What is your Trade Plan?

In many ways, a trade plan is a business plan. It should outline what your plan for winning the stock market game and how you are going to accomplish it. Every trade plan is a little different, so there's not one template that will work for everyone. Consider the following six items when constructing your trade plan. You must write a ½ page on the subject (due Feb. 20).

1. The products you will trade
2. The trading strategies you will use
3. How much money you'll invest in each trade
4. Your loss thresholds
5. How you'll make your investment decisions
6. Trading resources you rely upon and time allocation

Keep in mind, your trade plan doesn't have to be complicated. However, it should allow you to manage and track these key items. Crafting a plan that is too complicated will mean that you won't use it.

Most importantly, your plan should be a work in progress. As you refine your approach add detail to your plan over time.

Be Realistic

One of the prime benefits of a trade plan is that it allows you to realistically evaluate your trades.

To be a successful trader, you need to establish reasonable expectations for risk and reward. Your risk expectations, in particular, should be very clear. Don't minimize the importance of risk evaluation. Recognize also that your performance will be impacted by the action of the overall market.
Lastly, be realistic about your success rate on individual trades. It's impossible to be profitable on every trade.

Keep Emotions in Check

As most every experienced trader will tell you, learning to control your emotions is key to success. Having a trade plan is great for this, because it provides the structure for making decisions based on discipline, not emotion.

Remember, trading involves losses. The goal is not to win on every trade, but to have more profitable trades than unprofitable trades, or to make more on your winners than you lose on your losers. When you allow your emotions to control your trading, you're more likely to make bad decisions.

Here are two guidelines to consider for your trade plan that can help you rely on discipline, not emotion:

- Avoid increasing the size of your trades to try to gain back your losses sooner—in most cases, you should do the opposite.
- Avoid letting margin requirements drive your decisions and refrain from using up all of your buying power.

The Beauty of Simplicity

For most trade plans, simple strategies typically make the most sense—complex strategies can have unintended consequences if you don't fully understand the dynamics involved.

To be a successful trader, you have to develop a strategy that you understand and that you believe gives you the best chance at success. Don't allow anyone to talk you into strategies, markets or products that you don't understand.

Keeping things simple doesn't mean being lazy. One of the biggest mistakes you can make is quickly acting on the recommendations of trading "experts". Every trader has a different personality, different goals, different expectations and a different tolerance for risk. What works for one trader may not work for another.

Once you have a built an approach that works for you, maintain a constant state of learning. See how other approaches might compliment your plan. Test, learn, apply, and evaluate.

A Plan to Live By

We close with these basic, common-sense suggestions to consider weaving into your trade plan:

- If a stock moves against you and you wouldn't buy it at the today's price, consider selling it.
- No matter what happens, the market does not "owe" you anything.
- The market doesn't know and doesn't care what you paid for a particular stock.
- The market can remain irrational a lot longer than your capital can hold out.
- Learn from your mistakes.
- When in doubt, wait it out. In other words, if you're not sure what trade to make, don't trade.
- Don't let an unrealized gain become a realized loss—use available tools to manage risk
- Capital management and limiting your losses are of paramount importance.
- Define your profit-and-loss targets before you establish a position.
- Cut your losses and hold on to your winning stocks.
- Have a methodology for determining how much risk you're willing to take on each trade.

Remember, sticking to your trade plan can help bring discipline to your trading.