Tips for Traders | 7/27/2009 10:02:00 AM

How Do You Stack up Against Other Traders?

Let's be honest, if you are a trader on your own, trading your account, it is lonely and confusing out there. You are bombarded with advertising claims that assure you “Anyone can be a successful trader,” crazy claims offering to teach you how to “Turn $200 into $27,521 in six months trading forex!” and offers to sell you “Secrets the pros don't want you know!” Unless you have totally isolated yourself from every trading magazine, forum, and Internet site, you are pushed and pulled by all the “Too good to be true” claims.

I've written several articles on MoneyShow.com about realistic expectations, but this topic still remains on the top of my list of concepts I want to cover again when I see a useful example for a new article. This week, one of the students in my one-on-one mentoring program graduated. He will continue to attend group mentoring sessions, but our one-on-one work is finished for now. As a part of the last session, we went over his month-by-month statistical analysis and after we had finished, it dawned on me that if he would allow me to use his numbers, I had a basis for an interesting article. To make this example even more interesting, I approached two of my other students and both agreed to allow me to include their numbers as well. I'll be able to contrast the progress of three very different retail traders for you, and you'll be able to see how their monthly statistics stack up against your own, assuming you keep your own statistics.

You don't keep monthly statistics? If you don't, how do you evaluate your progress at the end of each month? I teach each of my students to have a “shareholders” meeting at the end of each month. They look at the results of their current month and compare and contrast the results with those from prior months. This comparison allows them to:

1. Measure their progress or lack of progress
2. Dig deeper into their trade-by-trade numbers if they see an anomaly in the statistics
3. Make an informed decision about their respective futures as traders. Is there enough progress over some periods of months for them to continue to trade? Traders who consistently lose money are spending a great deal of emotional and monetary capital on a hobby, not a living.
4. Make an informed decision about how much capital to invest in the upcoming month. Should they keep their position size the same or change it? Traders who consistently make money should put in place a position sizing plan to grow the size of their account.

But if you are on your own, with no guidance from an experienced trader or educator you can trust, you may not know what statistics to keep, and once you start keeping them, you may not know what the statistics are telling you. And chances are, you haven't seen any actual monthly statistics from people trying to learn to be consistently profitable. You may have seen the statistics of a professional trader or educator, and while comparing your statistics to them may give you a goal to shoot for, wouldn't it be nice to be able to see how your stats stack up compared to some people in your shoes?

With the generous help of three of my students, let's see if we can offer you a glimpse into the stats of people like you who are trying to be consistently profitable traders. Before I go any further, none of these trading statistics are being presented as “audited results.” They were presented to me by each of my students as actual results and they are meant to be representative of each of the three traders’ progress.

Let's call the first trader Albert. Albert first met me at a Traders Expo, where he took a free educational session sponsored by the CME Group on currency trading. After speaking to me in person, he e-mailed me several times and then attended my Market Maps basic seminar. He has been trading for a bit under two years, and before he took my seminar, his results were mixed. Some months he made money and some months he lost money. His account was not growing, though it was not shrinking by a great deal either. I think it's fair to say that Albert was surviving, but not flourishing as a trader.

Let's look at Albert's monthly statistics:

"Albert" *[Under two years of trading experience with mixed results]*

	Month Two of Mentoring	*Month three of Mentoring*
Total Net Profit	$ 12,788	$ 7,363
Number of Trades	127	143
Winning Percentage	80%	64%
Avg Winning Trade	$ 139	$ 122
Avg Losing Trade	$ 185	$ 71
Largest Winning Trade	$ 316	$ 741
Largest Losing Trade	$ (529)	$ (211)
Actual Risk Reward Ratio	0.75	1.71
Maximum Draw Down	$ (529)	$ (304)

Looking at Albert's monthly numbers after two and three months of one-on-one mentoring gives us a good measure of how his trading is evolving. It generally takes me three or four weeks to get a measure of where a student is, what he or she is capable of, and to identify any major faults in their trading.

As we look at Albert's second month of statistics, keep in mind that he had already taken my Market Maps basic seminar and had spent a good deal of time actively asking questions and showing his charts in the free MarketGeometry.com trading forum and getting constructive comments from the forum members. His trading had already improved a great deal before month two of mentoring, and you can see that he had a nice, profitable trading month.

But there are some obvious flaws in the his second month of trading:

1. His largest losing trade is larger than his largest winning trade
2. His risk/reward ratio is a bit low for my taste, but note that he trades, on average, about six or seven times a day. He also takes quick profits, so the size of his maximum draw down is a real concern. If he isn't playing for a large profit on a regular basis, he cannot allow himself to have a loss this large, unless it was an aberration caused by news or an extremely poor fill by his broker.

Now look at the next month in his statistics. His largest winning trade is considerably larger than his largest losing trade, and that's a very important step forward. He did make a smaller amount of money in month three and his winning percentage was lower as well, but those numbers fluctuate with market conditions and available trading opportunities.

The other big change from month two to month three was his risk/reward ratio, which climbed from 0.75 to 1.71. There are good things going on here! The higher the risk reward ratio, the easier it is to keep trading when you lose a few in a row, because if you hit an “average” winner, it will pay for more than one loser. If your risk actual or realized risk/reward ratio is 3:1, for example, one average-sized win will cover three average-sized losers. I call this “rolling forward” loss coverage—hit a few average-sized winners in a row and you have paid for four, five, or maybe even six losers if you hit a rough patch.

Here's the importance of keeping monthly detailed statistics: If he had merely looked at his net profit, he would have come to the conclusion that the first month was much better than the second month, and in my opinion, nothing could be farther from the truth, even though I do believe in looking at net profits. To become a consistently profitable trader, you have to depend on having a reliable, quality risk/reward ratio, have your maximum losses under control, and have your largest winners consistently larger than your losers. The statistics tell you what you can realistically expect going forward.

Let's look at a trader who is just starting out. Bobby had been trading for about nine months before he read one of my articles on MoneyShow.com. He must have liked what he read, because he e-mailed me, saying he had read every article archived at MoneyShow.com and wanted to know what else he could do to become a consistently profitable trader. We discussed his background and he showed me the results of his nine months of trading on his own. I suggested he either attend the next Market Maps basic seminar, because it would give him a firm foundation in money management and risk/reward ratios, as well as show him a trading methodology he might or might not like. He was currently using three or four indicators and trying to trade ten or eleven cash currency markets using mini-sized cash contracts.

He took the basic seminar and then attended a free Monday Market Maps pre-market live session, which the CME Group sponsors. After the first live session, he signed up for the subscription-based Tuesday through Friday sessions. After attending them for two months, he signed up for group mentoring. Each of these steps gave him a bit more structure to his education.

Looking at Bobby's average monthly trading statistics for his nine months of trading before he read the articles at MoneyShow.com and came over to the forum at MarketGeometry.com, it's pretty easy to tell that he was in serious trouble.

If he had continued trading like this, even though he was winning 53% of the time he made a trade, he would soon lose all of his trading capital, and in fact, his exact words to me when he first started attending the morning sessions was that his trading account was on “life-support.” At this point, after nine months of losing money, he either had to turn things around pretty quickly or stop trading for good.

"Bobby"

[Under one year of trading experience with poor results prior to beginning to study at MarketGeometry.com]

	Monthly Avg Before Studying	*After Two Months in Live Sessions*	*First 4 Weeks of Group Mentoring*
Total Net Profit	$ (1,771)	$ (379)	$ 167
Number of Trades	76	26	25
Winning Percentage	53%	46%	52%
Avg Winning Trade	$ 47	$ 40	$ 62
Avg Losing Trade	$ 102	$ 61	$ 53
Largest Winning Trade	$ 283	$ 169	$ 188
Largest Losing Trade	$ (680)	$ (152)	$ 102
Actual Risk Reward Ratio	-2.15	-1.53	1.17
Maximum Draw Down	$ (1,855)	$ (521)	$ (134)

This is another example of why evaluating your in-depth statistics on a regular basis is so important: If Bobby simply looked at his winning percentage—and right or wrong, that's the number many of you use to gauge your progress—he would scratch his head wondering why he was losing money, because he was making more profitable trades than losing trades, but that does not tell the whole story!

Bobby's largest losing trade was more than twice as large as his largest winning trade, and that's always a sign that a trader is not in control of their losses. His maximum draw down was huge, especially given the size of his average winning trade. The final meaningful statistic was his terrible realized risk/reward ratio: He was losing more than two dollars for every dollar he made! Bobby was right—his account was bleeding to death!

One of the most important concepts I teach in the morning sessions and in the seminars is the simple concept of controlling your losses. I personally have a maximum amount per contract I will risk and as I have written in the past here, before each trade, I write out a check in the air in order to drive home the amount I am considering risking per contract each time I trade. If the size of the check I am writing is larger than my maximum acceptable loss per contract, I simply pass on the trade. You must always be in control of your potential losses!

Looking at Bobby's statistics for the two months of trading after joining the live morning sessions, there are some improvements, but he is still in serious trouble.

The good news is that his largest losing trade is now smaller than his largest winning trade. Note that he also made significantly less trades per month compared to the prior nine months of trading. He now had a trading plan and methodology he was trying to master and he was slowing down and looking for trades that fit the style he was developing.

The bad news is that even though his realized risk/reward ratio had improved, he was still losing 1 1/2 dollars for every dollar he made. His maximum drawdown was still far too large relative to the size of his average winning trade, even though it had come down from $1,855 to $521. He was still losing money and he was still in serious trouble, and while there were glimmers of improvement, if he didn't make some serious changes quickly, his days as a trader would be over.

Bobby decided to sign up for group mentoring, which meets once a week. Traders show their trades, step by step, to the group, and then the group makes suggestions and comments and asks questions. Looking at his trading statistics after four weeks of group mentoring, there's quite an improvement across the board. His realized risk/reward ratio has climbed out of the negative and turned positive. He was now making a little over one dollar for every dollar risked, and though it's still a little low, it is a huge change from his prior trading months! His largest winning trade is better than his largest losing trade and the ratio is improving. His average winning trade is now larger than his average losing trade and he has a winning percentage above 50 percent. All those factors combined to help him make money for the month, a first for his short trading career. But I especially like the change in his maximum drawdown, which fell down to an acceptable $134.

Bobby is not out of the woods, however. This is only one month and he has quite a bit of damage to repair to his trading account. But if he can build on this solid trading month, not just by making money, but also by tightly controlling his risk, he may have turned the corner. When he shared these numbers with the traders at group mentoring, they were all extremely impressed with the turnaround!

Let's look at one more trader. Charlie and I met at a Traders Expo, and when he got home, he read every article of mine that is archived at MoneyShow.com. He then e-mailed me, asking me to accept him into the one-on-one mentoring program. I explained that he would have to take my basic seminar before we could talk about mentoring because he needed to know if my methodology would be interesting to him and the seminar would also give him a solid footing in money management.

Once he had taken the seminar, we began to talk via e-mail and over the phone. Charlie had been trading for about seven years, and he had spent a tremendous amount of money taking seminars, buying courses, and even paying several very high profile educators what I consider to be very large amounts of money for weekend one-on-one sessions. This is a sad case of how throwing money at a problem can be like throwing gasoline on a fire. Charlie had been trading for seven years and hadn't had a winning month—this was a very expensive hobby! I spent lots of time talking to Charlie before deciding to take him on in mentoring, because I didn't want to be part of a large parade of educators taking his money and not doing a thing to help him improve his trading. I was listening to him carefully and trying to decide if he had any character flaws that would prevent him from becoming a consistently profitable trader, and in fact, the more I talked with him, the more intrigued I was! I finally decided to take him in the one-on-one mentoring program once a spot opened up, and after four weeks of mentoring, these are his statistics:

"Charlie"   *[Seven years of trading experience with poor results prior to beginning to study at MarketGeometry.com]*

	2nd Month in Mentoring	*3rd Month in Mentoring*	*4th Month in Mentoring*
Total Net Profit	$ 14,667	$ 13,538	$ 14,741
Number of Trades	70	49	44
Winning Percentage	76%	92%	93%
Avg Winning Trade	$ 323	$ 310	$ 470
Avg Losing Trade	$ 146	$ 103	$ 233
Largest Winning Trade	$ 825	$ 975	$ 1,175
Largest Losing Trade	$ (250)	$ (150)	$ (250)
Actual Risk Reward Ratio	2.21	3.10	2.02
Maximum Draw Down	$ (350)	$ (250)	$ (225)

His first four weeks of trading were profitable, which was a moral victory for him. When he first started mentoring, we talked about what he was trading, what timeframe he was using, and how he set his maximum stops and profit targets. I still remember that in the first mentoring session, he showed me a trade in the e-mini S&Ps, and at one point in the trade, he had over 20 e-mini points of potential profit (that's more than $1000 a contract!) and he ended up making less than $100 on the trade. He also showed me another e-mini S&P trade that risked ten e-mini points ($500 per contract) to make a potential eight e-mini points ($400 per contract). These two trades alone gave me tremendous insight into his problems. He had been taught by several high-profile trading coaches that in order to make money in the markets, you had to keep from getting stopped out by using large stops, regardless of the risk/reward ratio consequences! To me, this is sheer folly! The first thing I had to do was get him to control his losses, in part by using reasonable stop losses. I made him decide on a maximum amount per contract that he would risk and he assured me he would only take trades with initial stop losses under that maximum amount.

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