What I Wish Someone Had Told Me 20 Years Ago

A Book About Getting Started in Trading

By Tom Hougaard

WHY DO MOST TRADERS FAIL?

WHY DO FEW TRADERS SUCCEED?

WHAT IS THE DIFFERENCE BETWEEN THE TWO?

WELCOME

Have you ever been to a talk or a presentation, and when you came home that night, you wished you had taken better notes? You remember the broad themes of the presentation, probably some of the stories, but many important details are gone from your memory.

I was asked by a CFD broker in Denmark if I wanted to give a talk on trading. Although I don't use the broker myself, I said I would do it, if I could give a talk about trading on the topics that I considered vitally important to profitable trading.

They agreed, and everyone was happy. The broker's clients were particularly happy. The broker had invited some 700 guests over two evenings to attend the event. I gave a passionate speech about what I felt constituted good trading. The feedback was great.

I gave out my email to the delegates during the talk, telling them they could email me if they wanted a copy of the presentation. I received 750 emails, requesting the presentation. A little odd, as only 700 attended, but I suppose word got out.

I wrote the speech using PowerPoint as my visual aide. The theme of the speech was to describe what it is like to trade for a living. I wanted to give a talk about the "secret" ingredient that no one really talks about. I didn't want to give a talk about trading and technical analysis. I wanted to give a talk about what is needed to make money beyond just technical analysis.

I knew there would be many younger people there too, and I also wanted to describe to them what it was like to venture out along this career path. What made me risk my safe career path for something as unstable as being a trader.

However, the book you are holding in your hand, was never my intention to write. This project started off very differently to how it ended. I wrote a lengthy PowerPoint presentation, one that covered everything I could think of that has significance and importance to the goal of being a home trader.

Then it dawned on me that it seemed silly that only the 700 who attended the talk would get the benefit of these PowerPoint slides. It also occurred to me that those 700 people, who did benefit from attending the two evenings, would forget most of the pearls (modestly speaking, of course) that was presented to them.

That is how this book came about. I don't regret doing it, but it turned out to be a significant undertaking, one that took a lot longer than I had anticipated. It was worth it though. A speech, after all, is so much more than just a PowerPoint presentation.

It turned into a marathon speech too. I don't know why I thought I could go through 170 PowerPoint slides during a 2-hour speech, and of course, I couldn't. I had to drop quite a few slides as time ran out.

The pages ahead essentially contain everything I wanted to say to each slide. As you go through the pages, you will see the actual slide from the PowerPoint Presentation inserted as well. You may want to make a note of the text on the PowerPoint slide too.

What to Expect

The pages ahead is telling my story, from reading a book about trading as a young man, to studying in the UK, to working for an American Investment Bank, to being a self-employed trader, to working for a major CFD broker for 10 years, to being made redundant and having to make money from trading as a "home trader".

The first few pages are focused on my journey to the trading industry, and how I got there. I wrote those pages for the benefit of the young people attending the talk, who were perhaps inspired by what I have accomplished. Since I don't consider myself a light in the academic world, I thought it would provide some inspiration to those who have a lot of "go get" attitude, but who perhaps lack a little in the academic suitcase. If you have both, the academic light and the "go get" attitude, there is no telling how far you will go.

20 Years Ago

This is the talk I would like to have heard 20 years ago. It would have saved me a lot of time and wasted hours. Maybe I am being unnecessary hard on myself. I don't think I wasted my time, but I did pursue paths that turned out to be a waste of my time. I suppose that in itself is a lesson. I think I would have been profitable sooner though, had I had what you have in your hands right now.

Sadly, there was just no one around to tell the story at the time. Trading amongst private individuals was not a common thing. Of course, home traders existed, but they were like warm summers in Denmark. You had heard about them, but you had never actually seen one. I had to figure it out myself. It took time. My hope is that this book can cut your learning curve down.

My Name

I realise I haven't even introduced myself to you. My name is Tom Hougaard. I am a trader.

If you had asked me 20 years ago, what I would give to be able to utter those words, I would have replied: "Anything".

Today, the answer hasn't changed, but my knowledge of trading, my knowledge and perspective of the art of this game, has changed. The last 2 decades of my life has been either working for a CFD broker or trading CFDs for myself. 20 years ago, I had an idea of what it would take to be a great trader. Today my answer is very different. 20 years ago, I would have said market knowledge. Today I would say self-knowledge and market knowledge. Don't worry, this is not a New Age hippie book, asking you to get in touch with your inner self.

The essence of this short book is to answer many of the questions that I wish I had an answer to 20 years ago. The essence of this book is to guide the newcomer. It is also a book for those who have a significant amount of trading experience. You and I know that trading is so much more than what you see on the screen.

I hope I am successful in this spirited and ambitious endeavour to enlighten the road ahead of you. If I fall short of my lofty goal, then I would love to hear what you think is missing. If I have failed to answer a question, then drop me a line: hello@tradertom.com.

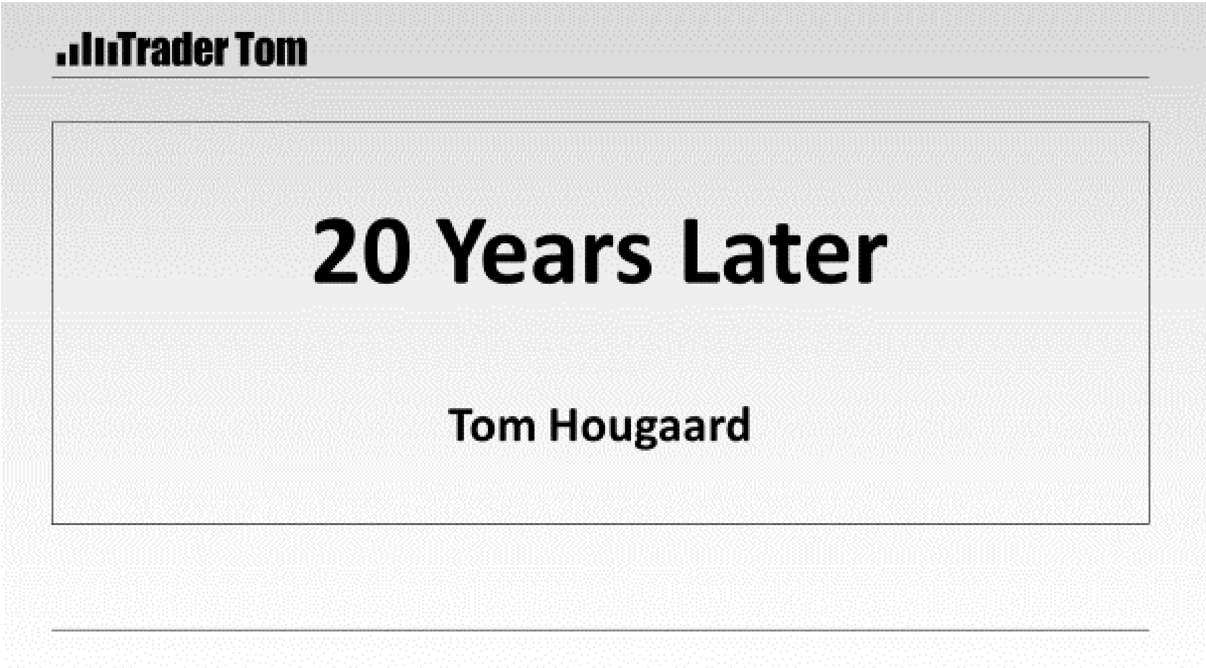
I hope you enjoy it. A special thank you to the 700 people at Saxo Bank who turned up to hear me speak about my great love, the financial markets and how to navigate them to make a dollar or two. I want to thank you for making it a memorable moment for me, and I thank you for your patience in waiting for the notes.

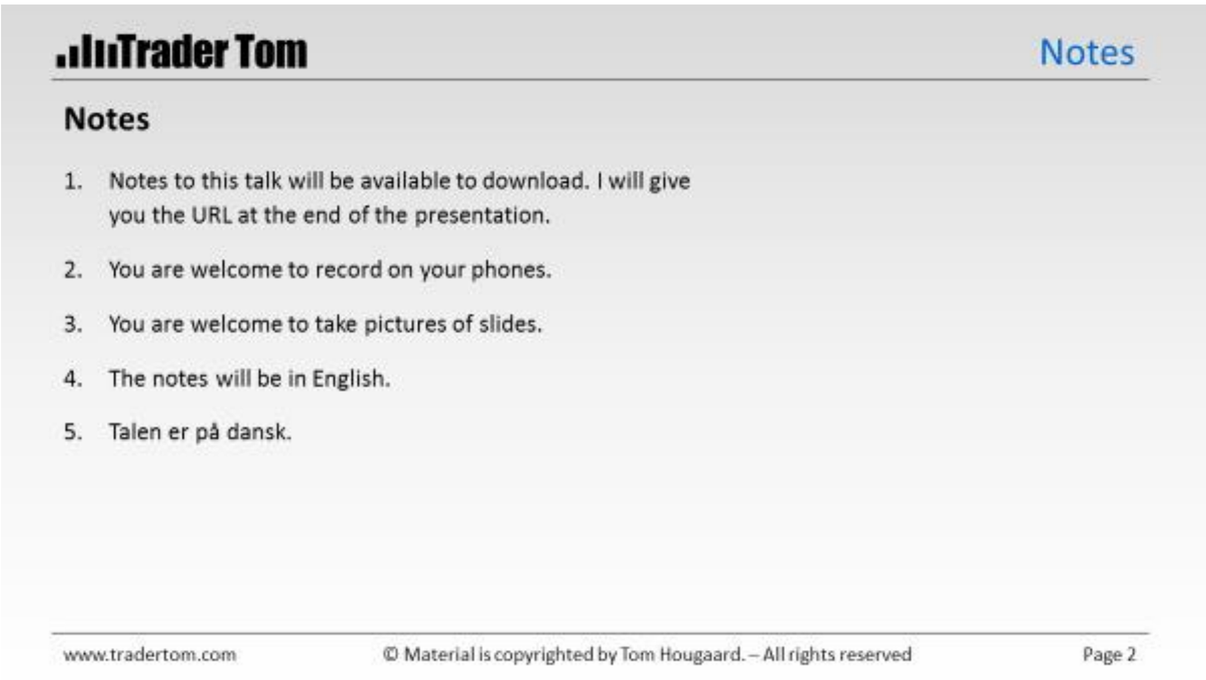
Tom Hougaard

October 2019

20 Years Later

Welcome to the presentation. I have called it "20 Years Later". It is the presentation that I would like to have heard 20 years ago. It would have taught me a lot about trading the financial markets, things that I had to learn the hard way by myself.





If you are new to trading, this book will guide you to a successful path. If you have traded for a while, and you know you haven't reached your full potential, I want to assure you that I have no intention of teaching you a "secret technique". Rather I would like you to read these pages with an open mind and consider the suggestions that I make within. If it is at all possible, do not let your ego get in your way by telling you that you don't need to read these pages, because you already know all there is to know. If you already know enough about technical analysis, then the answer to trading success is not more technical analysis.

This is not a book about technical analysis, but then again, even if it was, technical analysis has never made anyone wealthy. It is not trendlines and Fib Ratios and Bollinger Bands that makes people rich in trading. It is something entirely different. That is what this book is about. Yes, it contains many technical elements, but at the heart of the book is a desire to show you what makes good traders good, and how you can acquire the right approach to trading.

Who Am I?

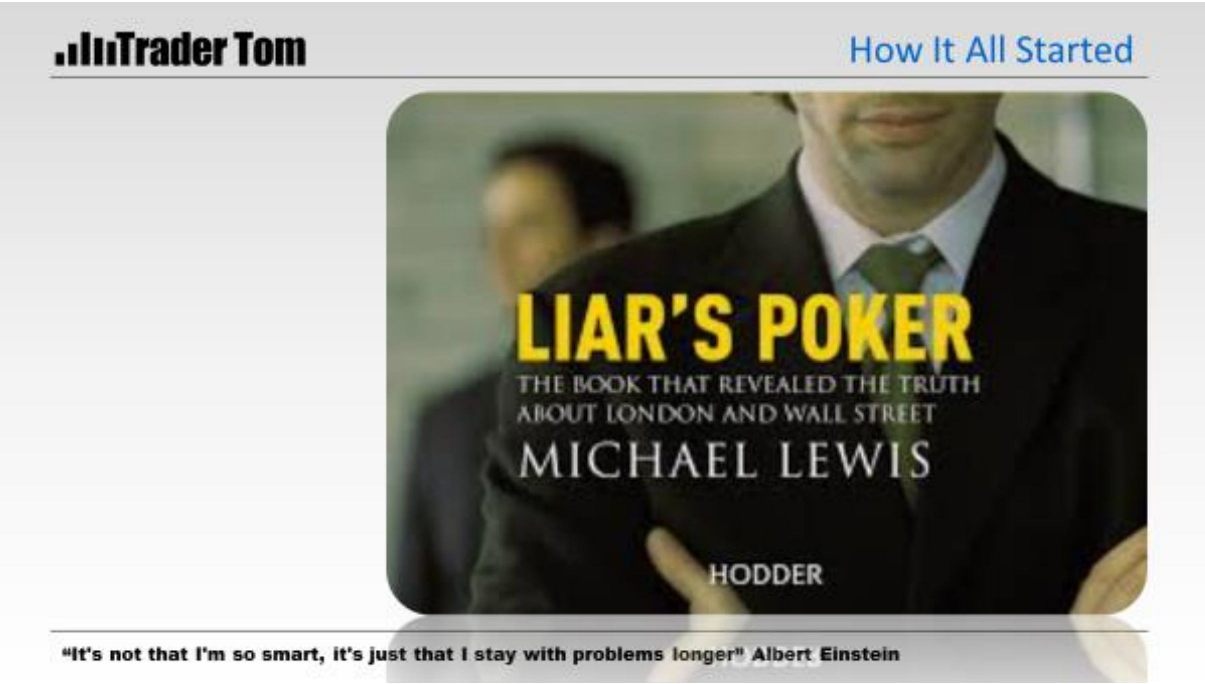
Who am I? My name is Tom Hougaard. I was born in Denmark in September 1969.I have a BSc in Economics and a Masters in Money Banking and Finance. None of those qualifications are relevant for trading! Indeed, they can be a great barrier to profitable trading.

My career highlights by and large are contained to working for JP Morgan for three years. I then became a home trader for a year and a half. It only lasted 18 months because I lost my money trading and I ran out of funds to live with. At that point I had applied to and been offered a job at Financial Spreads, a CFD broker in London. I started there in May 2001.

In 2009 I was made redundant and I have been a private trader ever since. As a little joke I wrote "Private Trader from 2009 to 2079". I am merely making an argument that if I don't drink alcohol, smoke cigarettes and drink sugary drinks, I should at least live till I am 110 years old and I hope to be a home trader till the day I die.

Liar’s Poker

My journey, the story I want to tell you, started when I came across a book called Liar’s Poker. Liar’s Poker is a period piece. It is an attempt by Michael Lewis to describe the excesses of the 1980s. In his own words it was meant to serve as a warning to future generations about the excesses of the finance industry, as well as serve as a warning to young people wanting to work in the financial industry.



I have to say that I find that amusing. I love Liar’s Poker. It served as an introduction to Wall Street and London for thousands of young men and women, who all wanted part of the action. It describes a young man travelling from America to Britain to study at a London university and subsequently being hired to work for an American Investment Bank. Salomon Brothers was at the time one of the biggest finance houses in the world.

The book describes what it was like to work as a sales trader and observe some of the big traders there. I was hooked, and I knew trading would be my vocation. I have since read many other trading books that are perhaps more specific about trading than Liar’s Poker, but as a starter book, I could not have asked for anything better.

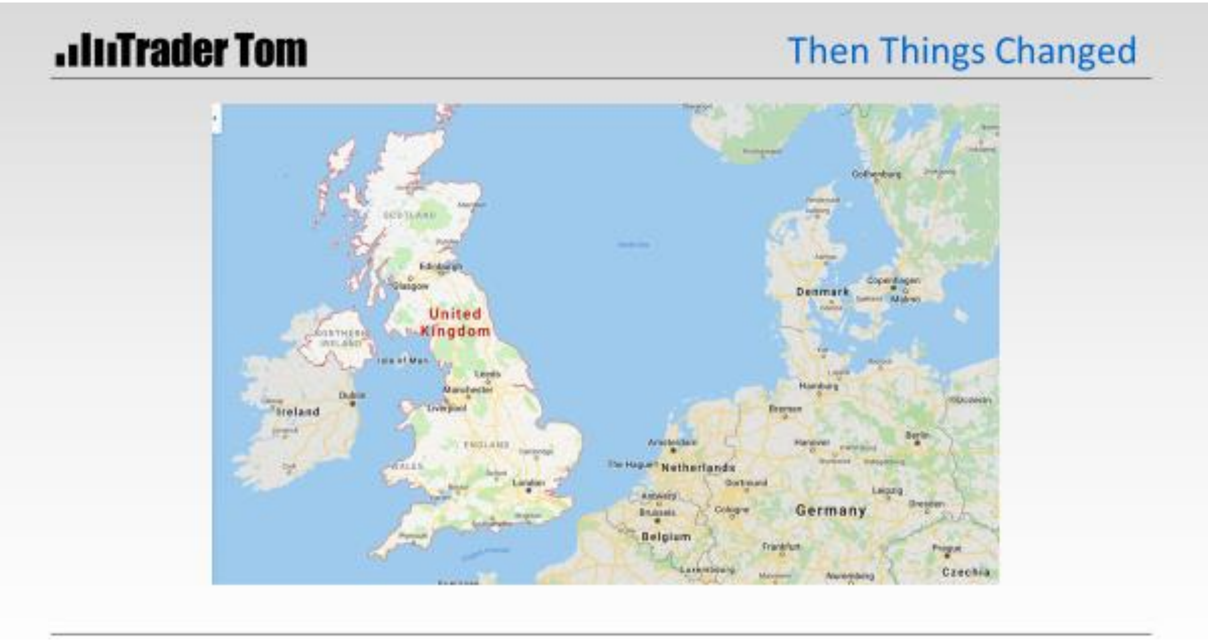
My life changed. It was a wake-up call. There is no doubt in my mind that my life changed after reading Liar’s Poker. I went from being a skateboard loving, football adoring, girl chasing young man, to being something entirely different. It was as if I had found my calling.

I started applying to university degree courses around Europe. I got a job at a pension fund. I figured it would have something to do with “the markets”. I worked all hours I could, day and night. During the day I would work at the pension fund and in the evening, I would race out to an amusement park in order to work there until 1am.

During the day I would absorb as much information as I could from Danish finance pages. I would read English books to improve my language skills. Incidentally, the first book I read to train my language skills was a book about global warming.

When I explain to my children how I went about selecting a university in the UK they cringe. Everything was done by snail mail. I remember having to sit a language test at the British Institute in Copenhagen, while in the office next door, someone was having a blazing argument with someone else. So much for peace and quiet.

I also vividly remember opening my mailbox and seeing the envelope that would contain my acceptance letter to a UK university. It was a big moment for me. My family was less than supportive. On the big day of departure, I had to make my own way to the airport. It got better. When you know something is right in your heart, nothing can stop you.



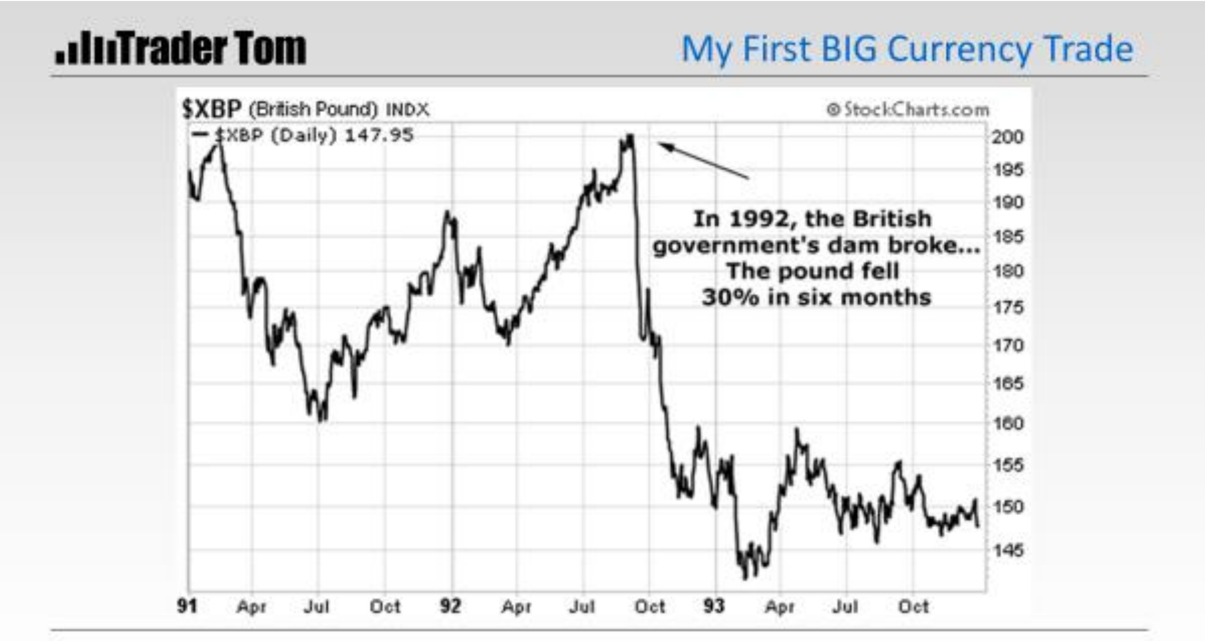
I made the journey from the safety of little Denmark to a big and pulsating Britain and I attended two different universities. I left home when I was about 21 years old and I have been away ever since. I have lived in many places around the world. The world has become a lot smaller in the last 30 years. Back when I started out, the world didn’t have the information technology and information infra-structure that we have available to us today. I am only telling you this to enlighten you to the fact that there has never been a better time to be a trader.

My First Big Trade

The hard work paid off in more than one respect. I was accepted to a good university in England and I got a taste of what real hard work meant. I was also incredibly lucky. I mean – REAL LUCKY. In 1992 England crashed out of the European Monetary System, although you might know it as the ERM, the Exchange Rate Mechanism.

Its purpose was to keep currencies within a tight band vis-à-vis each other. However, The United Kingdom was in a recession and had been for about 18 months. The Bank of England found it more and more difficult to maintain their currency within a tight band against other currencies within Europe.

So, as I was walking down to the bank with my 120,000 Danish kroner, looking to exchange them to British pounds, a major drama was unfolding in the financial markets.



This was of course all unbeknownst to me, yet it had a material impact on my studies. Had I walked down to the bank just a few weeks earlier I would have had to pay 11 ½ Danish kroner for one pound. But by sheer luck I walked straight into, and benefited from, one of the biggest currency-crashes the world had ever witnessed, and I was able to convert my Danish kroner at an exchange rate of about 9 ¼ as opposed to 11 ½.

It meant the difference between taking up a student loan to survive and not taking up a student loan. This may not make much sense to you, but you must understand that my annual budget was about 3000 pounds. I was just given an extra 2,600 pounds because of the weaker exchange rate.

On the chart above, the logic is very clear. You are seeing the price of an English Pound, expressed in Danish Kroners. The lower I could buy it, the better. As I said, I got very lucky.

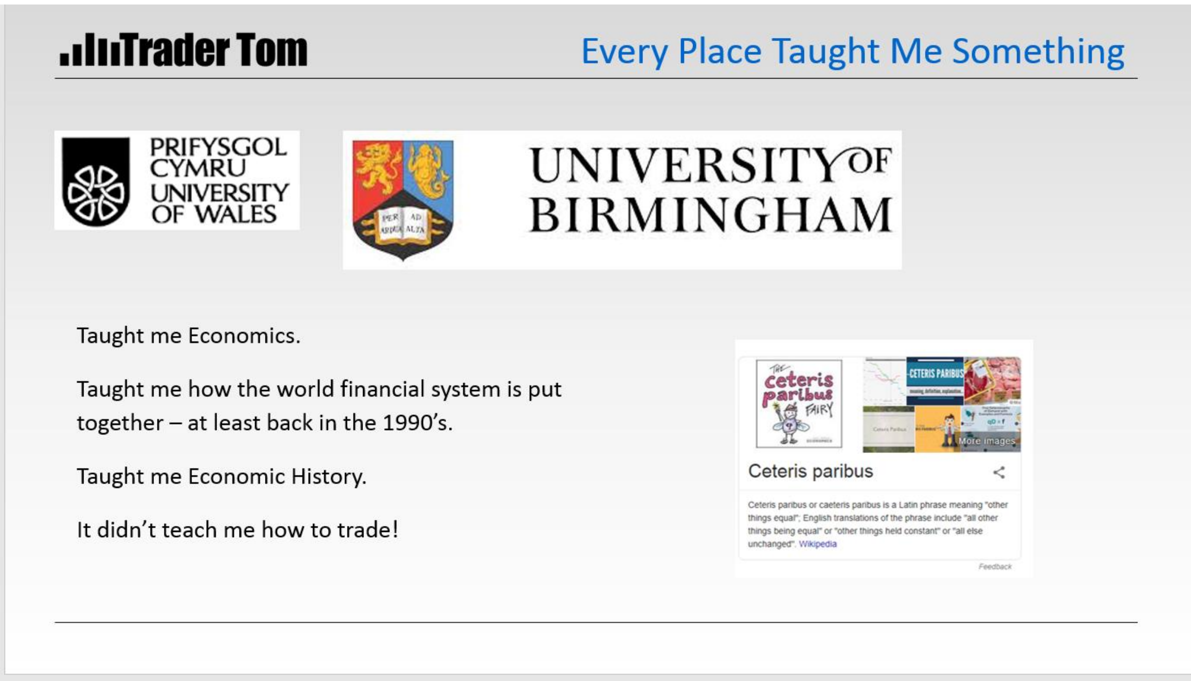
So, to me, George Soros, an international trader/speculator extraordinaire, and one of the major protagonists in the story of the plunging Pound in 1992, is one of my biggest heroes. He helped me go through my university education without having to borrow as much as a penny. Thank you, sir, ☺.

Slide 10

Slide 10 was relevant to the people I gave the speech to in Denmark. As it is not relevant to you reading these pages, I will omit it here. It contained a reference to a local TV program in Denmark.

University

Studying at university taught me what there was to learn about economic theory, and it taught me about how the financial markets were put together and how current economic theory tried to make sense of the world around us.



However, it didn't teach me how to trade. It didn't teach me how psychology and sentiment have a major influence on the financial markets. The major objection I had with my Economics degree course is an expression we called "ceteris paribus", or "other things being constant".

The idea is that you can test variables within an economic system, by holding other components constant. For example, you can test an economic system by varying interest rates, but you hold say productivity or employment fixed.

I saw the world differently. I enjoyed studying economic history more than I enjoyed studying models of the world. One of the pivotal moments came when studying the Rich Man's panic in 1903 and 1907. Bernard Baruch, a famed Wall Street speculator, made a substantial amount of money by correctly anticipating the consequences of a failed "corner" of a railroad stock.

A "corner" is when a group of people or a syndicate is inflating the price of a stock, in order to create a buzz, thus trying to entice more gullible investors to join the bandwagon, and then off-load the stock to the late comers.

What made an impression on me was how Bernard Baruch anticipated the sequence of events. He started to sell short a broad range of popular stocks, because he reasoned that the syndicate would have to raise money to keep their ill-fated "corner" alive, by selling out of their general stock portfolio. He was right. The general market declined rapidly. The Dow Jones index fell 49% in a few months. As the saying goes, he "made a killing."

From then onwards it became difficult to study economic theories. I found it was too theoretical in concept. I felt it made assumptions that made it a fallible structure. I am certain that my economic professors would be upset about my comments or turn in their graves. I just didn't think the world worked how it was portrayed in the lessons I took.

I have no doubt that economic factors will drive a market up and down. However, as a day trader I need to have a mental flexibility that is never described or accounted for in economic theory. I have seen markets fall on good news and I have seen markets rally on bad news.

To my mind the markets are made up of participants who have very different agendas timewise. There will be people hedging their exposure. There will be people who are speculating on one direction or the other. Within that group there will be speculators who anticipate a certain price movement over the next 30 minutes and there will be investors who at the same time will want to take a position for the next six months.

I don't think that economic theory has any value for a day trader. I will want to repeat that sentence. I simply do not think that economic theory has any value for a day trader. I am very careful about how I interpret news items. Only yesterday evening I traded the Dow before the close. It was a wildly bullish day. The Dow was up 500 points with 5 minutes to go of the trading day. Then for no reason, it falls 200 points in 5 minutes. Explain that economic theory!

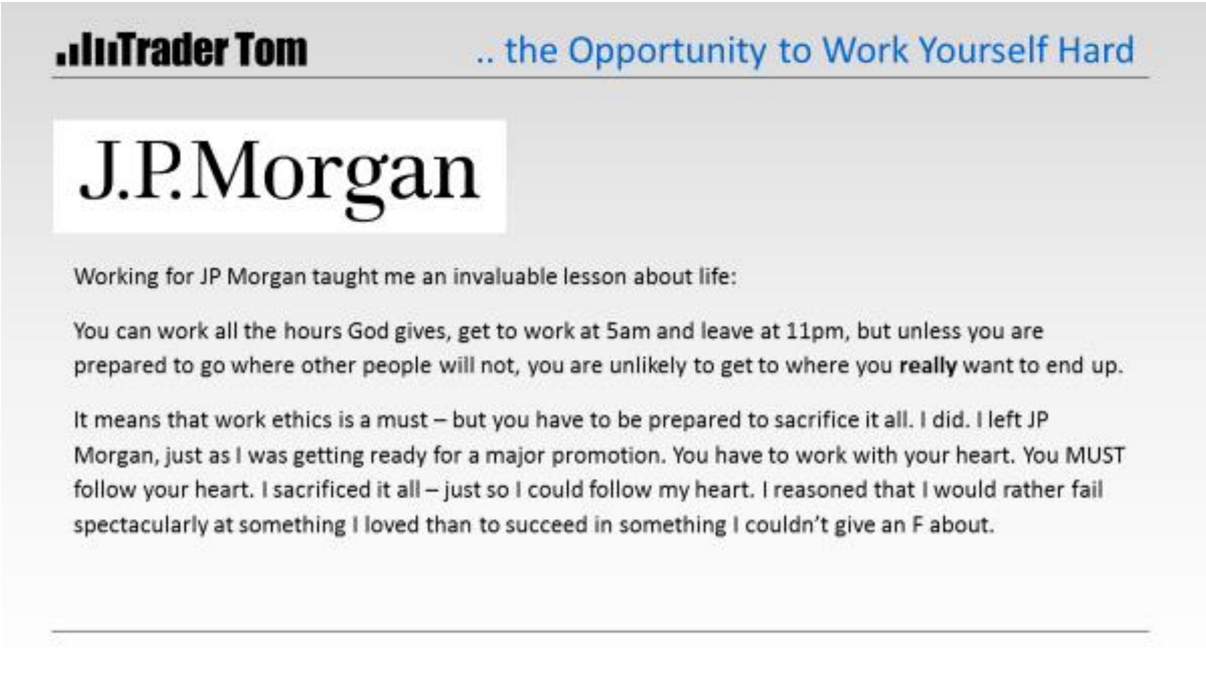
As I type this, in 2019, the world is witnessing something that no one thought would be possible. We are seeing negative interest rates in many places globally. If I had raised my hand in 1992 and asked my professor if we would ever see a day where people had to pay a penalty to have their money in the bank, he would most likely have sent me to have my head examined.

JP Morgan

After my graduation I tried for many graduate jobs within the banking and finance industry. I didn't get my dream job, working as a trader trainee, but I did get a good job working for Chase Manhattan Bank, later JPMorgan Chase. It was an invaluable experience. I arrived with a lot of energy and a lot of go-go courage. Working for an American investment bank is probably the best thing that could ever have happened to me.

I was able to channel my enthusiasm for the financial markets into my work. I worked with portfolio analysis and performance benchmarking, which meant I was able to observe the financial markets unfold before my eyes every single day. I happened to sit right next to a

Bloomberg terminal. I loved that machine. I would often sneak into the office building on Saturdays and Sundays to devour economic news and trading stories and download data.



The great thing about working for an American Investment Bank is that there is a very different work ethic than you will find in a typical European company. This may have changed in the last 20 years, but when I was working at JPMorgan we were literally allowed to work as many hours of overtime as we wanted to. The work was there if we wanted it.

I worked for the bank for close to 3 years and in those three years I never had a work month where I didn't do at least 40 hours overtime. It taught me how to stay focused during long hours of concentrated work, so when I left JPMorgan in late 1999, I was a hardened and seasoned workaholic. I don't say that with pride, but I don't think there is any point in hiding the fact that the reason for my success was not due to immense intelligence, but rather my work ethic. I just worked more than the others, longer hours. I made the sacrifice for what I wanted.

The paradox became evident when I walked onto a trading floor about two years later. I arrived with a bag full of enthusiasm and an almost unlimited amount of energy, coupled with an unrivalled work discipline. However, if the markets are quiet, a trading floor can be a very unusual place to work.

What I found was that people would sit around and read the newspaper or comic books, if there was nothing to do. If the phone didn't ring, you could hardly force a broker to do anything. I think this was the biggest culture shock I experienced, the contrast between a normal office job and a trading floor.

Yet I don’t regret for one second making the transition from a good career job to a job as a trader. I feel very strongly about working from your heart rather than from your mind. You must follow your heart in everything that you do. I sacrificed all forms of job security, so I could follow my heart.

I left Denmark so I could follow my heart of studying abroad and hopefully end up in a trading job. I sacrificed a promotion at JPMorgan so I could follow my passion, and I reasoned, and I still to this day reason that I would rather fail spectacularly at something I love doing than to succeed in something I couldn’t give a flock about.

Slide 13

Slide 13 was relevant to the people I gave the speech to. There were parts of slide 13 I wish I could have edited out. As it is not relevant to trading anyway, I have omitted it here.

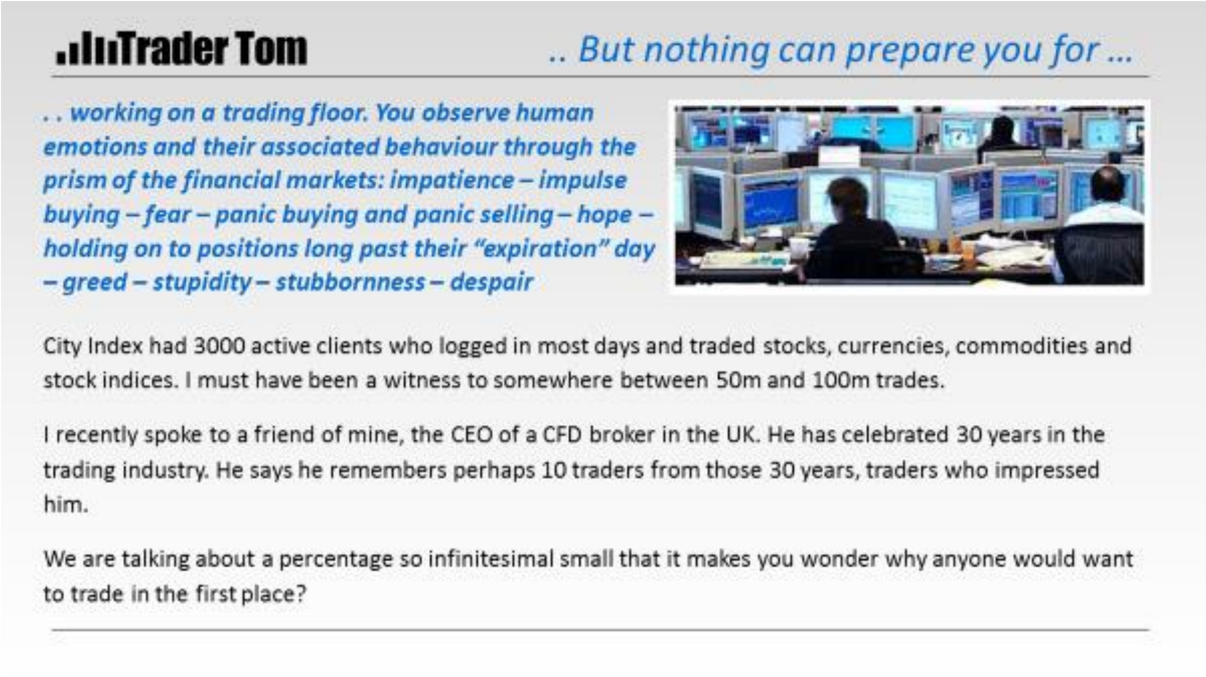
Trading Floor

Walking onto a trading floor is a special experience. I remember vividly being interviewed for a trading job after my university graduation. It took place on the trading floor, while the guy was watching the markets as well as interviewing me. You could tell that he was intensely focused on something, and I was an inconvenient distraction.

I have been in that situation MANY times in my life. I have made a commitment to someone or something, and the markets kicked off. Boxing day 2018 is a great example. I am trading the biggest one-day rally in the history of the Dow Jones index, while eating Xmas pudding. I had to hide my mobile phone under the dinner table so not to offend my host, and I had to fake numerous trips to the toilet so I could watch on a chart on my mobile phone what was going on in the markets.

Working on a trading floor is a special experience. There is a unique atmosphere there. It is nothing short of a gigantic melting pot of human emotions. It is hard to believe that the financial markets are a complex mechanism, if you just look at what is going on at a trading floor. It reminds you more of a local market stall on a busy Saturday morning, where one stall owner is trying to out-voice the next stall owner.

When you witness the raw barbaric emotions that unfold before your eyes on the trading floor, it is difficult to see how that fits into a finely tuned global economic environment that makes up the very fabric of our modern society and civilisation.



Working on a trading floor gives you front row access to observe the financial markets through the prism of human emotions and their associated behaviour. Here you see things that you would normally associate with anything but an orderly and logical financial market.

Raw emotions are freely being shown for the whole world to see. Impulse buying, panic selling, holding on to losses, refusing to admit defeat, greed, stupidity, stubbornness, despair, tears and abject depression or exhilaration and excitement, and all in quick succession of each other.

I got a job at a firm called City Index. It was owned my Michael Spencer, the founder of ICAP, the biggest US Government Bond broker in the world. City Index had about 25,000 clients, of which 3,000 were active most days. These clients would trade currencies, commodities, stock indices, individual stocks, options, bonds and anything in between. I estimate that I must have witnessed somewhere between 50 million and a 100 million trades in my career.

Honest Talk From CEO

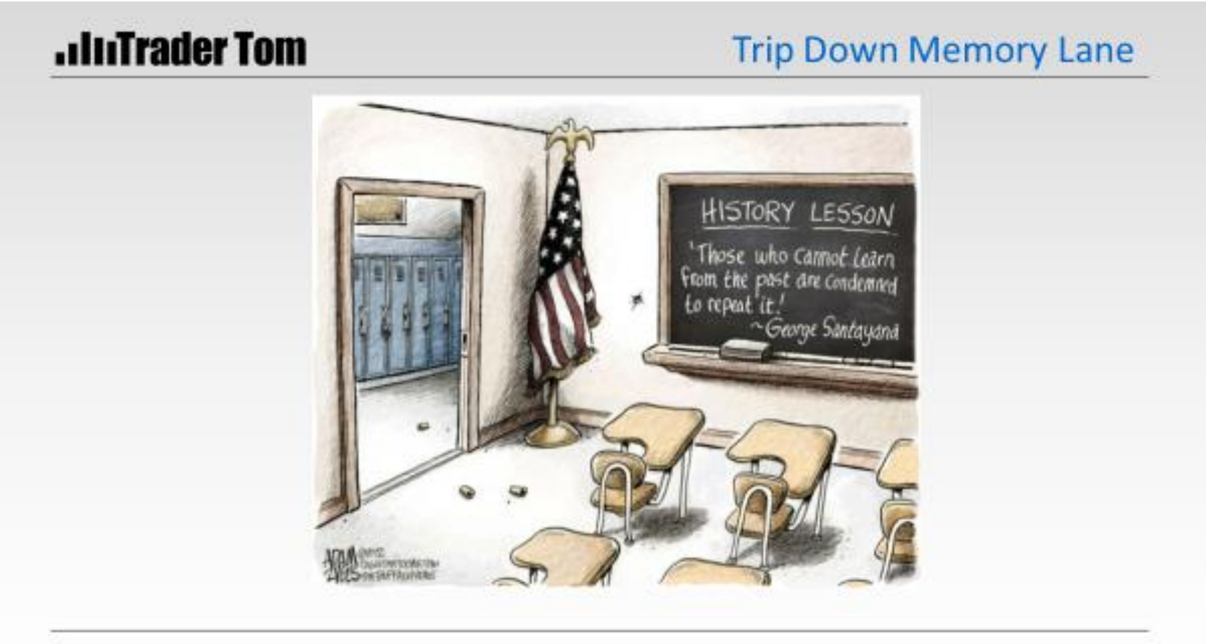
I recently spoke to a friend of mine, who is the CEO of a CFD company in London. I asked him if there were traders who had stuck out in his mind over his last 30 years on trading floors. He said that over the last 30 years he had witnessed many bizarre things, but in terms of good traders, he had seen very few.

Here is a man who has spent his entire adult life on trading floors. Yet he is incapable of remembering people who did well. We are talking about a percentage of successful traders so infinitely small, that it makes you wonder why anyone would want to trade in the first place, or if anyone could ever get good at this profession. I will return to my CEO friend in a moment, but first I want to take a trip down memory lane, so you can appreciate that the game of trading never changes.

Conditions 20 Years Ago

I keep an eye on all brokers, in order to make sure I trade with the best and cheapest broker. If you want a tip, email me. My contact details are at the end of the book. Today when I trade, I pay a 1 point spread in the Dax. The spread is the difference between the buy and sell price.

Sometimes I even pay as little as 0.9 or 0.8. However, when I started trading some 20 years ago, the spread intraday in the Dax was 6 to 8 points. I remember trading the Dow intraday. You had to pay an 8 point spread in the Dow for the intraday product.



If you wanted to trade the quarterly contract the spread was 16 points. This was at a time when the Dow was trading around 10,000. Today I am trading the Dow with a 1 point spread and Dow is now trading around 26,000. You are much better off trading in 2019 than you were trading in 1999. It was much harder to make money trading in 1999. The market has to move significantly less in your direction before you are at breakeven than it had to back in 1999. Yet despite all these advantages trading has not become any easier.

Slide 16

Another major advantage that people who start trading today have is the tools available from the brokers. Take a look at the Saxo Bank's platform. I highlight Saxo Bank here, not because they are Danish, but because the speech I gave was to their clients.

Here you see a broker that has provided pretty much everything and anything for their clients. You have access to news. You have access to level II data from stocks all over the world. You have decent bid-ask spreads. If an institutional trader from 30 years ago saw the tools that you are trading with today, they would be green with envy.

You have at your disposal every single conceivable analytical tool available from the vast resource pool of technical indicators. You have Bollinger Bands, you have Keltner channels, you have moving averages, you have tools that I have never even heard of or used myself.

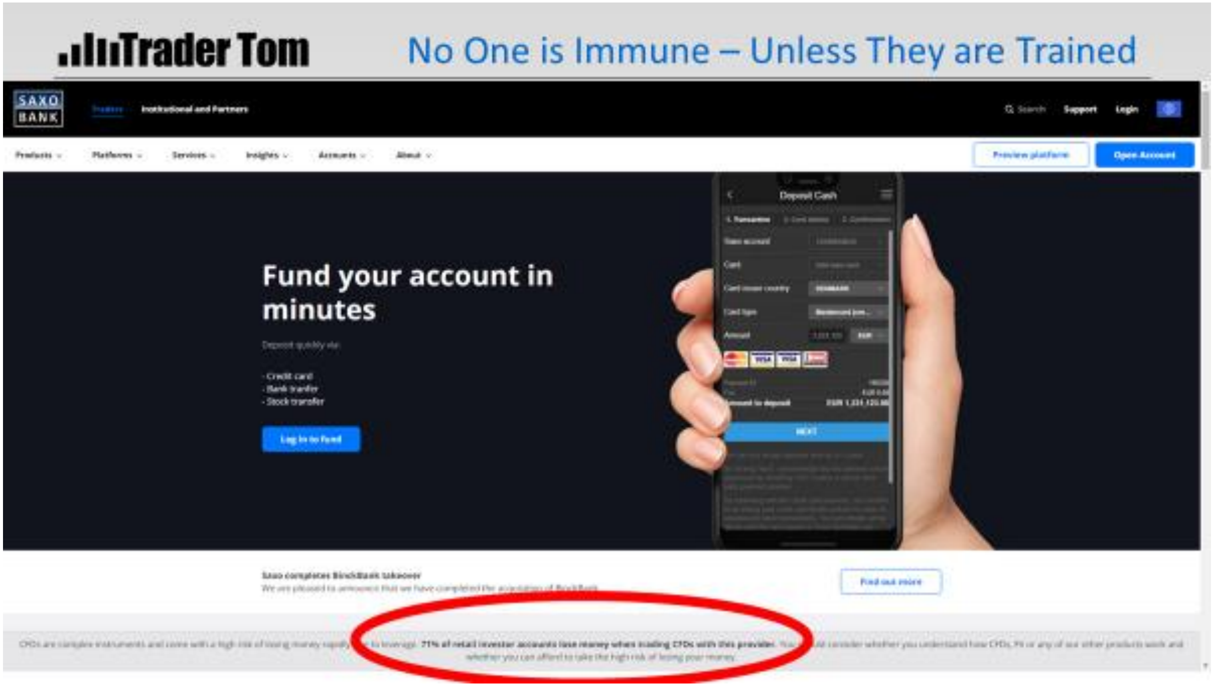
Suffice to say Saxo Bank and every other broker in the world have spared no expense in their effort to provide you with every opportunity to make as much money as you possibly can out of the markets. BUT it matters nothing. It really doesn't matter at all.

No One is Immune

Yet even though you have all those tools available to you and much more, no one is immune to the statistics of the financial markets. Unless you have gone through structured training or have been schooled by someone who is walking the path you yourself want to walk on, or you give this endeavour some serious thought, you will most likely fail to make a success of your time in the financial markets.

See for yourself!

Despite all the tools and bells and whistles Saxo Bank makes available to their clients, more than 70% of their clients lose money trading with them.



The text in the red circle says that 71% of all Saxo Bank clients lose money when trading CFDs.

Now please don't get me wrong, this is by no means a slight at Saxo Bank, nor is it an indication that Saxo Bank is anything but a well-meaning broker. You can look at the top 10 brokers of the world and the statistics do not change. You can look at CMC Markets, you can look at IG Markets, you can look at Gain Capital or you can look at any one of the top tiered or second tier CFD brokers. No one will have a statistic less than 65 to 70%.

There is one exception to that. I found a broker that has a 59.6%. I suspect it is because of their tight fixed spreads. The difference between the bid and the ask price is called the spread, and it does matter immensely to your trading how much you pay in spread. It is the silent commission.

So, what is the point that I am trying to get across to you?

Well that is a good question. What I'm trying to do is to make you see trading for the holistic enterprise that it really is. I am doing my best to make you understand that fundamental analysis or technical analysis or whatever tool you are using for your trading will simply not make you money over time, unless you add another ingredient to your trading. This ingredient is not easy to acquire, mostly because people are looking in the wrong place.

I do not want to sound like I am talking in riddles, but I accept that I am right now. Please carry on reading, and I will slowly but surely unveil what this ingredient is.

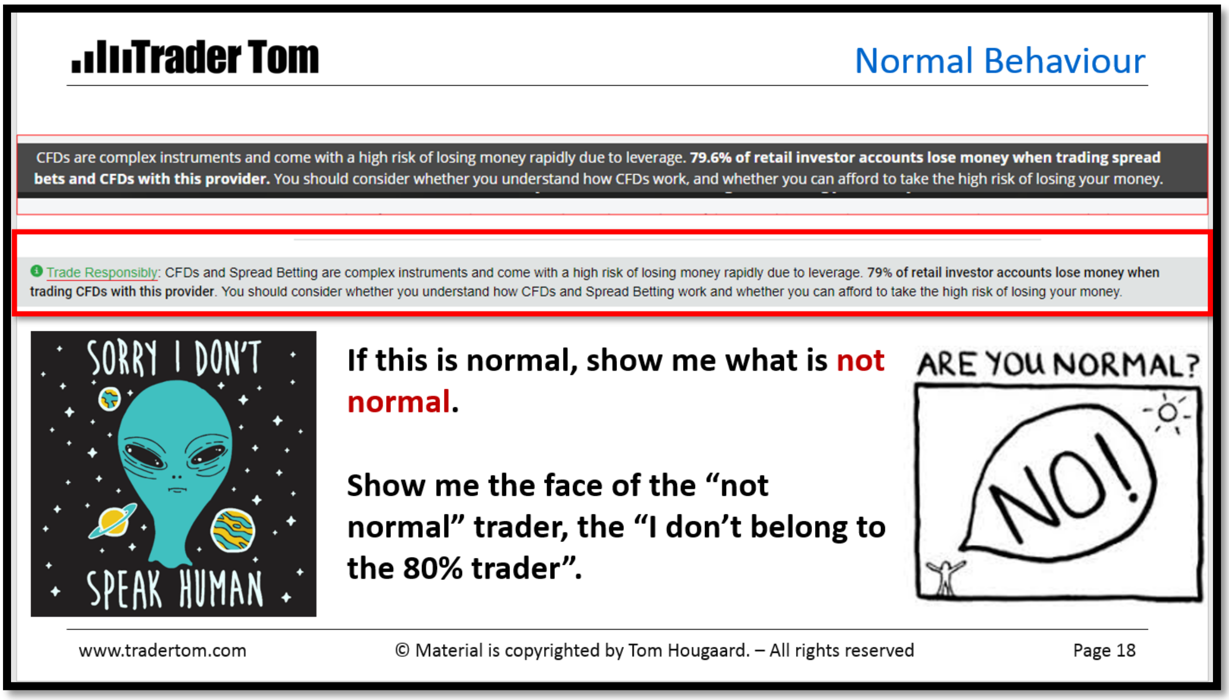
Normal is Bad

You may be sitting in the audience here tonight* thinking "*I thought this seminar was about how to make money trading. I thought I was going to learn tools and tricks that would help me in my trading.*"

(****author note***: *"in the audience" – reference to this being notes from a speech I gave*)

Well you are. I'm just not presenting it in a way that you had anticipated. And if you will allow me a moment of mischievous teasing:

If I gave you exactly what you thought you wanted and needed, it would not make a blind bit of difference to your trading tomorrow and in the years to come.



If you want to be a good a trader, if you want to achieve the level of success that you know is possible, you immediately need to stop thinking that the path to riches in trading has anything to do with the tools or techniques you are using.

Yes of course you need a strategy. Yes, you need a plan. Yes, you need to understand the markets. So, what is this talk all about, if it is not about tools and strategies? Well, let me address that question from a different perspective. Let me address it from the perspective of the people who work in the industry as brokers and sales traders and as marketing people.

When you go to trade shows, 100% of the focus by the exhibitors displaying their products is what I call "How To". How do I scalp? How do I swing trade? How do I day trade? How do I trend follow? How do I trade the FX market? The trade shows are geared towards providing you with solutions to what most people believe is what is needed to make money in the financial markets.

As a newcomer to the industry of trading, you are most likely guided by the very people who are likely to set you off on the wrong path. You are led to believe that it is all about technique and strategy, and no one is preparing you for the fact that it isn't strategy that will set you apart from other traders. It is how you think about your strategy and your ability to follow the strategy that will set you apart. If "strategy" was all there was to trading, it would be easy.

I was invited by the organisers of one of these trade shows. This one was in London, and I was told I could talk about whatever I wanted to. I decided to give a talk about the disastrous failure rate in the trading industry.

My argument is that **<u>if</u>** 80% of all CFD accounts lose money, the problem **<u>is</u>** a human problem. My argument is that everyone opening a CFD account are normal people with a normal way of thinking. There must be something inherent in the way normal people think and act that makes trading so unsuccessful for them. Why is there such a high failure rate in trading?

OTHER PROFESSIONS DON'T HAVE AN 80% FAILURE RATE

When I started in this business 20 years ago the spread in the DAX was 6 points intra-day and the spread in the Dow index was 8 points intra-day. Today, these indices have doubled or tripled from their price levels of 20 years ago (Dow was around 10k, and DAX was around 6-7k), yet the spread has come down to just 1 point with some of the brokers I trade with.

Therefore, it should be easier for traders to make money. However, it isn't. People are still struggling to make money trading. My main premise for this book is to get to the bottom of this conundrum. The approach I have taken is centered around the following facts:

1. It has never been easier to trade. The IT infrastructure is superb for traders.
2. The spreads have never been lower.
3. The margins have never been more favourable.

4. The tools have never been so readily available.
5. The brokers have never done so much for their clients as they do now.
6. The stock indices have never been higher, meaning there is volatility.

Additionally, I assume that people who open trading accounts are normal well-adjusted human beings, who are perfectly capable of functioning within society. I assume they are normal, without using the word "normal" as a slight or an insult.

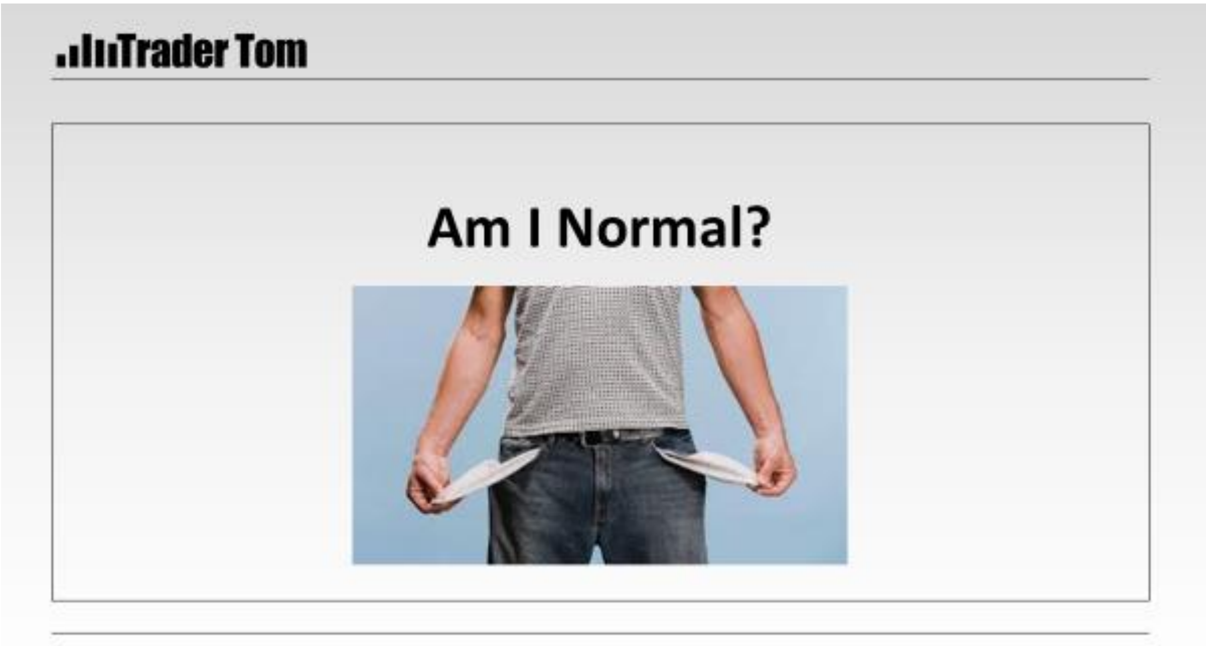
The question I want to ask, and answer is this: What does "normal behaviour" look like? How can I avoid being normal when I trade? The assumption is that the 80-90% of people trading are normal people, and I want to avoid acting like they do.

Are You Normal?

My argument, provocative as it is, in its simplicity, asks an essential question: Are you thinking like everyone else is thinking? Are you approaching trading like everyone else is approaching trading?

If so, you may have a problem.

If you think like everyone else, is it so strange that you get the results that everyone else is getting, even though you are smart, good-looking, have several school diplomas, and you have been a success at everything else in life?



What Normal People Do

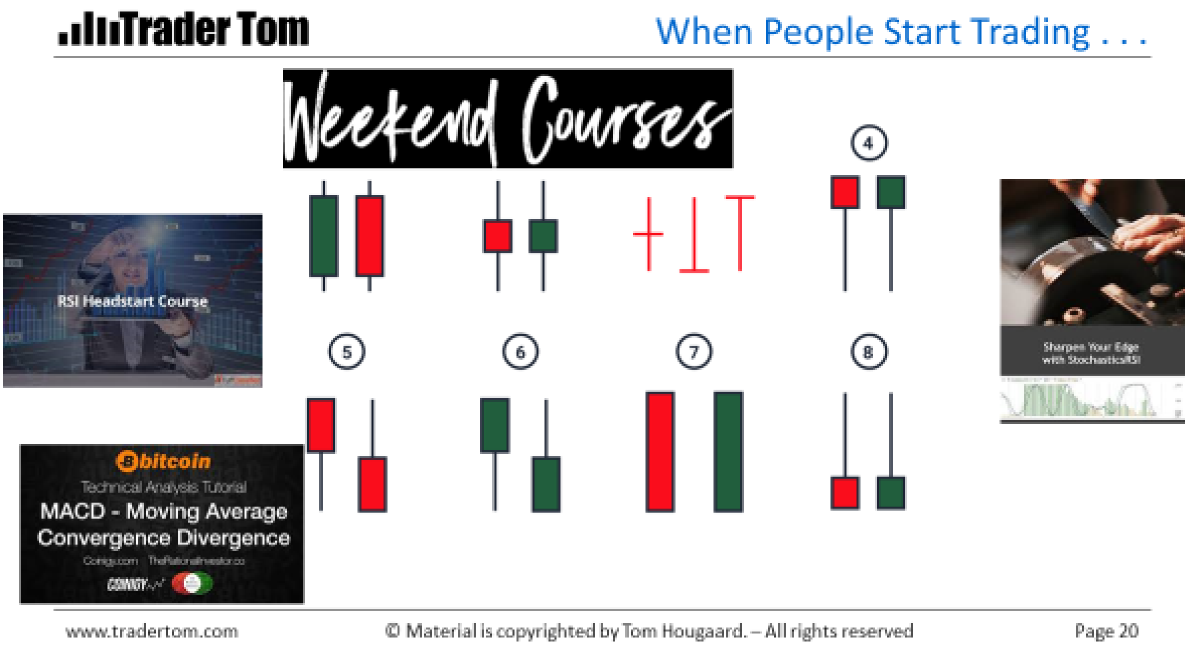
Let us take a look at what normal behaviour is. The normal behaviour is to engage in a never-ending cycle of education – looking for the next new edge. I knew from the moment I read Liars Poker that I wanted to be a trader, but I never had any formal training on how a good trader behaves. Why should I? I was always told that a good trader buys low and sells high.

Except every time I bought low, it always went lower and lower. What kind of advice is that?

And yet this is what we listen to when we start. This is the benchmark, and if this is the benchmark, then it is a miracle that it is only 80% that are losing. It should be 100%, because buying low and selling high is a sure way recipe for ruin.

It took me some time to accept this. I was good at catching tops in the market and I was good at picking lows. However, I also believe that there is an element of “selective memory” at play here. I think I want to remember the good calls and my mind conveniently filters out the bad calls.

People will learn to use tools such as candlestick analysis. People will attend weekend courses hoping to learn secrets. People will study the use of tools such as stochastics, RSI, MACD, moving averages, and the list goes on and on and on. This is normal behaviour in a nutshell.



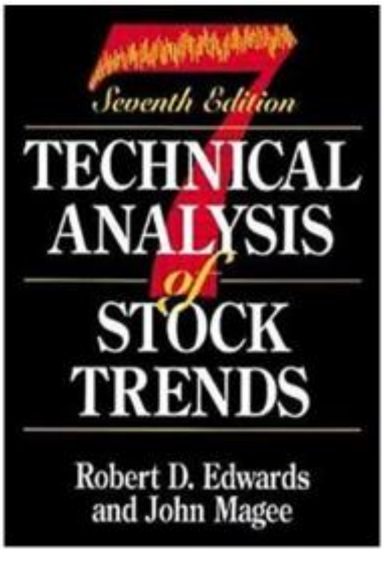
The Bible of Technical Analysis

Even the bible of technical analysis doesn’t do much to help a person on their way – once the initial learning curve is over. Over the years, many a Wall Street acolyte has made pilgrimages to the Trinity Church Bookstore to buy the bible. Not the King James version, mind you, but the "bible" for technical analysis authored by Edwards & Magee, which has sold more than 800,000 copies since its first printing in 1948.

What most readers don't realise, however, is that Edwards and Magee were not the real creators of modern technical analysis. It was a little-known technical analyst named Richard W. Schabacker.

A brilliant market technician, Schabacker codified almost everything there was to know about technical analysis up to his time -- which included such pioneering work as Charles Dow's Dow Theory. Between 1930 and 1937, he taught several courses to serious Wall Street traders and investors. Unfortunately, Schabacker died in 1938 when he was less than 40 years old.

Shortly before, Schabacker gave a mimeographed copy of his lessons to his brother-in-law, Robert D. Edwards, who rewrote Schabacker’ s lessons with the help of his collaborator, John F. Magee, an MIT-trained engineer. As a result, it was not Schabacker who received credit for the original compilation of technical analysis, but Edwards and Magee, whose work became a perennial bestseller.



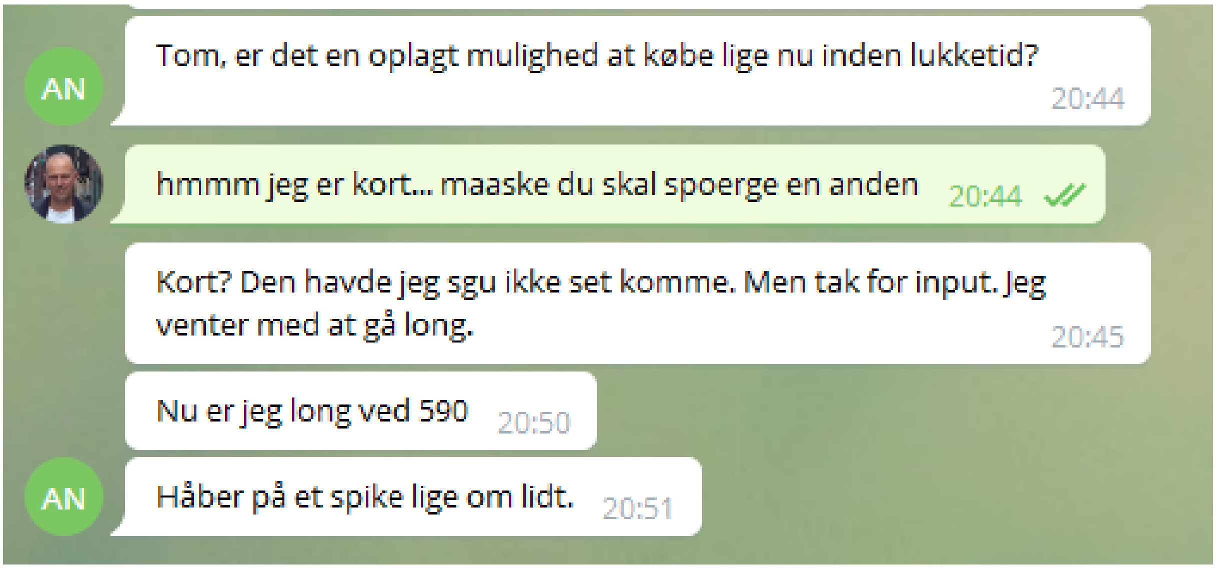
You can’t fault the book. It has everything you need to understand trend. However, as a day trader, it is simply not detailed enough.

This is not a criticism of the authors. I don’t think that day-trading, momentum trading, scalping and swing trading were even truly invented when this book was first created.

I may be vague, so let me be clear. Reading a book like the bible of technical analysis is a must, but please don’t think that it will make you a professional profitable trader, anymore than reading a manual on tennis will enable you to compete with Rafa Nadal.

Let me give you an example. It may help you understand better what I am trying to get across to you. Yesterday, the 1st October 2019, was a particularly bearish day in the Dow index and the DAX index. I was short all day and I had one of my better days, all verified and documented on my Telegram channel.

Towards the end of the day, when the Dow index was falling even lower, a student of mine contacted me and asked me a very alarming question. I have shown you the conversation, which is in Danish, so I will translate it.



"Tom, do you think it is a good idea to buy now, ahead of the close?"

I reply: "hmm, I am short....maybe you should ask someone else"

He goes on to express his absolute shock I am short, and a little later he goes on to state that he has bought the Dow at 590.

No professional trader would in their right mind engage with the market 10 minutes before the close. Why are you buying the Dow 10 minutes before the close on a day where Dow has fallen 400 points? You have had all day to find a short entry. What are you hoping to achieve, by being a buyer now? Are you thinking that because it has fallen 400 points that now it is cheap, and maybe just before the close, you may see some buying of these cheap stocks? I used to think like that too. That was when I was not profitable.

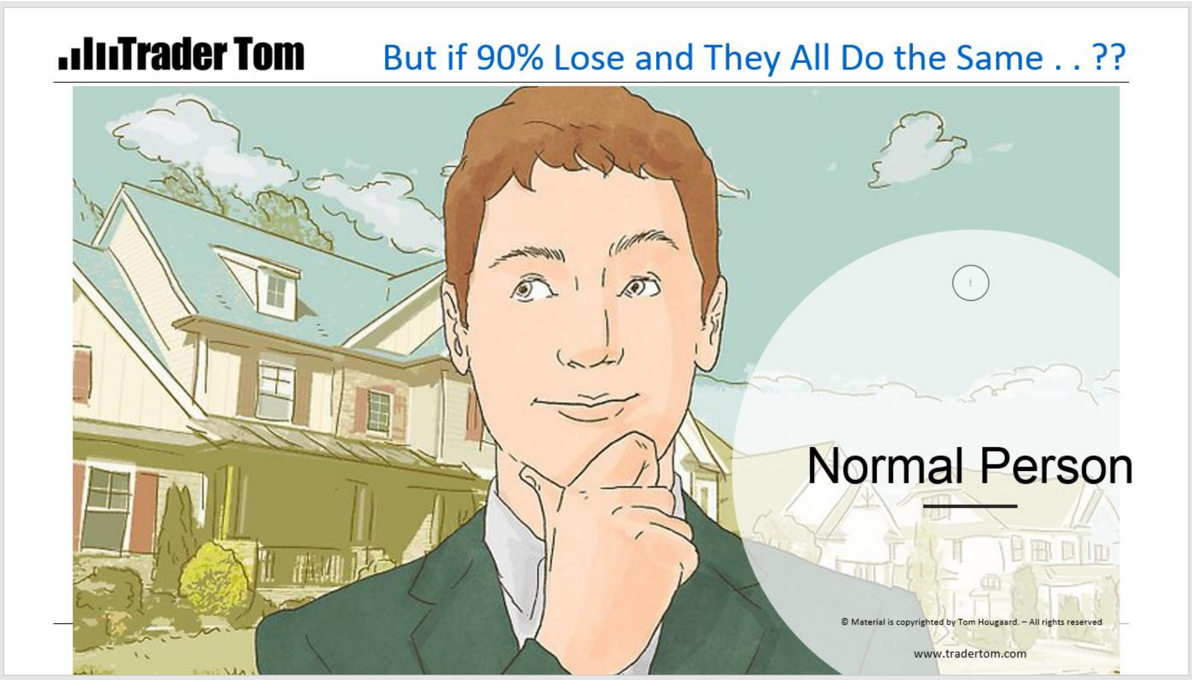
I know the Dow didn't rally into the close. There was no bounce. I am sure my student didn't lose a lot. It wasn't so much his wallet I was concerned about. It was his way of thinking. That is what this book is about. It is about making you think the right way about the market. That is where the 80-90% of losing traders tend to go wrong.

The 90% vs. The 10%

I needed an image for slide 22, so I asked Google what a normal person looks like? This is the picture that Google showed me of a normal person. If every person engaged in trading is a normal human being, meaning they are well-functioning, intelligent, considerate, hard-working, then why is there a 90% failure rate in our industry? That doesn't make any sense at all. Usually when people work hard at something they will succeed, or they will see some degree of success. That doesn't appear to be the case with trading.

If you are selecting a school for your child and the school has an 90% failure rate, I am certain you will not enrol your child in that school. This is the sad fact about the trading industry. We are fed a steady stream of information that is meant to help us in our quest to make money trading, yet we are missing the most important part. And the sad fact is that very few people know it. The brokers we trade with are not traders. They are no better to give you advice about trading than say a kitchen equipment maker can give you directions to become a Michelin-star chef.

We tend to engage in a never-ending cycle of predictability. We do well for a while. We are happy and our discipline weakens. We lose money. We strengthen our resolve and we get more education. We do well for a while. We lose money, we engage in more education. Sounds familiar?



Am I against education? No, I am against people thinking that all it takes is more education. Sure, it takes education, but it must be the right kind of education.

It is true that I myself run 1- and 2-day courses, so I could easily stand trial for being a hypocrite. In my courses I tell people that for every hour you spend on technical analysis, you must set aside at least 25% of that time to what I call "internal analysis."

You need to know what your weaknesses are. You need to know what your strengths are. You need to know what you are good at and you need to know what you are not good at. If you don't spend time trying to improve that, how will you get better? Very few people, if any, will engage in that level of introspection in order to gain the results they want.

Conversation with a CEO

I had a conversation with a friend of mine. He is the CEO of a major CFD broker in London. I asked him about the nature of their clients and their win-loss profit ratio.

Trader Tom — Conversation with CEO of CFD Broker

Tough Questions – Honest Answers

1. Are people good traders?	Yes and No.
2. Why "yes"?	More winning trades than losing trades.
3. Why "no"?	They run their losses longer.
4. How do you make money?	By letting people trade.
5. Do you hedge?	We only hedge big traders.
6. Do you have losing months?	Yes, at times, but very rare.
7. What are your best months?	When the market is in a "runaway mode".
8. What's the problem?	Clients have no emotional control.

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Tom:

You have worked in the CFD industry for 30 years. You must have seen some good traders along the way. Can you tell us about them?

CEO:

I wish I could. I have seen many people make a lot of money, but very few managed to keep the money. I started in the industry at a time when CFD trading was not a mainstream tool for trading. It was mostly very wealthy people or people who worked in the industry that had CFD accounts. These clients back then often traded as part of an “old boys club” kind of network. It meant they mostly traded specific shares and some commodities. Back then trading was nowhere near as prolific as it is today.

Tom:

Were they good traders?

CEO:

No, I would not say they were. We had clients who were well-known personalities in the City (City is slang for the financial district in London – like Wall Street is for America), and their personal trading was often atrocious, even though they were hedge fund traders or fund managers. It was almost as if they lost their discipline when trading their own money. I am certain they would not be allowed to trade for their clients in the manner they traded for themselves.

Today we have far more “smaller traders”, but the pattern is remarkably similar between a “small trader” and a “large trader”. Almost all clients have more winning trades than losing trades. As such you could argue that they are good traders. However, they tend to lose more, much more, on their losing trades than they win on their winning trades. The ratio is that for every pound they win, they lose about £1.66.

Tom:

How does a CFD broker make money out of that?

CEO:

Well, believe it or not, but we want our clients to win. I have a network of contacts to other CEO’s, and although we are competitors, and we would do anything to outmanoeuvre a competitor, we do have one shared wish. We wish our clients would trade better.

We try our best to help them. We give them every tool under the sun. We give them favourable spreads, and we give them news services. We give them sophisticated charting packages. We give them data. We give them analytical tools to measure their performance.

In short, we do absolutely everything we can to ensure they have all the tools they need to make money. And then we let them trade. The problem is that most smaller accounts tend to lose within a short space of time.

Trust me when I say I wish it was different. I don’t know what more we as a broker can do for our clients. We prefer clients make money because there is clear evidence, that those who trade and win, carry on trading. That is better for business.

The truth of the matter is that you can clearly see the difference between a consistently profitable trader and a normal trader. Their approach is very different.

Tom:

How can you tell whether someone knows what they are doing?

CEO:

There are a multitude of parameters that we may look at. If I have to narrow it down to the 5 most important factors, it would be these:

1. Account size
2. Trade frequency
3. Ratio of time spent holding winning vs. losing trades
4. Adding to winning or losing trades
5. Do client trade with a stop loss?

Someone who opens an account with anything less than $500 will with a very high degree of certainty lose that money, sadly. Someone who trades everything and anything, i.e. over-trading, will eventually lose their money. Anyone who is unable to hold on to their winners, but who are able to hold on to their losing trades, will eventually lose their money. Anyone, who adds to their winning trades will catch our attention (positively), but anyone adding to their losing trades will with near certainty lose their account deposit at some point – sooner or later. Anyone trading without a stop loss will follow that path too. We sadly see it all the time.

As you can see, as a broker, we do everything we can to help people making money, but people are people, which means they will find a way to self-sabotage.

43 Million Trades Analysed

His opinion resonates with another industry professional. His name is Rodrigues and he works for the FX company called FXCM. Rodrigues and one of his colleagues attempted to find out why there was such a high failure rate amongst the FXCM clients. FXCM has on a daily basis 25,000 people who trade currencies.

Rodrigues investigated all the trades executed over a 15-month period. The amount of trades was truly staggering. The 25,000 people executed close to 43 million trades. From a statistical point of view that creates a reliable and immensely interesting sample space to investigate. Specifically, Rodrigues and his colleagues looked at the amount of winning trades.

Trader Tom 25,000 People & 43 Million Trades

What is Normal in Trading?

	Your Answer	The Answer
Percentage winners?	_ _ _ _ _	_ _ _ _ _
Pips/points won?	_ _ _ _ _	_ _ _ _ _
Pips/points lost?	_ _ _ _ _	_ _ _ _ _

I would like to give you an opportunity now to think about how many trades were winning trades and how many trades were losing trades. You can represent it as a percentage of the overall 43 million trades. I will give you 10 seconds to think about.

If you feel it has any influence on the answer you want to give, I can tell you that most of the trades were executed in Euro Dollar, Sterling Dollar, Dollar Swiss and Dollar Yen. However, the vast majority of the trades were executed in Euro Dollar, where the spread industrywide is very tight. Unfortunately, that doesn't seem to make much of a difference to the outcome.

62% of all the trades by the FXCM clients ended with a profit. That is a little more than 6 out of 10 trades. That's a good hit rate. A trader with the hit rate of 6 out of 10 should be able to make money from trading. Of course, it does depend greatly on how much he wins when he wins and how much he loses when he loses. In there lies the problem for the 25,000 people.

See, they were very successful in terms of "hit rate". Yet when you look at how much they made on average per trade and how much they lost on average per trade, you soon realise that they have a major problem. When they won, they made about 50 pips. When they lost, they lost about 80 pips.

There's nothing wrong with having a system where you lose more on your losing trades than you win on your winning trades. However, it does require that you have a sufficiently high hit rate in order to absorb the losing trades.

Trader Tom 25,000 People & 43 Million Trades

What is Normal in Trading?

	Your Answer	The Answer
Percentage winners?	_ _ _ _ _	**62%**
Pips/points won?	_ _ _ _ _	**48 pips**
Pips/points lost?	_ _ _ _ _	**82 pips**

(62*48) – (38*82) = 140 pips deficit

A colleague of mine, a professional trader from South Africa who trades a hedge fund, has a hit rate of about 25%. I will tell his story later in the book. When he and his colleague lose, they lose 1X. When they win, they win as high as 25X. It stands to reason that my friend is immensely profitable even though he doesn't have a convincing hit rate, at least not from a traditional perspective.

Note during editing process:

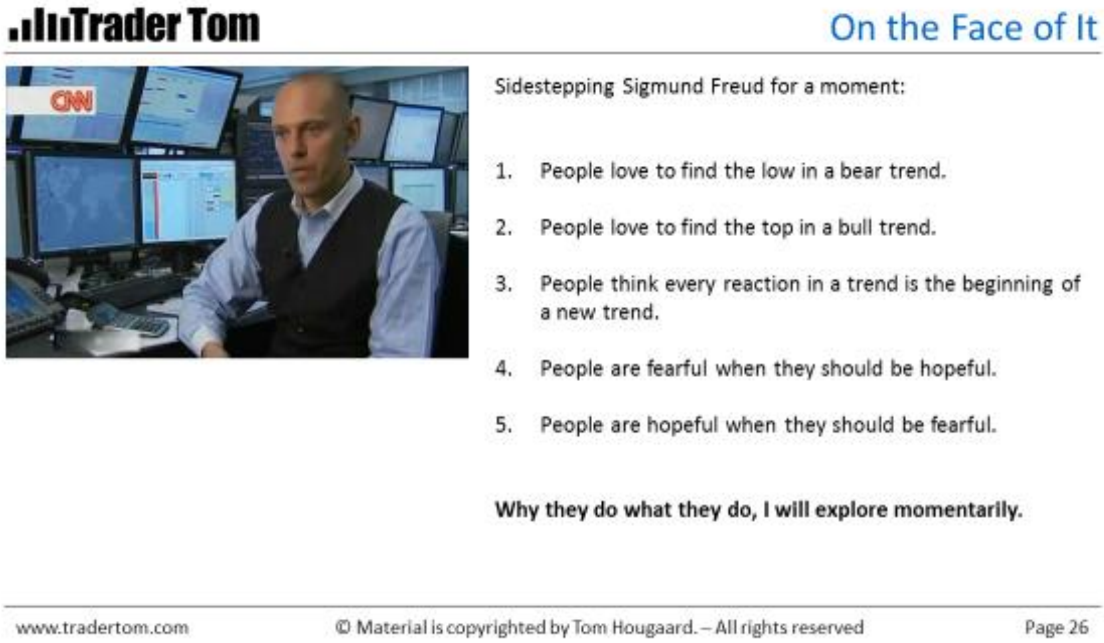
While I was editing this book, I came across this page, where there was a big blank space before the next page. I had something on my mind, but it was something that I found difficult to fit in anywhere in the chapters I wrote. I decided to simply offload my thoughts right here on this empty space, which by the time you read it is no longer empty. Here goes:

When I call out trades in my live TraderTom Telegram group, I will always announce a stop loss. Always! However, I often get asked if I have a target in mind. The answer is quite often a little sarcastic: "No, my crystal ball is out for repairs", or if I am particularly grumpy and tired, I will be rude and say "Sorry amigo, but do I look like a fortune teller to you?". Yes, I know. It is not very polite. I am sorry. Ignoring my blatant inability to be polite when I am sleep deprived, there is a deeper meaning to me not calling "targets" on my trades. It has a lot to do with "risk vs. reward".

I personally find the whole "risk to reward" an enormous flaw, but since I am the only one who ever talks about it, I accept that I am probably wrong. Still, hear me out. How on earth do I know what my reward will be? I literally do not know. Even if I pretended to know, say by using a measured move calculation or a Fibonacci extension etc, I know myself well enough to know that I will have added to my trade along the way, and when it got to my "target", I would not close it, because that is my philosophy. I would kick myself if I closed a trade at my target, and then it went even further. I would rather give away some of my open profits than miss out on potentially even more profits. Now I am probably making a big fus out of nothing, but targets are not for me. I want to see what the market will give me. I am prepared to accept that this may mean I will give away some of my open profits.

Interview with CNN

In an interview with CNN some years ago, I was asked about the traits of winning traders. In this very candid interview, I highlighted a few points that I felt differentiated the winning traders with the losing traders.



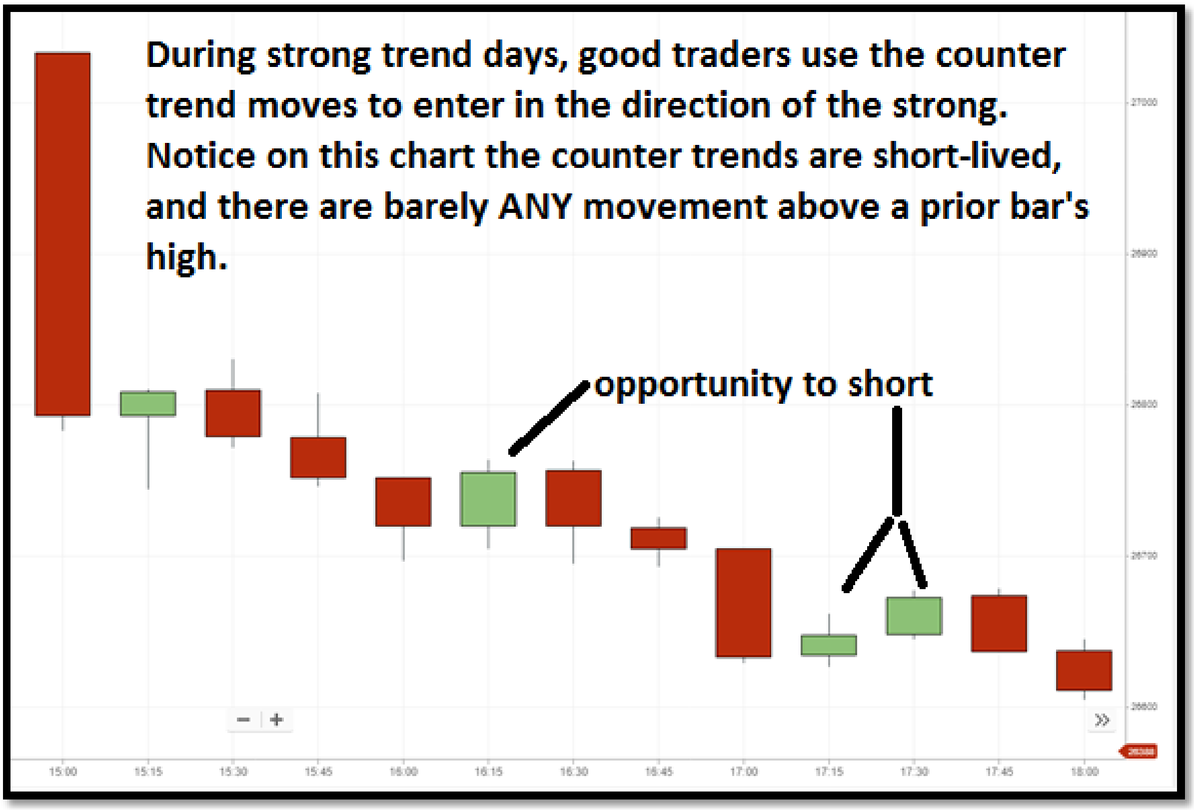
1 #

When the market is trending lower, whether it is intraday, or over a longer timeframe, there seems to be a tendency from retail traders to attempt to find the low of the move. Whether that is out of a desire to buy cheap and sell expensive, or because they use ineffective tools, I simply don’t know. What I do know is that this trait is immensely damaging to anyone’s trading account.

2 #

The opposite also holds true. When the market is trending higher, traders tend to want to find a place to sell short. Although, it must be said that people are generally better at jumping on board a market that has already risen, than they are jumping on board with a short position in a market that has already fallen significantly.

If the market has moved higher by a significant amount, especially in the very short-term, retail traders tend to want to fade the rising prices, i.e. they look to establish short positions. Again, this is probably the result of a distorted view of things being cheap and things being expensive.



3 #

The above chart is from yesterday in the Dow. It is used to illustrate my point 3. If you have sat on a trading floor during a busy day in stock indices you will know exactly what I am talking about now. If you have ever traded a very weak day in a stock index, or indeed in any asset/product, you will most likely understand what I am talking about.

Imagine the Dow is falling relentlessly during the afternoon of trading and you are sat on the trading desk observing people's trading behaviour.

You wonder why people attempt to find the low of the day when all the Dow is doing is going lower and lower. Then it occurs to you that every single time people are buying, it is because the market is making the slightest little bit of movement to the upside.

The chart above illustrates this perfectly. It is a weak day, but there are small pockets of strength where the Dow rallies a little bit. They are usually short lived, and the experienced trader uses it to get into short positions, while the inexperienced trader thinks that every single little counter reaction against the trend is the beginning of a new trend higher.

This is a common trait amongst traders. They think that every single little counter reaction against the trend is the beginning of a new trend. More fortunes have been lost trying to catch the lows in a falling market than in all the wars put together (unsubstantiated statement – made for emphasis – please don't do it).

Something is Plain Wrong

What is normal behaviour amongst retail traders? We know that 80 to 90% of all retail traders engage in the same self-destructive behavioural pattern. We know that 80 to 90% of traders do not make money consistently trading CFD's or spread betting. It is probably also fair to assume that those 80 to 90% of traders are intelligent, ambitious, self-motivated human beings, who like to create their own luck and forge their own way in life.

I have never met anyone who started trading because they thought it was the same as playing the lottery. Virtually every person I have ever met who was interested in trading and who wanted to learn more about trading have been self-starters, entrepreneurs, or students at an institution of further education.

Therefore, I think it's a fallacy to say that trading attracts the wrong kind of people. I think it attracts the right kind of people. I think it attracts the kind of people who have a chance of making a success at it. I think it attracts the kind of people who are not fooled by the Get Rich Quick schemes. I doubt many traders buy lottery tickets, purely on account of the odds being rubbish, and traders understand that all too well.

Nevertheless, something is wrong. Something is wrong when 80 to 90% of people fail. On this slide I have identified a handful or more of behavioural patterns that I think are detrimental to traders. The most frequently observed behaviour is that of letting a loss run out of control.

In order to do that the trader will have had to have no stop loss in place. If you are ever lucky enough to meet someone who is admitting that they have a big loss on their account, you could ask them why the position is still open?

Trader Tom — What Is Normal Behaviour?

Action	Reason	Subconscious Reason
1. I am letting my loss run.	1. I am hoping.	1. Avoid pain.
2. I am letting my loss run.	2. Indicator/Fib/etc says so.	2. Avoid pain.
3. I am taking my profits.	3. You can't go broke taking a profit.	3. Avoid pain.
4. I am winning, so I am reducing my stake.	4. I want to take it easy now.	4. Avoid pain.
5. I am losing, so I am increasing my stake.	5. I am trying to get back to where I was.	5. Get rid of pain.
6. I made my points for today so I stop.	6. I am afraid to lose what I made.	6. Avoid pain.
7. Trading without real conviction	7. I am bored / or scared of missing out.	7. Avoid pain of boredom or pain of missing out.

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The answer that you would most likely hear is that they are **hoping** that the position will turn around. As the saying goes, hope dies last. Our minds seem ill equipped to engage in risk management. Our minds have one primary objective: to protect us against pain, perceived or real pain. During the process of running an open position, which is producing a loss, our subconscious mind is telling our conscious mind to keep the position open. It will mask this message as well as it can, in order to protect the ego, which is more fragile to the subconscious than the state of your trading account.

When I read the above passage, during the review, I decided that this sounded a little bit "airy fairy." Here is the same message but written with other words.

As long as the losing position is open, there is hope that our luck will change, and the position will come good. The moment you close the position, and you crystallise the loss, the pain of the loss becomes real. I accept there are many permutations to this argument. Some would argue that the very act of closing the position is when you can stop agonising over the open loss and move on. I accept that. However, my primary argument is that the reason we are **hoping** has little to do with hope itself and everything to do with avoiding pain.

How many times did I see clients sit on losing positions for ages? I saw them fund their accounts to keep the position open – margin calls – just so they didn't have to take the loss. To compound my confusion, how many times did I see the position come good again, and when it did, the client would close the position? I saw it a lot. They didn't hold on to the position because they believed in the position. They held on to the position because they could not stand being wrong. The moment they were relieved of their pain of the losing position, they got out – for nothing. They were so relieved to have avoided the pain of being wrong that they completely ignored the fact that the market was now actually agreeing with them.

Whether you are taking your profits early under the excuse that "*you can't go broke taking a profit*", or you are on a winning streak so you are now reducing your stake size, you are essentially anticipating pain of losing some of your gains and you are now rationalising your way to avoid the pain, even though it hasn't actually happened. Perceived pain or real pain matters not to the subconscious. It will be treated with the same response and the same emotions.

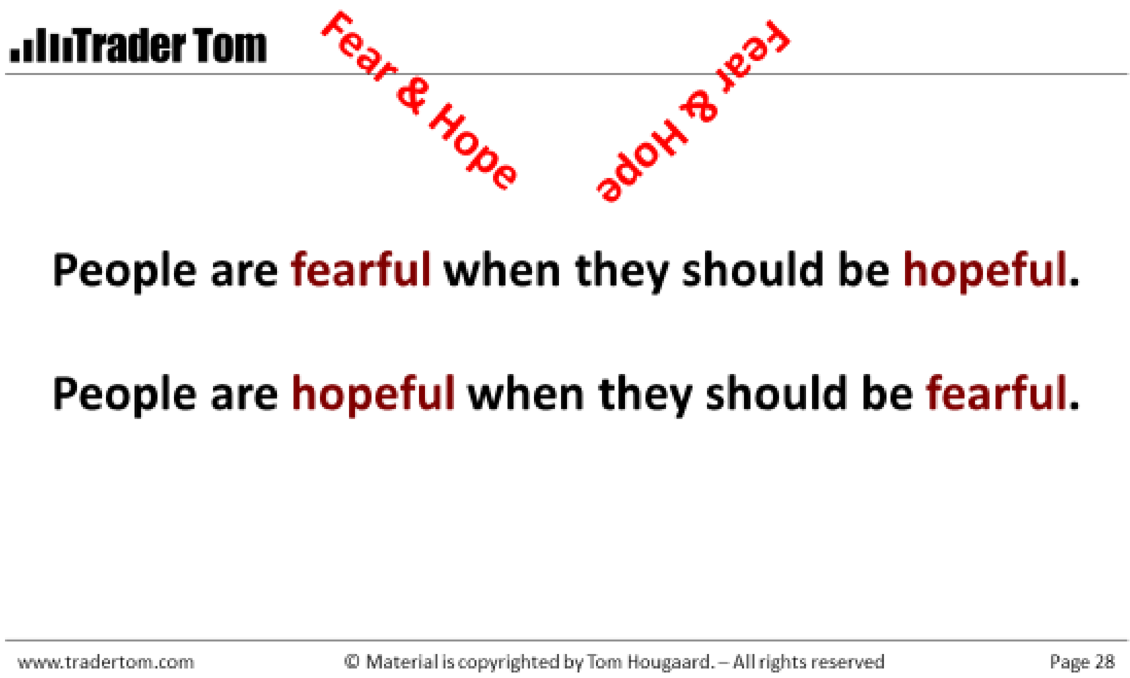
When the pain is real, i.e. real pain has manifested itself in body and mind, because of a trading loss, there is no end to the lengths our ego will go to make the money back. It is the primary driver behind the argument of "when wrong, double up". We tell ourselves during a losing streak that we are ever so close to beginning to win again, so the natural conclusion must be to double up in order to regain what has been lost. The real subconscious reason for doing this is to attempt to get rid of the pain. Now we are not trying to avoid pain. Now we are dealing with pain and we are trying to get back to that state of equilibrium where we were pain free.

Act Without Fear

As I said earlier, and I am at the risk of repeating myself, you learn a lot from observing millions of trades. If you want to stand a real genuine chance of making money as a trader from the financial markets, I believe with every string of DNA within me, with every fibre in my body, that you need to change the way you think about fear and pain and hope.

William Blake said that he who desires, but acts not, breeds pestilence. I have worked tirelessly towards being able to act, without fear and hesitation. What do I mean by that? Have you ever seen a chart pattern, or a setup of some nature on a chart, and your first impulse was to buy or sell, but then immediately that thought was followed by a reflex response of fear that you had no control over?

To be more specific, your free creative mind instructed you to do something, but your fear instinct immediately cautioned you not to follow through, because you might lose. Have you ever seen a market that was in freefall and you were afraid to sell short because you were afraid you might lose?


Trader Tom

Fear & Hope

Fear & Hope

People are fearful when they should be hopeful.

People are hopeful when they should be fearful.

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My basic premise with this book is to rid you of these fears. I argue that the 90% will too often take trades, because they fall into two categories:

1/ they look “cheap” to buy.

2/ they look “expensive” to sell short.

It can be a huge challenge for many traders to sell short something that has already fallen significantly. I will give you a good example. Yesterday the German DAX index fell from 12,497 to 12, 250. That is quite the fall for this index.

This morning you could sell short this index at 12,250, but many of my students did not like to do that because they were fearful that the market would bounce before falling. What they failed to understand at that precise moment in time was that

1/ the market had already shown it was weak. How often do you see one lonely red negative bar on a daily chart? Rarely! Weakness tends to come in clusters. So does strength.

2/ Whatever happened yesterday will most likely be replicated the day after. The markets are not THAT irrational. People are selling because they want to get out of the market. It is rare that you then reverse the very next day. Even if it did, your risk parameter would stop you out of your position.

Most of my students accepted the market was weak, and that it probably should be sold short, but no one dared doing it in a meaningful way.

This is the reason why the 90% lose. The reason why people do not make money from the markets has nothing to do with their ability to read the charts. It has nothing to do with their ability to understand what is going on in the market.

My basic premises that people

1/ think the wrong way before they get into a trade

2/ think the wrong way when they are in a trade

It reminds me of the late Mark Douglas, a real light in the trading industry - and an inspiration to thousands of people, when he said that good traders simply just think differently. That was the first thing he said at the start of his book “Trading in the Zone”. It started by stating good traders just think differently.

I have coined my own phrase. I argue that people are fearful when they should be hopeful and they are hopeful when they should be fearful.

I would like to explain that by the use of an example.

Imagine you have bought Dax at 10 and the market is now trading up at 25. Instead of thinking that the market may be on a tear higher, and it may go on to offer you many more points, you begin to fear that the points you have already earned will be taken away from you.

Hence my saying, you should be hopeful in a situation like this, but instead you are fearful. You are afraid that the points will be taken away from you, rather than letting the primary focus of your mind to rest on the hope that even more points will come your way.

The opposite holds true when you are in a losing position. You are now hoping that the market will turn around and take you out of your pain and bring you back into a state of equilibrium. Your soul objective is to get rid of your pain, and instead of being afraid that you’re going to lose even more, your focus is now on hoping that you would lose less. Every tick in your favour is celebrated. Every tick against you is ignored.

I would like to bring in a conversation I had with a student. We are discussing a position I have running in Sterling Dollar.

Him: It feels like gambling.

Tom: Please explain.

Him: Well, you have 40 pips in profit, but you will not let me take the profit.

Tom: I won’t stop you from taking the profit, but if you ask for my opinion, you should let the position run.

You might want to consider the following scenarios, and then ask yourself how you feel under each scenario:

1: Run position and you get stopped out for nothing.

2: Run position and it explodes higher.

3: Close position and it explodes higher.

4: Close position and it reverses.

Him: I think it is best to close the position and secure the profits, rather than risk that the market will take the profits away from you.

Tom: How would you then feel if the market exploded in your favour?

Him: I would be disappointed, but I could always jump back in again.

I believe this is what the 90% will think like. It is the reason why in the study of FXCM clients that the traders would lose more than they made. Hope dies last, and as long as there is hope, there is a reason to hold onto the position.

When the trader is confronted with a loss, they hope it will turn around. The operative word now is HOPE. When he or she is confronted with a profitable position, they are afraid the profit will disappear. The operative word now is FEAR.

My student naively thinks he can jump back in again, but he would undoubtedly have to do that at a worse price than the exit price of his profitable position, not to mention the transaction cost should be factored in as well.

So, the trader holds onto the position until such point where the pain finally becomes too much, and they close the position. Unfortunately, this point, this threshold tends to be further down the road than the threshold of hope.

This is what you need to focus on. This is what you need to work on consistently to change your pattern. I will not state whether it will be easy to do or difficult to do. It just is. There is no point in going any further in speculation if you can't get yourself to do what you must do, even though it feels uncomfortable to do.

You must be aware of the fact that in trading we are prepared to chase hope a lot further down the road of misery, than we are prepared to endure on the road of opportunity. It is just the way we are put together, unless you are aware of it, and you have a plan for combatting your natural behaviour.

However, I must come with a warning. Your mind is like a muscle. This is not a one-off quick fix any more than doing 100 push-ups once will make you look like Captain America for now and eternity.

Atrophy is not just a bodily concept. It is also a mind concept. You need to strengthen that mind of yours by repetition. I'm going to provide you with a brilliant way of getting control of your mind. I will present that idea towards the end of the book.

We are prepared to chase hope a lot further down the road of misery, than we are prepared to endure on the road of opportunity.

Note during editing process:

On an earlier page, I found some space, while I was editing the book. The same happened here, and I just happened to have something on my mind.

I am often asked how I control my risk when I am adding to my winning trades. It is a good question, and it should be addressed somewhere in this book. Now is as good a time as any.

I have just bought the Dow at 26,629. The Dow has already rallied from a base of 26,569, so I might be a little late to the party, but that doesn't bother me. Many a good trade has been missed because you thought you were too late. If I have an exit stop in place, I am fine to join a momentum move, even one that has been moving for a while.

The Dow prints 26,649, and I buy again. Now my stop loss on the first position has been moved to reflect the fact that I have taken on more risk. If my stop loss on the first position is 50 points, and I don't move my stop loss up, then I am essentially just doubling my risk.

I move my stop loss up to breakeven on the first position, and I place a stop loss on the second position as well. Where I place the stop loss on the second position is irrelevant for this discussion. It could be at the same place as the first position, or it could be a little higher or a little lower. The important point to remember is that although I have doubled my position by adding to my winning trade, I am not doubling my risk. My risk stays the same, more or less.

There is now an increased chance I will get stopped out of my position because my stop loss is so much closer than before. The flip side is that I will make much more money if the market continues in the direction it has already travelled.

Do you get it? There is no magic to it. It is a philosophy, but it is born out of a desire to NOT be normal. The normal thing to do is to "close half your position and let the other half run." Why would you do that? Why would you have the market agree with you, but you only ride it with half a stake. That is what the 90% is doing, and I don't want to do what the 90% is doing, no matter how logical it may seem. They are wrong over time, and I want to be right over time!

The Not-So-Normal Behaviour

What is the not-so-normal behaviour? Well, firstly, I am all too aware of the short comings most people display when they are trading: running a loss, cutting short the profitable positions, over-trading, trading for excitement and entertainment.

But this is already known to most, if not all people, so the “not-so-normal” behaviour goes somewhat beyond that. It is very rare that we ask ourselves why we do what we do. Why do I trade when I do? Why do I take profits when I do?

I think it’s time to bring in the words of a relatively unknown trader, but one who was hugely respected by his peers. He was a pit trader at the Chicago Board of Trade, and his name is Charlie De Francesca, also known as Charlie D.

My Hero Charlie D

Charlie De Francesca arrived at the floor of the CBOT, with a dream and a small account. He had a background from competitive college football – American style – but otherwise there was nothing about this guy that would indicate that he would go on to become the biggest trader in the US T-Bond pit in Chicago.

He had a rough start too. He barely traded in the first 6 months on the floor. He just stood there and observed. Then one afternoon something clicked, and he traded up a storm for 2 hours, and made himself $5,000. From then onwards there was nothing stopping Charlie D. He became a legend in the trading pit until his untimely death.

I will digress a moment here. In 2007 I met a person who was going to radically change my way of trading. It all came about by chance. I had come back from a lunch break and a colleague of mine returned from a meeting with an educational company. This educational company taught technical analysis and they were pitching their products to my colleague, who happened to be the head of marketing.

What you need to know about my colleague is that he was the most obnoxious East End London guy you could possibly imagine. He was brash, he was obnoxious (I know, I said that twice), he was arrogant, and no one could tell him anything he didn't already know. Yet somehow this educational company had gotten his attention. He spoke very glowingly about a gentleman called Dr David Paul, who had taken my colleague through some basic technical analysis.

He showed me the technical analysis, and it was basic. Yet there was something about the course material, which I had been given a copy of, that told me that I needed to engage in a conversation with this gentleman. It turned out that Dr David Paul had a two day trading course coming up in Johannesburg. So I booked myself on a flight to Johannesburg a few days later. It was one of the only times I have ever participated in formal training on the topic of technical analysis.

There is something incredibly humble about Dr David Paul. He has got a Masters in Mathematics, and he has a PhD in Metals. He used his immense brainpower to invent a drill for miners in South Africa. This was no ordinary drill. It was the kind of drill that would suck the gas out of the holes in the ground, while drilling, and thus saving lives, because it more or less eradicated the occurrences of explosions.

David Paul made himself a wealthy man, and he spent his time investing and trading. On the second day of the course David said something that would change my perspective on trading.

He said something along the lines of this: When you are in a winning position, instead of thinking where to get out, why don't you think about where to get in more?

He basically told me to turn everything upside down. Most traders with a profit will begin to contemplate where to take half the profit. Next they will begin to contemplate where to take the next half of the profit. David argued that this was what the 90% would do. He didn't use those exact words, but he did argue that if you want to make money trading, you need to do that which the majority finds difficult to do. The first time you try it, you may fall flat on your face. That is to be expected, but the next time it might be a little easier, and the next time a little easier again.

David was essentially arguing that when you are in a winning position, you should put pressure on your position. The argument for doing so was something he himself had observed when the market really began to trend.

I have tried to put a different spin on his words. When you want what you want, more than you fear what you want, you will have it. You want profits in your trading. You probably have a good instinct about trading. You probably also realise by now that it is your thinking that causes your problems, rather than your knowledge about the financial markets.

If the 90% of traders are engaged with taking half profits and letting the other half run, maybe the right thing to do is to double up on your position, or perhaps conservatively add a little to the position, when everyone else is taking half the profits. At least this is what I read between the lines, as I sat in that hotel conference room in Johannesburg.

I walked across the street when the workshop was over and locked myself into my hotel room. 10 minutes later I was in a short position in the Dax, and five minutes after that I had doubled up on my short. I don't recall how the trade went, but I recall moving my stop loss to breakeven on the first position and I then executed a second position.

Depending on your experience level, you may or may not be able to answer this question. Have you wondered why it is easier to add to a losing position than a winning position? I have wondered about that myself many times.

You decide that you want to enter short the market at 12,325. The market then moves up to 12,345 and you are tempted to add to the position.

Why?

Why is it easier to add to a losing position than a winning position?

Well, for starters, you would have loved to have sold short at 12,345 rather than 12,325 because you would get a better entry price. Therefore, getting in again at 12,345 makes sense from an economics point of view. That is plain simple logic. There is a chance that you have a stop-loss in mind, and there is a chance that you have a target in mind. Now you have an opportunity to have the same stop-loss as before, but you have 20 points less risk, and you now have 20 points more profit potential.

You have also created a higher average price, so the market only has to move 10 points in your favour, before you are at breakeven.

Simple and logical – something our minds love.

However, you will now have added to your position exposure, and the market has told you that you are wrong, at least right now. It was easy to do the wrong thing, because we attach a value to the market. When the market gives an opportunity to increase the value of our trade, it will seem compelling to us.

Why is it then difficult to add to a winning trade? If I bought at 12,325, and the market is moving in my favour, I am relieved. Now other emotions will enter the consciousness. There will be greed. You want to make more. There will be fear. You want to protect what you have made.

When the market reaches 12,345, you will be thinking that if you add now, you have increased your average price to 12,335. It means that the market will only have to move 10 points against you, before your position will now show a loss.

We decide to dwell on one or the other. That is the heart of the issue. We decide to dwell on the potential for bigger profits, when we add to our losing positions. We decide not to dwell on the fact that the market is telling us we are wrong.

We also decide to dwell on the fact that the market may take our profits away, if we add to our winning position, because we now have decreased our average price. We decide not to dwell on the fact that the market is corroborating with us. The market agrees, but we are doubters. On the other side of that coin is a market that disagrees with us, but we have blind faith that the market is wrong, and we are right. Hmm!!!!!!

Adding to a winning position can be uncomfortable to begin with. That is why I would love for you to read the book called Charlie D, the Legendary Bond Trader. Charlie D was an exceptional human being. He found trading hard to begin with, yet somehow, he became the biggest US government bond trader ever. He was a private trader, yet his trading size rivalled that of major institutions.

There is a great YouTube video of Charlie. His full name is Charlie De Francesca. You should put his name into YouTube. He gave a talk to other Chicago Board of trade traders, and this speech was recorded. It is also transcribed in the book, which is a good thing, because the video is old, and very grainy, and the audio is terrible. It is also 30 years old, which explains the poor quality of the video.

Trader Tom — Floor Trader and Outstanding Character

The Message

"But when you are a good futures trader, everything you do hurts."

You have got to fight it (your human-ness) unless there is a reason to do it, based on what you see in the market.

The most memorable quote from having read the book over and over, studying a gentleman who was not a success immediately, was this line: Everything you do hurts, when you are trading well.

Trader Tom — And not Successful Immediately

The Message

"But when you are a good (futures) trader, everything you do hurts."

Example of Not Normal Thinking

What you are seeing here is not an unusual situation for me to be in, but it once was. I am conscious that I may appear to be showing off and I like to avoid that. I do not want my message to be confused with a need to show off my skills. Lord knows I have days where I don't trade well.

I could also have shown you a losing trade (and I will next - and there are plenty of those too). I want to move beyond the "wow" factor and get to what I am really trying to illustrate with this slide. It is not the monetary gain I want to focus on. It is the way I added to the position.

Not the Result of Normal Thinking

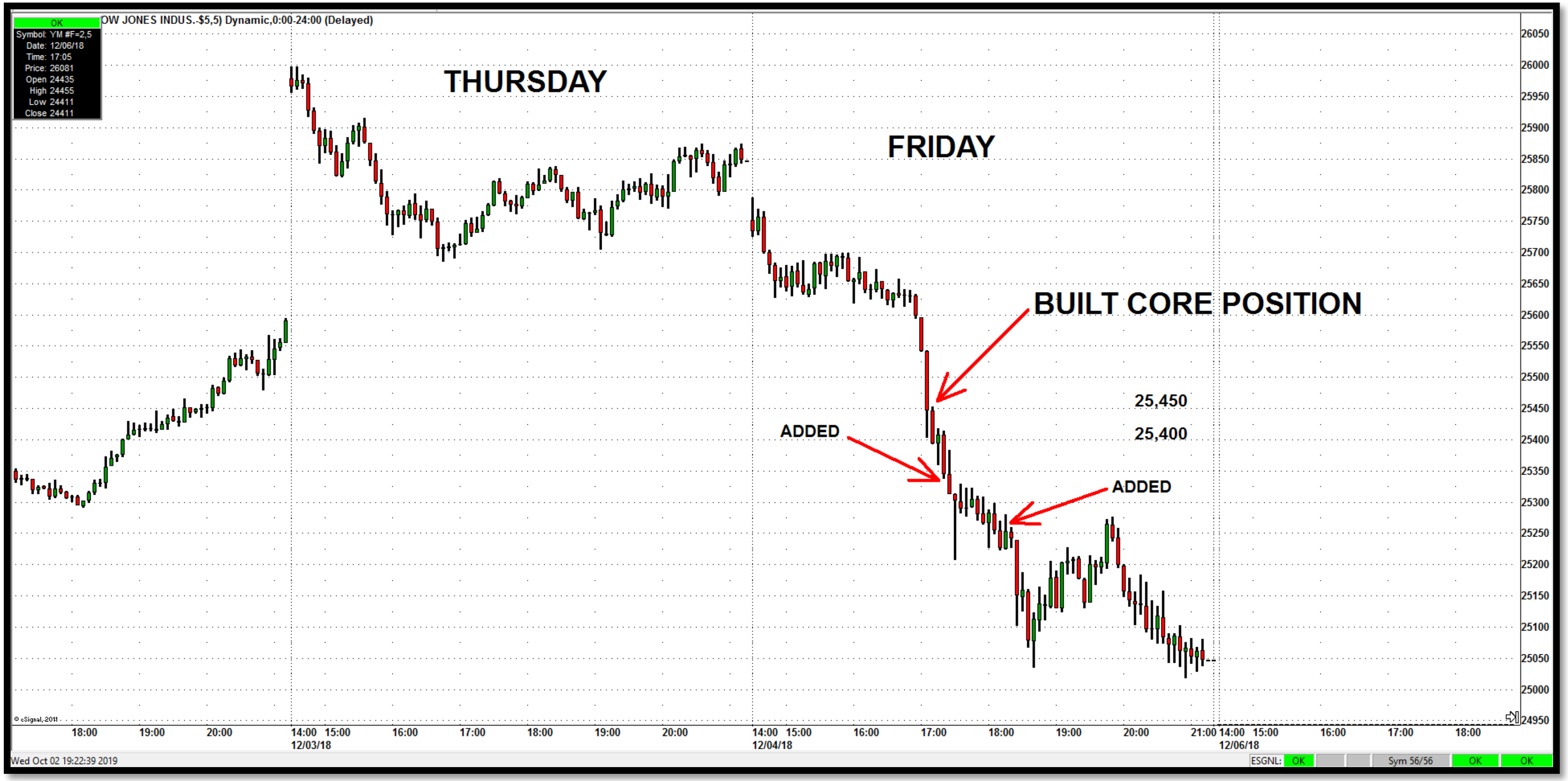
Wall Street	3,000.0 S	25419.6	25135.9	kr851,150.00
	500.0 S	25458	25135.9	kr161,500.00
	700.0 S	25455	25135.9	kr224,000.00
	350.0 S	25469	25135.9	kr116,725.00
	450.0 S	25455	25135.9	kr143,775.00
	200.0 S	25441	25135.9	kr61,100.00
	300.0 S	25329	25135.9	kr58,050.00
	250.0 S	25356	25135.9	kr55,250.00
	125.0 S	25258	25135.9	kr15,312.50
	125.0 S	25259	25135.9	kr15,437.50

I get many questions on how to add to a position. There are obviously as many answers as there are traders doing it. Each will have their own style and flavour, which suits them and their temper and personality.

On the next page I have shown you the chart for the trade above. The amounts you see are Danish Kroners. They are not Pounds or Dollars. It shows my "risk per point".

1/ The chart below shows a positive Thursday, and a Friday where Dow falls below the low of Thursday, and fills the gap from Thursday. Did you know that 78.6% of all Dow gaps of more than 10 points gets filled within 3 trading days? I turn bearish as the selling accelerates below the Thursday lows, and I start selling short. I scale into my position around 25,450-60, and I add to the position as the market moves down.

Dow Trading Friday 4th December 2018



2/ Dow moves against me. You can't see that here, but it does. My stop loss is in place. I am simply watching. I am hoping that I don't get stopped out. I don't mind "hoping", as long as the hoping is done with a stop loss. I don't move my stop loss further away. That would be denial. What I am doing is "healthy" hoping. I am hoping for more profits.

3/ The Dow moves in my direction. I add a smaller amount (200). What I am really doing here is critical to understand. I have been under water on my position, and now I am finally making money.

My brain has had to endure pain during the loss period, and I am now being sent signals from my mind to relieve my brain of the pain it felt during the losing period (15 minutes earlier).

I counter-act this pain by actively doing the very thing that causes me pain. I am embracing the discomfort by compounding it. If I am to actively engage in behaviour, which is the opposite of the 90%, then this is required. You will notice that my "add-on" is not a big position. Yet, it serves to reinforce the right kind of behaviour.

4/ The Dow falls strongly. I am in the safe zone now. My core position cannot be threatened. My stops are placed at breakeven. However, I am still prepared to let this trade turn into an insignificant trade (small profit trade) in the HOPE that it will turn into a significant trade. Therefore, although I am 100 points in profit, I am by no means relaxing. I am adding to my position again and again, in smaller increments, in order to reinforce the right behaviour.

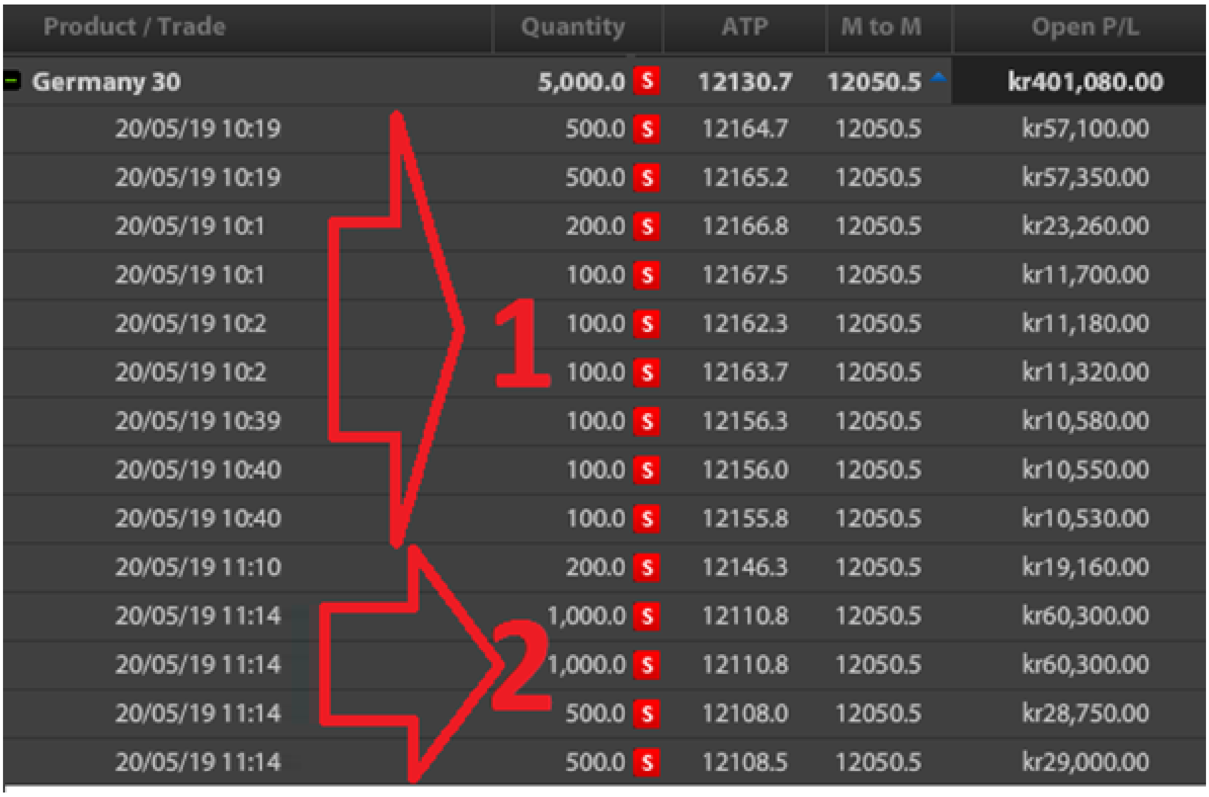
This trade has the potential to turn into a spectacular trade. It didn't. The Dow bounced strongly (before falling again), and although I made a profit, it was not the amount you see on this screen shot. That is very important for me to get across to you. Why? Because I think it is important that you understand that a good trader rarely gets out of his position at the maximum profit potential.

How can you? How can you discover what the market will give you if you are not prepared to let the profit run, and maybe give some of it back? Are there exceptions? Sure, of course there are. For example, If the market is about to close and you don't want to run the position overnight or over the weekend, then that is a perfectly valid reason to exit.

I have a philosophy to trading, which means I am prepared to sacrifice profits in order to discover how big the profit can get. If you don't have that philosophy, you will never discover how big the profit can get. If you always think of potential targets, using technical analysis, you are most likely just talking your way out of a good trade. You might be using ATR to time your exit, or perhaps you use a Fibonacci ratio to get out, but I don't subscribe to that.

There is a reason for that. When the market is trending, and I am on board the trend with a position, I hope that the market will close that night at its strongest/weakest for the day. It happens often enough to bet on occurring again. Yes, I have had plenty of disappointments, but I have had sufficiently enough stellar days to make it part of my philosophy.

Let me show you another example of a good trade, and this time I will show you precisely where I did add to the position. I will post my time and entry for you to study.



Product / Trade	Quantity	ATP	M to M	Open P/L
Germany 30	5,000.0 S	12130.7	12050.5	kr401,080.00
20/05/19 10:19	500.0 S	12164.7	12050.5	kr57,100.00
20/05/19 10:19	500.0 S	12165.2	12050.5	kr57,350.00
20/05/19 10:1	200.0 S	12166.8	12050.5	kr23,260.00
20/05/19 10:1	100.0 S	12167.5	12050.5	kr11,700.00
20/05/19 10:2	100.0 S	12162.3	12050.5	kr11,180.00
20/05/19 10:2	100.0 S	12163.7	12050.5	kr11,320.00
20/05/19 10:39	100.0 S	12156.3	12050.5	kr10,580.00
20/05/19 10:40	100.0 S	12156.0	12050.5	kr10,550.00
20/05/19 10:40	100.0 S	12155.8	12050.5	kr10,530.00
20/05/19 11:10	200.0 S	12146.3	12050.5	kr19,160.00
20/05/19 11:14	1,000.0 S	12110.8	12050.5	kr60,300.00
20/05/19 11:14	1,000.0 S	12110.8	12050.5	kr60,300.00
20/05/19 11:14	500.0 S	12108.0	12050.5	kr28,750.00
20/05/19 11:14	500.0 S	12108.5	12050.5	kr29,000.00

I am not on board the first push down. I look at the rebound for an opportunity to short the DAX index. Under “1” you essentially see me add a handful of smaller positions, rather than one big position. Most of them are added at a worse price than the first entry. This is consistent with adding to winning trades.

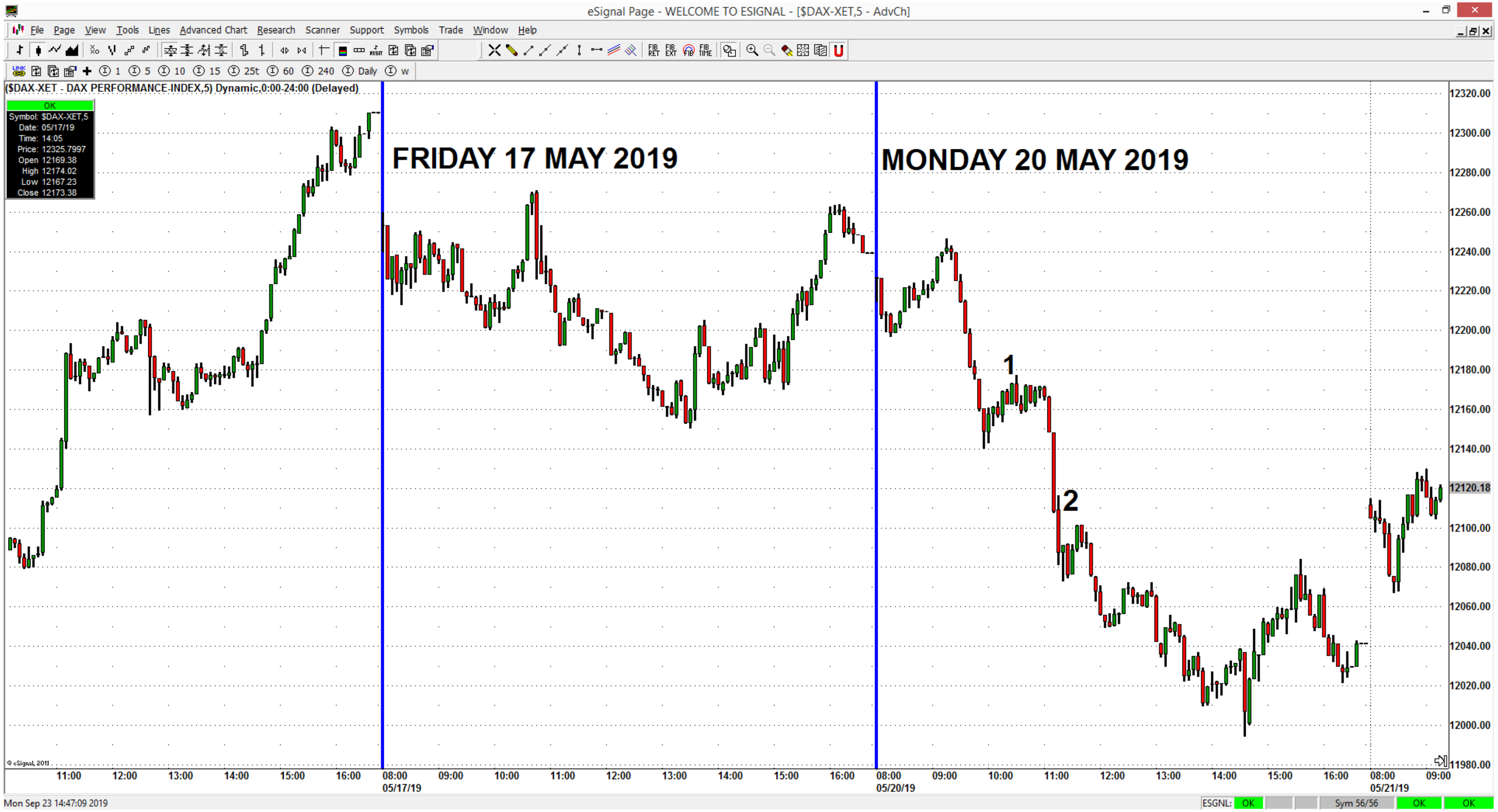
Dax finally caves in and resumes its downtrend. Now I have a profit and at “2”, I get aggressively short.

There are several things I would like to inspire you to see here:

1/ I am not afraid to sell short something that has already fallen in price. This is consistent with what the majority of people do not want to do.

2/ I scale into the position in this example, and I add aggressively to my short position once my position is in profit.

DAX Trading Friday 17th May 2019



I urge you to contemplate how you can add the element of “adding to winners” into your trading. I am not interested in re-writing your trading plan. I am not interested in making you into a copy of me. I am interested in trying to make you understand the value of “pain” in trading, as a barometer for adding to positions. If it is uncomfortable, then it is probably the right thing to do.

I hope to make you understand that by asking you a question. Which one of the two scenarios below gives you the most heartache?

Scenario A or scenario B?

Scenario A

You buy DAX at 12,125. Your stop loss is 12,100. Dax moves up to 12,150. You move your stop loss to 12,125. You add 100% to your position. Now you are long 200% in total, 100% at 12,125 and another 100% at 12,150.

At 12,175 you decide to take profit. You gain a total of 75 DAX points.

Over the course of the next 3 hours DAX moves up to 12,275. You are **not** on board. Your position 3 hours later would have been worth 275 points.

Scenario B

You buy DAX at 12,125. Your stop loss is 12,100. Dax moves up to 12,150. You move your stop loss to 12,125. You add 100% to your position. Now you are long 200% in total, 100% at 12,125 and another 100% at 12,150.

Dax moves up to 12,175, and you buy another 100%. You have moved the stop loss on the two prior positions to 12,150. Your average price is 12,150. You put a 25-point stop loss on the last position.

Over the course of the next 3 hours DAX moves in a range and finally you get stopped out at 12,150. You made nothing. Your maximum potential profit was 75-100 points, but you got nothing out of it in the end.

Which one of these two scenarios will cause you the most pain?

If it is scenario B, you can congratulate yourself from at least being able to add to winning trades. However, it is scenario A that causes me the greatest emotional pain.

It is for this reason that I am not keen on taking my profits. I find it very upsetting to see my position turn into a much bigger profit AFTER I am out of the trade. This way of trading is not without dangers. You trade bigger and bigger size, and the market on a big position doesn’t have to change direction by a lot before you give away a big portion of your open profits.

I promised you a losing trade, didn't I? Here is what happens when I lose my discipline, or I am on the wrong side of a Donald Trump tweet. However, I don't let my mind dwell on it for long. I have no way of anticipating market reversals, except if I use tools that I perhaps am not a believer in, in the first place. I have no way of knowing that Donald Trump was going to tweet.

I did what I had to do, and I lost. If you study the trade below, you will see an example of me breaking my rules. I add to a losing trade! I am not proud of it. That is why I am showing it to you. It is a way of holding yourself accountable. I am not going to punish myself for it. You make a mistake, you learn from it, you move on. The same mistake may crop up again at some other point, in a different disguise. Hopefully next time I am better at recognising my error sooner than I did here.

4,500.0	S	**11289.4**	**11314.0**	**kr-110,510.00**
300.0	S	11288.3	11314.0	[illegible]
350.0	S	11286.8	11314.0	[illegible]
400.0	S	11285.2	11314.0	[illegible]
500.0	S	11285.0	11314.0	[illegible]
500.0	S	11279.0	11314.0	[illegible]
500.0	S	11274.8	11314.0	[illegible]
450.0	S	11295.2	11314.0	[illegible]
500.0	S	11293.2	11314.0	[illegible]
500.0	S	11292.7	11314.0	[illegible]
500.0	S	11312.7	11314.0	[illegible]
2,000.0	S	**25392.4**	**25433.5**	**kr-82,150.00**
700.0	S	25378.5	25433.5	[illegible]
300.0	S	25378.0	25433.5	[illegible]
1,000.0	S	25406.5	25433.5	[illegible]

Daily Self Analysis

I am making an assumption that you already have a decent skill set in technical analysis. If you haven't, then that's where you must start. You can download my free 200-page book on trading from my website www.TraderTom.com.

It's free of charge.

https://tradertom.com/ebook/

Trader Tom — Daily Self Analysis

Mental Foundation for Profitable Trading

1. Are you prepared to do what the 90% are not doing?
2. Are you aware of your weaknesses?
3. Do you have a routine to counteract them?
4. Are you pushing yourself? Or are you "Sunday golfing?"
5. Are you trading your account or are you trading your past trades, or are you trading the markets?
6. Do you have a metaphor or a philosophy that enables you to detach from the outcome?

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The first question asks: are you prepared to do what the 90% is not doing? I know it's very easy to say: Yes, I am prepared to do what the 90% is not doing. However, what if you don't know what the 90% is doing? Then you are a little bit out of luck. I understand it is somewhat of an arrogant question to ask. It is arrogant to assume that I am different from anyone else. So, I think the first issue that needs to be addressed is, what is the 90% doing.

Trading With a Philosophy

What is it that I am meant to do? If you haven't got a strategy or a philosophy to trade from, then that is your starting point. I am going to assume that you have a strategy or some degree of technical expertise.

To me the "philosophy part" is more important. My philosophy could perhaps serve as an example to you.

1/ I prefer to buy strength rather than sell short into strength.

2/ I prefer to sell weakness rather than buying into a weak market.

2/ I will add (aggressively) to my winning trades, but I will never ever add to my losing trades.

Already there I am doing something the 90% will never engage in.

Trader Tom — Daily Self Analysis

Mental Foundation for Profitable Trading

1. **Are you prepared to do what the 90% are not doing?**

What does that involve? You need to create 2 things:

1. **A method you can trade from. This is a strategy.**
2. **A philosophy – Not any old philosophy – but one that makes you different to the 90%**

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There is an easier way of answering whether you are in the 90% group or in the 10% group. Are you engaged in research? Do you pour over the charts during your free time? Are you doing research over the weekends? Are you disciplined with your stop losses? Are you able to run a winning position for a lot longer than you perhaps are comfortable with? Are you often letting your stop loss take you out of your winning trades rather than closing them by yourself? Well, these are some of the qualities that will separate the 10% from the 90%.

This on its own doesn't ensure profits of course. However, I don't think anyone was ever immediately profitable in trading. I know it's easy to resort to stories about famous traders and how they blew up initially, before they made a success of themselves. It is somewhat of a cliché to hear stories like that. On the other hand, it may just serve as an inspiration to you, if things are not going exactly how you had imagined it would.

Paul Tudor Jones describes how his risk management was awful to begin with. He made it his life mission to get his risk under control. The rest is history as they say. He stands out as one of the greatest lights in the trading world. So, don't think it is rocket science what you must do to be in the 10% group. Trading is no different from any other endeavour.

It takes practice. It takes effort. It takes consistency. It takes application of the human qualities that makes us good at anything: patience, desire, tenacity, ability to withstand setbacks, having a grand plan, maybe do some visualisation of where you want to end up. There's nothing wrong with being a dreamer. But if you want your dream to come true, you need to back it up with a significant amount of planned routines. That is a "10% quality".

What is My Weakness?

Are you aware of your weaknesses? My weakness is "boredom" and "being too aggressive". I am also prone to shorting the market more than going long. I have at times been accused of fighting the trend. It is difficult to hide when you have a Telegram channel and you trade live every day, while streaming your trading account. All the criticism is true at times.

Do you have a routine to counteract your weaknesses? Yes, I have a routine to counteract them, but I am certainly human as well, and I fail often. They are not catastrophic failures. Ultimately, you have to remember that when you buy, someone has to sell, so there has to be differing opinions for there to be a market.

I will review past trades to remind myself of what I am hoping to achieve. I should say this gets much easier with time, and now it is simply part of who I am. My routine consists of going through a collection of some good trades and some poorly managed trades of mine. That is my warmup ahead of the trading day.

Are you pushing yourself? Imagine you have a trading strategy that yields a profit of some percentage. My question to you is: are you operating in your comfort zone or are you conscious of trying to increase your trading size little by little?

Trader Tom — Daily Self Analysis

Mental Foundation for Profitable Trading

1. Are you prepared to do what the 90% are not doing?
2. Are you aware of your weaknesses?
3. Do you have a routine to counteract them?
4. Are you pushing yourself? Or are you "Sunday golfing?"
5. Are you trading your account or are you trading your past trades, or are you trading the markets?
6. **Do you have a metaphor or a philosophy that enables you to detach from the outcome?**

The great thing about running seminars to me is that you get to meet people like yourself. My advantage is that I (in most cases) have more experience than the people I am teaching. I am not saying I am a better trader than they are, but I have "seen things" over the years, things that most people might well be aware of, but may not know how detrimental it can be to your trading.

For example, if a trader has had a few losing trades, there will be a tendency to bring the emotions of those trades into the decision process on the next trade. So now you are no longer trading the current trade by its own merit. You are also trading your last trade at the same time.

This sort of mental accounting can be quite detrimental to your account. Say for example that you lost 20 points on your last trade, and you now have a winning trade that is making you 20 points. If you are conscious of what your last loss was, then you may be tempted to do a mental accounting exercise, and close your position, to even the scale monetary and emotional scale.

This is perfectly natural, but "natural" is sadly a costly emotion. It is our "natural" human responses that makes us lousy traders. Just because it is natural does not mean it is in your interest to act this way. As Charlie D, who you will get to know later, says: *you have to fight your humanness*. This part is by far the hardest to train and the path to detachment and describing it is convoluted, but I will give it a try

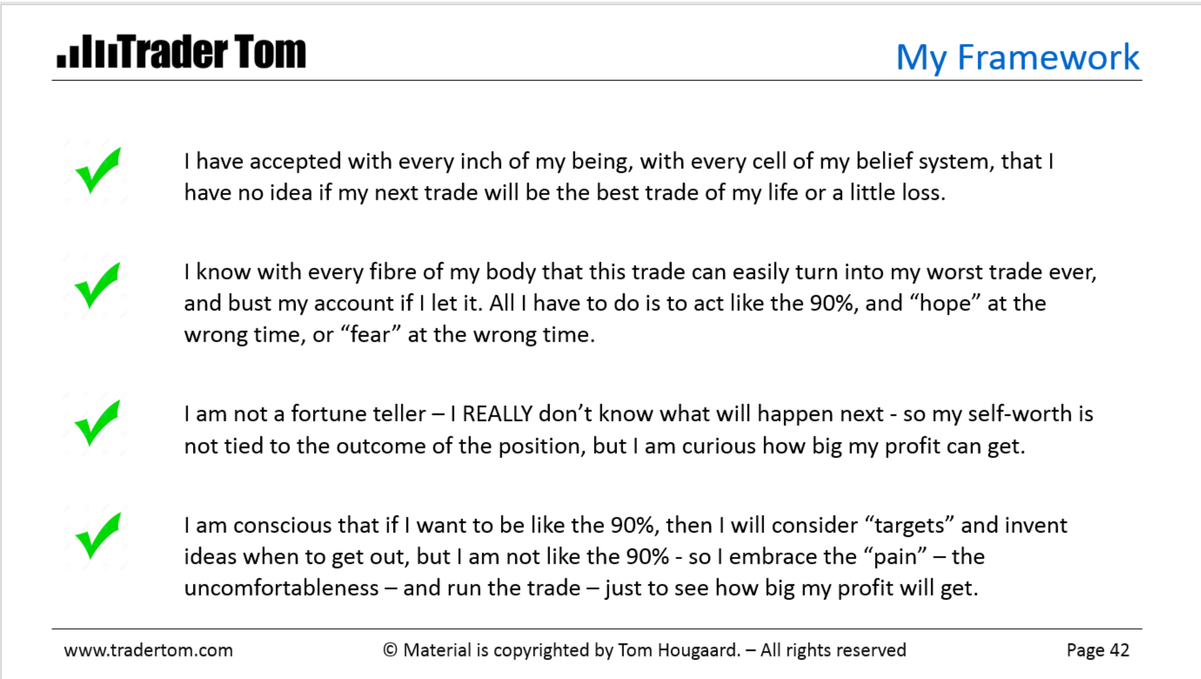
Imagine it is Monday morning. You have no open positions. You have done your chart preparation. The market is about to open. Do you have a mental plan? I am not talking about a strategy. I am not talking about a plan where you have decided to “buy here” or “sell there”. I am more interested in if you can tick these boxes – displayed below?

My Mental Framework

I have accepted with every inch of my being, with every cell of my belief system, that I have no idea if my next trade will be the best trade of my life or a little loss.

I know with every fibre of my body that this trade can easily turn into my worst trade ever and bust my account if I let it. All I have to do is to act like the 90%, and “hope” at the wrong time, or “fear” at the wrong time.

I am not a fortune teller – I REALLY don’t know what will happen next - so my self-worth is not tied to the outcome of the position, but I am curious how big my profit can get.



I am conscious that if I want to be like the 90%, then I will consider “targets” and invent ideas when to get out, but I am not like the 90% - so I embrace the “pain” – the uncomfortableness of the uncertainty – and run the trade – just to see how big my profit can get. If I tell you I treat it like a video game, and I try to beat my high score, would that resonate with you?

The Mental Giants

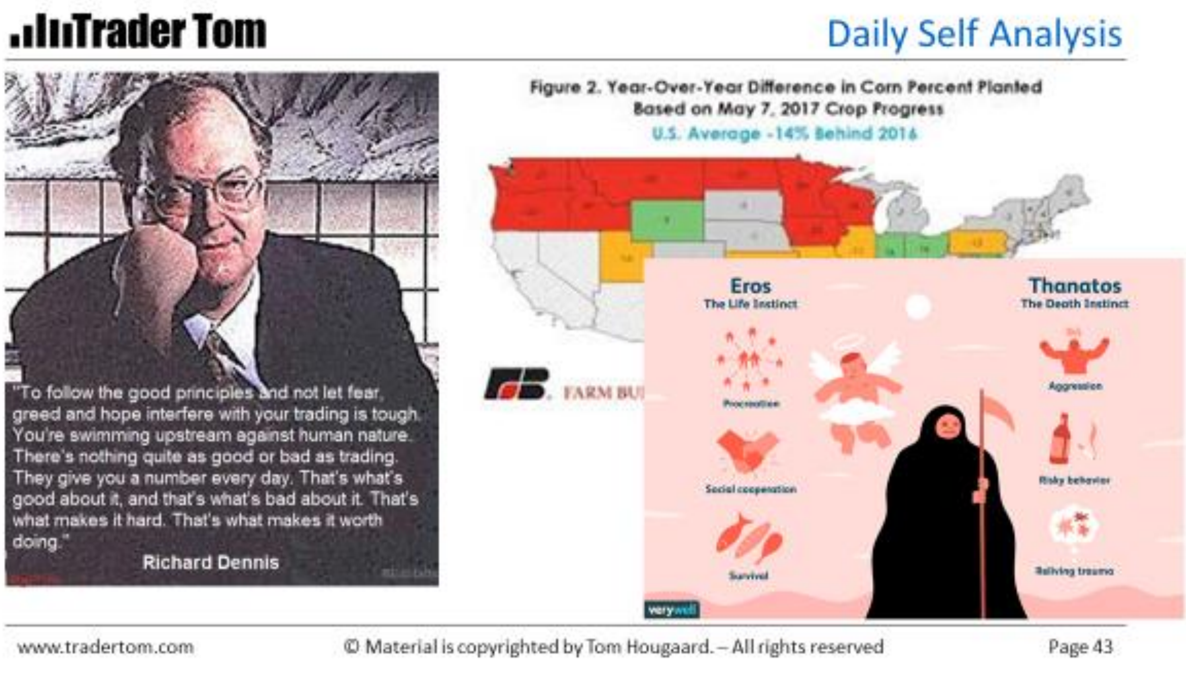
The most famous group of traders ever were the Turtle Traders. It was the brainchild of two Wall Street legends, Richard Dennis and William Eckhart. It is richly described in the Market Wizard book by Jack Schwager.

I want to spend some time talking about Richard Dennis. As I said, he is a famed commodity trader and also a former pit trader on the Chicago trading floors. Not so many people today know how he got so good at trading, and how he addressed the typical issues that faces every trader. He called it the battle with the self. The battle with self was where he focused his energies:

"*I think it's far more important to know what Freud thinks about death wishes than what Milton Friedman thinks about deficit spending*, "he said.

Someone who traded with him in the soybean trading pit in Chicago said this of him:

"*Dennis is much more likely to carry a book on Freud's theories than he is inclined to carry the latest crop report. He seemed to be far more focused on the mind's interaction with his trading than any corn report that may be published by federal agencies. That makes him very different to the rest of us*."



Mental Accounting

People will do what people will do. Nevertheless, I think point number three is one of the most important statements about trading that you will ever read. I don't think you can have a standard attitude about money and do well in the business of trading. I think there is a danger in trading when this one draws direct links between trading and life.

Let me give you an example: I am in a trade and it is not going the right way. I look at my profit and loss on my monitor, and I see how much money I am losing. I'm beginning to let my mind wander. I will imagine what I could have bought with the money that I am currently losing.

Trader Tom — Daily Mental Rehearsal

Maybe a little "new age" advice – but here goes

1. Making sure I am fit – strong body – rested body – rested mind
2. Practicing detachment – what we do is not normal.
3. You can't have a standard attitude about money and do well in this business.
4. **The best way to learn detachment is to practise it.**

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Maybe my partner has told me they want to go on holiday, or they would like to visit a car dealership for a new car. I begin to add up the cost of the holiday or whatever it is I am contemplating buying, and I look at how much I am down for the day or the week, and I observe how much my current position is making.

You have probably already figured out that this sort of mental accounting is not an ideal exercise for a trader. You are no longer trading the markets and assessing the situation dispassionately. You are trading your "new car" or "your holiday" or "your last trade".

Say for example that you received an unexpected inheritance, or you received a tax refund that you had not anticipated. Well, you are more likely to spend that money on reckless things. You often hear brokers and well-meaning educators say that you should only speculate with money that you can afford to lose. Well, that may be true. However, that is not the kind of attitude that I want to bring into the trading arena. I would rather bet on a person with discipline and a small account to make it, than I would be on a large account traded by a man with no plan and no discipline.

Of course, I am not arguing that one should take a loan in order to fund a trading account. Now that would be reckless. However, I don't think one should open a trading account either with the view that this money can be lost without consequences. This last sentence seems to go against my first statement which was, "*you can't have a standard attitude about money and do well in this business*." However, there is, to my mind, a big difference between being fearful and being reckless.

I am generally very careful with how I dish out advice. As I grow older and hopefully a little wiser, I realise that one man's meat is another man's poison. You simply can't tell someone how to live their life or do their job. The best you can do is to inspire them through your own path and example. So when I say to you that you can't have a standard attitude about money and do well in trading, I mean it from the perspective of experience. However, it is true for me, and it may not necessarily be true for you. I suspect it is, but I can't be sure.

I do much better when I don't look at my P&L during the day. Even if I was to glance over to my P&L to see how much money I have made or lost on the day, I am generally not unsettled from it. I prefer to know that I am in profit, but I will worry about the size of the profit when the trading is over. In the meantime, I will do what is the right thing to do dispassionately.

Let me finish off this rather important point with a quick generalisation. When I am trading on volatile days and I'm building up a big position, which is yielding a big profit, then I know from experience that I have to be very careful about assessing the market from a monetary point of view, versus assessing the market from a factual point of view. In other words, am I closing my position because I think the market has run its course, or am I closing the position because I want to feel good about myself and take away the anxiety of running positions?

This is where my philosophy to trading comes in handy. I treat it like a video game. My mission is to beat my high score. That makes it a game, one that I like to play over and over. It detaches me from the monetary outcome, and it means that I can evaluate and execute the plan from an objective point of view.

I will say this though. It is much easier to say this than to implement it. It takes time and practice. It is, would you believe it, one of the primary reasons for being so adamant about adding to winning positions. It is my way of counteracting the unconstructive signals my protective brain sends me.

By treating it like a video game I seem to be more detached. It works for me. I see the money as points. I want to beat my high score. It must sound juvenile, but it works for me.

Everyone Understands Charts

Developing low risk ideas is our job as traders. I think the 80 to 90% of people that lose money trading may very well have excellent abilities. They can read charts very well, and they understand patterns too. However, I think there is much more to trading than knowing a “head and shoulder” formation, a bar chart special pattern or a Fibonacci ratio.

I truly believe that what separates the 10% from the 90% is how they think when they are in a trade. Of course, you can learn things from studying charts. I run a one- and two-day course where I teach people things that I don’t think they would have noticed without considerable study time. I believe that’s what they are paying for, but that is not to say I am not aware of the very real possibility, that my students think that trading is all about techniques. It is for this reason that I run a live trading group every single day. I lead the way by showing people where I would like to be a buyer or where I would like to sell short.

Learning technical analysis is not difficult. It is what makes the field attractive to newcomers. What would you prefer: spend 3 years learning how to value companies and assess economic principles, or buy a good technical analysis book on a Saturday morning, and by Sunday night be quite proficient in TA? As I said, it is a no-brainer.

However, just because you have a STA diploma (Society of Technical Analysis) does not make you an accomplished trader anymore than reading a book on golf makes you welcome on the professional golf circuit.

Trader Tom

Developing a Low-Risk Idea

1. High performance traders approach their preparation like a pro tennis player approaches his preparation to a game.
2. The 90% that loses with spread betting and CFD companies, they know chart patterns as well as the best of us.
3. Successful traders also train people, but their skills are unlikely to be transferred to the student? Why is that?
4. Because there is much more to trading than seeing a double top pattern.
5. Why is it that there are more winning trades in our industry than losing trades? Because technical analysis is not difficult.

If people were not good technical analysts, I don’t think the FXCM clients from the previous pages would have a hit rate of 62%. I believe it is the knowledge of technical analysis amongst retail traders that cause the fact that there are more winning trades than losing trades in our industry.

A coin-flip strategy should produce a 50/50 outcome, but most retail traders have a hit rate around 65%. In my opinion this supports the argument that the real test of trading is how we think when we are in a winning trade or when we are in a losing trade.

I don’t think people need to learn more technical analysis to make more money. I think they need to learn how to play to their mental strengths.

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Let me get personal. Let me take you behind the curtains and show you what it's like to do what I do. Remember, I'm a private trader. I don't trade for a hedge fund. I don't draw a salary unless I win.

I survived the flash crash of 2010, but only just. I was lucky not to be heavily embroiled in the Swiss Central Bank drama 5 – 6 years ago. Every day there are plenty of opportunities to bust your account, if you are not mentally ready and fighting fit. And I can't rule out the possibility of just being plain unlucky by having a big position on, just as Donald Trump makes a Twitter announcement that moves the market against your position.

As I said, let me get personal. Today is the 1st October 2019.

I am currently in 2 trades. I am short the DAX. I am short the Dow. This is my third trade today. The first trade of the day, also a short in the DAX, got stopped out. It was one of those "unfair" ones, where the market clips your stop by a point or two, and then it moves in your favour. I lost 25 points on that trade.

I entered a short position in the DAX again shortly after, and the German index has fallen rapidly this morning. I added to the short position, as it fell, and right now I am plus 100 points in open profit.

Here is my first screenshot of the position. It is sent to my Telegram group at 09:02am (UK time).

		Amount	Open Price	Current Price	Open P/L
Germany 30	Sell	200	12479.8	12435.7	€8,820.00

Am I tempted to take my profit?

Yes?

Why is that?

Yesterday was a poor day of trading. I lost 150 points. I read the market poorly, or to be kind to myself, I had an idea, and the idea didn't work out. Either way, I lost 150 points.

If I close my DAX position right now, I can make up for the lost trade this morning, and I can recover a lot of the points lost yesterday.

I am also short the Dow. The Dow position is showing me a profit of 53 points. Am I tempted to close that trade? Yes. Why? Because if I close all the trades right now, I can make about 150 points. It would be as if yesterday and this morning's losses never happened. Now that is a soothing thought, isn't it?

You have this ping-pong dialogue in your head, arguing for and against taking profits. I am no stranger to that conversation. I may have many years of trading experience, but I still have those thoughts in my head.

What I am experiencing is known as Cognitive Dissonance. In the field of psychology, cognitive dissonance is the mental discomfort - psychological stress - experienced by a trader who holds two contradictory beliefs or ideas. This discomfort is triggered by a situation in which a person's belief clashes with new evidence perceived by the person. When confronted with facts that contradict beliefs, ideals, and values, people will try to find a way to resolve the contradiction to reduce their discomfort.

The best way for your rational mind to resolve the discomfort of a profitable position is to close it. The best way for the rational mind to resolve the discomfort of a losing position is to let it run.

From the book "A Theory of Cognitive Dissonance" from 1957, the author Leon Festinger proposed that human beings strive for internal psychological consistency to function mentally in the real world. He says that a person who experiences internal inconsistency tends to become psychologically uncomfortable and is motivated to reduce the cognitive dissonance.

One way to achieve the goal of reducing the discomfort is by making changes to justify the stressful behaviour, either by adding new unsubstantiated or irrelevant information to the cognition, or by avoiding circumstances and contradictory information likely to increase the magnitude of the cognitive dissonance.

In my case, I am conflicted. I am associating pain with the performance of yesterday. I am able to eradicate the pain by closing my positions right now. The way I am able to justify this reasoning is by ignoring the information the market is giving me about my position. The market participants agree with me that the market should be sold short, but instead of acknowledging this, I am considering ignoring it.

From a logical point of view, this all makes sense. From an emotional point of view, this is an inconsistent approach to trading. My trades from yesterday have no bearing on the markets today. It is a new day. It is a new set of circumstances. Yet to my mind, the two trading days are connected. To my mind I am continuing today what I did yesterday. Why wouldn't I be, I tell myself? If I am on a roll, I bring that enthusiasm and confidence with me to the next day.

Are you telling me that you can "reset" your emotions every morning? Are you telling me that you can go to bed at night after a blazing row with your loved ones, and you wake up all reset and emotionally in equilibrium? I doubt it. It is for this reason that I warm up ahead of the trading day, by going through a process. We will cover that later.

However, there is a simple way to resolve this cognitive dissonance. When I say "simple", I acknowledge that it is anything but simple, because we are dealing with emotions, and neither one of us are reasoned purely by logic. Where is Mr Spock from Star Trek when you need him? He battled to reconcile the two natures within him—the rational, staid pragmatism of Vulcan and the wild, un-tempered emotionality of Earth. This half-Vulcan half-human spent his entire life trying to accommodate these halves, for the purpose of creating a balanced centered being.

The cause of the conflict is down to fear. Let us call a spade a spade: we are afraid of losing money. We are afraid we are taking on too much risk. We want the upside without the downside. We want the big stake but without the risk. We want to win big and lose nothing.

It is our fear that stops us from conquering our wildest dreams. You know the clichés, as well as I do. Face your fears, live your dreams etc. I even have a notebook, which has on its front page my favourite fear quote. "Everything you ever wanted lives on the other side of fear."

Yet fear is a necessity in our lives. The human brain is a product of millions of years of evolution, and we are hard wired with instincts that helped our ancestors to survive. We need fear to ensure survival in certain situations, but many of the fears that we are hard-wired with are not appropriate for our trading.

Our minds have a primary function, which is to protect us against pain. If you introduce big drastic changes in your life, you are likely going to come face to face with that pain. A clever way to introduce staying power for your change is to introduce change slowly.

Say you set yourself the ambitious target of running a marathon, you achieve this goal by building up your body and mind for the task. Trading big size is exactly the same process. You need to give your mind time to learn to handle the mental anguish that comes from losing when the stakes are bigger.

There is no point in comparing yourself with others. Sure, take inspiration from others, but know this is a personal journey, and your job is to achieve an equilibrium mindset, no matter what size you are trading.

You want an example? You want some inspiration? Then why don't you cast your eyes on the photo below. This is a photo of a gentleman called Phillipe Petit, as he is making his way from one of the towers at the World Trade Centre to the other tower.

I saw the original documentary a long time ago. This was long before the Hollywood adaption of the story. What struck me about the incredible feat was the preparation.

It took Phillipe some 7 years of preparation to accomplish the feat. Did you think he just set off and hoped for the best? Hell no. He prepared and prepared. I took a snapshot from the Netflix documentary, which has old grainy black and white videos of his preparation.

As you can see from the image, his original training height was quite modest, compared to what he would eventually end up with.

Phillipe Petit is a fascinating character, and he is someone who has had to deal with fear at a whole other level than any of us ever had to. I have learned a lot about fear and identifying my own shortcomings by studying his approach to his craft.

He Wants to Visualise Victory

"*Before my high-wire walk across the Seine to the second story of the Eiffel Tower, the seven-hundred-yard-long inclined cable looked so steep, the shadow of fear so real, I worried. Had there been an error in rigging calculations?" How did he overcome his doubts? With a simple visualization exercise: "On the spot I vanquished my anxiety by imagining the best outcome: my victorious last step above a cheering crowd of 250,000.*"

He Exaggerates His Fears

Rather than try to muscle through or outwit fear, Petit suggests taming it by building it up so that when you are finally faced with your fear, you will be disappointed by how mundane the threat really is.

"*A clever tool in the arsenal to destroy fear: if a nightmare taps you on the shoulder, do not turn around immediately expecting to be scared. Pause and expect more, exaggerate. Be ready to be very afraid, to scream in terror. The more delirious your expectation, the safer you will be when you see that reality is much less horrifying than what you had envisioned. Now turn around. See? It was not that bad--and you're already smiling*."

He goes on to say that he has fears like everyone else. In particular, he talks about his dislike of spiders.

On the ground I profess to know no fear, but I lie. I will confess, with self-mockery, to arachnophobia and cynophobia (fear of animals). Because I see fear as an absence of knowledge, it would be simple for me to conquer such silly terrors.

“I am too busy these days,” I’ll say, “but when I decide it’s time to get rid of my aversion to animals with too many legs (or not enough legs—snakes are not my friends, either), I know exactly how to proceed.”

I will read science reports, watch documentaries, visit the zoo. I will interview spider-wranglers (is there such a profession?) to discover how these creatures evolved, how they hunt, mate, sleep, and, most importantly, what frightens the hairy, scary beast. Then, like James Bond, I won’t have any problem having a tarantula dance a tarantella on my forearm.

Petit's walk remains one of the most fabled, and stunning, acts of public art ever. He says there was no WHY to why he did it. To quote his own words, here he is:

To me, it is really simple. Life should be lived on the edge of life. You have to exercise rebellion, to refuse to tape yourself to rules, to refuse your own success, to refuse to repeat yourself, to see every day, every year, every idea as a true challenge, and then you are going to live your life on a tightrope.

I am quite cynical towards those who peddle clichés. It doesn't sit well with me to hear people say that I should run my profits, but I should cut my losses. It doesn't sit well with me when a female friend tells me she is in an abusive relationship, and another friend chirps in and dismissively states that the solution is to "just leave the bastard." It is a platitude. It is factually true, but it is nonsense, nevertheless. When a solution is obvious, the problem is rarely the only problem. You might as well tell an alcoholic to just stop drinking. There is a reason he is drinking, and there is a reason he is struggling to stop.

Failure is always a possibility in life. I participate in a radio program about trading and investments. The focal point of the show is the competition between me and two other traders. The competition is always fierce, and every week we are being questioned about the content of our portfolios. My trading style is quite black and white. If I think the market is headed lower, I will buy some put options or some bear certificates, and vice versa if I am bullish.

I learned a long time ago that the best way to shut down a journalist is to be 100% honest. So, when the radio host baits me by saying "uhh Tom, you got that one wrong huh?", the worst thing I can do is to start defending myself. If I start making excuses or put up defences, I simply pour petrol on that fire.

It is such a great metaphor for life. Own up to your errors and be done with it. So when the radio host is trying to engage in a line of questioning aimed at getting me to defend myself, I always double down in the opposite direction by saying something like "Oh my lord, I don't think I could have been more wrong, even if I tried", or "Oh boy, even a 5-year old could have done better than me."

We are bound to make mistakes in life, but mistakes are like fuel for the rocket of improvement. Talking of rockets, how do you think people like Elon Musk handle failure? He is trying to accomplish humongous life changing things -- things like the electrification of automobiles and the colonisation of space, and he does it while the whole world is watching.

For him the possibility of failure is ever present, but when he fails, it is a spectacular headline creating spectacle, and yet Musk just keeps on going and going, doing incredibly audacious, risky, and valuable things.

How does he handle his fear of failure? Or is he just some superhuman, genetically gifted individual with a mercifully malfunctioning anxiety circuitry? Nope. Apparently not. He has publicly stated he feels fear quite strongly. So how does he keep going despite this terror?

Passion

Musk, it seems, has a two-part recipe for fearlessness. The first essential ingredient is heaps and heaps of passion. The SpaceX was an insane venture, but he had a compelling reason for pushing ahead: “*I had concluded that if something didn't happen to improve rocket technology, we'd be stuck on earth forever. People sometimes think technology just automatically gets better every year but actually it doesn't. It only gets better if smart people work like crazy to make it better. By itself, technology, if people don't work at it, actually will decline. Look at, say, ancient Egypt, where they were able to build these incredible pyramids and then they basically forgot how to build pyramids.... There are many such examples in history... entropy is not on your side*." Elon Musk was not prepared to sit idly by and watch that outcome unfold.

Musk also deploys a strategy of fatalism. Just focusing on why you're taking a scary risk isn't always enough to overcome hesitation. It wasn't for Musk. He employed an additional strategy as well. You could call it strategic pessimism. He calls it "fatalism."

"*Something that can be helpful is fatalism, to some degree*," Musk has said. "*If you just accept the probabilities, then that diminishes fear. When starting SpaceX, I thought the odds of success were less than 10 percent and I just accepted that actually probably I would just lose everything. But that maybe we would make some progress*."

He is not the only one to use this strategy. By really visualizing the worst-case scenario can make you appreciate objectively what you are trying to achieve. It's a form of exposure therapy: by facing the thing you fear, you break its power over you and realise that you will survive even if the worst comes to pass.

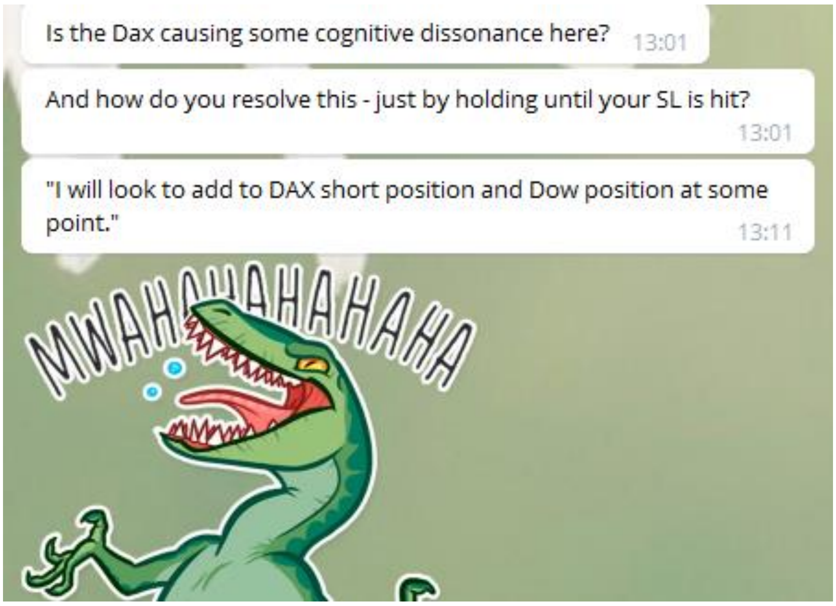
Have I digressed too far from the trading journey ahead? I don’t think so. I draw inspiration from many sources outside of the trading world. Kobe Bryant, Rafa Nadal, Charlie Munger, to name a few. Very different people, yet all obsessed with the journey and the enrichment of their lives and the perfection of their craft.

Is It for You?

Is it for you? I don’t know. Permit me to ask you a question: what is the alternative? You are reading this because you want to trade well. Perhaps it is time to acknowledge trading for what it is? It is a great way to expose all your insecurities. It is a great way to highlight your strengths. Work on your weaknesses and you will find that trading is much more than a job and an income stream. Failure is one of our greatest learning tools.

Well, that was a heavy section. I hope you are still with me. You know, one of the hard parts of change is how other people perceive our quest. Not everyone is as supportive as one could wish for. To silent our inner critic is hard enough, but when we also have to silence our friends and colleagues, it becomes much harder.

I was in a short position last week in the DAX. I have a running dialogue with many of the people who are in my Telegram group. One trader in particular had some good views on the market. However, he was often very vocal in his criticism of me. I had just posted some words about being torn between two outcomes, hence the chapter on cognitive dissonance. Here is what he sent me.



He is rather vocal about his opinion about my short position in the Dax index.

He posted this at 14:59. At that point the chart looked like this. I saw no reason to be long, but when someone you do trust and respect gives you an opposite opinion, it is a good opportunity to double check internally.

It may be a reflection of my own experiences, but I find that trusting myself and my own opinion – after I have given it considerable thought – is the best path forward.

Then at 3pm – one minute after his post to me – the market fell through a trap door, and it turned into one of the best trading days ever in my life. Trust yourself!

On this trade, here shown in a much bigger perspective, I am short from 12,470, with a stop loss at 12,495. I get stopped out, but I sell short again at 12,480. By the time the market is trading a 12,440, I am adding to my short position.

Poker Face

It is the 9th September 2019. It is a Monday, and I'm preparing for a series of speeches this coming week. I'm aware that I probably need to be a little careful when I'm trading. So I am trading at a 50% pace. It means my stake size is smaller than usual.

Still, there is plenty of room to mess things up.

Right now, I am in a position in the DAX index. Today is Monday. On Friday the unemployment report was released in America. The market reacted rather positively to it, so we expect that there will be some follow-through today. But the market is not in a rush today.

And here's a very important lesson: when the market changes its tune, you better make sure that you change your tune with it. When the market has been incredibly volatile, and then it calms down, it can be very difficult to adjust your trading to the new set of circumstances.

It is for this reason that I printed a picture of our very own Mads Mikkelsen (he is Danish) as the villain in Casino Royale, sat opposite James Bond. They may be playing poker, and poker is a game of statistics, a game of chance and odds. However, as anyone who has ever played high stake poker will tell you, there is a whole lot more to it than just "odds". You don't play the cards in your hand. You play the man opposite you. You may be sat with a strong hand, and you are barely able to contain your excitement, but the guy opposite you also seems quite content, and he keeps raising the stakes. Is he bluffing? Is he for real this time?

It may not be a direct metaphor to what trading is all about, but it goes a long way in explaining the game of trading. I may have a very strong opinion about what the market should do today, but unless the market collaborates with my opinion, the market wins. There's no point in you wanting to disco dance with the market if the market only offers you a slow waltz.

What I believe makes trading the challenge it is, is the "spectrum of outcome". All of us live normal linear lives. However, in trading "normal" doesn't really exist. Either you are doing very well, and you are making much more money than any normal day job could ever offer you, or you are losing money head over fist. One day you are the king of the jungle. Next day you are an old man in despair.

The challenge is the emotional roller coaster that is associated with it. You can do all the right things in the trading, but no amount of preparation can anticipate the unexpected, such as Donald Trump posting a Tweet, and you are caught on the wrong side of the market. However, if you don't find a way to roll with the punches, this business will grind you down.

That is the bizarre bit about the trading world. You can arrive in the morning, unprepared and hungover, and yet you happen to catch a break in the market, by chance and by luck, and you make a substantial amount of money. There are also days where you spend hours preparing, but the market is just not collaborating with your idea that day.

Virtually every single person in the world lives "linear lives". What do I mean by that? I mean that everything we do more or less is on a schedule. We more or less have the same amount of sleep every night, we more or less eat at the same time every day, we tend to get up at the same time and go to bed at the same time every day. We go to work at the same time and leave work at the same time every day. And we are most certainly paid a salary at the same time every month, and it means that our salary is the same every day. In other words, our lives are "linear".

Trading however is nothing but linear, and if you try to make it linear, you are in for big trouble. This transition is what baffles virtually everyone, and it is what makes trading difficult. You will not be able to ride the big winners because you think the markets are linear, and the market will reverse to the mean, so you had better get out with your profit before it does reverse. When you are losing, you sit and wait for the mean reversion, because you think everything in the world is linear, so you think that the market will come back at some point.

A man goes to work. He does his job. He goes home. He is paid for his service. Depending on his competency, he will get rewarded accordingly. Say for the sake of the argument, he is paid $500 for a day's work.

He now starts to trade, and he buys the Dow. The Dow explodes higher a few minutes later. He moves his stop loss to break-even. He is in a risk-free trade. His open profit is rising,

$500, then $750, $1,000 etc. He hasn't done anything for that money. He is making more money in a few moments than he does for a full day's work. His linear mind is struggling to cope with that. How can I make so much money for so little effort, he asks himself? The profits climb, and his linear mind begins to extrapolate. If I get to $2,500, it is a whole week's salary I have earned. If I get to $3,000, I can pay off my loan.

Every little tick up and down on his position is equated to a tangible objective. Every move higher is associated with more joy, more financial goodwill. Every move in the other direction is associated with burst dreams, with financial goals evaporated. You can hardly blame him for being emotionally exhausted. He is no longer trading the market. He is trading the size of his account. He is trading his dreams and his goals. He is no longer objective.

The linearity issue in trading is a problem I have heard no one discuss. I think it needs to be addressed thoroughly, perhaps more thorough than I can do it justice right now. In a normal job we have a sense of security. We know we will get paid a lump sum at the end of the month. That is called our salary.

However, in trading this safety is gone. Anyone who has ever tried to recreate the linearity from their normal jobs onto trading will testify that it is impossible. If you make $500 a day in a job, that equates to making 10 points a day in the Dow trading $50 per point.

"Anyone can make 10 points a day in the Dow", they tell themselves. Sure, most people probably can make 10 points, but there are some major flaws in the plan:

1. At what stage during the trading day will you make the 10 points? If you make it early, do you then just stop for the day?
2. If you start with a loser, do you then carry on until you have made the 10 points?
3. What if you have 10 points in profit, do you just take the reward, instead of letting the profit run?
4. Do you stop taking your losses because you feel you can't afford to close them, because then you are even further away from your daily target? "As long as the trade is open, there is hope", you tell yourself.

Our linear mindset is imposed on a framework, the markets, which is anything but linear. You can be majorly rewarded for very little work. You can be rewarded with a pittance or a loss, despite having sat at the screen for 12 hours without as much as a coffee break.

Therefore, it is vitally important for success in trading that you are trading the markets, and you don't trade a million other things, such as your last trade, or the state of your account, or any other of the dozen or so emotionally charged agendas that your linear mind has "kindly" constructed for you.

How do you avoid that? Well, there is no quick fix, but it all starts with an awareness of your state of mind. If you feel the slightest twinge of hesitation at the thought of executing a trade, then don't. Don't execute the trade until your rational mind (the one that saw the trading setup) and your emotional mind (the one that is going to make you ride this winner, or make you take the loss at the appropriate time) is 100% aligned.

What tools can you use for that? There are a few great tools for this objective. Here are some of my suggestions, not in any particular order of importance.

Imagine It

1. **Imagine it**. I think some would call it visualisation. It is a grand word for something as simple as simply imagining yourself achieving your desired outcome. Some people call it mental rehearsal. Don't let the new age smell to it put you off. If you are a logical thinking man or woman, you may be put off by the thought of using an airy-fairy New Age tool. I appreciate that, but I am not proposing you start wearing violet coloured clothes and put a daffodil in your hair. I am proposing you sit quietly and imagine a future trade, or even better a past trade, and you give it a better outcome, especially if you are unhappy with the original outcome.

Print It

2. **Print it.** I have plotted my best and worst trades on a chart on big A3 pieces of paper. As part of my preparation, I am looking at old trades. It reminds me of what I am trying to achieve. I have plotted my entry and my exit, and my add-on trades on the chart. I have also shown what happened after I exited the trade. How did the market evolve after I got out? Was there a good reason for the exit? It is time consuming. I will admit that, but you will get a very different perspective to your trading.

Control Your Mind – Control Your Future

The following pages, from page 55 to page 64 should be told as a story rather than as individual slides. So, I recommend you read the text and browse through the pages as it becomes relevant to do.

I don't want you to think that I'm a masochist. Nothing could be further from the truth. If I do tend to dwell on pain, it is more a reflection of pain's role in the context of trading profitably. What I'm attempting to do is a difficult endeavour. I'm trying to explain why 90% of all people fail in achieving their dreams and hopes when it comes to trading.

When so many people commit the same mistakes over and over, there must be a deeper meaning that has yet to be uncovered. Naturally I'm hoping that by now you will have a much greater understanding of what it is that is going wrong. I am not into trademarking, but if I could, I think I would trademark my own saying: **Control Your Mind - Control Your Future.**

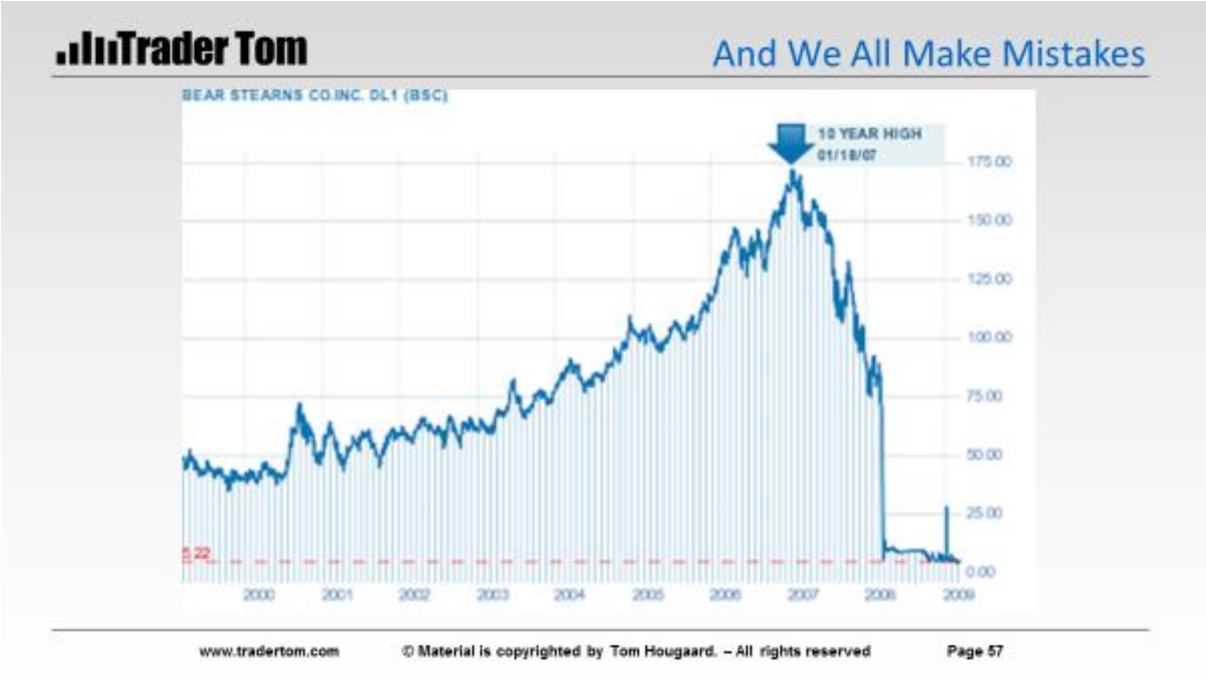
I don't want you to think that I am speaking to you from an elevated level either. I don't want you to put me on a pedestal, just in case you were tempted to do so. Professionals make mistakes. Of course, they do. All the time. I could sit here and speak mightily about trading, as if I never made mistakes myself, as if I never broke my own trading rules, but that would be a preposterous lie.

Of course, I make mistakes. Of course, I have bad days. Of course, I look back on certain trading days and I think to myself what the #### was I doing?

I remember very vividly watching CNBC during the financial crisis in 2008. Mr Kramer received an email from a viewer asking about the health of Bear Stearns. Now I am sure that if Mr Kramer had an opportunity to go back in time, he would most certainly amend what he said in that broadcast. He basically shouted at the screen, saying that Bear Stearns was fine. He probably had shares in the company. A mere 72 hours later Bear Stearns was gone, done and dusted, never to be seen again.

It is easy to be swayed by a "supermarket mentality" when we are trading. When we go into a supermarket, we are drawn towards the special offers. When I look at my shopping basket from this weekend, I see things that I wouldn't normally buy. Of course, I would need these things at some point or another. We all need toilet paper. We all need dishwasher tablets, and we all need hand soap. The reason why they were in my shopping basket this week was because they were on offer. Who can resist a 50% discount on toilet paper?

Being in a supermarket is one thing. Being an operator in the financial markets is an entirely different proposition, or at least it should be. You should not go into the financial markets with the same kind of mindset that you would when you enter the threshold of a supermarket. It's fine to look for bargains on household items but it is not necessarily fine to look for bargains in the financial markets.



It doesn’t matter where you are from. We are all governed by the same emotional laws of marketing. And if we don’t exert a conscious effort to release ourselves from the shackles of conventional thinking, we may very well end up as a bunch of City Index clients did back in 2006 - 2007.

Back then the stock called Northern Rock was one of the quieter companies in the FTSE complex. It basically went nowhere. However, suddenly in late 2006 it began a stellar movement higher. There was no real interest from the City Index client base in this meteoric rise of Northern Rock. No one participated in the upside. However, when it began to slide back down again afterwards, the interest rose. It was as if Northern Rock had the same effect on investors that half price toilet paper has on shoppers in a supermarket.

I worked at City Index at the time, and it was clear that Northern Rock had become quite a lively traded stock. The more Northern Rock fell in price, the more people got interested in the stock. At one point I received a phone call on a Saturday morning. At this point Northern Rock had slipped from 1200p down to around 500p. The person on the other end of the phone was a stranger to me. He had picked up my business card at one of the talks I had given on technical analysis. He apologised for calling me so early on a Saturday morning, but him and his friend had decided to invest in Northern Rock. At the same time, they had decided to get the opinion of a professional, just to double check if it was a good idea.

Apart from being rather annoyed at being woken up at 7 AM on a Saturday by a stranger, I was also annoyed with the question. At this point Northern Rock was in freefall. I roughly said the following to the stranger:

Look, I don't know what is going on with Northern Rock, but there is something horribly wrong. Although the general market is declining too, Northern Rock is declining much more. What I am afraid of here is that there is something amiss that we don't know about, and it has yet to be known to the market. It feels as if someone somewhere knows something is horribly wrong, and they are selling out while they can.

I told him that I had many clients who had been saying exactly what he was saying, but they said it about a share called Marconi. Fortunes were lost by clients who kept buying Marconi, even though it was falling and falling, because they engaged in bargain hunting. I was working for Financial Spreads at the time of the demise of Marconi.

It was horrible to see the fortunes being lost by our most valuable clients, simply because they did not want to admit they were on the wrong side of a bad share.

I said to him that from a trader's perspective, you are engaging in a very dangerous activity. If you buy Northern Rock now, it will be very difficult for you to have a meaningful stop loss. You are essentially trying to catch the falling knife. You talk as if Northern Rock is the only bank in the world worth investing in. You talk about Northern Rock as if it couldn't go bust. You talk about it as if the fact that it is 200 years old means that things couldn't get worse before it gets better. You even said it yourself: Northern Rock is too big to fail. It means you are already to some extent aware of the danger here.

There is a second reason why I don't think it's a good idea you buy Northern Rock. Let's say you are fortunate enough to witness a turnaround in the fortunes of Northern Rock. You will have trained your mind to think that it is perfectly okay to buy into things that are falling.

This works perfectly in a supermarket. Toilet paper has a practical use. Soap has a practical use, so when you are provided with an opportunity to purchase these items at a 50% discount, you should do it.

However, to believe that the financial markets offer discounts akin to what you're seeing in a supermarket is ludicrous. **The financial markets are not a supermarket with special offers.**

The Beauty Contest

John Maynard Keynes, the father of modern economics, expressed the essence of speculation with an analogy of a beauty contest. He referred to a beauty contest in a newspaper, where you were presented with 30 beautiful ladies. Your job was to rank these 30 ladies in terms of beauty. However, as John Maynard Keynes beautifully put it, this has nothing to do with whether you like blondes over brunettes, or you like tall ladies over small ladies. In fact, this has nothing to do with your own personal preference.

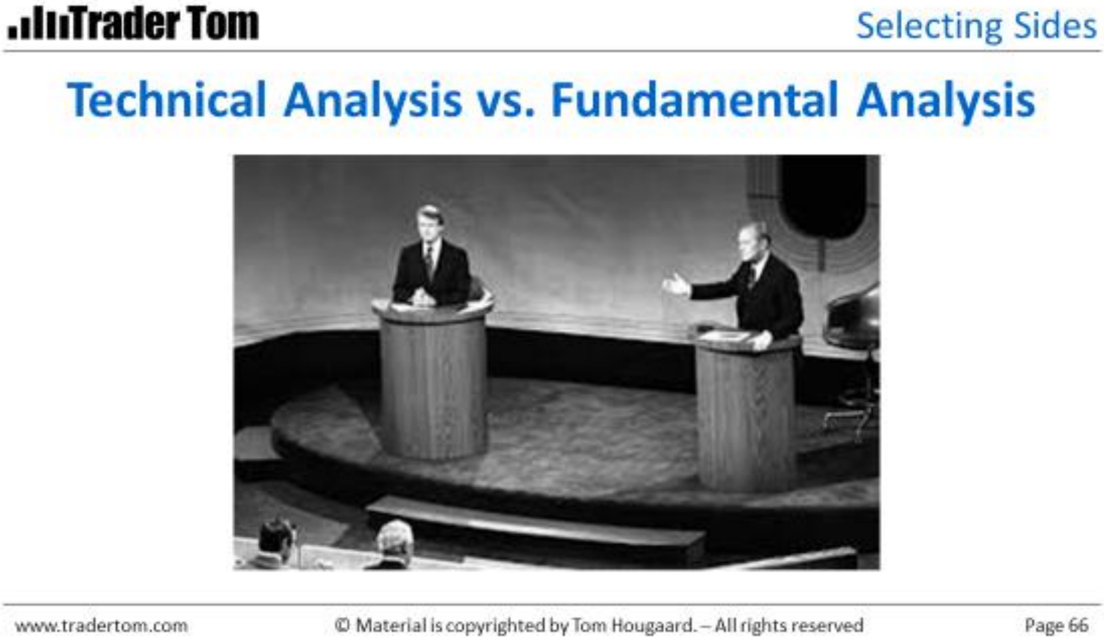
As a side note, I really wish that the first father of economics had been a woman. I wonder how we men would have reacted, if we had been one of 30 men in a picture, and ladies now had to rank us according to our masculinity or our muscles or the amount of hair on our heads. But times were different back then. So, I apologise to the women reading this. I am referring to an example from the past, but trust me when I say, I am somewhat uncomfortable with the example.

Mr Keynes said that his own personal preference was irrelevant. Rather he argued that his job was to consider what other people are considering. He basically stated that investing or trading is the art of figuring out what the other person is thinking. It was for this reason that I showed you the scene from Casino Royale, known as the poker scene. We're not necessarily just playing a game of investing. We are playing a game of trying to figure out what the person opposite us is thinking and what that person wants to do.

A Story About Technical Analysis

When I wrote the notes and the presentation for the two evenings, I knew I had to share the stage with another speaker. His name is Steen Jacobsen. He is brilliant at what he does, which is to approach the markets from a pragmatic and fundamental perspective. I admire him, and I knew that I would need to explain why I use charts, when I am actually equipped with no less than two university degrees in what could accurately be called fundamental analysis.

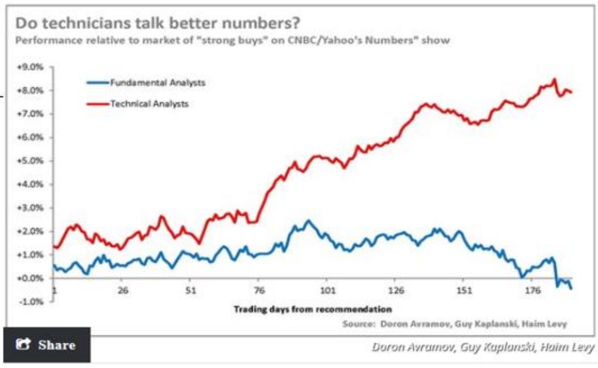
There are two major camps of analysis. There is the fundamental analysis camp, and there is the technical analysis camp. Fundamental analysts tend to pour scorn on technical analysts, while technical analysts tend to be rather disrespectful to people who have spent time and effort to learn the fundamentals of economics and stocks and sectors.



It is true that technical analysis is significantly easier to master than fundamental analysis. I spent four years of my life learning about the fundamentals of the financial markets, and I wasn't even trained in accounting. Conversely, you can pick up a book on technical analysis on a Saturday morning, and by Sunday night you will have a very good idea of what technical analysis is all about.

It is probably for this reason that most retail traders believe that the path to the financial markets and trading profits is through technical analysis. However, it is arguably down to personal preference which tool you use. Some have made fortunes using fundamental analysis and some have done the same using technical analysis. It is not often you get an opportunity to put the two sides off against each other. However, we are in luck.

CNBC runs a daily segment where a fundamental analyst and a technical analyst goes head to head, and they offer their opinion on where a stock or index or commodity is headed. Some researchers from a university, I think it was in India, decided to test which performed better. The result is shown on the next page.



Doron Avramov, Guy Kaplanski, Haim Levy

Consider first the stocks that the technical analysts identified as strong buys. They on average proceeded to outperform the overall stock market by 7.9% over the subsequent nine months, while the stocks they recommended as strong sells underperformed by 8.9%.

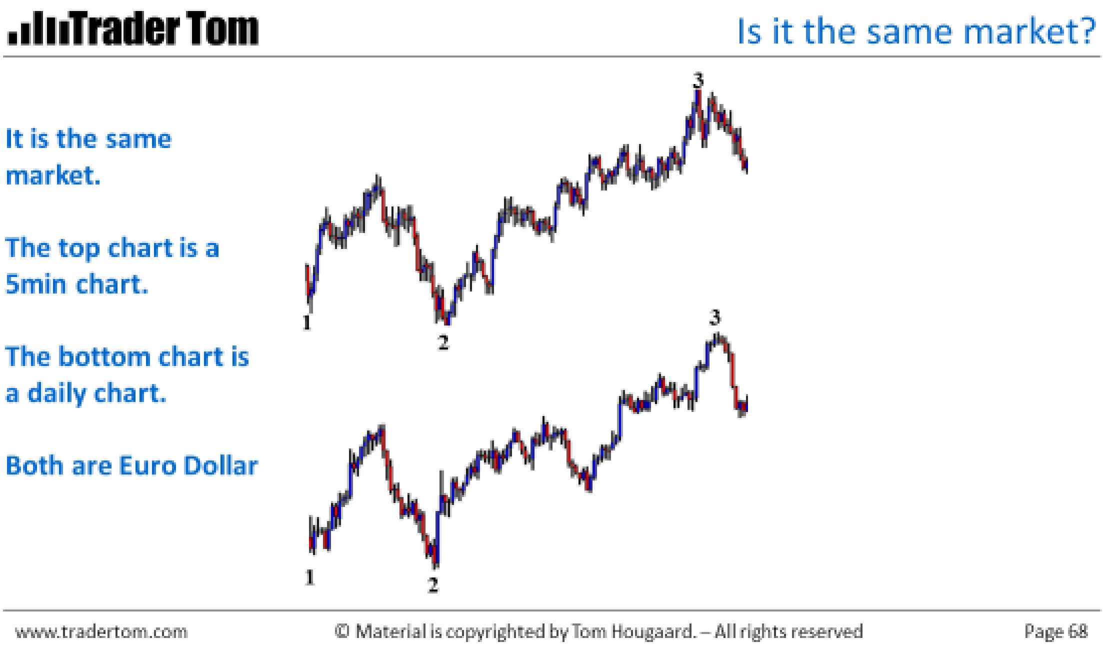
That spread of 16.8 percentage points is highly significant from a statistical point of view. As the professors put it in their study, it means that "technicians display rather impressive stock-picking skills."

Contrast that with the performance of the fundamental analysts. The researchers found that their strong buys proceeded on average to underperform the market over the nine months following recommendation — though not by enough to conclude at the 95% confidence level that these analysts were actually worse than random. Even worse, the stocks that these analysts rated as strong sells did not perform appreciably differently than those they considered strong buys.

It won't be easy for fundamental analysts to wriggle out from underneath the weight of these results. Since the TV show creates a head-to-head comparison on the same stocks over similar time horizons, the usual escape valves have been closed off.

The technical analysts in this survey have far superior returns than the fundamental analysts. I suppose you could argue that I am biased. I don't deny that. However, there is another reason why I prefer charts over fundamental analysis. It is not the only reason, but it is an important reason.

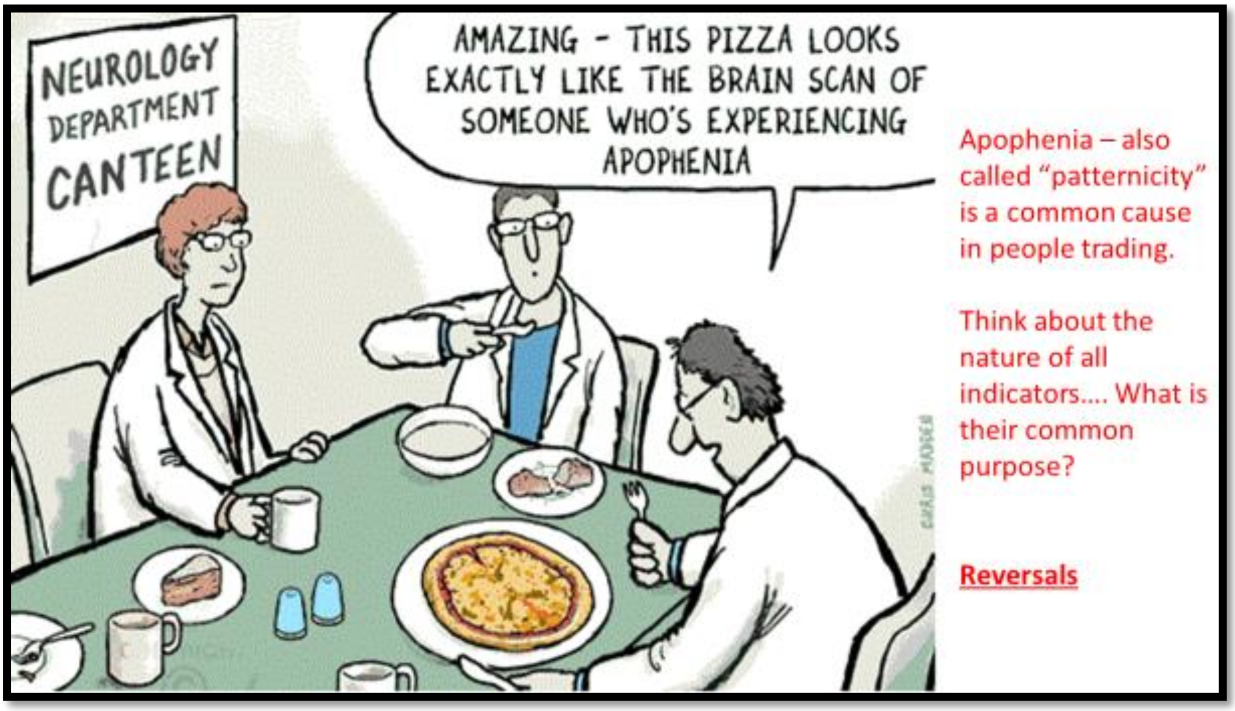
If I show you two charts side by side, and I tell you that one of these charts is a five-minute chart, and the other chart is daily chart, would you be able to tell which one is which?



What I find advantageous with chart analysis, is that it is applicable to the time frame that suits my temper. It is far superior in my mind to fundamental analysis, when it comes to entry points and exit points, and I can use the same tools, irrespectively of what time frame I am trading on. Am I opposed to fundamental macro analysis? I would be a fool if I dismissed the fundamentals. Believe it or not, the two should not be in opposing camps. They should walk hand in hand, as they complement each other and make up for each other's flaws.

Now, I would not go so far as to say that chart analysis is the Holy Grail. Yes, I have made a lot of money from becoming an expert in technical analysis, but I am also aware of the shortcomings in technical analysis. I don't believe that there is a Holy Grail when it comes to trading, and I certainly don't believe that chart analysis is the Holy Grail.

In Latin there is a word called **Apophenia**. Translating it into common English, it would be "patternicity". This behaviour is centred around seeing things that aren't there. Our minds tend to seek out the information that confirms the bias that we have already decided upon. Therefore, to be completely objective in chart analysis is virtually impossible.



My own mentor Bryce Gilmore once commented on this fact. He said to me: "Tom, you only see in the markets and on charts what you have trained your eyes to see."

I guess another perspective of such wisdom is expressed by Anais Nin. She said, "We don't see things as they are, we see them as we are." What is the relevance to trading, I hear you say? I had a friend a long time ago. Nick was a great trader, right up until 2004. Then he turned bearish the stock market. He kept shorting. The market kept going up. He just could not accept that there was no more downside after the bear market of 2000-2003. He didn't see the market as it was. He was it as he was. By the way, he is no longer trading.

Take a look at the image below. Now I don't mean to be rude. I am just trying to make a point. I am pretty sure I know what you thought you read.

There is even a very good chance that you got the second sentence wrong too. As I said, I didn't mean to cause any offence. I hope you can see the humour in this, while illustrating a very important point.

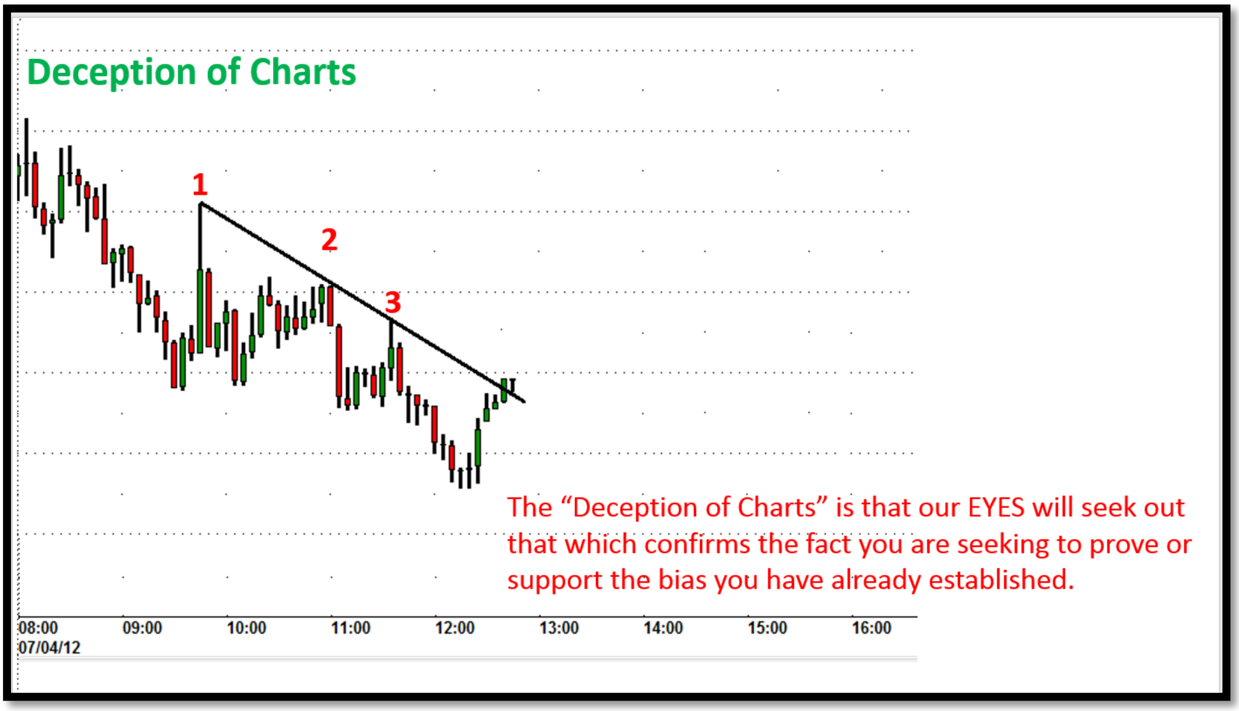
The editor of the book told me she nearly spat her coffee out from laughing. She admitted she also got the second line wrong. I hope I made my point. Again, apologies for the example. It was not to cause offence, but to make you think carefully.

The Curse of Patterns

I am going to enter the heavier part of this presentation. This chart is to illustrate the issue of patternicity in the context of chart analysis. In the early stages of our chart journey we come across trendlines. Trendlines are easy-to-use, and they give the appearance of a great trading strategy.

So, on this chart our chartist has skilfully drawn a line from point 3 and connected some lower tops on the chart. As the market breaks through the downward sloping trendline, it generates a BUY SIGNAL. If you are in a research position, and you draw enough of these trendlines after the fact, you're most likely going to conclude that trendlines are nothing short of a fantastic tool, perhaps the Holy Grail.

This is where I step in and say, be careful. Your eyes will tend to seek out that which you look to confirm. As we go to the next chart, you will now see a different perspective of the same chart and, as we progress to yet another chart, the next one in the series, you will see that actually there was a trendline before the one drawn, and this particular trendline was nowhere near successful as the trendline your eyes sought out, after the fact.



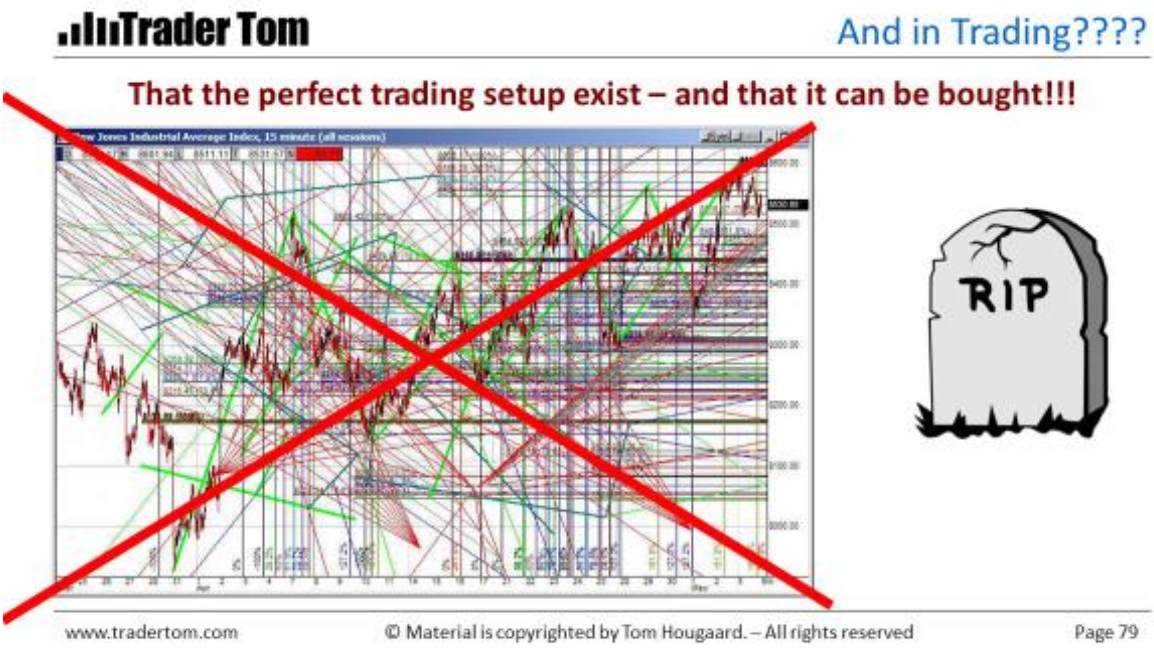
This is the danger of charts. When we research, we are looking for something to get us in on the long side, so we never miss a rally, or we look for something to make us sell short, so we never miss a short sell. We enter with a bias. This is Apophenia in play. Be aware!

Divorce Rates in Spain

I like to inject a little bit of humour when I can. Did you know that there is a 65% divorce rate in Spain and an 87% divorce rate in Luxembourg? There's only a 42% divorce rate in the UK. Does that mean that you have a higher chance of finding your soulmate on the British Isles than in the warm climate of Spain?

As I said, I only put these images into the book to provoke a feeling of "what is he going on about now????" Well, I admit that some believe the earth is flat, and some believe in soulmates and horoscopes. I don't. I consider such beliefs as ignorance.

And I sure as hell don't believe that the perfect trading system can be bought, yet alone produced.



My Style of Technical Analysis

I would like to show you what technical analysis can do for you. When you can act and perform without any form of fear of consequences and repercussions, you are trading from an ideal state. When you consider how many people lose money overall in trading, you logically have to conclude that achieving this state is not an easy undertaking. It would be foolish to think that this state of mind comes easily or even naturally. It doesn't.

In this part of the book I would like to show how to achieve this state of mind. It means building on the foundation of knowledge I outlined in the first part of the book. Bridging a theoretical concept with a practical application will take time. The great thing about this framework is that IF you can bring one thing with you, I can almost guarantee you what you want, which is trading profits.

What do you have to bring to the table? Well, I said one thing, but it is a little more than one thing, but there is one thing that towers over all the others: **patience**.

You have to be patient with yourself. You have to be able to let your knowledge settle and mature within you. If you trade small size now, but you want to trade bigger size in the future, then that journey will most likely be anything but linear. It will be a journey of progress and setbacks. It will be a journey of progress and status quo. I can guarantee you that. You have to grow into the trader you dream of becoming.

You must be patient with your trade entries. You have to be patient with yourself. If you can bring those two qualities to the table, then the rest will solve itself in time. You will grow your trade size at a pace where your mind will not be alarmed or be fearful. Let's get started with some technical analysis.

Time to Buy or Sell?

Here is a chart of the FTSE 100 (next page). After a hesitant open at 8am (the first bar after the gap in the middle of the chart is the 8am bar), the FTSE makes a move higher, makes a small retracement, and then pushes further higher. It then moves into a consolidation phase, where we see two lower highs.

The question is very simple:

Are you a buyer? - because we are in a trading range?

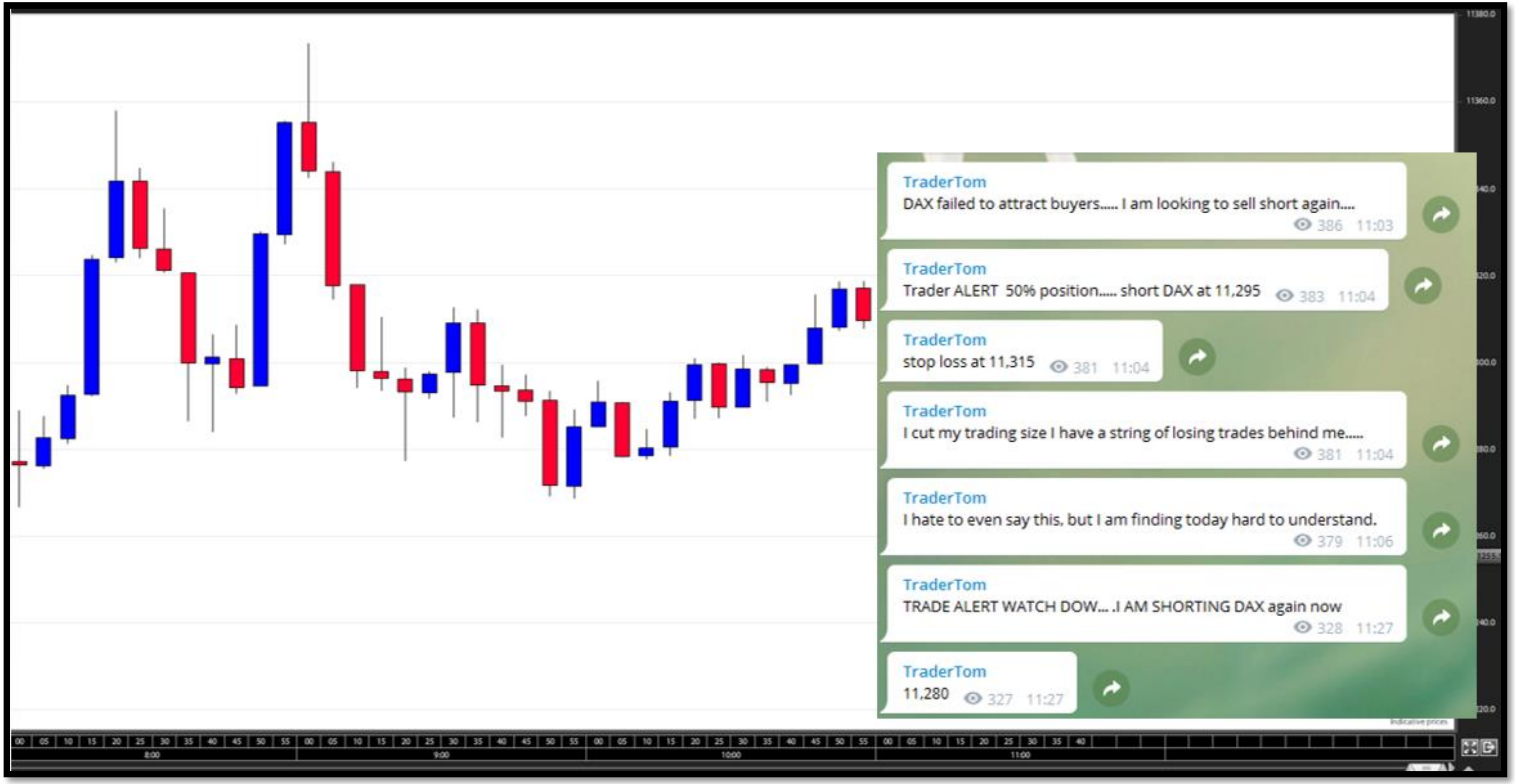
Are you a seller? - because it seems as if we are breaking below support?

What is your answer please?

The FTSE 100 index has a slow start to the day, which starts at 8am, at about the middle of the page, where there is a gap in the chart. Eventually the index rallies. However, by mid-morning the index has made a top and two lower tops. It is not overly bearish, but it is not overly bullish either. If you were confronted with such a chart, would you buy it, because it is the bottom of the trading range, or would you sell short because you have a series of lower highs and what looks like a break of the trading range? What do you think?

Same Pattern – Different Index

This is the German Dax index. It shows a similar pattern to the FTSE. It has also made a high, and then retraced into a trading range. It appears as if DAX is now in a trading range? Would you buy, in anticipation of a test of the highs? Or short, on account of the trading range?



Please ignore the comments in the box for the time being. I will explain them later. They merely show what I did in Telegram. Now I would like to ask you a straightforward question:

Are you a buyer?

Are you a seller?

What is your answer please?

Side by Side

Below we see both charts side-by-side. The DAX index is on the left side, while the FTSE index is on the right side. They appear relatively uniform in pattern: Both have a series of higher highs initially, and then both move into some form of consolidation range.

Have you decided what you want to do?

Back to the FTSE Index

We are back at the FTSE 100 index chart. Have you made up your mind whether you want to be a buyer or seller?

On the next chart we see that the FTSE meets buyers at the double bottom. Although it is not conclusive that we are headed higher from here, the bulls have certainly won the first test.

When you are confronted with the FTSE on this chart below, what would you like to do? Are you a seller or are you a buyer? At this point it seems as if the trading range is holding. As a trader who likes to run positions on “trend days”, it can be a frustrating experience to trade a sideways market. You think every little push below an old low or above an old high is the beginning of a new trend. Then the market turns around and goes back into the trading range. Considering that trading ranges is part and parcel of trading, there is no point in getting annoyed. Maintaining your mental composure at all time is essential. I find that it helps me tremendously to “warm up” before I start trading. It is an essential part of my preparation every day, and I attribute this component as the key to my trading success. I will explain later how I do that.

On the chart below, there are sellers at the double top within the trading range. So, although you have a series of lower highs and lower lows after an initial surge up, the market is not about to roll over. At least there is no evidence at this moment in time that it is about to roll over.

The reason why I am showing you these charts – perhaps a little tedious to go through bar by bar - is because I want you to appreciate the nature of trading. You see the FTSE 100 index roll over into a trading range, where there is little money to be made, except if you decide to trade the range. In this case trading the ranges means trading for 5 – 7 points, which might not be everyone's cup of tea. Unless you like scalping, there are not many points to be made here.

Yes, you will have no way of knowing this in advance so you need to approach trading from the viewpoint that literally anything can happen, and you need to appreciate that two near identical patterns can yield very different outcomes.

On the FTSE chart you would perhaps have been a seller right here – a bar or two earlier perhaps, in anticipation of the FTSE trading down to the low end of the range. Your stop loss would have been above the most recent high, or perhaps your stop loss would have been above the highest high for the day.

Either way, the FTSE is not showing signs that a big trend day is looming. Just remember that anything can happen.

When I look at the FTSE chart we have just seen, I am thinking "sell short". I have an early morning top, and I have a trading range within the context of a lower high.

Selling Short the Dax Index

We are back at the German Dax index chart, which is shown on the next page. Have you made up your mind whether you want to be a buyer or seller? One thing that you could decide to focus on – on these apparently near identical setups – is the fact that the Dax index seems to trade somewhat lower from the morning, compared to the FTSE index. The FTSE index is quite close to the morning high, while the DAX is comparatively weaker, as measured by how close the two indices are to the morning high. Even though the patterns are quite similar, the DAX seems weaker.

If you look at the comments within the chart of slide 86, you will see that I am looking to sell short the Dax index. You will also see that I am trading a smaller size because I have a string of trading losses behind me. I cut my trading size down to reflect that I might not be as "hot" as I could have wanted to be.

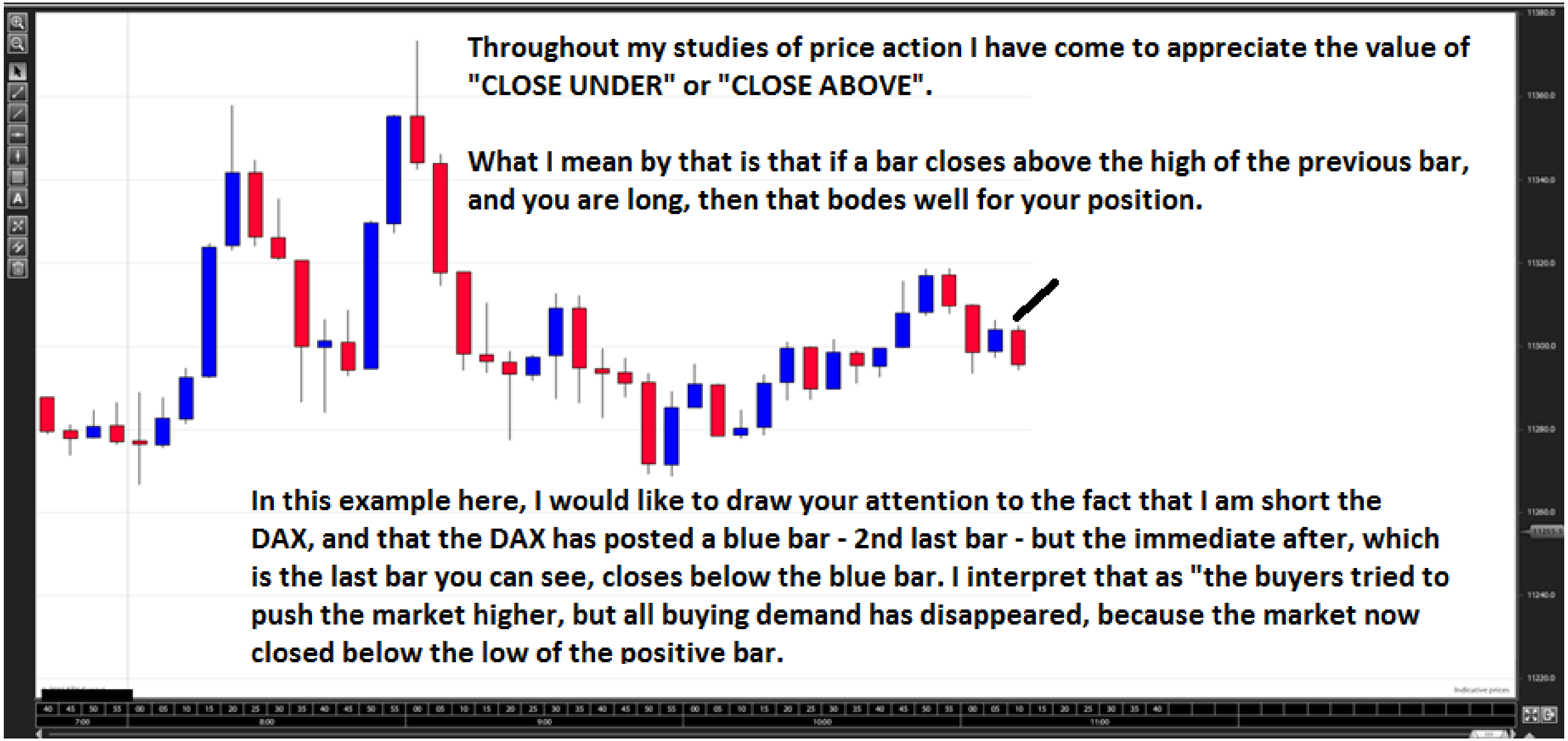
At 11:27am I issue a sell alert in the DAX.

I see a double top in the morning, and I see a subsequent trading range. I start my shorting the moment I see a red candle after a double top within the trading range. I think waiting for weakness before shorting is a great way to trade. It was something Bryce Gilmore once taught me. I think he used that strategy for a little extra confirmation before he entered a trade. He was a very good trader. I often traded live with him. He would tell me what he was doing live over the internet. It was quite an experience to hear him swear at the market to move ☺.

I have inserted some comments from the time of the trade. You can see that I make a comment on the fact that the moment the DAX is about to break through a critical area to the upside, it fails. The buyers have run out of energy. To me it looks as if the Dax is at a critical point. Within the context of the trading range, Dax appears as if it wants to move lower. The situation we are witnessing on this chart is near identical to what we witnessed on the FTSE chart. We have higher highs, followed by lower highs within a trading range. We can also see that ever since we hit the double top within the trading range, the German index has traded lower. The last two bars were red, followed by one blue bar,

which was unable to get above the high of the previous bar. It might seem irrelevant to you, but to me it is important. It tells me there is weakness in the market.

While you have very identical situations on the two indices, the outcome is very different. One index is trading within the confines of a trading range, while the other index is breaking down. My reasoning for showing you these two charts, as similar as they are, is to provoke a feeling of doubt in your approach to trading. Why on earth would I want to plant a seed of doubt in your mind?



Please don't misunderstand me, I'm not trying to plant seeds of doubt in your ability to make money. That is not my intention. However, my intention is to instil a sense of objectivity in your approach to trading. Now I won't go as far as to say you shouldn't care about the outcome. You are welcome to feel a flicker of joy when you are trading well, but don't overdo it. You are also allowed to be a little annoyed if you know you made a mistake, but again, don't overdo it.

Two stories spring to mind here, and one of them will contradict what I just said. I will start with that one. Brett Steenbarger once wrote about two traders he was coaching. One was perhaps a little bit like me. Stoic and calm*. The other, however, was a volcano of emotion. He would scream and shout at the screen, irrespectively of whether the trade went his way or not. Brett however could not discern any noticeable difference in their performance. So maybe a little emotion is not a bad thing.

* I am not always calm! I get royally upset when I am in a good position and some presidential jerk somewhere sends out a Tweet that lands me firmly on the wrong side of the market. Trust me, I am anything but calm in those situations.

The other story is about a French trader I read about, who traded for a hedge fund in London. He was described as an outstanding trader. One client described him as "humble and arrogant in equal measures – the perfect trader". The interview went on to describe that the trader had an absolute conviction on his trades, to the point of being arrogant, BUT he was equally quick to be humble when the trades didn't work out well.

So actually, maybe I should tell you to just be you. You should strive for that fine balance between confidence and humbleness. You need to be confident your trade will work out, but humble enough to admit when it does not.

Remember this saying: it is not what you know that kills you. It is what you think you know, but which just isn't so, that kills you. You are perfectly entitled to think you know where the market is headed, as long as you have the ability to admit you are wrong before the position kills you. Below is the outcome of the DAX trade. It went well.

The DAX and the FTSE situation is a case of the “same set-up – but different outcomes”. Use this example the next time you are annoyed a trade didn’t work out. It is just a case of “it didn’t work out this time.”

Hedge Fund with 25% Hit Rate

Before we continue with the chart and their associated comments, I would like to tell you a story about one of my friends. His name is Trevor. He is a professional hedge fund trader. He ran a small hedge fund with one of his friends. They had about £60 million under administration. You may remember him from the comments on page 31 in this document.

The reason why I want to tell you this story is because, as of right now, there is a very good chance that you have little or no idea about how professional traders trade and think. I hope the story will be illuminating, and I hope the story will give you a good perspective into how a professional trader thinks. It should also serve as a reminder that there are many ways to make money in the market. Your job is not to follow someone, but to find a way that you like, that resonates with you and who you are and what you like to do.

The story starts with me asking Trevor a question. I knew that he had been associated with Tom DeMark and his Sequential indicator. Tom DeMark is somewhat of a legend within the technical analysis world. I happen to have met him myself at a Bloomberg lunch many years ago. He seemed like a nice guy, although I had very little to ask him, as I was unfamiliar with his work. You see, his work was only available to those who had a Bloomberg terminal. The Bloomberg terminal at that time was some $25,000 a year. Today though Tom DeMark’s work is available on many trading platforms, in case you are interested.

As I asked Trevor about the sequential indicator, his eyes lit up. He told me a story about how him and his friend had decided that there was an edge to be gained from trading the sequential indicator on a very short-term timeframe in South African shares.

They moved to South Africa and started trading South African shares on a **one-minute chart**. I have never heard of a professional outfit, with significant funds under management, trade on such a short timeframe. However, that is not what impressed me most about the story. What impressed me the most was how they managed to make money on what other traders would consider an abysmal hit rate.

Most people believe that you have to deploy a trading strategy that has a hit rate which is at least better than 50%. Trevor told me that their results varied. There were times when they were hot, and there were times when they were not. When they were hot, the hit rate would push the 40%. When they were not, the hit rate was down in the mid-20s.

Overall though, Trevor told me, they had in their hands a tool that generated about 25-30 winning trades out of every hundred trades placed. They were wildly successful. They traded the fund for a handful of years, and then they returned the capital to the investors. They had made their money, and as neither of them were spring chickens, they decided enough was enough. It was time to go home and spend quality time with their families. Had they been younger, they probably would have continued.

Now I don't know about you, but I like the story. It reaffirms the idea that I have about trading. It is much more important how you think when you trade, than whether your trading strategy has a hit rate in the 50s or in the 70s or in the 90s. While the story is not conclusive evidence that anyone can make money trading, as long as they have the proper money management rules and the required patience, it is a brilliant anecdote of two traders being able to make money, even though their strategy on paper from a conventional point of view should not have generated a profit.

So, what was the secret? Well the answer is simple. Although they lost 75 trades out of a 100 trades, those 25 trades more than surpassed in profits what the 75 trades generated in losses. Trevor told me that they expected to make 25 times in profit what the risk was. He also told me that when they executed a trade, they expected it to work immediately. So, I grilled him a little bit on that point.

"What do you mean you expected it to work immediately?", I said. He said that when they executed a trade, they expected the trade to begin to work immediately. If they had bought at say 50, they would not want it to go to 48. If it went to 48, they would stop themselves out.

It meant they had plenty of small losses. Their back-testing had shown that if the strategy was to be traded correctly, it meant that it would work immediately. If it didn't work immediately, the strategy called for the position to be closed.

Over the next few pages you will find slide 91 to 96. It will show you the whole story of the FTSE 100 index trades. It will also show you the comments I have made, from the feedback I received from teaching this to students and delegates at talks.

I make a comment on the chart that I think is worth repeating here. The market doesn't reverse nearly as often as I am betting it will reverse. I think we as traders often see reversals that simply are not there. When you think about all the tools that are available to us, such as Fibonacci and Stochastics, their purpose is to highlight the potential for a reversal. I am very careful how I use these tools.

What I see here is an index at the top of the trading range. I know the day is bullish, but I am still inclined to sell short, on account of being a trading range. The market has traded sideways for 35 bars. Why should I bet it is about to change its tune now?

Short or Long?

But it did change its tune, and I was handed a loss again. If you saw this differently, I say WELL DONE. I was short and caught. There is truth to the expression that you should “get to know the product you are trading.” FTSE can be a strange fish to trade. And I am short again. ☺

The chart below is the same index, but I have had to use a different chart package, so this is the reason it looks different from the chart on the previous page. The circle on the chart below corresponds to the circle on the chart on the previous page. I have shorted the index again. I saw failure at the double top. My stop loss is just above the most recent top. I am yet again being made to sweat a position. Welcome to trading!

The Big Picture Once More

Finally, I am getting some traction on a trade. A good runner can really make a trading day, especially if you add to your position.

The Nature of the Game

Let's sum this up….

This game never changes, and it never will. Algorithms won't change the game. Laws won't change the game. Because this is an inner game, and you need to spend time – maybe not as much time as you do on charts – but a huge amount of time contemplating what human qualities you are bringing to the game of trading.

Trader Tom — Moving In the Right Direction

The Nature of the Game – not helping you

1. The players change – the brokers change – but the game never changes – because **you** are the game.
2. History clearly shows that the game of trading has never changed (e.g. 15k Merrill Lynch commodity clients data 4x losses vs. gains – empirical research – Larry Livingstone).
3. The very thing supposed to help you is what is keeping you trapped.
4. Charts are not a solution – they are an ingredient – but one ingredient does not make a dish.
5. The solution is not more charts – more indicators – because that is what everyone else is doing ….and…..they are mostly wrong!!!!
6. Everyone else is losing – thank you ESMA for pointing this out to us.
7. Remember – The "reptile mind" is there to protect you from pain – so introduce pain slowly..

Don't for one second think you can never be a big trader. Big traders started somewhere. AND big accounts do not have an advantage over you. Take nothing for granted – respect the market – and keep pushing yourself into the uncomfortable zone. That is where you will learn most about yourself. It may feel like you are failing, but you are not. You are growing.

I always thought that people who traded with the big names, like Goldman Sachs, were great traders. Then an insider told me that is just plain rubbish. Just because they trade with a big name does not mean they are winners. Goldman Sachs have many clients who bust their accounts every year. I personally knew of one guy who lost £5,000,000 with them.

Remember that the very thing the public think will help you, is the thing that will stop you from being successful, because they think it is all about system and method. It isn't. It is all about your inner dialogue. Charts are simply not the solution. They are an ingredient.

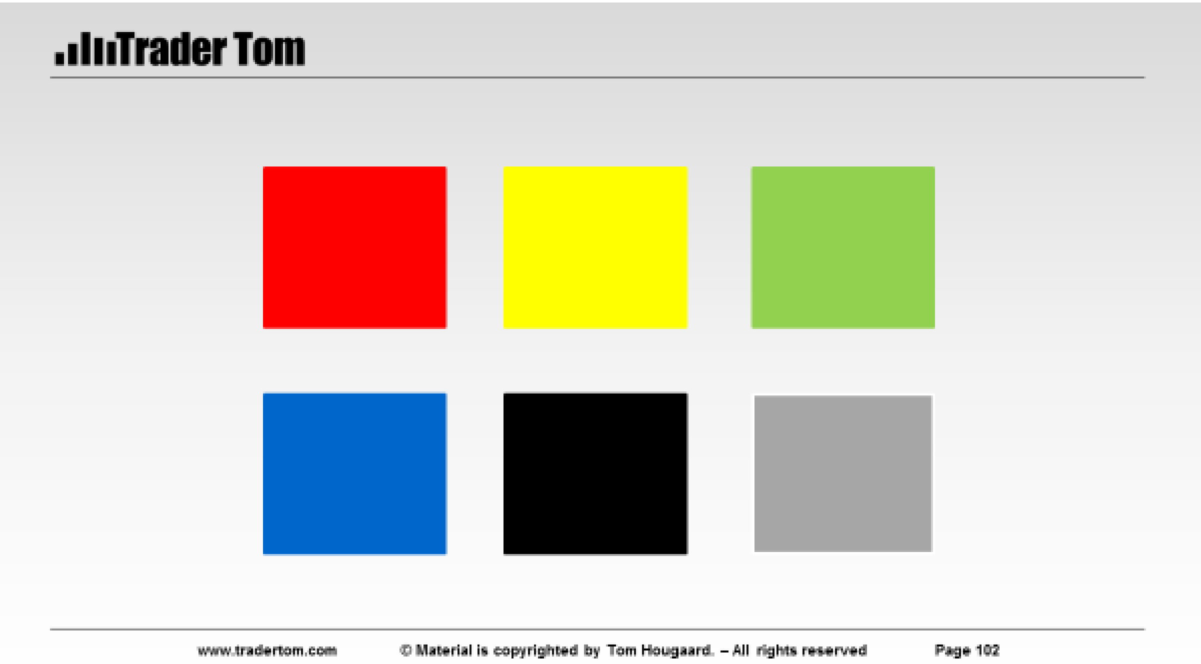
You can do this – but this is just like a diet. If your goal is to change in days, you will fail. MOST people completely overestimate how much they can achieve in a year and are oblivious to the immense change they can create in themselves and others in 5 years. The irony is that the 5 years will come and go, whether you do anything or not. You will either work time, or time will work you. Don't for one second think that this is purely a game of learning techniques and strategies.

Let me give you a taster of what you are in for. It might make you appreciate that your mind needs working on, to shape it into a mean lean trading machine. Here comes a little mind game to help you appreciate the power of our involuntary response system.

A Mind Game

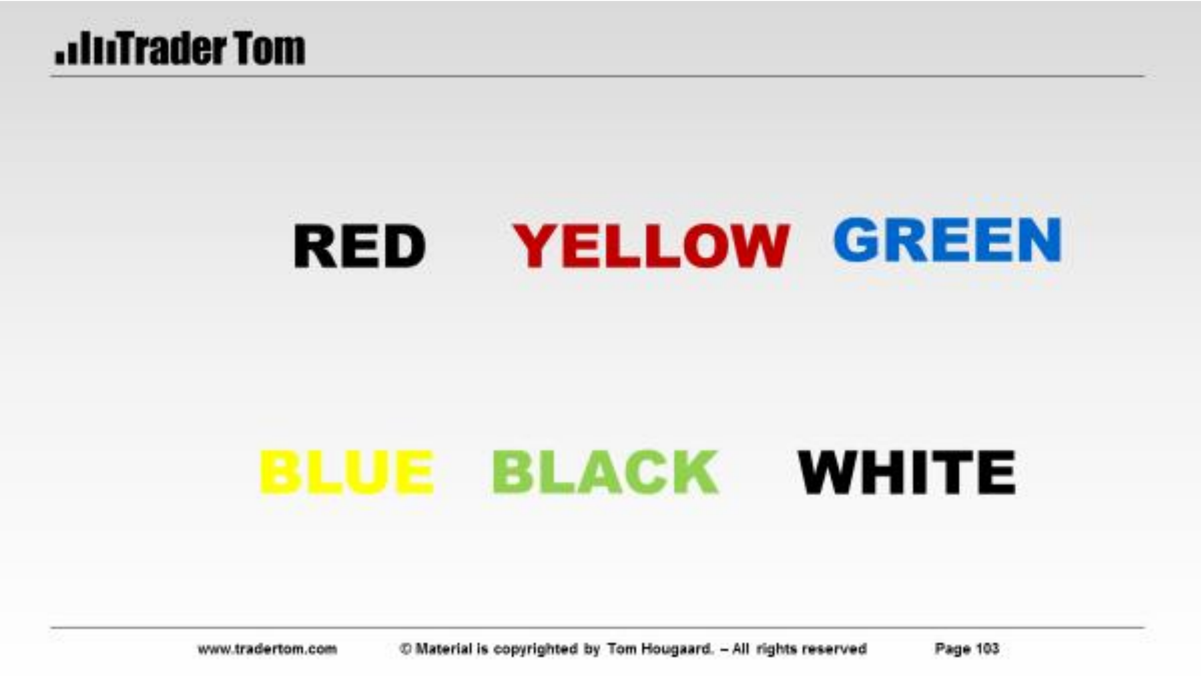
The next two slides have been adopted to the book. I am not sure it will work in a book format, but I decided to print it anyway. It is a mind-flexibility exercise. People who take it a few times report that it gets easier. I have shown you the slides, in English, and the purpose of the exercise is to go through the colours one by one. You will then notice how dominant your automatic response system is, even when you know that you are saying the wrong thing.

The object of the exercise is to name the colour of the shape. When you then come to naming the colour of the text, our minds will struggle to say "black", because the word "red" is written in black.



Now I am sure you found that pretty easy. Turn the page and as quickly as you can, say out loud the colour of the text. I said **the colour of the text.**

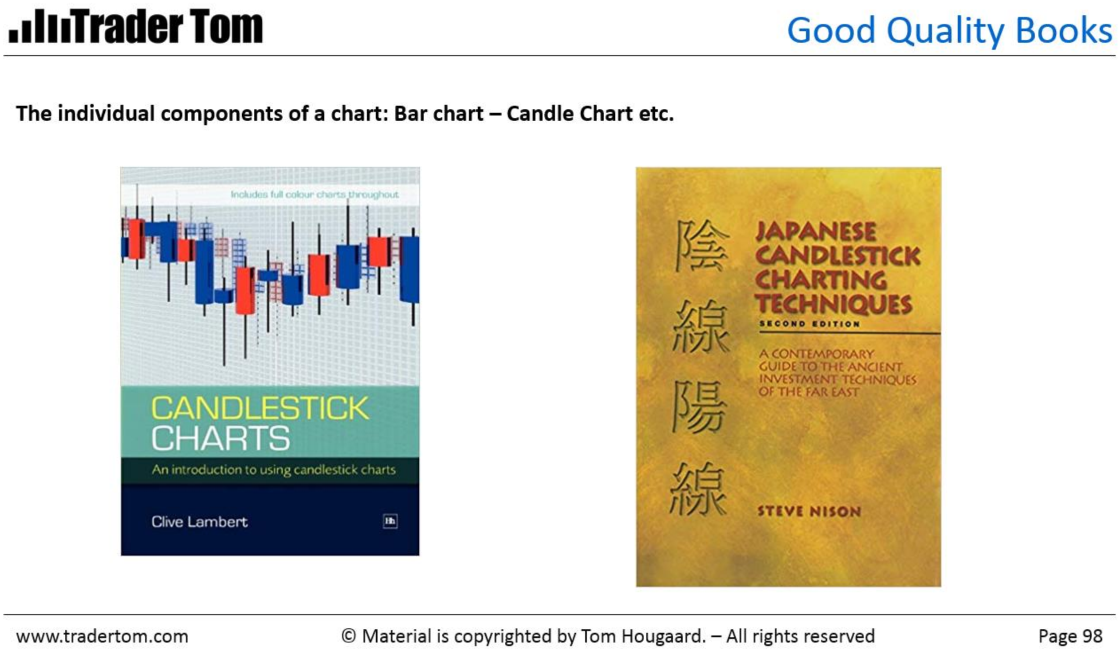
I did not say the words themselves. ☺ ☺ ☺



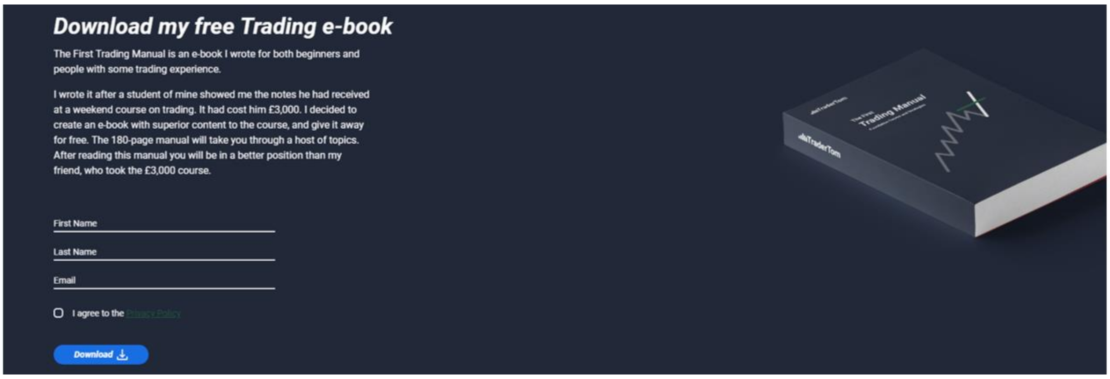
Recommended Trading Books

Below are some book recommendations. As I write this, I have some spare copies lying around of the Candlestick chart book by Clive Lambert. You are welcome to contact me and ask if I have got any left. If you pay postage, I will send it to you for free.

The book by Clive Lambert is every bit as good as the book by Steve Nison, but Steve's book is the first real work on Candlecharts, so I posted it here for nostalgic reasons. It is pricey.



I have written a book on trading and technical analysis, which is free to download from my website https://tradertom.com/ebook/.

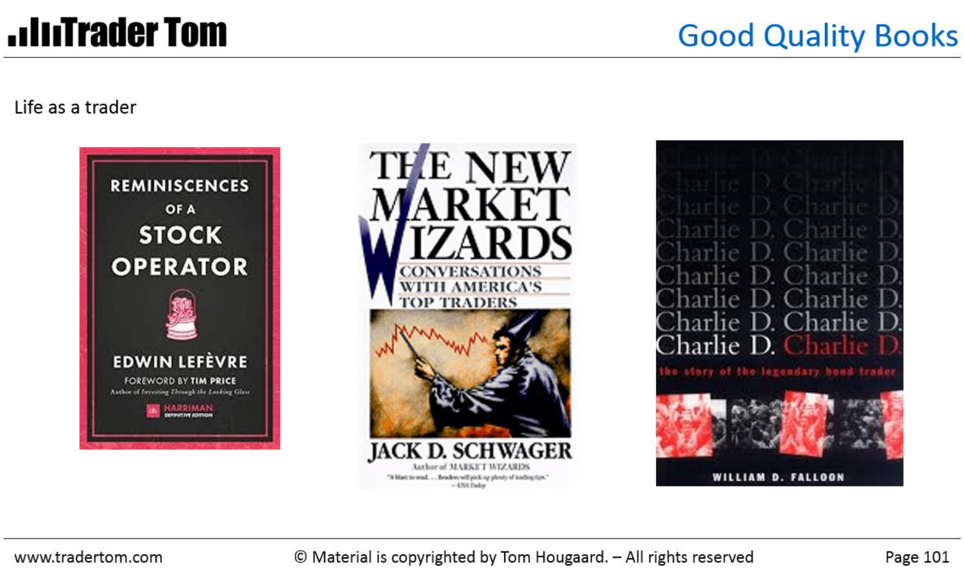


I must add a comment to the books below. I get far more out of reading anecdotes about traders and their behaviour and their trades, than I get out of studying a manual on technical analysis.

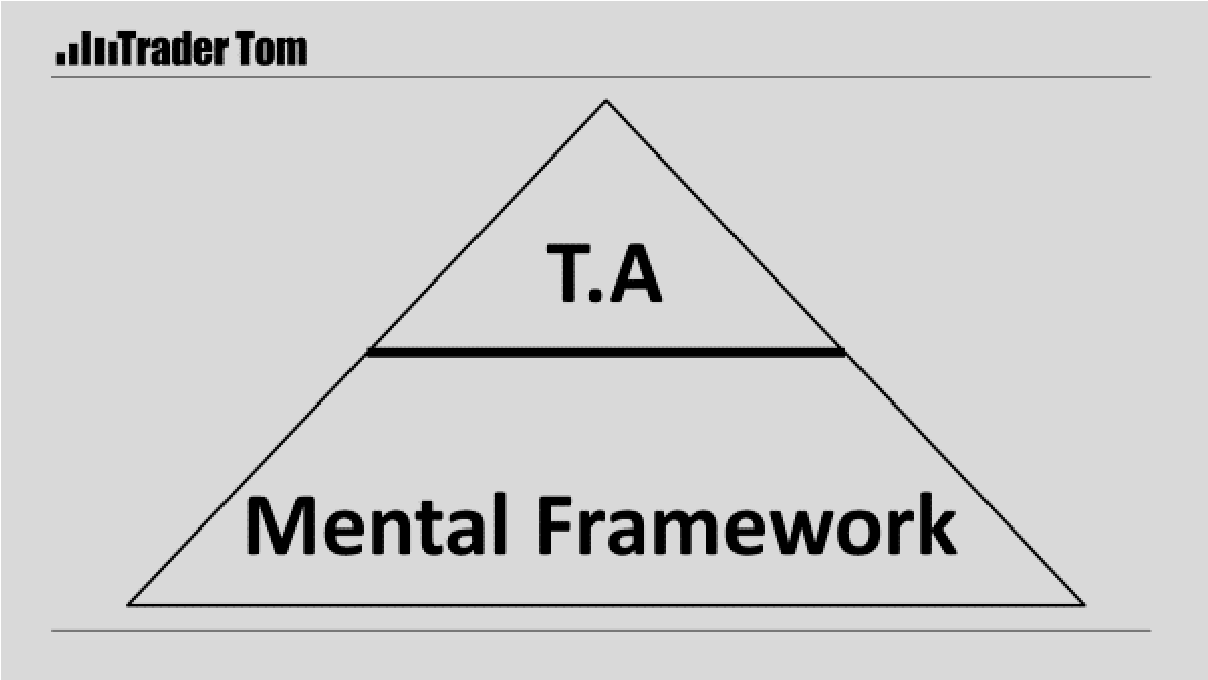
If you are anything like me then these three books will be enjoyable to you. However, I am not doing you any favours, if I don't give a special mention to one of these books.

The book about Charlie D is my favourite trading book. It is essentially a story about a guy who arrives at the Chicago Board of Trade, hoping to make a living from trading. Charlie D turned out to be a legend, and the author, William Fallon, who never actually met Charlie, does a great job in describing what Charlie D was like. He interviews his colleagues, his family, his friends, and his co-workers, who do a good job at painting a very interesting picture about the man who dominated one of the trading pits in Chicago.

I think this book is an absolute essential read for anyone who is interested in trading. It describes a man's journey, a man who wasn't successful to begin with, but who somehow overcame the odds to become one of the best.



My Experience with Students



It has taken me nearly two decades to understand why "how you think" is much more important than "how you trade" or "the tools you use". You may wonder why I didn't discover this earlier. The answer is that I didn't realise it until I started providing training for people. I would not say that my own career had been a "barn-stormer" either. I suspect I made all the same mistakes that everyone else is doing – more or less.

I don't think I am especially gifted, but I don't give up very easily. Sure, I gave up on learning to windsurf, but maybe I was never really into it anyway. I am into trading in a rather big way, and I have persisted, and I am persisting now.

There must surely be a couple of questions on your mind now.

1/ Why is he saying that he only learned the role of psychology when he started training people?

2/ Why is he saying he is "still persisting now"?

The answer to question 1 is as follows: I taught some 200 people on my 1-day seminar over a 4-year period. They were all taught the same, and they all had the same material at their disposal. They were all subjected to the same intensive training and the same follow-up web-seminars.

Out of the 200 people I have regular contact with some 50 of them. The last 150 have disappeared off the grid. I don't know if they are trading anymore, but I suspect they might not be trading. Did they give up? Was it not as easy as they had imagined? I will never know, unless I contact them.

The 50 people I have contact with is proof that it is possible to make the financial markets your playground on a full time or part-time/hobby basis. They engage with the music of the markets on a regular basis. They have persisted, and although their results are varying according to their commitment and their account size, they are still here.

This group of 50 people have proven to me that it is not enough to simply engage in the markets from a “technique” point of view. You must understand your own role. Are you trading from an opportunistic point of view, or are you trading from a point of view of fear or anxiety?

The group of 50 have proven to me that you can have the best understanding of a technique, but if you don’t have a fool proof mental stability, one that will ensure you don’t get knocked sideways when the market throws you a curve-ball, then you will without a doubt end up like the 90%.

It is really true when Richard Dennis said in the interview with Jack Schwager, in the book Market Wizards, that “we could print our trading rules on the front page of the Wall Street Journal, and people would still not be able to make money from our techniques.”

I have met some very smart people along the way, people who prided themselves with having a high IQ and being Mensa members. They failed. They were unable to make a success of it.

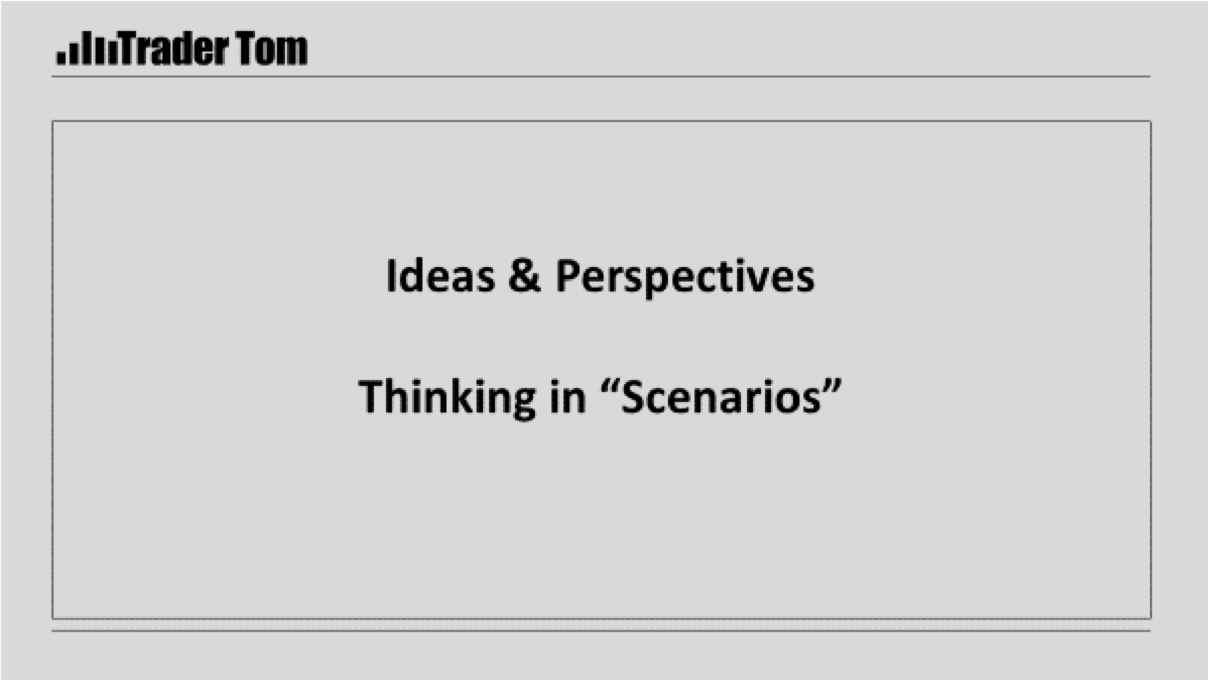
Why do you think that is? Could it be that their intelligence got in their way? Could it be that all their life they have grasped and understood matters quicker and easier than normal people, and now they were faced with a problem which required them to look inwards? The market is not an equation to be solved. It is not a conundrum that can be mused over during a casual conversation with a friend. It takes a lot of introspection to understand why your best intentions is not enough. To succeed you have to accept that how you normally handle “pain” and “discomfort” will not suffice.

This leads me perfectly into question number 2: Why am I saying that I am “still persisting now”?

There is a really easy way to answer that. A way that will make you understand it instantly, in the form of an analogy: When you lose weight, and you have done so successfully, can you go back to eating the way you did before?

Of course, you can’t. You would fail and you would put on the lost weight again. Trading discipline is not a one-off course or a one-off newsletter, or a one-off book, or a one-off session with your local therapist. It is a life-long devotion to your profession. If you do that, you will be rewarded with riches. If you don’t, you will “put on the kilos again”. Discipline is a muscle, and it needs to be nurtured constantly, like physical muscles. Otherwise, you will develop mental atrophy.

Scenario Strategies



Have you ever come across the expression of "thinking in scenarios"? Instead of thinking in terms of patterns or ratios or "overbought "and "oversold", you are thinking in terms of "cycle behaviour".

It is people who drive a market up or down. They do so for a million different reasons and time perspectives. Well, people are rather predictable in their behaviour. Don't be offended. I am too. We all are. However, if you are the observer of your habits, you are like the captain of a ship. You can direct at your will your behaviour. If you are not, then you are drifting through life.

People in the financial markets are hard workers and they work hard to keep their place in the markets. Of course, there is a natural attrition rate in the trading industry, but remember, your job is not to worry about the others, but to figure out what they are thinking and act upon it.

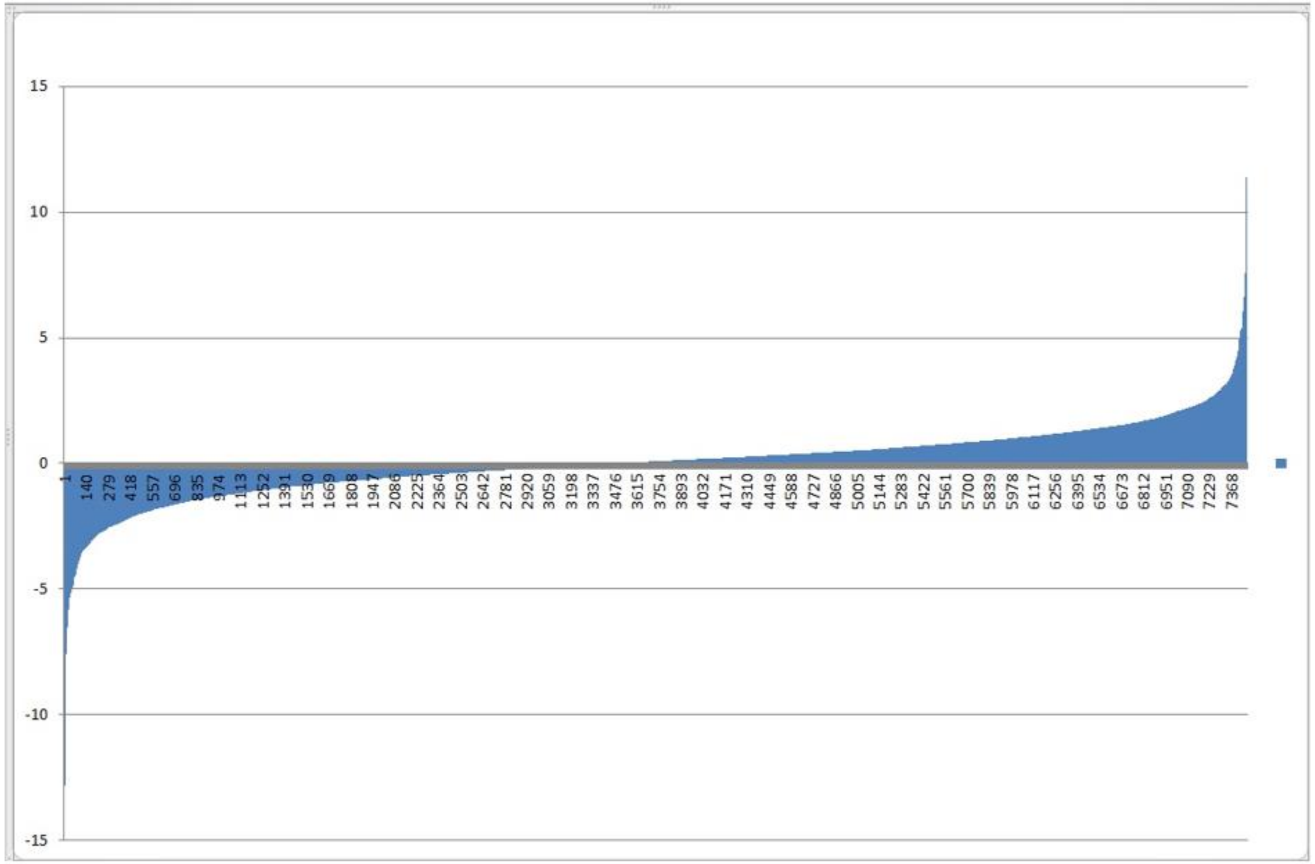
Very few people know that although the markets move through phases of expansion and phases of contraction (bull markets and bear markets), the ratio of winning and losing days for stock indices is 50/50. This is the Dow Jones Index closing prices – illustrated on a chart – over the last 30 years.

You can see the distribution of winning and losing days is identical. What are the implications of this chart? The Dow Index may have the best day or the worst day ever, but the day after, anything can happen. It would be wrong to assume that the market will continue what it did, statistically speaking.

It reminds me of 24th December 2018. The Dow fell 500 points, while the world was celebrating the festive season. On the 26th December, when the Dow opened again, after the holiday, the index had its best point day ever, rallying 1100 points.

Trader Tom

Statistics of 7500 trading days



Hypothetical Questions

Trader Tom I ask myself questions

1. How often does the Dow "gap up" or "gap down" in a year?
2. Is there any truth to the "As Wednesday goes, so too goes Friday"?
3. Is there a rhythm to the markets – 5 days on, 2 days off?
4. How often is Monday the low and Friday the high?
5. Does it help to know Fibonacci as a day-trader in Dow?
6. Is there any merit to the "strong Friday, strong Monday"?
7. How many days a year are "trend days"?
8. Is there any merit to "what Monday starts, Wednesday continues"?
9. Is there any truth to the 32 Calendar day cycle?

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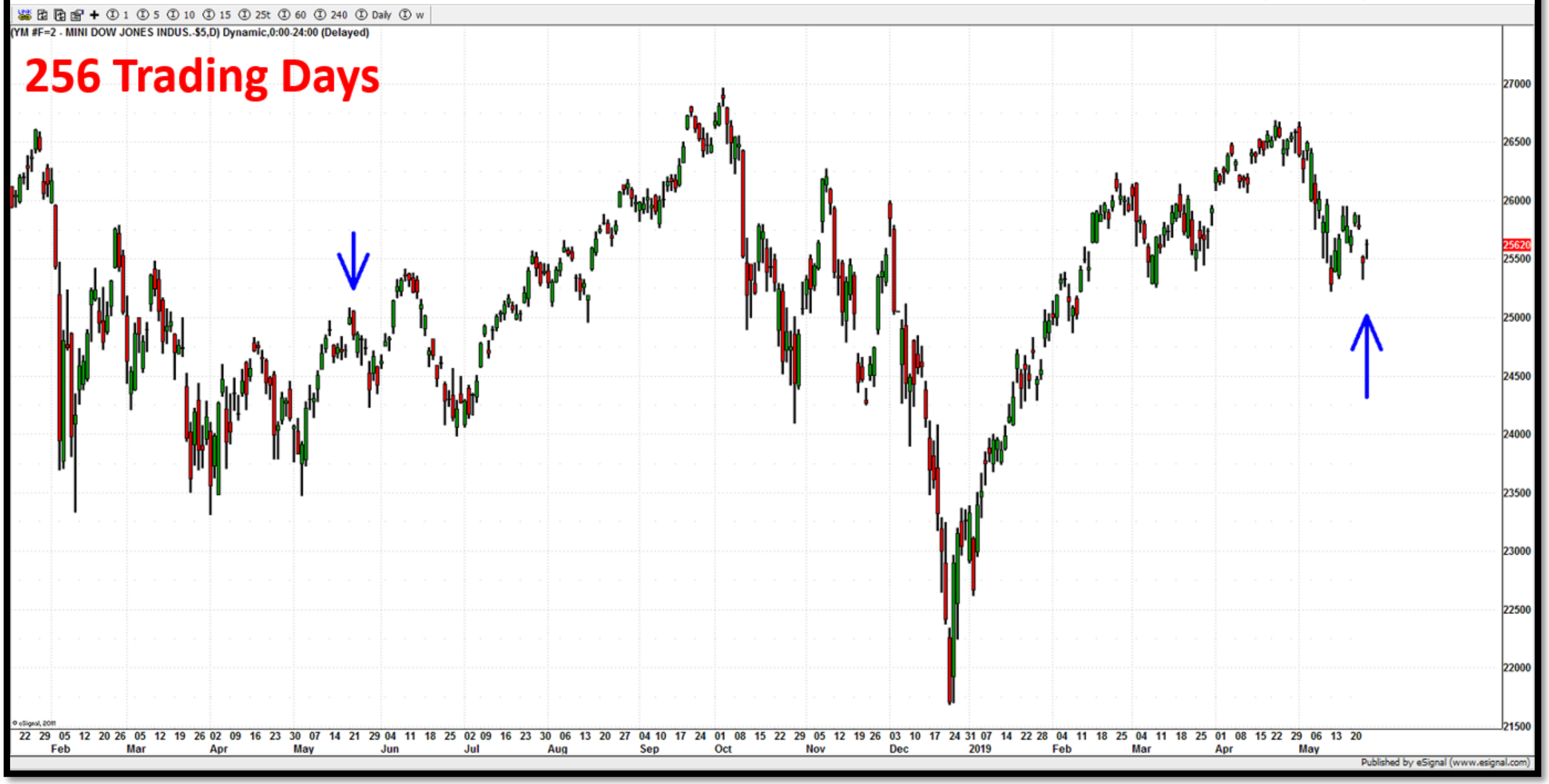
Testing a hypothesis in a market can be quite an interesting and stimulating exercise. Sure, it can also lead you to chase ideas that don't produce what you are looking for. What are you looking for? Anything that can uncover a "behavioural tendency", anything that can give you an insight into a "pattern of behaviour" which can give you an edge.

Some of the questions I have asked myself are: How often does the Dow "gap up" or "gap down" in a year? Is there any truth to the "As Wednesday goes, so too goes Friday"? Is there a rhythm to the markets – 5 days on, 2 days off? How often is Monday the low and Friday the high? Does it help to know Fibonacci as a day-trader in Dow? Is there any merit to the "strong Friday, strong Monday"? How many days a year are "trend days"? Is there any merit to "what Monday starts, Wednesday continues"? Is there any truth to the 32-calendar day cycle?

Here are some of the questions I would like to answer for you today. The research is conducted over 256 trading days in the Dow Jones index. During the time period I investigated, the 256 trading days, the market went through some explosive moves up and down, as well as settling into narrow trading ranges.

Trader Tom

Overview of Research Sample Space



Some Random Sample Questions

1. If Thursday is higher than Friday, then what does the following Monday look like?
2. If you only traded "extended bars", would you make money?
3. Is there evidence of Fibonacci at play intra-day?
4. Is there evidence to support that what Monday starts, Wednesday continues?
5. How often is a low or a high made in the first 30 minutes of the day?
6. How often do gaps occur? Do they always fill, as the saying goes?
7. How often does the market have trend days?
8. How do you trade a trend day?
9. Are there common denominators between strong* trend days?
10. Is there support for the comment that strong Fridays means strong Mondays?
11. If Tuesday is lower than Monday, then what does that mean for Wednesday?

These are some of the questions that I have asked myself and have set out to answer. The reason should be obvious. If I can gain a deeper understanding of a pattern in the markets, which shouldn't even be there, at least not to the naked eye, then I have gained an edge and a deeper understanding of how the markets trade.

Let me illustrate it with an entirely hypothetical example: what if you could prove with a high statistical probability that whenever a Wednesday coincided with an even numbered date, Thursday always gapped up in the Dow. Now I know this is a ludicrous example, and of course there is no truth to that hypothesis at all, at least I don't think there is, but it sure would give you an edge knowing this. You would most likely go home with an overnight position on the long side, hoping that the market would gap up the day after.

As I said, this is the hypothetical example, one that is a little silly. However, some of the things that I have uncovered also seemed silly on paper but once I started researching it, they turned out to highlight something that wasn't visible to the naked eye.

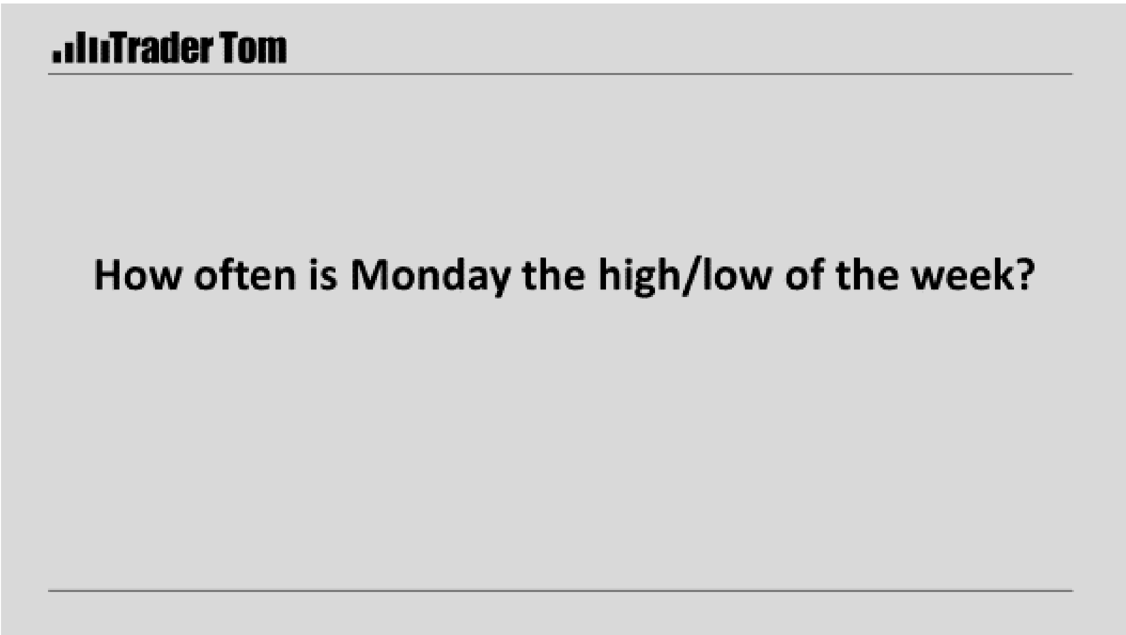
For example, I discovered that if Friday's trading was unable to trade above the high of Thursday's trading, then the probability of Monday the following week trading below the levels of Friday were above 85%. That is the kind of statistics that blows my mind. It gives me a much deeper understanding of how to trade under certain circumstances, and that is what I want to share with you now.

I'm going to start off with an example which unfortunately didn't yield any spectacular results. This happens. It would be nice if every single idea that you decided to test, every single hypothesis you decided to expend time and effort to uncover, yielded an amazing edge. Unfortunately, this is not always the case.

How often is Monday the high/low of the week?

It isn't often that Monday marks the high of the week or the low of the week. In a moment, after we have gone through this initial research, I will show you a much more important pattern. For now, I will state the facts. Over the last year, Monday has marked the high of the week, or the low of the week, 31 times, in the Dow Jones Index.

31/52 = 60%



This information by itself is not particularly helpful. However, say you prepare for trading for a Thursday, and you see that Monday is so far the highest day of the week, could that help you?

Is Thursday special?

Let me rephase the question to make sure you get the proper context. Imagine you are preparing your trading plan ahead of the market open on a Thursday in the Dow Jones index, and you see that both Wednesday and Tuesday traded below the high made on Monday. Would that in any shape or form influence the way the market trades on a Thursday?

If the markets are truly random, it would probably not mean anything. I didn't expect to find a pattern either. Nevertheless, I did the test and I was quite surprised to see the result of the research.

The results I share with you is the result of hundreds of hours of manual testing. It means I go through many print outs of charts. I am certain I could do it much quicker if I had a programmer to do the testing for me. However, while I am checking for data, I also take in other pieces of information.

If Monday is the high, how will Thursday fare?

What I have asked myself here specifically is this question: If Monday so far is the highest traded point for the last 3 days, i.e. Monday Tuesday Wednesday, then how often is Thursday going to trade below the low of Wednesday?

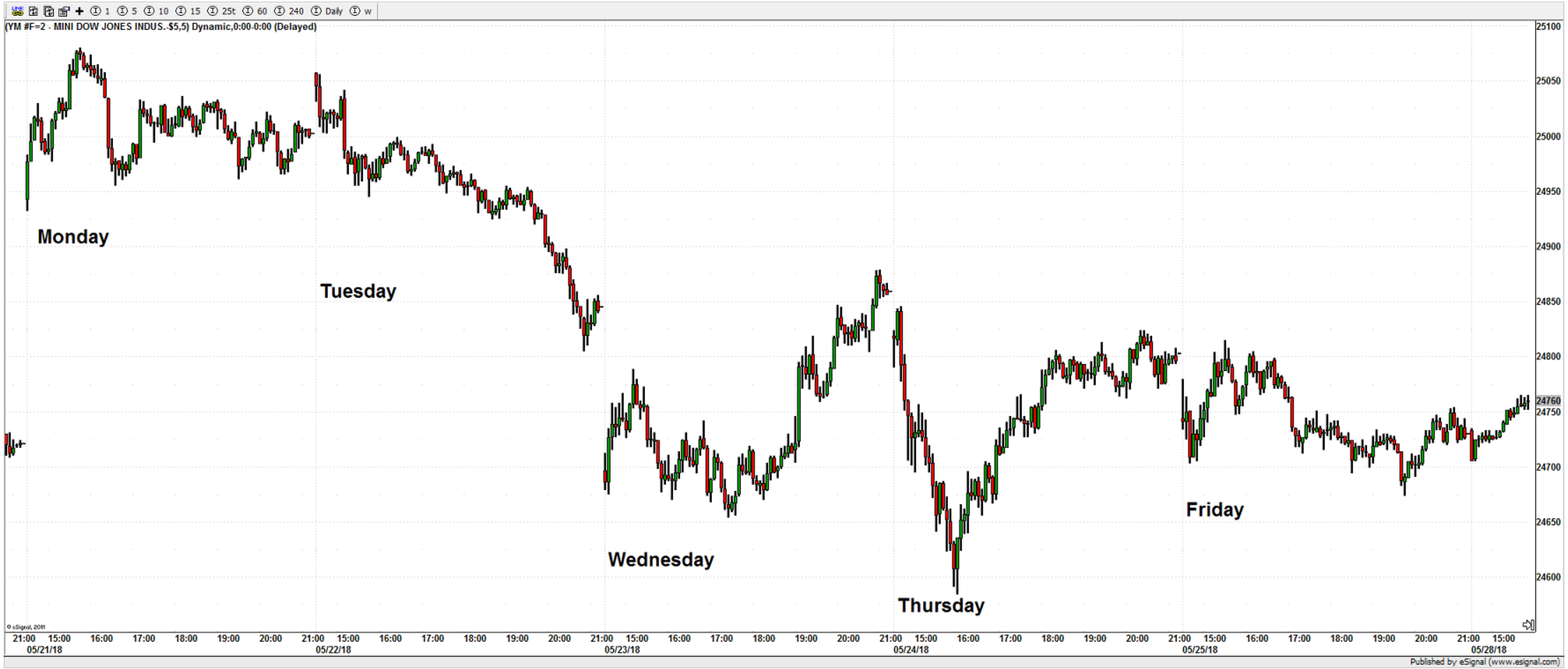
I found, out of the 256 trading days (about 65 weeks), there were a total of 25 times, when I was confronted with this possibility, i.e. Monday was so far the highest point of the week, and Tuesday and Wednesday were weaker than Monday.

Out of those 25 times, the Dow traded below the Wednesday low a total of 21 times. To me that is a significant piece of information. Let me show you some examples, and some close calls.

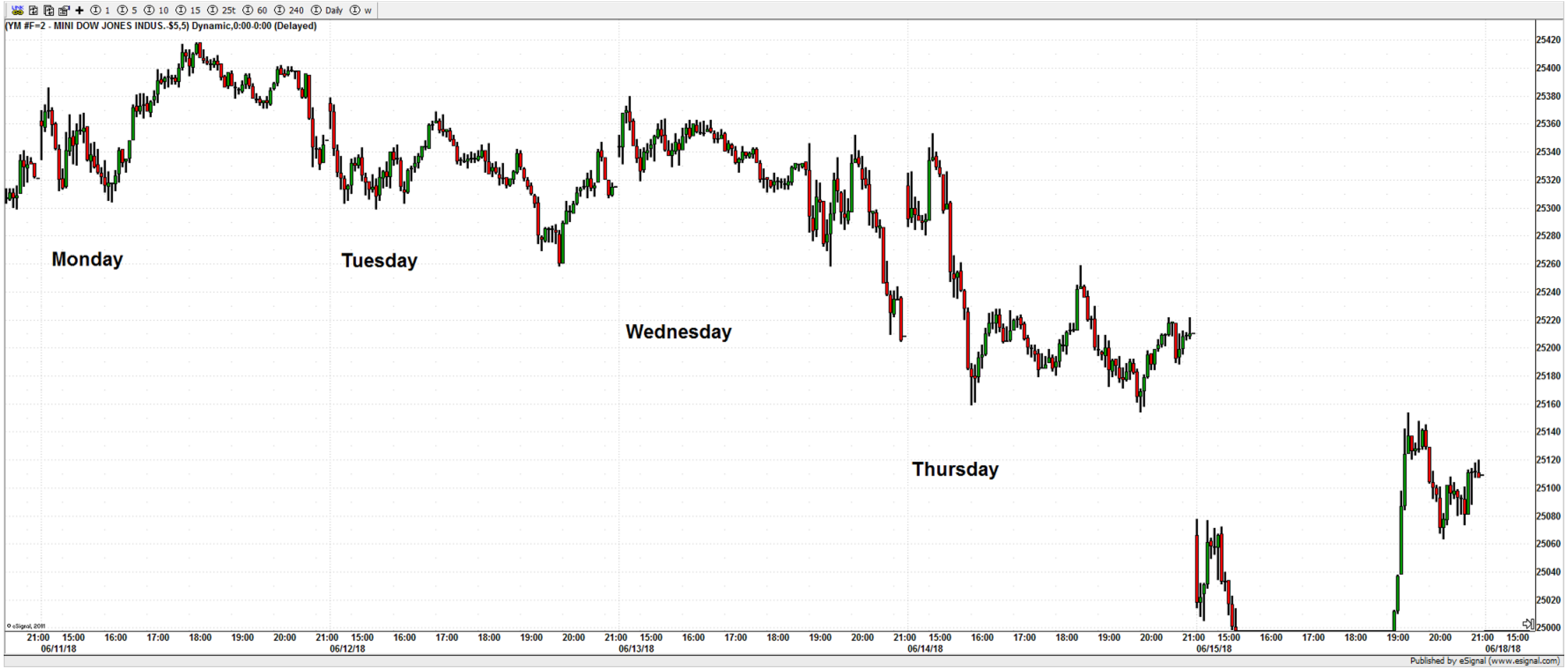
21/25 = 84%

Monday is the high of the week, by the time we are finished with trading on the Wednesday. The theory then states that when this happens, the odds are high – 84% - that Thursday will trade below the low of Wednesday.

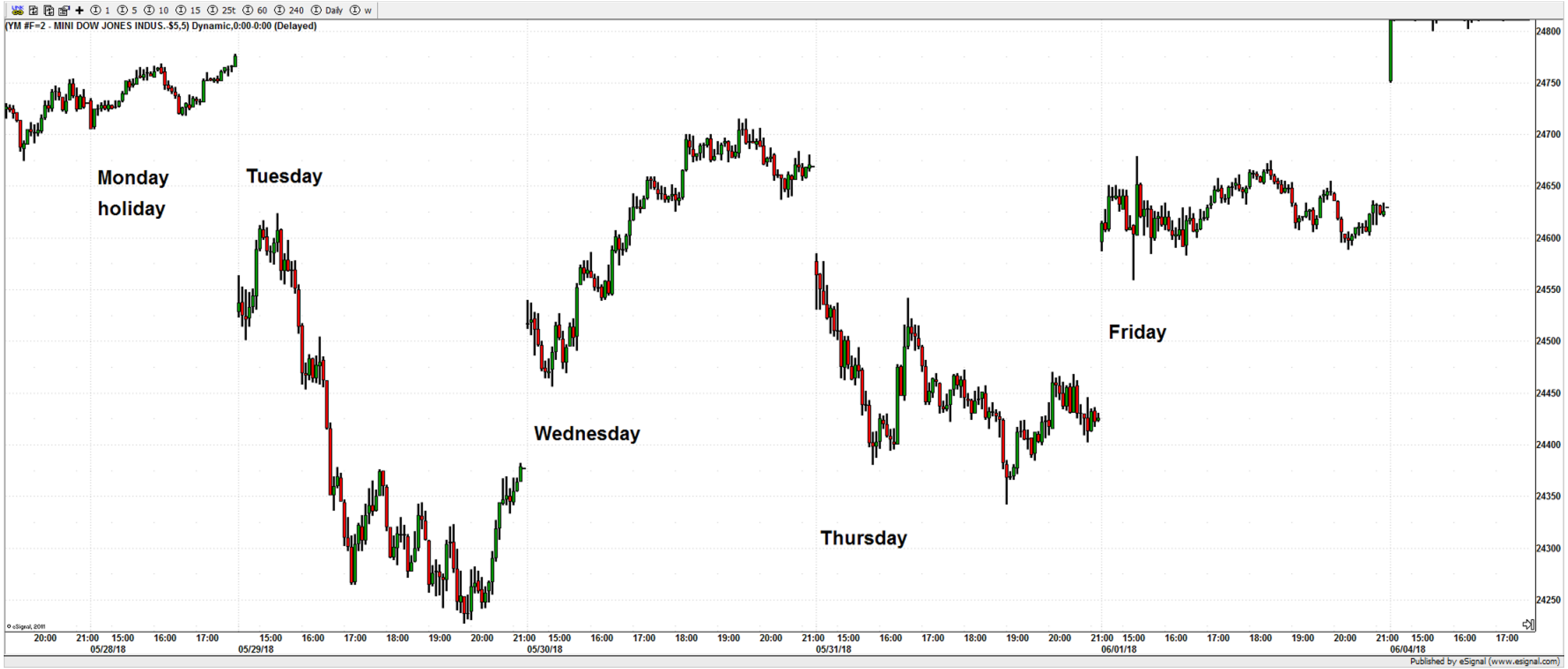
So, although the close on Wednesday was strong, the market still fell on Thursday.



A similar example where Monday is the high of the week, by the time trading starts on Thursday. The Dow index then goes on to trade below the low of Wednesday.

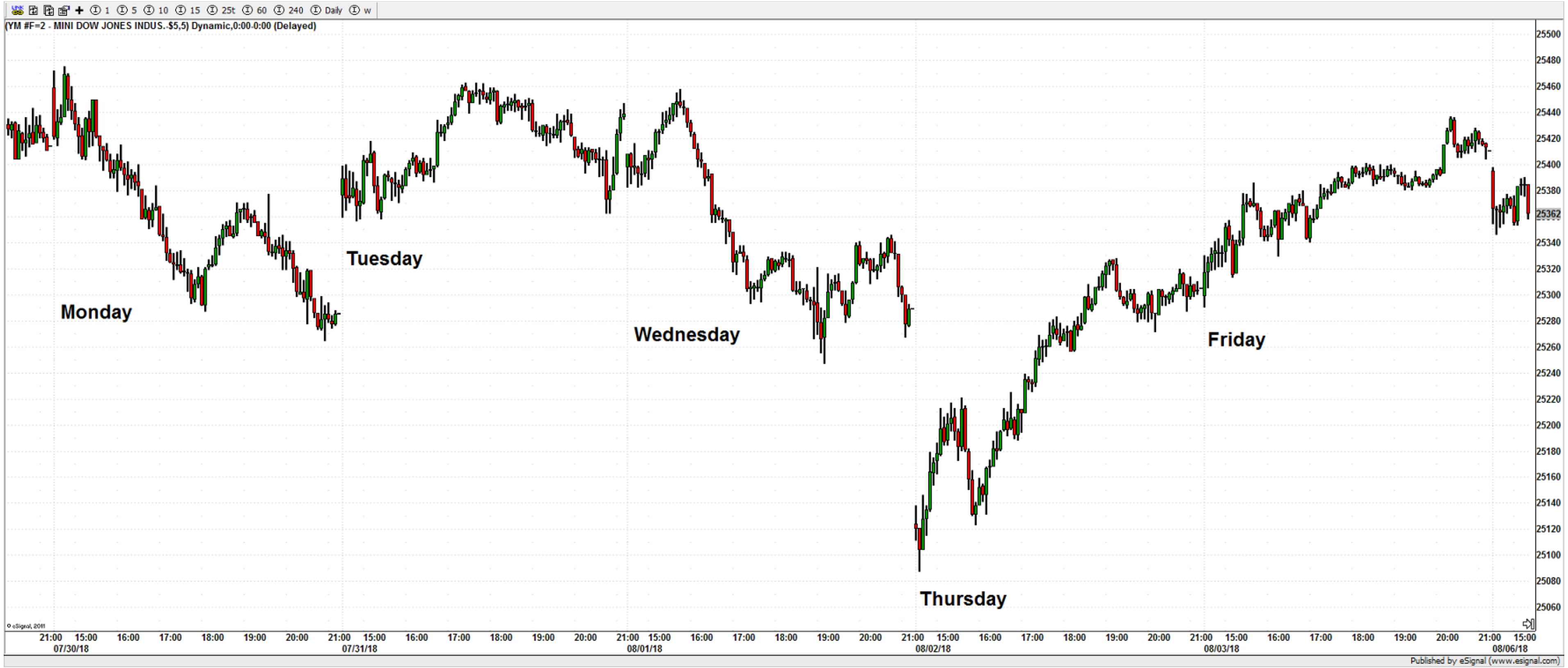


I really like the example below, because even though Wednesday was stronger than Tuesday, prices were unable to get above the highs of Monday.



On the chart below you can clearly see that Thursday traded below the lows of Wednesday.

The next chart, below, is a different example, one that highlights the fact that even though Thursday was weak, the market actually rallied all day. Yes, the statistics worked, but unless you had been short from Wednesday evening, you would not have made money from the short side on the Thursday.



I should make sure at this point that you understand that I am only showing the Dow from the NYSE open until close. I call this the "Regular Trading Hours." I am not showing the Dow market outside of those time frames. My argument is that this kind of testing can uncover patterns which will give you an edge as you prepare for the trading day. In this case, as you prepare for the trading day on a Thursday, you may want to consider that it is highly likely that the Dow will trade below the lows of Wednesday.

Here is an example that failed. The decline on Wednesday was severe, but there was no follow through during Thursday.

The Weekend Effect

Does the weekend make people forget?

I mentioned earlier that I work on “scenarios” which I then test. Another scenario that I have dreamt up is the idea of weakness going into the weekend. Specifically, what happens to “Monday” if the previous Friday trades below the highs of Thursday?

What happens when we start out trading on a Monday, and the previous Thursday’s high was higher than Friday’s high?

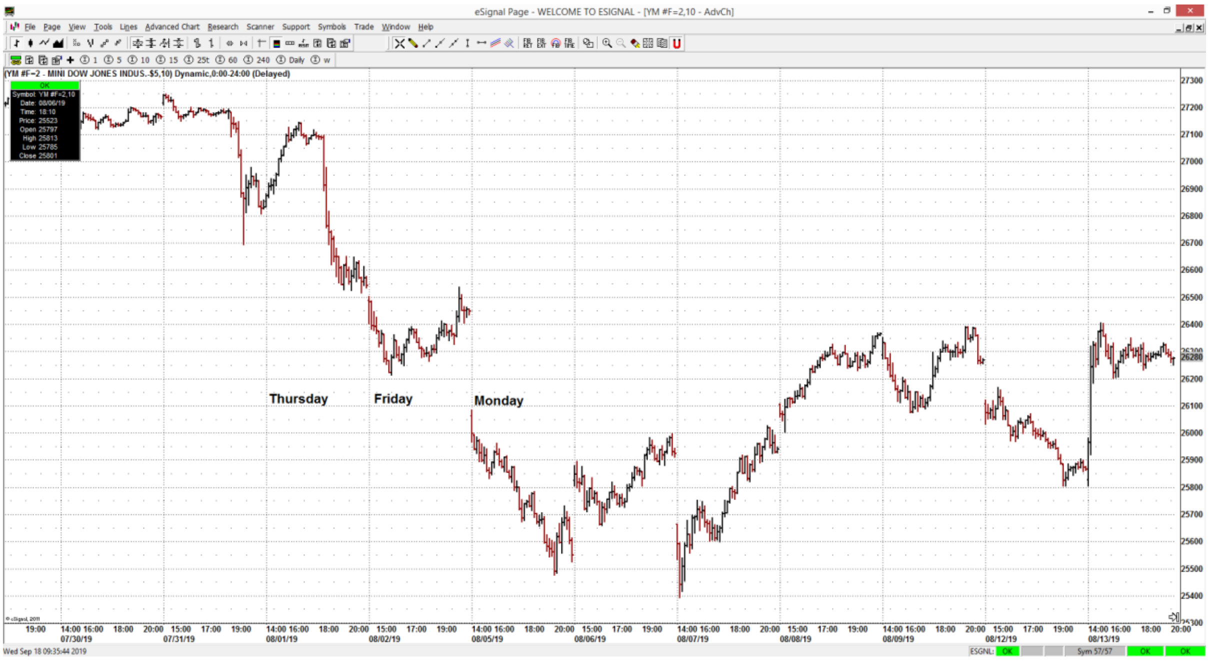
Over the last 52 weeks, there were 21 instances where the price action on Friday was unable to trade above the highest point of the previous day, Thursday. I then looked at what happened on the following Monday. If there was a holiday on the Monday, I would view the price action on the Tuesday.

Considering the random nature of the markets on a day by day basis, there shouldn’t be a pattern, and if there is, I have found an edge to exploit. I was surprised to find that on **20 out of the 21 occurrences**, the Dow traded lower on Monday, often lower than Friday’s low.

Let me show you some examples.

I am not in the business of deluding people, so here is an example where it does not work. Monday did not get below the lows of Friday.

And here is one I traded earlier in August 2019. I went home short over the weekend – always a very risky strategy – and I was rewarded for it (this time!).



I assume you notice that there are often gaps associated with the Thursday/Friday/Monday pattern. Gaps are an inevitable part of trading life. I would like to discuss gaps next.

Gaps in the Dow Jones Index

Gaps are common in the stock index markets. A stock closes on one day at one particular price, and then news is released about the stock. The market will bid up or offer down the stock of the open the next day. That leaves a “gap” on the price chart.

How many days did the Dow gap in the last year?

Common knowledge dictates that all gaps get filled because they are uneconomical for the exchanges and unhealthy for good “price discovery” in the market. Out of 256 trading day, how many days did the Dow make a meaningful gap of more than 10 points up or down? I have ignored gaps of less than 10 points. **The answer is 206 days**.

In other words, most days the Dow index would make a gap – 80% of days to be exact. This information is not particularly interesting by its own merit. I need to dissect this result.

The questions I asked were directed at developing trading setups. I wanted to know how the market reacted to gaps.

1. How often does the Dow make a gap and this gap is then filled the same day?

2. How often does the Dow make a gap, which is **not** filled on the same trading, but within the next two trading days?

3. How often does the Dow make a gap which is not filled over 3 trading days?

Out of the 206 days where Dow made a gap of more than 10 points, it closed the gap on the same day on 120 occasions.

120/206 = 58%

There is a 58% chance the Dow will fill the gap on the day. There were 86 times it didn't close the gap on the same day. How many times did it close the gap in the next 2 trading days, if it failed to close the gap during the same trading day of the gap?

The answer is 42 times.

42/86 = 49%

I can now conclude that gaps in the Dow will either close on the day or close within the next 2 trading days on 162/206 = **78.60%.**

Did you know that there are 78 bars of 5-min duration during the regular Dow index trading session? If the markets were truly random, each one of those 78 bars should have exactly the same probability of being the high or the low of the day. However, this is not the case. You are much more likely to see the high or the low of the day in the first 30 minutes of trading. I have compiled some stats for you below.

High or Low of the Day

All 5min bars:

1st bar of the day has a 20% chance of being the HIGH or the LOW of the day.

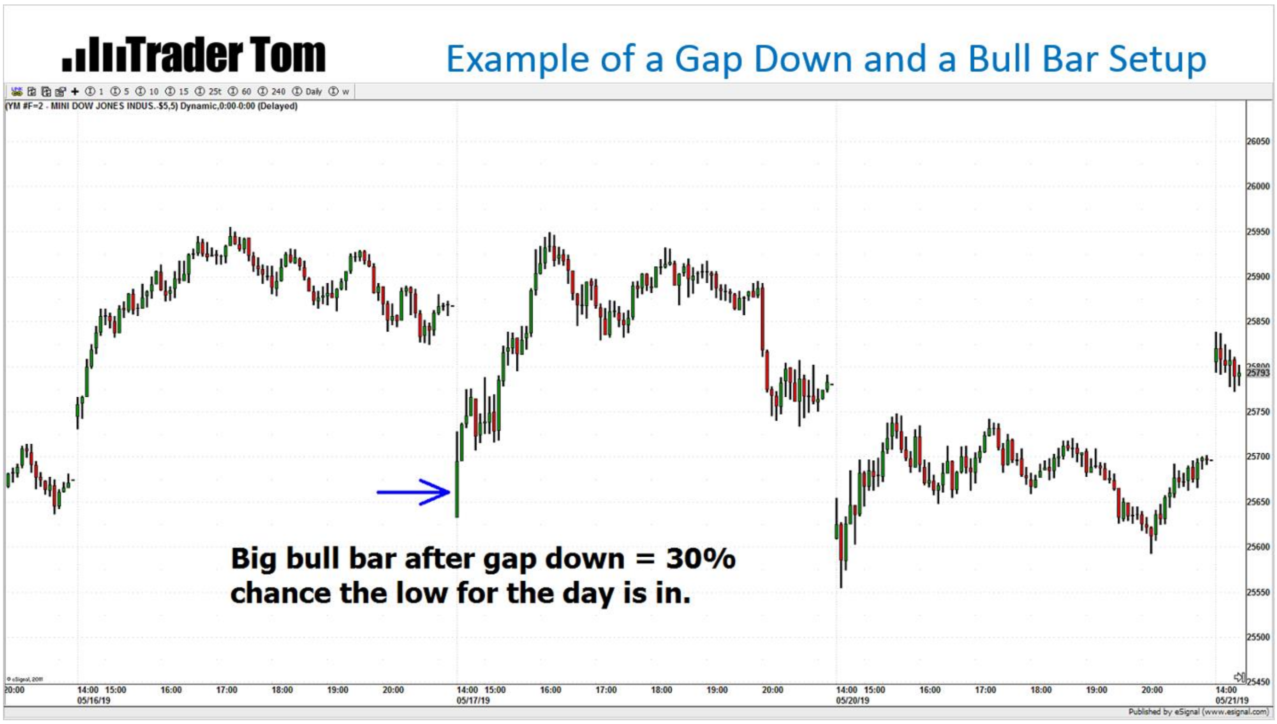
But, if we see a **BIG BULL BAR** after a gap down, or a **BIG BEAR BAR** after a gap up, then the odds are now 30% that we just saw the low or the high of the day.

By 30 minutes in, or by bar 7, there is now a 50% chance that the high or the low of the day is formed.

By the close of the 13th bar, around 1 hour into the trading session, the odds are now 70% that we have seen the high or the low of the day.

By bar 18, there is now a 90% chance we have seen the H or L for the day.

By bar 78, there is a 99.99% chance you have seen the high or the low of the day.



Nitty Gritty of Trading

Trader Tom

Example of a Trade

It is not pretty – but it is real – and it perfectly sums up what it is like to trade for a living…..

I would like to take you through a handful of slides from a trade that I executed. Admittedly, it is a winning trade, which is a little bit of a cliché, and quite predictable as well. The ego has a tendency to never want to portray ourselves from a weak side. Therefore, you will see two examples, one of which is a winning trade, and one of which is a losing trade. I think it's very important that you get a balanced perspective of trading.

I certainly don’t want to be the person who contributes to the enormous database of wrong information surrounding trading. It is not an easy task to make money trading.

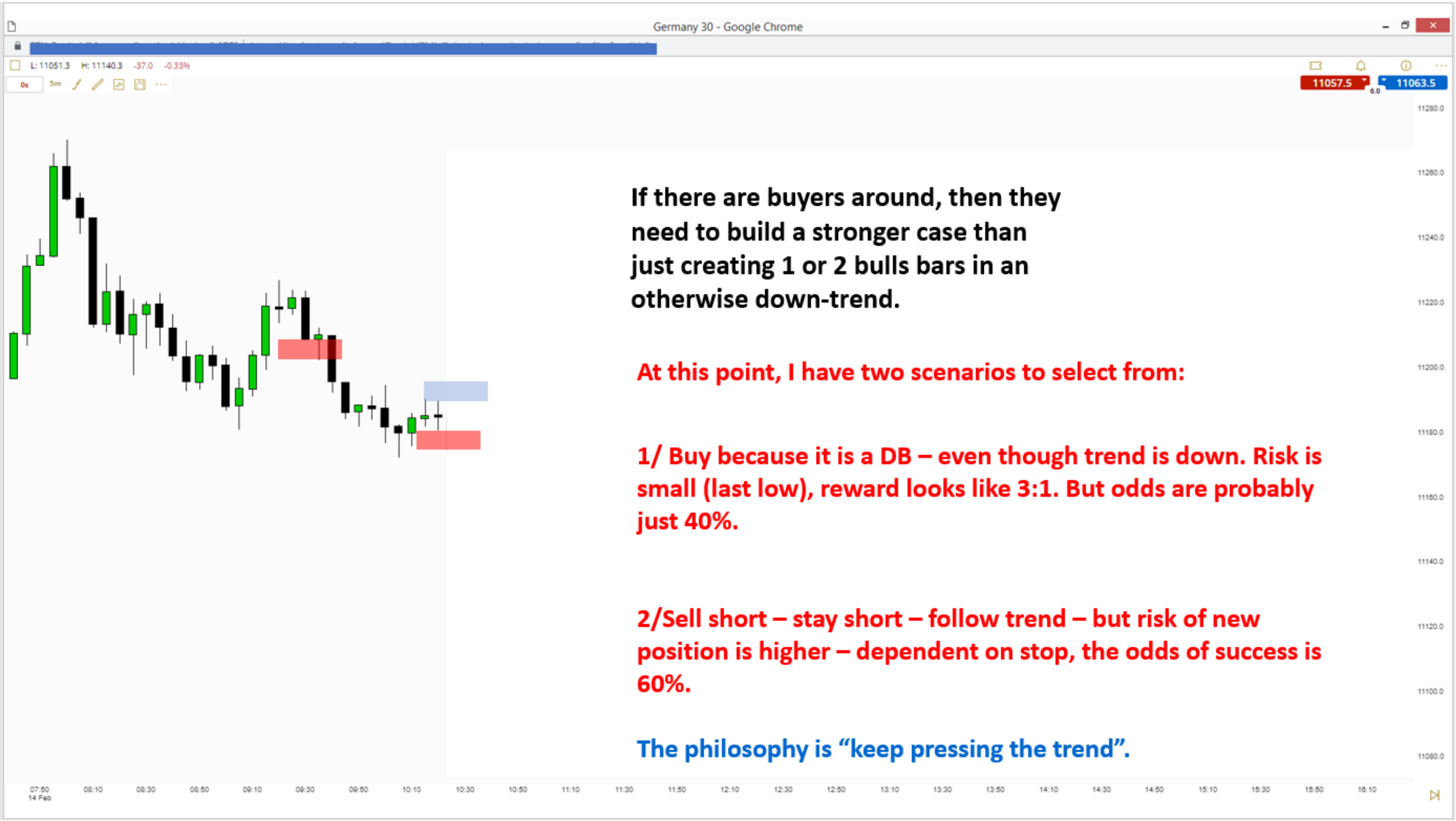
At the end of the day, you are not trading against some higher intelligence form. You are simply trading against the best and the brightest. They are people like you, who wants to make a living from trading.

Most of the people we are trading against, or with, are institutions. I don’t think that makes our job any easier or any harder. Institutions are after all run by people and algorithms are created by people.

Sure, some have more manpower than you have. Computers don’t get tired. However, you’re not looking to catch every single move in the market anyway. You are hoping to be in the market long enough to make a great living from trading, but you are happy to close your computer down at night. You have the ability to walk away and to be able to say enough is enough. You don’t have to make a market like a market-maker, and although there is pressure on you to make money, I can assure you that trading from an institutional point of view isn’t without pressure to perform as well.

I will now take you through the slides for the trade I executed.

This is slide 132. On this chart the Dax is in a downtrend. I'm making a comment on the chart that if there are buyers around, they haven't been able to exert their strength particularly well. All we have seen so far is one or two bull bars on the five-minute chart.



At this moment in time, I have two scenarios to select from. I can buy the Dax because it is a double bottom. The risk is probably relatively small, because I can put a stop loss just on the opposite side of the most recent low.

The odds of success on this particular trade is most likely not great. The market is after all in a downtrend, but my risk reflects the chances of success. I may not have a very high chance of winning the lottery, but the cost of buying a lottery ticket reflects my risk. If I lose, I lose a pound or a dollar. If I win, I am most likely going to become a millionaire. So the risk versus the reward is compelling, although I am not one to buy lottery tickets in the first place.

Alternatively, I can sell short the Dax, because I have a philosophy that states that I must keep pressing the trend. The trend today is down. Do you recall the slide that I showed you of the statistics of the Dow Jones over the last 30 years? Well, those numbers hold true for the Dax as well. Dax may very well be in an uptrend on the daily chart, but right here right now, on this five minute chart, the trend is very much down. This is the trend that matters to me.

The problem with executing a short position at this moment in time is not that you are not trading with the trend. The problem is that finding a place for your stop loss is a trickier proposition. Let us go through the scenarios that are available to you:

1. You can place a stop loss just above the high of the most recent bar. Your risk is tiny, but you are almost certainly going to get stopped out.

2. You can also place a stop loss just above the high of the last swing high some 12 to 15 bars earlier. The odds of getting stopped out now is smaller than before, but the flipside is, you now have more risk.

3. You can place your stop loss above the highs of the day. The chance of getting stopped out now is relatively small, but if you do get stopped out, you will suffer a loss which is proportionally high.

4. You could also trade without a stop loss. Then there is absolutely no chance that you will get stopped out. I don’t recommend that you trade without having a stop loss somewhere.

The next five-minute bar is a bear bar, and it closes at its low. The bulls are looking to buy the double bottom, while the bears are pressing for the trend to continue lower. This pattern you are seeing here should lead to more selling, it should lead to lower prices.

I don’t know if I made that clear above, but I am short this market. I am fully aware that the burden of proof is on both sides. It means that even though the market looks negative, this can very quickly change, if the bears take their foot off the accelerator.

Training an Unorthodox Way

The way I teach my students and the way I train myself is to show charts where you don’t see the full story. I only show a few bars at a time. In fact, most of the time I only reveal one bar at a time. While the trend is lower, the last 10 bars have overlapped, and the market is not trending lower.

What you should notice on this chart is what happens on the fourth last bar. When a market has a lot of overlap candles, or bars, but it is within the context of a bull trend or a bear trend, and the market then makes a new high or a new low, which quickly reverses, this makes me very suspicious.

If I at this point am not already in a position, this is what could make me jump into the market. In this short position I am getting concerned that this market is ready to move higher, maybe temporarily, maybe initiating a new trend higher. The odds of it happening are small but seeing a market that makes a new low after a sideways range, only to immediately be followed by three bull bars, is no longer looking so bearish.

I traded a setup similar to that today in Sterling Dollar. I think I should come up with a fancy name for this setup. Either way, fancy name or not, this setup is a “mis-direction” move. I have included a “before” and an “after” chart below.

The setting was as follows. Sterling Dollar had traded sideways throughout the night. The date is the 25th September and Boris Johnson, the sitting Premier Minister is in trouble. The Supreme Court of the United Kingdom has ruled that his suspension of Parliament was unlawful.

Some news or other pushed the Sterling Dollar higher initially. However, the very bearish looking red bar that followed is a clear indication that no one is buying Sterling Dollar. The red bar completely engulfs the previous bar’s body, and it closes right at its lows, below the low of the previous two bars.

Anyway, I am getting ahead of myself here. Let me show you the DAX chart first. Then I will show you the Sterling Dollar chart.

BUT the bears – the sellers – also need to prove they are strong enough to push the market lower.

While the overall picture is pointing lower, the last 10-15 bars have more or less been sideways.

The last 3 bars have all been bull bars.

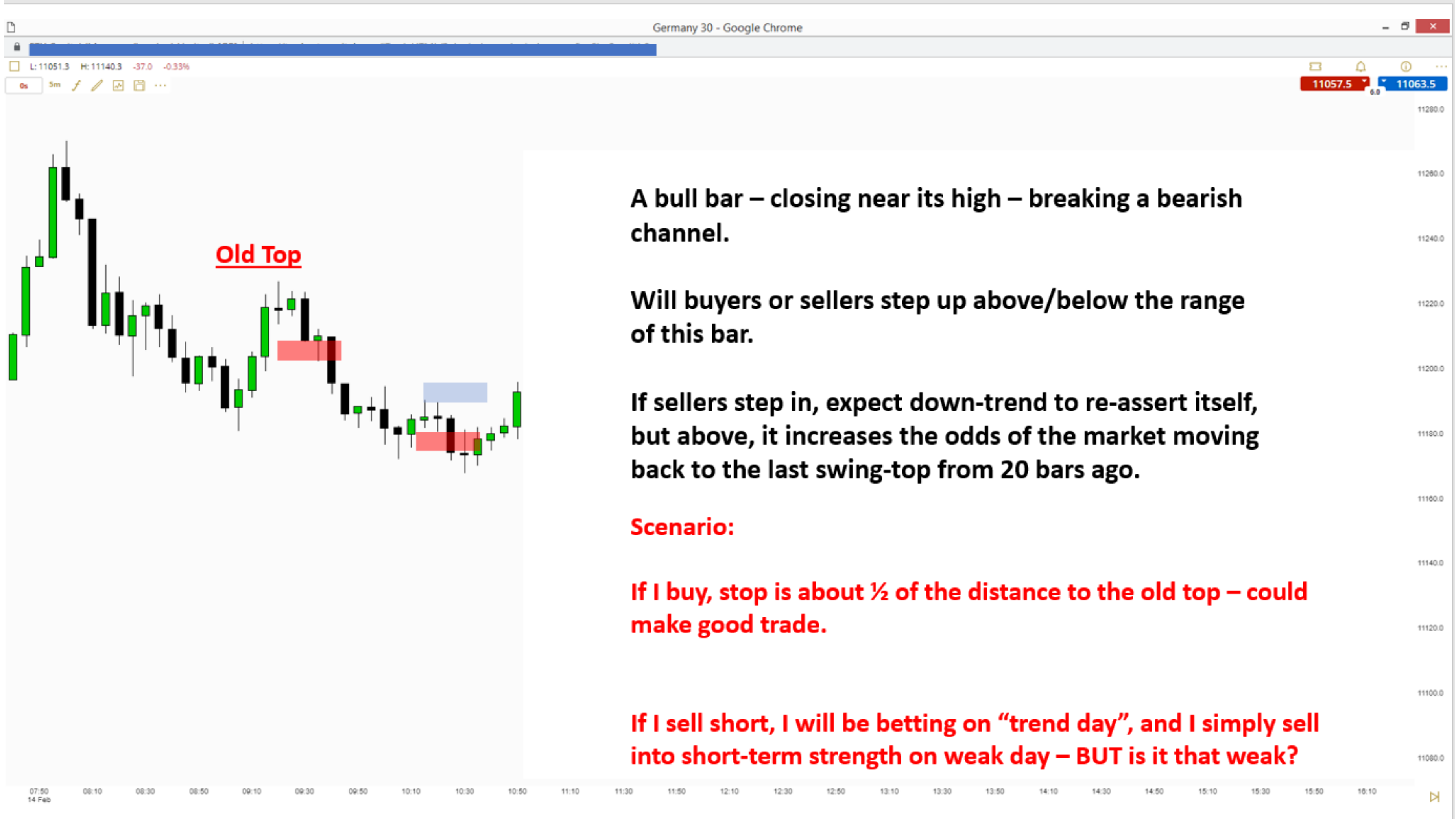
OBSERVATION

When a market has a lot of overlap bars, but within the context of a bull trend or a bear trend, AND the market makes a new low/new high, and THAT new low/new high “bar” is the one that should push the market further – well if it doesn’t and the market immediately reverses or does the opposite for 2-3 bars, I get concerned.

I am sorry to jump from one instrument to the next, and then jump back again. I hope you can follow my reasoning for doing so. This is the chart of Sterling Dollar. It shows a good Sell Short set up. The set-up dictates for a sell short position immediately. The risk can simply be determined to the point where this market shows strength again. I would assess that point to be above the high of the bar just a moment earlier.

The outcome was favourable. When you are in a winning position the real work begins. You need to consider when to add to the winner and when to move your stop loss, and when to close the trade. All these decisions are on top of when to get into the trade. Many argue it is a lot harder to exit a trade well than to enter a trade well. I have to agree with that opinion.

This is slide 135. We are back to the DAX chart. The next bar is not a complete surprise. It is not threatening the bear case either, but of course at this point my position is losing. When you are watching this chart here, you have two options. You can sell short, hoping that the trend will resurrect itself, and the market will push lower.



The odds are probably good here, because we have a micro trading range, and we have reached the top of that range.

If you sell short here, you have to consider where to put your stop loss. You can put your stop loss some arbitrary number of points away, or you can place your stop over the secondary top, or the highest top to the extreme left of the chart.

The further your stop is away from your entry point, the less risk you have of getting stopped out, but you risk more of your capital. It is as simple as that.

Alternatively, you can buy the Dax. If you buy the Dax, you are trading against the current trend, but your risk is relatively small, especially if you bet on the Dax going up to the high of the day.

The problem I have right now with being short the market is not that I think I am necessarily wrong. However, I think there might be a good chance that the market is going to make me sweat a little more.

Over the next few pages you will see the charts in their full size. I have annotated them for you.

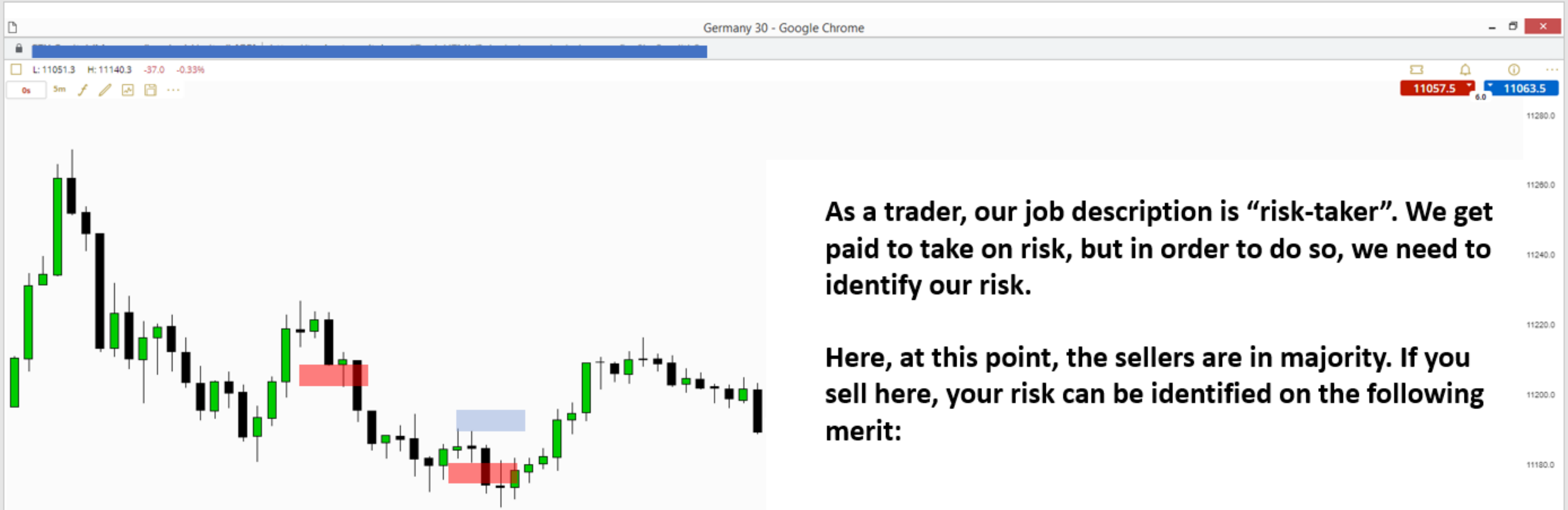
As you can see, I haven't put any comments on this chart. I purposely decided to give you an opportunity to make up your own mind. I know you can glance to the next chart, but if you were confronted with this chart during the trading day, would you be bullish here, or would you be bearish here?

I am aware that the DAX had built a base low, and it moved higher off that base.

I was keen to make sure that I had an appropriate stop loss, which meant I wanted to see the DAX move above the highs set about 30 bars earlier.

Next thing I was looking for was weakness. This weakness is coming on this chart. The index has approaced the prior high, and I finally get a bar that closes below the low of a prior bar. That made me feel good about the short position.


Germany 30 - Google Chrome
11057.5
11063.5
I am not observing an acceleration of the trend. The latest bar is very negative. It closes at its lows, and it is greater in length than the bars that came prior.
This is called an Extended Bar, and it is a good sign that the trend is accelerating.
Good for bears, not good for bulls.



As a trader, our job description is "risk-taker". We get paid to take on risk, but in order to do so, we need to identify our risk.

Here, at this point, the sellers are in majority. If you sell here, your risk can be identified on the following merit:

I sell now, and place stop loss above last high – 9 bars earlier: the odds of being stopped out on a move higher is high, but the reward vs. risk is probably 2:1. – or better if "trend day"…..

I sell now, but place my stop above the high 33 bars ago: the odds of being stopped out are low, but my reward to risk may not necessarily be in my favour.

I sell now and I place stop loss at the high of the day: the odds of being stopped out are low, but my risk may be disproportionate to my rewards.

If I had seen the previous chart, I would sell short immediately. I think this is a bearish pattern. The last bear is a bearish bar, and it is longer than the bars that comes before it. I call that an "expansion bar". What I find amusing is what happens over the next 12 bars – which is an hour's worth of trading.

The market goes into a tight range. This kind of trading range is enough to take the enthusiasm out of even the most alert day trader. The market just goes dead. There is even a saying, that springs to mind here: "don't short a quiet market".

And to add to the worry and insult, the market then begins to move higher again.

Just as the Dax is testing the double top - the top of the trading range - we begin to see the sellers come in again. This bar below – the last bar – is again longer in length, thus indicating more conviction and more volume, and hopefully a more determined move lower.

“Wig” is another word for “tail” on a candle. The DAX has made a low that has not been seen for some 25 bars.

These kinds of bars, the last three black bars, are very often indicative of an acceleration in trend, or a trend reversal. I would not hesitate to sell short here, if I was not already short. I would add to my short position here too.


Germany 30 - Google Chrome
L: 11051.3 H: 11140.3 -37.0 -0.33%
11057.5
11063.5
What is your philosophy?
Catch the low?
Trade counter-trend?
Press the existing trend without trying to guess where it will end
11280.0
11260.0
11240.0
11220.0
11200.0
11180.0
11160.0
11140.0
11120.0
11100.0
11080.0
07:50
14 Feb
08:10
08:30
08:50
09:10
09:30
09:50
10:10
10:30
10:50
11:10
11:30
11:50
12:10
12:30
12:50
13:10
13:30
13:50
14:10
14:30
14:50
15:10
15:30
15:50
16:10

What I would like you to be aware of on this chart is that the market moves from being in a trading range into trending. During the trading range there are many candles or bars that overlap. Once the trend begins the bars from an isolated point of view begins to look as if they are freestanding.

This is my favourite setup. This is a situation where I would become aggressive in my shorting. I would add to my winning trades, as the market prices lower. The reason why you are adding to your winning positions is because you are reinforcing a positive behaviour. You are not adding to a losing position. You are not taking half your profits either. You are pressing the winners. You are pressing the trend.

The reason why I brought this example to you is because I want to show you, in a tedious and drawn-out way, how taxing it can be on one's patience. You had the advantage of sitting with a printout in front of you. You do not have to sit for an hour in front of a screen, observing the market do absolutely nothing.

Pattern Recognition

A pattern can be 1 bar – and the predictability it gives you

A Set-up Which Failed

The previous trade was a good trade. There was no way of knowing that in advance. You hope for the best and you assess what the market has to offer you. The previous trade made good money. The next trade does not fall into the "good money category" even though it was similar in many respects.

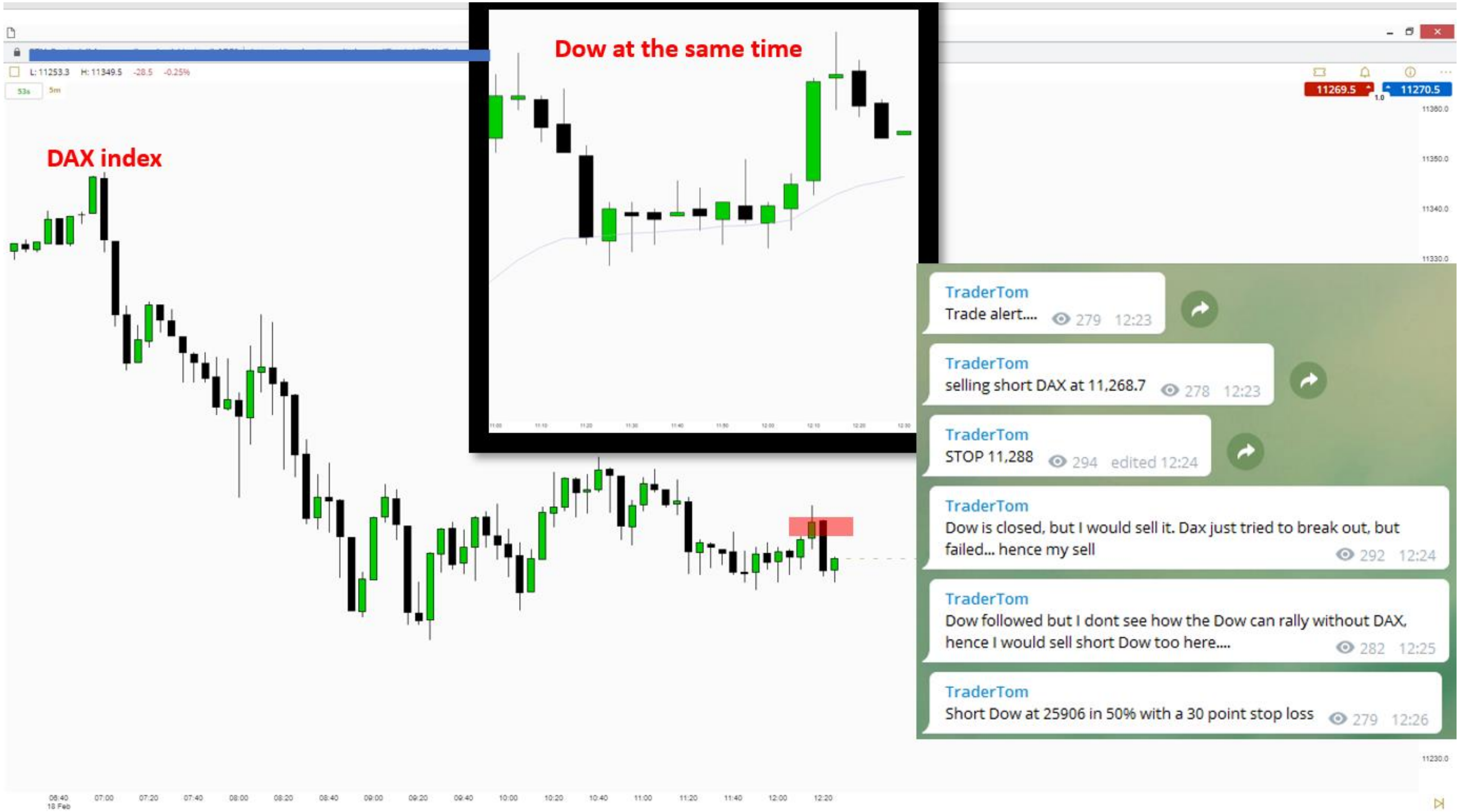
Stock indices tend to be correlated. This correlation can provide opportunities. One such opportunity played itself out in the DAX and it is shown on the next chart. The DAX index was in a downtrend on this particular day. I had a chart of both the Dow index and the DAX index, side by side, on my screens.

This pattern is easy to understand once you "get it", but the explanation of it is a little less "easy" to get across.

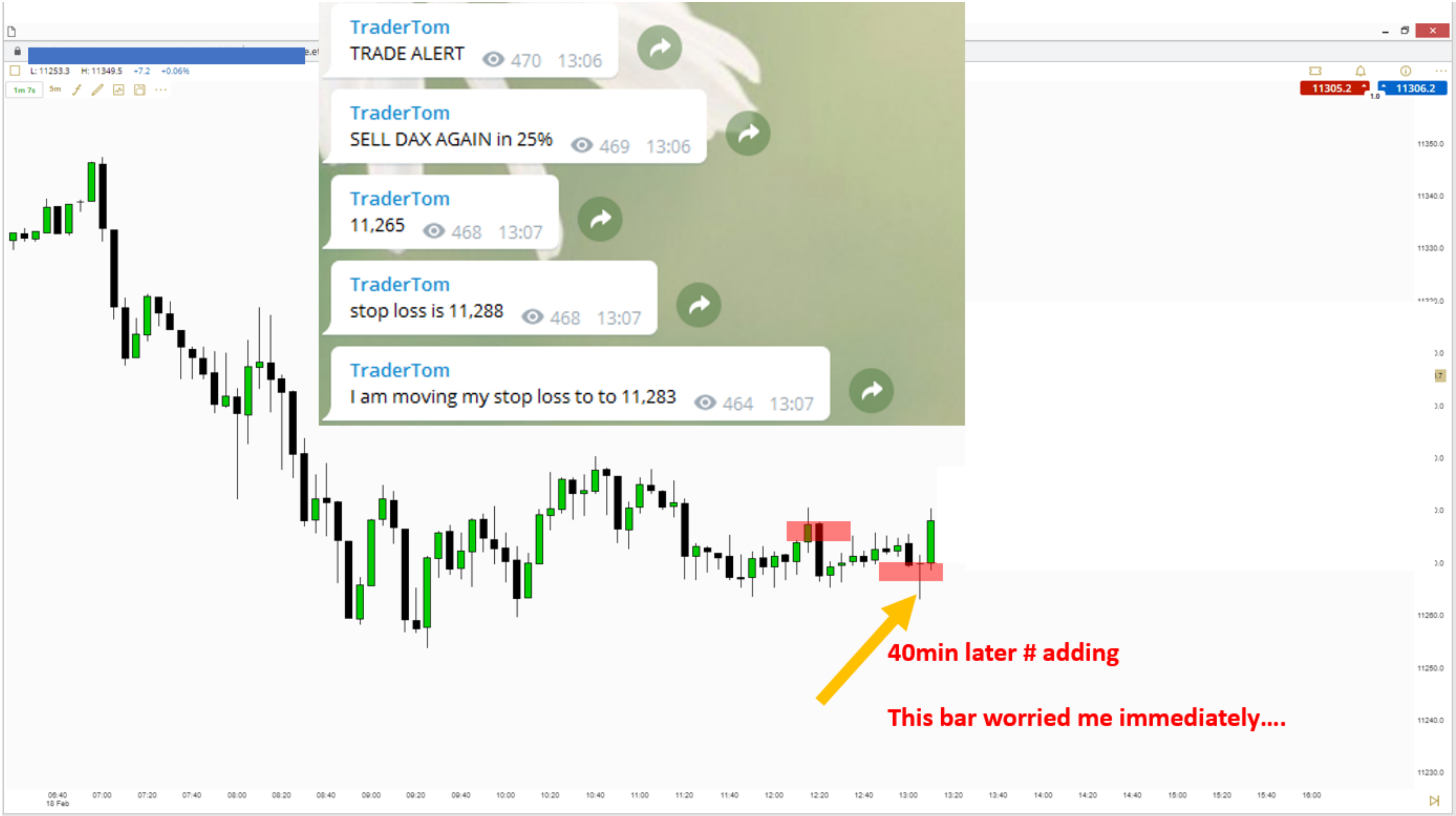
1. The Dow is making a "new high" within the context of a down-trend. It means that even though the Dow is trending lower, it managed to get above the high of the last counter-trend high.
2. The Dax index also tried to make it above its recent counter-trend high, but it fell hopelessly short of achieving that goal.

My conclusion is that Dax is very weak, and I want to sell short the weak index. You could argue that I have traded one index using information from two indices. That would be correct. I am shorting the Dax index because it didn't manage to make up to or above its most recent swing high, while the Dow did.

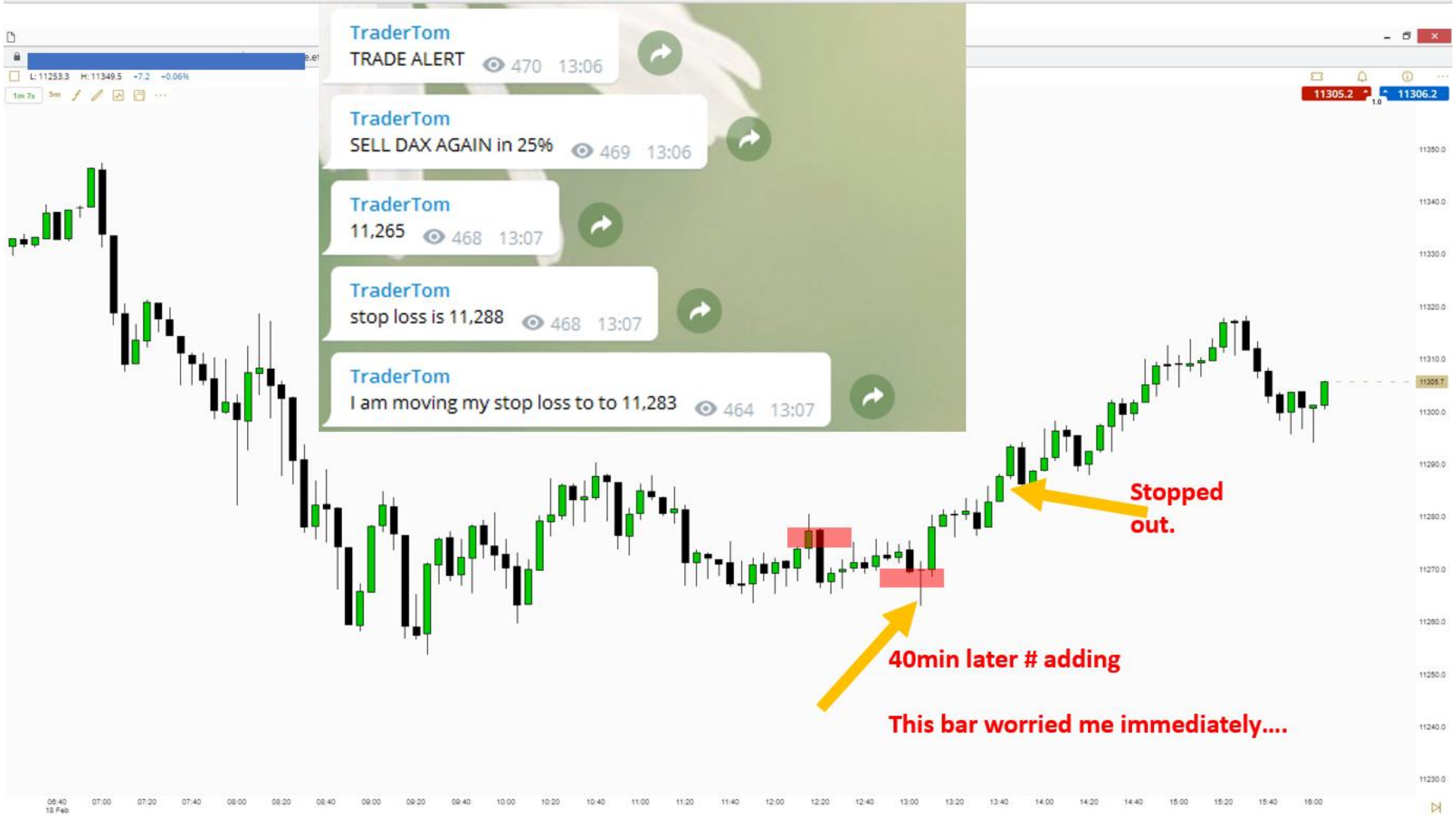
Hopefully you should be able to see that the DAX makes a lower high two bars before the current bar shown, while the Dow Index (in the black box inserted) actually makes a new high above the previous high. In other words, two correlated assets are moving in tandem up and down during the day, but the Dax is weaker because it is unable to make it above the most recent high, while Dow did. I call this “index divergence”.



However, this trade would go on to test my patience in a major way.



Eventually I was stopped out.



How to Get Better

Earlier in the book I wrote the following words:

"*Atrophy is not just a bodily concept. It is also a mind concept. You need to strengthen that mind of yours by repetition. I'm going to provide you with a brilliant way of getting control of your mind. I will present that idea towards the end of the book.*"

The time has come to follow through on that comment.

Accountability

I have a certain trade style. This trade style is responsible for my financial well-being. The trade style does not come natural to me. My natural trade style is that of a scalper. I can and do make money from scalping, but from experience I know that the big money is made from running and aggressively adding to positions.

Running positions when I want to take profits is a mental obstacle that becomes easier once I am mentally tuned into what I want to achieve. It is a question of living out the philosophy of how you want to trade.

To illustrate this, I invite you to let me take you through a trade. After I have done that, I will take you through how I prepare for a trading day. I think today is a perfect day to illustrate my routine. I am tired. I am not well rested in body and mind. I stayed up past my normal bedtime, because I wanted to see how Donald Trump reacted to his impeachment investigation. In short, I am not all "singing and dancing". I wish I was, but you can't control every aspect of your life, no matter how hard you try to prepare.

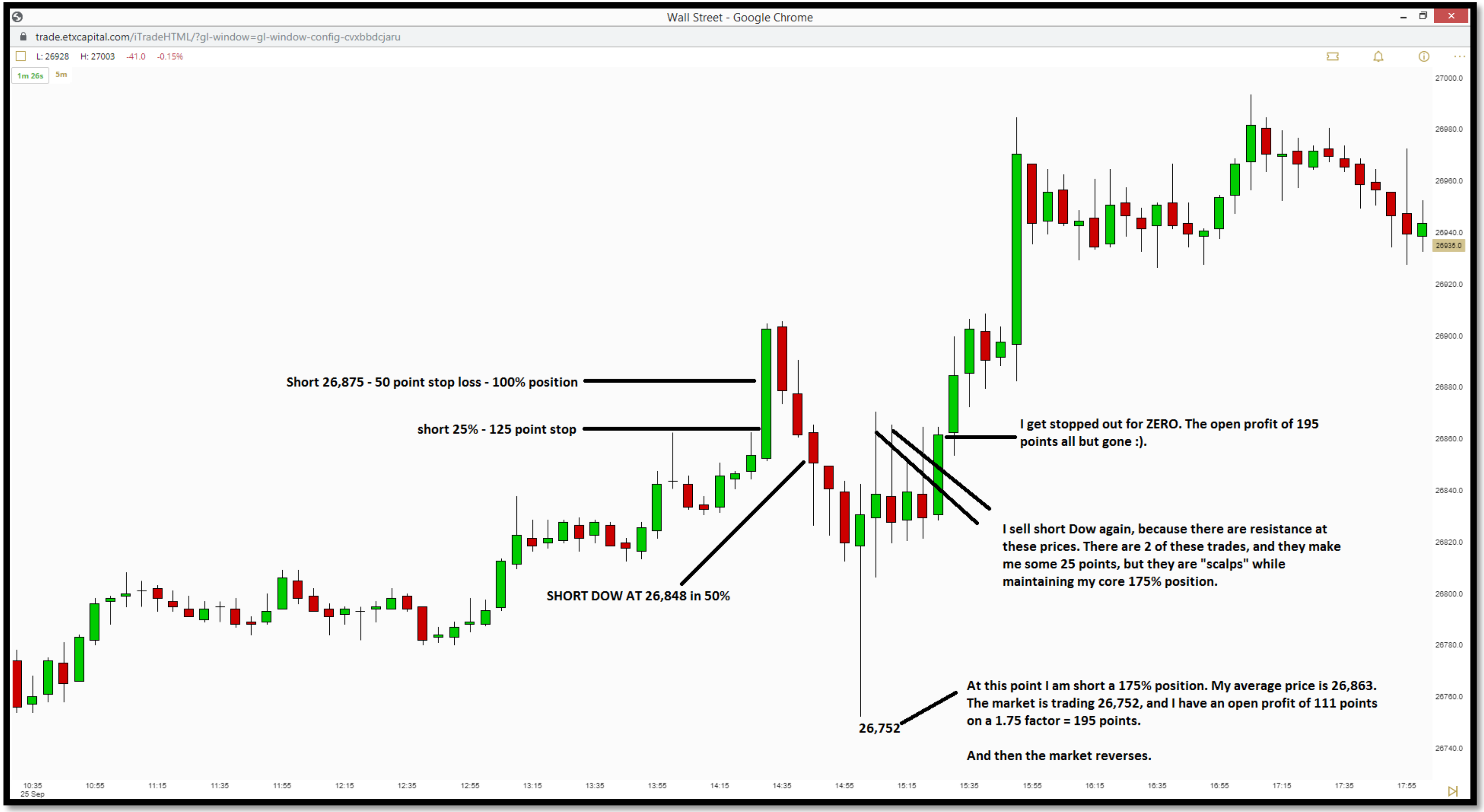
Mohammed Ali once said that the fight was won or lost far away from witnesses – in the gym, and out there on the road, long before he danced in the ring under the spotlight. His point was that it might seem he was born and destined to dance in the ring, but Ali knew that it was his training that created the illusion of dancing in the ring. I like that quote because it reminds me that our trading success is the result of our commitment to the outcome, we want to create for ourselves.

So here I am, on a wet dark Thursday morning at 5am, going over the trades from yesterday, like the one shown next. I can't stress this enough. It is not what we do every now and then that defines our lives. It is what we do all the time. I find that to be true in everything. In life, in relationships, in business, and in trading.

The reason why I go over my past trades are two-fold.

1/ I get to see if I have made a mistake or if my discipline is becoming weak.

2/ I get warmed up for the trading day ahead.


Wall Street - Google Chrome
trade.etxcapital.com/iTradeHTML/?gl-window=gl-window-config-cvxbbdcjaru
L: 26928 H: 27003 -41.0 -0.15%
1m 26s 5m
Short 26,875 - 50 point stop loss - 100% position
short 25% - 125 point stop
SHORT DOW AT 26,848 in 50%
I get stopped out for ZERO. The open profit of 195 points all but gone :).
I sell short Dow again, because there are resistance at these prices. There are 2 of these trades, and they make me some 25 points, but they are "scalps" while maintaining my core 175% position.
26,752
At this point I am short a 175% position. My average price is 26,863. The market is trading 26,752, and I have an open profit of 111 points on a 1.75 factor = 195 points.
And then the market reverses.

I would like to provoke a thought response from you, while you read this. I want to set the scene and then ask you a question. There is no right or wrong answer. There is only a right answer for you. It is just a question for you to think about.

Yesterday I was short the Dow. I have illustrated this on the previous chart. It shows my entrance, my add-ons and my exits. At one point I am plus 200 points on the position. The Dow index, however, violently reverses, and my position ends up with zero. Those are the facts. There is no pretending that I got out at or near the lows. I was plus 200 and I got nothing at the end of the trade.

After the trade was completed, I had some people contacting me, asking me various questions, and suggesting I should have taken profits. I accept that it must be tempting to point fingers, when you have all the facts in front of you, after the fact. However, when you are sat in the trade, it is an entirely different proposition, and that is where it is good to have a philosophy to one's trading.

As you are going to read this in weeks and months from now, I need to set the tone for the trade. I do that by showing you what I saw the moment I went short.

On the next page you will see exactly what I saw, when I went short. I am aware that there is a higher low right behind me, but I decide I want to sell short the double top. It is as simple as that. I am not making it more complicated than it is. There are no indicators to guide me. There are no moving averages to confuse me. There are no Bollinger Bands or Keltner Channels or whatever else traders will put on their charts.

Although this is not the right time to talk about this, I will just spend a few lines on the matter. I do not use indicators, because all indicators or band etc are made up from the three building blocks of the market: Price, Time, Volume.

I don’t need to see a distorted image of the reality, when I have the reality right in front of me!


eSignal Page - WELCOME TO ESIGNAL - [YM #F,15 - AdvCh]
(YM #F - MINI DOW JONES INDUS.-$5,15) Dynamic,0:00-24:00 (Delayed)
SELLING SHORT HERE
09/20/19
09/23/19
09/24/19
09/25/19
Thu Sep 26 10:46:00 2019

So now you know what I saw. Here is the question I want to ask you.

Scenario 1

You are short the Dow - like yesterday - and you are plus 200 in open profit - but the market reverses and you get nothing for your effort.

HOW DO YOU FEEL?

Scenario 2

You are short the Dow - like yesterday - and you take profit on the spike lower. You are happy. However, Dow continues lower for another 400 points? Your profit, the 200 points, would have been a 900-point trade.

HOW DO YOU FEEL?

Do you remember what this whole manual is about? It is about trading the proper way, by acquiring the right kind of mindset for it. It is what I wanted to know 20 years ago, if someone would have told me. My argument is that I would rather be short and experience the pain of seeing a lot of my profit disappear, than I would want to be short, take my profit, only to see the market move much further in my favour. That would cause me much more pain, than the pain I would get from being stopped out for very little profit.

I associate more discomfort with the prospect of missing out on a good move in my existing position than I receive comfort and joy from closing a position with a profit.

As I said, there is no right or wrong. It is just a philosophy to trading. There are many nuances to the example above. I hear people say

"I could jump back in again"

"you can't go broke taking a profit"

I accept there are nuances, but how you answer this question will define the kind of trader you are.

There is nothing wrong with taking profits, but the art to trading is not so much the entry as it is the exit. There was no way of knowing or anticipating that the Dow would reverse as violently as it did. Those who say they took profits down there would be the same people who would take profits at other times when the market will continue lower and they would be scratching their heads, wondering why they are not short.

My trade was true to the moment, and after the fact, we are all perfect traders. I think it is dangerous to think you cannot go broke from taking a profit. If you are anything like the 90%, you will have a tendency to run your losses longer than your profits.

By telling yourself it is ok to take profits and telling yourself that no one ever went bust from taking a profit, you are probably acting from a perspective which is based on fear rather than opportunity. If your profits are smaller or the same as your losses, then trading will never really become the thing you want it to be. You literally have an opportunity every single day, on every single trade, to practise and strengthen your “trading muscle”. Just don’t expect it to be easy, if you are anything like the normal 90%.

Your focus should be to build a level of consistency, not in trading, but in thought. If you don’t have a place where you train that consistency, a routine to counter-act the “normalities of thinking”, then that muscle will weaken.

God, I sound like a drill sergeant, shouting at the new recruits. I assure you that I am far from perfect myself, if that is any help, but I train with an awareness of what my weak points are. By being aware of my natural tendencies, by being aware of what my weaknesses have been and still is, I may be able to recognise it in “real-time” and have a chance of building new neural pathways that facilitates my new behaviour.

Expertise Comes with Experience

Last night I watched Roger Federer play Stefanos Tsitsipas at the Swiss Indoor semi-finals. I will readily admit that I admire Roger Federer, and I watch him whenever I can. I watched him play Rafael Nadal in the Wimbledon final in 2007 and I have been a fan ever since. It was the greatest tennis match I have ever seen.

What I noticed more than anything was his patience and his aggressiveness. In the final throes of a challenging match for both gladiators in London that evening I saw Roger Federer eye an opening in the armour of Rafael Nadal, and when he did, his demeanour became aggressive and focused like a laser beam. The parallels to trading are uncanny. Roger won 51.08% of all the points played.

As I sat watching the young Tsitsipas and the older Federer battle it out, I was battling with how to finish (or even start) this chapter, the final chapter in the book. After the match was over, I sat down trying to write. My mind was blank though, and I went to bed and fell asleep. I think the last thought I had before I fell asleep was if it was even possible to describe what goes on in my head when I am trading.

I woke up during the night and the first thing I became conscious of was fear. Specifically, how I had trained myself to trade bigger size. I will explain this in a second. First I want to dismiss some common misconceptions about reaching a goal.

Motivational Talk

I am not a trained psychologist. I have no formal training. I have read a significant volume of material on behavioural patterns, including depression and anorexia. I have also read my fair share of self-help books, written by people who are most certainly not psychologists. Their use of anecdotal evidence is frightening, in particular the notion that behaviour can be changed by talking positively to oneself.

You would think that the annual ritual of making promises to oneself on New Year's Eve would put an end to the ludicrous notion that positive self-talk has an ability to change people's behaviour, but apparently not. The idea we can become profitable traders and let profits run and cut losses purely by repeating a mantra are as ludicrous as believing in the tooth fairy. Yet people do it, even though there is no research that supports this argument.

In my thirties I read a number of books by inspirational authors. Napoleon Hill and his "Think and Grow Rich" was one of the first I came across. Then there was Zig Zigler on audio tape. He had quite an enigmatic way of telling stories, which I enjoyed. Then of course there was Tony Robbins and his Unlimited Power and then his Awaken the Giant Within.

I enjoyed the books so much I decided I wanted to attend one of these inspirational workshops. The first one in my town was a "workshop" with Tony Robbins. I use the word "workshop" in a very liberal sense, because I run trading workshops too. When I run workshops, I train at the most 10 people at a time. That is why I call it a workshop. You literally are there to be personally trained by me. The Tony Robbins workshop had some 9,000 people attending.

In hindsight I am not sure it was the best idea I ever had. I have quite a low tolerance threshold to hype and bullshit. I am just not a fan of the adulation of a guru. I am all for guidance and inspirational education, but you are not going to reach someone personally in a crowd of 9,000. It was a waste of my money. Damn, I could have bought a lot of books, really useful books, for the £700 I paid for that ticket. There is an inherent "time" problem with self-help gurus. I see it in my own industry. If you can't promise change in a person within a very short time frame, you are not going to sell your product. Change has to be instant to sell – even though it is bullshit.

Course headlines like "Become a millionaire trader by attending our weekend workshop" or "How to cure depression instantly" are catchy, and they sell. I accuse them of promoting a short-cut ideology, where success is somehow achievable through hacks and cheap gimmicks.

There is simply no amount of chanting that made Roger Federer into who he is, or his up-and-coming super-star opponent Tsitsipas in last night's tennis match. Chanting "Now I am the voice, I am a force for good, I will lead and not follow" will not make you good at anything. You might get psyched up, and you might be flooded with feel-good hormones, but they will wear off, and that is when your true self emerges. If you don't have a compelling argument for change, your commitment will falter like a New Year's resolution on the 2nd or 3rd of January. I tell my son that a compelling argument is that thing that will propel you forward long after your enthusiasm has worn out.

The Change Process

The decision to change can be instant, but change itself is a marathon, success is a marathon, achievements are a marathon, and anyone who has truly achieved success in life has treated their goals as such. I find documentaries much more inspiring than attending hyped up mega-events featuring toothpaste smiling gurus. I want to think for myself and I want to achieve my goals by stealth, not by making big arm movements.

So I diverted from the original theme of this chapter, by writing about inspirational gurus on a big stage, so that you understand that trading success is not a one-off exercise but a commitment to excellence. However, commitment is not the only ingredient in the recipe of a successful trader.

Take for example Stephen Hendry. He is not a trader, but he sure is an inspiration to me. Stephen Hendry is a retired snooker player from Scotland. For those of you who don't know what snooker is, here is a quick description of it: think of a traditional sized pool table; now make it twice as big; now add twice as many balls as a traditional pool game, and then appreciate that the balls needs to be potted in a very particular order. Welcome to snooker, an almost impossible game to play with any degree of competence and success for a novice.

Yet Stephen Hendry and Ronnie O'sullivan and the likes of them make it look so easy. I watched a documentary about the arrival of Stephen Hendry to the global snooker stage, and how he got there. He trained and he trained. He put himself in the most difficult situations during his practise sessions, until he was able to get out of those situations more than 7 times out of 10. His training sessions lasted 6-7 hours a day, every day.

It is October 2019 as I write this. I flew to London last week to give a speech on scalping at the London Investor Show. Explaining scalping is exceptionally difficult and I had brought a video of me scalping over an afternoon session in the Dow Jones. I thought it would help to show how I do it, and thus perhaps bridge the theoretical instructions with the practical applications.

After I showed the video, I had people comment on how easy I made it look. Well, I said, it has taken me many years to make it look easy. I had to overcome many challenges. If I sound like Donald Trump now, you have permission to shoot me. I am not trying to glorify my achievements. I am doing my absolute best to make you understand that trading is so much more than just watching a chart and placing a trade.

Fear or Hope?

I have worked 20 years in the CFD industry. I have seen too many people come and go. They arrived in the hope of easy money and they left considerably worse off. They simply never stood a chance against the much better capitalised and much better prepared colleagues in the marketplace. I would have gone the same route, had it not been for a lot of luck and meeting the right kind of people at the right time. I hope to God that this book comes to you at the right time.

The key turning point for my trading was when I began working on my fears. Let me put it in a way you will understand instantly: I can make you a very competent technical trader very quickly, but if you begin to tremble with fear the moment you increase your trading size, you will never fulfil your true potential.

If you are normal, you will experience what I experienced. If you are normal, you will experience what everyone else is experiencing. Why don't we start there? Why don't we start at that point where most people fail?

Most people can acquire the necessary technical knowledge to trade well. Most people can afford a good trading course or a good trading book. If you can't, then email me. I am very happy to give you the material you need to get a good technical foundation. You just need to bring your own commitment. So let us assume that you are a good technical trader, and let us assume that you are patient as well. Let us assume that when you are trading small size, you are able to hold on to your trades, and you even know how to add to the winning trades.

If 90% of all traders are unsuccessful, you can be damn sure they are unsuccessful for the same reasons. There are not that many reasons why people fail. Those 90% can be put into relatively few categories.

1. They are technically inept.
2. They are technically competent, but they are impatient.
3. They are technically competent, but they are fearful when the profits increase.
4. They are technically competent, but they are fearful when the stake size increase.
5. They are technically competent, but they are hopeful at the wrong time.

Trading psychology is a bit of a cliché. So are the many sayings surrounding fear. Fear is an essential ingredient for survival when you are trapped in a burning building. Fear doesn't make the building burn any less or any slower, but your mind sends a signal to your body to pump adrenaline into your blood, which in turn will make you think and respond at a heightened level.

“Out of control” fear is called panic. In a panic situation you are unable to think and you tend to act from reflex. People have literally died from smoke inhalation just inside the door of a burning building, because they panicked. The door was unlocked, but instead of pulling the door open, they pushed and pushed until they were overcome from smoke and lost consciousness.

I said that I think trading psychology is a bit of a cliché. To me the reality is that psychology is not about fixing a problem. It is not about treating a problem. It is about making changes through the expansion of people’s mind and perception. I knew I had to deal with my fear of losing open profits before I could begin to make more money trading. I used **fear and disgust** for that.

I have a good knack for making short-term predictions on a chart. I have used this skill extensively for my scalping and short-term trading. This skill was developed through looking at a 5-min chart every day for years.

However, it really is tedious to trade “singles” all day long. A “single” is going for a few points here and there. You may disagree as long as there are enough of the “singles” in your trading. I contend though that there is more money in “sitting” than in “doing”. There is more money in taking a position and running it than constantly moving in and out of the market.

Then what do you do with that knowledge when you realise that you can’t run positions? You begin to think deeply about the issue of the problem. You meet another trader who does not have this problem. You listen to his philosophy. You hear what he is thinking when he is in profitable positions.

I run a risk of opening myself up way more than I had intended to, when I started writing this book. It feels like I am letting every man, woman and child peek into my inner workings, with all its flaws and insecurities. How did I make the change when so few seem to be unable to do so? How do I control behaviour and sustain motivation to change? The answer is many-fold, but the primary driver may surprise you. I became disgusted with myself. I became utterly disillusioned and disgusted with myself.

Disgust

Many years ago, I had girlfriend. She was my first real girlfriend and I was her first real boyfriend. We were young, and we were very much in love. My girlfriend was a little round bodily, which I found very attractive. She, however, did not like her body image, so she began to diet. She had dieted before, but she had always failed to sustain a weight plan. Now she was in love, and her motivation shifted into another gear. The weight loss became dramatic, quite dramatic, and it led me and her family down a path that pains me to write about.

Anorexia is a serious psychiatric disorder, but (and forgive me here for using a tragic story to illustrate a point about behavioural change) it is an interesting motivational phenomenon. We are hard-wired to eat. We need no training to eat. Yet somehow this hard-wired pattern is overridden by a social motivation: the desire to not be fat. This force, this motivation is so strong in patients with an eating disorder that it proves to be immune to both medical and psychological treatment.

What is the basis for this powerful force of motivation? It isn't chanting, and it isn't positive self-talk. As I understand it, my girlfriend was motivated by disgust. She was disgusted by anything that looked and felt fat and overweight. This force was so strong it could keep her away from a hard-wired pattern of eating food.

As humans we are driven forward by forces. Those forces can be born out of a desire to move away from something, or they can be born out of a desire to move towards something. I happen to be a person who is primarily driven towards a goal in order to move away from something.

In my belief system and in my experience, "away orientated" goal setting is a much stronger motivational force than "towards orientated" goals. You can test this for yourself, using a simplistic scenario. What would compel you to lose weight more: a picture of you where you are in a perfect shape or a picture of you where you are obese?

I asked my circle of friends what they would prefer, and all agreed that they would find the "obese" picture a stronger motivator than the "perfect" picture, although a few did comment that they would probably still like to have both. Fair point.

I believe that disgust is a much stronger emotion than joy and happiness. We all have reasons to be happy every day, but we tend to forget that. However, disgust is not something we are likely to forget. You won't forget the rotten milk you drank by mistake, nor will you forget the client of yours who had such repugnant breath that you nearly threw up. That is a powerful motivator right there.

Ed Seykota once said that everybody gets what they want from the markets. When I read that, I dismissed it. I wanted to win, but I wasn't, so I clearly wasn't getting what I wanted.

End of story. It annoyed me that he had said that. The thought of never being able to trade profitably consumed me. I had spent so much time studying, researching, testing, formulating plans, calculating ratios that I really didn't know what more I could do.

If you look around in your life, you are likely to be able to find examples of dramatic changes, induced by disgust. What gets a person to finally commit to a goal is reaching the point of disgust. I got disgusted with my trading over a long period of time. The pattern was always the same: trade like a wizard, become over-confident, lose the account. I became so sick of it. Positive intentions, sticky notes on my trading monitor with mantras, and self-help exercises don't nearly possess the motivational force of physical disgust with oneself.

If disgust can turn eating into a behaviour to be avoided, and if disgust can turn an alcoholic's drinking into a thing of the past, then disgust can also turn you into the trader you would be proud of looking at in the mirror. I am sorry if I have shocked you. Those of you who know me well will probably be taken back by my extreme steps to ensure my pattern of behaviour in the trading arena is exemplary. I am not going back to the roller coaster ride I was on in my early trading days. I was so disgusted with the amount of money I lost. I was embarrassing.

We are most apt to change a pattern once we become truly disgusted by it. Would you continue to do business with someone who violated your trust and your contract with him and stole your money? No, you'd become so disgusted with such a dishonest character that you would cut all ties with him.

Well, that person is you when your own patterns violate your contract with yourself and cause you to lose money. Once you become truly disgusted with your own patterns, you'll shun them altogether.

A trader is losing and continues to lose because he doesn't want to change. Change is hard work. I began plotting my trades on the chart when the day was over. I put a marker where my entry was and where my exit was. It was horrible. It was like incriminating yourself over and over. I was disgusted with my recklessness.

I had to face up to the fact that I was actually an awful trader. I was like the guy who could recite the entire technical analysis syllabus for the Master Technician exam, but I could not stop myself from

1. Overtrading out of boredom.
2. Overtrading out of anger and a desire to get revenge.
3. Impatient trading – jumping the gun.
4. Trading against the trend – trying to buy the low in a move.
5. Fearful trading – by cutting my winners short because I was scared the money would disappear.
6. Constantly averaging in lower and lower – i.e. adding to losing trades.

Do you have any idea how horrible it is to come face to face with your own demons? Have you ever truly opened yourself up to criticism? I remember vividly standing up at a meeting saying, “My name is Tom Hougaard, I am an alcoholic.”

It was horrible. It was demeaning. It was belittling. It was so embarrassing. You are outwardly a success. You drive an Audi R8, a £100k car. You have two university degrees. You are admired by your peers, loved by your clients, and yet you are an abject emotional wreck.

It is like being stripped naked for the whole world to see your fat ass, your tiny willy, your saggy boobs, your cellulite, your scars, your spots, your pimples, your swellings and whatever else that happen to our bodies. It is absolutely everything you don’t want, and you have a hall full of eyes watching you.

But the truth is an entirely different story. You break yourself down, so that you can survive, so that you can get reborn into the person that you really want to be. You strip away the proverbial wallpaper of the rooms in your castle so that you can start over. Fresh start. Clean canvas. The walls are ready to be decorated how you want it. It is exactly the same process elite soldiers are trained. They are pushed beyond their breaking point. Then they are put back together again, stronger, wiser and with an unshakable faith in their own strength, their own abilities, their determination to get a job done, no matter what.

You know as well as I that what I just described is extreme. No one in their right mind likes to expose themselves like this. It is why we get defensive. It is why we fight our corner. Our identity is being questioned. Call it ego, call it what you want, but no one likes having their intelligence questioned. It is a lot less painful to continue down the known path than to stop, evaluate, and turn around.

There is the slightly nagging pain of continuing down the known path, but you soothe yourself by reminding yourself that you are not alone. There is power in numbers, even when everyone is wrong. Or you stop, and you evaluate, and you turn around, and the pain is relentless because everything is new, and you are naked, and exposed.

And yet that is power! There is power in being honest. There is power in standing up and saying to the world and yourself: this is who I am, I don’t like it, I hate it, I am embarrassed by it, but it is what it is. It is a clean slate. It is a fresh start. It is like a forest fire. It clears the debris. New growth can start.

I am not talking to you because I think you want to make a bit of extra cash from trading. I don’t care if you make a little or a lot of cash. I am talking to you because you are the 90%, which probably should be called the 99% and you want to be a 1%. I get it, and I want to hold your hand until you don’t need my hand anymore.

The successful traders are consistent in their approach and they work hard to stay there. My systems and approaches evolve but they don't change. There is no need to change once I have a method that resonates with me. That is the hard part of trading; to find a system that is compatible with who you are.

The Drifter Mind

How our minds work is fascinating. Our brains can be our best friend or our worst enemy. My mantra is written on virtually every page of any presentation I give. Control your mind – control your future.

You have to want to do what you do. You can live a life which is authentic to your soul, or you can live a life which is what you think people will want you to live. You can be authentic and **own** your life and take responsibility for everything you do. If you don't take ownership of your life, you are not the boss. You have to take full responsibility for everything that you do.

Why would you live a life any other way? Why be subservient? You must be the master of your own kingdom. But brace yourself. You will be forced to make many difficult decisions, and you cannot count on your mind to back you up, if your determination wanders a little.

You can't just walk through life or into things with your eyes half open. You have to know where you are going, and your eyes have to be fully opened. You have to take possession of your life, but as I said, you can't rely on your friends or your family or even your own bloody mind to help you. You have to know your weaknesses, and your weakness is that your mind will wander.

You will drift. Your mind will drift. It is perfectly natural, unfortunately. The solution is trivial but powerful. You have to constantly reaffirm your purpose. Whether you mediate, or shave in the morning, or brush your teeth, there needs to be some period in your day where you remember your purpose.

I am not a sucker for punishment, but I know I am a person who is compelled more by fear and disgust than by pleasure. I am more prone to procrastination if you tell me I will accomplish great things if I behave in such and such a way. If however, you tell me that I will lose everything I have worked for, you can be sure I will act. You can be sure I will get off my ass and behave in the right way.

This is the reason why I start my trading day with the exercise which I call Worst Case Scenario. I really don't care about analysing the markets. My eyes can spot a Fibonacci ratio a mile away (not that I use it), it can read a chart in a nanosecond, and I will have a good idea whether I want to be a buyer or a seller. That ability came from the thousands of hours of chart reading. Thankfully that knowledge stays there.

What doesn't stay there is my ability to always act in my own best self-interest. My mind needs constant guidance and direction. I don't know why that is, but it is. I suspect the majority of the population on planet earth is put together like I am. They just haven't come to realise it, and therefore they drift through life, rather than taking charge of their life. It doesn't mean you can't be financially successful, but wouldn't it be nice to be both financially and spiritually fulfilled? Your job after all is that thing that you do the most, outside of sleeping.

I am a professional trader. I cannot afford to go into the trading ring without being 100% prepared mind wise. My profession is a mind game like nothing else. If I want to win, I have to focus on what is important now. So Ed Seykota was right, much to my chagrin. I did get what I deserved, because I was only good at one part of the game. I was good at the technical part. I don't like this metaphor, but being good at the technical part of trading is like being good at putting together a sniper rifle, but what good does that do you, when you go into combat and you don't know how to handle yourself.

I have a girlfriend now. She is beautiful. I mean just stunning. There is not a day that goes by where I don't compliment her, and there is not a day that goes by where she doesn't lament about the size of her ass or her belly. It is quite sad to see the people you love put themselves down. That is the narrative of the outer world. It will make you feel bad about yourself, through the comparison of someone who has what you haven't got, and then you buy the solution, whatever that may be.

I actively take control of my inner world. I have to give myself enough confidence to reassure myself that we have enough to go out and kick ass in the markets every day. To make that challenge even more real, I post my trades for the world to see. I have never consciously thought about why I do it, until recently, when I was asked. Why do you do it? I do it because it keeps me accountable. It keeps me focused.

I have been as lost as they come, and the essence of the story was not to inspire you to get lost, nor is it to evoke sympathy, nor is it to tell a tale of "rags to riches", but to make sure you understand that exposing your weaknesses will be a good thing. Your mind is a tool. If you let it delude you into thinking all is well, you will not get the success you want in trading, or in life.

I mentioned my girlfriend a moment ago. I remember her going to Weight Watchers. There was a weekly meeting where you would go and weigh yourself. She didn't like it when the scales went the wrong way. That is understandable. Who likes to expose themselves to the world? Who likes to be weighed and have to admit that you hit the help-yourself buffet over the weekend pretty hard? Who likes to stand up and admit you failed yet again, and you drank yourself silly? No one! Who likes to admit to themselves they have yet again blown a trading account because they are incapable of handling their own emotions? No one!

Losing and failing might be a knock to the ego, but it is rocket fuel for growth. It sounds like I am trying to write a self-help manual for procrastination, a best-selling inspirational book. Rubbish. I am describing honesty. When you are honest with yourself, in the company of yourself, or on a podium in front of 40 alcoholics, or whatever the setting may be, you just took a step that 99% of the population don't ever contemplate taking. You already started the journey to winning.

So, the journey starts with the technical knowledge acquisition and the journey continues indefinitely with the constant evolving of both the technical and the mental training. Technical training is part of my day-to-day job, but the mental part needs more dedicated focus. Otherwise it gets lost in the noise of the outside world. I need dedicated time to muscle work that brain of mine. Here is the best example I can find for you right now.

Luckily this is a while ago, but it could happen any day of the week if I don't mentally prepare myself. I short a double top off the open. I am so certain that my research is right. The market will fall.

I don't have a problem with the first short position. I have a problem with the 4 next ones. I could even forgive myself for the last one, because at least I am shorting weakness. This is unstructured and undisciplined trading. I don't care how certain I am of something happening. If it isn't happening, don't pursue it as if it is. Showing you is so embarrassing!

This is part of my preparation. It has been the most useful tool to build mental stamina, and discipline. It reminds me of everything that is weak in me. It reminds me of how my mind, if left unchecked and untrained, will go on a rampage to seek excitement and gratification.

One of the best ways to increase profits is to do goal setting and visualisations in order to align the conscious and subconscious with making profits. I use fear to achieve my goals. I imagine trading a size which even in my mind makes me uncomfortable. I sit quietly in my bed or in my office. The world is quiet, and if it isn't, I stick a pair of ear plugs in my ears. I imagine I am trading, and the market is moving against me. I see myself cut the loss. I imagine I bought the XYZ, and I see it going my way. I feel the brain sending me signals to close the position to crystallise the profit. I see myself doing nothing, as I continue to watch the profit increase and decrease. I see a big profit turn into a small profit. I smile and accept it, and I move on, telling myself it is ok. I place my brain under as much stress as I can with imagined scenarios. I am long and the market is going my way, and a sudden news story breaks the market. I observe my fear shooting through the roof as my P&L turns into a bloodbath. I see myself closing the positions and going in the opposite direction. I see myself not getting unhinged just because the market is moving against me.

I have no idea how you are going to react to this. I wonder if you think it is brilliant or maybe useful but with a few personal tweaks. I wonder. Understand though that I learn visually. I get a message when I see it visually. If you tell me not to trade against the trend, it will not mean any more to me than when a cat meow. Show me a chart where my trades are plotted on, and I am trading against the trend, and preferably repeatedly, then I get the message.

This is my therapy. This is like seeing a psychologist every morning. I get fired up. The therapist expands my mind and my horizon. The goal is to remind myself of what behaviour I want to enact. It is about making changes and keeping the changes.

As I said, I am not sure I really want to publish this. You read about all the negative events in my life, just so you can make money trading. Well, I am a trader, but in writing this book I have to become a storyteller too, and if my purpose for writing the book is to make you a better trader, then so let it be it. I guess I will have to trust that all will be ok.

So how can I be so sure this will work for you? Behaviour is patterned. How we think, feel, and act have a pattern to them, and that patterning is what makes us who we are. The sum total of our patterns is our personality.

Sometimes our patterns interfere with our goals and dreams in life. They prevent us from being who we want to be or accomplishing what we want to accomplish. We are sometimes our own worst enemy, and seemingly we can't stop ourselves when we are in the moment. A man has anger issues, and yet when he becomes angry, he can't stop himself. A woman has eating issues, and yet she can't stop herself when she is in the moment of eating. A trader is fighting the trend all day and his account is suffering, but he can't stop himself. He is simply incapable of turning his position and trade in the direction of the trend. Only afterwards is he disgusted with himself.

The purpose is not to take away everything that is bad in our lives in one swift move. The purpose of my warm-up is not to guarantee I won't mess up. The purpose is to focus on what I want to achieve or become, while being mindful of the things that will most certainly sabotage my goals. The wonderful part is that I am almost certainly guaranteed success if I avoid the failures. I was guaranteed success with my weight goal if I could cut out all the coca cola I drank. I just had to be mindful of that, and the pounds began to come off. I didn't have to do anything else.

I don't have to be certain that my trade is going to work out. I just have to be certain I am mindful of my mind wanting to do things that is not in my own best interest. So I don't add to my losing trades. That in itself means I just need to be mindful of the one variable I can control.

My action in the morning is about changing the patterns that do not serve me. It started by observing another very successful trader and asking myself what was holding me back from becoming him? My technical abilities were just as good as his. I don't think he was financially much better off than I, but he was seemingly fearless. How do I become fearless in trading? Do I even want to be fearless?

I came to the conclusion that the trader I wanted to become was patient and aggressive when the time was right. It was like Federer playing in the Wimbledon final in 2007. He was patient and then he became aggressive. Now it was a question of reminding myself of that goal every day, and if necessary, several times a day. That is how habits are built, through repetition.

As I grow wiser to the ways of life, I realise that there are a lot of truths to John Lennon's quote "life is what happens to you while you're busy making other plans". We become so engaged in our day to day life, with responsibilities at work and home that the big picture of our lives stays in the background.

Day after day, year after year we busy ourselves with work and routines, only later in life to realise that opportunities have passed us by. So the first question to address in a change process is, "What do you want to change?" Or, stated otherwise, "How would you like your life to be different?".

I want to dedicate the time to trade well, to combat my natural inclinations that stand between me and successful trading. I want to prepare my mind every morning through a series of meditations and visual exercises. I will train my mind to act calmly through visualising myself in the situations and focus on my breath. I will calmly put myself through stressful situations to ensure I react how I would want to react, if circumstances were real.

Making changes entails far more than simply engaging in positive thinking or getting positive images in your head. I didn't want positive images. I wanted a portrait of dire hell if I didn't change. It may seem like a negative state of being, but it really isn't. It is immensely positive, albeit a rather tense way of getting what you want. What is the saying: "the end justifies the mean"? I have turned conventional thinking on its head. I do so because I know what compels me more. Roses don't compel me. Thorns compel me to action.

Consider the market itself. It is not so unlike us in its behaviour (because we are it – we are the market). It climbs the wall of worry, but it slides down the slope of hope. It might be a Wall Street saying, but it says a whole lot more about humans than it says about the markets. All I have done is used fear and disgust as my protagonist – my major motivator.

Well, this is it. I am finally at the end of this journey. I hope my experiences and my battles with the "self" can inspire you to find a more fulfilling path in your trading.

So, rather than making a big fuss and a grand closing statement, I simply want to wish you Godspeed.

Yours sincerely

Tom Hougaard

Examples of my warm-up slides.

Dow 7 Jan 2019