its value.

## **RULE NO 4**

Always carefully check your trade confirmations. On every trade you make, the law requires that the brokerage firm provide you with a detailed record of the transaction. The trade confirmation will indicate whether the trade was unsolicited (you initiated the trade) or unsolicited (the broker brought the trade idea to you). Devious penny stock broker will often mark trades "unsolicited" to avoid stringent registration and disclosure laws pertaining to penny stocks.

## **RULE NO. 5**

Buy only those penny stocks which are listed on the NYSE, ASE, or NASDAQ. Accurate timely price and volume information is available from many sources other than your broker. The Internet has literally thousands of sites

## **PENNY STOCK PROFITS**

---

which provide this information free. Company information on these stocks is readily available again from hundreds of sources. Each of these exchanges require that timely reports are filed with the SEC. The annual and quarterly reports of financial condition are available to the public from the SEC directly.

### **RULE NO. 6**

Never buy a stock with an inordinately wide spread. A wide spread presents unscrupulous broker-dealers with too many opportunities to profit from its trading with customers. It also indicates a thinly traded, easily manipulated stock. Stay away from them.

### **RULE NO. 7**

Never buy a penny stock with less than 3 market makers. This is never a problem with the NYSE, ASE, and NASDAQ penny stocks that we work with in our newsletter.

### **RULE NO. 8**

When you buy into a stock, decide in advance how many shares you plan to own. Then scale in your buying over time. Do not put your entire position on all at once.

### **RULE NO 9**

When you sell a stock, scale out of the position. Scale out of your positions over time. You do not have to be all in or all out when buying and selling stock.

### **RULE NO. 10**

When entering positions in penny stocks always use limit orders to specify your maximum buying price. When exiting positions a market order may be appropriate if you want to get out immediately.

### **RULE NO. 11**

Avoid brokers with 1000 or 2000 share cutoffs.

### **RULE NO. 12**

All other things being equal, avoid brokers with per share charges. When you are buying low priced stocks in the first place, per share charges can mount up.

## **STOCKS TO AVOID**

We have noticed that a number of the stocks listed below have been receiving heavy notice in Internet chat rooms and other sources of sometimes biased information. We suggest that you avoid the following stocks for the moment. They are listed on the OCT: Bulletin Board or the Pink Sheets. Wait until they qualify for the New York Stocks Exchange, the American Stock Exchange, or the NASDAQ. Of course some may very well go up. But our research suggests that at these price levels the potential risk outweighs the potential profit at this time.

Trudy Corp	TRDY	NAHC Corp	NAHC
Bico Inc	BIKO	Kaire Holdings	KAHI
Vertical Computer	VCSY	Kanakaris Wireless	KKRS
American Intl Petro	AIPN	Hitsgalore	HITS
Fonix Corp	FONX	Stereoscope	SSCP
Trans Energy	TRSG	Oklahoma Energy	OKOK
E-Prime Aerospace	EPEA	Wavo Corp	WAVO
Heilig Meyers	HMYRQ	Service Merchandise	SVCDQ
Iteq Corp	ITEQ	SI Diamond Technol	SIDT
Learncom	LRCM	Itemus	ITMUF
Go Online Networks	GONT	Aqua Vie Beverage	AVBC
Largo Vista Grp	LGOV	Auxer Grp	AXGI
US Office Products	OFIS	Far East Ventures	FEVI
Illinois Superconductor	ISCO	Prandium	PDIM
Hamischfeger	HRZIQ	Unicapital	UNPC
Tracker Corp	TRKR	Quest Products	QPRC
Tirex Corp	TXMC	Migratec	MIGR

EASY GUIDE TO GETTING RICH WITH PENNY STOCKS

# CHEAT SHEET CHECKLIST FOR SELECTING PENNY STOCKS

1) Is the stock traded on the New York Stock Exchange (NYSE ) American Stock Exchange (AXE ) or is it an OTC stocks listed on the NASDAQ ( BNASD ) If not, then go elsewhere

## 2) Is the company involved with new technologies?

Is the market for this product developing and growing? Yes No

Is the market for its products already mature and saturated? Yes No

e.g., a new manufacturer of PCs is not likely to be a good candidate

## 3) Examine the Balance Sheet in the financial statements

Is the current balance sheet audited?

Does the current balance sheet show more assets than liabilities?

How much debt is the company carrying compared to liquid assets?

High debt levels impede flexibility and interest rate expenses can eat up operating capital

## 4) Examine the Income Statement

Is the company making money?

Are earnings increasing?

If there are no earnings, check out sales numbers. Are sales increasing? Sales are a leading indicator of earnings.

## 5) Check out the prospects for the company's industry

Is the industry exhibiting growth?

Are there other stocks in the same industry which are outperforming the market?

## 6) Compare the company to its own industry

Does its products have some advantage over other industry members?

How does its earnings, debt levels, and growth compare to the industry?

## 7) What is the company's target customer base?

Will the customer base be expanding in the years ahead?

## PENNY STOCK PROFITS

---

### 8) Check out the management team

Does the CEO have prior successful experience?

Do the senior officers of the company own substantial company stock themselves?

Does a major part of the management team's compensation come from salaries or performance based on company profitability?

### 9) Check out the technical picture of the stock

Does the stock trade sufficient daily volume to enable you to buy and sell 1000 to 2000 shares of stock easily?

Is the volume increasing when the price rises?

Does the stock trade everyday? Avoid stocks which go for days without any trading.

Look at a price chart. Is the price at a level where buying has come in previously to boost it higher?

Is the price near a 52-week low?

If the price is near a 52-week high, how many times previously in the last 5 years has it traded at this level? What happened each time?

**10) Check out all recent news articles.** There are numerous Internet websites which feature news story archives you can check out. Look at [www.pcquote.com](http://www.pcquote.com) for one such source. If you do not have access to the Internet, most libraries have back issues of the WALL STREET JOURNAL, BARRON'S, or INVESTOR'S BUSINESS DAILY.

**11) No stock will be perfect in every aspect.** However, if the majority of the items above produce positive findings, you have found a stock worth buying.

### 12) Write down your purchase plan.

For example, if you want to own 1500 shares of a stock that is selling for \$2, you may enter limit orders to buy 500 shares at \$2, \$1.95, and \$1.90. Be prepared to adjust the buy prices higher or lower depending on the market. But do not chase prices if the stock moves away from you before you can put your whole position on.

### 13) Write down your exit plan.

What is your profit target?

How do you plan to take profits? Sell everything at the target price or scale out of your position at different prices. Write it down and follow it.

At what point are you going to cut your losses and exit the position? Write it down and follow it.

THIS PAGE IS LEFT INTENTIONALLY BLANK



