# Risk management in cryptocurrencies trading

This is the sixth part of our training lesson on cryptocurrencies trading that gives insight about risk management while trading cryptocurrencies.

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Risk management is said to be the most important part of crypto trading because the crypto industry is pretty new and you have to be very careful while selecting a cryptocurrency to trade. Lack of regulations in this industry makes it more vulnerable in comparison with traditional stock trading industry where each asset is listed on the market after proper approvals from the regulatory authorities. But here you can launch ICO without any regulatory approvals and can get listed your tokens on exchanges by giving some money rather based on proper audits.

This is the reason here you have to deal with some extra risk factors apart from the usual risks involved in the trading them. We have divided these risks into operational and technical risks. Let's dig deep into them.

## Operational risk

Fundamental risks in cryptocurrencies are pretty higher than the traditional market due to unavailability of proper regulations for the cryptocurrencies market.

- **Credit risk**

  Credit risk is related to the team behind a cryptocurrency project. There are hundreds of failed projects in the crypto industry. There were more than 2500 new ICOs launched in the last three years and the number of dead projects listed on deadcoins.com is more than 1,800 now. These numbers make credit risk most vulnerable to this industry. So you need to carefully evaluate the team behind the project as we suggest in the second part of our training series.

- **Regulatory risks**

  Regulatory risk is another major challenge faced by the cryptocurrency industry. Major regulations started developing and implemented in 2019 but that is causing the legal and regulatory risks for the older projects even. Like in 2019 alone, the SEC fined more than 10 crypto projects and asked some of them to return the money to their investors which causes a panic in the mind of traders resulting into sharp selloff and giving huge losses to the coin holders. Always look on this side of the cryptocurrency before you start trading it.

- **Cryptocurrency delisting**

  Delisting of cryptocurrencies from crypto exchanges is another major challenge faced by crypto traders. Delisting may be the result of regulatory pressure of non-compliance of operational requirements from the team behind the company. Even sometimes personal likes and dislikes have resulted in the delisting of major cryptocurrencies from major exchanges. To cope up with this risk you should only hold cryptocurrencies for the long term that have a strong fundamental base and have already been in the market for a long time. And you should only look to day trade the other coins that are new or do not have strong fundamentals behind them.

## Technical risk

Technical risks are related to the actual trading of the cryptocurrencies. You can avoid technical risks if you have a clear trading plan and execute it as planned. A cryptocurrency trader should never trade with more than 10% of the capital they have. They can add more later if needed in the margin trading to secure the position but should always try to remain liquid in the form of Bitcoins as well as in stable coins. Let’s take a look into some major technical risks involved in trading.

- **Position sizing**

  Proper position sizing is one of the most important things you need to consider while taking a trade. You might feel tempted to make a trade with 50% or even 100% of your trading capital after winning a couple of trades in a row but you will do no good to yourself this way. Always look to make a trade for the money you are comfortable losing. There are several formulas available to calculate the position size but everyone has a different risk appetite and if you invest more than your risk appetite then your emotions will get involved in your trading decisions which will not help on a long run for your trading business.

  I would recommend keeping your position size to 2% of your trading capital but you can adjust it to the level you are comfortable with. You should also define what maximum percentage of your capital you can trade in a day as you define it to 6% then you can only take 3 days in a day which will also help in avoiding overtrade.

- **Risk/reward ratio**

  Defining your risk/reward ratio for taking a trade needs to be decided in advance as well. You can not risk $5 to make $1 but you should risk $1 to make $5. You should never look to enter in a trade where the expected reward ratio is less than two times of risk associated with it. Risk and rewards are calculated based on stop loss and profit targets level of a particular trade.

  A specific example can be an asset sitting just above the major support line where it will take it only 1% to break the support line while the next resistance line is 5% from that level which should be your profit target. So in this case, if the price moves the opposite way you will lose 1% but if the price moved towards your way then you can make 5% from it. Keeping a 1:5 ratio means you will still be at breakeven if you lose 80% of your trade as one positive trade will cover the loss of other trades.

- **Stop loss + Take Profit**

  Planning stop loss and taking profit should also be planned in advance and orders should be placed as soon as you enter a trade. You should never leave a trade open without stop loss orders as you will be risking more money than the risk/reward ratio you initially calculated before entering a trade. Also never move your stop loss in a hope of bounce and even look to close the trade before it hits the stop loss if you are confident that trend is reversed. When price moves in the positive direction you should move your stop loss to the breakeven point but never be too tight doing it.

  Taking profit is also important to stay profitable. Profit is never yours unless you book it. Some traders do not book profit on its designated targets in a hope that price will further move in their favour but it might come back and you will end up making a loss. So always execute the plan as defined with no exception. Discipline will make you a successful trader.

- **Confirmation of setup**

  When you are entering a trade you need to look for confirmation before entering it. Like if you are looking to trade ahead & shoulders trading pattern then you should wait for its right shoulder to complete and enter on the breakdown. An early entry without proper confirmation can lead to a big loss. You might feel you are late entering a trade but at least you will have the confirmation of the setup moving into your way and trade it more confidently. Someone has even said, “entering a trade without confirmation is a suicide”. So always look for confirmation to stay more profitable.

- **Extensive testing**

  Extensive testing of your trading strategy will increase your chances of winning. Never take trading business casually. Always first test various trading strategies on demo accounts or by paper trading for 100’s of times and move to the real trading with the one having the highest winning ratio.

- **Monthly audits**

  Monthly audits of your trading performance are also very important to evaluate your trading results. You should evaluate each trade monthly to know if you were exposed to higher risk on a particular trade or not. It will help you to make adjustments in your future trading to stay more profitable.

We have covered various risk factors that can affect the cryptocurrencies trading. Do not try to implement all the points at once in your daily trading rather keep adding them on a consistent basis and I can assure you that you will be on the path to become a successful trader.