Let me ask you…

Do you know how to apply forex risk management so your losses feel like an "ant bite" to your account?

Do you have the ability to trade any markets or timeframes, and not blow up your trading account?

Do you know the secret to finding low-risk high reward trades?

If you answered NO to any of the above…

Then good luck to you.

I'm just kidding.

Now…

Today's post is going to be one of the most important you'll ever read.

Because if you apply the risk management and position sizing strategies, I can guarantee you'll never blow up another trading account — and you might even become a profitable trader.

And to prove my point, here's what you'll learn today:

- Risk management, what does it really mean
- What is position sizing and why it's the closest thing to the "holy grail"
- How to calculate position size in forex
- How to calculate your position size in stock trading
- Forex position sizing calculators
- The secret to finding low risk and high reward trades
- Why leverage is irrelevant and what you should focus on instead

Are you ready? Then let's begin…

Risk management, what does it really mean?

Risk management is the ability to contain your losses so you don't lose your entire capital.

It's a technique that applies to anything involving probabilities like Poker, Blackjack, Horse betting, Sports betting and etc.

Here's the thing:

If you have a $10,000 trading account, would you risk $5000 on each trade?

Of course not.

Because it only takes 2 losses in a row and you'll lose everything.

And even a profitable trading strategy won't save you.

Don’t believe me? Then let me prove it to you…

Imagine:

There are two traders, John and Sally.

John is an aggressive trader and he risks 25% of his account on each trade.

Sally is a conservative trader and she risks 1% of her account on each trade.

Both adopt a trading strategy that wins 50% of the time with an average of 1:2 risk to reward.

Over the next 8 trades, the outcomes are Lose Lose Lose Lose Lose Win Win Win Win.

Here’s the outcome for John:

-25% -25% – 25% – 25% = BLOW UP

Here’s the outcome for Sally:

-1% -1% -1% -1% +2% +2% +2% +2% = +4%

Can you see how powerful this is?

Risk management could be a deciding factor whether you’re a consistently profitable trader or, losing trader.

Remember, you can have the best trading strategy in the world.

But without proper risk management, you will still blow up your trading account.

It’s not a question of if, but when.

What is position sizing and why it’s the closest thing to the “holy grail”

Now you’re probably wondering:

“How do I apply proper risk management?”

The secret is…

Position sizing.

A technique that determines how many units you should trade to achieve your desired level of risk.

And this is the closest thing you can get to the “holy grail”.

But before you calculate your position size, you must know these 3 things:

1. Value per pip
2. The dollar value you’re risking on each trade
3. Distance of your stop loss

Let me explain…

1. Value per pip

Value per pip is the change to your P&L if price moves by 1 pip.

To calculate this, you need three things: Currency of your trading account, the currency pair traded, and the number of units traded.

Example 1:

Your trading account is in SGD.

You're trading EUR/USD.

You long 100,000 units of it.

Now…

If EUR/USD increases by 1 pip, what is the impact on your P&L (in SGD)?

Step 1: Determine the value per pip of the currency pair you're trading

Since you're trading EUR/USD…

The EUR is the base currency and the USD is the quote currency.

To determine the value per pip, look at the quote currency.

If you're long 100,000 units of EUR/USD, the value per pip is $10USD.

Step 2: Determine the spot rate between the currency of your trading account and the quote currency

The currency of your trading account is in SGD.

The quote currency is USD.

Thus, look at the spot rate of USD/SGD.

Step 3: Multiply the spot rate with the value per pip of the currency you're trading

Let's assume the spot rate of USD/SGD = 1.4000

So…

1.4 * 10 = 14SGD

This means every 1 pip movement in EUR/USD is worth $14SGD to you.

Example 2:

Your trading account is in USD and you long 500,000 units of EUR/GBP.

If EUR/GBP moves by 1 pip, what is the impact on your P&L (in USD)?

Step 1: Determine the value per pip of the currency pair you're trading

Since you're trading EUR/GBP…

The EUR is the base currency and the GBP is the quote currency.

To determine the value per pip, look at the quote currency.

If you're long 500,000 units of EUR/GBP, the value per pip is $50GBP.

Step 2: Determine the spot rate between the currency of your trading account and the quote currency

The currency of your trading account is in USD.

The quote currency is GBP.

Thus, look at the spot rate of GBP/USD.

Step 3: Multiply the spot rate with the value per pip of the currency you're trading

Let's assume the spot rate of GBP/USD = 1.25

So…

1.25 * 50 = 62.5USD

This means every 1 pip movement in EUR/GBP is worth $62.5USD to you.

Now to make your life easier, you can use a pip value calculator like [this one from Investing.com].

2. The dollar value you're risking on each trade

This means how much you're risking on each trade (in terms of dollar value).

I suggest risking not more than 1% of your account per trade. Why?

Because you don't want a few losses to put you in a steep drawdown, or wipe out your trading account. And not forgetting, you need proper risk management to survive long enough for your edge to play out.

Here's how to calculate your dollar risk per trade:

Let's assume you have a $10,000 account.

You're risking 1% of your capital on each trade.

Here's the math: 1% of $10,000 = $100

This means you'll not lose more than $100 per trade.

Remember, the risk of ruin is not linear. This means the more money you lose, the harder it is to recover back your losses.

% Loss of Capital	% Gain Required to Recover Loss
10%	11.11%
20%	25
30%	42.85
40%	66.66
50%	100
60%	150
70%	233
80%	400
90%	900
100%	Broke

3. Distance of your stop loss

The final ingredient is finding out what is the size of your stop loss (in terms of pips, or ticks if you're trading stocks and futures).

If you want to learn more, go watch the video below:

If you ask me, risk management and position sizing are two sides of the same coin.

You can't apply risk management without proper position sizing.

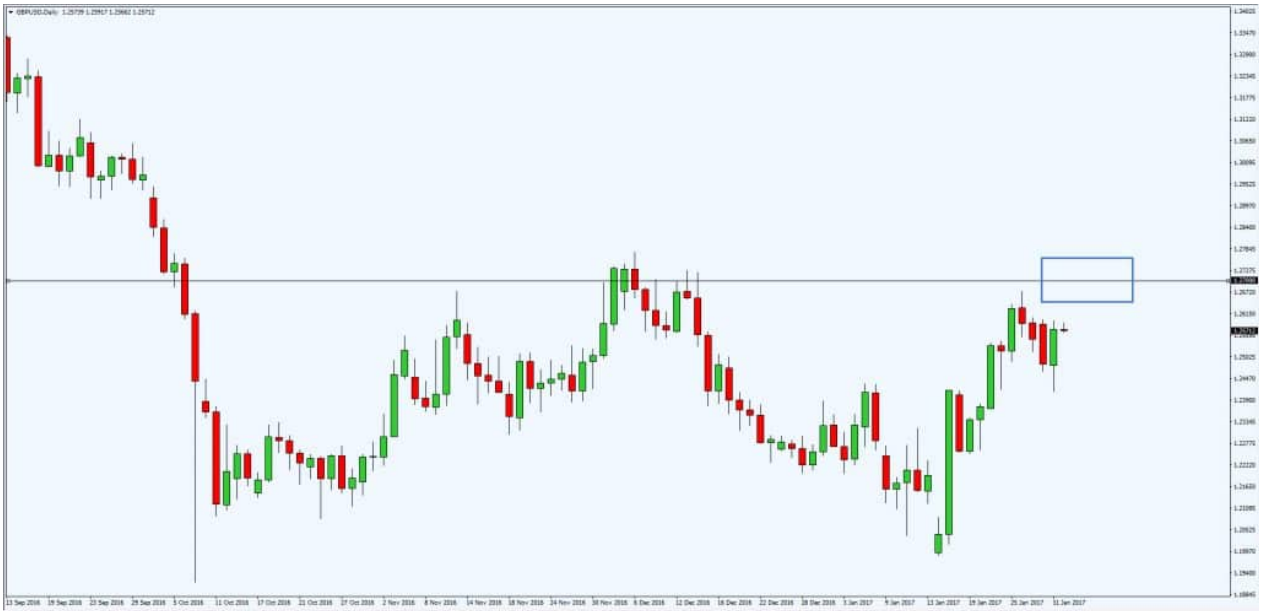
Next…

You'll learn how to calculate your position size for every trade, so you will never blow up another trading account. Let's go!

How to calculate position size in forex

Let's assume:

1. You have a $10,000USD trading account and you're risking 1% on each trade
2. You want to short GBP/USD at 1.2700 because it's a Resistance area
3. You have a stop loss of 200pips



So, the question is…

“How many units do you short so you only risk 1% of your trading account?”

Forex risk management — position size formula

Here’s the formula:

Position size = Amount you’re risking / (stop loss * value per pip)

So…

- The amount you’re risking = 1% of $10,000 = $100
- Value per pip for 1 standard lot = $10USD/pip
- Stop loss = 200pips

Plug and play the numbers into the formula and you get:

Position size = 100 / (200*10)

= 0.05 lot (or 5 micro lots)

This means you can trade 5 micro lots on GBP/USD with a stop loss of 200 pips; the maximum loss on this trade is $100 (which is 1% of your trading account).

Now you’re probably wondering:

“Rayner, this is so cumbersome. Is there a faster way to calculate it?”

You bet.

All you need to do is use a forex position sizing calculator and I’ll explain more in this video…

How to calculate position size in stock trading

Once you understand how position sizing works, you can apply it to all markets.

This means you can manage your risk like a pro no matter what instruments you're trading.

Here's an example for stock:

1. You have a $50,000USD trading account and you're risking 1% on each trade.
2. You want to long Mcdonalds at 118.5 because it's an area of Support
3. You have a stop loss of 250 ticks (which is $2.5)

So…

How many shares of Mcdonalds do you buy so you risk only 1% of your trading account?

Stock risk management — position size formula

Here's the formula:

Position size = Amount you're risking / (stop loss * value per tick)

So…

- The amount you're risking is 1% of $50,000 = $500
- Value per tick for 1 share = $0.01
- Stop loss = 250 ticks

Insert these numbers into the formula and you get:

Position size = 500 / (250*0.01)

= 200 shares

This means you can trade 200 shares of Mcdonalds with a stop loss of 250 ticks. If it's triggered, the loss on this trade is $500 (which is 1% of your trading account).

Remember, when you're trading stocks, the price can gap through your stop loss — causing you to lose more than you intended. This is a common occurrence during earnings season.

Now…

I know this is a slow way to calculate your position size for stocks. That's why you can use a position sizing calculator to make your life easier, which I'll explain more in this video…

Forex risk management — position sizing calculators

To make your life easier, you can use one of these calculators below:

MyFxBook – Position sizing calculator for forex traders.

Daniels Trading – Position sizing calculator for futures traders.

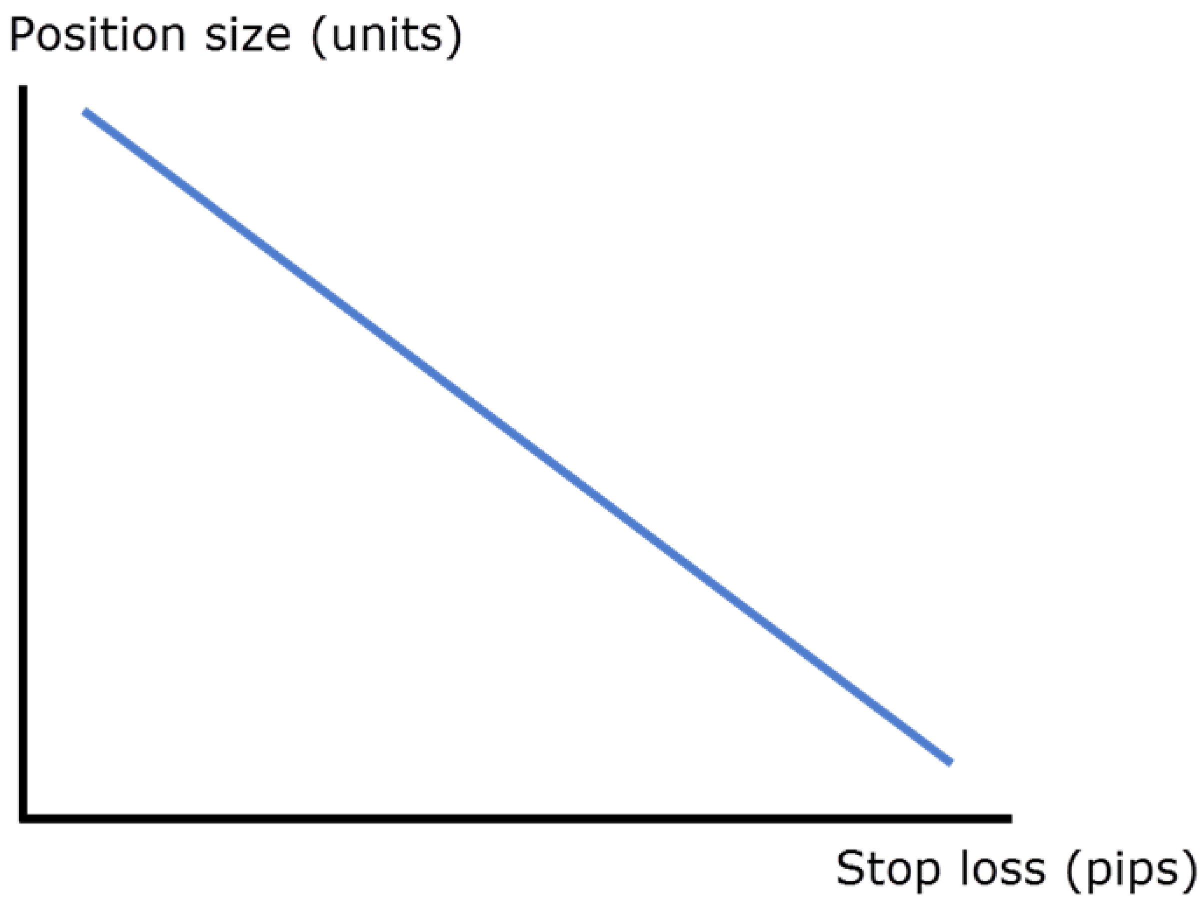
Investment U – Position sizing calculator for stock and options traders.

The secret to finding low risk and high reward trades

Here's a fact:

The larger the size of your stop loss, the smaller your position size (and vice versa).

Visually, it looks like this:



Now, let me prove it to you…

- Assume you're risking $1000 on each trade
- Value per pip for 1 standard lot is $10USD/pip
- Your stop loss is 500 pips on EUR/USD

So, how many units can you short?

Position size = 1000 / (500 * 10)

<u>= 0.2 lot (or 2 mini lots)</u>

For this trade, if the market moves 500 pips in your favor, **you'll gain $1000**.

But what if you can reduce your stop loss to 200 pips?

Position size = 1000 / (200 * 10)

<u>= 0.5 lot (or 5 mini lots)</u>

For this trade, if the market moves 500 pips in your favor, **you'll gain $2500**.

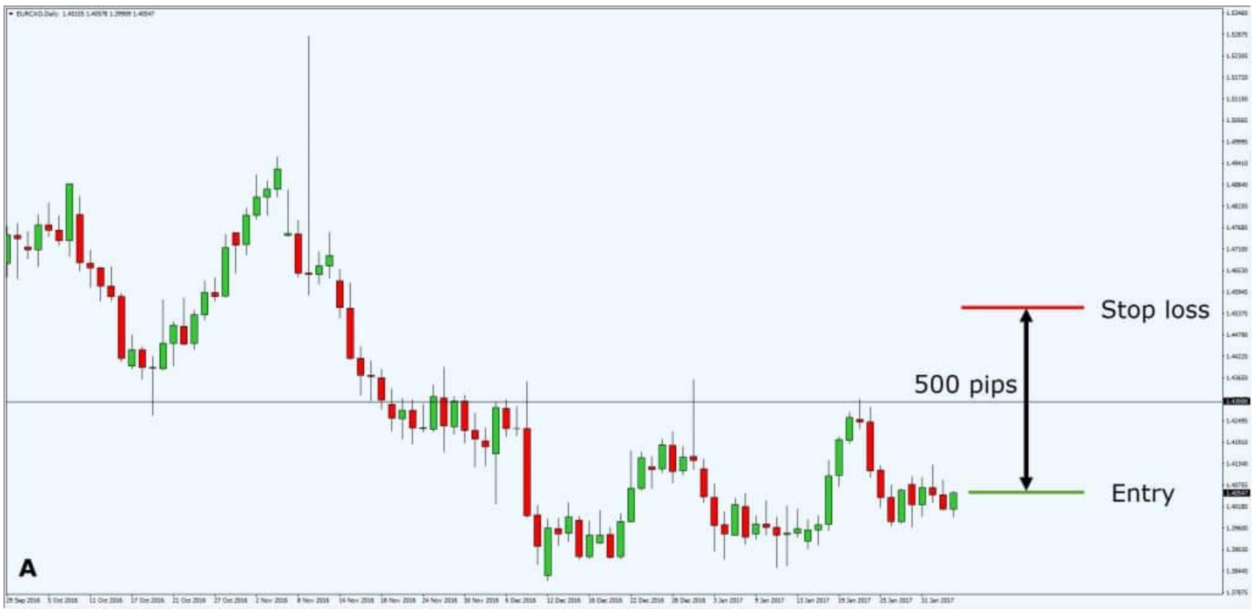
The bottom line is this… a tighter stop loss allows you to put on a larger position size — for the same level of risk.

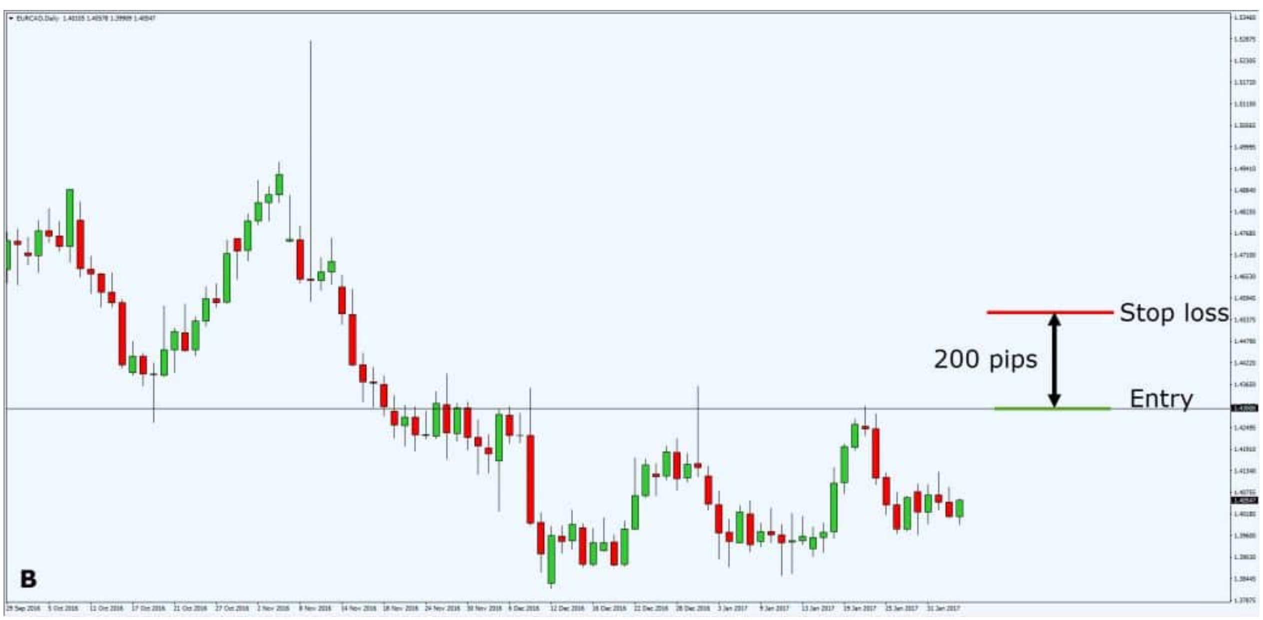
So, how do you apply this concept to your trading?

Simple.

By being patient and letting the market come to your level.

Here's what I mean:





Both A & B have the same stop loss.

The only difference is where you're shorting the market — and this makes a huge difference to your bottom line.

So, do you want to short A or B?

Why leverage is irrelevant and what you should focus on instead

This is one of the most common questions I get from traders…

"Hey, Rayner, how much leverage do you use?"

If you are unfamiliar with the term leverage, it means how many times larger you can trade relative to your account size.

So, if you have 1:100 leverage and your account size is $1000; this means you can trade up to $100,000 worth of the underlying instrument (like stocks, currencies, futures).

But here's the truth:

I don't bother about leverage. Why?

Because it has zero relevance to your risk management.

Let me explain…

- Assume you have a $10,000 account
- You risk 1% of your account on each trade
- Value per pip for 1 standard lot is $10USD/pip
- Your stop loss is 50 pips on EUR/USD

So, how many units can you trade?

Position size = 1000 / (50 * 10)

= <u>2 lots</u>

This represents $200,000 worth of EUR/USD, or in other words, **a leverage of 1:20**.

But…

What if your stop loss is 500 pips?

Again, apply the position sizing formula and you get…

1000 / (500 * 10)

= <u>0.2 lot</u>

This represents $20,000 worth of EUR/USD, or in other words, **a leverage of 1:2**.

Do you see my point?

In both scenarios, the maximum loss on each trade is $1000, even though you're using different leverages. Why?

Because the leverage you use depends on the size of your stop loss.

The smaller your stop loss, the more leverage you can use while keeping your risk constant.

And the larger your stop loss, the less leverage you can use while keeping your risk constant.

So…

Don't bother too much about leverage because it is largely irrelevant. Instead, focus on how much you can lose per trade, and adopt the correct position size for it.

Summary

- Risk management is KING. Without it, even the best trading strategy will not make you a consistently profitable trader
- Risk management and position sizing are two sides of the same coin. With the correct position sizing, you can trade across any markets and still manage your risk
- This is the position sizing formula that lets you achieve it: <u>Amount you're risking / (stop loss * value per pip)</u>
- The secret is entering your trades near Support and Resistance. Because you can have a tighter stop loss, which lets you put on a larger position size — and still keep your risk constant
- Leverage is irrelevant because it doesn't help you manage your risk. The only thing that matters is proper position sizing that lets you risk a fraction of your trading capital