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**The Importance of the Money Management in a trading system**

**Money management** is a critical point that shows difference between winners and losers. It was proved that if 100 traders start trading using a system with 60% winning odds, only 5 traders will be in profit at the end of the year. In spite of the 60% winning odds 95% of traders will lose because of their poor money management. **Money management** is the most significant part of any trading system. Most of traders don't understand how important it is.

It's important to understand the concept of money management and understand the difference between it and trading decisions. **Money management represents the amount of money you are going to put on one trade and the risk your going to accept for this trade.**

There are different money management strategies. They all aim at preserving your balance from high risk exposure.

First of all, you should understand the following term **Core equity**
Core equity = Starting balance - Amount in open positions.

If you have a balance of 10,000$ and you enter a trade with 1,000$ then your core equity is 9,000$. If you enter another 1,000$ trade, your core equity will be 8,000$

It's important to understand what's meant by core equity since your money management will depend on this equity.

We will explain here one model of money management that has proved high annual return and limited risk. The standard account that we will be discussing is 100,000$ account with 20:1 leverage . Anyway, you can adapt this strategy to fit smaller or bigger trading accounts.

## Money management strategy

Your risk per a trade should never exceed 3% per trade. It's better to adjust your risk to 1% or 2%

We prefer a risk of 1% but if you are confident in your trading system then you can lever your risk up to 3%

1% risk of a 100,000$ account = 1,000$

You should adjust your stop loss so that you never lose more than 1,000$ per a single trade.

If you are a short term trader and you place your stop loss 50 pips below/above your entry point.
50 pips = 1,000$
1 pips = 20$

The size of your trade should be adjusted so that you risk 20$/pip. With 20:1 leverage, your trade size will be 200,000$

If the trade is stopped, you will lose 1,000$ which is 1% of your balance.
This trade will require 10,000$ = 10% of your balance.

If you are a long term trader and you place your stop loss 200 pips below/above your entry point.
200 pips = 1,000$
1 pip = 5$

The size of your trade should be adjusted so that you risk 5$/pip. With 20:1 leverage, your trade size will be 50,000$
If the trade is stopped, you will lose 1,000$ which is 1% of your balance.
This trade will require 2,500$ = 2.5% of your balance.

This is just an example. Your trading balance and leverage provided by your broker may differ from this formula. The most important is to stick to the 1% risk rule. Never risk too much in one trade. It's a fatal mistake when a trader lose 2 or 3 trades in a row, then he will be confident that his next trade will be winning and he may add more money to this trade. This is how you can blow up your account in a short time! A disciplined trader should never let his emotions and greed control his decisions.

## Diversification

Trading one currency pair will generate few entry signals. It would be better to diversify your trades between several currencies. If you have 100,000$ balance and you have open position with 10,000$ then your core equity is 90,000$. If you want to enter a second position then you should calculate 1% risk of your core equity not of your starting balance!. It means that the second trade risk should never be more than 900$. If you want to enter a 3rd position and your core equity is 80,000$ then the risk per 3rd trade should not exceed 800$

It's important that you diversify your priers between currencies that have low correlation.
For example, If you have long EUR/USD then you shouldn't long GBP/USD since they have high correlation. If you have long EUR/USD and GBP/USD positions and risking 3% per trade then your risk is 6% since the trades will tend to end in same direction.

If you want to trade both EUR/USD and GBP/USD and your standard position size from your money management is 10,000$ (1% risk rule) then you can trade 5,000$ EUR/USD and 5,000$ GBP/USD. In this way, you will be risking 0.5% on each position.

## The Martingale and anti-martingale strategy

It's very important to understand these 2 strategies.

-Martingale rule = **increasing your risk when losing** !
This is a strategy adopted by gamblers which claims that you should increase the size of you trades when losing. It's applied in gambling in the following way Bet 10$,if you lose bet 20$,if you lose bet 40$,if you lose bet 80$,if you lose bet 160$..etc

**This strategy assumes that after 4 or 5 losing trades, your chance to win is bigger so you should add more money to recover your loss!** The truth is that the odds are same in spite of your previous loss! If you have 5 losses in a row, still your odds for 6th bet 50:50! The same fatal mistake can be made by some novice traders. For example, if a trader started with a balance of 10,000$ and after 4 losing trades (each is 1,000$) his balance is 6000$. The trader will think that he has higher chances of winning the 5th trade then he will increase this size of his position 4 times to recover his loss. If he lose, his balance will be 2,000$!! He will never recover from 2,000$ to his starting balance 10,000$. A disciplined trader should never use such gambling method unless he wants to lose his money in a

short time.
-Anti-martingale rule = **increase your risk when winning & decrease your risk when losing**!

It means that the trader should adjust the size of his positions according to his new gains or losses.

Example: Trader A starts with a balance of 10,000$. His standard trade size is 1,000$
After 6 months, his balance is 15,000$. He should adjust his trade size to 1,500$

Trader B starts with 10,000$. His standard trade size is 1,000$
After 6 months his balance is 8,000$. He should adjust his trade size to 800$

### High return strategy

This strategy is for traders looking for higher return and still preserving their starting balance.
According to your money management rules, you should be risking 1% of you balance. If you start with 10,000$ and your trade size is 1,000$ (Risk 1%). After 1 year, your balance is 15,000$. Now you have your initial balance + 5,000$ profit. You can increase your potential profit by risking more from this profit while restricting your initial balance risk to 1%. For example, you can calculate your trade in the following pattern:
1% risk 10,000$ (initial balance) + 5% of 5,000$ (profit)

In this way, you will have more potential for higher returns and on the same time you are still risking 1% of your initial deposit.



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