

## Five Fundamental Laws of Trading

Not long ago I had an interesting conversation with a trader who, like so many others, had struggled for years to find any real measure of consistency in their quest for success. Performance had hit a historic low with only one marginally profitable month all year. The pain of chronic losses mixed with her inability to understand how her depth of knowledge, experience and former success could now count for so little.

When traders come to me because they need help, they often have no clear idea what that assistance should be. Understandably, they want a quick permanent fix but that's usually an unrealistic expectation. With study, practice and experience most traders with a passion to succeed can enjoy some positive period of performance. The problem is that any period of prosperity traders enjoy will most likely be fragile and fleeting if the trader doesn't understand the Fundamental Laws of Trading.



These laws are inescapable regardless of the system, methodology or vehicle traders choose to use. Though there are more, I have chosen five of these for discussion so that they are fully understood. For some traders, these may serve as reminders of that which they already know but when a seasoned trader asks about the “accuracy percentage of a system”, I know that they possess little understanding of the nature of trading or how lasting success is achieved.

### **Fundamental Law #1 – Trading is an Acquired Skill, not an Innate Talent**

Although there are traders who have some degree of natural trading ability to begin with, those who approach it as a skill to be developed will usually stand the best chance of lasting success. Beginning the journey will be a smoother ride if the trader already possesses a high degree of patience, self-discipline and ability to remain focused with solid self-control.

These essential human qualities can be developed and traders should understand that self-mastery accounts for a far greater percentage of trading success than system mastery. Never believe that successful traders are smarter, gifted or just luckier. Passion and persistence trumps everything else.

### **Fundamental Law #2 – There Are No Winning Systems, Only Winning Traders**



No trading system in the world is any better than the trader behind it pushing the buttons. They can be of great assistance in the hands of trained, skilled traders, for sure. That's because they are a tool whose function is to

help the user do a better job just as a tablesaw would to the carpenter or GPS to a navigator.

It's amazing how many otherwise intelligent traders I meet who comb the internet in forums and webinars searching for a "winning system". Traders who lack confidence in themselves become obsessed in a futile quest for a system that will make all their decisions for them. They invest years and fortunes on systems but, until the broken trader is fixed, no system can work for the long haul.

This misguided mindset is not limited to traders. Many golfers, for instance, spend thousands of dollars on expensive clubs and gadgets and never see their scores improve one bit. Clubs, bowling balls, or trading systems, if the skill's not there, neither will the success.

### **Fundamental Law #3 – Successful Traders Who Stop Learning, Stop Winning**

In trading, staying on top means staying ahead. Markets are global and their dynamics get more complicated over time. Trading success is directly proportional to the trader's knowledge and skill but it's also dependent on the pertinence of that knowledge and the value of that skill.

Imagine going for a delicate surgical procedure and finding out that your surgeon wasn't on the cutting edge of his craft. That he hadn't learned anything new in 10 years. What if you learned that your doctor had botched a high percentage of his patient procedures because his knowledge was outdated and his skills were inadequate? Would you be a passenger on a plane if you knew the pilot hadn't flown in years and his license had long expired?



Every day traders whittle away their financial futures with systems or methods that have lost their edge and the markets have left them in the dust. Many fail to maintain the knowledge and practice necessary to know how to recognize and when to adjust to the ever-changing market dynamics. When a trader stops learning, losing won't be far behind.

### **Fundamental Law #4 – Goals are Your “Compass”**

For thousands of years since man first sailed the ocean blue, the success of their journey depended on the navigational method or device they used be it the stars or sextant. In trading, as in sailing the oceans, it's not enough to just know where you are. You must know where you are going. And, finally, you must have a realistic plan to get there.

I meet traders every day that either have no goals at all or the ones they do have are so vague or unachievable they are virtually worthless. I know traders who set their goals before they even learn how to trade. That's wishing, not goal-setting.

Make your goals realistic based on what you have proven you can consistently achieve over a reasonable period of time. Short and Long Term goals can't be based on what you want or wish them to be. If your trading account is going backwards then trying to set trading goals would be pointless. There's a logical proven process for setting consistent realistic goals and traders don't have to lose a dime in the process.

Learning to trade with consistent profitability can be considered your "internship" and, for many reasons, you should begin in simulation mode. It makes no sense to lose money while you struggle for self-control and a workable system. Modern trading platforms make trading in simulated mode virtually identical to real account trading. The only difference is on an emotional level. Simulation mode trading allows you to put your destructive negative human emotions aside while you master your system and build unshakable confidence in your skill.

You will make mistakes and lots of them at first. Keep diligent data and establish your short and long-term goals based on your proven results trading over a reasonable period of time. If your emotions affect your trading decisions, you are not ready to trade your live account.

As you gain mastery and your data proves profitability, here are some useful guidelines you should consider. Keep practicing and gaining knowledge daily until you are positive you have the skill, self-control and extreme confidence necessary to succeed going live. Do not strive for perfection as that is impossible to achieve. When you're ready to trade your live account, subtract about 20% from the results of your simulation data. If you are consistently averaging 25 ticks a day in sim in a given market, make your live trading goal 20 ticks. Making the transition from sim to live trading may have some effect caused by lingering emotions. Don't try to eliminate your human emotions. No one can. But you can control their ability to influence your trading decisions. That's not only an achievable goal, it's also imperative.



The more you perform a task the better you can perform it over time. As your knowledge, confidence and skill level increase, you will know when it's time to raise your short and long-term goals.

### **Fundamental Law #5 – 90% of All Traders Fail**

There's probably never been any official study done but any brokerage firm can probably confirm that the 90% failure rate is pretty close. Why so high? Well, first, let's be honest and admit that not everyone is cut out to be a trader. Trading is a totally mental exercise and some people lack the patience or the passion to overcome the many challenges it requires. But that wasn't the reason. Even after adjusting for career misfits, the trader failure rate is still embarrassingly excessive.

When I made the decision to teach as well as trade, my greatest concern was knowing that I could never accept that kind of failure rate. I wanted to know the reason for it and what, if anything, could be done to lower it. The answer was not what I had initially imagined but, once revealed, it made all the sense in the world. I just had to ask the right questions.

We already know that professional trading requires the ability to achieve and maintain pro level skills. Skills can be developed in a number of ways but not with the same effectiveness. So the question is, “What did they do to enjoy consistent success when so many others have failed?” Did they try harder? No. Most dedicated passionate traders spend as much time and effort as any other trader but success remains elusive. So it’s not lack of effort.

The difference between the consistent winners and the chronic wannabes wasn’t measured in money spent, effort given or passion possessed. I discovered nearly two decades ago that the difference was in trading knowledge and how that knowledge was acquired.

You can say a lot about trading but one thing’s for sure; there’s no shortage of knowledge. In fact, there’s too much. For the self-taught trader, it takes supreme effort and extreme discipline to not fall prey to the worthless information and bogus knowledge found in many articles, webinars and forums throughout the internet. What makes it even more confusing is that the knowledge that is useless to one trader can be a goldmine for another! How can that be, you ask? Let me explain the paradox in a true story.

In high school I joined the Bowling Club. I was a self-taught bowler and developed a smooth four-step approach by watching the pros on TV. By the end of my first year I carried about a 165 average. Many of the other kids had averages of over 200. Being competitive, I wanted to do the best I could for my team. So, every weekend I practiced. I went to a fingertip grip and the extra hook it gave me boosted my average to about 175 by my second year. My team was winning pretty consistently.

I noticed that many of the best bowlers used a five-step approach. So every weekend I practiced taking 5 steps instead of 4. Immediately, I noticed that I was getting a lot more power in the ball and I liked that. I kept practicing every weekend. By the end of my second year my average had dropped from a peak of about 180 down to 160...It was going backwards!

The problems were many. My timing and balance were shaky and inconsistent. So I did the logical thing and went back to a four-step delivery. But, by then I was doing so many things wrong I couldn’t get back on track. No matter how much I practiced on weekends, my average continued to drop. I think by my senior year I was around a 145 bowler. I lost all confidence in myself and my initial passion for the game was nearly gone.

As a freshman in college, it was mandatory that I take a course in some sport. I had a choice of handball, golf or, you guessed it, bowling. I dusted off the old ball and, true to form, I averaged about 140 after my first 3 or 4 outings. But this time I had an instructor. He was actually a great

bowler who had done quite well on the pro circuit years earlier. He could see the bad habits that I had picked up as a “self-taught” bowler. Things I wasn’t even remotely aware that I was doing. Within 3 or 4 weeks’ time, I was maintaining a 205 average per game! Never had I done so well.

That experience taught me a lesson that has stayed with me my entire life. Whenever I attempted to learn a new skill, whether it was a sport, selling a product, or as a public speaker, be the best I possibly can. That meant find an instructor, coach or mentor. Learn everything they know about that skill and master it. Then never stop learning and improving, especially if that craft is your career.

90% of all traders fail and 90% of all traders never had someone qualified to work with them on a consistent basis until they were able to trade on their own and reach their goals consistently. I am convinced there is a definite correlation. The lessons I learned those many years ago serve as my motivation to always recommend qualified mentorship to any struggling trader and to be a mentor to any trader who is willing to learn. It’s called paying it forward and that’s not a bad “law” for anyone to follow.