

Method Trading

A Reasoned Approach to Futures Trading



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Your vision. Our expertise.

A close-up photograph of a man with dark hair and glasses, wearing a dark suit jacket, a light purple shirt, and a patterned tie. He is looking down and to the right with a thoughtful expression, resting his chin on his hand. The background is a blurred, light-colored wall.

Match your trading method to
your goals and personality.

In futures trading, there are winners and losers. Either because of their emotional makeup, or their lack

of knowledge, some traders put themselves in positions from which they can't possibly hope to emerge successfully.

While their motivations may be primarily psychological, some of their failures can be directly attributed to a lack of understanding of

trading techniques. A well-designed trading method is the cornerstone of a disciplined approach to futures trading and there are many successful trading

methodologies. But what works for you doesn't necessarily work for someone else. It's very important that

you develop a trading method that matches your trading goals and personality, because without it, you run the risk of submitting to the temptations and stresses that are constantly present in the market.

Here are a few practical rules that can be applied

to any trading method. They are rules we believe you should integrate into your trading system, so you'll have the best possible chance for success.

“A well designed trading method is the cornerstone of a disciplined approach to futures trading.”

The Rules to Follow

1 ADOPT A DEFINITE TRADING PLAN.

Because of the emotional stress inherent in any speculative situation, you must have a predetermined method of operation that includes a set of rules by which you operate and to which you rigidly adhere, in order to protect you from yourself. Very often your emotions will tell you to do something totally foreign or negative to your market trading plan. It is only by adhering to a preconceived formula that you can resist the emotional temptations and stresses that are constantly present in a speculative situation.

2 IF YOU'RE NOT SURE, DON'T TRADE.

If you're in a trade and feel unsure of yourself, take your loss or protect your profit with a stop. If you are unsure of a position, you will be influenced by a multitude of extraneous and unimportant details and will probably end up taking a loss.

3 BEING RIGHT PART OF THE TIME SHOULD STILL YIELD PROFITS.

In speculating, it would be folly to expect to be right every time. If you have the proper trading techniques, you should be able to cut your losses short and let your profits run so that even being right less than half of the time will show excellent profits. This point is re-emphasized in Rule Four.

4 CUT YOUR LOSSES AND LET YOUR PROFITS RIDE.

The basic failing of most speculators is that they put a limit on their profits and no limit on their losses. A trader hates to admit to being wrong, and will often let losses ride in hopes that eventually the market will turn around. After a while, a trader who is wrong will begin hoping for a small loss and give up hoping for a profit. Human nature also dictates that an individual wants to take profits right away and be "right." There is an old saying, "you never go broke taking a small profit," but you'll certainly never get rich that way.

Small profits are the direct opposite of the best way of making money in speculation. If you are correct when entering a speculative situation, you will know it almost immediately and will show a profit. However, if you are wrong, you will show a loss and you should remove yourself from the situation as quickly as possible.

Taking a small loss does not necessarily mean you were wrong in your thinking. It simply means that your timing was perhaps incorrect and that you should wait for the correct timing and situation to allow you to reenter the market. Remember, in any speculative situation, the market is the final judge. You must let the market tell you when you are wrong and when you are right. If you show a profit, ride it until the market turns around and tells you that you are no longer right, and, at that time, you should get out, but not before! On the other hand, the market will also tell you if you are wrong and it would be a serious mistake to argue with what it is saying.

Market Observations

While the following are not specific trading rules, they are general observations that will aid in formulating an understanding of markets.

1 RETAIN CONTROL OF THE SITUATION AND YOURSELF.

Do not allow your position to control you. It is a mistake to find yourself in a position larger than you can reasonably handle. When this occurs, you will find that the sheer size of the position, rather than the facts of the situation itself, affects your judgment.

2 THE MARKET DOES NOT KNOW THAT YOU OWN IT.

You must remain impersonal in your trading. When you take a position and you are wrong, remember it is better to get out immediately! The market will not feel badly about it if you do, but you will if you don't.

3 THE MARKET ALWAYS LOOKS ITS WORST AT ITS BOTTOM.

It is important to remember that before the market turns around it is at its very worst. Therefore, be prepared to treat each day objectively by not allowing emotional fervor to cloud your judgment.

5 IF YOU CAN'T AFFORD TO LOSE, YOU CAN'T AFFORD TO WIN.

As stated in Rule Four, losing is a natural part of trading. If you are not in a position to accept losses, either psychologically or financially, you have no business trading. In addition, trading should be done only with surplus funds that are not vital to daily expenses.

6 DON'T TRADE TOO MANY MARKETS.

It is difficult enough to successfully trade and understand a specific market. It is next to impossible for an individual, especially a beginner, to be successful in several markets at the same time. The fundamental, technical and psychological information necessary to trade successfully in more than a few markets is more than most individual traders have either the time or the ability to manage.

7 DON'T TRADE A MARKET THAT IS TOO THIN.

A lack of public participation in a market will make it difficult, if not impossible, to liquidate a position at anywhere near the price you want.

8 BE AWARE OF THE TREND.

It is vitally important that you can recognize a strong force in the market, either bullish or bearish, and that when this force is at its height it would be folly to attempt to buck it. However, you must learn to recognize when a trend is about to run its course, or is near exhaustion. If you can learn to recognize the early signs of exhaustion, you will avoid staying in the market too long and will be able to change direction when the trend changes.

9 DON'T ATTEMPT TO BUY THE BOTTOM OR SELL THE TOP.

It simply can't be done unless you have the aid of a crystal ball or some other tool which could be peculiar to the mystic. Be content to wait for the trend to develop and then take advantage of it once it has been established.

10 NEVER ANSWER A MARGIN CALL.

This rule acts as a stop loss when your position has weakened considerably. By dogmatically and arbitrarily adhering to this rule you will be forced to get out of the market before total disaster sets in. It is often difficult to admit you're wrong and get out of the market (which you probably should have done well before you received a margin call). However, the presence of a margin call should act as a final warning that you have let your position go as far as you conceivably can (unless the initial margin is out of line with the volatility of the contract).

11 SELL THE FIRST RALLY OR BUY THE FIRST BREAK.

Generally a market that has just established a trend (either up or down) will have a reaction. Good interim profits can be made by recognizing this reaction and taking advantage of it. For example, in a bull market, the first reaction will generally be met by investors waiting to buy the break. This support generally causes the market to rally. The reverse is true of a bear market.

12 NEVER STRADDLE A LOSS.

A loss by itself is difficult enough to accept; however, to lock in this loss, thus making it necessary for you to be right twice rather than once (which you previously found impossible) is sheer absurdity.

4 EQUITY...EQUITY...EQUITY... NOT CASH.

If another trader is long from 100 points below the market and you are long from the opening that day, you both had the same amount invested in the market from the time both of you were long. Therefore, if the market goes up 10 points you have each gained the same amount. You should not be confused by the fact that someone has taken a position prior to you. You must be concerned with your own situation primarily. Each day start fresh. Your unrealized profits or losses from previous days should not enter into your decision regarding the course of action you will take.

5 TREAT UNREALIZED PROFITS AS IF THEY'RE YOUR OWN MONEY.

They are! Naturally, the opposite also holds true.

Futures trading involves the substantial risk of loss and may not be suitable for all investors.

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