A Beginner's Guide to Day Trading

Learn the basics of day trading with this informative guide outlining the techniques and psychology involved, as well as how to manage risks

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WHAT'S INSIDE

The rise of day trading.......4

What is day trading?.......4
The benefits and risks.......5
How to get started.......6

The technical basis of day trading.......7

Technical versus fundamental analysis.......7
The basics techniques.......8

The basics underpinning a day trading strategy.......14

Finding the right asset classes.......14
Risk management.......15
Using a stop loss order.......16

The psychology behind trading and a pro's trading know how.......19

Top five tips for trading in the zone.......20
Charlie Burton's view.......20
Day trading strategy examples.......24

Day trading can be one of the most exciting careers you can have. Over the course of a single trading day you trust in your abilities to spot buying and selling opportunities in various asset classes to potentially make a profit. There is a thrill to developing a trading strategy through research and analysis and potentially seeing all that hard work pay off.

Day trading allows you to be your own boss, but to enjoy that freedom a great deal of research, commitment and importantly discipline is needed. No longer will you have to answer to managers as you sit at home making decisions that are yours and yours alone. But day trading, and the inherent risk, isn't for everyone. Even those willing to forge ahead and put their own cash on the line must carefully consider many crucial areas beforehand and a create a rigorous strategy that must then be adhered to.

From looking back at the history of day trading, to who does it, why they do it and most importantly how, we will explain some of the key factors to consider when starting out and provide you with insights on technical price analysis.

The guide will cover some different strategies that can be adopted, how to manage risk, how to know when to close a trade and what you can do to better understand the psychology behind trading to help you "trade in the zone".

We will even, thanks to the help of an expert day trader, give you a glimpse at how you could choose to set up your trading desk – from the number of screens you need to what music might get you in the best trading mood.

We hope that by the end of this guide you will have acquired the basic tools and knowledge needed to begin trading your way.

THE RISE OF DAY TRADING

The instantaneous trades executed by complex algorithms are a far cry from the humble beginnings of day trading

TICKER TAPE MAY make you think of huge parades, as soldiers, politicians or festival floats are engulfed in a flurry of torn paper gleefully cast from open windows lining city streets. But the humble ticker tape once fulfilled an important role in prompting an important shift in the narrative of trading.

In 1867, many decades before computers and the internet, the creation of the first telegraphic ticker tape machine helped traders and brokers communicate information about transactions on the New York Stock Exchange floor, while ticker tape became the catalyst for day trading. But how exactly did this newly established system encourage this way of trading?

What is day trading?

A day trader buys and sells a security looking to profit from any price changes during a single trading day. They most commonly aim to trade easy to sell stocks, indices, commodities or currencies in stock exchange and foreign exchange markets – either with their own cash or borrowed.

A trader can buy stocks in anticipation of being able to sell them at a higher price at a later point. Or through short selling a trader can borrow a stock to sell before buying it back and returning it to the original lender. In this instance, the trader is betting that the share price will drop after it is sold so that it can bought back at a lower price and the difference can be pocketed.

In order to anticipate price changes, no matter how big or small, traders utilise a range technical analysis and chart reading to look at past price action. Traders will also carefully monitor scheduled market announcements such as company financial updates, economic statistics (such as the highly anticipated non-farm payrolls) and interest rate changes. The reason for this is they are hunting for momentum. They need price movement and these scenarios

typically result in price moving.

Traders will use all this information to predict how markets and prices will react to such news and which stocks might offer big returns. A stock that moves up and down a lot – a volatile stock – is ideal for profitable day trading. It is about making quick decisions to take advantage of those swings.

Alternative intraday strategies include the exotically named scalping, which involves making a large number of trades a day trying to profit from very small price movements, or the somewhat controversial high-frequency trading that uses algorithms to make high volumes of trades rapidly to capitalise on fluctuations caused by positions taken by large institutions.

The benefits and risks

Typically, a trader will use online trading platforms to make their trades throughout the day, the number of which is dependent on their particular strategy. The trader will then close their positions before the markets close ready to implement their strategy again the next day, ideally after a good night's sleep dreaming of the profits they have just made. Another benefit of day trading is that it can be done remotely. Many do it from their own homes.

Day trading has the advantage over regular investing in that a trader will not own a stock overnight, which means they are not exposed to sudden swings in prices because of some unexpected and off-diary event like the collapse of a business or a tweet from Donald Trump or Elon Musk. Everything is contained within the times you are invested in the market, which allows you to keep complete control over your strategy.

But day trading isn't for everybody, as you need to have a good understanding of how markets work before you begin. It also needs a huge amount of determination and mental toughness to shake off the trades that don't work and cost money. You should only trade if you think you can handle the regular losses on the path to hopefully becoming a successful trader. If not then stay away.

Day trading software

When sat at their trading desk day traders will need to be able to log in to an electronic communication network that allows them to access information, such as bid and ask quotes for securities, and be able to automatically match and execute orders. There are various applications which allow them to connect directly with brokers to make immediate or automatic executions of trades, but if you'd prefer not to, there are some options that aim to help avoid paying commission to brokers.

Traders will also need to have software which can help them analyse stock or currency patterns, charting software and products that include news on stories that might impact their positions or strategy.

Another must have for traders is portfolio tracking software. This can be used to look at previous trades, identify mistakes and improve strategy. Market scanning software will allow help by flagging potential trading opportunities.

Back testing software can also be used to

Successful Traders

Paul Tudor Jones

The billionaire trader and investor made his fortune shorting the 1987 stock market crash. He forecast that people would buy index puts to lower their portfolio risk, thus driving the market down even lower. On Black Monday (19 October) he reportedly tripled his capital from short positions on stocks.

Day Trading Statistics

According to a 2018 report from BrokerNotes there are

13.9 million

online traders globally

Roughly one in seven traders is female – a total of 2.7 million worldwide

gauge how a strategy would have fared in past market conditions, allowing traders to perfect future moves.

Mobile trading software in the forms of apps are becoming more popular. They are useful tools when on the move offering market updates, trends and stock price. But, some currently question their capabilities and services compared to more established desktop applications.

How to get started

If you are ready to start trading you need to consider the markets and securities in which you are most interested. Typically it's best to get good at a few specific instruments, likely from the same category. Such as US indices or a few specific FX currencies. An individual will also have to consider how much money they can afford to trade with – and potentially lose – and how much time they have to focus on the activity.

You need to decide on a strategy – which we will talk about in later chapters – and invest in the necessary software. Do your research, go to trader conferences and talks (such as those organised by Opto) and join trader social networks to exchange ideas and information.

While day traders can trade in individual company stocks, whole indices such as the FTSE 100, commodities and currencies are good starting points for beginners. Remember, consider the volatility of a security or market. Although more swings in prices may make a security or market better to trade with more volatile price moves also increase risk.

THE TECHNICAL BASIS OF DAY TRADING

Day trading requires the ability to understand and analyse charts – here are some of the basic techniques

THERE ARE TWO core analysis types that traders typically partake in. The first of these, fundamental analysis, as the name may suggest involves focusing on how a company's fundamentals — revenues, earnings, assets and liabilities. The trader will look at a company's book and its potential future returns, then assess if the current price is overvalued or undervalued as an indicator as to whether it is a good investment. Ultimately, a trader can try to use this information to measure a stock's intrinsic value as well as predict market performance.

Then there is technical analysis. Technical analysis is the evaluation of a financial asset through the study of historical market statistics, such as price movement and volume and chart patterns, to give indications of market sentiment.

Some analysts specialise in technical analysis, while others favour purely fundamental analysis and some even consider both. It is up to the individual trader to choose which they lean on more heavily, but ultimately, the information gleaned from either approach will prove useful when trading

In day trading, however, technical analysis is often used more, as fundamentals become less important when trading intra-day price action. Fundamentals typically come through on longer-term trends and are therefore well suited to longer-term trading/investing.

Technical analysis involves analysing patterns and spotting trends in historical trading data such as price movements and volume. This allows a trader to decide the best buying and selling opportunities in a chosen market and to determine the best

time to enter or exit a trade.

There are three core theories in technical analysis: that everything a trader needs to know about a security can be found in its price, that market prices move in trends rather than erratically, and that these trends tend to be repeated in cycles.

The basics of technical analysis

Don't be surprised if you get called a chartist when someone learns you're interested in technical analysis. Creating, maintaining and understanding charts, is after all at the heart of this method.

You can plot the information of a security's past price changes on a chart to determine and evaluate how it changes over time. When used well a chart can provide an indication of future price performance, allowing a trader to time their entry or exit from a given market, as well as helping them determine where it is best to place a stop loss (See 'using a stop loss order' in chapter three).

HERE ARE THREE BASIC TECHNICAL ANALYSIS TECHNIQUES TO START IMPROVING YOUR SKILLS:

1 UNDERSTANDING CANDLESTICK CHARTS

While there are numerous charts and ways of charting a stock's performance – from simple line charts to mountain charts, to much more advanced examples such as a renko chart – one popular and but highly effective way to chart daily price movements is using a candlestick chart.

A candlestick chart is composed of a series of candlesticks – symbols that show the distance between the opening and closing prices of a security, the daily range of a stock, and sentiment.

The colour of each candlestick is important, as it indicates the direction of the market. A green or white body will show that a security has increased from a previous

How to time your trade entry using trend lines:

According to CMC Markets, there are two rules that can be applied to trend lines and channels when day trading:

1. Declines in price that approach an uptrend line, or price rises that approach a downtrend line, can be good opportunities to initiate positions in the same direction as the trend line.

2. The penetration of an uptrend line, particularly on a closing basis, is a sell signal, and the breakout of a downtrend line is a buy signal. Normally, analysts apply a minimum percentage price move (1% breach on a stock for example) through the line or a full candle close on a significant time frame, such as an hourly candle, to cement the move. The trader needs to hold the break, or it can reverse sharply if they can't follow through.

FIG. 1: UNDERSTANDING CANDLESTICKS

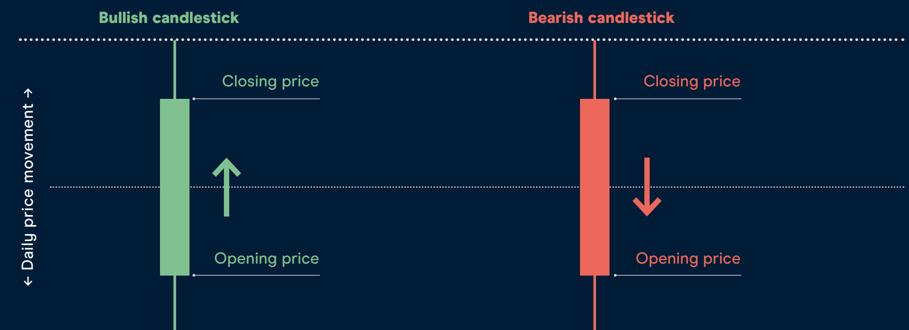


FIG. 2: UNDERSTANDING DOJIS

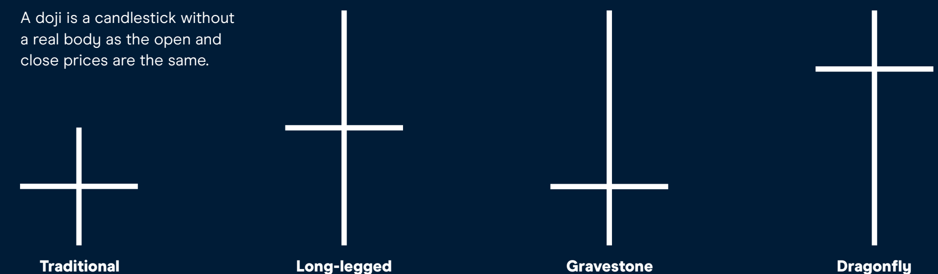
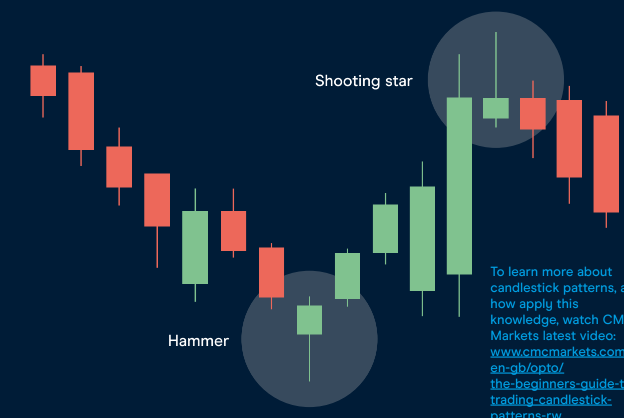


FIG. 3: A HAMMER AND SHOOTING STAR

In this example of a hammer, the long wick on the hammer candle (left circle) shows where price tried to test lower levels, but strong buying came into the market. This increases the likelihood of further bullish candles (upward price movement).

The shooting star formation (right circle) is like an inverted hammer, but occurs in an uptrend. A shooting star can indicate a bearish reversal is about to happen as price tried but failed when testing higher levels.



To learn more about candlestick patterns, and how apply this knowledge, watch CMC Markets latest video: www.cmcmarkets.com/en-gb/opto/the-beginners-guide-to-trading-candlestick-patterns-rw

period of time (a bullish candle), while a red or black body signifies that the price has decreased (a bearish candle) – see figure 1.

The base of the body of a bullish candlestick will show the opening price of a security, and
the top the closing price. The reverse is true on a bearish candle, wherein the top of the candlesticks body indicates the open price and the base the closing price

The wicks, both top and bottom, indicate the range of price movement during the day. Longer wicks can indicate rejection of a price level, as the price throughout the day has been pushed much higher or lower before settling.

An important candlestick form is a called doji, a hammer or a shooting star. See fig. 2/3.

Candlesticks can be useful alongside a number of other technical analysis techniques to help a trader notice patterns that can be used to determine the short-term direction of a security's price. Using this knowledge alongside a number of other charting techniques determine the best time to enter or exit a trade. They also indicate market opportunities, as they can flag to a trader the balance between buying and selling pressures and market indecision.

By using this knowledge alongside a number of other charting techniques, a trader can begin to notice patterns that can be used to determine the short-term direction of a security's price.

2 CHART ANALYSIS: UPTRENDS AND DOWNTRENDS

In an uptrend, a price will reach higher highs than previously, and when the price drops again, the lows will be higher than previous lows. Conversely, in a downtrend, a price will reach lower highs than previously, while it also reaches lower lows.

Whenever there are two data points on a chart a trend line can be drawn. This could be done by connecting one high to the next, for

How candlestick patterns indicate price direction

There are numerous candlestick patterns that can be used to indicate different market movements. Here, are a couple common ones.

Bearish/bullish engulfing
Engulfing patterns consist of two candles, with the body of the second extending past that of the first. They are used for identifying trend exhaustion and possible reversal. (fig. 4)

Rising/falling wedge
Wedges are multiple candlestick formations that involve extended durations. They indicate a tightening of support and resistance lines, where these lines tend to converge. They are useful for identifying the continuation of a prevailing longer-term trend and when a price might break through a support or resistance level. (fig. 5)

FIG. 4: BULLISH ENGULFING

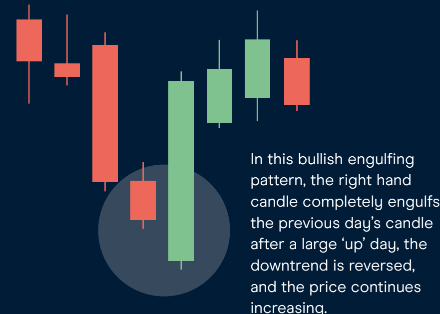


FIG. 5: FALLING WEDGE

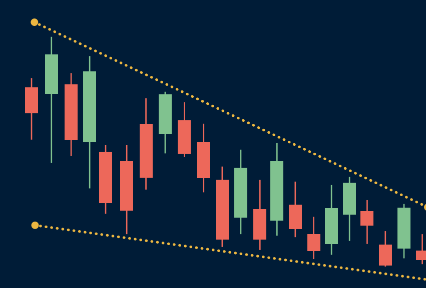


FIG. 6: UPTRENDS

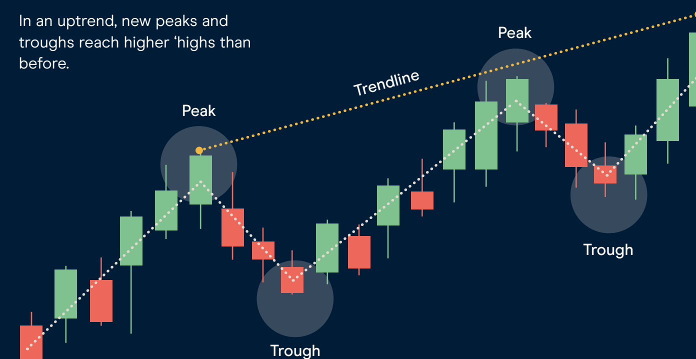
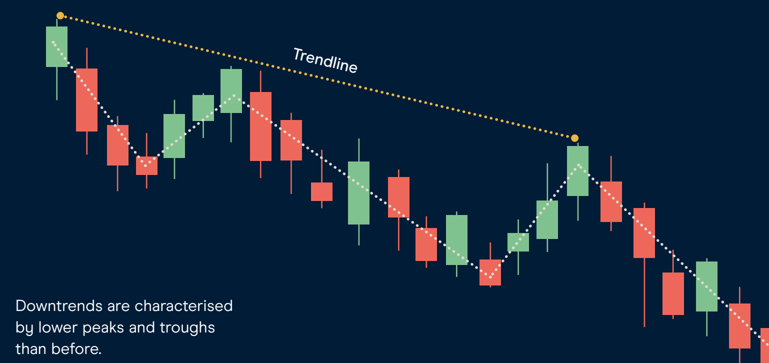


FIG. 7: DOWNTRENDS



instance. This trend line can then be used to project where the next wave of highs or lows could happen.

The price channel is the space between two trend lines. The channel is where you will follow and analyse the price action activity. It's important to use price action analysis, as trend lines show areas where a security's price could move to rather than will move to. See fig. 8.

3 SPOTTING SUPPORT AND RESISTANCE LEVELS

A support level refers to the position at which a price of a security stops going downwards due to a concentration of buying interest overcoming selling pressure, and a downtrend reverses course. Typically these support levels form where there has been previous price action in the market (see fig. 9).

A resistance level is the opposite – when the price of a security stops climbing due to selling pressure overcoming buying interest. This pushes the price of a security back down after an uptrend. On a chart, support and resistance levels are highlighted with trend lines either in a horizontal or angled direction.

If a trader is able to accurately spot a support or resistance level on a chart then they can present opportunities to enter a trade. A trader could enter with a buy position at, or just above, a (valid) support trend line.

If a security's price decline reaches this line the price could, in theory, increase again, leading to a profit. With resistance, a trader looking to short a stock can do so as at or just below this trend line. As the price reaches this point, a short seller can sell their stocks as the price is likely decrease, enabling a profit on the short.

These chart patterns work because other traders in the market are playing off the same indicators. If enough volume of traders supports this move it can be a self-fulfilling prophecy of the crowd.

Without considerable practice and experience trend lines can be misplaced or miscalculated. Also, there are some considerable risks involved when using them, given that prices can, in certain circumstances, break out of a support or resistance line, causing a loss for a trader.

In this instance, the technical characteristics of this line will be reversed — the broken resistance line would become the new support line as the price reaches new highs, while the reverse is true of a broken support line (see fig. 8/9).

> "Without considerable practice and experience trend lines can be misplaced of miscalculated"

FIG. 8: PRICE CHANNELS AND BREAKOUTS

FIG. 9: SUPPORT AND RESISTANCE LEVELS

THE BASICS UNDERPINNING A DAY TRADING STRATEGY

Now, finally you are ready to put practice into action, to take the bull market by the horns and start trading for real

Finding the right asset classes to trade

We've seen that price analysis can help in trying and determine which securities might break out of patterns or move through support and resistance. But stocks are myriad and analysing each and every one would be a sisyphean task. Therefore, software such as stock screeners
are helpful when trying to whittle down the number of securities to consider. These can be based on filters such as daily average trading volume, volatility and one-day or one-week percentage change.

There's an ongoing debate as to whether traders should only concentrate on a few specific securities or start from scratch and find new asset classes regularly based on what's moving or has momentum. Familiarity with certain securities will allow a trader to become somewhat attuned to its nature, characteristics, and status. However, concentrating on the same few securities could also limit the scope of a trader's activity, potentially risking missed opportunities. It is up to the individual, ultimately, and part of developing their strategy will involve determining how often, and what assets classes, to rotate.

Volume as an indicator

While price movements are a key indicator, measuring the volume of a security is also helpful when making the decision to trade or not to trade.

Volume indicates the number of units or shares of a particular security that are changing hands from one trader to another over a certain time period. Typically, it can appear across the bottom of some charts.

Volume is important for day traders as it is a gauge of the liquidity of a given asset class. That is to say, the ease at which a trader can buy and sell or to get in and out of a position. A stock screener is important for day trading as it can tell you what has volume on a given day or point in time. This may not be assets that typically have a high average daily volume (for founder of Ezeetrader Charlie Burton's take on volume, see page 18 later in this chapter).

The most consistently traded ETF based on volume in the US is the SPDR S&P ETF, which is known to have a daily volume of 100 million or more, according to the balance. The publication suggests that while preference varies trader to trader, most will look at stocks with at least one million in daily volume.

When to trade

According to many seasoned traders, stock markets offer the best liquidity in first few hours after they open.

Risk management

Before a trade is placed, a trader should consider what they are willing to risk losing in order to gain a profit, this is commonly referred as a risk-reward ratio. Simply put, the risk to reward ratio is the amount a trader is willing to risk versus the potential gain throughout a trading period. For example, if a trader is willing to risk £100 to make £100 profit, their risk to reward ratio would be 1:1.

However, a trader with this ratio is unlikely to profit much in the long-term if they lose as much as they make. Realistically, a trader will want to ensure that potential profits are multiples of what a trader is risking. The percentage of wins of many traders can be below 50%, but the important thing here is that their wins will be much larger than their losses.

"When placing a trade, you should be aiming to make at least twice as much money as you are risking," says David Madden, analyst at CMC Markets. "For example, you may enter a trade with the view of making £200 on the transaction, and you are comfortable risking £100 on the trade."

Madden cites a common trading statistic, that professional traders and investment banks only get around 40% of their trades right, and they have the discipline to cut losing positions and push winning ones – something less experienced traders may not. With that in mind, a low ratio over time may eat into a trading balance if successful trades are not forthcoming.

"Risking too much money for a potentially small profit isn't sensible," Madden explains. All day traders have regular losing trades. It's good practice to accept this and create a strategy that works with this in mind.

The benefits of journalling

Get yourself a notebook and pen and at the end of every trading day note down what trades you have made. When did you open and close and were you successful or not?

You can then analyse your performance over the next weeks and months to find trends and improve your future strategy. Are you taking too much risk or not enough? Are your trades too small or big? Is this the right market and strategy?

Like an ordinary diary, don't worry about getting philosophical. Ask yourself how you were feeling when you made a particular trade and what happened? Did you feel rushed? Were you distracted?

Note the market conditions and whether it was a busy or quiet news day. Did this affect the markets? If so, how? Are there any patterns?

Portion size

Most professional traders may typically risk around 1% to 1.5% of their account balance on a trade, although this figure will vary from trader to trader. Anything above that could cause significant damage to your ability to continue trading. If you have a balance of £30,000 then 1% is £300. So, divide that by 50p per share and then your position size is 600 shares.

Using a stop-loss order

Traders can use a stop-loss order to help them manage their risk. The stop loss helps to minimise loss by enabling a trader to get out of a problematic trade. Stop-loss orders will stay in effect until they are either triggered, cancelled or a position is liquidated. Stop-loss orders can be either a buy stop or a sell stop, the latter of which is the more commonly used.

How do they work?

If a trader places a stop-loss order at a certain threshold, when the price of a stock reaches that point, then the stop loss will be triggered, closing the trade at the next available price. Let's say you open a trade at a buy price of 7310p, placing a stop-loss at 7300p. If the price fails to increase but instead falls to 7300p, the stop loss will be triggered, and your trade would be closed at the next available price.

Where to place a stop loss?

Many traders stick with a rule of putting it behind the next key support or resistance area or if you prefer to risk less per trade then behind the previous full candlestick low (when buying) or high (when selling).

Other types of stop loss

A trailing stop-loss order will, in essence, follow a price as it increases or decreases. Take fig. 11 for instance. Now imagine the price rose to 8000p before dropping back to 7300p. If the original stop-loss order remained, all the profit the trader made would be wiped out. However, a trailing stop-loss order would increase a number of points below the price, so as it increased by 690p, so would the stop loss. (fig. 12) The position would be closed when the price turned around and began to fall rather than at the original stop-loss order price of 7300p, minimising profit loss.
As well as using stop-loss orders, a trader can also set a daily limit based on the number of trades lost in a row or a percentage loss from an account. This is simply the amount of money will allow themselves to lose in a day before calling it quits.

When to stop: what's my maximum drawdown?

A drawdown commonly refers to when a share price declines after a peak and measures the difference between the peak to trough in a stock's performance. For example, a stock might hit a peak of £100 before declining into a trough of £50 before later returning to another peak of £100. In this instance, the drawdown on the stock measured between the peak and trough is £50 – expressed as a ratio of 50%.

The same will apply to a trading account, which may hit a peak of £100,000, before dropping to £90,000 over a given periods, and eventually returning to a peak of £100,000. In this instance, the drawdown was £10,000 or 10%.

Maximum drawdown is when a trader calculates "the greatest peak to trough differential" that can occur before a new peak is made, netpicks.com explains. That is to say, during back testing, a trader can see what the maximum differential is between two given peaks in their trading account would be based on historical trends.

"In doing a proper back test of your trading strategy, you will learn the optimal risk per trade you should be using to sustain your trading account during the pullback in your equity curve," Netpicks.com states.

In essence, a trader can use maximum drawdown to determine how healthy or otherwise their trading strategy is. Traders should beware that drawdowns are inevitable, but a strong strategy should always take them into account. You won't escape them. It's also important to think about what you would be comfortable losing. Can you handle more risk per trade? There will inevitably be more drawdown risk with this strategy. If you can't it's better to risk less per trade.

FIG. 10: DRAWDOWNS

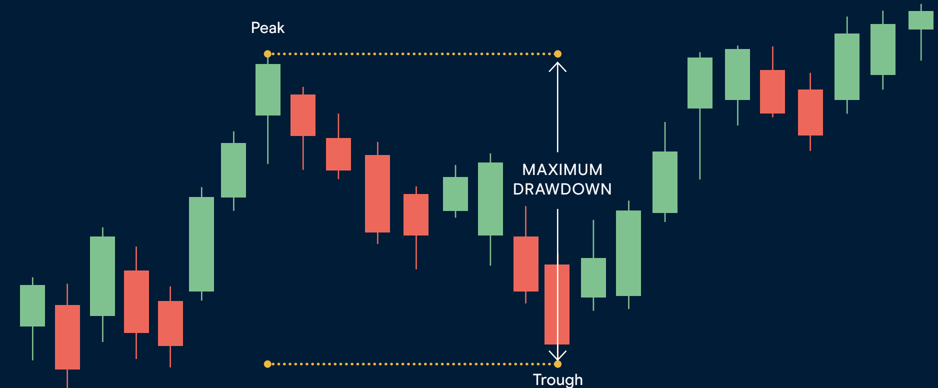


FIG. 11: STOP LOSS

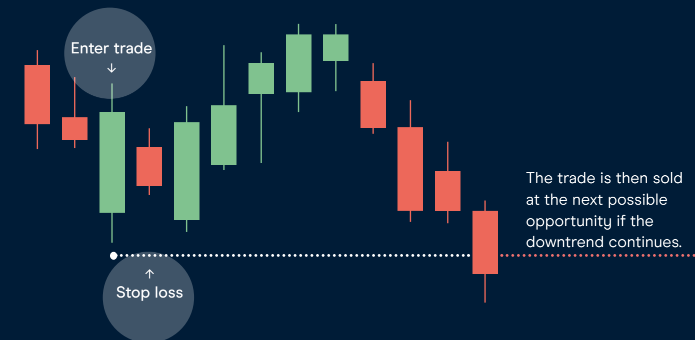
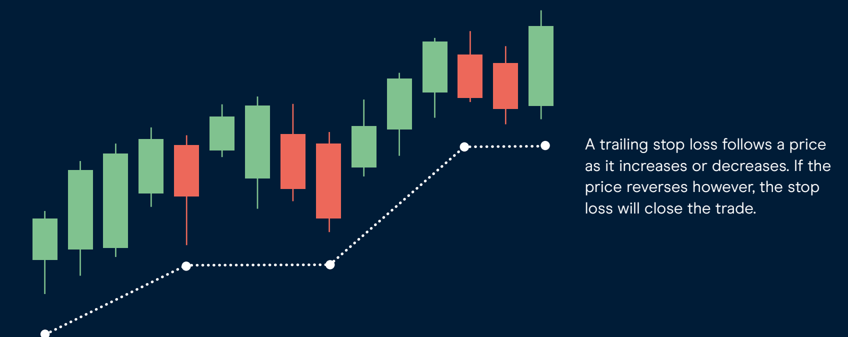


FIG. 12: TRAILING STOP LOSS



Insights from day trader Charlie Burton

Charlie burton is a full-time trader with more than 22 years of experience. He is the cofounder of Ezeetrader, a service that provides market research and analysis, and is based in the UK

"When I left my full-time position in the fund management sector, I was particularly keen to improve my work/life balance. There is a great deal of corporate entertaining you need to do in fund management, and it can be wearing on your family life, health and time.

I've been trading from home since 2001. I don't have to go into an office and I sit at my desk with my dog at my feet. It's what I wanted. A peaceful environment with no noise.

That includes no music, although I do know of other traders who say classical music helps them think, relax and trade.

In terms of what is physically in front of me, I have six monitors. But that's only because I like multi-tasking.

For most day traders you only really need to have two big widescreens. That would be fine. You don't need to have 20 screens that the marketeers on the internet say are necessary. That's nonsense.

On the screens I have a range of different charts looking at a variety of markets, emails on another, my broker terminals set up and a news feed which helps me to tap into the economic and political sentiment and developments.

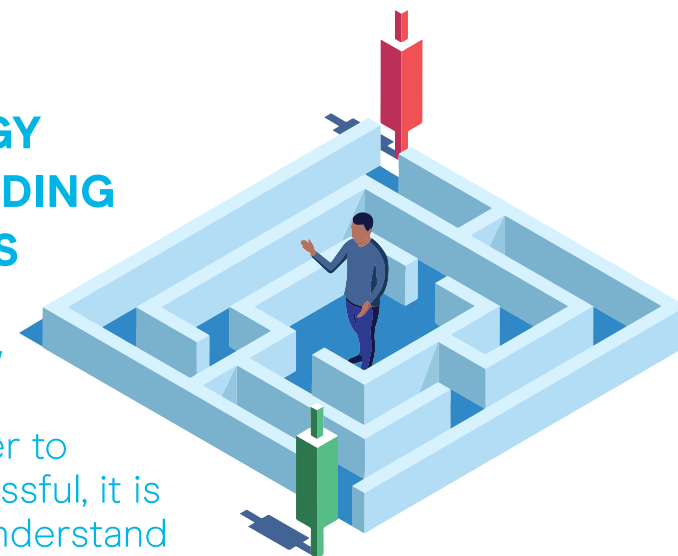
One of the worst things you can do is have Bloomberg TV on, because you are bombarded with information from analysts. I turned Bloomberg off in about 2001.

In terms of time frames, I look at the markets from 7.30am to mid-morning and then again when the US wakes up from between 1:00pm and 3:00pm.
A lot of economic releases come out at 1:30pm, so it's an important time to find trading opportunities.

I used to look at screens 12 hours a day and although it has given me lots of benefits, I'd recommend beginners identify specific time windows for their trading and to stick to them.

It means that you can take the dog out for a walk during the day without stressing that you are going to miss a trade."

THE PSYCHOLOGY BEHIND TRADING AND A PRO'S TRADING KNOW HOW



For a day trader to become successful, it is important to understand their choices and how to overcome certain bad behaviours

Follow your own rules

Discipline is one of the most important attributes that experienced traders have in common. That is why it is important to keep a watchful eye on bad habits and look to resolve them as soon as possible.

Trading in a disciplined way involves a carefully considered set of rules, a mental framework, determined to govern any particular trading decision. But what is even more important is following this framework.

Finding ways to ensure these rules aren't broken is crucial to any day trader's ongoing strategy. As a day trader, it is a good idea to re-evaluate your framework at the end of each month, due to the shorter timeframe of this style of trading.

Manage your money

A principle that should underpin any traders' strategy is money management, regardless of timeframe. Before entering the market an identification of their risk-to-reward ratio, pot size, allocation per bet (relative to overall pot size), plus many other factors should be made (for more on this see 'Risk management' in chapter three). Certainly, potential traders looking to be in the business for many years to come will need to apply successful money management strategies.

A trader's risk-to-reward ratio is important (see previous section). Remember, it does not matter that you win 90% of the time if your losses are much larger than your gains.

Never forget to use stop losses to manage risk when placing orders to enter the market as an added insurance (see previous section on stop loss types and how to use them). Prior to entering any trade, understanding and being comfortable with how to set a stop loss order is essential. This is a good habit to have and will help protect many traders from trades that go against them.

Five tips for trading in the zone

1 Stay level-headed. You should always try to remain calm – this is especially true when you are faced with a loss. Maintain a calm disposition and react in accordance with your rules. Mentally rehearse your worst-case scenarios so that if they do occur, you are prepared.

2 Don't let other traders' opinions influence your strategy. Sometimes other traders will offer their views on the market and give advice without considering your trading methodology. If you want advice you should consult a qualified professional who will be able to appreciate your style of trading and give their thoughts accordingly.

3 Be patient. Emphasis needs to be placed on the importance of patience when trading. If you can't find any viable trading opportunities, don't trade for the sake of it. As you get to know a market you may find that knowing when to open or close a trade becomes easier. Your intuition will become sharper as you become more experienced.

4 Be aware of your stress level. Day trading can be stressful as it requires constant attention and motivation. You can counter this by taking time to think about your priorities. Get some perspective on trading and its place in your life. If you feel like your stress level is rising it's probably a good time to step away. You can come back to trading later when you are in the right frame of mind.

5 Never be afraid of realising your profits. If you find that you have exited a trade at a profit but the trend continues, don't regret your decision. You have made a profit, so start looking for the next opportunity. If you worry that you are frequently exiting too early and are missing out, you could design and test a re-entry technique.

Charlie Burton's view

We asked professional day trader Charlie Burton to explain what made him start trading, the methods he uses, and the psychology he's adopted

Why did you begin day trading?

My interest in day trading began in 1997. I was working in the finance industry at the time, mainly in fund management, and one day a financial advisor that I knew well said he had a spare ticket for a trading course. I went along and listened to trading experts telling us how to trade options on US stocks. I was fascinated and started swing trading in my spare time.

It was in late 2001 that I left my full-time fund management role, not just because I wanted to try trading full-time, but because I was burning the midnight oil too much. There is a lot of corporate entertaining in the fund management sector and I felt that my work, life and health balance was a little out of sync. So, as I had cash behind me, I decided to take a year out and see if I could make it as a day trader working from home. When I began, I had a watchlist of about 30 or 40 decent sized companies along a spread of industry groups. I had two or three gold mining companies as well as engineering and tech firms. They were all trading from $20 a share up to $80 a share. Today I mainly trade FX, stockmarket indices and commodities. I don't do stocks, but it really is all the same.

> "You are looking at a chart and if the stock is having a nice upward trend and it does a pullback to an overshoot of a 20-period then I will start to get interested"

What do you think are the key factors to consider when day trading?

With stocks, the fundamentals are less important than the price action if trading over a short period. So, if a sector is up on any market, be it the FTSE 100 or S&P, because there is perhaps a lot of news out around it, it is the sentiment that attracts you.

What is going to send a market or stock up or down currently is more likely to be caused by what US President Donald Trump has been tweeting that day than the fundamental measurements of the market or stock itself.

Fundamentals are much more important in the medium term but if you are a day trader you are trading short-term price action.

How do you define a strategy?

There are a million and one trading strategies, but here is a simple concept.

You are looking at a chart and if the stock is having a nice upward trend and it does a pullback to an overshoot of a 20-period simple moving average then I will start to get interested.

If it does this on a five-minute chart but I know that on the hourly chart the trend is up that's a good sign to me that the price will probably turnaround and resume the uptrend.

What are your thoughts on technical analysis?

The thing with trading is that there is not one single thing that you use to try and make money. Because if you just rely on one thing, like a candlestick pattern, then you might as well chuck it out of the window. It is not enough.

It is the person, the trader, who makes the edge to these things.

As an example, if you are using a candlestick pattern, is that reversal pattern going into a support level or is it just a random candlestick pattern sitting in the middle of a cluster of candlesticks?

I do look at candlesticks but only in the context of what is going on generally within the markets. So, the dollar index is obviously an important measure of what is going on with that currency.

Do you find looking for patterns or for trends more beneficial?

In the context of the dollar on a monthly chart, I know that could have repercussions going into the next month and maybe the next month after that. That sort of information could be quite useful to me. But just a random candlestick on a five-minute chart is less important.

What is more important is the overall trend

of the stock and then trying to place some sort of context within that trend. So, don't buy just because it is going up.

I tend to buy when there is a pullback within the context of an overall trend. There is an old phrase: 'fade the short-term trend in favour of the longer-term trend.'

If the long-term is up, let's say on an hourly chart, but the short-term on a five-minute chart shows the market has been coming down over the last two hours, what you do is fade that short-term trend on the five-minute chart so you do the opposite of what it is doing. If it has been coming down, you want to be finding a support zone to then buy it because the overall hourly trend is still to the upside.

It should therefore just be a pullback within that overall trend.

It could be that suddenly you get a cluster of reversal type candlesticks which start to form as it starts to bottom. Maybe, but maybe not – always think of the context.

How do you trade volume?

Do you want to be trading penny stocks? No. In the US stock market, I would never touch anything less than $10 a share. Stocks with low volume can have big gaps against you, which is dangerous. You are better off trading higher volume companies (for more on this, see chapter three). I used to trade the same stocks day in and day out, Apple and a few other big firms, and would not look at anything else.

> "Mindset determines your discipline and whether you overtrade or revenge trade. Developing a skin like a rhino is what traders need to do"

Why? Well, I have always been a big believer in focus and getting used to the personalities of the markets and stocks I am trading. So rather than doing a scan of the market and it kicking up a stock on that day – which you can do – I would just look at my 30 or 40 stocks each morning.

Of those, there would be a handful appropriate for trading on that day. A scan could pick out say Tesla. I would think I have never ever traded it before, I might know nothing about what is going on with the electric car industry and all of a sudden CEO Elon Musk comes out with an announcement I was unaware was going to happen. It is better to be familiar with a company than not and getting caught out.

But back to volume. When you are looking at a chart within a day there is a volume indicator and there are times during the day when you might get a big volume spike. A selling candle with a big, high-volume spike can quite often mark a low point. So, volume can be used to show places where suddenly you reach a saturation point or a selling climax. It could be enough of a low for a day trader to get in and try and profit from.

Why is risk management important?

Lots of people don't use stop losses but they should. You hear a lot of traders who say that they use a mental stop, but they can't be genuine if they do that – they are more of a gambler.

They say that they sit in front of the screen and know when they are going to exit, so if the price comes down to that level then they will just close off. The problem is that trading is all psychological. Say the market comes down to that level and goes through it very quickly, then the trader is tempted to stay in and wait for it to come back up. Then it never does and all of sudden they have gone way off their original plan.

So, use stop losses, risk up to 1% of an account per trade and don't try to choke the trade. You do get a lot of traders who try and place their stops too close to the current price. Give it enough room to breathe. If anything, put a smaller position size in and have a slightly wider stop.

How important is having the right mindset?

A trader's mindset is 80% to 90% of all trading. You can have all the technical abilities and read every trading book that is out there, but without the right mindset you won't make it.

Let's say there are 10 trades and you have a system with a 60% win rate. The first three trades are losers so when the fourth trade comes along you hesitate and decide not to take it because you are in a panic. The fourth goes on to be a winner and you get frustrated and angry and swear you will take the next trade, but it is again a loser. Now you are really disappointed, but you have forgotten that missed opportunity.

Mindset determines your discipline and whether you over trade or revenge trade. Developing a skin like a rhino is what traders need to do – take the knocks and realise that you are going to be wrong five times out of ten. But do you know what? Those five times is all you need! Most people go into trading expecting to be right nine times out of 10 and that is completely the wrong way of looking at it.

Also, don't focus on the trade you are in right now. Of course, it is important but don't fixate your entire livelihood on the outcome of that trade. What is important and more statistically relevant is the outcome of the next 30 trades. Stick to your rules and have a tried and tested approach, then measure your success over the long-term.

You can develop the mindset. We don't naturally have those skills because we are human beings and we are not predisposed to trading. It is counter-intuitive because we are putting money on the line and it becomes emotional. It brings up fear and greed.

A fearful trader will struggle to run a trade to its profit target and jump out too early. A greedy trader will hold on to their trades and never bank them. You need a bit of both. You must roll your sleeves up and have a good time horizon. Accept you won't be a millionaire overnight. It takes time and experience for you to get used to rejection in the market. However, once you get used to that, you get a trader's mindset.

> "A trader's mindset is 80% to 90% of all trading. You can have all the technical abilities and read every trading book that is out there, but without the right mindset you won't make it"

Charlie's Three Key Takeaways

1. "If a stock is having a nice upward trend and it does a pullback to an overshoot of a 20-period simple moving average then I will start to get interested."
2. "In the US stock market, I would never touch anything less than $10 a share."
3. "Use stop losses, risk up to 1% of an account per trade and don't try to choke the trade."

Day trading strategy example

Fibonacci retracement patterns

This strategy can be used with stocks or indices as a day trading strategy. It uses technical analysis to plan entry and exit of trades by applying Fibonacci retracements levels to charts. These levels act as support and resistance levels on a chart.

To create a Fibonacci retracement you take two points. A recent high and the trading low before this. Charting software, such as that available with CMC Markets (See fig. 13) will then plot the key Fibonacci points of 23.6%, 38.2%, 50%, 61.8%, 100% between these two points.

We are day trading these setups so use candlestick charts with either 1 hour or 15 minute bars.

Timing the entry

This strategy would look to go long based on a 50% retracement from the recent high. You can place an order to open once price has hit the 50% retracement mark. See fig. 14. Placing a stop loss just behind the 61.8% level. This level is the support level that you're hoping will hold and if it breaks you're looking to exit the trade. These levels are relatively tight, but it keeps your losses small.

Price target

Your price target will always be the 123.6% extension of the move. We will not exit the trade until this level is hit.

Extra notes

Try to only enter trade setups one hour either side of the UK or US markets opening for indices. For stocks try to only trade the market open. The reason for this is you need momentum and liquidity, and this is during these times.

To minimise your risk you can move your stop loss to break once the 100% level is touched.

Fibonacci doesn't just apply to rising markets. If a market has fallen then Fibonacci fans will apply the retracements to the bounce back up. See fig. 15.

For more details on fibonacci retracements patterns try this: www.cmcmarkets.com/en-gb/trading-guides/what-is-fibonacci-trading

FIG. 13: FIBONACCI RETRACEMENT SET UP ON CMC MARKETS PLATFORM

FIG. 14: POSITIVE EXPAMPLE

The candles hit the 123.6% extension target continuing on to the target price.

FIG. 15: NEGATIVE EXAMPLE

The candles do not continue to the target, instead they go through the stop.

CMC Markets is an execution-only service provider

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