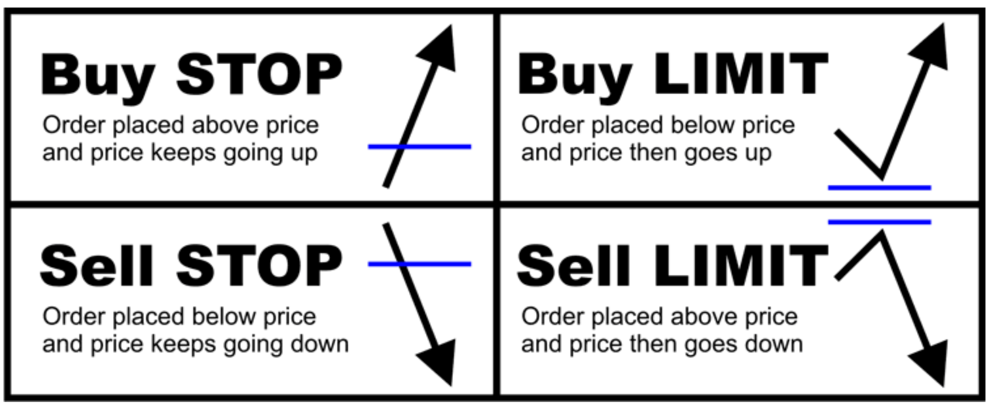
Trading Best Practice

Definition

- Trading is about making emotionless decision based on risk management and strategy.
- Trading is a zero sum game.
- Price action and charts are a representation of human behaviour.
- For any trade, you will:
    - Make profit;
    - Take loss.
- There are two ways to make profit: Long and Short.
- For any position, you can do:
    - Sell all;
    - Sell some;
    - Buy more;
    - Hold.



Psychology

- Technically, trading isn't very hard, psychologically, it's the hardest game on the planet. Intellectual demands of trading are modest, but its emotional demands are immense.
- It is human nature to take profits quickly and losses slowly.
- Logic wins and impulse kills. Trading impulsively is simply gambling.
- Warren Buffett: "Be scared when people are greedy, and greedy when people are scared".
- The fastest way to go broke is to try to get rich quick.
- To be a profitable trader, you have to learn not only how markets work, but how

your own ego and emotions work against you.
- Being a profitable trader or investor is not about chart patterns or predictions. It's about emotional intelligence and a systematic process.
- Nobody should quit a paid job to trade unless he has been profitable for last 2 years and capital traded came from profits.
- Do not exit your trade just because of your fear to give back profit. Instead exit your trades based on your exit signal. This ensures you ride your profits to compensate for the little losses that you will incur along the way.
- Trade small sizes while learning.
- Do not count money in open trades. Thinking about money interferes with decision making.
- Your survival and success depend on your willingness to cut losses while they are relatively small.
- Trading is not about being right. It is about losing small when you are wrong, and winning big when you are right.
- Do not find an excuse to place a trade. Follow your trading plan strictly.
- Less trading + patience = profit.
- You should always manage your trade on the time frame you are entering. Not on a lower or higher time frame.
- Downtrends tend to move twice as fast as uptrends.
- What is high can go higher and what is low can go lower. The market is never too high to long, or too low to short.
- Stop loss order is the greatest trading tool.
- If you can’t take a small loss, sooner or later you will take the mother of all losses.
- It’s better to get stopped for a loss than take a small profit.
- Always choose a price level that will prove your trade entry was wrong and set a stop loss at that level. Exit your trade when proven wrong.
- There are 3 way to set stop loss to reduce risk:
    - Volatility stop: base on the Average True Range (ATR), need to identify the current ATR and multiply by a factor of your choice (2*ATR, 2*ATR, 4*ATR etc.);
    - Time stop: instead of exiting your trades based on price, you exit your trades after X amount of time has passed;
    - Structure stop: you take into account the structure of the market and set your stop loss accordingly (for example you set your stop loss below support).

Methodology

- Strategic trading goals are:

    - Conserve capital;
    - Generate income;
    - Increase account size.
- Before entering a trade, write down your trading plan, especially these three numbers: entry, stop and target. Placing a trade without defining these numbers is gambling.
- Keep a trading diary and review it
- Look at 3 things only:
    - Price action and charts;
    - Volume;
    - Context.
- Don’t trade every day, only take a couple of trades a month (Pareto law: 80% of profits come from 20% of trades).
- Remember your goal is to trade well, no to trade often.
- Don’t expect the market to behave exactly the same way twice. The market is an artist, not a computer.
- Most breakouts are exhaustion moves that are soon aborted. Most breakouts fail and are followed by reversals.
- Trade your plan and take full responsibility for each trade and ignore the opinions of others.
- Most trading errors arise from emotional mistakes:
    - Greed trades too big;
    - Fear exits winners fast;
    - Hope holds losing trades too long.
- You don’t need to know everything about the markets to make money. You just need to be really good at one thing.

Risk management

- The most important aspect of trading is risk management.
- There are two quick ways to ruin an account:
    - Not use stops;
    - Put on trades that are too large for that account’s size.
- Never trade with money you can’t afford to lose: have a budget for trading that if you start to losing it you can handle emotionally and mentally.
- Learn to take a loss but on’t hold on to a consistently losing coin.
- Alexander Elder: “Successful trading should be a little bit boring”.
- Write down your entry level, profit target, and stop for every planned trade in order to compare your risk and reward.
- There's 4 possible outcomes for your trade:

- Small win;
- Small loss;
- Big win;
- Big loss (eliminate this outcome).

The Mathematics of Losses	
How much must you make to break even?	
If you lose:	You must make:
5%	5.3%
10%	11.1%
20%	25.0%
30%	42.9%
40%	66.7%
50%	100.0%
60%	150.0%
70%	233.3%
80%	400.0%
90%	900.0%