



# Fundamentals of Risk Management

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# Overview

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- Risk Management
- Components of Trade Risk
- Applying Risk Management Components
- Risk Management Plan
- Mechanical Risk Management
- Risk Management Examples



# Risk and Management

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What is Risk?

- Definition: A situation involving exposure to danger

What is Management?

- Definition: The process of dealing with or controlling things or people
- In situations that have risk, the lack of identification and management of risk is described as a threat.
- Humans are constantly performing variations of Risk Management with choices and activities every day.

# Risk Management



There are 18 black slots, 18 red slots, and two green slots.

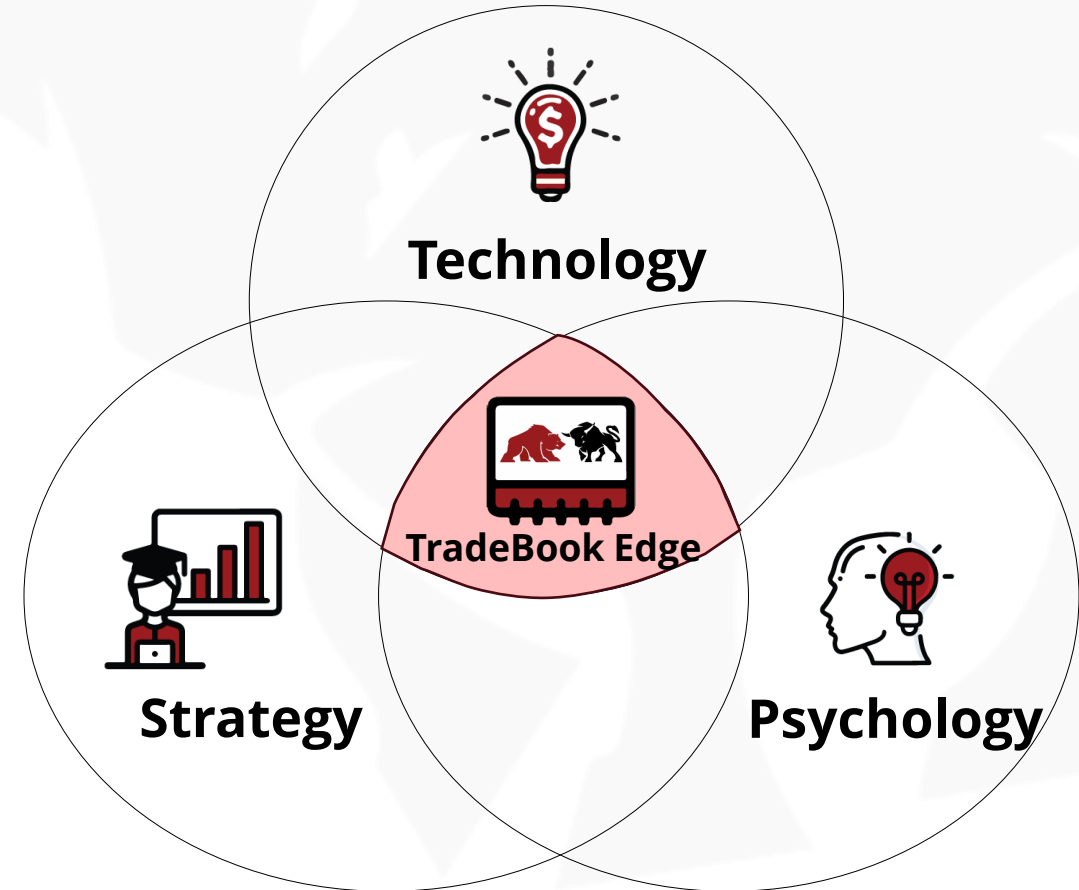
Your chances of hitting a black or red are equal: **47.4%**.

Casino probability will be **52.6%**, because of those two green slot.

The **5.26%** 'spread' is known as **the house edge**.

# Risk Management

- What is Risk Management?
  - Definition: Process of identifying, assessing and controlling threats to an organization's capital and earnings.
  - In the context of Trading, risk relates to any threat to trading capital.
- Risk Management Framework (RMF)
  - Risk Identification
  - Risk Measurement
  - Risk Mitigation
  - Risk Reporting and Monitoring
  - Risk Governance
- Trading Threats
  - Trader Issues (Core Risks)
    - Technology Knowledge
    - Strategy Knowledge
    - Psychology
    - Physical Well-Being
  - Mechanical Issues (Non-Core Risks)
    - Internet Connection
    - Platform and Data Issues
    - Power Outage
    - Mother Nature



# Components of Trade Risk

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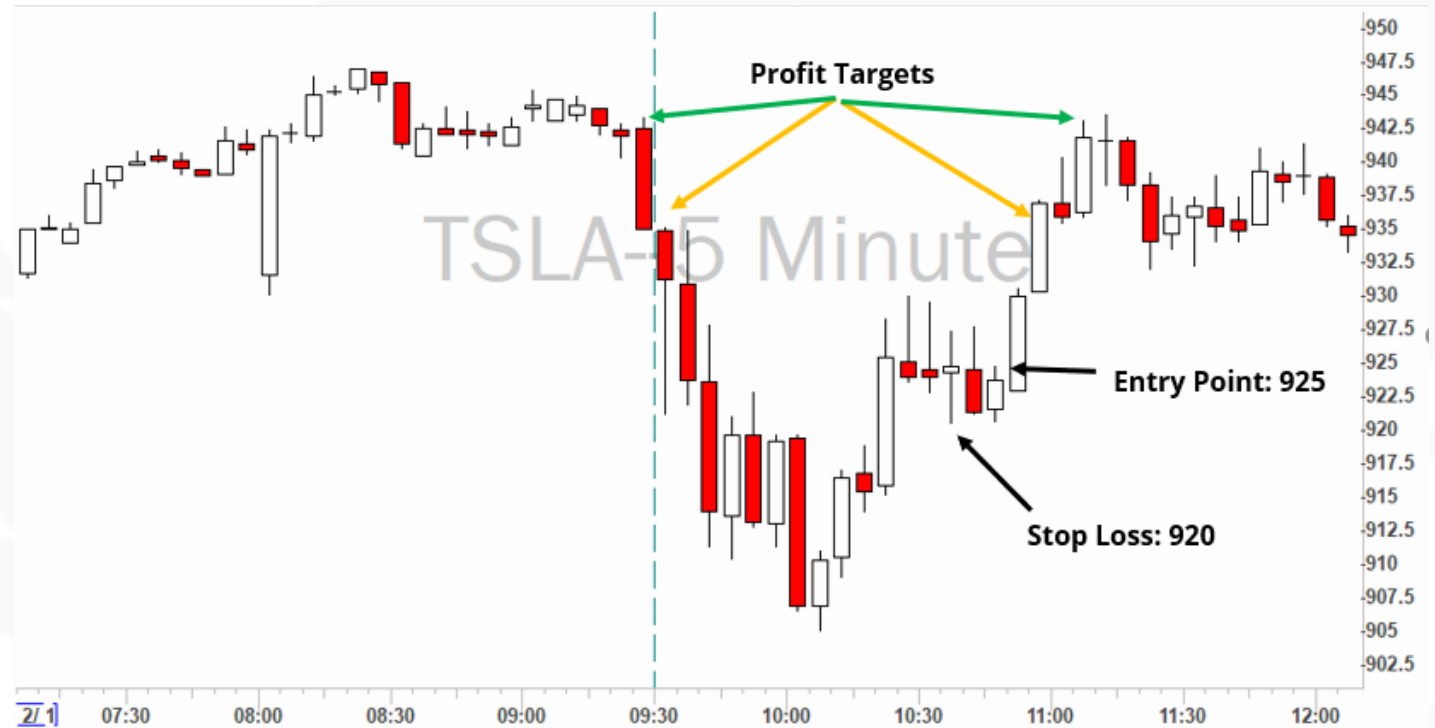
- Trade Risk to Reward (R:R)
  - Entry
  - Stop Loss (Manual and/or Hard)
  - Profit Target(s)
- Share Sizing
  - Fixed Share Size
  - % of Account/Buying Power
  - Fixed Dollar Amount per Trade (R Value)
- Stock Attributes
  - Bid/Ask Spread
  - Average True Range (ATR)
  - Float
  - Intraday Volatility
- Trade Strategy
  - Trade Instrument
  - Setup and Criteria

# Trade Risk to Reward

All trades should have clear entry, stop loss, and profit targets defined as you are considering the setup.

Trade Example:

- Entry: 925 (5 Minute High)
- Stop Loss: 920 (Technical Level)
- Profit Target(s)
  - 935 (High of Day / Twice the Risk)
  - 940 (Premarket Area / Triple the Risk)



# Risk to Reward

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Traders find edge by understanding and managing risk as defined by their trade's Risk to Reward Profile.

<b>Risk:Reward = 1:1</b>	<b>Risk:Reward = 1:2</b>	<b>Risk:Reward = 1:3</b>	<b>Risk:Reward = 1:5</b>
Risk = 2%	Risk = 2%	Risk = 2%	Risk = 2%
Reward = 2%	Reward = 4%	Reward = 6%	Reward = 10%
Trades Won = 6	Trades Won = 4	Trades Won = 3	Trades Won = 2
Trades Lost = 4	Trades Lost = 6	Trades Lost = 7	Trades Lost = 8
Total Profit = 4%	Total Profit = 4%	Total Profit = 4%	Total Profit = 4%

# Share Sizing

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## Account Threats and Risk Management Rules

- Do not risk more than 1% of your account on any single trade (Shark Bite) 
- Do not allow account to draw down in excess of 7% per block of time (Piranha Bites)



## Share Sizing Methods

- Fixed Share Size
  - 100 Shares per trade for stocks priced 25 to 50/share
  - 50 Shares per trade for stocks priced 50 to 100/share
  - 25 Shares per trade for stocks priced 100 to 200/share
- % of Account per Trade
  - Account Size: 10,000
  - Risk per Trade: 1% of Account
  - Total Risk per Trade =  $10,000 * .01 = 100/\text{trade}$
- Fixed Risk Per Trade (R Value)
  - R = 50 meaning every trade risks 50 dollars

Choosing a Share Sizing Method is depending on the trader

# Trade Example with Share Sizing

Let's apply various Share Sizing Methods to the previous Trade Example.

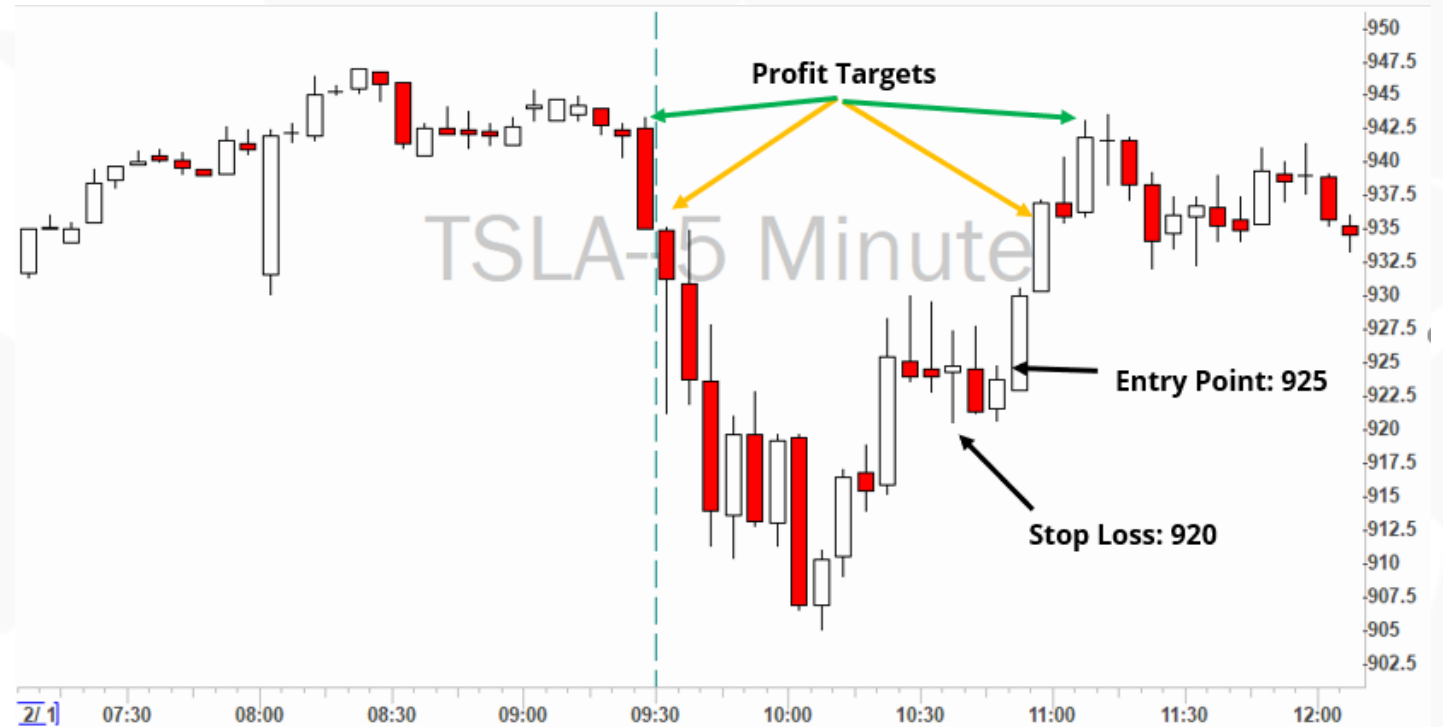
Account Size: 10,000 (40,000 Buying Power)

Stop Loss Range: 5.00

1% of Account: 100

R Value: 50

- Fixed Share Size
  - Max BP: 43 Shares
    - Stop Loss would risk over 1% of account
  - Depends on Trader Criteria
    - 10-20 Shares
- % of Account (1%)
  - 100 per Trade / 5.00 Stop Loss = 20 Shares
- Fixed Risk per Trade (R)
  - 50 per Trade / 5.00 Stop Loss = 10 Shares



# Share Sizing Table

	\$ 10	\$ 25	\$ 50	\$ 75	\$ 100	\$ 125	\$ 150	\$ 200	\$ 250	\$ 300	\$ 400	\$ 500	\$ 600	\$ 800	\$ 1000
<b>\$0.05</b>	200	500	1,000	1,500	2,000	2,500	3,000	4,000	5,000	6,000	8,000	10,000	12,000	16,000	20,000
<b>\$0.10</b>	100	250	500	750	1,000	1,250	1,500	2,000	2,500	3,000	4,000	5,000	6,000	8,000	10,000
<b>\$0.15</b>	67	167	333	500	667	833	1,000	1,333	1,667	2,000	2,667	3,333	4,000	5,333	6,667
<b>\$0.20</b>	50	125	250	375	500	625	750	1,000	1,250	1,500	2,000	2,500	3,000	4,000	5,000
<b>\$0.25</b>	40	100	200	300	400	500	600	800	1,000	1,200	1,600	2,000	2,400	3,200	4,000
<b>\$0.30</b>	33	83	167	250	333	417	500	667	833	1,000	1,333	1,667	2,000	2,667	3,333
<b>\$0.40</b>	25	63	125	188	250	313	375	500	625	750	1,000	1,250	1,500	2,000	2,500
<b>\$0.50</b>	20	50	100	150	200	250	300	400	500	600	800	1,000	1,200	1,600	2,000
<b>\$0.60</b>	17	42	83	125	167	208	250	333	417	500	667	833	1,000	1,333	1,667
<b>\$0.75</b>	13	33	67	100	133	167	200	267	333	400	533	667	800	1,067	1,333
<b>\$1.00</b>	10	25	50	75	100	125	150	200	250	300	400	500	600	800	1,000
<b>\$1.25</b>	8	20	40	60	80	100	120	160	200	240	320	400	480	640	800
<b>\$1.50</b>	7	17	33	50	67	83	100	133	167	200	267	333	400	533	667
<b>\$1.75</b>	6	14	29	43	57	71	86	114	143	171	229	286	343	457	571
<b>\$2.00</b>	5	13	25	38	50	63	75	100	125	150	200	250	300	400	500

# Stock Attributes

1.20



BAC	47.1 - 45.9	PCL 46.14	N
Last	46.85	0.71 (1.5%)	Vol 39,183,600
Lv1	46.85	46.86	Bid-Ask Spread: 0.01

Index	S&P 500	P/E	12.96	EPS (ttm)	3.56	Insider Own	0.11%	Shs Outstand	8.43B	Perf Week	3.57%
Market Cap	374.32B	Forward P/E	12.19	EPS next Y	3.79	Insider Trans	-2.31%	Shs Float	8.10B	Perf Month	3.62%
Income	30.56B	PEG	0.54	EPS next Q	0.79	Inst Own	72.90%	Short Float	0.93%	Perf Quarter	-3.43%
Sales	47.67B	P/S	7.85	EPS this Y	-32.00%	Inst Trans	0.17%	Short Ratio	1.50	Perf Half Y	21.55%
Book/sh	29.54	P/B	1.56	EPS next Y	16.21%	ROA	0.90%	Target Price	51.32	Perf Year	54.01%
Cash/sh	108.19	P/C	0.43	EPS next 5Y	23.89%	ROE	10.50%	52W Range	29.57 - 50.08	Perf YTD	3.71%
Dividend	0.84	P/FCF	-	EPS past 5Y	7.40%	ROI	7.30%	52W High	-6.27%	Beta	1.37
Dividend %	1.82%	Quick Ratio	-	Sales past 5Y	0.80%	Gross Margin	-	52W Low	58.74%	ATR	1.32
Employees	209000	Current Ratio	-	Sales Q/Q	7.40%	Oper. Margin	89.10%	RSI (14)	54.92	Volatility	3.17% 2.88%
Optionable	Yes	Debt/Eq	2.03	EPS Q/Q	69.00%	Profit Margin	54.90%	Rel Volume	0.76	Prev Close	46.14
Shortable	Yes	LT Debt/Eq	1.11	Earnings	Jan 19 BMO	Payout	23.90%	Avg Volume	50.51M	Price	46.94
Recom	2.40	SMA20	-0.03%	SMA50	2.84%	SMA200	9.43%	Volume	38,541,034	Change	1.73%

# Stock Attributes

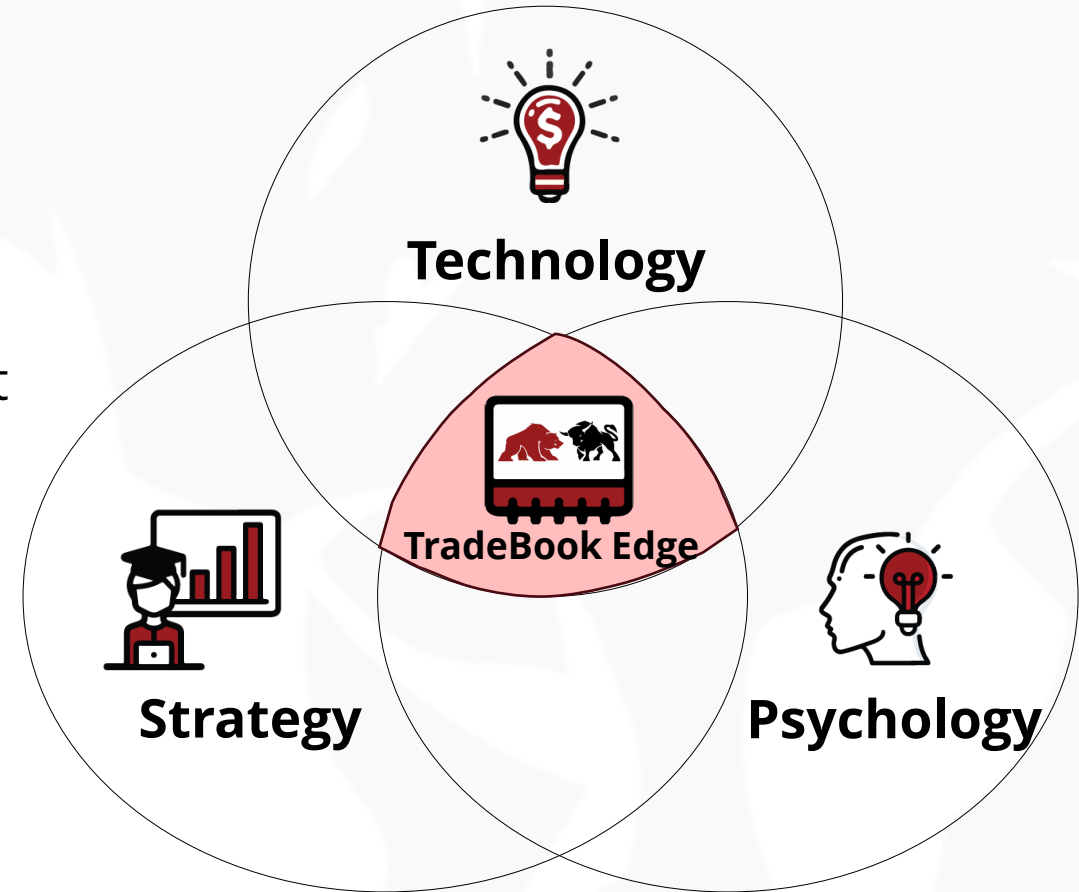


TSLA	↑	943.7 - 905	PCL 936.72	Q
Last	934.75	-1.97 (-0.21%)	Vol 24,213,099	↕
Lvl	933.61	934	Bid-Ask Spread: 0.39	S

Index	S&P 500	P/E	191.44	EPS (ttm)	4.89	Insider Own	0.10%	Shs Outstand	1.00B	Perf Week	0.72%
Market Cap	940.71B	Forward P/E	75.80	EPS next Y	12.36	Insider Trans	-94.14%	Shs Float	803.81M	Perf Month	-12.48%
Income	5.52B	PEG	8.82	EPS next Q	2.24	Inst Own	42.30%	Short Float	2.79%	Perf Quarter	-15.91%
Sales	53.82B	P/S	17.48	EPS this Y	165.00%	Inst Trans	-0.42%	Short Ratio	0.79	Perf Half Y	31.99%
Book/sh	27.11	P/B	34.55	EPS next Y	22.32%	ROA	3.90%	Target Price	942.20	Perf Year	11.54%
Cash/sh	16.03	P/C	58.45	EPS next 5Y	21.70%	ROE	8.90%	52W Range	539.49 - 1243.49	Perf YTD	-11.36%
Dividend	-	P/FCF	103.00	EPS past 5Y	19.70%	ROI	4.60%	52W High	-25.11%	Beta	2.04
Dividend %	-	Quick Ratio	1.10	Sales past 5Y	50.80%	Gross Margin	25.30%	52W Low	72.62%	ATR	69.14
Employees	70757	Current Ratio	1.40	Sales Q/Q	56.80%	Oper. Margin	6.10%	RSI (14)	44.42	Volatility	8.85% 6.80%
Optionable	Yes	Debt/Eq	0.30	EPS Q/Q	430.70%	Profit Margin	4.00%	Rel Volume	0.85	Prev Close	936.72
Shortable	Yes	LT Debt/Eq	0.24	Earnings	Jan 26 AMC	Payout	0.00%	Avg Volume	28.55M	Price	931.25
Recom	2.60	SMA20	-7.81%	SMA50	-9.76%	SMA200	14.22%	Volume	24,156,625	Change	-0.58%

# Trade Risk Plan Overview

- I will risk \$ \_\_\_ or \_\_\_% of my account per trade
  - \$50
  - \$20
- I am allowed to scale up my size after \_\_\_
  - After 2 weeks straight of green days
  - After two weeks of consistency following my Plan
- My daily profit target is \$ \_\_\_ or \_\_\_% of my account
  - \$25
  - \$50
- My daily max loss is \$ \_\_\_ or \_\_\_% of my account
  - \$50
  - \$60
- I am allowed to take a max of \_\_\_ trades per day
  - 3
  - 3



# Mechanical Risk Management

- Mechanical Issues
  - Internet Connection
  - Platform and Data Issues
  - Power Outage
  - Mother Nature
- Tools & equipment you have for an emergency
  - Generator
  - Backup Computer and Peripherals
  - Phone
  - **Platform Risk Controls**

The screenshot shows a window titled "Account 223712 TRTESTREP2" with various risk management settings. The settings are organized into several sections:

- Max Loss:** 0.00. When NET PL (Realized + Commissions) reaches this value.
- Warning Loss:** 0.00. When realized+unrealized reached, Warning Trader.
- Total Loss:** 0.00. Max realized+unrealized Loss, if reached, no new order.
- Curr EQ Lmt:** 0.00. Current Equity Limit, if reached, no new order.
- RemEQ(%):** 0. Remain EQ(%) Limit, if reached, no new order.
- Position Total Loss:** 0.00. Max realized+unrealized Loss per position, if reached, no new order.
- Position Unreal Loss:** 0.00. Max unrealized Loss per position, if reached, no new order.
- Pos Mkt Val Loss(%):** 0.00. Max Real+unreal Loss per position (% of initial market value), if reached, no new order.
- Pos Mkt Px deviate(%):** 0.00. Position market price loss deviate from avgcost(%) if reached, no new order.
- Pos Loss Warning:** 0.00. Unrealized Loss per position, if reached, Warning trader.
- Pos Loss Warning:** 0.00. Real+Unreal Loss per position, if reached, Warning trader.
- Pos Loss Warning(%):** 0.00. Real+Unreal Loss per position (% of initial market value), if reached, Warning trader.

Additional settings include:

- Count in Commission for Total Loss/Warning Loss/Curr EQ Lmt
- Enable Auto Stop
- Downcount:** 0. Auto Stop downcount (sec) when total/NET PL reached Total/Max Loss.
- Max Share:** 0. Max auto stop execution share per day.
- Max Auto Stop Order Size:** 0. Delay for next order if exceed max order size (sec): 0.

Stop Gain settings:

- Stop Gain. Account Net Realized PL Thresh: 0.00. Drawdown Percent of Max Net PL: 0.00.
- Account Total PL Thresh: 0.00. Drawdown Percent of Total PL: 0.00.
- Pos Stop Gain Thresh:** 0.00. Drawdown: 0.00. Close position when unrealized PL < drawdown value from max unrealized value.
- Pos Stop Gain Thresh(%):** 0.00. Drawdown: 0.00. Close position when unrealized PL < drawdown value from initial market value (%).

An "Update" button is located at the bottom right of the window.

# Physical Risk

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Corresponds to physical impairment due to activities within the Trader's control.

- Sleep Deprivation
  - Hunger/Dehydration
  - Air Flow Conditions
  - Hangover from Controlled Substances
- 
- Having a Risk Management Plan in place when your physical condition is at risk for trading can prevent poor performance and additional stress when unnecessary.

# Platform Risk Controls

Most Trading Platforms have ways to enter Loss Thresholds that can act as a Safety Net for unexpected events.

Mitigates various types of risk

- Mechanical Risk
- Psychological Risk
- Uncategorized Risk

Traders can blow up accounts in as little as a single trade without these in place.

The screenshot shows a window titled "Account 223712 TRTESTREP2" with various risk control settings. The settings are organized into several sections:

- MaxLoss:** 0.00. Description: When NET PL (Realized + Commissions) reaches this value.
- Warning Loss:** 0.00. Description: When realized+unrealized reached, Warning Trader.
- Total Loss:** 0.00. Description: Max realized+unrealized Loss, if reached, no new
- Curr EQ Lmt:** 0.00. Description: Current Equity Limit, if reached, no new order.
- RemEQ(%):** 0. Description: Remain EQ(%) Limit, if reached, no new order.
- Position Total Loss:** 0.00. Description: Max realized+unrealized Loss per position, if reached, no new
- Position Unreal Loss:** 0.00. Description: Max unrealized Loss per position, if reached, no new
- Pos Mkt Val Loss(%):** 0.00. Description: Max Real+unreal Loss per position (% of initial market value), if reached, no new order.
- Pos Mkt Px deviate(%):** 0.00. Description: Position market price loss deviate from avgcost(%) if reached, no new order.
- Pos Loss Warning:** 0.00. Description: Unrealized Loss per position, if reached, Warning trader.
- Pos Loss Warning:** 0.00. Description: Real+Unreal Loss per position, if reached, Warning trader.
- Pos Loss Warning(%):** 0.00. Description: Real+Unreal Loss per position (% of initial market value), if reached, Warning trader.

Additional options include:

- Count in Commission for Total Loss/Warning Loss/Curr EQ Lmt
- Enable Auto Stop
- Downcount:** 0. Description: Auto Stop downcount (sec) when total/NET PL reached Total/Max Loss.
- Max Share:** 0. Description: Max auto stop execution share per day.
- Max Auto Stop Order Size:** 0. Description: Delay for next order if exceed max order size (sec): 0

Drawdown settings:

- Stop Gain. Account Net Realized PL Thresh: 0.00. Drawdown Percent of Max Net PL: 0.00
- Account Total PL Thresh: 0.00. Drawdown Percent of Total PL: 0.00
- Pos Stop Gain Thresh:** 0.00. Drawdown: 0.00. Description: Close position when unrealized PL < drawdown value from max unrealized value
- Pos Stop Gain Thresh(%):** 0.00. Drawdown: 0.00. Description: Close position when unrealized PL < drawdown value from initial market value (%)

An "Update" button is located at the bottom right of the window.

# Risk Management Example

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- Threat: Power Outage during Live Trading
- Risk Identification:
  - Type of Risk: Mechanical
  - Core Risk?: No
- Risk Measurement:
  - Frequency: Rarely (<1/month)
  - Exposure: Low (Other Risk Mitigation will Trigger)
- Risk Mitigation:
  - Generator to restore power
  - Mobile Platform to manage active trades
  - Time Spent waiting for Power Restoration
- Risk Reporting:
  - Journal event as a note in Trading Journal
  - Ensure Threat Frequency isn't concentrated

# Risk Management Example

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- Threat: Lack of Strategy Trading Reversals
- Risk Identification:
  - Type of Risk: Trader – Strategy
  - Core Risk?: Yes
- Risk Measurement:
  - Frequency: Daily
  - Exposure: Depends on Trader Discretion
- Risk Mitigation:
  - SIM Trading for Practice and Development of Trade Book Criteria for Strategy
  - Live Trading using Smaller Risk per Trade
  - Lower % of Total Trades until Performance Objectives are Met
- Risk Reporting:
  - Journaling Performance for trades
  - Reviewing Trades actively to adjust expectations

# Resources

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Bear Bull Trader Education Center: <https://bearbulltraders.com/education-center/>

- Risk Management Webinars
- DAS Risk Controls
- DAS Hotkeys

Bear Bull Traders Downloads: <https://bearbulltraders.com/course/downloads/>

- Technology Documents
- Strategy Documents
- Psychology Documents





# Useful icons



# TradeBook



# Trilogy of Trading Success

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**Technology**

Mondays



**Strategy**

Tuesdays



**Psychology**

Wednesdays



**Mentorship**

Thursdays

# Edge of Your Trading

