

Essential Risk Management For Long Term Success



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Definition

Risk is the possibility of something bad happening

Risk involves **uncertainty** about the effects/implications of an activity, often focusing on negative, undesirable consequences

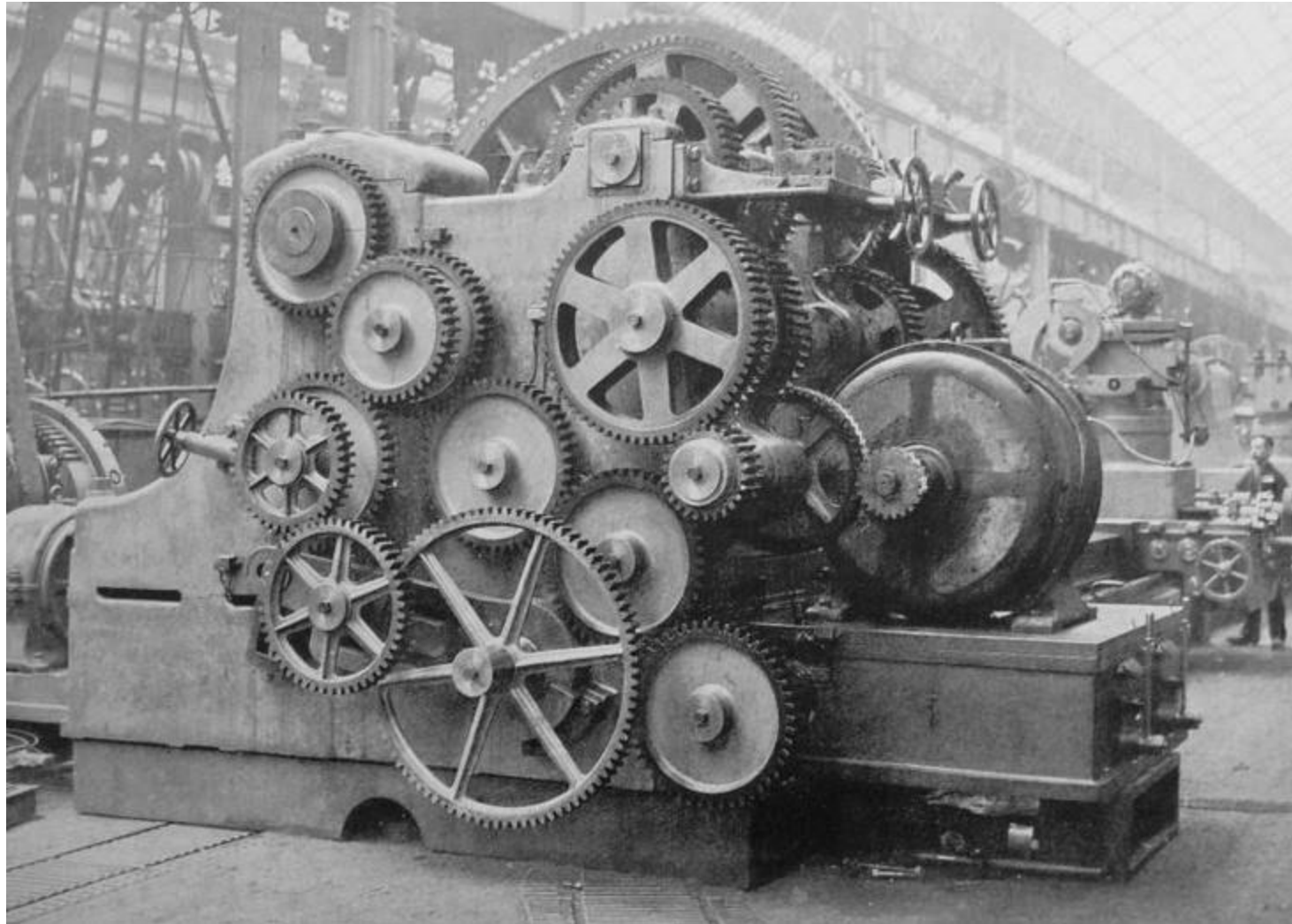
Risk Lesson #1

Know how you get paid

How Do You Get Paid In Trading??



How Do You Get Paid In Trading??



How You Get Paid

Effectively managing risk

How You Get Paid



How You Get Paid

Markets

- What the stock will do
- What market/world events will occur (after you enter a trade)

Tactics

- Effectiveness of your strategy(ies)
- How much you are risking per trade
- How robust are your tools and processes

Execution

- How often you deviate from your strategy(ies)
- How often you do not adhere to your stop loss (+ve or -ve)
- How you manage the trade (i.e. partials, adding, exiting)

ACCEPT

REDUCE

AVOID

Risk Lesson #2

**Think like an owner,
not an employee**

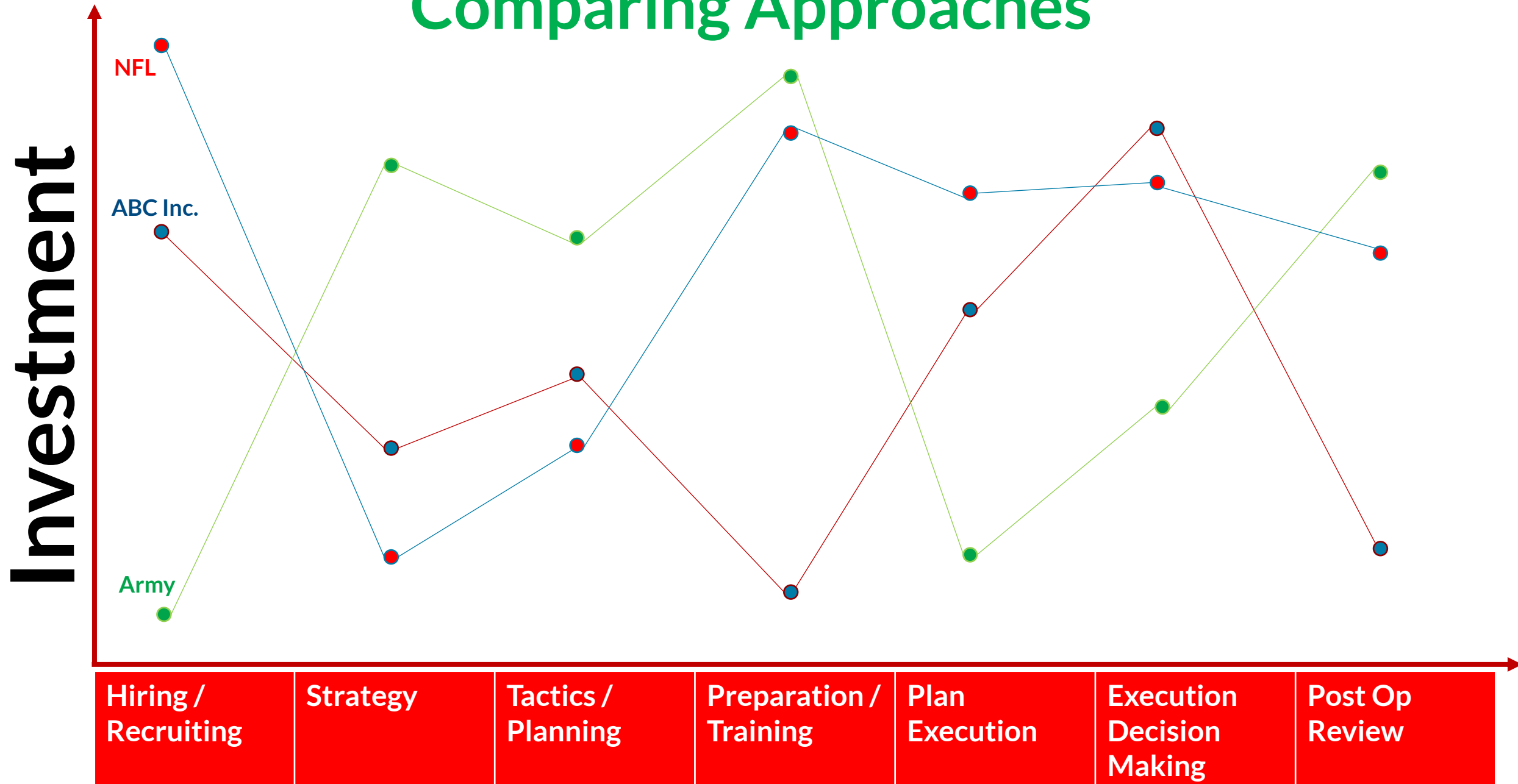
3 Scenarios



Comparing Approaches

Hiring / Recruiting	Strategy	Tactics / Planning	Preparation / Training	Plan Execution	Execution Decision Making	Post Op Review
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Comparing Approaches



The Trading Approach



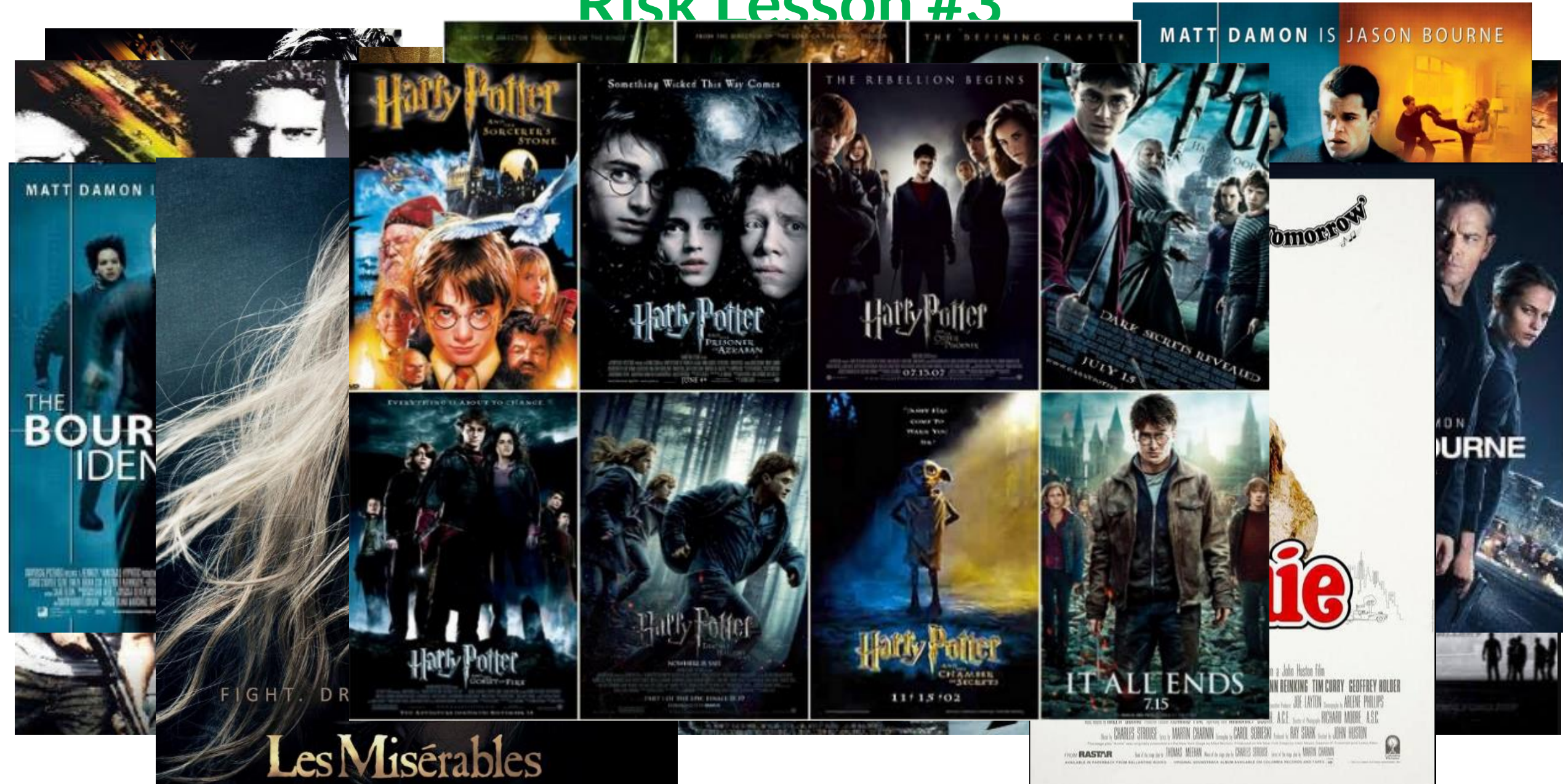
The Trading Approach



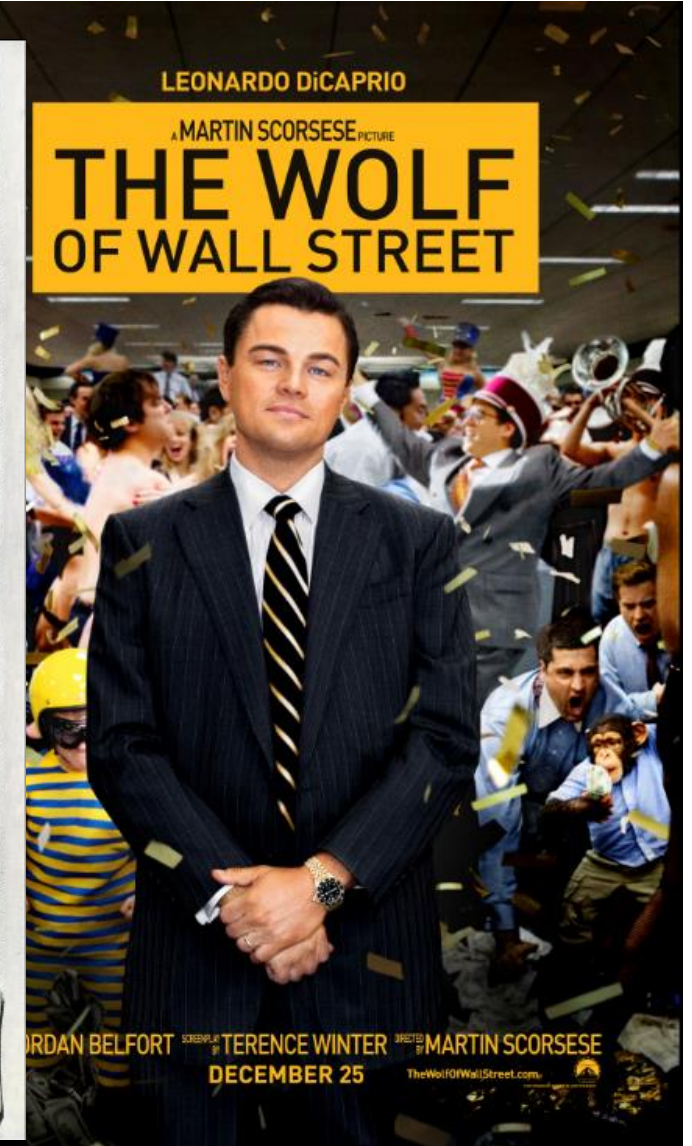
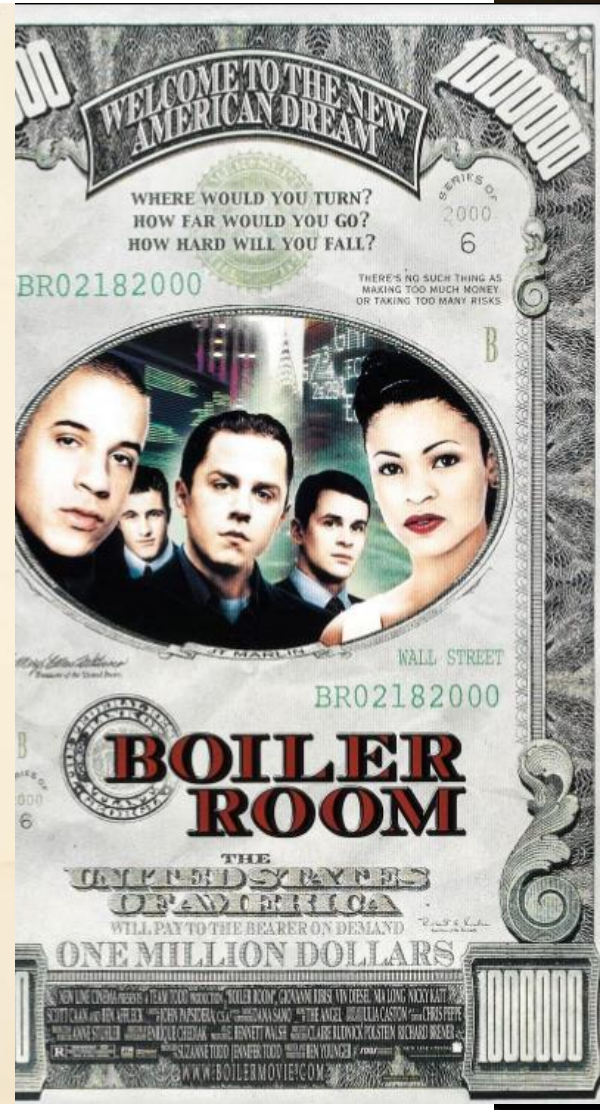
Risk Lesson #3

**Act like a leader
and not a (rogue) agent**

Risk Lesson #3



Risk Lesson #3



Risk Lesson #2



Risk Lesson #3

In real life, rogue agents die, destroy their lives and/or end up in prison

**Be the one they want to take down!!
(i.e. the stable, boring leader)**

Risk Lesson #4

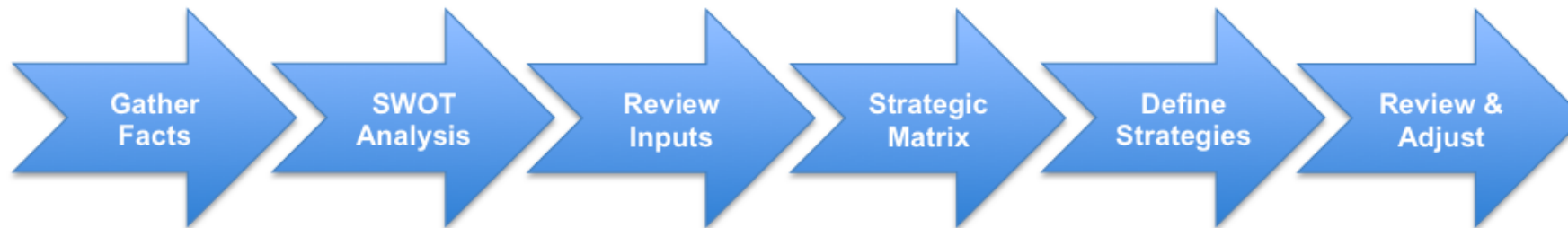
**Create a plan and execute it
flawlessly**

3 Scenarios



Business Planning

Strategic Plan Process



Gather Inputs

- From all Stakeholders
- Customer analysis
- Competitor analysis
- Industry analysis
- Environmental
- Company performance
- Company strategies

SWOT Analysis

- External Analysis
 - Opportunities
 - Threats
- Internal Analysis
 - Strengths
 - Weaknesses
- Strategic Questions
- Strategic Issues

Review Inputs

- All Stakeholders
- Review Inputs
- Review SWOT Analysis
- Define 3-4 key statements

Strategic Matrix

- All Stakeholders
- Define Strategies to address SWOT combinations:
 - Opportunities vs Strengths
 - Opportunities vs Weaknesses
 - Threats vs Strengths
 - Threats vs Weaknesses

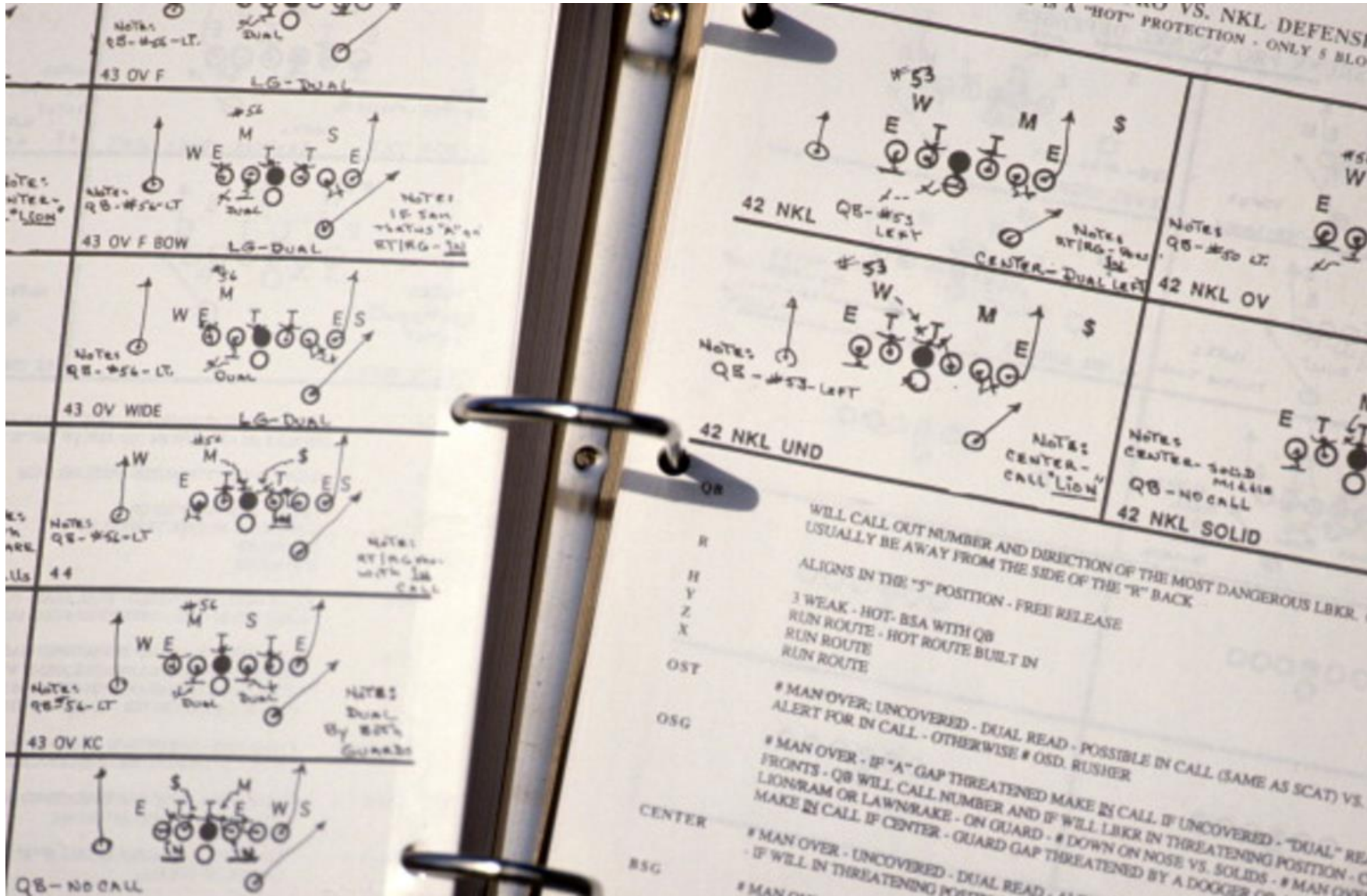
Define Strategies

- Objectives
- Key Strategies
- Short and Long Term Goals
- Operational Plans

Final Reviews

- All Stakeholders
- Review Strategies
- Review Goals
- Review Plans
- Adjust as necessary

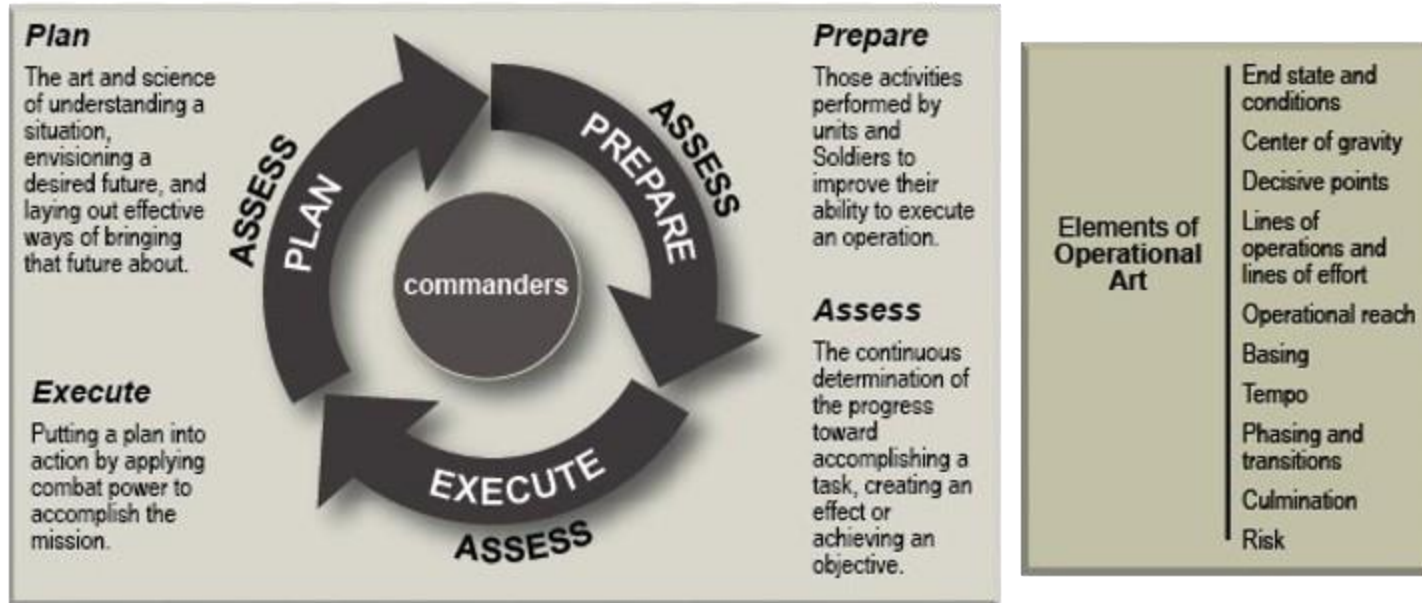
NFL Playbook



US Army Operations Process

The Operations Process

The Army's framework for exercising mission command is the operations process – the major mission command activities performed during operations: Planning, preparing, executing, and continuously assessing the operation.



Central idea . . .

Commanders, supported by their staffs use the operations process to drive the conceptual and detailed planning necessary to understand, visualize, and describe their operational environment; make and articulate decisions; and direct, lead, and assess military operations.

guided by . . .

Principles

- Commanders drive the operations process
- Apply critical and creative thinking
- Build and maintain situational understanding
- Encourage collaboration and dialogue

Strategic Trading Plan

Trading Plan – Mountain Pass (Double Top/Bottom reversal)

This is a Trend Reversal Pattern that can occur at the end of a low of the day.

The key characteristics of the Mountain Pass are:

1. Is the end existing
2. Sets a new high/low
3. Fails to set a 2nd new high/low
4. Pulls in, then crosses
5. Hopefully goes to the next level

This pattern is best played on the 1, 2, 5, 15, 30, 60, 120, 240, 480, 960, 1920, 3840, 7680, 15360, 30720, 61440, 122880, 245760, 491520, 983040, 1966080, 3932160, 7864320, 15728640, 31457280, 62914560, 125829120, 251658240, 503316480, 1006632960, 2013265920, 4026531840, 8053063680, 16106127360, 32212254720, 64424509440, 128849018880, 257698037760, 515396075520, 1030792151040, 2061584302080, 4123168604160, 8246337208320, 16492674416640, 32985348833280, 65970697666560, 131941395333120, 263882790666240, 527765581332480, 1055531162664960, 2111062325329920, 4222124650659840, 8444249301319680, 16888498602639360, 33776997205278720, 67553994410557440, 135107988821114880, 270215977642229760, 540431955284459520, 1080863910568919040, 2161727821137838080, 4323455642275676160, 8646911284551352320, 17293822569102704640, 34587645138205409280, 69175290276410818560, 138350580552821637120, 276701161105643274240, 553402322211286548480, 1106804644422573096960, 2213609288845146193920, 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Business Planning



Strategic Trading Plan

TRADER'S BUSINESS PLAN



Mission Structure

VISION

Drafting a business's vision statement is an important step in the creation of a business plan. It is one part the owner's dream for the business and another part the path the owner is laying for their business in the future. The vision statement is generally written with long-term perspective in mind. The statement should be well-written and compacted into one or two descriptive and passionate sentences about your desires for pursuing trading as a career.

MISSION STATEMENT

A mission statement is a key tool that can be as important as your business plan. It captures the essence of your trading goals and the philosophies which support them. Equally important, your mission statement signals what your business is all about to yourself. Answering these questions will help you create a verbal picture of your business plan:

Who is going to be your support network?
What are your long-term goals?

When are you available to trade?
Who are you going to learn from?

Why do you want to day trade?
What capital is available to you?

TIMELINE

A timeline should be used to manage the progression from your initial decision to start trading, to your trading education and simulator training program, to entering your real goal of live trading. This timeline is essential to tracking the various tasks that need to be completed in each step of your journey. It is continuously updated as progress is made to ensure your trading business does not become stagnant. It is also beneficial to evaluate progress and keep the focus on how much has been accomplished.

SWOT ANALYSIS

STRENGTHS	WEAKNESSES
What are you the best at? What skills do you have that others don't? What do others say is your strength?	What could you improve? Where do you have fewer resources than others? What are others likely to use to outperform you?
OPPORTUNITIES	THREATS
What opportunities are open to you? What trends could you take advantage of? How can you use your strengths to gain an advantage?	What trends could harm you? What is your competition doing? What trends do you anticipate in the market you are in?

Resources

TOOLS & SERVICES

- High-speed Internet Service**
You need a reliable internet provider that offers high-speed internet.
- Broker**
You need a high-quality discount broker. Your broker is your vehicle to trade.
- Trading Platform**
Fast trade execution is the key for day traders to be successful. You need to be able to move in and out of trades quickly.
- Screeners**
Thousands of stocks are moving in the market every single day, but finding a setup that is both consistent and a good fit is really hard. Trade ideas to screen for scanning the market is a great tool for finding the best trades.
- Community of Traders**
Trading alone is very difficult and can be emotionally overwhelming. To follow with you ask your questions? Online communities are excellent places for meeting like-minded traders. They can be powerful learning tools.

JOURNAL

A trading journal is a tool to keep track of all of the trades you have made. A few of the benefits of a trading journal are that it allows you the ability to monitor your progress, to analyze which strategies are working, and to assess if determining what areas you need to improve in. The trading journal can be as detailed as you would like, but at a minimum a trading journal should include the following information for each trade:

Stock
Entry, stop loss, profit target
Time of the trade
Date

What you did well
What you did not do well
What you can improve on
A psychology review

Planning

MONEY AND RISK MANAGEMENT

I will risk \$____ or ____% of my account per trade.
I am allowed to scale up my size after being consistent.
My daily profit target is \$____ or ____% of my account.
My daily max loss is \$____ or ____% of my account.
I have platform risk controls enabled: ☐ Y ☐ N
I am allowed to take a max of ____ trades per day.
My break-even win accuracy is ____%.
I stop trading or wind down when the clock reads ____.

STRATEGIES AND PATTERNS

I don't trade the first ____ minutes after the Open.
I trade stocks with at least ____ million share float.
I prefer to trade stocks with a price range of:
\$ ____ (min) \$ ____ (max)

TRADE MANAGEMENT

I take ____% off my position on each partial while exiting.
I move my stop to break-even after taking partials. ☐ Y ☐ N
I seek a realized return of ____ times the amount I risk.
(Average-risk ratio)
My stop losses are ☐ Manual ☐ Hard
My mean setups are _____
See TradeBook for more info.

ACTION PLAN

The action plan explains how you will operate and manage your trading business. It addresses the back office activities that do not relate directly to your trading plan. Some of these activities include:

- Setting up your trading station
- Deciding on a community
- Developing an educational plan
- Obtaining a tax planner
- Choosing a broker, platform, and internet provider
- Establishing accountability relationships
- Developing a routine
- Analyzing statistics from your trading
- Developing your own TradeBook

EDUCATIONAL PLAN

Creating an educational plan gives you a visual picture of what you will need to accomplish over a period of time and provides you with an idea of how long it will take to meet your trading goals. It is important to know what is required as you progress through the learning curve. Having a well thought-out plan allows you to manage expectations throughout your journey.

Sample Educational Plan:

- Months 0 - 2**
Learn (Read, Watch, Hear)
- Months 3 - 5**
Plan (Create Goals, Timeline, Journal, Trading Plan, Build discipline)
- Months 6 - 8**
Practice (Develop a Routine, Trade Sim, Review strategies, Develop Plan, Journal, Start Demo)
- Months 9 - 11**
Play (Trade Sim, Trade Live, Improve Practice, Strategies, Trading Plan, Journal, Run Demo)
- Months 12 - 1**
Perform (Trade Live, Improve Routine, Strategies, Trading Plan, Journal, Run Demo)

Objectives

GOALS

Setting daily, weekly, monthly, quarterly, and yearly goals (and making progress on them) assists in maintaining a positive emotional attitude toward the ups and downs of learning to day trade. Ensure you have SMART goals:

- Specific**
Each goal is direct, detailed, and meaningful.
- Measurable**
Each goal is quantifiable to track progress or success.
- Attainable**
Each goal is realistic. You have the tools and/or resources to attain it.
- Relevant**
Each goal aligns with your business plan.
- Time-based**
Each goal has a deadline.

TRADING RULES

Rules are developed outside of market hours when we have a clear head and are not under pressure or distress. These rules are made to safeguard us when our mind is clouded and our emotions are at their peak. Rules are our friends who will protect us from ourselves.

- Day trading is not a strategy to get rich quickly.
- Day trading is not time. It is a serious business, and you should treat it as such.
- Day traders do not hold positions overnight. If necessary, you must sell with a loss to make sure you do not hold on to any stock overnight.
- Always ask, "Is this stock moving because the overall market is moving, or is it moving because it has a unique fundamental catalyst?"
- Success in day trading comes from risk management. Trading low-risk entries with a high potential reward. The average risk/reward ratio should be 2:1.
- Your losses will keep you out of the market for a long time. Your only job as a day trader is to manage risk. You cannot be a successful day trader without excellent risk management skills, even if you are the master of many effective strategies.
- Never trade only stocks in Play. High relative volume stocks that have fundamental catalysts and are being traded regardless of the overall market.
- Experienced traders are like quail in the woods. They jump out at just the right time, take their profit, and get out.
- Follow confidence, where the crowd is greater than the open, indicate trading momentum. Follow confidence, where the crowd is less, than the open, indicate selling pressure.
- Indicators only indicate, they should not be allowed to dictate.
- Profitable trading does not involve emotion. If you are an emotional trader, you will lose your money.

 TRADING TERMINAL.COM

www.BearBullTraders.com

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Risk Lesson #4

strategic business

**Create a plan and execute it
flawlessly**



Risk Lesson #5

**Accept risk within your plan, but
focus it where YOU choose**

Accepting and Taking Risk

“Life is all about taking risks. If you never take a risk, you will never achieve your dreams.”

-Anonymous

“He who is not courageous enough to take risks will accomplish nothing in life.”

-Muhammad Ali

“Take the risk or lose the chance”

-Anonymous

“There can be no great accomplishment without risk.”

-Neil Armstrong

“The biggest risk is not taking any risk. In a world that is changing really quickly, the only strategy that is guaranteed to fail is not taking risks.”

-Mark Zuckerberg

Accepting and Taking Risk



Accepting and Taking Risk



Focus Your Risk Decisions



Risk Lesson #6

Any risk within your plan is good risk.

Any other risk is bad risk

Planned Risk

Financial Risk

Daily maximum loss

Daily risk-per-trade

Psychological Risk

Loss of confidence

Failure to execute

Planned Risk

What risks can you identify?

Execution mistakes

Impulsive decisions

Self doubt

Changing TradeBook (while executing)

Lack of prep

No strategy

Not trusting yourself

Lack of patience

Over confidence

Planned Risk

Create a plan that addresses
ALL
the risk elements that matter to *you*
and allows you to execute on your
overall trading plan(s).

Calculating Your Risk

Most investment banks and proprietary trading firms use highly complex measurements for performance and risk

- The Sharpe ratio
- The Sortino ratio
- The Adjusted Sortino ratio
- Gain to Pain (GPR) ratio
- Value at Risk (VAR)

Calculating Your Risk



Calculating Your Risk

**For retail traders, only 2 measures
matter:**

**Daily Maximum Loss
&
Profitability**

Calculating Your Risk

Daily Maximum Loss

$$= 1 / \text{Win Rate\%} * (\text{Risk per Trade})$$

e.g.

$$= 1 / 25\% * \$100$$

$$= \$400$$

e.g.

$$= 1 / 75\% * \$100$$

$$= \$133 \dots \text{or } \$200$$

Note: Consider your desired daily trading volume and your emotional handling of losses before finalizing.

Calculating Your Risk – Profitability Calc

		Win Rate										
Payoff Ratio		25%	30%	35%	40%	45%	50%	55%	60%	65%	70%	75%
	1	-50%	-40%	-30%	-20%	-10%	0%	10%	20%	30%	40%	50%
	1.2	-45%	-34%	-23%	-12%	-1%	10%	21%	32%	43%	54%	65%
	1.4	-40%	-28%	-16%	-4%	8%	20%	32%	44%	56%	68%	80%
	1.6	-35%	-22%	-9%	4%	17%	30%	43%	56%	69%	82%	95%
	1.8	-30%	-16%	-2%	12%	26%	40%	54%	68%	82%	96%	110%
	2	-25%	-10%	5%	20%	35%	50%	65%	80%	95%	110%	125%
	2.2	-20%	-4%	12%	28%	44%	60%	76%	92%	108%	124%	140%
	2.4	-15%	2%	19%	36%	53%	70%	87%	104%	121%	138%	155%
	2.6	-10%	8%	26%	44%	62%	80%	98%	116%	134%	152%	170%
	2.8	-5%	14%	33%	52%	71%	90%	109%	128%	147%	166%	185%
	3	0%	20%	40%	60%	80%	100%	120%	140%	160%	180%	200%

$$\text{Payoff Ratio} = \frac{\text{Average Winner}}{\text{Average Loser}}$$

Calculating Your Risk – Profitability Calc

Win Rate

Payoff Ratio

	10%	15%	20%	25%	30%	35%	40%	45%	50%	55%	60%	65%	70%	75%	80%	85%	90%	95%
1	-80%	-70%	-60%	-50%	-40%	-30%	-20%	-10%	0%	10%	20%	30%	40%	50%	60%	70%	80%	90%
1.2	-78%	-67%	-56%	-45%	-34%	-23%	-12%	-1%	10%	21%	32%	43%	54%	65%	76%	87%	98%	109%
1.4	-76%	-64%	-52%	-40%	-28%	-16%	-4%	8%	20%	32%	44%	56%	68%	80%	92%	104%	116%	128%
1.6	-74%	-61%	-48%	-35%	-22%	-9%	4%	17%	30%	43%	56%	69%	82%	95%	108%	121%	134%	147%
1.8	-72%	-58%	-44%	-30%	-16%	-2%	12%	26%	40%	54%	68%	82%	96%	110%	124%	138%	152%	166%
2	-70%	-55%	-40%	-25%	-10%	5%	20%	35%	50%	65%	80%	95%	110%	125%	140%	155%	170%	185%
2.2	-68%	-52%	-36%	-20%	-4%	12%	28%	44%	60%	76%	92%	108%	124%	140%	156%	172%	188%	204%
2.4	-66%	-49%	-32%	-15%	2%	19%	36%	53%	70%	87%	104%	121%	138%	155%	172%	189%	206%	223%
2.6	-64%	-46%	-28%	-10%	8%	26%	44%	62%	80%	98%	116%	134%	152%	170%	188%	206%	224%	242%
2.8	-62%	-43%	-24%	-5%	14%	33%	52%	71%	90%	109%	128%	147%	166%	185%	204%	223%	242%	261%
3	-60%	-40%	-20%	0%	20%	40%	60%	80%	100%	120%	140%	160%	180%	200%	220%	240%	260%	280%
3.2	-58%	-37%	-16%	5%	26%	47%	68%	89%	110%	131%	152%	173%	194%	215%	236%	257%	278%	299%
3.4	-56%	-34%	-12%	10%	32%	54%	76%	98%	120%	142%	164%	186%	208%	230%	252%	274%	296%	318%
3.6	-54%	-31%	-8%	15%	38%	61%	84%	107%	130%	153%	176%	199%	222%	245%	268%	291%	314%	337%
3.8	-52%	-28%	-4%	20%	44%	68%	92%	116%	140%	164%	188%	212%	236%	260%	284%	308%	332%	356%
4	-50%	-25%	0%	25%	50%	75%	100%	125%	150%	175%	200%	225%	250%	275%	300%	325%	350%	375%
4.2	-48%	-22%	4%	30%	56%	82%	108%	134%	160%	186%	212%	238%	264%	290%	316%	342%	368%	394%
4.4	-46%	-19%	8%	35%	62%	89%	116%	143%	170%	197%	224%	251%	278%	305%	332%	359%	386%	413%
4.6	-44%	-16%	12%	40%	68%	96%	124%	152%	180%	208%	236%	264%	292%	320%	348%	376%	404%	432%
4.8	-42%	-13%	16%	45%	74%	103%	132%	161%	190%	219%	248%	277%	306%	335%	364%	393%	422%	451%
5	-40%	-10%	20%	50%	80%	110%	140%	170%	200%	230%	260%	290%	320%	350%	380%	410%	440%	470%
5.2	-38%	-7%	24%	55%	86%	117%	148%	179%	210%	241%	272%	303%	334%	365%	396%	427%	458%	489%
5.4	-36%	-4%	28%	60%	92%	124%	156%	188%	220%	252%	284%	316%	348%	380%	412%	444%	476%	508%
5.6	-34%	-1%	32%	65%	98%	131%	164%	197%	230%	263%	296%	329%	362%	395%	428%	461%	494%	527%
5.8	-32%	2%	36%	70%	104%	138%	172%	206%	240%	274%	308%	342%	376%	410%	444%	478%	512%	546%
6	-30%	5%	40%	75%	110%	145%	180%	215%	250%	285%	320%	355%	390%	425%	460%	495%	530%	565%

Calculating Your Risk

Risk Management Cycle

1. Calculate (or estimate) your Profitability
2. Calculate (or invent) your Daily Max Loss
3. Trade for 1 month
4. (Re)calculate your Profitability
5. Review all plans and decide what to change!
6. Repeat

Calculating Your Risk – Profitability Calc

		Win Rate										
Payoff Ratio		25%	30%	35%	40%	45%	50%	55%	60%	65%	70%	75%
	1	-50%	-40%	-30%	-20%	-10%	0%	10%	20%	30%	40%	50%
	1.2	-45%	-34%	-23%	-12%	-1%	10%	21%	32%	43%	54%	65%
	1.4	-40%	-28%	-16%	-4%	8%	20%	32%	44%	56%	68%	80%
	1.6	-35%	-22%	-9%	4%	17%	30%	43%	56%	69%	82%	95%
	1.8	-30%	-16%	-2%	12%	26%	40%	54%	68%	82%	96%	110%
	2	-25%	-10%	5%	20%	35%	50%	65%	80%	95%	110%	125%
	2.2	-20%	-4%	12%	28%	44%	60%	76%	92%	108%	124%	140%
	2.4	-15%	2%	19%	36%	53%	70%	87%	104%	121%	138%	155%
	2.6	-10%	8%	26%	44%	62%	80%	98%	116%	134%	152%	170%
	2.8	-5%	14%	33%	52%	71%	90%	109%	128%	147%	166%	185%
	3	0%	20%	40%	60%	80%	100%	120%	140%	160%	180%	200%

$$\text{Payoff Ratio} = \frac{\text{Average Winner}}{\text{Average Loser}}$$

Calculating Your Risk

Where to look for opportunities:

- Adherence to (Tradebook) rules
- Mental preparedness
- Average winner
- Win Rate
- Partialling approach
- Stock selection
- Trade timing (time of day and duration)

Risk Lesson #7

**It's all on you.
DO NOT blame anyone, or
anything else**

Seven Risk Lessons

1. Know how you get paid
2. Think like an owner
3. Act like a leader
4. Create a plan and execute it
5. Purposely focus your risk
6. Planned risk is good
7. It's all on you