

# Learn to Trade Guide

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Spread betting and CFD trading typically require the deposit of a small percentage of the total trade value. As the financial outcome is determined by the price movement on the total trade value, profits and losses can quickly exceed the initial deposit. Ensure you understand the risks as these products are not suitable for everyone. These products are only intended for people who are over 18.

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# 1. Spread betting

## What is spread betting?

In recent years, spread betting has grown into one of the most popular, accessible and dynamic ways to trade on the financial markets. Offering the opportunity to trade on both upward and downward movements in all kinds of markets for a fraction of the investment that would be required in the underlying markets, spread betting has become the tool of choice for all kinds of investors.

If you think a particular asset is likely to rise or fall in price, you can invest in that movement, and your profit or loss will be multiplied by the extent to which the asset moves in either direction. If you bet on an asset to rise, your profit will be the number of points it rises multiplied by the size of your stake. If it falls, your loss will be the number of points it falls multiplied by your stake.

Spread betting is a low-cost way to access the financial markets. Unlike with direct trading, you don't need to commit the value of the underlying investment, but instead deposit only a fraction of the overall value, allowing you to magnify your potential earnings to a degree that would not be possible if you bought the underlying asset itself. This also allows you to spread your investments around a range of trades, freeing up your capital for other forms of investment.

Please remember that spread betting and CFD trading are leveraged products and can result in losses quickly exceeding an initial outlay. They are not suitable for everyone and you should make sure you fully understand the risks involved. You must be over 18 and resident in the UK."

## Types of spread bets

Selftrade CFDs and Selftrade Spread Betting offers a range of different spread betting options to suit your requirements. These allow you to structure your trading to suit your view of the markets and your own financial arrangements, giving you the flexibility that you need.

### Daily Funded Trade

A Daily Funded Trade (DFT) is a spread trade where Our Price is based on the current market price of the Underlying Instrument. Daily Financing and dividends are not included in the calculation of Our Price but appear as separate charges or credits to your account. There is no overnight crystallisation of open profits or losses, financing charges or dividends until the Daily Funded Trade is closed or partially closed. Daily Funded Trades typically have a long term settlement date (as specified in the Market Information).

### Quarterly Bets

Quarterly Bets have a set expiry date, allowing you to make a trade and then sit back and see where the market takes it. These bets are based on specific quarters and you can make a trade at any point in the three months leading up to the expiry of the contract. Quarterly bets are more suited to taking a longer term view of the market than Daily Funded Trades, however they do not need to be held until expiry – you can close the contract earlier than the expiry date if you wish.

With quarterly bets, the financing charge is built into the spread – there is no additional overnight financing charge.

## Why use spread betting compared with other ways of trading?

However much time you have to keep track of your trades, spread betting allows you to tap into movements on global financial markets. It differs from other types of trading in a number of significant ways:

- Compared with direct share trading, spread betting is faster-moving, more easily accessible, more flexible and can be done at much lower cost. Spread betting with Selftrade CFDs and Selftrade Spread Betting offers you access to markets all over the world, it is simple, and it allows you to speculate on market movements at only a fraction of the cost of direct investment in the underlying markets.
- One of the main advantages of spread betting is the access it provides to a wide range of markets that would otherwise not be accessible to the retail trader. Through spread betting you can speculate on the price movements of gold, oil, or currency pairs as easily as you can trade on the price movements of an individual share. What's more, the thousands of markets available are all accessible from a single account, and can be traded in a size that suits you.
- Spread Betting is free of both UK stamp duty and UK Capital Gains Tax (CGT), although tax laws are subject to change and depend on individual circumstances and is free of Brokers commissions.

Spread betting does, however, carry far higher risks to your capital than many traditional forms of trading. It is important that you understand the risks involved before you start trading.

## How does spread betting work?

With spread betting you are quoted two prices. The lower of these two prices is the 'bid' and is the price you will receive if you sell. The higher of the two prices is the 'offer' and is the price you will pay if you buy. The difference between these two prices is the spread, and reflects the cost of trading.

## Here are some simple examples of spread betting in action.

### Index trading

The UK 100 Index (the index of the UK's 100 largest companies by market capitalisation) is at 5950, and you expect it to rise. On the UK 100 DFT, Selftrade CFDs and Selftrade Spread Betting is quoting a spread of 5949/5951 (bid 5949, offer 5951). You open a long position at £10 per point, buying at 5951.

Scenario 1	Scenario 2
As you hoped, the UK 100 Index rises. When the index reaches 6000, you decide to take your profits. The Selftrade CFDs and Selftrade Spread Betting spread is now 5999/6001, so you sell at 5999.	The UK 100 Index falls. When it reaches 5900 you decide to cut your losses and pull out. Selftrade CFDs and Selftrade Spread Betting is now quoting a spread of 5899/5901, so you sell at 5899.
Result	
You bought at 5951 and sold at 5999, giving you an increase of 48 points, which at £10 per point makes a profit of £480.	You bought at 5951 and sold at 5899, giving a fall of 52 points, which at £10 per point makes a loss of £520.

### Equity trading

You think Royal Bank of Scotland shares are overvalued at 350p. Selftrade CFDs and Selftrade Spread Betting is quoting a spread of 349p/351p, so you open a short position at 349p at £10 a point.

Scenario 1	Scenario 2
RBS shares start to slide. When they reach 300p you decide to take your profits. Selftrade CFDs and Selftrade Spread Betting is now quoting a spread of 299p/301p, so you close your position at 301p.	RBS shares rise. When they reach 400p you decide to cut your losses. Selftrade CFDs and Selftrade Spread Betting is now quoting a spread of 399p/401p, so you close your position at 401p.
Result	
You sold at 349p and bought at 301p, a fall of 48p, which at £10 a point makes a profit of £480.	You sold at 349p and bought at 401p, a rise of 52p, which at £10 a point makes a loss of £520.

Please note: In the above examples, financing charges and payments have been omitted to keep them simple. It is important to remember that holding a long position overnight will incur financing charges, while holding a short position overnight will benefit from financing payments. These payments will need to be taken into account when calculating your final profit or loss.

## 2. CFDs

### What are CFDs?

A CFD is an agreement between you and a provider such as Selftrade CFDs and Selftrade Spread Betting to exchange the opening and closing values of a particular trade. Trading in CFDs (Contracts for Difference) has grown rapidly in recent years to become a highly popular form of investment among both individuals and institutions. CFDs provide investors with access to the price movements in financial markets at a fraction of the cost of direct investment in those markets and are often used as hedging devices.

If you think a particular asset is likely to rise or fall in price, you can open a CFD on that asset, either going long if you think the asset will rise or going short if you think it will fall. The provider offers a price and the investor deposits a fraction of the overall value of the trade and then has access to the full benefits of movement in the price of the underlying asset, without actually needing to own the asset itself.

CFD trading offers a way to invest in financial markets all over the world without having to provide the full cost of the underlying asset. It provides the opportunity to make the same total profits (or losses) from price movements as traders in the underlying markets but at a fraction of the cost, resulting in the chance of a much better return on investment.

### Why trade CFDs compared with other ways of trading?

- Compared with direct investment, trading CFDs offers access to worldwide markets without the cost and complication of trading assets in those markets directly, making it a cost-effective way to provide yourself with a broad range of trading opportunities. You can make your investment as large or as small as suits your requirements and tailor the structure of your CFDs to your own needs.
- The ability to go long or short and the range of markets in which CFDs are available make them an ideal tool for investors, whether you are looking for a simple leveraging opportunity or for a hedging tool to be used as part of a complex investment portfolio.
- CFD trading also has the advantage over direct investment of being exempt from UK stamp duty, which is charged at 0.5% on the purchase of UK equities.
- Unlike spread betting, profits from CFD trading are liable to UK Capital Gains Tax (CGT). This has advantages and disadvantages. Although you will pay tax on any profits from your CFD trading, you can offset any losses from your CFD trading against your CGT liability. If you are trading CFDs as part of a wider investment portfolio this can be a useful benefit. Remember tax laws are subject to change and depend on individual circumstances.

It is important to remember, however, that CFD trading carries a far higher risk to your capital than many traditional forms of trading. It is important that you understand the risks involved before you start trading.

### How does it work?

With CFD trading you are quoted two prices, as with traditional equity trading. The lower of these two prices is the 'bid' and is the price you will receive if you sell. The higher of the two prices is the 'offer' and is the price you will pay if you buy.

Here are some simple examples of CFD trading in action.

### Index trading

The UK 100 Index is at 5950, and you expect it to rise. Selftrade CFDs and Selftrade Spread Betting is quoting a spread of 5948/5952 (buying at 5948, selling at 5952). The value per index point on the UK 100 Index is £1, so you open 5 long CFDs at 5952, making £5 a point.

The value of your position is  $5 \times £1 \times 5,952 = £29,760$ . With Selftrade CFDs and Selftrade Spread Betting requiring a margin of 5 per cent on index CFDs, the margin requirement is  $£29,760 \times 5\% = £1,488$ .

Scenario 1	Scenario 2
The UK 100 Index rises. When it reaches 6000, you decide to take your profits. The Selftrade CFDs and Selftrade Spread Betting spread is now 5998/6002, so you close your position at 5998.	The UK 100 Index falls. When it reaches 5900 you decide to cut your losses. Selftrade CFDs and Selftrade Spread Betting is now quoting a spread of 5898/5902, so you close at 5898.
Result	
You opened your position at 5952 and closed at 5998, a rise of 46 points, which, at £5 a point, makes a profit of £230.	You opened at 5952 and closed at 5898, a fall of 54 points, which at £5 per point makes a loss of £270.

### Equity trading

You think Royal Bank of Scotland shares are overvalued at 350p. Selftrade CFDs and Selftrade Spread Betting is quoting a spread of 348p/352p, so you open a short CFD on 1,000 shares at 348p.

The value of your position is  $1,000 \times £3.48 = £3,480$ . With Selftrade CFDs and Selftrade Spread Betting requiring a margin of 10 per cent, the margin requirement is  $£3,480 \times 10\% = £348$ .

Scenario 1	Scenario 2
RBS shares start to slide. When they reach 302p you decide to take your profits. Selftrade CFDs and Selftrade Spread Betting is now quoting a spread of 298p/302p, so you close your position at 302p.	RBS shares rise. When they reach 402p you decide to cut your losses. Selftrade CFDs and Selftrade Spread Betting is now quoting a spread of 398p/402p, so you close your position at 402p.
Result	
You opened your short position at 348p and closed at 302p, a fall of 46p, giving you a profit of £460.	You opened your position at 348p and closed at 402p, a rise of 54p, giving you a loss of £540.

Commission is payable on some CFD trades, including equity trades. Full details of commissions can be found in our Market Information Sheets.

Please note: In the above examples, financing charges and payments have been omitted to keep them simple. It is important to remember that holding a long position overnight will incur financing charges, while holding a short position overnight will benefit from financing payments. These payments will need to be taken into account when calculating your final profit or loss.

## 3. Our markets

Spread betting and CFD trading with Selftrade CFDs and Selftrade Spread Betting offers you access to thousands of different markets around the world.

Whether it's individual stocks in the UK, the US or Europe, the Australian dollar versus sterling, or pork bellies and soya bean oil, our trading platform allows you to take both long and short positions on a huge range of markets that would otherwise be unavailable to the ordinary investor. It opens up a world of investment opportunities in all kinds of exciting and fluid markets, allowing your trading to be as focused or as complex and adventurous as you wish.

### Equities

Selftrade CFDs and Selftrade Spread Betting offers spread betting and CFD trading on thousands of individual stocks in UK, US and European markets. Equities on offer include the UK's largest 350 stocks by market capitalisation, US stocks on the Wall Street and in the US Tech 100 Index with market capitalisation of more than \$1 billion, and European equities quoted on the major exchanges with capitalisation of more than €1 billion.

### Stock Indices

For a broader view, we offer prices on the overall stock index for markets in the UK, Europe, Asia and the US. Markets covered include the UK 100 Index, the Wall Street Index, US Tech 100 Index, Hang Seng and the German 30.

### UK market sectors

As well as specific stocks and overall indices, we offer prices on individual sectors of the UK market. More than 30 sectors are quoted including banks, pharmaceuticals and biotechnology, oil and gas, and media.

### Currencies

We offer spread betting and CFD trading on a wide range of currencies including sterling, euro, yen, Swiss franc and US, Canadian and Australian dollars.

### Precious metals and commodities

We offer prices on gold, silver and other precious metals, on oil prices and on the main commodities markets, including cocoa, coffee, sugar, pork bellies, wheat and soya bean oil.

## 4. Features

Spread betting and trading CFDs with Selftrade CFDs and Selftrade Spread Betting brings a wide range of features. Unrivalled price transparency and highly competitive spreads and margins ensure you get the most from your trading, while the range of markets we offer ensures that there is something for every investor, whatever your area of interest or level of expertise.

### Margin trading

As forms of margin trading, both spread betting and CFD trading offer you the chance to leverage your position, providing greater potential returns (or losses) than would be available through direct investment in the underlying asset. Whether spread betting or trading CFDs, you are required to deposit only a small percentage of the total value of the position, allowing access to substantial returns for a relatively small investment.

### Worldwide markets

You can trade equity, index, currency and commodities markets all over the world from a single online account, supported around the clock by telephone dealing and customer service staff.

### Instant access

Our state-of-the-art trading platform gives you instant access to your account, whenever, and wherever you want to trade. Spread betting and CFD trading offer all the tools you need to make the most of trading opportunities around the globe, with firm quotes, accurate tracking of the underlying instruments and comprehensive market news.

### Maximum leverage

In today's volatile markets, the opportunity to take long or short positions on a huge range of assets at a fraction of the cost of the underlying investment offers the opportunity to make profits whatever the direction of the markets. The leverage offered by CFDs and spread betting provides a particularly strong advantage at a time of tight credit markets and uncertain economic outlook, and the number of traders recognising the benefits of these products continues to increase year on year. However, it is important to remember that this form of leverage trading carries a far higher risk to your capital than many traditional forms of trading.

### Hedging opportunities

CFDs and spread betting offer a highly cost-efficient method of hedging against other investments. A relatively small investment in the opposite direction in these markets can easily offset any possible reversal on a bigger direct investment elsewhere.

### Tax benefits

Spread betting and CFD trading also offer substantial tax benefits. Spread betting is exempt from both UK stamp duty and UK Capital Gains Tax, while CFD trading is liable to UK Capital Gains Tax but is exempt from UK Stamp Duty. However tax laws are subject to change and depend on individual circumstances.

## 5. Margin and risk

Spread betting and CFD trading are derivative products that you trade on margin. That means that you need only to deposit a small fraction of the value of the underlying investment to gain access to the benefits of movements in the price of that investment. Investors in the underlying market, on the other hand, would need to provide the total cost of the investment in order to benefit from movements in its price.

Spread betting and CFD trading offers the opportunity to make large returns for a small initial outlay. This also means SB & CFDs have more risk than holding traditional shares because it is possible to lose more money than your initial capital outlay.

### What are the risks?

The differences between the risks faced by investors in spread betting and CFDs and those in the direct markets are best demonstrated by an example from the share market.

If you bought 200 shares in a particular company at 500p a share, you would know that the limit of your risk on that investment was £1,000.	
If, in the worst possible case, the value of the shares fell to nothing, your maximum potential loss would be £1,000.	If, on the other hand, you opened a long spread bet on those same shares at £10 per point, your potential risk would theoretically be much larger. Just a 20 per cent fall in the share price, by 100p, would see your loss reach £1,000. A further 20 per cent fall would lose you another £1,000, and a complete collapse in the price to nothing would see you lose £5,000, five times the loss of the direct shareholder.

That's an extreme example but a possibility. But even in the case of more realistic movements in share prices, the risks of spread betting and CFD trading can be higher than with direct trading. To take the shares mentioned above, if the price fell by just 5 per cent to 475p, the value of the direct purchaser's investment would fall by only £50, whereas the spread better would be down by £250.

These potential losses are simply the opposite side of the potential profits if things go well. Selftrade CFDs and Selftrade Spread Betting offers a range of risk-management tools to keep your losses well under control and limit them to a level you are happy with.

### Understand your risk appetite

The potential returns from spread betting and CFD trading far outweigh the potential returns from direct investment given the same price movements, and so do the potential losses. Before committing yourself to spread betting or CFD trading, you need to have a good idea of your appetite for risk. Selftrade CFDs and Selftrade Spread Betting offers a wide range of tools for limiting your risk, but it is still important to understand the potential for being caught on the wrong side of a price movement.

If you prefer a low-risk, low-return approach to investment, then perhaps spread betting and CFDs are not for you. But if you are prepared to risk larger (albeit limitable) losses for the chance of larger returns, then you're in the right place.

## What is margin trading?

The margin is the deposit factor required for a particular type of trade, multiplied by your stake, that you need to have in your account to open a position. The margin for each type of trade depends on the market, and is set according to the volatility of that particular market, usually somewhere between 10 and 20 per cent.

The margin required depends on the value of the underlying trade. For example, if you opened a spread bet of £10 per point on a particular share, that would be the equivalent of buying 1,000 shares, because each penny movement in the price would be worth £10 to you. If the share was worth 500p, then your bet would be the equivalent of a position in shares worth £5,000 (1,000 x 500p). If the margin requirement was 10 per cent, then you would be required to put £500 (£5,000 x 10%) in your account to open the position.

If the price moves in your direction, then your initial margin plus the increase in the value of your position will ensure that your margin requirements are covered. If, however, your position moves against you, you will be required to put further funds into your account to cover your margin requirement.

For example, if you have opened a long position on the above shares, at £10 per point, and the shares fall by 10p to 490p, you will have lost £100, leaving your account showing £400. The margin requirement of your position will now be £490 (490p x 1,000 x 10%), so you would be required to deposit a further £90 to cover your total position.

## 6. Managing your risk

Although spread betting and CFD trading carry higher risks than more traditional investment, by using the risk management tools available through Selftrade CFDs and Selftrade Spread Betting you can limit the risk of every trade you place. These tools are available to all clients and are simple to implement.

It is crucial to understand the products that you are trading and to apply the most appropriate risk-management tools. As with traditional share dealing, the most successful spread betters and CFD traders are the ones who understand and manage their risks. The potential profits from this kind of investment are amplified, but so are the potential losses, and the use of stop losses and guaranteed stop losses will help you to manage the downside without affecting your potential gains.

### Stop loss

A stop loss is an order to close an open position when the market reaches a predetermined level. The potential loss on a position is limited by requesting that the trade is closed once the price has fallen to that level. Stop losses do not guarantee the price at which your trade is closed – a stop loss will trigger a close order at the next available price in the market. This means that if the market ‘gaps’ your stop loss level, your trade will not be closed at exactly this price. To guarantee the closing price of a stop loss order you should use a guaranteed stop loss.

### Guaranteed stop loss

A guaranteed stop loss order offers a level of certainty above other stop losses. It guarantees that the level at which your order will be executed is the exact level that you set, regardless of any gapping in the market or Selftrade CFDs and Selftrade Spread Betting trading hours. An additional spread or charge is applied in connection with a guaranteed stop loss order. Selftrade CFDs and Selftrade Spread Betting offers guaranteed stop losses that are especially useful in volatile markets, when prices can move suddenly and significantly and may not hit the exact level at which you set your stop loss. Guaranteed stop losses are not available on all markets and are available at an additional charge – details of the markets available can be found in our Market Information Sheets.



Client opens a sell position at the  $\uparrow$  at the yellow line (approx 14120). By selling, he thinks the price will fall. After falling nearly 20 points (to approx 14100), the price gaps (which can happen in volatile markets such as Oil – you can see further evidence of gapping in the graph above), and opens again at 14145 (where the green line is).

**Scenario A:** With his opening trade, the client attaches a standard stoploss (to buy) at blue line (approx 14130). As the price gaps past his stoploss price, the position will only be closed at the next available price (green line).

**Scenario B:** With his opening trade, the client attaches a guaranteed stoploss (to buy) at the blue line (approx 14130). Even though the price gaps past his stoploss price, as it is a guaranteed stop it will still close the position out at the price he chose (blue line, approx 14130).

## Limit orders

Limit orders are placed at a better price than the prevailing price. For a purchase, a limit order would be set at a price below the current price, and for a sale it would be set at a price above the current price. They can either be set independently or attached to an open position. Limit orders are useful if you believe the price of the underlying asset will move to a more favourable level in the future, but you do not want to watch the market until this happens to make your trade.

Take profit orders: Limit orders for a sale are set at price above the current price, and are also known as 'take profit' orders.

As the name suggests, they will lock in your profit if the price of your instrument moves to your chosen level.

## Stop orders

Stop orders are placed at a worse price than the prevailing price. An order to buy would thus be placed at a higher level than the prevailing price, and an order to sell would be placed at a lower level than the prevailing price. Stop losses and guaranteed stop losses are stop orders used to limit downside potential, but a stop order can also be used to open a new position when a market reaches a point at which you believe it may see a reversal of recent trends.

## One cancels the other orders

One cancels the other orders are used to link a stop loss order and linked limit order to an open position. They are generally used to set maximum profit and loss levels. If one of the orders is executed the open position is closed and the remaining order is automatically cancelled.

## 7. Trading styles

### What sort of trader are you?

To become a successful trader in any market you need to define your approach. In spread betting or CFD trading, as in any other market, there are a number of styles traders can adopt, all of which can provide a route to successful trading. Most traders find, however, that one style best suits their temperament, abilities and resources, and that focusing their activity on that approach yields the best results.

If you can identify the kind of trading to which you are best suited, you will take an important step along the road to becoming a successful trader, and you will also set yourself parameters that will help make your trading more disciplined and targeted, expanding your skills and experience in the area where they can have the biggest impact.

The table below is designed to help you think about which category you fall into. Many people fit into more than one category and will hold many different positions at a time. The most important thing to do is remain disciplined and not overcomplicate your trading strategy. Ultimately you will find a style that suits you.

	Day trader	Swing trader	Position trader
Objective	Capture intra-day movements only	Trade short term directional moves over a few days	Trade longer term from days to weeks, to capture larger trends
Trade held overnight	No	Yes	Yes
Average number of days in trade	1 only	1-5 days	5+ days
Number of trades	High	Medium	Low
Usual Trading strategies	Technical analysis	Technical analysis	Fundamental with Technical analysis

### How do you make your trading decisions?

In all financial markets, from traditional share-dealing to the most highly engineered derivatives trading, there are two main approaches to making trading decisions. All traders use either one approach or the other, or employ a combination of the two.

#### Fundamental analysis

Fundamental analysis is a method of evaluating an asset by attempting to measure its intrinsic value. Fundamental analysts study everything from the overall economic and industrial conditions to the financial condition and management of individual companies.

This method of analysis takes into account economic data such as GDP, inflation, employment, balance of trade and retail sales figures, plus government monetary and fiscal policies and consumer trends. On a smaller scale, it also examines individual companies' revenues, earnings, return on equity, profit margins and other data to determine its underlying value and potential for future growth.

Fundamental analysts combine all this data into an overall picture of the general and specific outlook for a particular asset and make their trading decisions on the basis of that data.

## Technical analysis

Technical analysis is a method of evaluating an asset not by its intrinsic value but on the basis of analysis of statistics generated by market activity, such as past prices and volume, using charts to identify patterns that can suggest future movement in the price of that asset.

Technical analysts believe that the historical performance of securities and markets are indications of future performance. They use tools such as indicators and oscillators to predict the direction in which markets will move on the premise that price movements are patterned and cyclical rather than random. Thousands of techniques are used by technical analysts around the world to track the movements of markets and predict their next moves.

## 8. Trading strategies

Spread betting and CFD trading can be used in all kinds of complex ways. Some of the most sophisticated traders in the financial markets make regular use of these tools as part of their portfolios, including as a way of hedging their investments, as a method of improving their tax efficiency and as a low-cost way of replicating their positions in equity and other markets. All these trading strategies are open to investors through spread betting and CFDs, and it's well worth examining how you could use the different opportunities on offer.

### Speculation

The simplest reason for trading with spread betting or CFDs is the cost-efficient opportunities they offer for speculation. They provide the ordinary investor with access to a huge variety of markets that would otherwise be well out of reach, and allow you to make relatively small investments with potentially large returns, providing the maximum leverage for your capital. Thousands of small-scale private investors and experienced professional traders make use of the leveraged opportunities offered by spread betting and CFD markets.

### Hedging

Spread betting and CFD trading are ideal ways to hedge against the risk of a fall in the value of your other investments. If you have an equity holding in a particular company, for example, you can open a short spread bet or CFD on that company's shares, protecting yourself against a decline in the shares, at only a fraction of the cost of the shares themselves. The same method can be used to hedge positions in currency, commodity and other markets, whether your main investment is long or short, providing an essential and cost-effective way of protecting your overall portfolio. The absence of stamp duty and, in the case of spread bets, UK Capital Gains Tax, adds to the appeal of these tools as cost-effective hedging instruments.

### Pairs trading

Spread bets and CFDs are also ideally suited for pairs trading. Pairs trading is a strategy in which you aim to profit from one asset outperforming another. A common example of pairs trading is where you examine two companies in the same sector and open a long position on the stronger of the two and a short position on the weaker. This particular strategy is based on the expectation that if the overall sector rises the price of the stronger company will rise more quickly than the price of the weaker, leading to a profit, and that if the sector falls the weaker company will fall more quickly than the stronger one, again leading to a profit. The same approach can be applied to companies across different sectors but with other kinds of relationships, such as when they represent different points in a supply chain.

### Replicating or replacing equity positions

One appeal of spread betting and CFD trading is as a way of either replicating equity trading positions or replacing those positions entirely. The low margin requirements involved in spread bets and CFDs offer you the opportunity to invest in the markets you like, but at a fraction of the cost and with a lower tax liability than in direct trading. Rather than pay the full value of shares, you can either replace parts of your equity portfolio entirely with spread bets or CFDs on the same assets, or use spread bets and CFDs as a low-cost way of increasing your investment in the markets that appeal to you.

## Tax-efficient trading

Many investors choose spread betting and CFD trading for the tax benefits involved. While gains on direct investments in the underlying assets are liable to UK Capital Gains Tax and UK stamp duty, spread betting is liable to neither and CFD trading is liable only to Capital Gains Tax. However, tax laws are subject to change and depend on individual circumstances.

Remember that there are pros and cons to exemption from Capital Gains Tax. While your profits will not be taxed, your losses cannot be offset against profits in any other investment.