Avoid the 5 common Trading plan errors that can impact on your results

Mike Smith Senior Educator, GO Markets

Australian Technical Analysts Association

1

Disclaimer and Risk Warning

GO MARKETS
first choice for trading

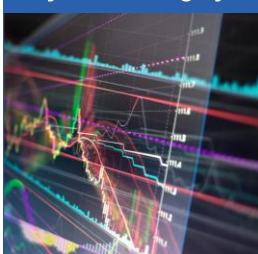
This webinar is from GO Markets analysts or external speakers, - based on their independent analysis or personal experiences. Views or opinions or trading styles expressed are of their own; should not be taken as either representative of or shared by GO Markets.

Advice (if any), is of a 'general' nature and not based on your personal objectives, financial situation or needs. You should therefore consider how appropriate the advice (if any) is to your objectives, financial situation and needs, before acting on the advice.

If the advice relates to acquiring a particular financial product, you should obtain and consider the Product Disclosure Statement (PDS) and Financial Services Guide (FSG) for that product before making any decisions.

2

Why are trading systems important?



What are we trying to achieve?

- Clarity of what we must do as a trader
- Consistency in execution
- Confidence in action
- Continuous development towards the trader we can be

- The ONLY way to achieve this is through learning and action in creating clear and comprehensive systems that are :

1. Executed
2. Altered on gathered evidence

3

It is a choice to create and execute a comprehensive, unambiguous trading plan.

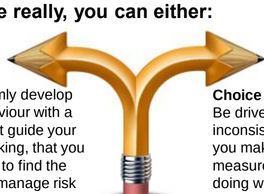
- Your trading plan is your #1 critical trading system.
- It should be comprehensive, guiding behaviour in the reality of the market.
- Ideally, your plan should be "dynamic", i.e. it changes over time as you gather evidence as to what works for you as an individual trader.

4

So what does this choice really mean....

It's quite simple really, you can either:

Choice 1
Confidently and calmly develop consistency in behaviour with a series of actions that guide your trading decision-making, that you can test and amend to find the optimum system to manage risk and take profit on an on-going basis.



Choice 2
Be driven by feeling, whims and inconsistency with the decisions you make, with reduced ability to measure whether what you are doing works or not, beyond a single trade.

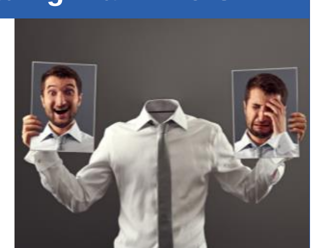
Logically, which is more likely to produce desired results for a potential lifetime of trading?

5

5 Common Trading Plan Errors

- The majority of traders have systems that may have one or more of the following:

1. An entry bias with exits incomplete.
2. Excludes key "conduct" issues of position sizing (sub-system), how to manage economic data, max number of positions, max market exposure.
3. Have statements that are ambiguous and not specific enough to enable consistency in action, nor measurability.
4. Are not evidence based in terms of what works for you (and doesn't) as an individual trader.
5. Have no sub-system for the addition of new indicators.



6

#1 - An entry bias with exits incomplete.

Why avoiding this is important?

- Consistency from trading idea, through entry to exit of every trade is crucial.
- Many experienced traders suggest that exits are as, if not more, important than entry and yet a disproportionate amount of effort, time and money is invested into entry.
- Separate outline for each strategy required.

Should include (every time!):

- *Name of strategy*
- *Entry criteria – technical and fundamental*
- *Stop loss criteria*
- *Profit target criteria (if set)*
- *Trail stop system*

7

#2 - Excludes key "conduct" issues (using position sizing as an example)

Why avoiding this is important?

- Position sizing (answering the question of how much of a position should I enter) along with effective exits are the two critical components in the extent to which you profit or loss.
- Many trading errors and subsequent major account drawdowns may be due to inappropriate position sizing.

8

So what are my 'Position Sizing' options

Dependent on experience in this sub-system

Beginner:

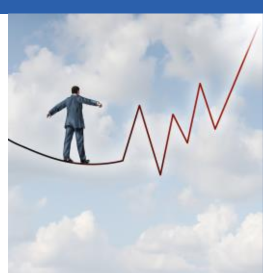
- Utilise a set formula on entry based on a % (often 1-2%) of your trading capital. Adjust on a monthly basis

Intermediate:

- As part of your trail stop and accumulation systems have your initial position sizing that retains your risk in the life on a trade within a tolerable level

Advanced

- Develop a formula that position sizes according to underlying market conditions



9

…So how might this work?

- You will already have a standard position sizing formula.
- Your challenge as you develop is to create a set of criteria that would result in various position sizing actions

e.g.
Level 1 - Strong compelling evidence.
Level 2 - Normal compelling evidence
Level 3 – Weaker than normal compelling evidence (or more general market risks).

And for each of these assign a risk level e.g. 1%, 2%, 3%

10

#3 - Have statements that are ambiguous

Consider the following trading plan statement

"I will take a long trade if the price breaks through an identified line of resistance with increased volume"

Does this facilitate consistency in action and measurement of how well it serves your trading outcomes?

Issues:

- When?
- What is a 'break through'? Increased volume compared to what?

11

So this is what it could look like.

e.g. For long trade…

Entry

- Entry on candle close (within last hour)
- Price in top third of candle if long
- Volume bar higher than previous 2 bars
- 0.5 ATR through key level (resistance)
- No significant economic data (specify) or company reporting within 3 weeks.

12

#4 – Trading plan is not evidence based

- The evidence we seek is to develop a plan sufficiently individualised for our personal interaction with the market.
- Evidence based trading is ONLY possible if there are robust mechanisms and behaviours in place to be able to do so.
- Essential for system "confidence" a critical part of the ability to exercise discipline in execution.

On a broad level these include:
1. A recording system **(e.g. a journal)**
2. Sufficiently specific statements that can be followed religiously and are measurable (i.e, Y/N or numeric)
3. Behavioural consistency that ensures that there is follow through (this comes with evidence).
4. A method through which these can be reviewed systematically AND fed back into trading system

13

So what can we do with this?

Once a sufficient level of the infrastructure and process is in place then testing new approaches is possible. Such testing can include:
1. Reliability (can results be replicated in different market conditions or do you need to adjust for this too).
2. Strategy V Strategy (may be whole system or sub-system e.g. trail stop systems)
3. Alternative entry/exit indicator perimeters with existing indicators
4. Alternative indicators

So, lets take three trail stop strategies as an example…

14

Trail stop alternatives…

For example in trading plan…
- I will review my chart at least at the end of every candle on my chosen timeframe.
- I will trail my stop at the 20 EMA of the candle close.
- If the price is more than 2x my initial risk level away from the 20EMA then I will use the 10EMA as a trail.

Method	Trader Challenges
Price/MA cross	a. Which MA? b. Which period? c. When? d. Rapid move = change of MA?
Trend pause/ retracements	a. What constitutes a pause? b. How close to previous pivot?
MACD signal line V histogram	a. When? b. Which timeframes?

15

#5 – No sub-system to add a new indicator

- Be clear what an additional indicator may add (what is the gap you are trying to fill?)
- A back-test = A test of a trading system retrospectively, the purpose of which is ONLY to determine whether a system or system change is worth testing prospectively.
- ONLY test one thing at a time (if entry then exits uniform):

1. You can retrospectively look at trades you have already closed and judge whether there would have been a result difference.
2. Look at recent charts that would have met entry criteria of your existing system to see what the impact of the additional indicator would be.
3. Make a decision on what constitutes a "critical mass" of trades to test **prospectively**

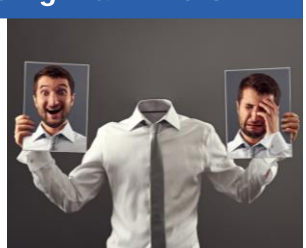
Note: Although rarer, the process is the same if looking to remove indicators from your system

16

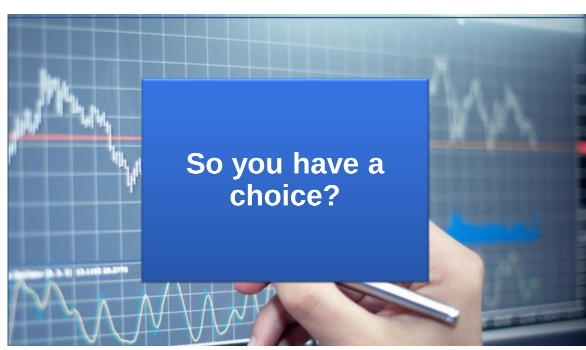
5 Common Trading Plan Errors

- The majority of traders have systems that may have one or more of the following:

1. An entry bias with exits incomplete.
2. Excludes key "conduct" issues of position sizing (sub-system), how to manage economic data, max number of positions, max market exposure.
3. Have statements that are ambiguous and not specific enough to enable consistency in action, nor measurability.
4. Are not evidence based in terms of what works for you (and doesn't) as an individual trader.
5. Have no sub-system for the addition of new indicators.



17



18


And to help…
www.gotradeacademy.com/kit
mike.smith@gomarkets.com

19