The Market is Always Right
The 10 Principles of Trading Any Market
By Thomas A. McCafferty

Introduction

Trading is a stressful profession. You have to make quick decisions about whether to cut your losses or wait for the stock market to turn in your favor. Even though technology and information have helped traders to improve the odds, a trader's success or failure can still be determined by the trader's basic human nature.

The Market is Always Right provides you with an understanding of the trader's mind and emotions and how they can be powerful tools in the management of the markets. It explains how experienced traders control their emotions while trading, which is a must during both good and bad times. This book shows the trader how to deal with their emotions, manage their stress levels, increase their knowledge, and improve their confidence when making trades so that they can maintain control in any market.

Thomas A. McCafferty has been involved in the cash, commodity, futures, options, and securities markets for thirty years. He has developed his years of experience by supervising brokers in the industry and trading for his own account. As a branch office manager for the Securities Corporation of Iowa, he was registered as a futures broker, securities broker, securities and option principal, and insurance broker. He has also written several books on investing and the markets, including Winning with Managed Futures, All About Options, and Understanding Hedged Scale Trading.

Overview

The Market is Always Right is divided into ten chapters, each of which covers a basic principle in trading the markets:

1. The market is always right – A trader must follow the will of the market or risk losing everything.
2. It’s all in your head – You have to learn how to trade, know your limits, follow your instincts, and stay disciplined.
3. You can’t prepare enough – Trading is a serious business, so make sure that you develop good habits, use the tools that exist to your advantage, and develop a trading plan.
4. Supply and demand rule the markets – Understand the rules of supply and demand, make use of trends, and sell into strength.
5. Commit your thoughts to paper – Develop a written trading plan so that you can focus on your objectives and set realistic goals.
6. Developing and perfecting your trading shtick – Find an approach to trading that works for you, look for trading opportunities, and make sure that you are prepared for the opportunities when they arrive.
7. Enhancing your shtick – Find ways to improve upon your trading approach, make sure that you have the tools to make the trades, and work with a mentor to help you improve your trading skills.
8. Dealing with one of the toughest parts of the game: discipline – Learn the rules and create a system to force yourself to follow those rules, find the right time to trade, learn to anticipate the market, and maintain your focus.
9. Staying the course – Preserve your capital to take advantage of real opportunities, learn how to survive by managing your losses, and maintain your focus.
10. On becoming the ideal trader – Reinvent yourself as the ideal trader, understand the seven deadly sins that prevent traders from achieving their goals, and learn about your inner self.

The Market is Always Right

The first law of trading: Accept the fact that the market is always right. As a trader, you must learn to bend your will to the market; when you attempt to fight the market, you risk disaster. The combination of all buyers and sellers – and not the individual trader – determines the value of a stock being bought or sold. If the market is moving against your position, then you have to either get out of its way (i.e., sell the losing stock) or risk losing everything you invested.

How do you deal with this fact? Determine what amount of money you are willing to risk on a specific trade (e.g., a specific dollar amount, a percentage of the investment). This allows you to cut your losses when your limit has been reached. This strategy will prevent you from tying up capital that can be applied to winning trades or wiping out your existing capital. You can always buy the stock again at a lower price if it has value.

Note that investing and trading are not the same; do not approach trades with an investor's mentality. Investors are concerned with long-term growth and wealth; traders should be concerned with short-term returns and income.

Knowing that the market is always right means that you have respect for the market. This means understanding the mechanics of trading, doing your research before you trade, taking your profits when the time is right, and limiting your losses before they go too far.

It's All in Your Head

In order to trade, you must **learn** to trade. Trading is a business – run it like a business. You need to take courses at a trading school, purchase the proper equipment, pay the necessary fees (e.g., a seat charge for trading on a trading floor, monthly fees for using trading software from home), and spend the time required **actually making trades** in order to become an accomplished trader.

You must have a passion for trading. This means reading at least one book a month on trading, reading <u>The Wall Street Journal</u> the first thing in the morning, watching <u>Wall Street Week</u> in the evening, and making trading a very central part of your life.

There are several ways to mentally and emotionally prepare you to trade. Find a trading level and style with which you are comfortable. Accept the fact that losses are going to happen. Maintain a positive attitude when trading; fear and doubt can hurt your trading ability (i.e., if you are afraid to lose money on a trade, or you are not confident about when to get out of a trade, then you are letting fear and doubt affect your trading success). You can increase your confidence by decreasing the size of your trades so that the risk is lower. Take responsibility for your own trades; do not rely on anyone else's tips (except for the advice of your mentor). When you have had enough, walk away until you are ready to resume trading. Pace yourself (i.e., do not make too many trades) when you are doing well.

Analyze and make each trade based on the rules that you set (e.g., Are you going to trade from home or on a professional trading floor? Will you trade a thin or thick market?). Learn to develop and follow your trading instincts (this can only come from the experience of actually trading).

You Can't Prepare Enough

As a trader, you must become as diligent and methodical in your preparations for a trading day as the sniper planning for a mission. To survive in the trading world, you must get an edge on the markets. This means that the trader must develop a daily ritual, which may include listening to Bloomberg radio updates in the morning, reviewing and updating key leading indicators throughout the day, and preparing a trading plan for the day.

Being prepared to trade means having access to, and knowing how to interpret, the data provided by the market. Technical analysis is the trader's primary tool because it provides immediate feedback on the markets. Charts (e.g., price charts) represent actual trading activity and provide trading signals, allowing the trader to make quick decisions. Determine the mood of the market based on your analysis, and then make trades based on what you observe on the charts. Set up the stock to trade, calculate the risk-reward ratios, enter the trade, exit your position as soon as the stock reaches the profit target or stop-loss price, and then evaluate your performance.