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TODD HARRISON

The ten trading commandments

Commentary: Rules learned from a career of successes - and mistakes

By Todd Harrison
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Fight? No, not yet. Not until me and Harvey get the rules straightened out. -- Butch Cassidy

NEW YORK (MarketWatch) -- I remember why I wanted to be a trader. I figured that the easiest way to make money was to stand near the cash register.

Of course, as I discovered through my 16-year career, there's a reason why consistent producers get paid the big bucks. Flashy bets and big swings sometimes connect but, in the end, a disciplined approach pays the bills.

I've tripped plenty through the years, the types of missteps that almost cost me my livelihood. But I preserved, climbed the ladder and morphed those mistakes into valuable lessons. First as a vice-president at Morgan Stanley, then as a managing director at the Galleon Group and, finally, as president of Cramer Berkowitz. My approach wasn't always constant but, in the end, certain rules allowed me to stay in the game.

These are those rules.

1. Respect the price action but never defer to it. The action (or "eyes") is a valuable tool when trading but if you defer to the flickering ticks, stocks would be "better" up and "worse" down and that's a losing proposition. This is a particularly pertinent point as headlines of new highs serve as sexy sirens for those on the sidelines.
2. Discipline trumps conviction. No matter how strongly you feel on a given position, you must defer to the principles of discipline when trading. Always try to define your risk and, above all, never believe that you're smarter than the market.
3. Opportunities are made up easier than losses. It's not necessary to play every move, it's only necessary to have a high winning percentage on the trades you choose to make. Sometimes the ability not to trade is as important as trading ability.
4. Emotion is the enemy when trading. Emotional decisions always have a way of coming back to haunt you. If you're personally attached to a position, your decision making process will be flawed. It's that simple.
5. Zig when others zag. Sell hope, buy despair and take the other side of emotional disconnects in the context of controlled risk. If you can't find the sheep in the herd, chances are that you're it.
6. Adapt your style to the market At various junctures, different investment approaches are warranted and applying the right methodology is half the battle. Identify your time horizon and employ a risk profile that allows the market to work for you.
7. Maximize your reward relative to your risk If you're patient and pick your spots, edges will emerge that provide an advantageous risk/reward. Proactive patience is a virtue.
8. Perception is reality in the marketplace. Identifying the prevalent psychology is a necessary process when trading. It's not "what is," it's what's perceived to be that dictates supply and demand.
9. When unsure, trade "in between" Your risk profile should always be an extension of your thought process. If you're unsure, trade smaller, or paper trade, until your identify your comfort zone. Trading "feel" is cyclical and any professional worth his or her salt must endure slumps.
10. Don't let your bad trades turn into investments. Rationalization has no place in trading. If you put a position on for a catalyst and it passes, take the risk off win or lose.

There are obviously many more rules, but I've found these to be the common thread through the years. Each of you has a unique risk profile and time horizon, so some of these commandments may not apply. As always, I share these thoughts with the hopes that it adds value to your process. Find a style that works for you and always allow for a margin of error. No approach is failsafe.

If there wasn't risk in this profession, it would be called "winning," not trading.

Good luck today.

Todd Harrison is the founder and CEO of Minyanville.

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