Twitter Thread by The_Chartist ■

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Your checklist of risk management

Common Sense Management of Risk

Risk control is as much an issue of common sense as it is complex rules and mathematics. Most of this chapter shows how various rules, measurements, and leveraging techniques can reduce risk for both discretionary and algorithmic trading; however, successful traders have applied common sense, without complex formulas, for a long time. Some of these successful principles are:

1. *Only risk a small amount of total capital on any one trade.* The total amount risked should allow you to comfortably survive a number of losses in a row. No trade should ever risk more than 5% of the invested capital.
2. *Know your exit conditions in advance.* There should be a clear exit criterion for every trade, even if the exact loss cannot be known in advance.
3. *Large profits mean large risk.* If the average profits or average losses are too large relative to the investment, then smaller positions should be taken.
4. *Exit a trade quickly.* Exit a trade as soon as you recognize that it has gone wrong. Don't try to manage the loss. Many floor traders believe that the smartest trader is the first one out.
5. *Don't meet margin calls.* Experienced traders believe that a margin call is an objective statement of a trade that's gone wrong, or a system that is not meeting expectations. It is a time to review trading performance rather than invest more.
6. *Liquidate your worst position first when lightening up.* The profitable trades have proved that they are trending or performing properly; the losing ones have proved they are not. Stay with the good positions and liquidate the worst.
7. *Be consistent with your trading philosophy.* If you are a trend follower, then keep losses small and let profits run. You cannot be a trend follower by taking profits whenever they occur.
8. *Be sure the trading profile is compatible with your risk preference.* You cannot follow a strategy that takes risks that are uncomfortably large. Be sure that profile is agreeable to you.
9. *Plan for contingencies.* Nothing ever goes as planned, and you must be prepared for infrequent but important exceptions, such as a price shock. Do not be undercapitalized.