

Since markets are closed I am going to post one of my most favorite chapter from "Trading in the Zone" This chapter will release you from agony of losing and emotional pain. Read it please because it will show you how thinking in probabilities are way to become **Elite Profitable Trader**. PDF of this great book I included. Enjoy and kick ass and make money!

TRADING IN THE MOMENT

Traders who have learned to think in probabilities approach the markets from virtually the same perspective. At the micro level, they believe that each trade or edge is unique. What they understand about the nature of trading is that at any given moment, the market may look exactly the same on a chart as it did at some previous moment; and the geometric measurements and mathematical calculations used to determine each edge can be exactly the same from one edge to the next; but the actual consistency of the market itself from one moment to the next is never the same.

For any particular pattern to be exactly the same now as it was in some previous moment would require that every trader who participated in that previous moment be present. What's more, each of them would also have to interact with one another in exactly the same way over some period of time to produce the exact same outcome to whatever pattern was being observed. The odds of that happening are nonexistent. It is extremely important that you understand this phenomenon because the psychological implications for your trading couldn't be more important.

We can use all the various tools to analyze the market's behavior and find the patterns that represent the best edges, and from an analytical perspective, these patterns can appear to be precisely the same in every respect, both mathematically and visually. But, if the consistency of the group of traders who are creating the pattern "now" is different by even one person from the group that created the pattern in the past, then the outcome of the current pattern has the potential to be different from the past pattern. (The example of the analyst and chairman illustrates this point quite well.) It takes only one trader, somewhere in the world, with a different belief about the future to change the outcome of any particular market pattern and negate the edge that pattern represents. The most fundamental characteristic of the market's behavior is that each "now moment" market situation, each "now moment" behavior pattern, and each "now moment" edge is always a unique occurrence with its own outcome, independent of all others. Uniqueness implies that anything can happen, either what we know (expect or anticipate), or what we don't know (or can't know, unless we had extraordinary perceptual abilities). A constant flow of both known and unknown variables creates a probabilistic environment where we don't know for certain what will happen next.

This last statement may seem quite logical, even self-evident, but there's a huge problem here that is anything but logical or self-evident. Being aware of uncertainty and understanding the nature of probabilities does not equate with an ability to actually function effectively from a probabilistic perspective. Thinking in probabilities can be difficult to master, because our minds don't naturally process information in this manner. Quite the contrary, our minds cause us to perceive what we know, and what we know is part of our past, whereas, in the market, every moment is new and unique, even though there may be similarities to something that occurred in the past. This means that unless we train our minds to perceive the uniqueness of each moment, that uniqueness will automatically be filtered out of our perception. We will perceive only what we know, minus any information that is blocked by our fears; everything else will remain invisible.

The bottom line is that there is some degree of sophistication to thinking in probabilities, which can take some people a considerable amount of effort to integrate into their mental systems as a functional thinking strategy. Most traders don't fully understand this; as a result, they mistakenly assume they are thinking in probabilities, because they have some degree of understanding of the concepts. I've worked with hundreds of traders who mistakenly assumed they thought in probabilities, but didn't. Here is an example of a trader I worked with whom I'll call Bob. Bob is a certified trading advisor (CTA) who manages approximately \$50 million in investments. He's been in the business for almost 30 years. He came to one of my workshops because he was never able to produce more than a 12- to 18-percent annual return on the accounts he managed.

This was an adequate return, but Bob was extremely dissatisfied because his analytical abilities suggested that he should be achieving an annual return of 150 to 200 percent. I would describe Bob as being well-versed in the nature of probabilities. In other words, he understood the concepts, but he didn't function from a probabilistic perspective. Shortly after attending the workshop, he called to ask me for some advice. Here is the entry from my journal written immediately after that phone conversation.

9-28-95: Bob called with a problem. He put on a belly trade and put his stop in the market. The market traded about a third of the way to his stop and then went back to his entry point, where he decided to bail out of the trade. Almost immediately after he got out, the bellies went 500 points in the direction of this trade, but of course he was out of the market. He didn't understand what was going on. First, I

asked him what was at risk. He didn't understand the question. He assumed that he had accepted the risk because he put in a stop. I responded that just because he put in a stop it didn't mean that he had truly accepted the risk of the trade. There are many things that can be at risk: losing money, being wrong, not being perfect, etc., depending on one's underlying motivation for trading. I pointed out that a person's beliefs are always revealed by their actions.

We can assume that he was operating out of a belief that to be a disciplined trader one has to define the risk and put a stop in. And so he did. But a person can put in a stop and at the same time not believe that he is going to be stopped out or that the trade will ever work against him, for that matter. By the way he described the situation, it sounded to me as if this is exactly what happened to him. When he put on the trade, he didn't believe he would be stopped out. Nor did he believe the market would trade against him. In fact, he was so adamant about this, that when the market came back to his entry point, he got out of the trade to punish the market with an "I'll show you" attitude for even going against him by one tic. After I pointed this out to him, he said this was exactly the attitude he had when he took off the trade. He said that he had been waiting for this particular trade for weeks and when the market finally got to this point, he thought it would immediately reverse.

I responded by reminding him to look at the experience as simply pointing the way to something that he needs to learn. A prerequisite for thinking in probabilities is that you accept the risk, because if you don't, you will not want to face the possibilities that you haven't accepted, if and when they do present themselves. When you've trained your mind to think in probabilities, it means you have fully accepted all the possibilities (with no internal resistance or conflict) and you always do something to take the unknown forces into account. Thinking this way is virtually impossible unless you've done the mental work necessary to "let go" of the need to know what is going to happen next or the need to be right on each trade. In fact, the degree by which you think you know, assume you know, or in any way need to know what is going to happen next, is equal to the degree to which you will fail as a trader. Traders who have learned to think in probabilities are confident of their overall success, because they commit themselves to taking every trade that conforms to their definition of an edge.

They don't attempt to pick and choose the edges they think, assume, or believe are going to work and act on those; nor do they avoid the edges that for whatever reason they think, assume, or believe aren't going to work. If they did either of those things, they would be contradicting their belief that the "now" moment situation is always unique, creating a random distribution between wins and losses on any given string of edges. They have learned, usually quite painfully, that they don't know in advance which edges are going to work and which ones aren't. They have stopped trying to predict outcomes. They have found that by taking every edge, they correspondingly increase their sample size of trades, which in turn gives whatever edge they use ample opportunity to play itself out in their favor, just like the casinos. On the other hand, why do you think unsuccessful traders are obsessed with market analysis.

They crave the sense of certainty that analysis appears to give them. Although few would admit it, the truth is that the typical trader wants to be right on every single trade. He is desperately trying to create certainty where it just doesn't exist. The irony is that if he completely accepted the fact that certainty doesn't exist, he would create the certainty he craves: He would be absolutely certain that certainty doesn't exist. When you achieve complete acceptance of the uncertainty of each edge and the uniqueness of each moment, your frustration with trading will end. Furthermore, you will no longer be susceptible to making all the typical trading errors that detract from your potential to be consistent and destroy your sense of self-confidence. For example not redefining the risk before converting it into a trade is by far the most common of all trading errors, and starts the whole process of trading from an inappropriate perspective. In light of the fact that anything can happen, wouldn't it make perfect sense to decide before executing a trade what the market has to look, sound, or feel like to tell you your edge isn't working? So why doesn't the typical trader decide to do it or do it every single time?

I have already given you the answer in the last chapter, but there's more to it and there's also some tricky logic involved, but the answer is simple. The typical trader won't predefine the risk of getting into a trade because he doesn't believe it's necessary. The only way he could believe "it isn't necessary" is if he believes he knows what's going to happen next. The reason he believes he knows what's going to happen next is because he won't get into a trade until he is convinced that he's right. At the point where he's convinced the trade will be a winner, it's no longer necessary to define the risk (because if he's right, there is no risk). Typical traders go through the exercise of convincing themselves that they're right before they get into a trade, because the alternative (being wrong) is simply unacceptable. Remember that our minds are wired to associate.

As a result, being wrong on any given trade has the potential to be associated with any (or every) other experience in a trader's life where he's been wrong. The implication is that any trade can easily tap him into the accumulated pain of every time he has been wrong in his life. Given the huge backlog of unresolved, negative energy surrounding what it means to be wrong that exists in most people, it's easy to see why each and every trade can literally take on the significance of a life or death situation. So, for

the typical trader, determining what the market would have to look, sound, or feel like to tell him that a trade isn't working would create an irreconcilable dilemma. On one hand, he desperately wants to win and the only way he can do that is to participate, but the only way he will participate is if he's sure the trade will win. On the other hand, if he defines his risk, he is willfully gathering evidence that would negate something he has already convinced himself of.

He will be contradicting the decision-making process he went through to convince himself that the trade will work. If he exposed himself to conflicting information, it would surely create some degree of doubt about the viability of the trade. If he allows himself to experience doubt, it's very unlikely he will participate. If he doesn't put the trade on and it turns out to be a winner, he will be in extreme agony. For some people, nothing hurts more than an opportunity recognized but missed because of self-doubt. For the typical trader, the only way out of this psychological dilemma is to ignore the risk and remain convinced that the trade is right. If any of this sounds familiar, consider this: When you're convincing yourself that you're right, what you're saying to yourself is, "I know who's in this market and who's about to come into this market. I know what they believe about what is high or what is low. Furthermore, I know each individual's capacity to act on those beliefs (the degree of clarity or relative lack of inner conflict), and with this knowledge, I am able to determine how the actions of each of these individuals will affect price movement in its collective form a second, a minute, an hour, a day, or a week from now."

Looking at the process of convincing yourself that you're right from this perspective, it seems a bit absurd, doesn't it? For the traders who have learned to think in probabilities, there is no dilemma. Predefining the risk doesn't pose a problem for these traders because they don't trade from a right or wrong perspective. They have learned that trading doesn't have anything to do with being right or wrong on any individual trade. As a result, they don't perceive the risks of trading in the same way the typical trader does. Any of the best traders (the probability thinkers) could have just as much negative energy surrounding what it means to be wrong as the typical trader.

But as long as they legitimately define trading as a probability game, their emotional responses to the outcome of any particular trade are equivalent to how the typical trader would feel about flipping a coin, calling heads, and seeing the coin come up tails. A wrong call, but for most people being wrong about predicting the flip of a coin would not tap them into the accumulated pain of every other time in their lives they had been wrong. Why? Most people know that the outcome of a coin toss is random. If you believe the outcome is random, then you naturally expect a random outcome. Randomness implies at least some degree of uncertainty. So when we believe in a random outcome, there is an implied acceptance that we don't know what that outcome will be. When we accept in advance of an event that we don't know how it will turn out, that acceptance has the effect of keeping our expectations neutral and open-ended. Now we're getting down to the very core of what ails the typical trader. Any expectation about the market's behavior that is specific, well-defined, or rigid—instead of being neutral and open-ended—is unrealistic and potentially damaging. I define an unrealistic expectation as one that does not correspond with the possibilities available from the market's perspective. If each moment in the market is unique, and anything is possible, then any expectation that does not reflect these boundary-less characteristics is unrealistic.

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