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33rd Year as a FX Professional

Important Trading Traits

Forex trading is a highly competitive undertaking and some of the key factors which separate the successful traders from the unsuccessful ones are as follows:

Discipline and Patience

Successful traders know through bitter experience over many years that without a strong trading discipline, their trading capital will not be preserved and their chances of trading profitability are much diminished. They know where to set their stop losses and not to change these based on anything other than objective analysis. Successful traders also know the virtue of patience and the importance of being selective about which trades they execute and to let profitable trades run their course. Unsuccessful traders on the other hand are typically less disciplined and more impatient in their trading. They succumb to human emotions, second-guessing their analysis and/or professional advice and are less stringent in their trading/risk management.

Risk/Money Management

Successful traders know that preserving trading capital is imperative to their trading existence and therefore are strongly protective of this. They know that any one loss or series of losses is all part of the trading game and that for long term trading success they must ration their trading capital appropriately, only risking a small percentage of their capital on any one trade. In contrast, unsuccessful traders do not show the same respect for their trading capital and are prone to incur losses which materially erode (or even eradicate) their trading capital unnecessarily.

Adequate Capitalisation

Successful traders treat trading as a serious undertaking and like any business, it needs to be adequately funded. Embarking upon any venture without sufficient funds is a recipe for failure and being under capitalised places the trader at a serious disadvantage at the very start. Unsuccessful traders fail to understand this and are too often "blown out" due to inadequate funding.

Operating as a Business

Successful traders treat their trading as a business and consequently follow a professional approach. After all, imagine a business with no rules, procedures and systems which operates solely on an ad hoc basis. The chances for success would not be high. This is contrasted by the approach of many unsuccessful traders who crave the excitement and thrill of forex; trading haphazardly and with inadequate risk/money management.

Trading is a Long Game
Successful traders do not "throw in the towel" or become disconsolate when going through inevitable trading troughs. They understand that losses are an inevitable part of the trading experience and it is how they manage these rough patches which is the most important thing. It's important not to take trading losses personally. As long as you execute properly and have the appropriate stop loss, trading losses are just part of the normal trading process. Unsuccessful traders too often fail to see the "woods from the trees" and succumb to the pressures of trading troughs to their detriment.

Stop Loss Placement

Stop losses are essential in FX trading, as none of us knows what the markets will do next. We might think we know but that's not the same as actually knowing. Therefore, traders utilise stop losses as insurance against being wrong and trading losses (no matter who you are) are inevitable.

One of the challenges facing traders is exactly where to place their stop loss. There is no single "right answer" to this question but there are some useful guidelines.

Perhaps the most obvious, is to place a stop loss just under a prior support or just above a prior resistance. This satisfies the "test" of being technically objective and lends some degree of comfort to the trader, as if stopped out, there are likely to be plenty of others similarly affected. Unless the trader falls victim to the bank and hedge fund "big boys" deliberately running the stops, placement of a stop loss at these key levels is a good "rule of thumb" that your timing (at the very least) is wrong on this trade and with discretion being the part of valour, it is far better and more prudent to retire to the side-lines, until the dust has settled.

Another worthwhile stop loss placement is just under or just above a key mathematical (Fibonacci) retracement support or resistance, respectively. Such mathematical inflexion points often mark turning points in the direction of the market, in trading degrees ranging from intra-day, short term (24-28 hours) to medium and even long term.

Novice traders sometimes use stop losses based on an arbitrary number of trading pips (eg. A fixed 30 pip stop loss for intraday trading or 60 pip stop for short term trading purposes) for no technically objective reason. This is possibly done with the intention of losing only a certain amount of pips on each trade but other than that is entirely "random".

Whilst it is crucial to employ effective money management (and this means minimising losses and treating trading capital with the greatest of respect) if a stop loss has be placed higher or lower than otherwise desired (based upon an objective technical assessment of the market) then you should lower your trading position size, in order to keep any potential loss within acceptable boundaries. When it comes to stop loss placement, two important guidelines are:

1/ Ensure that there is a technically objective/justifiable stop loss level (as discussed above) and

2/ Ensure that each trade has a favourable risk:reward ratio. In other words, trades should be entered when the profit objective comfortably exceeds the loss potential (if your stop loss is triggered). This ensures that the average monetary amount of your winning trades exceeds the average amount of your losing trades.

Forex Trading is a Numbers Game

In forex trading, it certainly “feels” good being right a lot more than being wrong but the key is to try to ensure that your winning trades are maximised and that your losing trades are ruthlessly liquidated (well before they fester into a serious wound, as this can be highly detrimental to both your P+L as well as your trading psyche).

Traders can be right more than 50% of the time but if their risk management is ineffective, then they can still (and probably will) end up losing money. This is why trading is a numbers game. Sure, a trader can have a sound trading approach but without the discipline and application to employ effective money management, winning trades will be exceeded by losing trades running longer than they should and the trader will still flounder.

In my 30+ years as a full-time FX professional providing FX trading advice, I have come across many different traders the world-over and witnessed countless examples of traders who have been earnest and committed in their trading intent and sufficiently resourced yet still managed to lose money (in some cases, a lot of money) due to ineffective risk/money management.

It’s like the quintessential gambler who boasts about his winnings but stays quiet about his losses. One of the many old trading adages is to be vigilant about your losses because profits take care of themselves. In fact, profits should be maximised but the trader is always well advised to be extremely vigilant over losses and in particular (and this cannot be emphasised enough) in not letting losses run, as this is akin to “trading harikari”.

Anecdotally, I recall a particular instance of a seasoned trader (and subscriber of mine) who had been trading FX successfully and was grateful for the advice which I provided him with over the years. However, one day in 2008 an “accident” occurred. The facts are as follows: He entered a trading position but mistakenly committed to a significantly greater position size than intended (due to a “fat finger” episode). Instead of taking immediate remedial corrective action, he assumed this much larger position size on the basis (as he later recounted to me) of being “in for a penny, in for a pound”.

The market went against him but he maintained his losing position (longer than was appropriate) and then made (in my opinion) the cardinal error of leaving for a vacation whilst still holding a (large) losing trading position with no firm stop loss. By the time he settled into his overseas holiday destination and checked the market, a major trading break had occurred and a bad trading loss had turned into a financial disaster for him. A totally unnecessary “own goal".

Even with the best advice, long-term successful trading demands stringent risk/money management.

What's the appropriate Trading Leverage ?

One of the issues that confront all traders and which is perhaps especially significant for novice traders, is how much leverage to use when trading forex. Although there is no one "right answer" to this question, there are some important guidelines.

FX "promoters" (or in many instances, hucksters) boldly advocate a principal advantage of FX trading being that you can trade on up to 50:1 leverage and that this enables you to make a lot of money, very quickly. The promoter (a quick review of the internet shows that there are is no lack of them) emphasizes only one side of the ledger - the profit component.

Trading on 50:1 leverage (or anything even remotely like this) is akin to a school boy driving a formula one racing car, or a club tennis player taking on Roger Federer! The leverage is far too high and allows no margin of safety, nor the placement of strategically positioned stop losses but those based solely on financial considerations. In short, trading on such leverage is more akin to gambling in a casino with no relative advantage. It is only a matter of time, before the novice trader blows-up his trading account.

Just as charlatans claiming pills and potents are elixirs, offering cures for all our ills and eternal youth for all - beware the FX promoter claiming extreme trading leverage is the golden key to riches. Many veteran trading professionals believe that trading successfully over the long term requires mastering trading leverage. This means utilising sufficient leverage to enable you to maximise your trading profitability but also minimising trading leverage so that you never take "a big hit" and that any one loss or series of losses does not compromise your trading capital or your participation "in the game".

Trading is a "long game" and this requires effective risk/money management and determining the right leverage for any given trading situation is an important part of this.

Although trading leverage will vary dependent upon stop loss placement and perhaps even the confidence a trader has in a given trading position, as a broad "rule of thumb" many professional traders will typically operate much of the time on trading leverage in the vicinity of 3:1 or lower.

Such leverage may seem incredibly low to the novice trader (and most certainly to the rabid FX promoter) but whilst such leverage does not provide "instant" outlier profits, what it does do is the following:

It allows the trader to withstand a series of relatively small and manageable trading losses, since collectively they do not have a material effect on the trader's capital and it enables the trader to place his/her stop loss at a technically/strategically appropriate level.

The size of your trading position should be made to "fit" your stop loss placement. A wider stop means a reduced trading size and vice versa. Trading leverage is a powerful tool but if not properly respected, will likely eventually prove to be a trader's downfall.

The Rewards of Medium Term Trading

There are a number of different ways "to skin the cat" in forex trading, ranging from intra-day "scalping" to short-term trading and medium-term position trading. The greatest financial return can be expected from medium term FX trading, where the trader attempts to participate in multi-week trend moves and ride them for as long as possible.

Of course such trend moves don't present themselves every day and they take quite awhile to resolve, so they are not every trader's "cup of tea". Many traders like the "participation" aspect of forex trading and that means trading more frequently than medium term trading permits.

One of the problems many traders encounter with such medium term trading is the financial risk aspect. When identifying a trading situation, which has significant medium term potential, the targets will be "big" and not wanting to be stopped out too soon, traders often allow plenty of room on their stop loss.

The problem with this of course is that if stopped, a significant trading loss occurs, resulting in an unacceptable loss of precious trading capital. The prudent approach in this situation is to reduce your trading size, ensuring that if stopped, the trading loss will not cause too significant a draw-down in your trading capital.

My approach is along the following lines: When my technical analysis detects currencies offering medium term trading potential, objectives are identified and my focus then turns on to how to "get-set" (or enter) this trading opportunity, with minimal financial risk.

To do this, I treat this situation just as I do any other short term trading opportunity, with my stop loss reflecting this. If I am stopped out, then no harm is done, as my trading capital is not compromised. My first objective is to be able to move my stop loss to break-even as soon as practically possible. Thereafter, if the trade starts to work out, I will stay with it as long as possible and adjust my stop loss (according to my technical assessment) as time progresses.

Profits are realised either when my principal target is attained, a subsequent Chart or Elliott Wave structure forms (which contradicts the prevailing trend) or when the market stops me out (via my trailing stop loss).