The Importance of Exit Strategy

By Lance Beggs

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“Simply put, when the edge is gone, get out!”

…Mike Reed, www.TradeStalker.com

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About the Author

Lance Beggs is a full time day-trader with a current preference for emini-futures and forex markets. His style of trading is discretionary, operating in the direction of short-term sentiment within a framework of support and resistance.

As an ex-military helicopter pilot and aviation safety specialist, Lance has an interest in applying the lessons and philosophy of aviation safety to the trading environment, through study in human factors, risk management and crew resource management.

He is the founder and chief contributor to http://www.YourTradingCoach.com, which aims to provide quality trading education and resources with an emphasis on the 'less sexy' but more important aspects of trading – business management, risk management, money management and trading psychology.

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The Importance of Exit Strategy

In June 2008 I published a three-part article series in my newsletter at www.YourTradingCoach.com, titled, "The Importance of Exit Strategy".

It's my belief that this is one of the most important article series I've produced so far. And I'm pleased to see that my readers agree - the positive feedback shows they found great value in this material.

So… to make it a convenient read, here it is in ebook format. I hope you enjoy it.

Article 1 – There is No Perfect Exit Strategy

I was chatting to another trader this morning about exits, and thought it might be time to share my understanding of 'the basics' of exit strategy and exit management.

It really is an area of trading that gets very little attention compared to the other end of the trade – the entry. Go into any forex trading forum and you'll find thread after thread talking about the latest entry method, but very few threads having an intelligent discussion on exits.

It is my belief that your success in trading has more to do with ***how you exit your trades***, than it does with your entry.

Now, in discussing risk management today, we're not going to consider the use of defined-risk options strategies. I believe they're a great technique for risk management in a swing trading or position trading timeframe, but that's perhaps a subject for future articles or videos.

For now, let's consider standard stop loss placement and exit management.

So, what's best?

- Should we use a tight stop loss to cut any losses quickly, or a wide stop loss to allow some room to move?
- How quickly should we move the stop loss to breakeven?
- Should we take profits at a target, or should we let the profits run, perhaps trailing a stop behind the price?

Let's look at some example charts, from the GBP/USD five minute timeframe, although the principles are the same for any market and any timeframe.

In Figure 1 below, let's assume our setup was the moving average cross, and we entered long at the open of the candle after the first green candle. The entry point is marked at 1.9727. At tight stop might be at the point marked S/L 1, just below the green candle. A wider stop might be at position S/L 2, below the recent swing low, and the 1.9700 level. So, is this a good trade? Well, really our profit and loss depends on how we manage our trade and where we exit.

Figure 1

If we took profit at the 1.9750 level, marked as A, due to expectation of a pause at that round number level, then we had a good trade. If we moved the stop loss to breakeven from either S/L 1 or 2 on the initial rally, and got stopped out at position B, then I guess that's a good trade as well, although we have no profits to show for our work. If we hadn't moved our stop loss to breakeven though, we had another opportunity at C for an exit at the 1.9750 level when price stalled there a second time. Once again, a good exit in hindsight. If we didn't take that though, because maybe we've heard that it's best to always let profits run and to trail stops below the swing lows, then maybe we were stopped out at D for a couple of pips loss, as price broke below the lows of B. This is not a great result at all, but at least the loss is small. It's certainly better than the larger loss (after having been in profit for quite a while) that occurs when stopped out at point E, as price hits S/L 1, or at point F as price hits S/L 2.

And of course, in this case if you'd acted out of fear and failed to exit at S/L 2, and held onto your trade hoping, wishing and praying for the market to turn around, you've been rewarded, as an economic news release turns the market and moves it in your favor to much higher profits. And the market actually went quite a bit higher than this.

So what was best stop loss technique in this case? Certainly the gambling approach here – no stop loss at all – but there's no way any serious trader would consider that a valid approach. The market could easily have moved rapidly in the other direction, and possibly will for that trader's next trade, or the one after, taking them a massive step towards ultimate trading failure. For those of us actually interested in risk management, taking profits at a predefined target (in this case the 1.9750 level at point A) was clearly the best result. Trailing stops just did not work. And a tighter stop loss, in this case S/L 1 was clearly better than a wider stop at S/L 2, in minimizing our loss when the market failed to carry through to higher prices.

Let's try another example, shown below as Figure 2. It's the same chart as before. We've just moved slightly forward in time.

Figure 2

This time, we've identified the failure to breach the 1.9750 level on two occasions, followed by the establishment of a lower low. We'll enter short on the break of the lower low, shown in figure 2 at 1.9715. Those employing a tight stop loss might place it at position S/L 1, above the recent green candle and doji. And for those using a wider stop, it might be placed in the vicinity of S/L 2, above the swing highs.

So, what works best here? A wider stop, or a tighter stop? Taking profits at predetermined target levels, or trailing a stop?

In this case, we might have a target of the zeros, 1.9700, which leads to a take profit point marked as A. Good outcome – we've banked a profit. If we prefer to see a bit more of a stall at our target levels, rather than just a touch, then we possibly got out at B as the break below the zeros failed. Still a good outcome – the same result as before, around 10 pips.

If we don't take profits at target points though, but prefer just to trail a stop, then we've either got an exit at position C, D or E, depending on whether the stop loss had been moved to breakeven, or remained still at S/L 1 or S/L 2.

And this time, our gambler has not had luck go their way. Holding the trade past the stop loss, or in fact having no stop loss at all, proved to be a terrible strategy, and possibly the last trade that person ever does depending on how long they held on.

So once again, in this example, a tighter stop loss was clearly better than a wide stop in minimizing risk if the trade turned bad, and taking profits at predetermined price levels was clearly superior to trailing a stop.

But is that always the case? No absolutely not. I simply picked two examples that show this outcome.

(By the way – a little side comment here – all those sales ads showing profitable trades as a reason why you should spend your hard earned dollars on their trading strategy – they've been selected for that ad simply because they show the outcome you want to see – just like I've selected these examples. Don't believe the charts in the ads, as any indication of potential future profitability. With that public service announcement out of the way, let's get back to the article…)

Let's look at a third example.

Figure 3 below shows an entry short on a continuation of momentum downwards, entering short at 1.9672. A tight stop loss may have been placed at S/L 1, just above the long upper shadow. A wider stop may have been placed at S/L 2, above the higher swing high.

Figure 3

In this case, it's irrelevant how wide our stop is, as the trade moves quickly in our expected direction. Taking profits though at our predetermined price target, in this case maybe a stall at the 1.9650 level, in the vicinity of point A, is clearly not the most profitable strategy. Trailing a stop beyond the swing highs would keep us in the market much longer, beyond the edge of this diagram, for a total profit of around 100 pips.

Clearly in this case, trailing stops performed better than a predetermined price target.

One more example, in figure 4, below.

Figure 4

This time, the market has broken down from where price is labeled S/L 2. There is a rally, with two large red candles suggesting a continuation of momentum in the down direction. We enter short following the second large red candle, at 1.9530.

If our strategy was to use a tight stop loss, we might place it in the vicinity of S/L 1, above the recent highs. If our strategy was to use a wider stop, it might be placed above the higher swing high and the start of the downtrend, at S/L 2.

In this case, the tight stop loss takes us out of the market at the upthrust shown by point A. While the wider stop loss at S/L 2 clearly allows us the necessary room to move until the position gets into profit. Taking profits at a predetermined price level, in this case a stall at 1.9500 shown by position B, is again not as profitable as trailing the stop loss lower.

So, this time, a wider stop loss is the better strategy on entry. And for ongoing management of the trade we're better off trailing a stop than exiting at a predetermined profit level.

So what have we learnt from these examples? This is what I've observed:

a. In each case, the profit or loss taken out of the trade was more a result of our chosen stop and exit method, not our entry. For the same entry, there were numerous possible exits, some profitable, some breakeven and some at a loss. This is why I say that, although it's important to identify a high probability entry, it's much more important to focus on the exit.

b. We cannot know, except with hindsight, what will be the most profitable exit strategy for that particular trade. Sometimes a tight stop is best. Sometimes a wider stop is best. And for ongoing management of the trade, sometimes a profit target is best, and sometimes a trailing stop is best.

Ok, so the exit is more important than the entry – that's good.

But there can be no perfect exit strategy that best manages every trade – that's not good.

So what's a trader to do?

We'll follow up later in a continuation of this article, when I discuss the exit principles that I have found work best for me. Till then, no matter where you place your stops, NEVER hold your position as price moves past your stop loss, wishing, hoping and praying for it to come back into profit. That's gambling – it's not trading.

Article 2 – My Exit Beliefs

In part one of this article, we considered a few questions:

- Should we use a tight stop loss to cut any losses quickly, or a wide stop loss to allow some room to move?
- How quickly should we move the stop loss to breakeven?
- Should we take profits at a target, or should we let the profits run, perhaps trailing a stop behind the price?

In attempting to answer these questions we looked at a number of charts, we chose entry criteria, and then looked at possible options for the exit.

And this is what we discovered:

- Firstly, in each case, the profit or loss taken out of the trade was more a result of our chosen stop and exit method, not our entry. For the same entry, there were numerous possible exits, some profitable, some breakeven and some at a loss.
- And secondly, we cannot know, except with hindsight, what will be the most profitable exit strategy for that particular trade.

In other words - the exit is more important than the entry. The exit has more bearing on whether the trade ends in profit, or in loss. But there can be no perfect exit strategy that best manages every trade.

Sometimes we are better off with a wide stop. Sometimes we are better off with a tight stop. And for ongoing management of the trade, sometimes in hindsight the best results would have come from exiting a target price. Other times the best results come from trailing a stop.

So what's a trader to do?

In this part of the article, I'd like to discuss the some of the principles or personal beliefs that I used in formulating an exit plan. Coming up then in part three, we'll examine my exit strategy, and share some advice from great authors and traders who have shaped my current beliefs regarding exits.

As always, don't believe a word I say. This is simply what works for me, based on some of my market beliefs. I'm serious – you need to test everything. If what works for me contradicts or is incompatible with your style of trading, then it probably won't work for you, either technically or psychologically. By all means try it. But journal your trading results, and review them to learn your lessons, retain what works, and discard or improve what's not working.

Enough of that – let's get onto exits.

BELIEF #1 – Fixed rules don't work

At least none that I know of!

I am assuming from some of the email feedback I received over the last week, that people were hoping I was going to present the 'holy grail' exit rule, along the lines of:

- "If the standard deviation of the 14 period average true range (ATR) is less than 2/3 of π times the 3 period ATR, then set the stop at 1.8 ATR, else 2.5 ATR. Now set your stop and walk away."

Sorry folks, that's not how I work. And I'm really sorry if that disappoints you. By all means, test that last rule, but do not trade with it because I really did just make it up. The fact is that I don't know of any objective rule like this that you can apply to ensure you get the best type of exit each time. As we discovered in part one, you CANNOT know which exit would have worked the best, until the trade is history. The good news though is that you don't need a fixed rule like this.

BELIEF #2 – You will never perfect your exit strategy.

Case in point - Larry Connors, co-author of 'Street Smarts' with Linda Bradford Raschke, recalls in that book a retired friend of his who made over $100 million trading futures who stated that his biggest weakness was that he never mastered his exit strategy.

If you haven't mastered your exit strategy, then don't worry – you're in good company.

I haven't mastered mine either, and although I'm still well short of my $100 million, I am comfortable with the imperfection of my exits.

You need to accept imperfection. You need to accept less than ideal results. When you conduct discretionary backtesting, and look at the chart, and say, "I would have exited that one at the minor resistance area here", or "I would have trailed that one." Well, accept that you probably wouldn't have done that. Your live results will not be as good as the charts look in hindsight. But that's fine.

BELIEF #3 – The real damage is psychological, not financial.

The real damage done by taking a large loss is not necessarily the financial damage, but rather the psychological damage. Holding a loss past the stops digs a hole that psychologically is very hard to get out of.

The real damage done by exiting a trade for a small profit and then watching it blast off without you, to what could have been the trade of your life, is not financial – lost opportunity didn't cost you any money. Rather, the real damage is psychological.

The damage through watching a profitable trade turn around and go right through breakeven to exit at the maximum stop is not financial, but psychological.

We are human, so single trade errors will happen. However, the worst mistake of all is allowing poor money or risk management to continue beyond that one trade, eroding our capital and placing us into a large drawdown. The psychological damage here is often overwhelming, and is what will take many novice traders right out of this game.

BELIEF #4 – Your exit strategy must be designed to match your trading psychology.

This is possibly the most important part of exits, in my opinion. If you take nothing else away, at least please consider this belief and see how it relates to your own trading.

Because of the fact that the real damage is psychological, I believe you need to design your exit strategy to best match your trading psychology. This may not necessarily be what produces greatest profits.

Do not optimize for maximum profits. Instead, optimize to ensure compatibility with your trading psychology.

Do you hate missing the big moves, more than anything? Then you need to perhaps consider wider stops, to ensure you're not stopped out before the move, with some form of trailing stop to keep you in the market for the whole move. Of course, this wider stop will come at the cost of a lower winning percentage.

Do you hate seeing a profitable trade turn into a loss? Then you should design your exit strategy to include aggressive movement of your stop to breakeven, or a small profit. Of course, this will come at the expense of being stopped out more often on a retracement, and missing the real move.

You'll see an example in part 3 of this article series when we look at how my exit strategy is designed to fit with my trading psychology.

BELIEF #5 – A good defense is better than a good offense.

Your goal is to ensure the market cannot take you out of the game. You must, before anything else, ensure you survive to trade another day.

There can be five possible outcomes from any trade:

- Large win
- Small win
- Breakeven
- Small loss
- Large loss

The nature of the market is 'uncertainty'. It doesn't matter how certain your analysis is, you are still dealing with probabilities, and you will still face losses.

What can you, as a trader, control?

You have limited control over the profits. Yes, if the market provides a profitable move then your exit strategy determines how much profit you get, however you can't control the size of the move the market offers you. You have to accept whatever the market provides, and just try to take your part out of the move. You have limited control over the profits.

How much you lose though, is totally within your control. If you end up taking a large loss, it's simply because you didn't exit for a smaller loss.

The larger losses are what can take you out of this game. If you ensure you never suffer a larger loss, then you'll get lots of small wins, lots of small losses, lots of breakeven trades, and some big wins, but you should never suffer a big loss, and so you increase the likelihood of surviving to trade another day. We control risk to ensure we do not get big losses.

BELIEF #6 – Different exit styles produce better results in different market conditions

In a choppy sideways market, taking profits at pre-determined price targets will generally over time produce better results than trailing a stop.

In a smoothly trending market with what I call nice flow, a trailing stop will generally over time produce better results than taking profits.

Fairly obvious so far! However I also believe that in a trending market, that trends with a very volatile and choppy price action, once again taking profits at pre-determined price targets on each of the swings will generally over time produce better results than trailing a stop.

So, how does your market move? This should influence your trading style and exit management. And does this still suit your psychological requirements we discussed earlier?

BELIEF #7 – Stop placement involves a trade-off between winning percentage and the ratio of average-win to average-loss

We saw this briefly when we discussed psychology.

When we use stop loss management in to attempt to increase our winning percentage, it often comes at the cost of a smaller average win/loss ratio, through either smaller average wins or larger average losses.

For example, widening your initial stop will increase your percentage of winning trades by giving price more room to move into profit without being stopped out, but this will come at the expense of a larger average loss on those occasions you do get stopped out.

And when we use stop loss management in an attempt to increase our average win/loss ratio, it often comes at the cost of a smaller percentage of winning trades.

For example, tightening up your initial stop will result in your losing trades being smaller in size, and possibly increasing your average win/loss ratio. However, your winning percentage will also be decreased, simply because you will now be stopped out more often.

The same applies when considering targets. It seems very common for people to give trading advice, that you should set your stop and then place a profit target at two times the risk, or three times the risk. By increasing the size of your average wins to 2 or 3 times of the size of your average loss like this, you will automatically incur a reduction in winning percentage. You can't avoid that.

So this brings us back to psychology. What are you more comfortable with, a small percentage of winning trades, but bigger profits when you do win, or a large percentage of winning trades, being happy with smaller wins each time?

I know! You want a large percentage of wins with each one of them being large. Dream on – it just doesn't happen.

BELIEF #8 – Initial stop loss placement should be at a point that says your analysis or timing was wrong.

Keep your stops as tight as you can, but make sure they're beyond the noise of the market. If your analysis and timing was correct, the price should never get to the stop.

So, set stops based on the price action, not just based on how many dollars you are willing to lose. If the price action requires too much dollar risk, then lower your position size to reduce the risk accordingly, or just pass on this trade.

BELIEF #9 – When the edge is gone, get out

You don't need to hold your trade till it stops out. No-one is making you stay in the market. Simply put, if the price is not moving how you expected after entry, then get out. You can always get back in again later if another setup or trigger occurs.

In fact this is a great way to increase the average win to average loss ratio, not by increasing the size of your average win, but by reducing the size of your average loss.

A lot of people won't take trades which offer less than a 2:1 win/loss ratio. I'll accept 1:1 any time, because I aim to not let the trade hit the stop. If price shows the edge is gone, I'm out of there. So my average loss will therefore be less than 1.

So, let's take a short break to allow you to absorb this, and in part 3 we'll continue by reviewing my approach to intraday trading stop management, and then looking at some great advice from traders and trading educators who have played pivotal roles in shaping my exit beliefs.

Article 3 – My Approach to Exits

Welcome back. Based on the information we discussed in parts 1 and 2 of this series; let's now discuss my personal approach to exit management for short-term intraday trades.

The best way to do this is to first consider, what is my goal from trading, how do my chosen markets move, and what psychological needs do I have to satisfy with regards my trade management and exits.

Firstly, what am I trying to achieve with my daytrading?

My ultimate goal is consistent income. I am not swinging for the big home run trades. If I get one, that's great, but it's not the goal.

I trade for income. I accept that not every day will end in profit, but I do aim for each week to end profitably, and certainly every month. So, I can't wait around for the big moves. I trade the small swings, and I look for consistent income.

So, in developing my exit strategy, we need to consider a requirement for consistent income. This means that both a high percentage of winning trades, and tight risk control, are important factors in the design of my exit strategy. To some degree, traders often see these requirements as mutually exclusive. While a higher percentage of winning trades is often achieved by widening stops, this is not possible in my circumstances, where I need to also keep risk as low as possible. I am satisfied though that the nature of my preferred setups, being at areas of support and resistance, generally ensure a higher probability entry. As such, my stops can be placed as tight as market action allows. In addition, in order to minimize risk, no trade can ever be allowed to place my trading career at risk. The average win/loss ratio must be kept under control such that an average loss is easily overcome by one average win. And any individual loss should never be such that it cannot be overcome by one profitable days trading.

How do my markets move?

I had a reader ask recently whether I believe the saying, 'the trend is your friend'?

Well, if that saying is true then I believe it is a very fickle friend indeed. I find trend trading very difficult psychologically, due to the lower winning percentage that trend traders typically have to endure as they get chopped up again and again waiting for the big move.

There's a commonly stated belief that forex markets trend really well. That may be true in longer timeframes, but my experience doesn't agree with that for the short timeframes that I trade.

These markets spend a lot more time in sideways or choppy market action, rather than nicely trending. Of course, when they do trend, it can be a great move.

So, given that is my view of the markets and the timeframes I trade, I need an exit strategy that does not rely on trends developing. Perhaps then, for me, predetermined price targets will be the better strategy.

But what about my psychology? What needs do I have to satisfy, and are they compatible with my goals and my view of the markets?

Firstly, I hate losses, but even more I hate unnecessary losses. So I will immediately take any loss when the system says to exit, in order to ensure the loss is no greater than necessary. Under no circumstances will I accept a lack of discipline on my part leading to a loss greater than the predefined stop loss. So I need a clearly defined exit strategy, and full focus while in a trade to ensure I manage my risk as per my trading plan.

Secondly, there is nothing worse for me than seeing a profitable trade turn into a loss. I'm happy if it retraces and I get out at a small profit. I'm happy if it retraces and I get out at breakeven. But if it's in profit and retraces, and I let it go to a loss, I've failed in my job of managing this trade. So I need to perhaps consider an aggressive movement of the stop to breakeven.

And thirdly, although I would love to catch all large market moves, I'm not too concerned if I don't trade the whole move. I am happy if I've taken consistent small profits out of the trend at each of the high probability entry points.

All three of these psychological requirements are compatible with my goals and view of market direction, as described earlier, pointing to a strategy involving tight risk control, aggressive movement of the stop to breakeven and taking profits at predetermined price targets.

So, having established the general requirements for an exit strategy that meets my goals, my view of the market and my psychological needs, let's look at it in a little more detail.

Initial Stop Loss Management

1. The initial stops must be tight, but beyond any noise, ideally positioned beyond either the swing high/low or entry candle high/low depending on market action. The stop position must be such that if the price gets to that position then the trade setup and/or timing were incorrect, and I really want to be out of the markets. If the market is not flowing well, and there is considerable candle overlap, consider placing the stops a few pips further to allow for a minor test and breach of the stop area by a pip or two.

2. The nature of my entries is that, if valid, they should move very quickly in my expected direction. Therefore, in order to minimize the size of my average loss, I can consider an exit of my position before the fixed stop loss as per the following price action or time based stop rules:

    a. I will exit the trade before the stop loss if price action indicates that my setup may no longer be valid. This includes any significant stalling of price or loss of momentum, or indications of a possible reversal. If price should setup an entry again, I can always re-enter, but it's better to be out of the market waiting for a valid re-entry, than just hoping the current one works.

    b. If in doubt at any stage about the validity of my entry signal, I will exit and reassess, rather than wait for price to hit either the stop or target.

    c. After any reasonable period of time without price achieving a profitable position (usually three candles, but flexible depending on price action), I will consider exiting or tightening the stop if price action allows.

    d. Trades against the direction of the trend are treated more aggressively, with respect to early exit.

Ongoing Exit Management

1. Aggressive movement of the stop to breakeven as soon as price shows a loss of momentum. If price was only slightly into profitability, consider tightening the stop loss towards breakeven if price action allows. Both these actions may result in getting stopped out on a retracement, before price moves in the expected direction. That's fine. I accept that. Having exited, I can objectively reassess the entry setup, and if applicable re-enter the market. And if I don't get a re-entry, and the price moves on without me, I don't mind. I missed this one, but getting out was the right thing to do. The retracement could easily have continued in the opposite direction, stopping me out for a greater loss. I have minimized my risk. I have traded well.

2. Trades against the direction of the trend are treated more aggressively, with respect to early movement of the stop to breakeven.

Multiple Parts

1. Having established requirements for consistent income, my primary exit strategy will be through a predetermined price target. However by trading multiple parts to each trade, I will provide myself greater flexibility.

2. Part one will always operate with a take profit level. The location of the target is flexible, depending on my assessment of price action, but will typically be the next area of minor or major support or resistance.

3. Part two will involve either of the following:

    a. In a smoothly trending market, this part will be managed via a trailing stop, positioned beyond swing highs/lows. It may be moved tighter for any parabolic or impulse moves, to lock in a portion of those extra profits – consider positioning the stop based on smaller timeframe price action.

    b. In a sideways market, or a choppy market (whether trending or not), part two will be exited via a target level, typically the next major support or resistance level. Supposedly the market is not trending around 70% of the time. Therefore this is the default exit method. Trailing stops should only be used when the markets is visibly trending in a very smooth fashion.

4. If price stalls prior to achieving either target, part one may be exited anytime. Part two should be should be given more opportunity to reach its target, or a breakeven exit, however may also be exited if I feel the trade has lost its edge.

News or Economic Releases

1. Prior to any news or economic release in which it is reasonable to expect volatility, consider either closing out trades, or if well in profit then just tightening the stops right up. If extreme volatility is possible (for example during the monthly Non-Farm Payroll release, or any interest rate decision), then part two profit targets may be removed from the market.

That's essentially it. It's quite simple, but has considerable flexibility to allow for discretionary changes based on my feel of the market flow.

I'll repeat a few of the disclaimers already mentioned in other articles. This exit strategy is simply the one I have found most effective for me. It is not necessarily the most profitable. In fact my testing shows slightly better results by just trading part two positions; however it's optimized to suit my psychology which needs these regular profits, no matter how small. I like it, it works for me. There's no guarantee it will suit your style of trading, or in fact will even be profitable for you at all. By all means, take the parts you like and test to see if they fit with your strategy. The key word though is 'test'. Test everything before taking it live.

There are numerous variations on this multiple part approach as well, so adapt that approach as you see fit. And don't just limit your testing to the multiple part exit. Why not also try scaling in, with each part at different prices?

Advice from the Experts

I hope you got value out of that. I'd like to finish up with acknowledging four great traders who have been influential in helping shape my beliefs about trade management and exits, through sharing a couple of exit based quotes from their books or websites:

Larry Williams in "Long Term Secrets to Short Term Trading":

- "Based on my research and experience, I have developed a powerful and profitable belief system: I believe the current trade I am in will be a loser... a big loser at that."
- "Every major loss I have had trading (and I've had more than my fair share) has come from believing my current trade would be a big winner, so I did not follow the rules of the game. Adopt my belief system, that this trade will most likely be a loser, and you sure as heck will protect yourself!"

Mike Reed, from the great articles on his website, and from his book "Read the Greed":

- "Your concern is 'limiting losses'. I care more about this than anything else in trading."
- "Every successful trader I've met has a way of getting out early on bad trades."
- "No matter which route you take, identifying and exiting losers is the key to trading."
- "Never let a gain turn into a loss. This will mean getting out of most trades a little (or a lot) too soon. You just have to live with it. Swing for home runs (greed) will ruin your trading. There is no mechanical formula that I know of, (such as, "move your stop to break even after you get 3 ticks gain") that will work. You have to develop a feel for how the market is acting at the moment, and use your feel to reduce your target or advance your hard stop. This comes with experience."

- "Simply put, when the edge is gone, get out!"

- "Once I enter a trade, I do so because I have an edge, and the clock begins to tick. The trade should begin to go my way very soon. I cannot assume that I'm right and let the market move against me and continue to move against me just because I want to be right. Instead, the market must quickly prove that my entry was correct, and move in my direction, or I assume that I am incorrect, and exit the position. You must assume you are ***incorrect***, and ***exit*** the position. You must assume you are ***incorrect*** until you are proven correct.

Larry Conners and Linda Rashcke, from "Street Smarts":

- "The main goal of each trade is to minimize risk rather than maximize profit."

- "Remember that both in short-term trading and mechanical systems, the distribution of winners is skewed. Most of a month's profits might come from only two or three big trades. Much of the time the individual profits may seem small, but more importantly the losses should be small, too."

- "If you keep your losses to a minimum on every trade, you will have 80 percent of the battle won."

- "Be pleasantly surprised when a windfall occurs, but never be looking for "the big one". The market will decide how much profit to give you. Only you can decide how much to limit your loss."

- "The real skill is in not losing money."

- "Maybe there is no such thing as the perfect exit strategy, but you have to lock in profits when they're there, even if it means getting stopped out of a small reaction. People tend to focus on the one out of 20 times they really did leave money on the table and not look at all the other trades where getting out was the right thing to do."

Happy Trading,

Lance Beggs

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