

# The Risk Management Framework

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Position sizing, capital protection, and the rules every trader needs before risking real money.

**6**

## Core Frameworks

Position sizing to drawdown recovery

**3**

## Risk Calculators

Ready-to-use formulas you can apply today

**1**

## Survival Rule

The single principle that changes everything

# Why This Exists

And why risk management is the only edge that never expires.

Most traders lose money. This isn't opinion — it's data. Regulatory disclosures across major brokers consistently show that 70-80% of retail traders lose money. The industry sells entries, setups, and signals. Nobody sells survival. This guide exists to fix that.

Risk management isn't a chapter in a trading course. It IS the course. Everything else — technical analysis, fundamentals, sentiment — is useless if you've already blown your account. Position sizing, drawdown limits, and capital protection are the foundation. Without them, you are gambling.

## THE ONE RULE

### Survive first. Profit second.

Every framework in this guide serves this single principle. If you remember nothing else, remember this: your only job is to still be trading next month.

## What This Guide Covers

**Framework 1:** The 1% Rule — How to size every position so a single loss never threatens your account

**Framework 2:** Risk-to-Reward — Why entries matter less than you think and exits matter more

**Framework 3:** The Daily Loss Limit — How to stop bad days from becoming catastrophic days

**Framework 4:** Drawdown Recovery — The maths of recovery and why prevention beats correction

**Framework 5:** Correlation Risk — Why "diversified" positions can all lose at once

**Framework 6:** The Pre-Trade Checklist — A repeatable process that removes emotion from every trade

## IMPORTANT DISCLAIMER

This guide is educational content only. It is not financial advice, trading advice, or a recommendation to trade. Past performance is not indicative of future results. Only trade with money you can afford to lose.



# The 1% Rule

Never risk more than 1% of your account on a single trade.

This is the most important rule in trading. Before calculating entries, targets, or stop losses, you need to know one thing: what is 1% of your current account balance? That number is your maximum risk per trade. Period.

## POSITION SIZE FORMULA

### Position Size = Account Risk / Trade Risk

Account Risk = Account Balance x 0.01 (1%)

Trade Risk = Entry Price - Stop Loss (in pips) x Pip Value

Result = The lot size that risks exactly 1% of your account on this trade

## Worked Example

Account balance: \$10,000

1% risk per trade: \$100

Trade: EUR/USD

Entry: 1.0850

Stop loss: 1.0820 (30 pips)

Pip value at 1 lot: \$10 per pip

**Calculation:**  $\$100 / (30 \text{ pips} \times \$10) = 0.33 \text{ lots}$

**Maximum position size:** 0.33 lots

## Why 1% and Not 2% or 5%?

At 1% risk per trade, you would need 100 consecutive losing trades to blow your account. At 2%, it takes 50. At 5%, it takes 20. The maths of ruin is unforgiving — the larger your risk per trade, the faster a losing streak becomes terminal. Professional traders and prop firms almost universally operate at 0.5-1% risk per trade. There is a reason for this.

### KEY INSIGHT

**The 1% rule is not about individual trades. It is about still being in the game after 6 bad weeks.**



# Risk-to-Reward Ratio

Why exits matter more than entries.

Most traders obsess over entries — the perfect candlestick pattern, the ideal breakout. But your edge comes from the ratio between what you risk and what you stand to gain. A trader who wins only 40% of the time can be consistently profitable if their average winner is 2-3x their average loser.

## BRAKEVEN WIN RATES BY RISK:REWARD

R:R Ratio	Breakeven Win Rate	Win Rate at 50%	Outcome
1:1	50%	Break even	Break even
1:1.5	40%	+Profitable	Profitable
1:2	33%	+Profitable	Profitable
1:3	25%	+Very profitable	Very profitable
1:0.5	67%	Usually losing	Usually losing

A 1:2 risk-to-reward ratio means you only need to be right 33% of the time to break even.

## The Practical Application

Before entering any trade, define your stop loss and your target. Calculate the ratio. If the ratio is below 1:1.5, the trade is not worth taking — regardless of how good the setup looks. This single filter eliminates most bad trades before they happen.

- Define your stop loss FIRST — based on market structure, not a random number
- Set your target at minimum 1.5x your stop distance
- If the target does not make structural sense, skip the trade
- Track your actual R:R across 50+ trades to find your real numbers
- Your win rate and average R:R together determine your edge

### KEY INSIGHT

**You do not need to be right most of the time. You need your winners to be larger than your losers.**



# The Daily Loss Limit

How to stop bad days from becoming catastrophic days.

A daily loss limit is a hard cap on how much you allow yourself to lose in a single session. Once you hit it, you stop trading. No exceptions. No revenge trades. No "one more to get it back." The purpose is to prevent emotional decision-making from compounding losses.

CONSERVATIVE	STANDARD	AGGRESSIVE
<b>2%</b>	<b>3%</b>	<b>5%</b>
Maximum daily loss: 2% of account	Maximum daily loss: 3% of account	Maximum daily loss: 5% of account
Best for newer traders and volatile markets	Used by many professional prop firms	Only for experienced, high-frequency traders

# Drawdown Recovery Maths

Why prevention always beats recovery.

The relationship between drawdown and recovery is not linear — it is exponential. A 10% loss requires an 11% gain to recover. A 50% loss requires a 100% gain. This is why capital protection must be your obsession.

**THE DRAWDOWN RECOVERY TABLE**

Drawdown	Required Recovery	Difficulty	Severity
5%	5.3%	Easy	●
10%	11.1%	Manageable	●●
20%	25%	Difficult	●●●
30%	42.9%	Very hard	●●●●
50%	100%	Nearly impossible	●●●●●

# Correlation Risk

Why "diversified" positions can all lose at once.

If you are long EUR/USD and long GBP/USD, you do not have two trades — you have one trade with double the risk. These pairs are heavily correlated because both are essentially short-USD positions. A single dollar move hits both. Understanding correlation is understanding that position count does not equal diversification.

**HIGH POSITIVE** +0.85 to +1.0

EUR/USD & GBP/USD — Move together. Double risk.

**HIGH NEGATIVE** -0.85 to -1.0

EUR/USD & USD/CHF — Move opposite. Can hedge.

**LOW CORRELATION** -0.3 to +0.3

EUR/USD & AUD/JPY — Mostly independent.

**THE RULE**

Count correlated positions as a single position for risk purposes. Total correlated risk stays under 1-2%.

# The Pre-Trade Checklist

A repeatable process that removes emotion from every trade.

- Have I identified my stop loss based on market structure?  
Not a random number
- Is my position sized to risk exactly 1% (or less)?  
Use the formula on page 3
- Is my risk-to-reward ratio 1:1.5 or better?  
If not, skip the trade
- Am I within my daily loss limit?  
If at the limit, stop trading today
- Do I have correlated positions open?  
Reduce size if total correlated risk > 2%
- Am I trading based on my plan or on emotion?  
If emotional, close the platform
- Have I checked the economic calendar?  
Major news = wider stops or no trade

# Putting It All Together

The six frameworks work as a system, not individual rules.

Every framework in this guide supports the others. The 1% rule determines your position size. Risk-to-reward filters your entries. The daily loss limit stops emotional spirals. Drawdown recovery maths explains why prevention matters. Correlation awareness ensures your 1% doesn't secretly become 3%. And the pre-trade checklist enforces all of it before every single trade.

This framework is not a strategy. It does not tell you when to buy or sell. It tells you how to survive long enough for your strategy to work. The best entry in the world is worthless if you have already blown your account.

## THE COMPLETE FRAMEWORK — SUMMARY

- 01 The 1% Rule** — Never risk more than 1% per trade
- 02 Risk-to-Reward** — Minimum 1:1.5 ratio or skip the trade
- 03 Daily Loss Limit** — Stop trading after 2-3% daily drawdown
- 04 Drawdown Recovery** — Prevention beats correction — always
- 05 Correlation Risk** — Correlated positions = single position
- 06 Pre-Trade Checklist** — Run every check before every trade

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