



Brainy's Articles on Share Trading

Trading practise Back Testing and Paper Trading

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Introduction

If you had some losses in the share market, have you thought about how often you could afford to have the losses? What about consecutive losses? And how much money can you afford to lose?

You can increase your chances of success in share trading by making sure you have a *trading strategy* written down, and that you have done some *back testing* and/or *paper trading*. In this article in Brainy's series on Share Trading (number ST-3100), we take a look at these two techniques, and the pros and cons of having a "practise" at share trading before we actually do it for real.

Overview

Consider these facts:-

FACT#1:- Rushing in? — Many of the people who start out trading in shares rush into it and lose money — reputedly at least 80% of those who start, but some research shows as many as 95% lose money.

FACT#2:- Consecutive losses. — It is possible to trade shares, and to have as many as ten losing trades in a row. If you were to risk more than 10% of your capital in every trade, and then have ten consecutive losses, your available capital will be reduced to NIL!! Could you afford this? And what would you do then?

FACT#3:- Cut losses early (unintentional risk-taking is dangerous). — Many of the people who jump into share trading take excessive risks because they don't understand simple money management and risk mitigation techniques. This includes the need to cut losses quickly to keep them to a minimum, and to let profits run. Then with the value of the profits out-weighting the value of the losses, it should be possible to come out ahead.

FACT#4:- How to minimise losses? — There are some simple and effective ways to minimise the risks of share trading, and to minimise any losses, and maximise any profits. But the concepts and techniques need to be learned. It is not wise to simply "*learn them the hard way*".

FACT#5:- Psychology, fear and greed. — Without doubt, psychology plays a very important part in profitable share trading. If we can get a handle on the psychological aspect, and understand the emotions of fear and greed that tend to drive the market, then we can be in control of our emotions. Without this understanding, we might be heading down the road to ruin.

To increase your chances of success with share trading, it is important to have a clear idea of the market situation that needs to occur for you to place an order to buy, and an order to sell. That is, a *trading strategy*. The idea of trading strategies, and some samples, are included in other Articles in this series on Share Trading (see Chapter 6, "Trading Strategies").

Once you have a *trading strategy*, it needs to be tested to give you confidence of its likely success. Two of the techniques that can be used are known as *Back Testing* and *Paper Trading* and they are explored in the following pages.



Figure 1: How often can you afford to have losses?

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