Tim Trush & Julie Lavrin

Introducing

True Money Management

Your guide to financial freedom.

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Successful traders are prepared for the worst possible situation. Unsuccessful traders hope it will not happen. A math formula that will shock you.

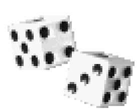
Chapter I: Why do traders fail?

I.1. A shocking experiment

Ralph Vince is a well known financial investor. He performed a very famous experiment known as the Ralph Vince experiment. He took 40 PhD. students and set them up to trade with a computer game. Now, these forty people all had doctorates, but Mr. Vince made sure that none of their doctorates involved any sort of background in mathematical statistics or trading. In the game, they were given $1,000 and 100 trades, with a 60% winning percentage. The rules were simple. When they won, they won the amount of money they risked. When they lost, they lost the amount of money they risked. So, after all 40 students had completed their 100 trades, how many do you think made money?

Only two students out of 40 were able to make money, the other 38 failed to succeed.

Recall: they had 60% winning percentage. I means that they won 6 trades from 10 in average. The odds were in their favour, so why they lost money? Why only two students out of forty were able to win? It doesn't make any sense!

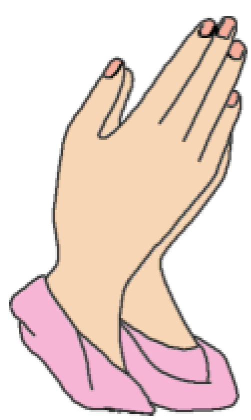


I.2. How a good strategy “fails”

It is not the strategy – it is the trader who fails. That's the truth. The experiment shows that most traders fail even if they are trading a winning trading system. For that reason we had to write this book. We want to give you a clear answer as to why most people fail to make money consistently. Imagine you are one of the students. You bet $100 and win $100. You bet another $100 and win another $100... and you feel rich... And then suddenly you lose $100. You are still laughing: $100 loss is not so big, you are thinking that you will win next time and recover that small loss. But you lose another $100. You become uncertain and since you want to recover your two losses as quickly as possible (it is a normal human behaviour called greed), you bet $200 to get $200. You are praying to win. But what happens if you lose again? You become very angry and you want your money back immediately! This is the worst situation – you let your emotions gain control of your trading decisions. From that point on, you will probably never recover your money back and the chances are that you will blow out the whole account. You will bet more and more in the hope of winning back all that you have lost in one single trade. If that lucky trade makes you rich, then good luck! But please realize that you cannot make a living from trading if you act like a spread gambler. You need to follow strict money management rules to succeed as a trader.

Remember: Unsuccessful traders are risking more money in the hope of recovering losses quickly. Successful traders are doing just the opposite. Greed is your worst enemy.

You will get enlightened after reading the paragraph **II.2. Money Secrets**.



Chapter II: The secrets

II.1. Psychology secrets

We named this chapter “secrets” because a very small proportion of all traders really understand what distinguishes good traders from bad traders. You are probably bombarded with guaranteed money making methods all the time. When someone can't succeed, he thinks that the methods don't work or specifically don't work for him or her. These traders are locked in a vicious circle. And unfortunately, they leave one method and go looking for another one. They are wasting time and energy in searching for the Holy Grail that will make them rich. They think that making a huge amount of money is very hard. What a joke! If you understand the basic psychology of trading, you will be light years ahead of the losing traders. The shortest path to becoming successful is to study your own psychology. We and our students often say that trading is the easiest way to make money. Most people simply can't believe this. If trading were so easy, why are there so many traders not making money? They are studying hard, reading all the newspapers and magazines about trading, they are discussing trading techniques on the forums but still they are not making money. They are all making the same mistake! Some of them are extremely stubborn and they won't accept that it is psychology, discipline and proper money management that distinguishes good traders from bad traders. **Not** economic education or the amount of effort put into trading. Most of our students succeed in just a few months studying our methods. These who succeed have read this book several times. Finally, they have been able to fulfil their dreams. So what's the problem that is causing some traders not to make money?

- *They just won't admit that trading is easy!* Their approach is too complicated because they think that if trading were so easy, there would be more multimillionaires around. But the real multimillionaires have already realised that trading is easy.
- *Greed.* We talked about greed in paragraph I.2. and we will talk of it again in the next paragraph. Greed is your worst enemy, and it lies in your head. Fight it!
- *Some people trust financial advisers for their trading methods.* Most financial advisers give false promises that they will make you rich. They do it for money. The real traders share ideas with you just for fun.
- *Most people follow the crowd.* They are selling dollars because all the traders in the forums are shouting: “SELL THE DOLLAR!” They log on to their platform immediately and sell the dollar. Avoid this! Be yourself!

Remember: The main reason why traders fail is human psychology. Another reason is improper money management.

II.2. Money secrets

What is in reality a trading strategy? A strategy gives you entry and exit points based on some sort of information (charts, indicators, fundamentals, etc.). You know when to enter the market and when to exit. But something is missing here... the strategy doesn't tell you **how much money** you have to risk on any one trade. You need to know how many *minilots*, *lots* or *contracts* to open every time. This is in fact the most important part of a successful trading strategy.

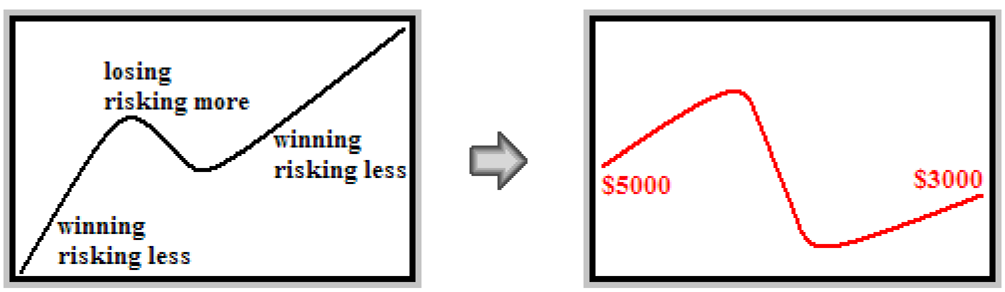
To make things clear, let's talk about Gambler George and Trader Tim. It is important to understand the difference between them, so read carefully.

George is trading because he has heard somewhere that he can make a large amount of money quickly. When George is winning, he stays calm and bets the same amount of money on every trade. When he feels rich, he is afraid of losing his hard earned money. So he bets a smaller amount of money on the next trade. When he is losing, he becomes angry. He bets a larger amount of money to recover the losses quickly. George risks less when he is winning and risks more when he is losing.

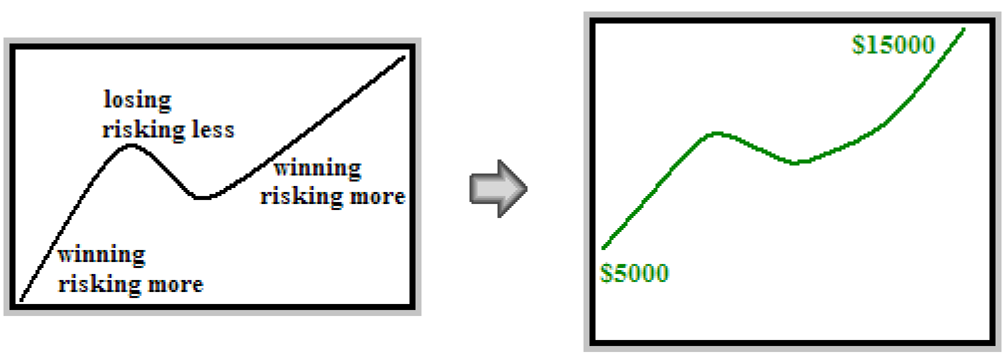
Tim is a serious trader. He makes exactly the opposite decisions. When he is winning, he bets more. When he is losing, he bets less. It sounds really strange and counter-intuitive, so why is he doing this? Because his money management tells him so. He doesn't let his emotions control him and his decisions. He doesn't play like everyman. He acts like a money making machine.

Remember: The world's top traders are trading in this counter-intuitive fashion. They are behaving differently from "normal" people. They are making money consistently and making a nice living.

A winning strategy Account result



George is trading... George lost.



Tim is trading... Tim made a profit.

...they both trade the same strategy!

Chapter III: Achieve exponential earnings and never fail

III.1. Achieve exponential earnings

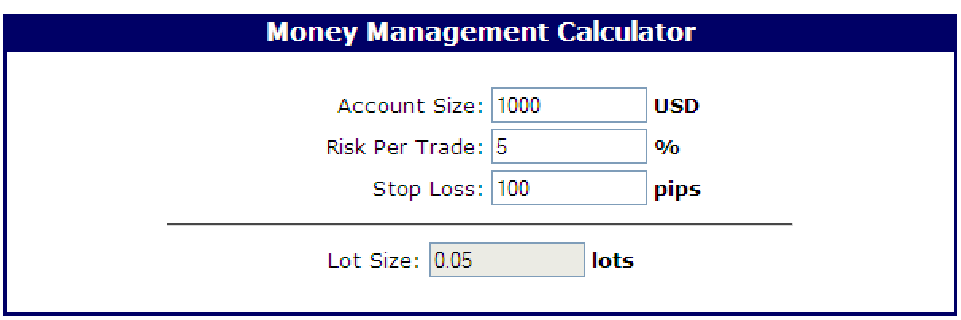
In the last two paragraphs we will discuss the secret formula to achieve exponential growth and completely avoid the risk of your account falling to zero. This is the heart of this book. This is the way that millionaires trade.

a) The basic money management is to risk a constant amount of money. It is recommended to choose 5% of initial account for beginners.

Example: Buy GBP/USD at 2.0000 How big position should I open?		
Example targets (given by a strategy):	Take profit: TP = 2.0100 Stoploss: SL = 1.9950	Reward is 100 pips. Risk is 50 pips.
Initial Account:	$5000	
You want to risk 5%	$250	
How many minilots should I open?		
If you open 1 minilot:	one pip = $1 50 pips = $50 You would risk only $50. The reward would be only $100.	
You need to open 5 minilots:	one pip = $5 50 pips = $250 You will risk exactly $250. The reward will be $500. That's what you wanted.	
Answer: Buy 5 minilots of GBP/USD.		
The formula is:	**Minilots = (5% Account) / (Risk in pips)**	

Tip: Use the Money Management Calculator!

www.truemoneymanagement.com/calculator



Example a) Imagine you are trading a strategy with a 60% winning percentage and let the reward be two times more than the risk. This means that you set up your profit target two times bigger than the stoploss. For example, if you bet $100, you will either get $200, or lose $100. Another example: if you bet $250, you will either get $500, or lose $250. Imagine you are a disciplined trader starting with $5000 and risking $250 on every single trade. The history of twenty trades should look like this:

Trade No.	Account	Risk	WON/LOST	Account
1	$5000	$250	WON $500	$5500
2	$5500	$250	WON $500	$6000
3	$6000	$250	LOST $-250	$5750
4	$5750	$250	WON $500	$6250
5	$6250	$250	LOST $-250	$6000
6	$6000	$250	WON $500	$6500
7	$6500	$250	WON $500	$7000
8	$7000	$250	LOST $-250	$6750
9	$6750	$250	WON $500	$7250
10	$7250	$250	LOST $-250	$7000
11	$7000	$250	WON $500	$7500
12	$7500	$250	WON $500	$8000
13	$8000	$250	LOST $-250	$7750
14	$7750	$250	WON $500	$8250
15	$8250	$250	LOST $-250	$8000
16	$8000	$250	WON $500	$8500
17	$8500	$250	WON $500	$9000
18	$9000	$250	LOST $-250	$8750
19	$8750	$250	WON $500	$9250
20	$9250	$250	LOST $-250	$9000

Your account reached $9000 so you earned $4000 after twenty trades. This kind of money management is widely used by disciplined traders but it has two disadvantages:

- It will **not** make you rich. You will earn a constant sum of money each month. That's the same as being employed. Quite ineffective.
- After ten consecutive losses, you will wipe out a half of your initial account ($2500). After twenty losses you will wipe out the whole account ($5000).

b) Imagine you are trading the same strategy but using another money management system. The advanced money management system is to risk a constant percentage of your current account every time. It is recommended to choose 5% for beginners.

Example b) The history of the same twenty trades would look like this:

Trade No.	Account	Risk 5%	WON/LOST	Account
1	$5000	$250	WON $500	$5500
2	$5500	$275	WON $550	$6050
3	$6050	$302.5	LOST $-302.5	$5747.5
4	$5747.5	$287.38	WON $574.75	$6322.25
5	$6322.25	$316.11	LOST $-316.11	$6006.14
6	$6006.14	$300.31	WON $600.61	$6606.75
7	$6606.75	$330.34	WON $660.68	$7267.43
8	$7267.43	$363.37	LOST $-363.37	$6904.06
9	$6904.06	$345.2	WON $690.41	$7594.46
10	$7594.46	$379.72	LOST $-379.72	$7214.74
11	$7214.74	$360.74	WON $721.47	$7936.21
12	$7936.21	$396.81	WON $793.62	$8729.83
13	$8729.83	$436.49	LOST $-436.49	$8293.34
14	$8293.34	$414.67	WON $829.33	$9122.67
15	$9122.67	$456.13	LOST $-456.13	$8666.54
16	$8666.54	$433.33	WON $866.65	$9533.2
17	$9533.2	$476.66	WON $953.32	$10486.51
18	$10486.51	$524.33	LOST $-524.33	$9962.19
19	$9962.19	$498.11	WON $996.22	$10958.41
20	$10958.41	$547.92	LOST $-547.92	$10410.49

There are several advantages:

- The first thing that you will have noticed is you have earned more. In the previous example you made $9000, now you have made $10,410.
- You are in fact acting like Trader Tim. The smaller the account, the less you risk.
- As your capital grows, you can open larger positions. This leads to exponential growth of your account. As your account reaches $10,000, you risk two times more than $250 (because 5% of $10,000 = $500). As your account reaches $20,000, you risk four times more (because 5% of $20,000 = $1000). It is extremely good to see that making $10,000 dollars costs the same time as making $5000 dollars before. You can double your money every few months. This is the way that new multimillionaires are born!
- The probability of wiping out the whole account tends down to zero. We will cover this topic in the next paragraph.

III.2. Never fail

An example is worth more than 100 words.

Trade No.	Account	Risk 5%	WON/LOST	Account
1	$5000	$250	LOST $-250	$4750
2	$4750	$237.5	LOST $-237.5	$4512.5
3	$4512.5	$225.63	LOST $-225.63	$4286.88
4	$4286.88	$214.34	LOST $-214.34	$4072.53
5	$4072.53	$203.63	LOST $-203.63	$3868.9
6	$3868.9	$193.45	LOST $-193.45	$3675.46
7	$3675.46	$183.77	LOST $-183.77	$3491.69
8	$3491.69	$174.58	LOST $-174.58	$3317.1
9	$3317.1	$165.86	LOST $-165.86	$3151.25
10	$3151.25	$157.56	LOST $-157.56	$2993.68
11	$2993.68	$149.68	LOST $-149.68	$2844
12	$2844	$142.2	LOST $-142.2	$2701.8
13	$2701.8	$135.09	LOST $-135.09	$2566.71
14	$2566.71	$128.34	LOST $-128.34	$2438.37
15	$2438.37	$121.92	LOST $-121.92	$2316.46
16	$2316.46	$115.82	LOST $-115.82	$2200.63
17	$2200.63	$110.03	LOST $-110.03	$2090.6
18	$2090.6	$104.53	LOST $-104.53	$1986.07
19	$1986.07	$99.3	LOST $-99.3	$1886.77
20	$1886.77	$94.34	LOST $-94.34	$1792.43

Imagine the worst possible situation. Ten or twenty consecutive losses in a row. A horrible period of bad luck or poor trading. Ten consecutive losses would probably ruin every beginner. But look what happened to your account using this system. Actually, you have lost less than a half of your account. Look what happened after twenty consecutive losses in a row (an extremely unlikely coincidence). You are still alive!

If you used the basic money management described in paragraph III.1. a), your account would definitely fall to zero (because 5% x 20 losses = 100% account).

The math formula holds good:

$$\text{Account after } n \text{ losses} = A \cdot \left(1 - \frac{p}{100}\right)^n$$

Now you can easily compute what happens after n consecutive losses if you start with account value A.

Examples:

$p = 5, n = 10$	$5000 * (1 - 0.05)^{10} = 5000 * 0.95^{10} = 2993.68$	Here we got the same results as in the table above.
$p = 5, n = 20$	$5000 * (1 - 0.05)^{20} = 5000 * 0.95^{20} = 1792.43$	
$p = 10, n = 10$	$5000 * (1 - 0.10)^{10} = 5000 * 0.90^{10} = 1743.39$	

The last example shows us what happened after ten losses if you risked 10% instead of 5%. You are still alive. Some very advanced traders risk 10% or far more. Since they risk more and get more, they achieve amazing results in the trading competitions (e. g. World Cup Championship®). This is their secret.

Remember: Successful traders are prepared for the worst possible situation. Unsuccessful traders hope it will never happen.

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Happy Trading!

Risk disclaimer:

Trading foreign exchange on margin carries a high level of risk, and may not be suitable for all investors. The high degree of leverage can work against you as well as for you. Before deciding to invest in foreign exchange you should carefully consider your investment objectives, level of experience, and risk appetite. The possibility exists that you could sustain a loss of some or all of your initial investment and therefore you should not invest money that you cannot afford to lose.

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