Financial Analysts Journal ›
Volume 59, 2003 - Issue 6

EQUITY INVESTMENTS

The Profitability of Day Traders

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Pages 85-94 | Published online: 02 Jan 2019

Cite this article https://doi.org/10.2469/faj.v59.n6.2578

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Abstract

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extracted only the confirmed trades for analysis, and the final data set contained 324 individual day traders. We used two analytical techniques.

In the “trade-matching” methodology, we matched daily buy and sell trades (also buy and short-sell trades) by the number of shares of a given order number. In the “flat-stock” technique, we sorted data for a given trader by stock, then by date, and by time. A “trade” was defined any time the trader had a “flat” position (zero net position) in the stock. The premise behind both methodologies was that price times number of shares bought is a cash outflow and price times shares sold is a cash inflow.

We found that 116 traders (35.8 percent) had a net profit greater than zero after commissions and 208 traders (64.2 percent) had a net profit less than zero after commissions. Therefore, we found almost twice as many losing traders as winning traders in the data set. The most profitable trader made more than $197,000, and the least profitable trader lost more than $748,000. The average gross profit for all traders was more than $8,000, whereas the average net profit was about –$750. Thus, transaction costs apparently preclude earning an excess profit in most cases.

The results also showed that 35.8 percent of traders made a positive net profit, 19.4 percent made more than $5,000, and 14.2 percent made more than $10,000. These figures contrast with the 64.2 percent of traders who had negative net profits, the 25.0 percent … $10,000.
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- About one trader in five is more than marginally profitable.
- Statistical evidence supports the notion that day-trader profitability is related to movements in the Nasdaq.

The fact that at least 64 percent of the day traders in this study lost money suggests that being a profitable day trader is more difficult than the industry maintains. The implication is that aspiring and novice day traders should give careful consideration to why they think they will be among the 20 percent of day traders who make at least $5,000 day trading. At a minimum, novice day traders should make sure they have enough initial capital to survive the three- to five-month learning period that the industry suggests is necessary to become successful.