ReadySetCrypto Trading Edge Masterclass

Module One: Why Do Retail Traders Suck At Making Money?

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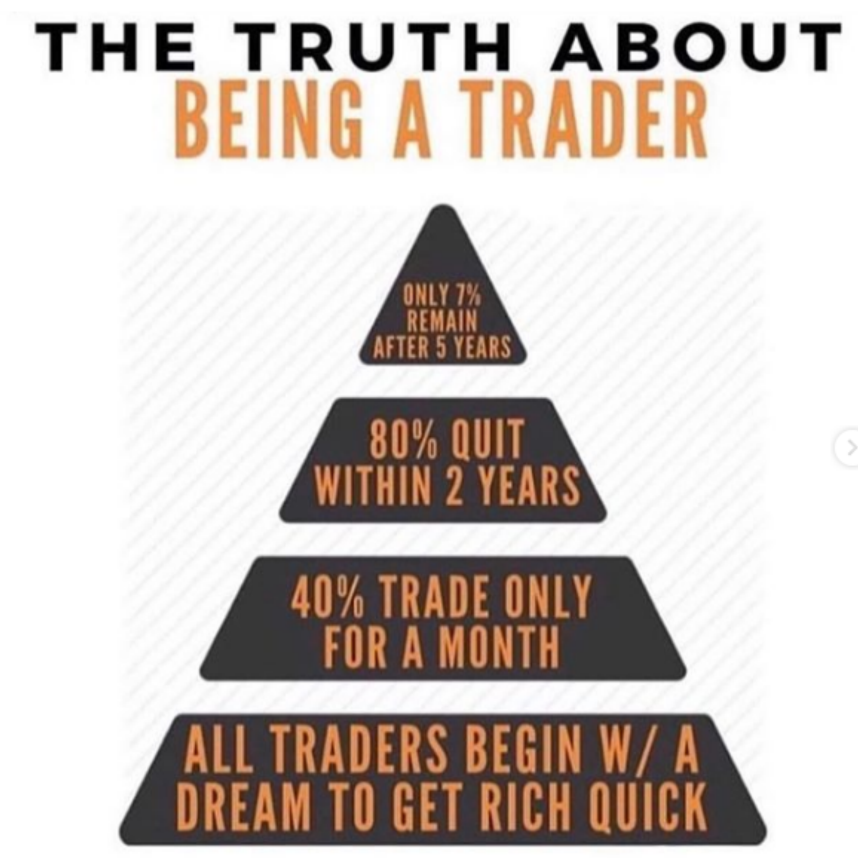
Retail Traders Suck At Making Money in Markets!

Look, if you know me, I don't usually start out a conversation by hurling out an insult, but I owe it to you not to sugarcoat the issue, and attack the problem directly. If you're a retail trader working in a non-professional environment trading your own capital, chances are very high that you're struggling for reasons that you can't quite explain.

The fact is that the vast majority of Retail Traders lose money. And everyone loses money, and continues to do so until they correct their approach to the markets.

They stumble into this venture like a drunk at the end of a "pub crawl," eager to sample the wares. They wake up the next morning, bloodied and bruised, not sure what occurred. And this scenario repeats itself again and again until you start making connections as to WHAT WORKS and WHAT DOES NOT WORK! And those answers are evasive, with some lessons being invisible until you've spent years at it.

This diagram from Instagram user @salarzaifx puts things into proper perspective:



The usual reaction to not achieving immediate success is to blame other forces, and the "usual suspects" come to light in every chat thread: market makers, whales, bears, institutions, dark pools, etc…in short, any entity that's larger than you are has suspect intentions (because they're different from yours) and MUST be the one that's causing funds to mysteriously remove themselves from your account.

I'm a realist; I know my own journey through this maze, and it was very similar to that of others. Your journey, should you decide to accept it, will likely be similar to mine. What I hope to accomplish in this program is to lay out the truth as plainly as possible for everyone to see, show you the WHY, and then show you what you need to DO to quit funding others' accounts and start keeping your fair share.

And it will not be easy. Trading is simple, but it's not EASY. And this is because humans process risk in an irrational manner. So I can tell you to do something, you can agree with me, tell me that you're going to do it…but when the moment hits, your "default response" will kick in and prevent success.

So that's our mission; you need to first understand why we are flawed creatures, and why your previous success at your career has very little bearing on your ability to create edge in a financial marketplace.

But if you're able to "hack" that cortex and understand why your brain does what it does, then you've taken the first step on your journey. You have to know the enemy, and it's YOU.

After all, you're not really trading against the market. You're actually trading against YOURSELF.

Let's start by understanding WHY retail traders suck so badly at this pursuit.

Retail Traders Don't View Risk Through the Right Lens

When I say the word "risk" to you, what is the first image that goes through your mind?

Perhaps you think of an image like Philippe Petit's amazing tightrope walk between the twin towers of the World Trade Center in 1974:

Talk about RISK, right? One slip and it's a long way down. But that's the first thing that most people think about, which is the ***negative outcome***. You think: "If I tried walking on that tightrope, I'd surely fall!" Was Petit thinking about that? Perhaps just a little bit, he'd be inhuman if he didn't, however in many interviews after the fact he talked about his PURPOSE or VISION of being the first to do walk between the towers. He focused on the REWARD first, not the RISK.

What other images come to your mind when you think of the word "risk?" The general connotation of the word "risk" is a bad one in today's society, is it not? Think of all the phrases that you're bombarded with on a daily basis:

- "That's a RISKY investment…"
- "This activity does come with some risk…."

We are taught from DAY ONE on this planet that RISK IS A BAD THING!

Let's go back to another "height" example since they're so visceral. For those that haven't seen the documentary "Free Solo," Alex Honnold recently became the first human to "free solo" El Capitan in Yosemite. (that means NO ropes or other means of assistance) It's an incredible movie and might be one of the most phenomenal feats accomplished by a human being.

Just imagine climbing a 7500' high (2300 meters) sheer granite wall with nothing more than your fingers and toes between you and a vertical drop that you would not survive. No parachute, by the way. (too heavy and cumbersome)

Was Alex focused on the RISK? No, he systematically removed the risk of the feat by understanding every inch of his ascent through dozens of "roped" test climbs. He knew that if he focused on the RISK of the event, that he would not be able to accomplish moves that required his absolute trust that the grip would hold. (i.e. "the Boulder Problem" for those that have seen the movie)

But humans like Phillipe Petit and Alex Honnold are beyond rare. They focus on the accomplishment of a feat and literally TRAIN the risk out of the equation.

So what do the rest of us do? **We focus on our fears first. And what we focus on will expand.** Who's to blame for this? We'll point at biology first.

The Fight or Flight Response

You may have heard of the "Fight or Flight Response." This was first described in 1914 by Walter Bradford Cannon as a "physiological reaction that occurs in response to a perceived harmful event, attack or threat to survival." [1]

You've all felt this before…something stressful happens such as a personal confrontation, and your reptilian brain alternates between different courses of action, such as punching the antagonist in the nose, or running away.

So it's in our BIOLOGY (programmed before birth) that we will react to stressful situations (like RISK!) by interpreting it as a threat and either fleeing or killing the source of our stress.

And did you know that the source of this interpretation (the Amygdala) in your brain cannot discern the difference between a physical threat and an intellectual one? (this is why an insult is often referred to as a "slap in the face")

As we'll see later in this program, this can be the source of a lot of unexplainable actions if we don't learn to process risk correctly, eliciting responses such as "*Why did I do that?!*" after a trade.

Retail traders suck at trading because they view their trades as a "threat" due to risk, and their default biological response is "fight or flight." And we know how well that works, don't we?

Parents Teach Us "Risk = Bad"

Your parents loved you and didn't want anything BAD to happen to you, so they erred on the side of caution when it came to that dirty word "risk." See if any of these sound familiar to you:

- "Don't play in the street, you'll get hit by a car!"
- "I don't want you playing that game, you'll get hurt!"
- "I don't like you hanging out with that boy. He's dangerous."
- Or in adolescence, "Why not pick a safe career like Accounting?"

[1] https://en.wikipedia.org/wiki/Fight-or-flight_response

I could go on and on but you get the point. Most parents will do ANYTHING to remove "risk" from your childhood, all in the name of protecting you to give you a chance at a long, healthy life.

So you attain adulthood with the mantra "risk=bad" firmly entrenched in your brain. And what's the first thing that we do when we get into any kind of investing?

You're going to look for the Holy Grail strategy that offers unlimited gains with little-to-no risk.

Retail traders suck at trading because they believe "risk" is the enemy to be avoided. And this practically ensures their fate due to this next statement:

<u>We Trade "Not To Lose," Instead of Trading To Win</u>

Have you ever watched a sports match where one team got a comfortable lead, almost assuring themselves of a win….and then they got cautious and started playing "prevent defense," or playing not to lose instead of continuing to "play to win?"

It's enough to make you want to tear your hair out if you're following the team with the lead. There are examples in every sport of this, but a really good recent one is the 2017 Super Bowl between the Atlanta Falcons and the New England Patriots. The Falcons were playing lights-out and were up 28-3 against the hapless Patriots. The Falcons were actually going to win their first championship! Just play conservatively, run out the clock, and the trophy would be theirs.

Have you ever felt like this before? You've got it "in the bag, just don't screw up!" Remember, what you focus on will "expand!"

Back to the game…the Falcons began to play "not to lose," instead of "playing to win" which they had been doing up to that point. You could literally feel the ground shift at that point as the Falcons went back on their heels and started playing from a position of "fear." It was the fear of giving up the lead.

Ultimately the Patriots scored 31 unanswered points and won the game.

And this is exactly how retail traders go about their business; we trade "not to lose" instead of "trading to win." And we do it like this:

<u>Retail Traders Crap Like An Elephant and Eat Like a Bird</u>

Well, visual vulgarity works if you'll remember this statement. And odds are, you will. What this means is that because we "trade not to lose," we end up taking very small profits when we do find a way to win a trade. And when we lose a trade, it's an enormous pile of fecal matter that will take some time to recover from.

Most retail traders focus too much on their “win rate,” because they equate that with success as has been drilled into them for their entire lives. A score of “95” on a test shows 95% correct and is better than 65%, right?

So the first thing that a retail trader does is to try to maximize their winning percentage, because it’s “natural” and builds confidence. But you can have a winning percentage of 90% and still lose money, simply because your profits are small (eating like a bird) and your losses, while rare, are huge. (elephant)

And all of these things happen because we’ve been taught that “risk is bad.” We focus on avoiding the negative outcome, and what we focus on will expand in our lives.

So we don’t know how to use risk to our advantage, and the “default” or “biological” way of processing risk often leads to MORE risk, or a WORSE outcome than we would have realized had we not “played it safe.”

So maybe in trading (as well as other pursuits in life) our biology and our well-meaning parents have steered us wrong. If you’re like most, you’re almost certainly not happy with the trajectory of your results, so let’s see some of the ways that our perception needs to change in order to realize profitable results…

There is No Reward Without Risk

You've heard the words "risk" paired with "reward" and there's good reason for that. The concept of "Reward," which is what we're all after, does not come without a cost. RISK is the currency of financial markets, and REWARD is normally commensurate with the RISK taken with any transaction.

Hiking across Antarctica represents very high risk, but your reward is also very high; not only for your life experience, but also being able to book yourself on the lecture circuit for the next ten years.

Hiking across New Jersey represents very low risk, and your reward will be little more than a new pair of shoes and a small mention in the local paper, asking the question, "WHY?"

So what is the FIRST thing that we do when we decide to tangle in the financial markets?

We look to minimize risk to the lowest possible level. The lower, the better!

And how do we "minimize risk?" In all of the worst ways possible:

- **Socially:** We ask friends and family what they "think" of our investments. After all, some of them went to Business School so they must know the right thing to do! Or we ask the common repository of collective intelligence, Twitter…where you can always get an opinion for free!
- **Emotionally:** We look for investing decisions that "feel good." Perhaps we have summoned the courage to put a fair amount of capital into a trade; we do what we've always done, wait until that decision feels "just right" before we pull the trigger.

Any of these sound familiar? It's perfectly understandable to REDUCE risk using the techniques that professionals use (covered later!) and professional traders absolutely reduce their risk before, and during a trade. But the professional trader is using RISK as an ally, as they use RISK MANAGEMENT to control their outcome in a trade, and not RISK AVOIDANCE which is the tool of the new retail trader.

One more time:

- Retail Traders view RISK as a negative "thing" to be avoided, so they practice RISK AVOIDANCE.
- Professional traders view RISK as desirable, and an essential component of any trade. They practice RISK MANAGEMENT to leverage risk in a controlled manner.

The two methods are night and day different.

Making The Decisions That Feel Good

Humans celebrate those who have “intuition” or a “gut sense” of what to do. After a while, you get good at your job and you’ll intuitively know exactly what to do.

A new driver hitting snow & ice for the first time will overcorrect and ultimately just lock the brakes up in a panic when they lose control. An experienced winter driver can negotiate hazardous conditions with a light touch on the controls and is able to counter-steer their way out of trouble, without resorting to stomping on the brakes. They don’t have to THINK about it, it’s intuitive.

And you will bring this sense of “intuition” to the financial markets based on everything that you have experienced in your life to this point.

You’ll think that it will allow you to profit from it. In the vast majority of cases, you will be dead wrong. Think about some of the underlying biases that we have been taught that everyone just “accepts:”

- Risk is Bad.
- A high winning percentage is good.
- Protect those profits!
- You can’t lose money taking profits.
- A trade is not a “losing” trade until you actually close it!
- Stress: Fight or Flight response.
- Asking others will bring you a clearer sense of what to do and make you feel better about your decision.

These are all of the “common sense” elements that you think will bring value to your trading. After all, “common sense” is very valuable in a work environment. The brilliant (but impossible) engineer might just invent the next viral app, but in the process of doing so, they might be absolutely impossible to deal with in the interim. Most corporate environments reward the steady, dependable, common-sense knowledge worker whose years of experience tend to come in handy now and then.

(I’m not denigrating those skills, there’s a lot of value to that in a shared workplace)

But there’s ALMOST ZERO benefit to “common sense” in the financial markets.

Think of the term; “common sense” really means “to think for others.” And using others’ opinions and judgment in financial markets is suicide.

Think about the last time that you went to a big sporting event, especially if you were rooting for the “home team.” One of my favorite things to do in college was to watch football on a Saturday afternoon with 80,000 of my closest friends. We all cheered for the same players and the good plays. We booed the refs and the other team. Life was good, being part of a big happy family like that, especially if we won the game.

And this is how many retail traders like to invest; ASK THE INTERNET! It works for everything else, doesn't it? You trust those Amazon and Yelp reviews, don't you? Without question! We now have an entire generation that can evaluate purchasing decisions without lifting a finger. And we've learned to "socialize" our decisions in this manner.

And there's not a more dangerous thing that you can do when you trade. This automatically makes you part of the "investing herd."

What are the decisions that "feel good" to make in the financial markets? The ones where you are going along with the rest of the crowd.

You don't know it yet, but that "feel good" trade is likely not going to work out for you.

What are the decisions that "feel bad" to make in financial markets? The ones where you are on your own, taking a contrarian viewpoint to everyone else. You begin to have doubts, because everyone else is telling you that you're wrong.

It's very difficult to make the decisions that "feel bad" in financial markets. But after a while, you'll start to see a correlation between "how bad" a decision feels…and the positive results.

I summarize this effect to my students in one sentence: **"The very best trades that you'll take will feel absolutely horrible to enter."**

So avoid trading with the crowd by asking everyone else for their opinion. Think independently and take the hard setups to put yourself on the other side of the crowd.

Expecting Linear Success

Many people venture into the financial markets after several successful years at their job, and assume that they can expect the same linear path to profits. I once had a Dentist ask me, "*Doc, I knew that when I entered Dental School, that I would spend four years there, then another year of residency, and after that I would have an expected return by going into practice. Why can I not expect the same thing with investing?*"

Great question.

My experience with this quandary has been that heaping on additional knowledge in the art and science of trading can provide some incremental improvement. Some of the "linear" steps that you can take would be, for example:

- Learning more accurate chart reading
- Limiting your activities to very specific instruments and timeframes
- Learning new trading strategies
- Learning to "read" market character and adapt your strategies.
- Learning more financial fundamentals
- Learning better risk management

And the list goes on and on and could take up pages. The point here is that you could learn about Every. Single. One. of these concepts and could spout chapter and verse about different concepts at lectures and parties.

Yet I would put you in front of a live market and you'd be paralyzed with indecision.

All of the "book knowledge" in the world will not make you "Market Smart." There is no linear correlation to how much technical information that you pack into your skull…to your trading performance.

Until….you learn how to deal with ONE specific point. It's this:

Human beings process risk in an irrational manner. And it's particularly evident when humans get together and process the same risk collectively.

And this is why the investing "herd" gets it wrong.

When "everyone" sees the same thing, they're about to be wrong.

And this is why "frothy" markets that are vaulting higher attract everyone out of the weeds, fearing that they will "miss out" on this historic move (i.e. Bitcoin December 2017), and markets that are selling off hard causing everyone to be completely negative….will typically see rallies come out of the blue which no one believes until it's too late.

So humans interested in attaining success in the financial markets will attain *some* success if they go through the usual “linear” path of piling on more book knowledge, but until they understand these two things, they will not retain profits:

- **How the investing “herd” processes opportunity and risk in an irrational manner..**
- **And how YOU process opportunity and risk in the manner that you’ve been taught…**

And this is the “crux of the biscuit” that we need to fix.

The investing “herd” will forever get it wrong. And you need to learn how to identify the behavior of this “herd” and move in an OPPOSITE manner to them.

And YOU have been thinking about RISK in the wrong manner for your entire life, and will have to start making small, incremental changes in how you process risk.

The “common sense” things that you “think” will make a difference in your ability to create and retain profits….will NOT work in financial markets.

In short, nearly EVERYTHING that you’ve learned that makes you a smart, valuable person on this planet….will work against you in your quest to create profits in financial markets!

Linear success can happen, but only if you’re willing to push the big red “reset” button and unload the baggage that you assume is helping you.

Summary - Why Do Retail Traders Suck At Trading?

OK, if I haven't repelled or insulted you too badly yet, and you're still here….congratulations! There's hope for you in this world of trading.

Either you will learn these concepts the hard way like everyone else, and quite frankly most don't learn them at all, before quitting and claiming that the "game is rigged!"

….or you can start today to embrace your human traits and figure out which ones are impeding your progress.

Yes, the financial markets offer a continuously flowing river of opportunity that can provide you the life of your dreams….but no one tells you that you basically have to RE-WIRE how your brain processes risk, and that you MUST learn to think independently. You cannot do this on your terms! These are not cafeteria-style skills that you can pick and choose, unless you want to continue to contribute to others' trading accounts.

Here are just a few of the concepts that we'll work on in this program:

- Learning to think of the word "risk differently
- Learning to stop looking to others for guidance
- Learning to think independently
- Learning to make the tough decisions
- Learning what works…and what does not work from your life experience

Most of these will go "against the grain" in what you either THOUGHT should be important to investing success, or were TOLD would lead to success. (mostly through TV commercials)

This is not an easy nor simple journey. But oh is it worth it…

Homework and Next Steps

Please complete the following tasks before moving to the next module:

- [ ] Watch the associated video for this module.
- [ ] Look at some of the trading decisions that you've made in the past; were they influenced by social media or financial media sources?
- [ ] What was the last "feel good" investing decision that you made? Did it work out?
- [ ] Have you made any investing decisions that felt terrible to enter, yet worked out?
- [ ] Have you made any investing decisions while emotional, like a "panic sell?" Did it work out for the better?