Fear: Traders' Thought Demon (Part 1)

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by Dan Gramza

The business of trading can be fertile ground for negative thought choices. If you let them, these negative thought choices can become your demons and sap your positive mental energy. By identifying and understanding the realities of these thought demons, a trader is better able to redirect energy away from them and diffuse their power.

The most common thought choice demon for traders is fear. Traders encounter opportunities for fear on a regular basis. If allowed, fear will confuse and emotionally paralyze a trader.

A fear can feel overwhelming and difficult to handle when it is being consciously or unconsciously experienced. Fear can create the envelope of our reality because the fear can determine what we do and avoid doing so that we do not experience the fear.

Fear is a reaction to a memory of a past experience which leaves the thought, "I will never do that again." Fear can also be the anticipation of an unknown, future event, or a "possible" future outcome. It can range from apprehension to dread. The intensity level of a fear is directly proportional to the amount of energy we choose to feed it.

Thought choices that support fear provide a great example of how we create our reality and what we experience. For example, a trader sees a wonderful trading opportunity but is frozen in fear and does not take it. His fear could be a memory of a past trade that didn't work, or as protection against a "possible" losing trade and what he perceives will result in emotional pain if the trade does not work. However, what the trader doesn't realize is that when he was frozen in fear, he was experiencing exactly what he was fearful of – emotional pain at that present moment in time. He was experiencing his fear in the present, not in his anticipated future. His fear was emotional pain and he is experiencing, consciously or unconsciously, this emotional pain at the moment he was frozen in fear and unable to make the trade.

It is important when sensing fear, to pay attention to breathing. Often, when a person experiences fear he tends to hold his breath or to breathe in short and inefficient shallow gasps of breath. Both of these breathing approaches will increase intensity and heighten his fear and anxiety. Taking slow deep breaths is very important in assisting the trader to control his fear reaction. The deep breathing will allow more oxygen to circulate to the brain and help the trader stay focused.

Let's examine and de-energize some of the most common trader fears:

Losing Money

If a trader chooses to be afraid of losing money, there are two things he should consider:

1. **Any time money is used to make money there is a level of associated risk.** The intent of a trading business is to have money make money. Therefore, there is an associated risk of losing money in trading. If the idea of losing money is very uncomfortable for the trader, he should examine this fear. If the trader cannot get beyond this fear, the conclusion may be that he should not be trading.
2. **In any business, not every business decision will make money.** This is also true in the trading business. There is a high level of certainty that no matter what trading techniques are used, not every trading business decision will make money. Therefore, by the very nature of the trading business a trader will have losses. Keep in mind, it is not the profit or loss from one trade that determines the success of a trading business. Rather, it is the total trading profit from a series of trades.Since not every trading decision will make money, the key is having appropriate risk management parameters that do not overexpose trading capital to any one trade. Since the trader

never knows with absolute certainty which trades will be profitable, only trades that completely comply with every aspect of the trader's trading strategy should be entered. In this way, every trade has an equal chance of being successful.

Lack of Control

A trader who doesn't understand the difference between the aspects of trading he controls and those he does not is in for a rude awaking. In general, people try to control a situation in order to get what they want or in order to avoid surprises and the experience of fear.

This approach does not work when applied to trading. The trader soon finds out he does not control the market's behavior. Even large traders' influence on the market is only temporary. The fact is, no trader can control the market, and this lack of control can be unsettling for some. A trader may hesitate putting on a trade, or feel that he is out of control and doesn't know how to take the next step.

These are elements of the trading process that you do not control:

1. You do not control the market's reaction to fundamental information.
2. You do not control the market's price movement.

These are elements of trading that you do control:

1. You control your acceptance of the risks involved in trading.
2. You control your choice to reduce risk by identifying techniques that have a high probability of success.
3. You control your level of risk by determining how much of your trading capital will be allocated to the trade.
4. You control your choice of when to enter a trade.
5. You control your choice of when to exit a trade with a profit or loss.
6. You control your choice of when to add to or reduce a position.
7. You control your choice to transfer risk by using hedging or spreading techniques.
8. You control your choice to eliminate trading risk by deciding when not to trade.
9. You control your choice of how you emotionally react to profitable trades and the inevitable unprofitable trade.

As you can see, the aspects of trading you do control far outnumber those you don't. It is not necessary for the trader to be in control of the market to establish a profitable business.

Failure

Many traders consider failure to be a missed trade or a monetary loss. Fear of failure, as they define it, causes them to hesitate when putting on a trade, or not making the trade at all. Some traders may even take an unproductive trade personally and believe that they are the failure.

The fact is, missed trades and monetary losses are part of trading. True failure for a trader is not following his trading game plan.

This means not entering a trade, taking profits or taking losses when required by his trading approach. The trader who chooses to take the results of a trade personally has put energy into the belief that the outcome of a business decision reflects who he is as person. This is a mistake, and deadly for a trader.

The good news is that these are all areas you, as a trader, control. It is your acceptance of the risks associated with trading, your understanding that each trade is a business decision and nothing more, and your discipline and consistency in applying your trading strategies that will determine the productivity and success of your business.

Emotional Pain

Instead of taking responsibility for their trades, some traders believe that the market is intent on causing them emotional pain with each losing trade. They forget that no matter what source of information they used to make the trading decision (broker, newspaper, newsletter, hot tip or their trading system), the trade is their responsibility once it is executed.

The fact is that the only emotional pain a trader can have is self-inflicted. There is no emotional relationship with the market, except what the trader imagines. The market is an entity that brings buyers and sellers together and that's it. It does not know that you, as a trader, exist. Nor does it care about who you are, your feelings, your social status or how much money you have. This makes the market your perfect, unbiased trading partner.

Taking responsibility for trading decisions and consistently following your trading game plan are key to eliminating the potential for self-inflicted emotional pain.

Missing a Trade

Many traders fear the missed trade. No matter how great the trader thinks the missed trade was, there will always be another trade, just as good, at some point in time. The chance of a trader missing a trade drops dramatically if he is trading in the present moment with an awareness of his markets, and consistently following his trading strategy.

Hesitating to Enter a Trade

A trader may hesitate or abandon entering a trade because he senses his own fear. His conscious or unconscious interpretation is, "If I am sensing fear, then I should not be doing this trade." The bottom-line reason why a trader hesitates is because he is not totally confident in his trading strategy or in himself. He can change this by properly researching and understanding his trading strategy, and by practicing the techniques I've identified to help increase his confidence.

Staying in a Profitable Trade Too Long and It Becomes a Loser

The major reasons why a trader fears overstaying his welcome in a trade and allowing a profitable trade to become a losing trade are:

1. **The lack of predetermined profit exit criteria.** The trader never determined under what circumstances he would capture profits. Whether it is a change in fundamentals, a magnitude objective or a change in technical analysis parameters, the decision of when to exit a trade must be determined before a trade is entered. Otherwise, the trader runs the risk of letting profits slip through his fingers, as well as of providing himself with an excuse to become emotionally involved with trade.
2. **The fear that if he exits a profitable trade, the market may continue and he won't capture "all" the profits.** The trader is forgetting that if he establishes parameters for re-entering a trade, he can get back into the trade if the trend continues. He is also forgetting that profitable trading occurs by consistently following his personally researched trading strategy, not by always buying the exact low or selling the exact high of a market.
3. **The trader becomes comfortable, lazy and emotionally attached to the trade.** He forgets that a trade is a business decision and nothing more. When exit criteria are reached, the trade is exited. Period. There is nothing to think about or discuss.
4. **The trader held the position through other pullbacks and it eventually continued in a favorable direction.** The trader's approach worked because the pullbacks were profit taking moves* and the trend continued in the previous direction. There will be times, however, when the pullback is not profit taking, and the market <u>will</u> change direction. The trader must be prepared for

all contingencies.

5. **Greed drives the trader to hold on to the trade.** A greedy trader will never be successful because he will never be satisfied with his profits. This trader will over-stay his welcome in the trade because he will want more than the market can give at any point in time.
6. **The trader begins to think of how he will spend the trade's profits and refuses to exit as he sees his spending plan disappear.** He forgets that the profit in the trade is not his until he closes the position.
7. **The trader steps out of his trading strategy profit exit and begins to hope for more profit than his trading strategy can provide.** The trader forgets that his hope is irrelevant to his trade. The price behavior and his trading strategy are his guides, not his hope.

*A profit taking move occurs when prices temporarily move in the opposite direction of the current trend. For example, a bullish trend is in place moving prices in an upward direction. A downward bearish countertrend move is caused by sellers who previously bought and were long the market, who now want to take profits. To do this, these traders exit their positions by selling and closing out their previous long positions. If there are enough sell orders from long traders selling to overwhelm the buying orders coming into the market, a bearish countertrend will begin, moving prices downward. This bearish countertrend will sustain this downward movement as long as this profit taking action is in place. Since the cause of the countertrend movement is the profit taking actions of long traders, the overwhelming sell orders will stop when they finish taking profits. At this point, there is no reason for the countertrend move to continue, and the bullish trend will continue in its original upward direction. The opposite is true when sellers are buying to take profits in a bearish trend.

Panicking and Staying in a Losing Trade Too Long

The major reasons why a trader fears panicking and staying in a losing trade too long are:

1. **The lack of predetermined risk management loss exit criteria.** The trader never determined under what circumstances he would exit a trade with a loss. Just as with the profit exit, whether it is a change in fundamentals, a magnitude objective or a change in technical analysis parameters, a decision of when to exit a trade must be determined before a trade is entered. The worst time to decide when to exit a losing trade is when the losing trade is occurring. If the market is moving quickly or slowly, the trader can become emotionally involved with the trade and frozen in inaction as he sees money being drained from his account.
2. **The trader is emotionally involved with the trade and cannot bring himself to take the loss, learn from it and move on to the next trade.**
3. **The trader forgets that not all of his trades will make money.** He continues to stay in the trade hoping the loss will change to a profit. He forgets that a trade is a business decision and nothing more. When exit criteria are reached, the trade is exited. Period. There is nothing to think about or discuss.
4. **The trader thinks exiting the trade will somehow mean that he has been "wrong," so he continues to hold on to the losing position.** The trader forgets that trading has nothing to do with being right or wrong. A trade is either a profitable or unprofitable business decision.
5. **Greed drives the trader to hold on to the trade.** A greedy trader will never be successful because he will never be satisfied with his profits.
6. **The trader steps out of his trading strategy and begins to hope the trade will work.** He is not consistently following his trading and risk management strategies and he is setting himself up for disappointment, frustration and inconsistent trading results.

Uncertainty of the Future

Successful traders know that the market can do anything at any time. They realize they cannot predict the future, so they don't waste their time trying. They also understand that the results of each trade are independent of each other. They do not carry emotional baggage from the outcome of profitable or unprofitable past trades. Instead these traders focus on the opportunity the market is presenting at the present moment, and the application of their trading strategy. If applied correctly over time, the trading strategy will provide them with a profitable result.

Being Embarrassed and Losing Face

The only embarrassment in trading is what the trader creates. Remember, the market is the ideal, unemotional, non-judgmental, impersonal trading partner.

Some traders, whether on the floor surrounded by other traders or behind a computer screen and talking to a broker, let their egos interfere with running their trading business. They fear embarrassment or losing face and allow their perceptions of what others may or may not be thinking determine how they manage their trades. Such a trader may not exit a losing trade because he just put the trade on and he feels it would be embarrassing to exit so soon. Instead, he stays in the trade, suffers an even greater loss, and exits the trade only when his pain from the loss is greater than his fear of embarrassment. He thinks he has shown them that he's tough, he can take it, and he showed the market who is boss.

This emotional baggage is totally fabricated by the trader. The only thing he has shown is that he is not a very good businessperson, and he has emptied the money from his account trying to prove that he is right. The business of trading is not about being right – it is about making money. His focus should be consistently applying his trading strategy.

Being Wrong

The concept of "being wrong" implies there is a personal connection between a trading decision, which is an impersonal business decision, and the outcome of a trade. It is dangerous to make a personal connection to the outcome of the trade, because it mixes the trader's self worth with an impersonal business outcome. A trade is only a trade. There is no personal connection to the outcome of a trade unless the trader consciously or unconsciously creates one.

The fear of being wrong is further magnified when a trading decision is not productive and the trader takes it personally. He begins to feel consciously or unconsciously that he is incompetent, a bad person or an unworthy person, and he stops trusting himself. The result is that at the next good trading opportunity, the trader hesitates to enter the trade and an opportunity is missed. The trader then sees the profitable results from the missed trade and, instead of bolstering his confidence in the fact that his trading strategy works, he becomes frustrated and less confident.

This trader is not afraid of the market. He is concerned with his ability to trust himself. Instead of thinking in terms of "right" and "wrong," he can describe the results of his trades as productive or unproductive, profitable or unprofitable, or cooperative or uncooperative. This depersonalizes the trade results and keeps them in the proper perspective.

Summary

As a trader, what fears have you created? We create our fear by using past experiences or anticipating and imagining what the future will hold. We do not control the past or the future. We do control our reaction to the present moment. If we spend our time thinking about what has happened or what may happen, we are not in the present moment and we are not exercising our control over our reaction to the current situation. The result is that our fears become our reality, and this reinforces our fear belief system.

Overcoming fear is self-empowering, and it builds confidence to deal with future challenges. Remember, the only limitations you have are the limitations you impose on yourself.

This article is an excerpt from Daniel Gramza's book: *Trading in the Eye of the Storm.* Part II of this article follows in the next post.

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