Brainy's Articles on

Share Trading**

Position size and calculator

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This article
is NOT free*

Introduction

When setting out on a journey of share trading / investing (or in share market derivatives like CFDs), two people could use very similar strategies, but end up with one person making good profits, while the other one is making significant losses. This can easily happen if the *money management* is unplanned, or somewhat haphazard.

This Article in Brainy's series on Share Trading (number ST-4400) provides information on just one aspect of money management — *position sizing*. When buying shares in a company, the *position size* simply refers to the number of shares that you intend to purchase (also referred to as the *parcel size*). This Article focuses on trading in shares, and does not specifically consider derivatives like CFDs, nor short selling; but the principles and ideas can still apply.

Table of Contents

The Overview section of this Article below talks about the relevance and importance of *position sizing*. The following sections provide a step-by-step process to calculate an optimum *position size*, and address the topic in more detail. Traders and investors often use some sort of *position size calculator* to quickly calculate an optimum position size. To support this topic there is a Position Size Calculator available in the Members' section of Brainy's *Share Market Toolbox* (in Excel spreadsheet format), and there is information below that explains how to use that calculator.

NOTE: There are no guarantees of any sort offered with this material.
Anyone who uses the spreadsheet calculator does so bearing all risk.

Investor or trader?

The question of how an *investor* and a *trader* are different is often asked, and sometimes debated hotly. In many situations it is easy to classify someone as an *investor*, and someone else as a *trader*. But the boundaries between the two types can be blurred, and sometimes difficult to distinguish.

All of the *position sizing* principles that are described in this Article are equally relevant to both *investors* and to *traders*. Whenever an investor decides to purchase a parcel of shares, it can be called an *investment*, and the act of purchasing the share parcel is actually a *share trade*. Hence, the two terms *investor* and *trader* can often be used rather interchangeably.

Overview

When you buy a parcel of shares, you need to decide how much of your hard-earned money to invest. For example, if you have $10,000 to invest, should you invest all $10,000 in one position and put the whole lot at risk? Or should you invest a smaller amount? Also, should you simply invest an equal amount in every open position? Or is there an optimum amount for each position? How can you work out the optimum amount to invest? Or, why bother to work it out? What difference does it make?

It can be very beneficial to consider the "optimum" amount of capital to allocate to a position.
By actually risking the maximum amount that you can afford to "risk", then
you are taking maximum advantage of favourable price movements to maximise profits.

The rest of this Article talks in more detail about how to calculate an optimum position size, and the idea of putting only "2% at risk" — known as the "2 Percent Rule" (the "Fixed Risk amount per trade" method). And it shows you a very quick, easy and simple way to work it out using the available *Position Size Calculator* spreadsheet. A quick view of the calculator is included in this Article on page 2 below. Take a quick look at it now. At first glance it looks a little complex, but it's not really.

** - The two words *trading* and *investing* are often used somewhat interchangeably.

Note: This information cannot be relied upon. It is only a guide. There is no guarantee of success.

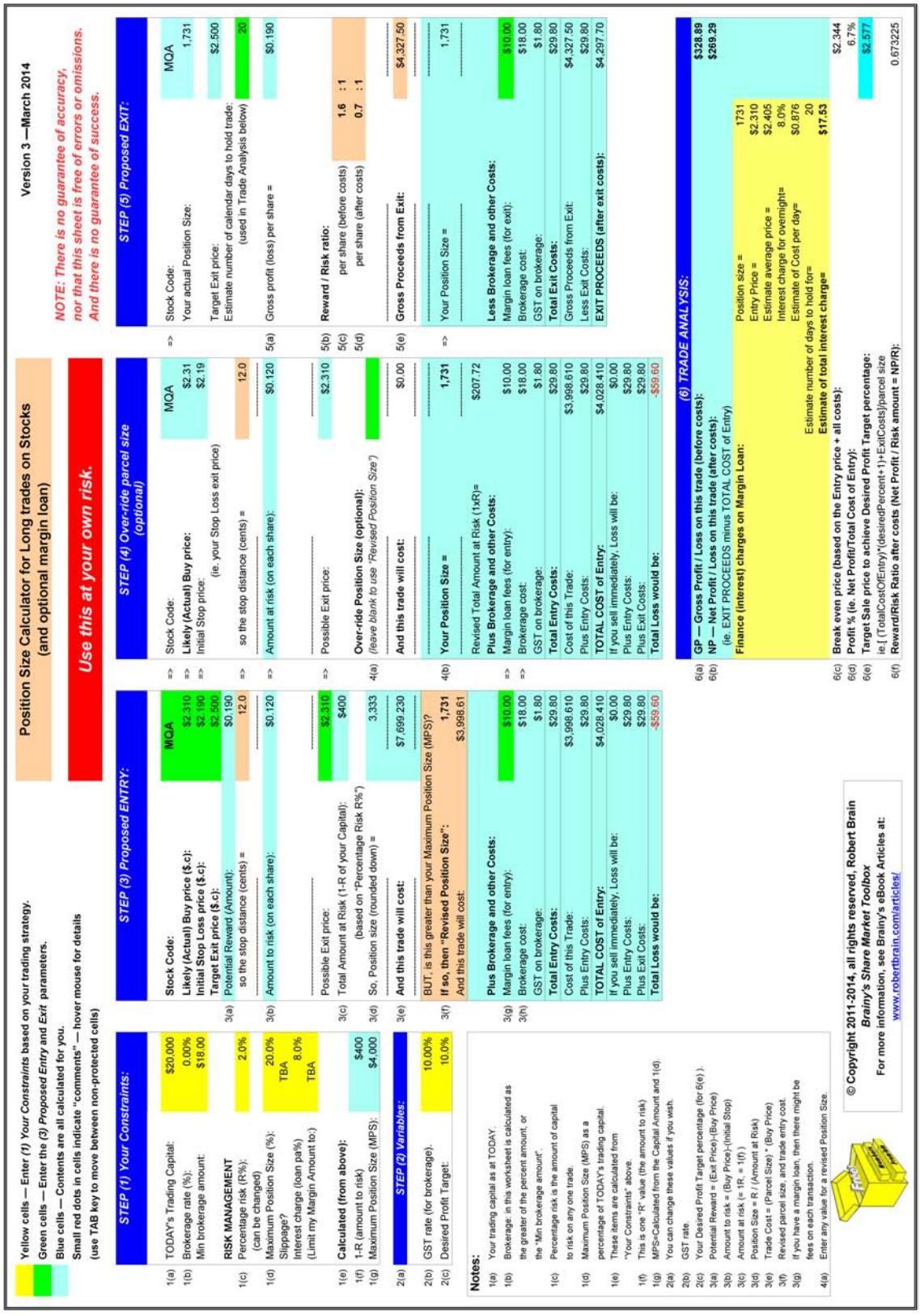

Figure 1: The Position Size Calculator spreadsheet (version 3).
NOTE: No guarantees are offered with this spreadsheet calculator.

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