

Levère, Edwin – Reminiscences of a Stock Operator

John Wiley & Sons, first edition 1923, [Equity Investing] Grade ★★★★★

With surprisingly few exceptions those who have achieved real success on the stock market come from one out of two camps. The first one is value investors with a time horizon of 2 to 5 years and the other is momentum investors with a time horizon of 3 to 18 months. Few in each camp understand the other. Both camps have their own heroes and just as Ben Graham is the father of value investing, Jesse Livermore is the father of momentum investing - or speculation as he would have called it himself. This book is the fictionalized self-biography of Livermore written by the journalist Edwin Levère. Ever since its publication in 1923 the book has been the primary book classic amongst traders.

Livermore lived a stormy life. He succeeded to accumulate huge fortunes a number of times only to lose it all in a series of bankruptcies. Livermore's life tragically ended when he shot himself in a public lavatory. What makes the book a timeless classic is that it captures the psychology of a trader. The reader is able to follow Livermore's mistakes, the lessons he learns and all this turns into classic trading advice and insights. According to Livermore himself the chief mistake was that he got too impatient and that he invested in assets he didn't understand. As Livermore saw it a speculator should always take responsibility for his losses and not try to blame them on markets or bad luck. He kept a trading diary where he analysed his mistakes to avoid them further on.

In the short to medium term the main driver of stock prices is the effect that mass psychology has on supply and demand. This is as true today as in the time of Livermore and this is why the book has lost none of its actuality. In the words of Livermore "Wall Street never changes. The pockets change, the stocks change, but Wall Street never changes because human nature never changes." According to Livermore most people

invest without structure, they act from tips, hopes and rumours. Without a system and patience to wait for the right opportunities they make countless psychological mistakes. The role of the speculator is to take advantage of these errors.

Livermore was a trend follower. Follow the path of least resistance and never fight the tape. Buy stocks with strong momentum in markets trending up, short the weakest stocks in markets that trend down and have the discipline to stay out of markets that show no clear trend. Livermore didn't try to predict markets, he tried to react faster and more correct to the changes that occurred. One key lesson that Livermore learnt was to let profits run – why should you sell stocks that's developing fine? Instead sell the stocks that show a loss. In the bucket shops where Livermore speculated as a youngster there was a stop loss rule triggered when a position showed a 10 per cent loss. This developed into a life-long rule. "Never average down."

There is no real structure to the book, just the story of Livermore's life in chronological order, all told in an old fashioned but still accessible language. Levère is a good story teller and even though he had no prior experience of financial markets he spent several weeks interviewing Livermore. He weaves together the ebbs and flows of Livermore's life with his speculation and the trading lessons learnt. Together with for example Bernard Baruch, Livermore was a new breed of speculator that built on rules and systems instead of secret stock pools and insider information. It's really a treat to get into the mind of this giant of the financial history.

Few professional traders of any rank would admit that they missed to read this book and I wouldn't try to apply for a job at a hedge fund without being able to nod affirmative on the question if I had. "The trend is your friend".

Mats Larsson, December 28, 2011