Trading is a business - trading is not a sport, and despite what many believe, we’re not gambling. We are simply using probabilities and statistics in our favor, coupled with technical analysis based on past patterns and market behavior, to make our plays.

Before we can make money, we must define the rules that define our risk parameters. It is always risk first, profits second. What are our goals? To become a better trader, hold onto our cash, and live to trade another day. Amateurs place trades without thinking, without knowing, and without quantifying their risk. Don’t be an amateur.

All of the following should be clear and acceptable to you BEFORE placing the trade:

**The Setup**

I’m taking this trade because it’s a defined setup in which I have an edge. Trades based on feelings are a no-go. No setup, No trade.

**Position Sizing**

I know what percentage of my account I’m risking on this trade. Our traders generally have between 1%-5% of their account at risk per trade. Do not risk more than you’re willing to lose to take a stab at the setup. John in particular pushes this higher, but don’t forget that he is a very experienced, professional trader.

**Profit Target & Stop Loss**

I know where I will exit if things go right, and if they go wrong. Know how you define these levels and have the discipline to stick with them.

**Overall Account Risk**

I know what percentage of my overall account is tied up in all my trades combined, and I am not over allocating my money. Having more than 20% of your account allocated in short-term, options positions can put you at high risk of capital loss in flash crash or tanker event situations. Longer dated, income style trading has acceptable risk parameters of up to 50% of your account, due to the longer dated nature.

**Concentration Factor**

I know how many positions I can reasonably handle at one time to trade well, and adding this position isn’t going over my limit. It’s better to select less trades and trade them meticulously than overtrade, blow up my trades, and make unnecessary mistakes. John doesn’t like having more than 6 positions, though Henry is fine going over this limit. You must find your own happy medium.

**Exposure**

I’m keenly aware of my overall exposure, and I try not to have my risk concentrated too much in one sector or dependent on one market direction. Having a portfolio that contains strictly long calls on tech stocks will fare a bit worse during a down day in XELK than a portfolio that contains a mix of options strategies and positions. This can include directional plays with long calls, and theta decaying positions utilizing credit spreads and iron condors.

**Acceptance**

I fully accept that this trade could go to zero. Always be prepared for anything, and it will happen.

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**The Probabilistic Mindset**

1. Anything can happen.
2. You don’t need to know what is going to happen next in order to make money.
3. There is a random distribution between wins and losses for any given set of variables that defines an edge.
4. An edge is nothing more than an indication of a higher probability of one thing happening over another.
5. Every moment in time is unique.

Have questions, or just want to learn more? Visit us online at www.SimplerTrading.com or call 512-966-2659.