THE PLAYBOOK

AN INSIDE LOOK AT HOW TO THINK LIKE A PROFESSIONAL TRADER

MIKE BELLAFIORE

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The PlayBook

An Inside Look at How to Think Like a Professional Trader

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To my dad, who teaches me the most valuable lesson: work ethic

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Mike Bellafiore is the co-founder of SMB Capital, a proprietary trading firm in New York City; SMBU, their education arm; and SMB Systems Trading, their algorithmic trading division. He is the author of “the trading classic” *One Good Trade*. His firm has regularly appeared on CNBC, Bloomberg TV, CNN Money, Fox Business, the BBC, and in the *Wall Street Journal* and the street.com. SMB’s trader training program was highlighted on the TV documentary *Wall Street Warriors*. An international lecturer, Mr. Bellafiore has built trader training programs globally for hedge funds, prop trading desks, and retail traders, working with some of the world’s largest traders. He lives on the Upper West Side, with his wife and newborn son.

Introduction

> Weaknesses don't matter if you find solutions.
>
> —Ray Dalio

The PlayBook will help you become a better, bigger, more profitable, increasingly efficient, well-rounded, calmer, happier, and grateful trader. This book teaches you how to make more of the trades that make the most sense to you, with larger size, holding them for the real move, so that you boost your trading P$L. It will gift you with the tools to realize what I argue should be your ultimate goal: becoming *your best trader* (YBT). The PlayBook is the derivative of something good coming from personal hardship (mine, as it turns out). Let me tell you how it all happened and how the PlayBook can transform your trading performance.

***

I was in my hotel room in Phoenix, Arizona, preparing to talk to the Scottsdale–Phoenix meet-up group when my BlackBerry vibrated. It was my mom.

"Michael, I am so sorry to tell you this. Your father has had a stroke. It's not good. I don't know what to do."

"Here, please talk to your father," continued my mom.

She put my dad on the phone. Well, more accurately a man's voice came to the phone. It could have been my dad, but it was hard to tell. The man on other end of this phone clearly had had a stroke. "Hello" was "Hawooooh" and with great strain from the speaker. The man gave the phone back to my mom.

"Mom, let me check when I can get out there and call you back."

"Okay, thank God. Thank you, Michael."

I hung up the phone, went to Kayak.com, and punched in an airline search for from Phoenix to Tampa. My hands felt frozen from the shock. I could arrive very early the next morning if I left in the next hour, or in the early afternoon with the first flight out the next day. I thought: Seriously, you can't get from Phoenix to Tampa in a few hours. Driving would take forever, the same with a bus, and there were no trains.

Guilt for my inadequacy to immediately be in Tampa persecuted my mind and body. In 46 minutes, I had a commitment to give a lecture to a group important to me to support and for which I'd flown across the country. But my family needed me. I needed to be in Tampa for them urgently. Should I bolt to the airport, cancel my presentation, and land in Tampa early morning the next day? Should I do the talk and head out on the first flight the next morning? I called my wife. I called my sister. I called my mom. This was my prisoner's dilemma. We decided on the first flight out the next morning. I hated this decision.

I arrived at the venue for the Scottsdale–Phoenix meet-up, which to me appeared like a quintessential location shoot for those political town hall meetings. *And now running for the Scottsdale city council, please help me welcome candidate Mike Bellafiore.* What was I doing here? None of this was helping my mom or dad. I was physically present while my mind was observing the absurdity of my presence.

So I went and did it: I stood on my feet for three hours talking to a room full of mostly retired investors. I had painstakingly prepared a talk on short-term trading setups, but after one look around the room of this friendly senior citizen crowd, I scrapped my prepared remarks to engage this demographic. I got lost in our talk for a few hours, with appreciative attendees coming together as a community, a trading community. They were admirably in attendance to learn more about the markets, meet some new people who invested like them, and perhaps spend a night away from mindless reality TV. There cannot be enough great meet-ups for investors/traders across the United States. People like me have an obligation to support them. Such communities make our markets better for the plain reason that a well-educated trader class manifests a better market.

I gave that audience everything I had, answered every last question, and shook each hand with a smile such that no one detected my personal hardship. *Just like my dad would have done.* Engrained in my memory is a snapshot of my dad on his hands and knees, paint, dirt, and muck smothering his work blue polo, improving a family property for one of his tenants. This is work ethic. You do things as well as you can because what else is there?

At 9 p.m., I walked out of the hall exhausted, on-the-road famished, and about to face one of the most difficult years of my life. I drove my rented mid-size back to my resort hotel, asked for a 3:30 a.m. wakeup call, and passed out soberly, still in my suit and shoes.

BAA-RING!!!!

BAA-RING!!!!

My next conscious moment was the phone in my room ringing as I awoke feeling as if a 300-pound lineman had just sacked me. The early hour brought me that sleep-deprived physical pain, stomach discomfort, and uncomfortable head pressure. Somehow I got on a plane, with my bags, and touched down in Tampa.

I called my mom.

“Hi, Mom. I’m here.”

“Oh, Michael, thank God you’re here. Your father is at Morton Plant Hospital. Do you know where it is?

“I’ll find it.”

I walked into my dad’s hospital room, my mother sitting across from him, pale and trying to force an unworried smile. When her first-born son entered a room, my mother usually stood and made me feel like there was nothing else more important than me. She tried this now-impossible task while living her life-changing moment. I looked to the right at my dad, smiled, but inside was *astonished*. He couldn’t talk. He couldn’t move. He couldn’t lift his hand. “Michael” was “Mikahhhhh.” The strongest person I have ever known was now as fragile as a newborn.

This was so much worse than my mother had explained. I made happy small talk, unsure when to stop the farce. After this absurd hospital custom, my mom grabbed my arm and pulled me into a private room a few doors down the hall.

“Mom, people make full recoveries from strokes. Let’s not assume anything. When can we get him rehabbing?”

Okay, at this point (or well before, and if so, thank you for your patience), you might be wondering why I’m sharing this personal story with you, an account that has yet to say a single thing about trading. As it happens, this drama is pertinent, as you are about to see. And if ever there is a person who can inspire you to improve everyday as a trader, or serve as an allegory for the path of the new, developing, or underperforming trader, it is a recovering stroke victim. Further, an event like this helps traders place their work in the proper context. No one has ever lost a loved one in a losing trade. More to the point, the PlayBook might never have been born without this calamity.

* * *

Fast-forward (and bypassing medical bureaucratic details too numerous to recount), we finally freed my dad out of the hospital and into a 24-hour rehab center, where he (and I to a lesser extent) would live for the next 2 weeks. I write often on the SMBU blog that trading is an exercise in getting better everyday. A stroke victim personifies the ultimate real-life, all-consequences example of a struggle to get better each day. Your brain has been injured. New connections in your brain circuitry to control walking, speaking, and thinking must be remade. Harder still, you must do all of this in the autumn of your life, when you're supposed to be slowing down and enjoying the rewards you worked your whole life to reap.

Building your PlayBook is a similar test. As a trader, you must make connections in your trading brain for the setups that make the most sense to you. Then you can execute these plays as automatically as you breathe, walk, and talk. But before, each trade is a struggle of indecision and uncertainty. More about this soon.

I called Steve Spencer, now one the most recognized U.S. equities traders in the world, the best man at my wedding, and my partner at SMB. "My dad has had a stroke. I am going to be here for a while."

"Okay, stay as long as you need."

I didn't wonder for even a moment whether I would help my dad in his rehab. There were only moments when I questioned whether I needed to do more. My dad had given me so much. We ate dinner together every night during my childhood. I cannot recall a game he ever missed. He never declined a throwing session, which led to me becoming a college athlete. College. Law school. Now I would be there to help him.

Day one of rehab was one of the better days of my life, during the worst period of my life. I love the science of performance enhancement and saw it all-day, in real-time, inches from me. We went to speech therapy, physical therapy, and occupational therapy. Dad couldn't do much, and everything was so difficult. Picking up a sandbag during occupational therapy was impossible. I had to lift his back to get him into a bridge position during physical therapy. He still really couldn't talk. In a lighter moment, we got into trouble during speech therapy for not following one of the rules. Threats were made at us, and angrily. We laughed and laughed and laughed some more about potentially getting kicked out of the rehab home. As if there is anything really bad that can happen to you after having a massive stroke or seeing your hero after he has had one.

By the end of the day, Dad improved. He had the infrastructure to make progress, like a new trader must. And he was determined with every breath and thought to get better. Mom used to say she never met anyone as determined and focused as my dad. The rehab center was seeing that. He worked.

I returned home that first day to our Clearwater Beach family condo, which overlooks the Gulf of Mexico at one end and Tampa Bay on the other. My mom, obviously anxious and eager to hear my report, sprung up from her reclining chair upon my arrival. "Mom, he is going to make a substantial recovery."

"Oh, Michael, that is such wonderful news."

For the next ten days, I woke early, grabbed a few protein bars, and headed over to the rehab center to spend the day with my dad. I had in my head that the more he moved and thought, the better he would get. Sort of like the more screen time you get as a newb, the more you improve. During rest breaks, I asked him to punch my hand. By day three, he could. I would move my hand up and down, and he would slap at it. You could sense his brain struggle to figure out how to get his arms to hit my hand.

It was also hard to miss how my dad outworked the others in rehab (and by a large margin). Many did enough not to get in trouble, literally stopping their reps when the staff stopped looking. My dad did extra reps.

After every rehab set where I noticed progress, I praised him. We built from the positives. I would tap his stomach and say, "Good set" or "Good work, Dad." The trading coach in me knew that to sustain his motivation I had to encourage the effort and not the result. I knew that act of touching would help reduce his stress and communicate we were in this together. Before I headed home after day five, I pulled his chair right up to mine, waited for his eyes to meet mine, smiled, and said unwaveringly, "You are going to make a substantial recovery. People can make remarkable recoveries from strokes. Keep working. You are going to get better." I could have been talking to one of my traders.

I sensed he wanted to get better *for me.* Of course, he wanted to improve for himself, but he also wanted to get better for me. I wanted (no, needed!) him to get better, and he read that. I see this behavior in my traders with whom I am close. They do not want to disappoint *me.* Coaches who love their players will see them do almost anything not to disappoint them. Love is a powerful motivator.

During speech therapy, my dad earned the nickname "Friendly Frank" because he gabbed with everyone in the facility. Friendly Frank grasped that he needed to talk as much as he could to expedite his speech progress. So he talked to everyone. He was working to get better and enjoying himself with his latest challenge.

There were periods of frustration to overcome. On one particular day, my dad got discouraged at a lack of staff attentiveness. He directed unkind comments at their competence and performance. He was acting like a trader on tilt. I had to keep him focused on his task. When Dad started complaining about bad service, I refocused him on the only thing that was important: our day of improvement. I told him to count to ten when he got mad, and to take deep breaths between each number. All that mattered was that he play as much as he could with his rubber bands and speech exercises and jabbing drills we had created to speed his recovery. I could have been talking to one of my favorite traders moaning about *high-frequency traders* (HFTs). In trading, we say, "One Good Trade and then One Good Trade and then One Good Trade." (I hear there is a pretty good trading book by this title.)

My wife flew down for Christmas. I hadn't seen her for a few weeks at that point, which was just two months after our wedding. She got a kick out of seeing my dad working so hard, stopping to talk with everyone, and answering every question asked to the rehabbers during group therapy.

"Frank, don't raise your hand. You can't answer every question."

"Why not?"

She laughed. My dad and I laughed. We all laughed again together. He had a point. Why not?

On day ten, my dad stood, placed his right hand on a handrail, and walked 40 yards up the rehab hall and then back. Wow! He was going to walk again! I couldn’t wait to go home and tell my mom.

The prior four nights my mom had been very ill. She had a history of stomach issues and couldn’t keep anything down. She wasn’t sleeping. Her back was terminally screwed up, and she was in constant pain. I found her pacing our condo in the middle of the night trying to relieve her back pain. Doctors say one of the mistakes a family makes is not looking after the spouse of the stroke victim (in this case, my mom).

Before my wife and I left the rehab center that day, my dad asked me to go check on my mom. Ever selfless, he was first worried about her and her health. As hard as life had been after taking that call about my dad from my mom, it was now about to get worse.

My wife and I grabbed some dinner at the mall in Tampa and then headed back to the condo. I opened the door and found my mom face down on our kitchen floor.

I sprinted right to her, turned her over, and found a huge welt above her left eye, which had absorbed her fall. I called 911. “My mom is unconscious. Send an ambulance.”

“Okay, sir. Where are you?”

I answered.

“Is she breathing?”

“How do I tell?” And on it went.

“Clasp your hands together and push against her chest. I will help you with the tempo.” And the guy was going, “And push and push and push and push.” My mom was covered in sweat and obviously dead, and here I was, in my opinion, just hurting her body.

“Mom, please wake up. Mom, please wake up.”

Seemingly hours later, really approximately 15 minutes, the paramedics and police arrived. Like some *CSI* episode, the paramedics took over and applied machines and technology to my mom. In cases like this, the police look around. They ask you questions. You show them your license. They are doing their job, and their presence is comforting, but you cannot help but think, “Does anything else matter but that my mom is obviously dead? How in the world am I going to tell this to my dad?”

We followed the paramedics to the nearest hospital. Well, we started to, but then got lost. We eventually arrived, and then waited in the waiting room (never has a room been so aptly named). It was bizarre: I was certain my mother had passed, but we were waiting around as if she had an ankle sprain and were anticipating X-ray results. I called my sister.

"We're at the hospital. Mom had an accident."

Now, you wait, and you know what they are going to come and say. They hand you a plastic bag of your mom's possessions. Strange thoughts drift about like, "God, is that a ginormous diamond necklace she wore!" They escorted us from the waiting room into an exam room and told us the doctor would come with news. News? The doctor is going to come and tell us that my mother is dead.

Some young, sweet Indian doctor and kind-eyed nurse entered the room. *Well, this can't be good.* The nurse was obviously there to help us with the grieving. If it were good, there would be no nurse. This must be protocol.

"I am so sorry to tell you that your mother has passed away. You can go and see her now." I entered the room and felt more grief than one should possibly have to bear. And I felt an awful and strange protective guilt for the trauma to which I had just exposed my wife. How could I have missed not paying more attention to my mother?

My sister flew down on the next day, Christmas, with my then one-year-old niece Kate. My little sister had ordered me not to tell my dad until she arrived. Mom always said, "Never awake anyone with bad news. It can wait until the morning." It's funny the things you never question said by your mom.

We found my dad. I wasted little time. "Dad, we lost mom last night." My heart broke looking at my dad's face as he absorbed this news. We brought in Kate to play on Poppa's lap, desperate for some way to distract.

Over the next several days, we flew my dad back to Long Island, buried my mom, moved my dad into a rehab center in our hometown, and kept moving.

During all of this, the markets don't close, the competition in the trader education space doesn't discontinue business, trading systems need tweaking, and my traders require coaching and direction. Deals have to be negotiated, calls returned, and problems solved. But I wasn't able to work. I had lost my mom, and my dad needed my help. I was emotionally unavailable.

Later, at a conference in Singapore, I proclaimed that starting SMB was the stupidest, most arrogant, naive thing I had ever done. Starting a firm like I did, essentially from my Upper West Side apartment and with no outside funding, was overly-ambitious. I cannot help but think the years of my mom telling me I could do or be whatever I wanted led me to start SMB. Now that unconditional voice of confidence was silently resting. Meanwhile, the strongest person I had ever known was broken and years away from a significant recovery.

As if things were not bad enough, they were about to get worse.

The Perfect Storm

A perfect storm of events compiled to stop and reverse SMB's forward progress. As a firm or business, particularly in the money business, you never want to be backtracking; after all, the firm's very existence depends on forward momentum. Running a prop firm is very expensive. Specifically, even a flat month in P&L can cost 200k plus after fees, expenses, staff, and rent. From profitable to broke can come fast. Add to this strain 1) some of our profitable traders left, 2) the industry as a whole was struggling, 3) a large legal bill was ahead, 4) new regulation increased costs, and we were headed in the wrong direction. All of this came when I wanted to be elsewhere, with my dad and family.

I always love how people think running a business is so easy, particularly a trading firm. Respectfully, it isn't. And your individual trading business will not be easy for you to run either. We will be upfront about not having all the answers, mistakes made, the need for timeouts during personal struggles, and the necessity to persevere as a trader or firm. Solutions must be found, you must uncover a way to subsist and even reinvent yourself. This is true even for the best traders and firms. This is the life we have chosen. As it so happened, *The PlayBook* was the key for how we weathered this storm.

A great clash lay ahead, one that would have been daunting even if I were at full strength. But I wasn't. My mental state held us back. For example, SMB was sucked into a contentious negotiation with our third-party provider. We leased space and routed our trades through this third party. I had to excuse myself from these meetings because the idea of fighting over a nickel on tickets just wasn't in me. Nor was I in the proper state of mind for the day-to-day grind of running a prop-trading desk, educational arm, and our new systems-trading division. When you have just experienced trauma, stress can trigger a return to a state of trauma, which is unhealthy.

Ciao Bella

That perfect storm? First, some of our consistently profitable traders left. At that time, the career path for our traders was this: become a consistently profitable trader and then get bigger. How 2007! Other firms (poachers from the League of Lesser Firms) learned of the success of many of our home-grown traders. These firms started offering our built-from-scratch guys race-to-the-bottom trading deals that we could not match. It would be hard to find objective traders who would not acknowledge that we offered the best training and infrastructure for the beginning trader. Most of our competitors even admit this. The problem was we were not offering enough value to those who we had trained to become consistently profitable heading into their year three or four with us. SMB thought loyalty and our present value would keep the traders we built for their entire career. We were mistaken.

Here's where we were wrong. If a firm is only going to offer the chance to get bigger after traders are consistently profitable, these traders might forget or undervalue the firm's contribution to their success. At that point, you can be viewed as just a buying-power provider, for which some profitable traders do not want to share much of their profits. In 2009, traders were seeing their profits shrink from the historic trading opportunity of 2008, so some sought ways to keep more of their take. Poaching firms were desperate to fill their emptying seats and so pitched our traders. In fact, one firm kept a file of all the bad things they could say about SMB and literally handed our guys this information. It was mainly printouts of trader forum nonsense, home of the anonymous failed trader and made-up testimonials. I have heard from reliable sources that this firm is responsible for many of the negative quotes in these forums about competing firms. This mistakes playing tackle, being a tough businessman, with being unethical. Some of our guys wanted to find a way to get closer to their 2008 levels and fell for this sell of greener pastures.

SMB had a math problem. You see a prop firm takes losses on underperforming or new traders so that one day those better traders will have a new crop of traders around them offering fresh ideas, new strategies, and lower transactions costs. You are only as good as the stocks you trade. Sixty extra pairs of well-trained eyes calling out trading opportunities helps you as an experienced trader. Then these new traders develop strategies that you have not considered, which you might add to your trading quiver. Further, when these new traders get good, transaction costs decrease for the firm, which can be spread to all traders. When the older, profitable traders squeeze the firm for minimal profits, the firm cannot support the lesser traders' losses.

Simply put, our profitable traders asked for deals that we could not meet within our prop trading model. They got upset that we weren't matching the race-to-the-bottom deals that poacher arcades were offering them, so they left. After a few guys leave, others find other reasons to leave. A firm can become like a downtrending stock that needs a catalyst for it to change direction. Arcades offer a seat and computer but do not offer downside risk, draws, or value-added trading tools and services to traders. It's cheaper to trade at an arcade. I don't have a problem with another firm talking to our traders that approach them. I am even okay with another firm approaching a trader who came to us as experienced. I have a problem with that firm approaching traders I built from scratch and selling them on a better world of slightly lower transactions costs. One trader left to save maybe $500 a month. That is about the cost of parking in NYC. Seriously, that is the business you are in?

Pitch them on added value, specifically technology, more downside, better education, and so on. Show them how you can significantly increase their P&L. That is fair game as far as I am concerned. Also, show some decency. Don't come after the guys I spent ten hours a day with for three years. Playing the lowest cost provider game with rates now so cheap actually harms better firms like mine who invest in their traders. Without firms like SMB, there will be no new blood of future star traders. Also, it sells a false premise that lower transaction costs will improve your P&L. Unfortunately, too many trade to their P&L regardless of transaction costs, meaning that once you know your costs you factor that into all of your trades. Your overall results stay the same. This is just trader psychology.

Perhaps the reason for leaving was our limited career path. Perhaps it was the tougher market of 2009 forcing traders to look elsewhere. Perhaps after three years of our coaching it was time for a new voice for some of them. With our past model of "get good and get bigger," perhaps our desk was more like a college basketball program where, after four years, seniors graduate or turn pro and you have to develop a whole new set of players. Perhaps those traders should have been more loyal.

Whatever the reasons, winners get to write history. You cannot keep losing consistently profitable traders and then claim you were right. That is a world of failure. All that said, I am proud that most of those traders were grateful for the trading education they received from our firm, how much they learned, and our indisputable contribution to their trading success. Some now are seven-figure traders. Many gross more than $250,000 each trading year. A few are even running their own firms. A bunch manage money for others. A half-dozen even work at places like Bridgewater, the second-largest hedge fund in the world. One thing was crystal clear from the loss of traders in 2009–2010: We needed to get better and offer more.

In full disclosure, I was deeply hurt by this trader exodus. Intellectually I am aware that I am not supposed to take such things personally, that business is business. That is beyond my capacity. Guys I train are more like friends and family to me. I spend too much time with them, worry too much about their progress, and get to know them too well not to miss them when they leave. This even applies to traders who don't succeed; it's a horrible feeling that haunts me for weeks when a guy fails. What's worse is when new recruits come in and don't see some of those great traders you helped develop. That is tremendously disappointing.

And there was more.

The Intraday Trading Contraction

Adding to my strife, the intraday trading industry as a whole was struggling. This was not indigenous to intraday trading; in fact, it is more accurate to note that the equity trading world was hurting. So difficult was this period that intraday trading godfather Steven Schoenfeld penned an infamous letter to his traders putting them on notice that many would soon be fired if their performance did not improve. The biggest, baddest, and richest intraday trading firm on the Street was cutting costs. Also, there was the "day trading is dead" blog of the week. These were exaggerations. Day trading (a term I refuse to recognize; it's called *intraday trading*) was contracting, times were tough, but it was not dead. When I first started, we were taught the trading principle that not all years on the Street are wildly profitable. I did not hide any of this on my blog penning numerous posts on this subject.

In one of these "day trading is dead" blogs of the week, I lost a friend who runs an established finance website. From my perspective, SMB was very helpful to this site when it first launched, earning it credibility on the Street. His site posted a sensational, irresponsible blog post titled "Day Trading Is Dead." The industry was down enough; this post that would be read by many didn't need to exaggerate. I knew the author of this piece, who had spent like three minutes in the field of intraday trading, and also knew that the title had been changed by my former friend for the purpose of driving traffic. I called respectfully lobbying the website to rechange the headline to its original title. He did, but that was the last we spoke.

Firms were shrinking as traders were being washed out. HFTs were seen as ruling the day. Allocators were pulling funding of the bigger intraday traders as their appetite to back discretionary traders waned. It was a tough time for the intraday trader and firm.

And then came the worst moment of my trading career.

The Government

Steve was calling. I answered.

"Hey, how are things?"

"I have some bad news. We just received a subpoena from the SEC to be a witness to an investigation."

Adding to all this, SMB was about to absorb a major legal spend complying with an SEC witness subpoena. Remember our third-party partners with whom I couldn't bear to argue? They were being investigated by the SEC. We were issued a subpoena to be a witness to their investigation and provide documentation that related to them.

And the hits just keep on coming.

My dad had a stroke, my mom had passed, we lost some of our better traders, equity trading was suffering, and now we had to provide hundreds of pages of documents and pay a top lawyer god knows how much because someone else was potentially in trouble with the SEC?

WTF!

There is something about getting documents from the government, any documents; no matter how innocuous they might be, it just scares the heck out of you. Add to this that at this time penalizing the Street, anyone on the Steet, was political treasure. We immediately wondered if we were doing something the SEC had decided to use its enforcement power to correct. And if they did, how far would they go? This may seem odd, but the rules for trading firms at times are not clear, even after review from your lawyers. And you cannot just call up the SEC and get their guidance on activities. They tell you when you are wrong only after you act, not before. You could be doing something improper without your counsel or you knowing it. Regulators can decide you were doing something incorrect without you being able to foresee it. That is just the way it is. It is a weird game of moving regulatory target practice, even for the good guys on the Street.

As a firm, you do the best you can so that the government never even wants to ask a question as to whether you are or were doing something improper. Firms in our space had been shut down by the SEC, with partners banned from the business. To clarify: Those firms were doing some very shady stuff that was clearly illegal. Was the subpoena as a witness just a ruse to start investigating us next? While most likely not, at this time our sole focus was not to end up on the front page of the *Wall Street Journal* and live to play another day.

More perverse during this whole fiasco, I felt like a guilty person. I racked my brain thinking, reviewing, wondering if we had done something wrong. I am a lawyer, so is Steve, and our business model is regularly scrubbed by attorneys. None of us could think of anything. The whole reason I started SMB was to give new, developing, and underperforming traders their best chance of succeeding. Check the thousands of blogs we have shared for free in the blogosphere. See *One Good Trade* and the hundreds of webinar hours released to the trading community. And here I was worried about having done something improper and having to expend money and time and stress to contain this matter?

WTF!

Imagine sitting down with your newlywed wife and telling her that news.

WTF!

We spent five days finding the best attorney. We spent the next six months paying him and his firm and providing all the documents requested by the SEC. We shared hundreds and hundreds of pages of documents through our lawyers. Our e-mails, contracts, and trader results were delivered. Again, I felt like a villain, while desperately trying to find something we could have done untoward. We were part paranoid, part responsible business owners playing outstanding defense.

As it turned out, we were, in fact, not next to be investigated. We really were only a witness. And that third party in the end had done nothing improper. It turned out this third party was one of many being scrubbed by the SEC simultaneously. But this was huge money, brain, and time drain that required daily attention during a period when we were not at our best. The result of this industry-wide investigation was most prop firms moving to regulated entities, registering their traders, and dealing with the added cost of this regulation.

Just Doing Their Job

The SEC and other Wall Street regulators have a difficult job. Wall Street is a dangerous, powerful place with a few dishonest players. It's often the case that "good guys" are in fact the crooks; so how can governmental lawyers know whom to trust? Jon Corzine, a U.S. senator, governor of New Jersey, and former head of Goldman Sachs, blew up his futures firm, MF Global, including customer money totaling $1.6 billion, with absurd trading risk. Long Term Capital Management, whose traders were once known by the phrase "the smartest guys in the room" blew up $4.6 billion following the Russian financial crisis, which required intervention by the Federal Reserve. The head of JPMorganChase, who used to possess the best reputation on the Street, testified to Congress that a "London Whale" trading loss would be in the vicinity of $2 billion. It turned out to be more than $6.2 billion. Recently, major banks, most notably Barclays, have been fined and charged with fixing interest rates. And let's not forget Bernie Madoff.

> And then we have the mortgage-backed securities fiasco, which was perhaps the heart of the 2008 financial collapse. Our prestigious banks took outsized risks with mortgage-backed securities, and then tax payers had to bail them out. Some journalists, however, have argued that it wasn't so much that the banks took outsized risks. It's that they engaged in outright fraud. As *Rolling Stone* reporter Matt Taibbi has noted about the 650-page bipartisan report titled *Wall Street and the Financial Crisis: Anatomy of a Financial Collapse*, the document compiled "a mountain of evidence" against Goldman Sachs. Evidence of "gross, bald-faced fraud delivered up in such quantities as to almost serve as a kind of sarcastic challenge to the...Justice Department." Consider this morsel. Goldman's CFO, David Viniar wrote, in an internal memo, of the urgency to reduce the bank's giant bet on mortgages. "Let's be aggressive distributing things because there will be very good opportunities as the markets [go] into what is likely to be even greater distress, and we want to be in a position to take advantage of them." Taibbi's translation: "Let's find as many suckers as we can as fast as we can, because we'll only make more money as more and more shit hits the fan."
>
> Clearly, there are many leaders in finance who do things that are unconscionable such that it brings a pox on all of us. So, the government has to investigate fully, even a matter as small as ours. The sins of others are a regulatory tax on all of us.

Okay, so this was not the best of days for our firm. SMB was not very good. On the Street, like in golf, we learn to play the ball where it lies. We needed a solution. We knew improvement would take time, at least two years. We needed to invest in our strength, building new and developing traders, with new and better techniques and wait. We went all in on our core competency, building profitable traders from scratch.

The PlayBook Becomes Our Solution

Some traders on our desk still needed my help during our rebuilding phase at SMB. But I needed a time out. I had learned enough not to trade in this psychological condition, so they wouldn't receive my tick-by-tick, real-time trading instruction. With me on the desk, actively trading, a new trader learns the best stocks to trade, the setups that are worth risk in real-time, strategies for various trading patterns, how to read the tape at expert level, how to get big and hold, and much more. Real-time coaching is the most effective way of working with a new, developing, or underperforming trader. Mentoring and reviewing a trader's work after the close or a lull in the trading action is effective but not as beneficial as real-time coaching. (I find it disappointing when trading education firms don't know the difference between mentoring and coaching.) This is true of any sport. Going to the office on most days was not possible, as I was still helping my dad rehab, so face-to-face, one-on-one coaching sessions with our traders also were not an option. I faced a quandary: How could I contribute to the firm in this psychological state—and from Long Island?

The answer was The PlayBook. I needed a way to show our traders I still cared about their progress, though as this absentee coach. You cannot teach or coach anyone if students/players do not know you care. Reviewing their PlayBook trades and providing detailed feedback showed them that I did. I required a way to rebuild the desk without being on the desk.

Also, I coveted a way to get our core of developing traders bigger in their best setups. They suffered from what I call and outline inside this book *Trader Wuss Syndrome*, afraid to "man up" in their better risk/reward opportunities. Further, I craved a way for our traders to transition into more intraday swing trading, what we call Trades2Hold, from the momentum trading that worked so well in 2007 and 2008. HFTs had gamed that strategy out of the market, save for the very best momentum traders. Moreover, I needed a way to get them to hold their trades longer for the real move. In addition, because we had a solid core of young traders, I wanted them to learn more from each other.

The PlayBook was their framework to talk most specifically about trading setups with this strong core. The act of talking about your trading with fellow traders is a very powerful progress tool. I needed to get our firm back on track and our traders improving—and I had to do it all from a distance. And so out of this crisis the SMB Playbook was born. It was our solution.

The Truth about Trading

People often ask me to autograph *One Good Trade*, which I do with gratitude. I receive appreciative e-mails daily about how my work has helped traders, which makes my day. When I was in Singapore, I literally couldn't pass through the lobby of my hotel without someone recognizing me and asking to take a picture. Perhaps the large billboards of Jim Rogers and me presenting at a big conference was the cause. SMB recently had to shop for a new trading space in NYC for a *joint venture* (JV) with a larger firm. Apparently, very few traders missed *Wall Street Warriors*, and some of our other appearances, as they easily recognized Steve and me when we walked onto a trading desk looking to sublease space. I have been introduced as a "trading expert" to multiple packed-house lectures. If you Google my name, you can find some pretty nice things said about my writing and the contribution my firm has made to the trading community. All of this makes me very uncomfortable in the sense that some might think that I, and people like me, have mastered the trading game. I haven't. I never will. This is impossible.

What you can learn from me, my firm, and *The PlayBook*, and the reason I have shared so openly about the personal events described earlier, is the truth about trading. These truths often escape what I call The Financial Media Entertainment Complex and leave many new traders misinformed. You must get better every day. Even if you do become a great trader, you'll sometimes face personal struggles and need a timeout. When you become a successful trader, this is not the end. There is no trader destination. Trades will stop working, and you will have to find new ones that do work. Seven-figure traders can walk around in a frustrated daze desperately searching for a return to just a profitable month. Trading is a sport of survival, reinvention, and perseverance, even for the successful trader. That is why I shared the earlier personal anecdotes. That is why it is so important for each trader to develop his or her own PlayBook. This is what I hope you learn from this book.

Yes, You Can!

Even though trading is so very challenging, you *can* do it! The market doesn't care where you went to school, who your father is or isn't, what country club you belong to, your past stardom as a college athlete, or your

IQ. But the right path to success does matter. The daily rehearsal, practice, thinking, trade talking, and review are crucial. You must embrace the mindset to improve every day, build from your strengths, and develop your PlayBook. That's why, and I hope you agree, that this is an important book for your trading development.

Martin Seligman teaches us in his wonderful book *Learned Optimism* that we should absorb difficult events, such as mine described earlier, and learn to look beyond the hardship to recognize those moments in our life that appear catastrophic and to embrace them as opportunities to open our minds for the good that could follow next. And I found the good. I found The PlayBook.

Rogue Traderette, a terrific blog run by an Aussie woman, notes the difference between optimism of the common glass-is-half-full kind to what she considers to be real optimism:

> Real optimism is the ability to attribute the good stuff to "that's how life is" and the bad stuff to "that's how things are [at] this moment, but not forever.

We did make it through the storm. We did find a solution, which perhaps you can learn from. We are stronger than ever. Tomorrow can be better than yesterday. Our traders improved, our work developing traders was recognized, and we built a new and stronger office with everything new, developing, underperforming, or even experienced traders need to excel.

Developing your Playbook will be a personal journey of trader rehearsal. Your goal should be to improve to become a *Consistently Profitable Trader* (CPT) and then a YBT. Focus unrelentingly on what setups make the most sense to you. Your storms will come, but you can persevere and find your path to becoming a stronger trader.

What's Inside

Here's how the PlayBook works: After each trading session, I ask the players on our desk (and now you?) to archive a trading setup that made the most sense to them during that day. They archive this play in a template form, which we share: the SMB PlayBook. This exercise brands their winning trades in their trading brain, synthesizes the most important market patterns for them to study, and helps them internalize their best trading setups so that they trade them instinctively in real-time. There is no real-time deep thought and hesitation for their A+ trades. They spot a favorite trading pattern, they execute (*and* with size). The best traders know when they are right and get bigger. They spend their energy searching for more of their favorite setups and focus on where they can add size responsibly. In this book, you will learn how to get bigger in your best trades so that you improve *your* trading performance.

In this book, most chapters are divided into three sections: an introduction to a pro trader; their PlayBook trade; and a review of this trade with the trader, our desk, and me. We begin most chapters with a delicious look at a character, a pro trader, and his journey, from which you will learn. What best practices can you co-opt from this trader? What should you avoid? What solutions worked for some of these traders that you can implement if you experience similar struggles? You will meet experienced, new, developing, and underperforming traders, some who made it and some who failed. As is my writing niche, interesting, page-turning, and often humorous trader stories are wrapped inside of trading principles and lessons to help you improve your trading performance, while enjoying this read.

The second part of most chapters is a specific trade archived in SMB PlayBook form. You will learn patterns that our desk uses that you might co-opt for your trading. We break down each trade as follows:

The Big Picture

Intraday Fundamentals

Technical Analysis

Reading the Tape

Trade Management

Trade Strategy

Trade Review

Note the detail provided for each archived trade. It is not my intention to preach that you should dissect trades exactly like I do, as you may trade a different product or time frame or see the markets differently than me. I do, however, encourage you to develop a similar *system* of archiving your best trading setups that makes the most sense to you in the format that works best for you. Frankly, if you have not developed your PlayBook, you should. Recently, I met with a series of very experienced but underperforming traders. The common denominator for this group was that none of them had a methodology to archive their favorite setups, nor could they clearly, definitively, and instantly articulate their best plays. They were more or less just flying by the seat of their pants (that is, unorganized and unstudied intuition). Your PlayBook's contents are up to you. But its existence, with all due respect, should not be. *All traders should build a PlayBook*.

The third part of most chapters consists of a trade review between the pro trader introduced, our desk, and me. Tick by tick, we review the highlighted trade. Trading fundamentals and principles are explained and explored as we unveil these trades made by pro traders. Pay closest attention to how we think through our trades, the detail, the clarity of thought, and the standard of professionalism. To be a pro, you must learn first to think like a pro.

You do not become a great trader by being shown cookie cutter technical setups and then soon become successful. That is a myth from what I call Trader Disneyland. It would be wonderful if Trader Disneyland existed, marketed and spun by too many that it does, but it doesn't. I intend to teach you how to think like a pro trader and develop a methodology that enables you to recognize your strengths, provide a foundation for you to prosper when the markets change, and jump start your progress to becoming a CPT and then YBT.

The PlayBook begins smartly with a summary of how to develop a PlayBook trade in Chapter 1, while explaining the top ten ways it can help your trading. Chapter 2 reviews the trading journey of Shark, the model for those who want to quit their job and take up trading full-time. He gets his own chapter because he is the best trainee, the hardest worker, I have trained in five years. Chapter 3 introduces the concept of Reasons2Sell that will give you a guideline for how to exit your winning trades. Also, this chapter highlights a trade setup in Knight Capital after its infamous $444 million trading error that Shark archived and we reviewed together, paying close attention to whether he had enough size.

Next in Chapter 4, you meet TO, who teaches you how to compete as a pro trader and find out how good you can be. You also get a sneak peek into his personal daily trade review. Further, TO walks us through a Fade Trade, a trading pattern that melds best with his personality. Chapter 5 introduces Pippen, who presents a path to follow for developing and new traders. We do something special in this chapter and review the historic IPO of Facebook, stock symbol FB, with his trade review. Chapter 6 explores the insufficiency of trader education in colleges, introduces the humorous and concurrently sad "GM test," and *pounds the table* about what traders should be doing before they turn pro. Special Projects, our intern, is placed on the hot seat as we review his Reversal Trade, a powerful trade for developing traders.

Chapter 7 introduces Prep, who might just become the hero of underperforming traders everywhere, as he made almost every mistake a trader can make but stayed in the game. We review his failed trade in JCP that was still One Good Trade. Stay tuned for the plot twist involving Prep in the postscript of this section. In Chapter 8, we introduce Rudy to debunk the theory that the bright start their trading career on second base, ahead of others. I allegedly rip Rudy in this memorable trade review, of an awful Technical Trade. What some call "rip," I call essential critical feedback. In Chapter 9, Iceman challenges you to take on more risk with your trading and gives you an inside look at the psychological journey from newb to pro trader. We check out his gutsy Opening Drive Play in the high beta stock, LNKD. This chapter helps you answer an important trading question: Are you taking on enough risk in your trading?

In Chapter 10, we study an SMB icon, GMan, to demonstrate the importance of continuous great coaching in your trading career. GMan shares his favorite and most profitable trade of late in great detail, the Pullback Trade, transcribed from an SMB teaching event in Singapore. This trade is worth many re-reads. Chapter 11 brings us to South Africa, showing how The PlayBook can help pro traders in other markets and products. We meet some interesting players from the largest prop firm in South Africa and review a few trades we made with them while I visited. *The PlayBook* concludes with my assessment of the future of trading, focusing on our future opportunity. *It has never been a better time to be a trader!*

You will learn to think through your trades and develop your own PlayBook. This book exposes you to trading patterns that you can co-opt and start to make your own. Trading fundamentals and principles too numerous to list are included with each trade review, with our traders recounting their trading journey. You will marvel at the work and detail of a pro trader striving to compete in the highly competitive world of the proprietary trading. You will laugh, shake your head, and learn from the stories shared by some we trained from scratch on my desk. This book was written to be a page-turner while also offering significant market lessons. I want to remind you that this is a game to be enjoyed and that you can play successfully with the right purposeful practice, archiving your best trading setups that make the most sense to you.

It is also my ultimate hope that you embrace the opportunity you have, that you are grateful each day for the privilege to follow your passion, and that you discover the true value of striving to be your best trader, whether successful or not.

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How's my dad? Did he make a full recovery? Not *yet.* But he has made a substantial recovery. His relentless will to improve inspires me. Let's give him some more time. As for you, there are about 250 trading days a year for you to progress by working on your PlayBook. My firm? Things are going really well for us, which we will discuss the how and why of inside. Keep moving forward in your trading career motivated perhaps a bit by my story but more authoritatively by the words of Ray Dalio, founder of the largest U.S. hedge fund:

> Weaknesses don't matter if you find solutions.

Next, let's explain how to create a PlayBook and how it can improve your trading. It is my great privilege to present to you, *The PlayBook.*

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1. The PlayBook

> Use whatever works, and take it from wherever you can find it.
>
> —Bruce Lee

The PlayBook is a series of archived trades that make the most sense to you. The idea is for you to build from your strengths (the plays in your PlayBook) and minimize your weaknesses (anything not in your PlayBook). We break gazillions of bits of market data down into trading patterns that you can excel at, everything in your PlayBook. This chapter demonstrates how you build a trade with five indicators, explains those indicators so that you can use them when constructing your PlayBook, shares a template for your PlayBook, and finishes with the top ten ways The PlayBook can help your trading.

I stood at the lecture podium at Pier 61 in NYC (coincidentally one banquet hall over from where my wife and I held our wedding reception) in front of institutional banks, hedge fund traders, and large prop traders dissertating how and why discretionary traders were being undervalued. A smartly dressed gentleman from a big bank, or so his conference badge read, raised his hand and asked, “What do you see as the primary weakness presently among experienced discretionary traders?” I replied instantly, “A lack of methodology to build from their strengths.” If I had been asked about a developing or new trader, my answer would have been the same. We will fix that together in this book.

For the experienced trader, *The PlayBook* will give you that methodology to specifically understand, archive, and help internalize what you trade best, engineering improved results. Many underperforming developing traders have so much good in their trading, so many patterns that yield promising P&L gains, while still not reaching their goals. But they do not understand what they do best and what they should eliminate. *The PlayBook* will help the underperforming developing trader keep more from their better trades, make more on these setups, and get rid of the trades not worthy of their attention. New traders are deluged in a sea of fast-moving, confusing data, unaware of which market information to focus on. *The PlayBook* will help newbs pinpoint the data that is most important, while putting together plays that they can trade profitably. In the States (United States), it is joked that Robitussin, “tussin,” is the core to any ailment. Well, for the trader, no matter the product or market, and of all experience and skill levels, *The PlayBook* is your tussin.

The key to your optimal trading is to stick mostly with what you trade best. During a Saturday brunch with a good friend and pro trader, I was given the most awesome analogy for explaining the power of *The PlayBook.* Let me share it with you.

Say you want to open a pizzeria. You believe that you have developed the perfect combination of dough, cheese, and sauce. You sink all the money you’ve saved, and some borrowed from family members, into the pizza joint. You open with great pride; after all, you have achieved your dream. But then a customer comes in and asks, “Hey, can I get a taco?” Would you serve him a taco? No, of course not, because you make pizzas. As traders, we can often jump from strategy to strategy that may not be our strength to our P&L detriment. Do what you do best and stop trying to make tacos.

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We make trading decisions based on five indicators, or *checks:*

1. The Big Picture

2. Intraday Fundamentals

3. Technical Analysis

4. Reading the Tape

5. Intuition

We think of a trading decision as a big circle with all of these variables inside. Can you picture that big circle with your decision making tools inside? It’s up to the trader to determine what proportion of the circle to color for each variable, how much weight to give each indicator. But every decision includes considering the impact of each of these five checks. It’s most important for your trading career to understand what to consider when deciding to make a trade as opposed to whether your trading decision was correct. This is an enormously important distinction for the pro trader to grasp. In fact, Peter Brandt, who wrote the marvelous book *Diary of a Professional Commodity Trader*, said as much:

> Many novice pedestrian traders focus on the next position. Consistently successful traders focus on the process and care little

about the outcome of the next trade. The distinction is enormous.

You get better at how much to weigh each check with time. Just keep sticking to the right thought process.

It's how you think through a trade that is most important and sustains. If you are looking for a system to follow that will work consistently to the end of days, I have some bad news for you: It does not exist. My favorite trade is the Trend Trend Trade, which we will discuss. I have identified specific market variables that define this setup and drafted rules to manage this play. But every Trend Trend Trade is a little different, requiring tweaking for my trade entry, stop, size, and exit. Even automated strategies require constant reconfiguring. If you think of trading as "red light, sell, and green light, buy," you should probably find another game to try or book to read.

Let's do something very powerful for your trading career together. How about we learn how to think through trades comprehensively, individually, and with structure? That way, we can adapt to the always-changing markets and develop PlayBooks for any market, any product, any trade, and any time. Let's not pretend trading is easy, that there is some holy grail to your success and give this sport and you the respect it deserves. Having said that, make no mistake: This is a game each of us can win!

Let me explain each of these checks and give examples of how they affect our trading decisions so that you can later use them when formulating your PlayBook. Also, throughout the book, we use real-time trading examples of trades made by SMB traders to supplement your understanding of each indicator, so take comfort that this is just the start of my explanation on how to use these variables to make trading decisions.

The Big Picture: First Know What Is Moving the Market

Let's start with the Big Picture. We do not initiate a trade without understanding the Big Picture for the market. The *Big Picture* is the strength or weakness of the overall market and what catalysts are moving it. More specifically, we need to know the following:

- What are the most important technical levels in our markets?
- How far is the market from important technical levels?
- Is the market trending up or down?

- What is the market most concerned about presently?
- What is moving the market?

As a trader, know the story the market is most interested in. Picture yourself writing the copy for a nightly financial news station. What would you highlight? This information is massively important to all of your trading decisions and uniformly undervalued by underperforming traders. For example, if the majority of market participants are hypersensitive about whether the euro zone will remain intact, like they were in the summer of 2012, then news of a member potentially exiting should affect the market. We need to know this narrative and be prepared for how it may move our trading positions. A stock in a beautiful uptrend (we jokingly say *supermodel chart*) may be sold if negative market news hits, as this will probably bring selling to the entire market and your positions. If the market is most interested in new housing starts, we hawk this number before and after its release, factoring this into our individual stock decisions. In fact, we might not trade until after the release of this number.

Steve Grasso, governor on the NYSE, pointed out during a CNBC spot that 80 percent of stocks move with the markets. If there is a market event or technical level that will most likely move the market, you must start every trading position cognizant of and contingent on these factors. Your stocks do not trade in a vacuum. They do not even just trade by sector. They are a part of a bigger team, team overall market, that moves up and down for reasons you can spot, understand, and game.

One evening I was having a late dinner, swapping training stories and techniques, with an old-school Schonfeld Securities trader who works mainly with developing traders. He stopped eating his lamb Slovakia, looked up, and insisted with that classic prop trader absence of tact, “You have your guys come in early and read the news, right?” You must know the Big Picture.

See the example in KSS, shown in Figure 1.1. KSS was in a supermodel uptrend. Our desk was long, big, sitting, and waiting to collect our spoils. The market during this trade was most concerned about our government avoiding the U.S. fiscal cliff. Speaker of the House John Boehner, after a negotiation session with the President, held a short press briefing and announced that it was now less likely the fiscal cliff would be avoided. The result? Our supermodel chart turned into a dog. The stock dropped out hard after the comments and then reversed into a downtrend. Know thy Big Picture!

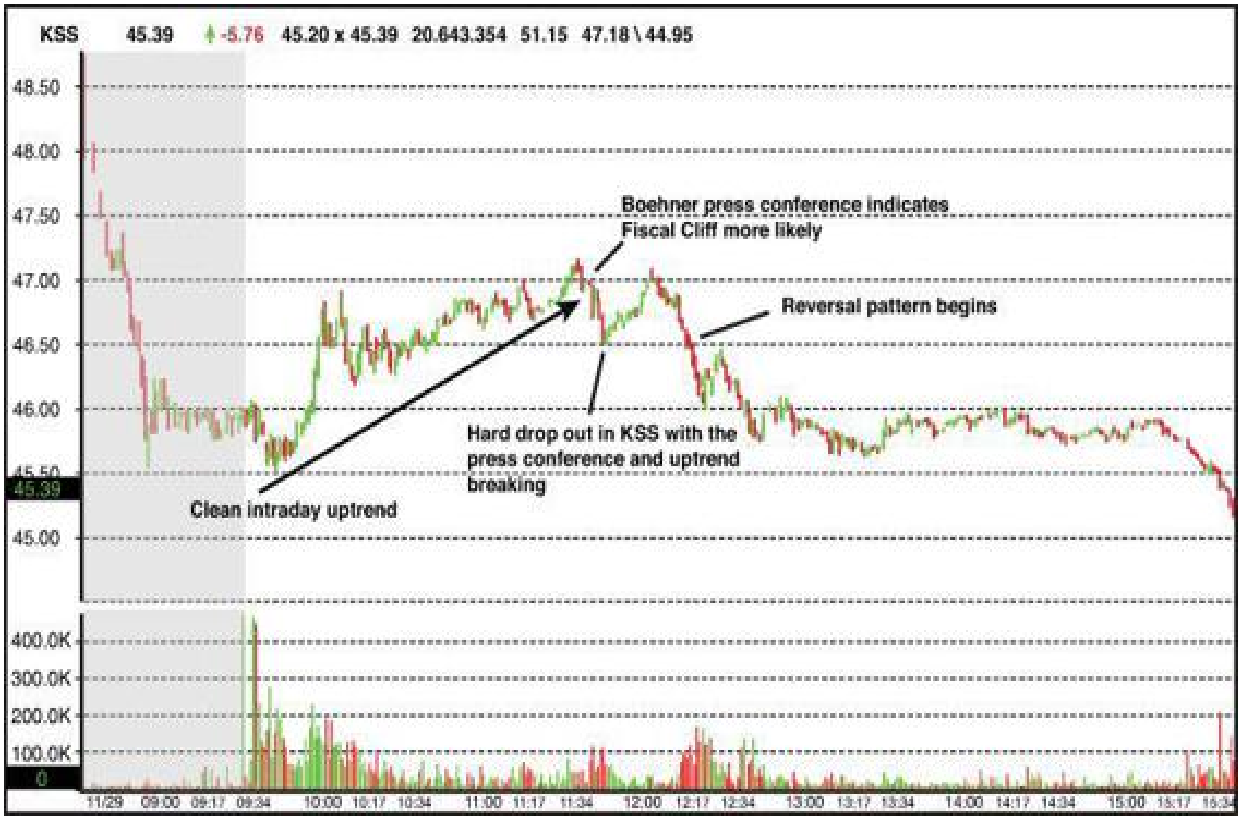


Figure 1.1

Now that we understand the Big Picture on a trading day, we can consider the Intraday Fundamentals or, said another way, fresh news in a stock.

Intraday Fundamentals: Trade with Real Order Flow Behind Your Stocks

In *One Good Trade*, I wrote about the opportunities from trading *Stocks In Play* for the short-term trader, as this allows us to be most efficient with our capital. *Intraday Fundamentals* is our fancy way of saying we want to trade a Stock In Play. To be even clearer, we seek stocks that have fresh news. This fresh news can come after the previous close or before the open.

Fresh news provides potential real order flow into the stocks we are trading. Real order flow, in turn, increases the chances of a stock trending in the same direction cleanly (fewer or no shakeouts), which makes trading easier and more profitable. For example, if a stock is In Play and forms a bullish flag pattern (a technical pattern showing strength), we are more confident to take a long position because the fresh news makes it more likely that the buying will continue. Not all bullish flag patterns are created equal. One for a Stock In Play holds a much better win rate and risk/reward opportunity than a plain vanilla bullish flag setup. So we stick with stock patterns that have a built-in catalyst.

How about a cheat sheet for finding the Stocks In Play? I asked our summer training class of 2012, during one of our hundreds of hours of personal classroom instruction (and in between all of my humorous jokes of course), to make a list of the Super Stocks In Play. These are the best of the best Stocks In Play. There are certain news events that make a stock a Super Stock In Play. Here's the list these young guns came up with from my daily instruction:

- Improved margins.
- Government investigation.
- Raised guidance going forward.
- Revenue significantly better than expected.
- Gained market share.
- New product, new drug, new something to sell.
- The market cannot put a ceiling on earnings.
- Stock +/– 3 percent with increased premarket volume.
- SMB Radar score of 6 or higher.
- Spencer morning meeting (SMB a.m. meeting): top three ideas.

Let's discuss each news event that produces a Super Stock In Play.

Improved Margins

Anytime you read that a company has increased its margins, stop what you're doing (perhaps kiss your significant other on the cheek with a huge grin) and develop a plan to trade that stock. Margin improvement is a very powerful catalyst that sends stocks higher during earnings season. Essentially, the company is making more on the product it is selling, which, in turn, generally has a positive effect on the performance on the stock. Conversely, falling margins may cause a sharp decline in the price of stock (see Figure 1.2). Note I use *generally* and *probably* and *should* to describe market fundamentals. As a trader, I inhabit a universe where I am almost never certain of anything. Overconfidence of a trading position should be saved for those who appear on TV, which I again refer to as the Financial Media Entertainment Complex. Real traders doubt and question and reconsider and are skeptical. Oh, and we certainly never wear ties!

Figure 1.2

Government Investigation

Any type of government investigation (SEC, FBI, IRS, DOJ, and so on) is extremely negative for a stock (see Figure 1.3). Sell, sell, sell! Upon the breaking news that a company is under investigation by a government body, most responsible traders sell first and ask questions later. You can often expect a prolonged and outsized move to the downside when such news hits. The investigation has to be properly explained away by the company before the Street will regain the confidence to assume long risk in this security.

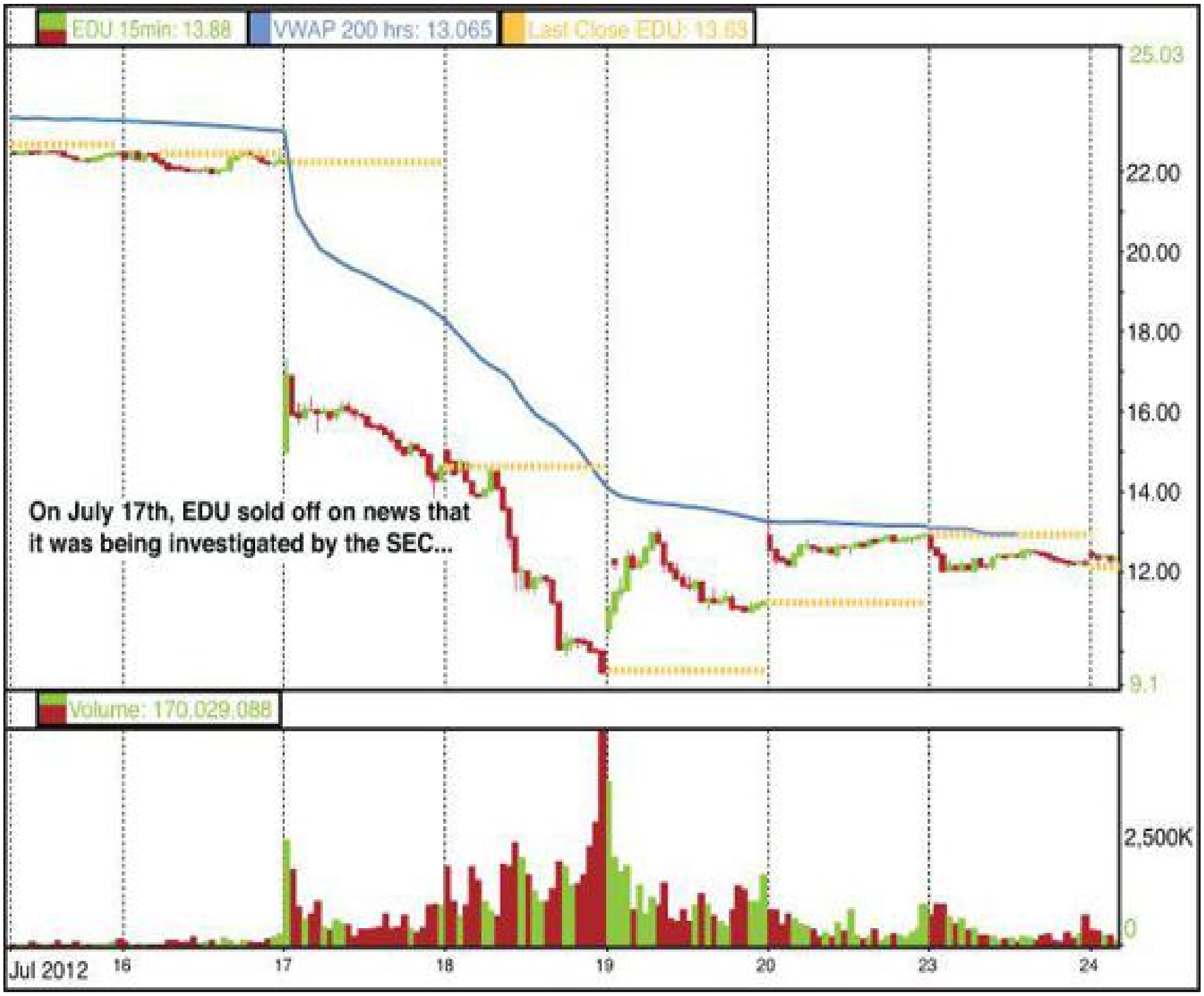


Figure 1.3

Raised Guidance Going Forward

When a company raises guidance going forward, kiss your significant other again and start considering long positions (see Figure 1.4). Traders' expectations about a stock's upside can be changed drastically with such news. When a company raises guidance in an earnings release, you can expect a possible outsized move to the upside. The market looks forward six to eight months, so a company's guidance going forward is more important than the bottom-line number for the reported quarter. Understand this distinction. Look for excellent risk/reward long opportunities.

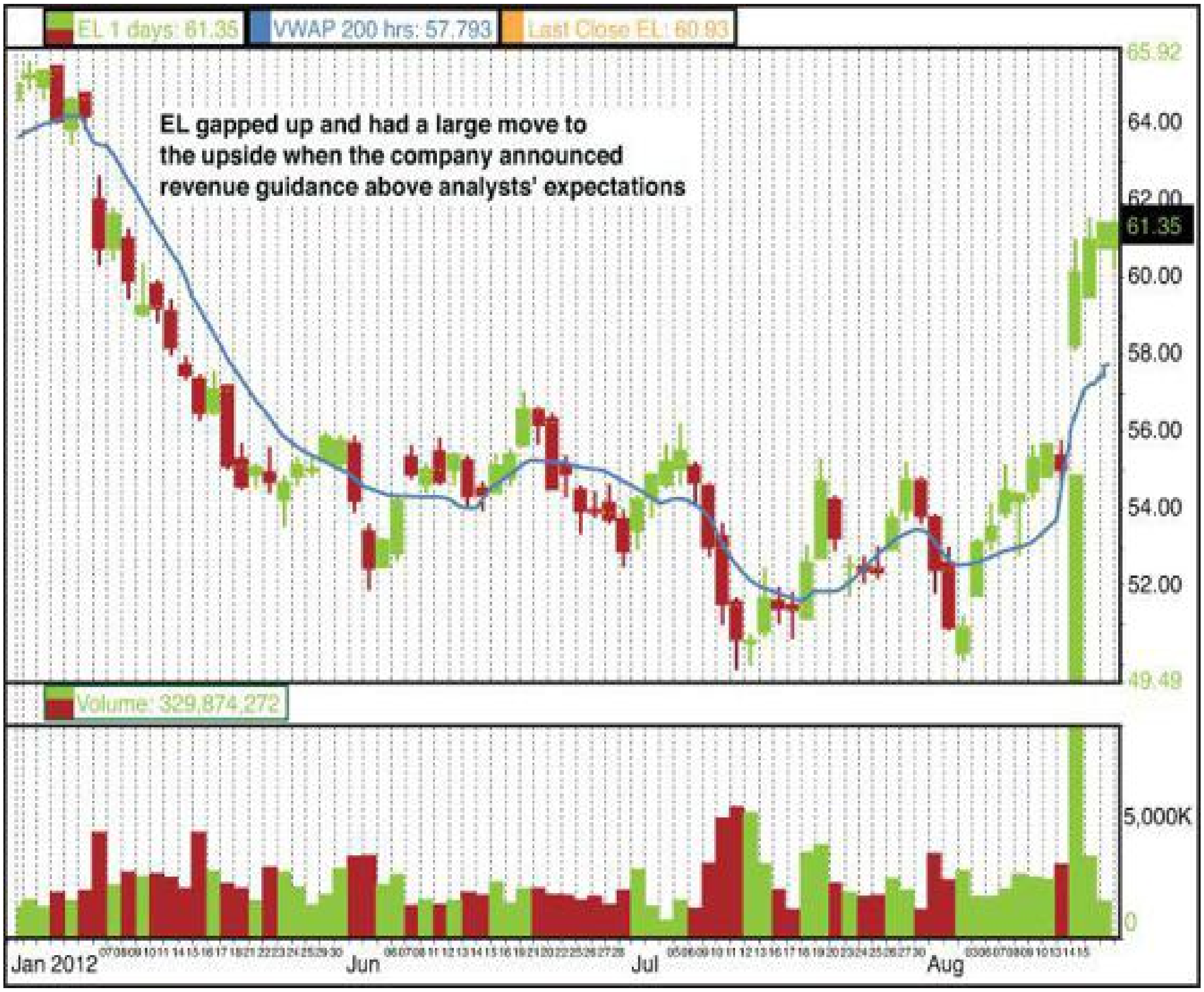


Figure 1.4

Revenue Significantly Better Than Expected

If a company reports revenue much higher than the analysts' consensus, this can also dramatically improve the psychology for a long position in the stock (see Figure 1.5). This situation creates conditions for a powerful move to the upside. Reported revenue is more important than the bottom-line number. Revenue is the best gauge for how the core business of the company is doing. If a company sells widgets, we want to know how many widgets it is selling (the health of the core of the business) as opposed to whether the company got a one-time tax break on its property.

Figure 1.5

Gained Market Share

When a company's market share increases, this shows that the business has an edge over others in its sector (see Figure 1.6). This behavior also can raise expectations about a company's performance going forward, and as a result, the price of the stock should go higher.

Figure 1.6

New Product, New Drug, New Something to Sell

When a company announces a new product, this announcement improves how traders view the business going forward in a fundamental way (for example, more profits). Depending on the market reaction, this type of announcement can lead to substantial moves either up or down. For example, ARNA exploded after approval of a new weight-loss drug (see Figure 1.7).

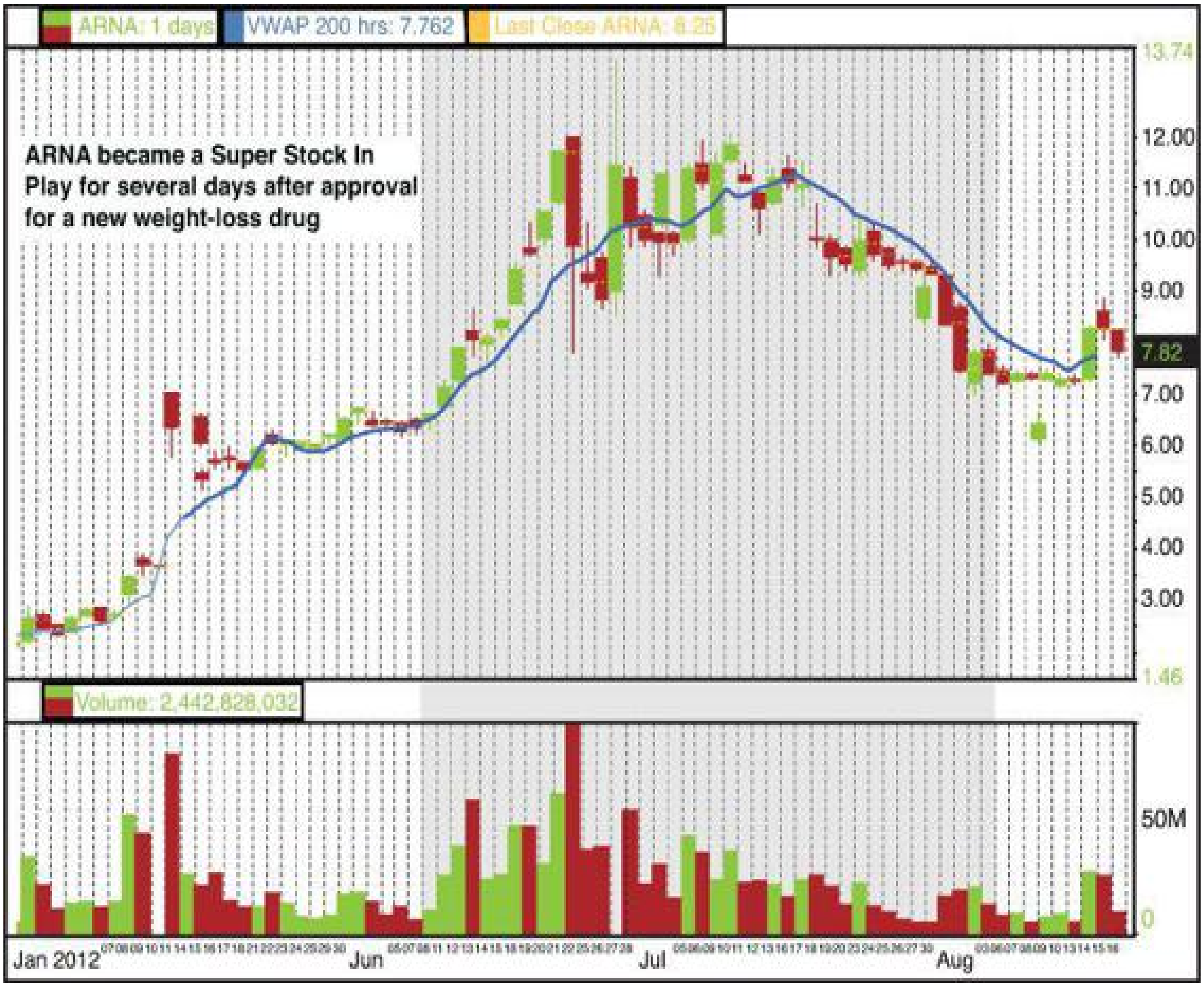


Figure 1.7

The Market Cannot Put a Ceiling on Earnings (Growth Stocks)

Analysts and traders can't always quantify the market reaction about a company. For example, how much is a social media company worth? How profitable is a new, groundbreaking product? Many times, this uncertainty can lead to large moves in stocks—sometimes for extended periods (see Figure 1.8).

Figure 1.8

My friend and renowned trader Joe Fahmy has instructed traders/investors not to look at the PE for growth stocks because they tend to trade much higher than established companies. You don't want to miss terrific risk/reward longs because you are wedded to stocks trading at a particular PE. Think of any company in the late 1990s that associated itself with the Internet (as a trading vehicle, not necessarily an investment). There was a ton of money to be made trading the upside of Internet stocks while they were in their growth stage. These opportunities repeat in new companies with a tremendous growth story.

Stock +/– 3 Percent with Increased Premarket Volume

A stock +/– 3 percent with increased premarket volume is your cheat sheet for finding the Super Stocks In Play. When a stock has gapped up or down during premarket hours with large amounts of relative volume, this provides important signals for how the stock will trade once the market opens. Usually, these stocks proceed to make large moves intraday (see Figure 1.9).

Figure 1.9

SMB Radar Score of 6 or Higher

When you see a stock ranked on the SMB Radar, our proprietary trading tool, at 6 or higher, these stocks should usually merit your attention. Generally, these stocks have the most potential to move relative to the market. Good traders use great tools to find the best stocks for them to trade, like our stock scanner, the SMB Radar. We say this is a discretionary trader being more bionic, as they are using technology to find more of their favorite setups.

Spencer Morning Meeting: Top Three Ideas

Spencer broadcasts a morning meeting each day to our traders and tools subscribers. The top three ideas that he presents during the morning meeting should be stocks that you pay close attention to intraday; they will usually be the best to trade. The takeaway here is veteran traders are excellent at understanding what has the potential to move dramatically during a trading session. Go find them for your trading.

Let me share an important advanced trading note about Intraday Fundamentals. Sometimes the Intraday Fundamentals are so exciting that you will just want to be in the stock anytime it offers a hint of entry. I call this just *playing* to the traders on my desk. The fact that the stock *might spike* is a reason to be in it. This can make for some sloppy trading, but it's worthwhile. And for the sake of clarity and sessions without unnecessary trading rips, I said sometimes, as in these occasions are rare.

Admittedly, a lot of in-and-out trading can be psychology grueling for the trader who hates to be wrong. Dr. Momentum, from my last book, *One Good Trade,* got so mad at me for encouraging him to trade what I thought was a special opportunity with a highly volatile stock that after a trading rip he smashed his keyboard and stormed off the trading floor, cussing me under his breath. Suppose that a company announces that it has improved its market share or developed a new product or increased guidance going forward or improved its margins. This is news that tends to create a clear trending move, which means that you may not need a wonderful technical setup or see strong buying on the tape to pull the trigger. Anytime you spot the stock not going down, this might be enough to enter long. The risk/reward that the stock might make a powerful move might be too much to miss.

Now on to the number-one trading indicator worldwide and most misused, our favorite trading crutch: Technical Analysis.

Technical Analysis: Friend and Foe

When we consider Technical Analysis, we check long-term and short-term technical levels. With our long-term technicals, we want to find the next big technical resistance or support level for the stock we are trading. If a stock is near such a level, this will affect our trading decision. For example, if we are considering a long but the stock is near a long-term important technical resistance level, we probably will pass on that trade, even if our other trade decision variables signal to buy. Why buy a stock so close to long-term technical resistance? We will be more likely to buy if the stock clears this long-term important technical resistance level, but not until then. As for short-term technicals, if a stock is in an intraday bullish flag pattern, this makes it more likely for us to get long. We teach our traders to focus on getting long, strong stocks when they see a bullish flag pattern and short, weak stocks where they see a bearish flag pattern as long as the long-term technicals do not say stop.

Influenced by former SMB trader Adam Grimes, who wrote the must-read technical analysis book *The Art and Science of Technical Analysis*, we keep our charts clean and with few indicators. Most technical indicators were discovered by Grimes to lack a trading edge. Also, we are consistent with our approach to which charts (what time frames) we view before making a decision. This approach is advocated by my very good friend Brian Shannon, who wrote one of great technical analysis books, *Technical Analysis Using Multiple Timeframes.* Flipping from indicator to indicator or from different time frame to different time frame as your solution to underperformance is a path to trading failure.

Let me clarify: We will take trades solely based on technical analysis. For example, if we find a very significant technical level, we trade almost exclusively based on this level. We score our technical levels from one to ten and develop a system for making trades if the technical level is very significant (seven and above). Also, we weigh technical analysis more heavily when trading high-beta stocks. High-beta stocks move actively on most intradays. These high-beta stocks have a daily built-in catalyst, as so many are trading them off technical levels. Examples of high-beta stocks are/have been AMZN, AAPL, GOOG, BIDU, NFLX, CMG, and LULU, to name a few. A good cheat sheet for finding these stocks is at StockTwits 50 (http://stocktwits50.com), which consistently tracks the best performing stocks. It's usually the case that if you have a high-beta stock with a significant technical level, you will not need fresh news to trade it. We will discuss much more about all of this later.

Let me make an important point about trading using technical analysis here. As stated earlier, sometimes Intraday Fundamentals are absent from our decisions. And if a stock is near a very important technical level, it might not need Intraday Fundamentals to consider. If that is the case, you will want the best of the best technical setups before considering an entry. Developing, new, and underperforming traders often struggle trading off technical analysis at the start because they are not selective enough with their technical setups. They trade off technical levels that are not important enough for a consistently profitable trade.

I sat with Jeff Augen, author of six trading books on options and SMB Options Tribe contributor, as he showed me his technical analysis tool, the Phase Indicator, which consists of very powerful algorithms to spot entry and exit points in the market and stocks. Even with this powerful tool, his most effective offerings to his clients are the best of his best buy signals on the S&P. To be even clearer, please just trade off only the best technical setups.

The probability that a stock will continue trending is often absent with an ordinary technical setup because there is not a large enough catalyst that will make it more likely for other market players to buy or sell. Such a large catalyst is often present with fresh news. So you will need to see a significant technical level to make consistently profitable technical trades. Make sense?

Here's a thought for you to consider about whether to trade a stock. When I think about making a trade, I envision someone from a sales and trading desk at a big bank on the other end of the phone pitching clients to buy or sell a trading idea. If you were pitched by a sales trader to buy BIDU because it traded above an important technical level, would that make a majority want to buy the stock? If not, pass on the idea. If you determine a majority would be easily convinced to trade this idea, start to focus on setups in your PlayBook to execute on this opportunity. *Now* this stock is worth your intellectual energy, emotional capital, and trading skill, which you must protect as precious treasures worthy only of the best of trading opportunities.

For all the demonization of *high-frequency traders* (HFTs), technical HFT algorithms actually improve your chances when trading off the most important technical levels. These algorithms scan the market for such setups. When a stock crosses an important technical level, HFT technical programs automatically enter trades. Then other automated strategies sense the increased volume and trend of this stock and buy. So in this new market of algorithms, it can be a self-fulfilling prophesy to trade off the best levels.

Since we started SMB, the one area of weakness I see most among traders of all products is Reading the Tape. It is true that Reading the Tape has become more difficult of late (especially because of HFTs), but you can still gain a trading edge with these skills. GMan created a two-day course, Reading the Tape, to help improve these skills for the traders who lack them. It is too difficult to explain Reading the Tape in written form, so we created a video series. Your entries and exits determine your trading score at the end of each session. Not having the skill to enter and exit at the best price leaves the trader with a significant handicap.

Reading the Tape: Find Better Entries and Exits

When we are considering longs or shorts, we watch the tape to find the entries that improve our risk/reward. When we read the tape, we look at the Level II data on our trading platforms. Specifically, we watch the bids and offers that have entered the market and all the time and sales (we also say *prints*) for a stock. Doing so gives us specific information about intraday support and resistance levels and catalysts for a stock's next direction. In Chapter 3, "The Day Knight Capital Almost Fell (A Support Play)," we review a trade that Shark made in KCG, an Unusual Hold on the Bid, as an example of how to use the tape for a better and bigger entry.

During a phone call with management at a $10+ billion U.S. hedge fund, I was amazed to learn that some of the top traders in the world are experts at developing trading theses but rank amateurs when it comes to discerning ideal entry prices. Obviously, I don't write this to put them down. I only intend to point out that while some of the world's great fundamental players can develop wonderful theses about future investing events, they lack the knowledge on how to express those ideas at prices that offer the best risk/reward for their trades. As short-term traders, we are experts at entering our trades at the best risk/reward prices but weak in developing an investment bias. Why? *Because we're traders, not investors nor macro players!* So our job as intraday traders is to watch the tape and find the best areas for entry that improve our win rate and risk/reward. You will see throughout this book how we use this skill to start and exit our positions at the best prices with trades made on our desk, risking our capital.

Intuition: Unartful Things Said During an Interview

> "Trading is in my genes."
>
> "I have a knack for knowing where the market will close at the end of the day."
>
> No, it's not; and no, you don't.

Intuition is that guiding voice in your head that tells you when to buy or sell, and it is something developed only after years of screen time. Experienced traders learn to trust that inner voice, as it is a money-making indicator. New traders have not developed this voice and, worse, often make the mistake that they have it. In this case, listening to a faux inner voice is a harmful indicator. When your intuition as an experienced trader signals a trade, you put on that trade.

John Netto, author of *One Shot – One Kill: Precision Trading Using Technical Analysis*, expresses the importance of intuition in every e-mail with this signature:

The 10 Attributes of a Great Trader:

1. Heart/Courage
2. Intuition
3. Vision
4. Discipline
5. Decisiveness
6. Patience
7. Confidence
8. Focus
9. Being Dynamic/Fluid/Flexible
10. Willingness to Learn and Improve

Doing the daily work necessary to become a great trader, such as archiving a PlayBook trade and doing a daily review, is vital to developing your intuition. Here is a snippet from a trade review from an SMB trader working on building his intuition:

> I have been trying to work on how to get that **“sixth sense” of when you really can get that feeling of when a stock is going to really have follow through** or when it’s simply a waste of time. I know this is a very nuanced topic that takes years of tape reading over different market conditions to develop, but I really got to thinking about it after Monday.
>
> I was in an EBAY trade when the stock had technically broke out above a level on good volume and was consolidating at the highs in a 10c range for over an hour with the market grinding up. I got big in this setup and thought for sure when it broke above the highs it was really going to run. It ended up going up 8c and then just stopping out all the longs below the consolidation.
>
> I don’t know how to explain this, but I was watching the tape almost the whole time and something just didn’t feel right. I was able to learn from this experience a little bit and noticed M was a weak stock on Friday on the SMB Radar going into the close, consolidating at the lows. The chart looked great, but I started watching the tape and debating whether it was worth hitting the break in the consolidation to the downside and ultimately passed. M only went down another .14. Just something about the way it was printing led me to believe there would be no panic below.

After time, review, experience, practice, pain, jubilation, frustration, anger, regret, grief, guilt, fear, revelation, confusion, doubt, humiliation, self-blame, self-loathing, coaching, perseverance, self-critique and thought, you will learn to use intuition as a powerful trading indicator.

So in each PlayBook trade, we place all these checks into a pattern we want to archive. We do this daily with the trade that made the most sense to us during that trading session. The work compounds daily until we have built a powerful PlayBook, thus (and this is the most exciting part) helping you become *your best trader* (YBT).

The PlayBook: An Example with a Second Day Play

Let’s take a look at a PlayBook trade example in a powerful setup for the new, developing, and underperforming trader: Second Day Play. When we make a trading decision, we consider those five indicators (or checks) listed at the beginning of this chapter. When we archive a setup for our PlayBook, as SMB Trader The King of Men did for us below, we also include the following:

- Trade Management
- Trade Strategy for the setup (optional but recommended)
- Trade Review

As you will see, Trade Management is a review of how well we traded the opportunity. I impress upon my traders to pay closest attention to whether they could have been bigger responsibly in a trade, specifically where and why. (Re-read that last sentence please. Now highlight it! Okay let's move on then.) Trade Strategy for a particular setup was added after we started doing a bunch of these PlayBook trades. Our more diligent traders added trade strategies to their favorite setups. Think if you traded this play 1,000 times how would you attack it? And then develop a set of rules for this setup. Finally, we end each PlayBook trade with a Trade Review. Overall how does the trader feel about how they traded this setup? What levels are most important for this stock going forward? What trading ideas can we develop for tomorrow learned from today? Use the trading information you gained from trading today to profit more tomorrow.

Allow me to make one important clarification for your PlayBook. This is an example of how you might construct *your* PlayBook. You may see the markets differently and choose a different template. Awesome! You may trade a different market or product and devise a variant template. Terrific! Add stuff, eliminate some of these indicators, replace checks with checks that are important to your trading. I hope my template can help you build a PlayBook that works best for you. If so, outstanding!

Second Day Play: Trend Trend Short EDU

The King of Men

July 18, 2012

Trade Strategy: Trend Trend Short

Trade a stock in play the day after it had negative fresh news.

• Determine the most important intraday levels from day one of that Stock In Play.

• Find the intraday low and the prices where increased volume was done. These prices can be used for a powerful trend trend short Second Day Play.

• Look for stocks that have moved +/- 5 percent on day one, trended down, and closed near the bottom intraday.

• Short when the stock holds below an important technical price from day one and hold until there is a Reason2Cover (see Chapter 3).

Second Day Play Fundamentals

• Stocks trade cleaner.

• Intraday swing trade with a Reason2Cover as our exit.

• Once below technical levels from the previous day, it's game on.

• Note that Second Day Plays don't have to occur exclusively on the second day. In some cases, the stock can consolidate for several days before the key levels are finally taken out. If the proper setup doesn't develop on the second day, set alerts that don't expire in front of the important levels, wait for the levels to be tested, and reevaluate when the stock returns to those important prices.

SPY: The Big Picture

• Knowing the trends and levels in the overall market is crucial to executing Second Day Plays properly. They can be used to get more or less aggressive depending on the direction of the market relative to the direction of the Second Day Play setup. When the trend in the market lines up with the trend in the individual stock, trading these types of setups can present a great deal of opportunity.

• After closing above the 136.00 resistance level on July 17, the day when EDU was first in play, SPY opened on July 18 at that level and trended upward through the morning before flattening out and consolidating between 137.00 and 137.60.

• The market was unable to test the next resistance at 137.80, but closing above 137.00 was a bullish sign.

• Holding below 137.00 could put 136.50 and 136.00 back into play, and holding above 137.00 the recent high of 137.80 could be tested.

• Above 137.80 it looks like 140.00 is the next target.

Intraday Fundamentals

• EDU, which has been in a downtrend since mid-June, had a significant gap down to new lows on the in-play day on the following bad news:

  • **July 17: 10:28 AM** Shares of New Oriental Education & Technology (EDU -27.2%) crater after a **SEC investigation** into the company is announced on an earnings CC.

  • An investigation by the SEC is a very severe piece of bad news.

• This was a Second Day Play, but on the day in question, there was an additional piece of bad news:

  • **July 18: 1:42 PM** New Oriental Education (EDU -19.1%) slumps again after Goldman Sachs suspends itsT rating due to a previously announced SEC investigation and Muddy Water sets it short-selling sights on the financials of the company.

Technical Analysis: Long Term

• EDU started to trend down in early June, eventually pulling into the 22.00 area, which was supported from the beginning of 2012 prior to its earnings announcement.

• The gap down to new all-time lows on earnings and the SEC investigation confirmed the weakness in the stock, and on July 17 the stock was extremely in play.

• On an average day, EDU trades fewer than 2M shares and moves about 1 point. On July 17, EDU traded over 30M shares and moved over 5 points intraday. Both the intraday high and low were levels to watch the following day, but the weakness in the stock made a continuation of the downtrend more likely than a reversal.

• Staying objective and flexible is important. If the stock had opened up very strong on July 18 and traded above the intraday high from the previous day, a gap fill to 22.00 could have been in the cards. However, in this particular case, a great deal of confirmation would be required to make a reversal play.

• The best kind of Second Day Plays are the trend-trend setups. In this instance, EDU was broken longer term as well as weak intraday on July 17.

Technical Analysis: Short Term


EDU 15min: 9.48
VWAP 200 hrs: 12.732
20.21
19.00
18.00
17.00
16.00
15.00
14.00
13.00
12.00
11.00
10.00
9.48
9.2
Volume: 75,859,376
2,500K
0
17 Jul
12:00
16:00
18
09:30
12:00
15:00
16:15

• Watching EDU closely is important because the stock defined several important levels that were useful for the Second Day Play.

• 15.50, the bottom of the midday range, is a relevant level. 15.00 is also important as an inflection point from the open that tried to show support in the afternoon.

• The most important level is the low at 14.00. This level was approached twice, and EDU ended up closing near the low.

• EDU did open higher on the second day, and offered some excellent opportunities to get short. Once the stock got below the previous low, it did retrace back into the range from the prior day. This made me wait for additional confirmation of the weakness in the stock.

• Some buyers were still willing to step in, but once the prior low dropped a second time, there was no turning back. The selling pressure mounted, and the stock made three distinct down moves, with periods of horizontal consolidation in between.

Reading the Tape

• The tape in EDU on July 18 was cleaner than it was on July 17, which is one of the benefits of the Second Day Play setup. This offered some excellent entry points with controlled risk.

• Once the downtrend started, there were sellers on the tape that continued to step down from 14.50 to 14.00 to 13.00 to 12.95 to 12.00 to 11.40 to 10.00 and all the way into the close below 9.50.

• When the sellers took a break, the stock would consolidate but never retrace, and a great deal of volume was done at all these points.

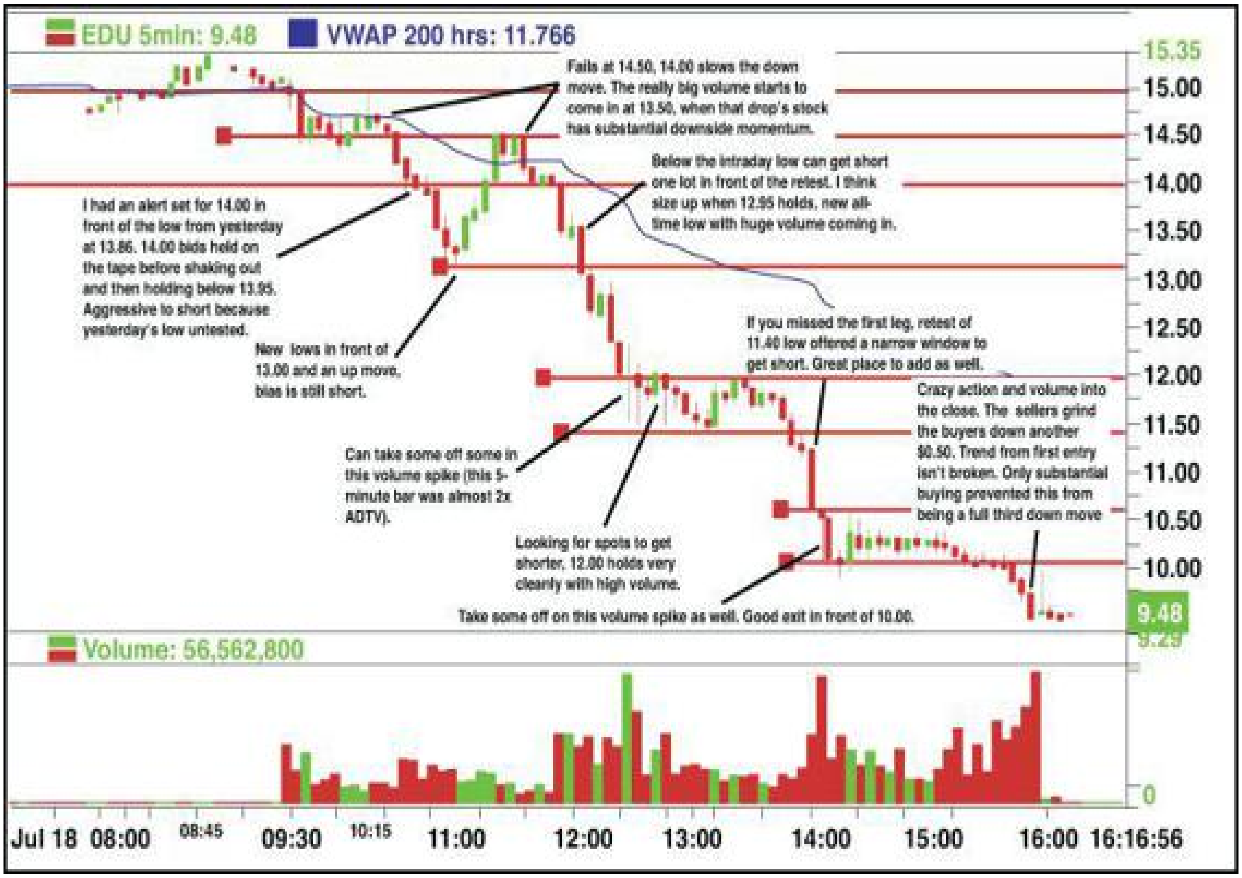
• Paying close attention to the tape made the pattern of the stock clear. When the first down move from 14.50 to 11.50 was over the stock made a finishing print. This was indicated by the massive volume that occurred at 12:30 p.m.

• The same pattern happened again when the 11.50 support level dropped. The tape signaled that move had stalled, with massive volume printing into 10.00.

• Both of these volume spikes were good chances to lighten up the short position and capture the profit, but neither give enough indication of reversal to get flat. The weakness of the stock and the power of the short setup necessitate holding a core short position with size until a clear signal indicates that the downtrend has ended.

• There was no reason to get flat until the close, and the price action below 10.00 was very unique on the tape. There was immense selling pressure and volume, and the only thing that prevented the stock from making another measured move to prices below 9.00 was a resilient buyer who fought the sellers for every cent.

Trade Management



Trade Review

• This trade is an excellent example of a Second Day Play using levels established on a first-day gap. The price action was a bit cleaner, but the exceptional volume stood out to me. EDU usually trades under 2M shares a day, but on July 18 it did over 50M. The longer-term view on the Technical Analysis slide puts the relative volume into perspective.

• The word *long* shouldn't even be a consideration when trading such a weak stock. The only relevant questions are where to get short and where to get shorter.

• Getting short immediately when the new low drops the first time makes sense on momentum, **but I was waiting for a consolidation at a new low** as a spot to get involved, which is a conservative approach. I used the previous day's trading pattern as a clue because it wasn't really good to trade before noon. When the volume came in on a holding offer at a new low, that was a powerful indication that the stock was about to go lower.

• Lightening up on the massive volume spikes made sense. Both times this was confirmed by a subsequent horizontal consolidation without any real retrace, which is a bearish sign.

• Adding at 12.00 made sense to me because the tape was clean and my risk was defined. One of the benefits of the Second Day Play is that the intraday levels are likely to be cleaner and more well defined.

• Adding at the retest of the latest low at 11.40 makes sense to me, as well, but the timing window to get that trade in was very small.

• The price and volume action into the close was like nothing I'd ever seen before. It looked as if there was a buyer or a couple buyers that was the only thing stopping the stock from going down another point and a half. This is a unique Second Day Play in that this stock was exceptionally weak and actually did more volume on the second day than the prior day when it was first in play, but it was a clean, powerful downtrend once the stock held an offer below the intraday low from the prior day.

• **If I am not max size in this setup, I am leaving money on the table. Look for this weakness to continue. The same pattern and approach could work the subsequent day, as well.**

Let's take a look at how the PlayBook can help your trading.

Top Ten Ways the PlayBook Can Help Your Trading

The top ten ways the PlayBook can help your trading are as follows

1. Find the best setups *for you.*
2. Eliminate the trade not worth your intellectual, emotional, and financial capital.
3. Get bigger in your A+ setups.
4. Hold your trades for the real move.
5. Sidestep those annoying HFTs.
6. Accelerate your learning curve.
7. Lower your trading stress and pull the trigger.
8. Take the first step toward developing auto strategies.
9. Think through your trades like a pro so that you can adapt when the market changes.
10. Align yourself with the future of trading.

Find the Best Setups for You

You might ask, "Bella, why not just show us the best setups and let us copy them?" Come on, some of you are thinking that, right? The answer is because this does not help you become a better trader. There, I said it. And I just contradicted 98 percent of all trader education.

My challenge here is to teach you how to think like a pro trader so that you learn how to build the best setups for you. My goal for you is to become a self-directed consistently profitable trader who can sustain through any market.

Frankly, it is harmful to rely too much on the direction of others. You might find yourself in a trade that you lack the skills to manage. Paul Tudor Jones, legendary trader and founder of the Robin Hood Foundation, is famous for cracking that if you gave tomorrow's newspaper to most traders they still wouldn't make money. Let me explain why you need to develop a PlayBook *for you* so that *you* can make trading setups on *your* own (while, of course, still getting some help from some influential trading thinkers/investors).

Barry Ritholtz wrote in his blog The Big Picture (www.ritholtz.com/blog/) that there is no free lunch for the trader/investor. In addition, he wrote:

> No one on television is going to make you wealthy. There is no magic formula or silver bullet or secret hedge fund.
>
> The best investors generate long-term returns by making rational, unemotional decisions.
>
> They do their homework and spend time and effort learning the basics.
>
> They are unemotional, intelligent, and patient. You can be as well.

Ritholtz's advice finds company with legendary trader David Einhorn, who was asked at a recent conference for stock tips. His response? "It doesn't make sense to follow me or anyone else into a stock. Do your own work."

Dr. Brett Steenbarger, trading author and trading psychologist, who has worked with some of the world's biggest traders, concurs: "Every great trader has an outlook and set of methods that are distinctively his own."

Further, I had the honor of sharing the stage with all-time great investor Jim Rogers for an event with Shares Investment in Singapore during a Q&A, with a full-capacity audience of traders/investors. It was an all-day event with multiple opportunities for the audience to ask Jim questions. I counted ten separate attempts to get Jim to share a "hot stock pick." With his southern charm, he sidestepped each request politely and entertainingly. Finally, he stopped on stage, paused (thus grabbing the audience's attention), and taught, "Giving you a hot stock tip will not help you if you do not know how I am going to trade the idea. You may not know how to sell it into a big move or buy more at the right time." (Then he advised everyone in attendance to become a farmer.) From the legend's lips to your trading brain: Make trades your own.

I have seen countless developing traders sit next to superstar traders and make no improvement to their trading. These traders are often befuddled. How can this be? I am sitting next to this great trader but I am not making more? The reason is each trader cannot make money in a setup unless he makes the trade his own. We will offer you the ingredients for you to put together a PlayBook of trades that make the most sense to you, but you have to decide how much salt tastes good to you (in this case, that is, the right balance of the Big Picture, Technicals, Intraday Fundamentals, Reading the Tape, and your Intuition).

Finally, I have witnessed a series of traders fail at one product or time frame and excel at another. Seth Freudberg, who created the The SMB Options Tribe, an educational resource division for options traders, brags about Trader Derek, who was a fledgling trader before he found spread options trading. Remember Angel from *One Good Trade* who never made it as an intraday equities trader at a competing firm? He has found impressive success with a new product and time frame, again options. I have trained guys who were not particularly good intraday traders but found their own niche and pull seven figures from the markets. Find the setups, product, and time frame that makes the most sense to you.

Having said that, we will take a detailed look at some awesome risk/reward setups that we use consistently. You are welcome to co-opt them for your trading and start the work to make these setups your own.

Look, there's no question that you can learn from observing others. But when it comes time to trade on your own, you cannot rely on the style or techniques of other traders. Learn from how they think, prepare, review, and work at their craft, but do not copy their trading. You have to find your own way as a trader, but—and this is the key point—a way that is supported by developing tried-and-true techniques that you take and then make your own. The Beatles "took" what they could from Buddy Holly or Chuck Berry or Jerry Lee Lewis, and then they found their own way, their own style. Same for trading: Understand what the masters have done, and then incorporate what you've learned into your own style.

The PlayBook will get you to stop copying that star trader or guru and crafting a PlayBook that works for you. You will learn to build from your strengths as a trader by best understanding the setups that make the most sense to you. You will learn to trade them more frequently *and* with more size.

Eliminate the Trades Not Worth Your Intellectual, Emotional, and Financial Capital

You are losing money trading setups not worth your intellectual, emotional, and financial capital. Just because you can make a trade and understand that setup does not mean you should be taking it. Most developing traders would improve their trading dramatically if they mined their trading results and eliminated their lesser trades. We call them D trades. And that is being nice about it. Get rid of your crap trades; they not only cost you money but also emotional and intellectual capital.

At the end of the month, most traders will see the majority of their profits derive from their favorite plays. Not only are they in their favorite setups, but these trades work *and* work quickly for you. For example, some on our desk have eliminated most of their scalp trades because they were stressful, not very profitably, and took their attention away from the Trades2Hold that were printing money. Even if you are making some in a setup, if that trade is taking your attention away from your more favorable trades, this is a loss to your trading P&L.

The act of sitting down and writing out the plays that make the most sense to you helps to synthesize the trading data for you. It narrows the data to only the plays that you like the best. You do not need to be in every trade. You need to be in as many trades that work, make the most sense, and are not overly stressful to you. Change this about your trading and you will see substantial progress both in your trader well-being and profitability.

Get Bigger in Your A+ Positions

Most failing traders, to their detriment, overly obsess about their trading weaknesses. Your PlayBook will force you to spend much more effort building from the setups that work for you. When you construct a list of your best trades, you will have greater confidence to size up in a similar pattern the next time you see one. You will have sorted out the setups that don't work for you from the ones that do, and you will consequently intellectually and mentally spend time preparing for the setups that are worth more risk. Every trader wants to get bigger. Understanding and then archiving the variables of your best setups will help you trade with more size when you spot your favorite setups. The act of putting down on paper these A+ trades will prepare you to be more willing to add risk to such future setups in real-time.

Building your PlayBook will help you get bigger in your best positions. Trading coach Dr. Doug Hirschhorn offered in an interview at Trade2Win.com that most traders leave money on the table because they do not take on enough risk when the best opportunity is present (www.trade2win.com/boards/articles/19576-doug-hirschhorn-interview.html).

Let me offer a trading technique from our desk that you can use to improve your P&L. From your entire PlayBook, determine your A+ trades, the best of your best trades. For these setups, develop a *rule of risk* that you must take when you spot an A+ setup. For example, we ask our traders to place 30 percent of their intraday stop loss on every A+ setup. After each month of profitability, gradually raise your intraday stop loss and hence your size with your A+ setups. Over pizza on Stone Street, Dr. Steenbarger shared with five of our better traders, "As you slowly build your size, you will see yourself as a big trader and the stress of those larger positions diminish. Now you are just a big trader doing what you do: trading big."

If you fail to place this amount of risk, you are guilty of a trading error. You can lose money on my desk, but I get after you when you pass on an excellent risk/reward opportunity. I caught one of my traders not big enough in a CMG trade for which he was 2 points in the money, with the stock still trending down.

Bella: "How many shares do you have?"

SMB trader: "100 shares."

Bella: "Why bother? Why were you such a wuss? What is the worst thing that can happen? You have to take on risk when the market offers a favorite setup."

So this work will leave you understanding your best setups and with our rule of risk taking on more size in them. This is your personal P&L elevator.

Hold Your Trades for the Real Move

There is a knock on my door. Trader A walks in, "Bella, I have trouble holding my positions for the real move. Any advice?"

This scene has repeated itself every week since the inception of SMB.

An e-mail for an underperforming prop trader at another firm: "Bella, I am cutting my winners too early. Any advice?"

This e-mail has repeatedly been sent by various traders since the beginning of SMB.

Tweet from a retail trader: "@mikebellafiore advice on how to hold my winners longer?"

Lots and lots of these tweets have come my way.

Okay, be honest, how many times have you beat yourself up over selling too early? It's alright; by the end of this book, we will help you with this.

So we have an issue we need to discuss: holding your trades for the real move. Generally, traders have not taken the time to understand what I call a Move2Move trade from a Trade2Hold. That is, is this a very short-term trade, a Move2Move trade? Or is this a Trend Trend Trade, Trade2Hold, where we are trying to capture the real move? First, you must answer what you expected out of the trade before you can determine whether you failed to hold. Often, a trader laments not holding with a Move2Move trade that was exited properly.

Your PlayBook will help you map out Move2Move trades and Trades2Hold for your trading. If you are in a Move2Move trade and a stock continues higher, you will not fret that you left money on the table. You didn't. You made your Move2Move trade. That was your trade, and then you moved on. What happens after does not matter.

With your Trades2Hold, we encourage you to develop a plan for exit. For a long, we say hold your Trades2Hold until there is a Reason2Sell: your plan to exit. If you do not, you traded poorly. But if there was no Reason2Sell (explained in detail in Chapter 3) and your stock reversed, well, then you did the right thing. In this instance, don't stress about giving back profits. Remember that your job is to do the right thing. It is not to make as much money as you can with each trade. This is an important distinction. Such unreasonable pressure on your trading is an unhealthy spiral to trading frustration.

Sidestep the HFTs

I stood in our training room fielding a question from a new trader. I had heard this question from every starting trader training class since 2009.

With a look of concern, the newb asked, "Bella, how do we combat the HFTs?"

KMay, who had taken our college summer training course, traded while in college, and had just joined our prop desk in Manhattan, was sitting in on this teaching session. Immediately, she responded, "We do not trade against the HFTs. We do our own thing and stay away from them." Thank you KMay.

In 2009, we shifted our trader training from momentum trading and scalping to Trades2Hold or intraday swing trades. We did so to sidestep the HFTs who were dominating these strategies. There is close media attention to the effects HFTs have on our markets and trading strategies. Some, like Mark Cuban, owner of the Dallas Mavericks, have gone so far as to call for a transaction tax on short-term trades. As an aside, and I say this respectfully, I am not sure why he has an opinion on this; it is not exactly his area of expertise. You don't see me go on ESPN offering advice about whom the Mavs should trade, though if we grabbed a beer I would spew an opinion on the matter. Spencer went on Bloomberg TV articulating his expert opinion on why this was not a good idea for the U.S. equity markets (you can find his non-expert opinions about the NBA on his Twitter feed).

Sometimes we just cannot compete against HFTs. For example, I cannot beat an HFT to scalp in and out of a stock for 20 cents. I get cut on the bid, watch the HFT get a print .5 cents above my bid (yes, you read that correctly: .5 cents), and then they are off. I could sit there and work myself into a stir with all the bids and offers for which I get cut by HFTs trading through dark pools, but I don't have time for that. Because I am not a Buddhist monk, I might swear at this HFT chiseling under my breath (even occasionally out loud). But then, because this is a waste of energy, I quickly refocus. Last time I checked, I do not set securities policy or determine rulemaking for U.S. equity trading.

Because I cannot microscalp anymore because of the HFTs, I have to play another game. Intraday swing trades is that new contest. We focus our PlayBook on Trades2Hold, patterns where stocks will trend for multiple points intraday. HFTs still frolic in these patterns, shaking me out, reversing clean trends, but this not so often that I cannot compete in this game. As KMay taught, we sidestep the HFTs.

Accelerate Your Learning Curve

Taking the time to archive your best setups for each trading session will speed up your learning curve. From my seat time, this is one of the biggest reasons for traders failing at our game (or more appropriately, from a lack of time). In the end, many need to make a certain amount of money by a given time, and if they cannot, they have to move on. It might not be that they cannot do it, it's just that their money clock ran out. Anything you can do to increase the reps you get with trade setups is giving yourself a better chance of profiting more quickly.

When you make a trade in real-time, that is one rep. When you take the time after the close to archive that setup, that is another rep. When you review that setup, that is another rep. When you share this trade with your desk and discuss it with another trader, this is another rep. From past research we can conclude, your brain makes no distinction between trading live and thinking of a trade as live. All of this adds trading experience for your trading brain. All of this increases your chances of making it in our game and keeping that money clock from sounding.

Focusing on your best trades minimizes the data that the new and developing trader must synthesize to make trades. You search for your setups and exclude others that are not in your PlayBook. This helps you execute better on your best setups, since your decisions are not distracted by plays that don't appeal to you or have not worked.

Your PlayBook offers a framework for you to discuss specific setups with other like-minded traders. You're not having a general trading discussion about trading AAPL; you're having a detailed talk about an Opening Drive Play in AAPL on 10/12/12 at 9:45 in AAPL. This is a better and faster way to make trading progress.

Lower Your Trading Stress and Pull the Trigger

Which trades do I take? How big should I be? For the new and developing trader, anxiety builds trying to answer these questions. A trading session can be so stressful, preceded by a preparation session of all stress. But when you understand what you do best, and when you have compiled what you do best in print form, you find yourself free to just focus on executing. You will find that you have decreased your trading stress.

Your PlayBook will help you view each trade as a pattern you have predetermined is worth risk. You will understand that your job is to place risk when you see setups that offer an excellent risk/reward opportunity. The act of compiling trades worth risk will help you to lessen the stress manifested from failed trades. Your internal conversation will go like this:

> That is a trade in my PlayBook. I want to put on risk when I see these trades. I cannot control the outcome. Did I do the right thing? Yes. Okay, great, so now next trade.

As opposed to an internal conversation like this:

Should I make this trade? If I make this trade I might lose X. What does this company do again? I don't know if I should make this trade. What are my rules for this trade again? Do I like making this trade? Wait is this a bullish flag pattern or a doji round-house reversal underneath-the-shirt wedge 80/20 pattern? (OK, I made up this last technical pattern. But you get the point.)

And then you miss the trade or enter too small. This is not how a pro trader thinks.

Building a PlayBook helps you to pull the trigger in your trades. That is a Trend Trend Trade, short 30 percent of my stop. That is an Opening Drive Play, long 10 percent of my stop. That is a Reversal Trade, long 10 percent of my stop and waiting to add size. It is not that the pro trader thinks faster than you; it is that he is just spotting his favorite patterns and executing while the newbs are thinking and twisting themselves into a ball of confusion. This is a common obstacle for many traders. Thinking through your trading, reviewing your work, talking trading, working with a mentor—any act of you reviewing your trading makes pulling the trade in that reviewed setup more automatic.

Take Your First Step Toward Being an Autotrader

Mapping out the trades that make the most sense to you is your first step toward being an autotrader. You are developing rules for when you want to enter the market. This is what autotrading, or as others say, quant trading or algorithmic trading, is.

One thing I encourage more experienced traders on my desk to do is create rules for how you would trade each set up. There is a "Trade Strategy" section for how to trade a Trend Trend Trade, for example. If you trade this setup 1,000 times, how would you trade it? This is a general framework for how you would attack this trade; if some variables then differ, you can make small adjustments from your system.

Even starting with simple rules as outlined here (and from a new trader on our desk in his PlayBook) is a start in your quant career. Obviously, as you get more serious about developing automated strategies, you will add more rules to your strategies.

Gap and Go Strategy

- Find a stock that has gapped up on the open more than 3 percent on relative increased volume.
- Find areas where the stock is consolidating above the gap or levels where it is safe to enter on a pullback to prior resistance that can act as support.
- Once the stock can break above the consolidation holding the gap levels, you have a well-defined entry and should expect the stock to quickly find higher prices on the breakout.
- Adding at places where the buyers are able to hold the bid above the consolidation break gives room to add size with clearly defined risk.

SMB created a *joint venture* (JV) in NYC with KTG, Kershner Trading Group. The JV:

- Backs experienced traders
- Trains and backs new traders who go through our recommended college training path
- Backs, coaches, and mentors the right underperforming, developing traders
- Funds automated trading models

We take all the downside risk and encourage our traders to trade big.

We agreed to this JV partly because KTG had developed new technology to allow discretionary traders to build trading models without the necessity to code. (We also provide on-site quant support for the models that need it.) Their proprietary software allows discretionary traders to build models for their best setups. In today's trading environment, we cannot miss any of our best setups. And we must be big in our best opportunities. GMan wrote a series of automated strategies in a month with these tools. One experienced trader went from underperforming to a seven-figure path almost instantly because of this improved technology. Start mapping out your best trades with your PlayBook and find software and tools that will enable you to express these trades so that you pull as much money from the markets as possible. Automated trading is no longer just for the quants.

Think Through Your Trades Like a Pro

Trades work and then do not work. What is most important is for you to adapt when the market changes. Understanding how to think through your trades will help you shift to setups that are working for the changing market. This saying sums it up the best: Give a man a fish (tell him a trade to make) and you feed him for the day. Teach a man to fish (how to think as a pro trader) and you feed him for a lifetime. For example, when I first started trading, I was a relative-strength tech trader. Those plays in INTC, MSFT, and CSCO do not work anymore. But what does stay with me is how to craft a trade that offers an excellent risk/reward, so I can take this thinking and focus on intraday trend plays that are paying in today's market. Using the five variables to construct PlayBook trades provides a thorough and high level of trader thinking for each trade that sustains.

Your Trading Future Starts with Your PlayBook

When SMB lost some quality traders in 2009–2010, our career path was insufficient. HFTs and trader losses caused my firm to develop a better model for trader and firm. The margin of error is too small for a newbie to be just a discretionary intraday trader and then a bigger discretionary intraday trader. Trading data does not support this as a realistic career path for too many (there are exceptions). What is the future career path for a trader? It's to be a multimarket, multiproduct bionic discretionary quant trader—all made possible by the PlayBook.

Before we look at what that is, let's review an unfortunate anecdote from a former prop trader in that antiquated career path:

> Dear Mr. Bellafiore,
>
> My name is Brady [named changed], and I just finished reading your book *One Good Trade*. I know that your book was released two years ago, but I figured that you'd still enjoy receiving positive feedback from your readers.
>
> In all honesty, I think your book is spot on when it comes to the world of prop trading. I've read many day-trading books in the past, but none of them come close to yours. Unlike the other books that I've read, so many sections of your book offer insight/knowledge that is actually relevant to today's world of trading.

Also, I had a lot of laughs reading stories of your former/current SMB traders. I worked on a prop desk in St. Louis [location changed] for two years, and many characters in your book were similar to traders whom I encountered on my own desk. My favorite story of yours was about the new trader who put up monster numbers on his first day but did so by trading poorly. We had a guy on our desk who made $3K on his first day of live trading, but he was trading like a putz. On his second day, he put up similar numbers, and our desk aptly gave him the nickname Golden Dick because everything he touched turned to gold. When our head trader came back from vacation and saw the type of risk that Golden Dick was taking to generate his numbers, a closed-door meeting (shouting match) ensued, and Golden Dick's days were numbered. Several blowups later, and Golden Dick was too afraid to trade anything but the demo.

Before you even wrote your book, I used to visit SMB's Web site on a daily basis. You and your team really offer a lot of help and knowledge to the trading community. When I worked on the desk, my mentor/boss/funder named Boss [named changed] (who was also rich from trading the Internet bubble) used to bust my balls for reading your team's blogs. He didn't approve of screen recordings/psychology/notes/etc. His philosophy was "Trade, Trade, Trade. That's the only way you can improve."

I love Boss and would do anything for him, but he is a poor teacher. There is no doubt that Boss is an incredible and profitable trader, but he could never explain his methodology coherently. His tape reading skills were superior, but when you asked him to explain his methods he'd tell you to "figure it out by yourself." In many ways, your trading skills/system are alike. However, he preached 10c plays and trading a basket of IPO stocks (which you could only trade on the long side until they became unrestricted).

In late 2008, Boss used his own personal money to start a prop desk. His idea was to hire 20 new graduates and train them to read the tape and scalp the crap out of the market dime for dime. However, without proper tutelage and resources, the desk did not perform well. One by one, Boss began axing the unprofitable/unmotivated traders. I remember one day I had just

> finished reading *Psycho-Cybernetics* by Dr. Maltz, and I was anxious to use some of his quick positive meditation techniques. I closed my eyes for a moment to clear my mind, and when I reopened them a trader named Eddie who sat on my right was gone. I asked the other traders where he went, and they said that "Boss just fired him." So much for positive meditation. Two years past, and 20 traders got chopped down to me and 2 others (one of them being Boss's brother).
>
> It's easy to call yourself a trader, but trading is never easy. Despite my ups and downs, the daily 4hr+ round-trip commutes from [where he lived] to St. Louis and my long-term girlfriend (now fiancé) busting my balls, I still truly love equity trading. It's the greatest job in the world for those who can make the grade. I'm currently a trader at a BD/IA in Boston, which involves more operational duties than actually trading duties, and it's tough knowing that there are other traders out there living the dream. Your book actually rekindled my fire for trading, and I've been trying to use your firm's philosophy to find stocks to trade. However, with my firm's $28 ticket charges (bogus) and terrible buying power, trading just isn't quite the same.
>
> I just wanted to thank you and the other traders at SMB for all the wisdom you share on a daily basis. I feel like I learned more about trading by reading your book than I did from actually trading those two years. I don't know if I'll enter the arena of intraday trading in the near future (fiancé and my advancing age seems to be my kryptonite), but if you ever opened a shop in Boston I'd be the first person to send in my resume. Your philosophy and culture is simply outstanding, and that's something that I could have surely used two years ago.

This former trader followed up with a few questions.

I wrote about the failure rate of a proprietary trader previously. It is time for an update. Let's use a follow-up question asked to me by Brady as the centerpiece for this discussion:

> Mr. Bellafiore,
>
> When I parted from the desk, my mentor/head trader said that I started trading during one of the more difficult times to learn how

to trade. At the time, I didn’t know if he was blowing smoke up my butt to make me feel better because he knew how much effort/time I put into it.

Are your newer traders (one to two years of experience) having success in the current market? From time to time, my mind starts thinking about trading again, and I wonder how the newer traders are faring in this market. I still keep in contact with the one or two traders who are left at my old desk, but they haven’t brought in any new traders in months.

Thank you for your time.

My Response and the Future of Trading

I do not like to say someone is a failed trader. I call this the *irrelevancy of ones*. You traded at one place, with one style, under one business model, one infrastructure (for education, coaching, and mentoring), during one market time, with one platform and set of trading tools, and during one short phase of your life. What does that really tell you about your trading?

Intraday trading has been much harder for the new trader. The margin of error to succeed is much smaller than at most others times in my trading career. This is not indigenous to intraday trading. My friends in the trading business tell me it extends to equity trading as a whole, futures, FX, hedge funds, and so on. But I am only an expert in my field and will stick to that. I have been saying and working very hard to get our industry to pivot and adapt.

First, as traders, we must improve our methodology. We must understand our best trades and a find a way to archive these opportunities: your PlayBook. There are too many old school traders overly reliant on their intuition. Intuitive tape readers or other intuitive technique traders without a clear methodology must do better organizing their best trades. Further, traders must become more bionic. After traders map out the rules for their favorite setups, they must be armed with custom filters that alert trader to *all* of these best opportunities. We cannot miss our best trades in this tougher market, nor, with the ability to build better trading tools, is there an excuse to. Since traders will be in more trades as a result of better alerting technology, they also must have access to exit management tools to handle the additional positions proficiently. Now we have created a bionic discretionary trader, producing increased P&L.

But we can do even more, like trade other products. Options trading based on the principles of your best intraday trades in your PlayBook can be very effective. Some patterns work better with other products. You may have noticed SMB added The Options Tribe, an options trading and education arm. Learn to express your best setups with other products. Now we have built a multiproduct bionic discretionary trader.

But there is still more.

Joining the quants is working very nicely for some intraday traders. We have added this to our portfolio on the firm and individual trader level. The problem is most traders cannot code. Proprietary software now exists that makes it easier for the noncoder to build automated strategies. Now we have sculpted a multiproduct bionic discretionary quant trader.

Finally, as our markets become increasingly interconnected, expressing our favorite setups in other markets will be the norm. I recently worked with South African/London traders who added U.S. equities to their trading quiver. All of this engineers the multimarket, multiproduct bionic discretionary trader. And all of this is possible only if you build a PlayBook of your most opportunistic trades.

We still see a solid success rate of 30 percent to 40 percent for those who take the right path before they turn pro, like going through college training and trading. Also, we are still having success coaching and mentoring underperforming developing traders from firms that do not add sufficient value. What we do not see is the one-style, one-product newb with little to zero experience trading on no-edge technology and with six to eight months to prove himself having much of a chance. (I have been stuck housing SMB around trading arcades such as this, with five guys interviewing Wall Street dreamers for their next conquest. They say things like, “You have a background in finance. You probably will get out of the gates very quickly and make a lot of money." No they won't. What kind of a jacka$$ would say something like that? The two times SMB was caught around an environment like this, we picked up our entire firm and left within months.) We recommend for these traders to join our farm team at SMBU or something like our farm team and spend some time developing skill, being more patient and realistic about the time required to trade profitably, before they consider trading pro.

Anyway, I hope that helps. Marry that girl!

Thanks for sharing your story with the trading community. It was very well-received.

If you are ever in NYC, stop by and we will take you to lunch.

MHB

My hope for you is that this book gives you the tools to build your trading PlayBook. It will help you frame your own unique PlayBook that best utilizes your strengths. Remember the teachings of Ritholtz, Steenbarger, Rogers, and Einhorn. And then, from this PlayBook, you can sort out you're A+ trades, the ones that work best for you, and add tools to become more bionic. Then later on you can express these ideas in other markets (see Chapter 11, "South Africa"). You will learn whether you can express these setups better with different products. You will have the tools to learn other products by developing a series of PlayBook trades for different instruments. And all this work will leave you with detailed specificity about the plays that work for you. You will then be just a few steps away from being an autotrader, thus adding another revenue line to your trading and increasing your P&L. This is your majestic trading future, sponsored by your Playbook.

Now let's meet Shark, an inspiration for those who have never traded before and want to be a star trader.

2. Trade Like a Shark

In 2009, this was my standard pitch to new traders:

> Do not come to SMB if you are not willing to work hard. This will not be easy. You must work harder than you ever have in your life. If you do not work hard, we will get rid of you. Nothing personal, just understand who we are. If you do not do what we ask, we will bench you, which means place you on the demo.
>
> We do not take off trades. One Good Trade, One Good Trade, One Good Trade. I am going to push you to improve every day. And our goal is for you to become as good as you can be. Not good, but your absolute best.
>
> There are no guarantees. There is a good chance you are not going to be good enough. But if you really want to learn how to trade and become a pro trader, this is a great place to start.

2009/10 was a difficult time to start a trading career. First, most just cannot handle what we expect from them (more accurately what the market expects from them). Add to this that during 09/10 SMB was not very good. We had lost some traders. We were rebuilding. I could not be around much because of my family issues. New recruits were not surrounded by scores of experienced traders. Add to that, most prop firms were scaling back at this time as discretionary traders were mostly unprofitable. Add to that, the market kept going higher as the financial media kept warning us another major move down was imminent. Add to that, *high-frequency traders* (HFTs) were eating our lunch with past successful trading strategies. Add to that, regulators were applying pressure on prop firms that made trading more expensive for all new traders. Man all those extra fees really add up.

During this time period, we received this cover letter:

> Dear Sir or Madam:
>
> Please accept this e-mail as an application for the Entry Level Trading Position posted on Craigslist. I recently graduated from Ithaca College in Ithaca, N.Y., with a Bachelor’s Degree in Business Administration and a concentration in finance. I am confident that I am a perfect candidate for a trading position. I am

hardworking and intelligent, as demonstrated by my academic success. I am level tempered, which is a characteristic that will ensure that I do not let emotions negatively affect my trading strategy.

I love the sort of strategic thinking that goes into assessing macroeconomic variables to predict the movement of securities and currencies. I have always loved and been successful at games that involve a similar type of strategizing (e.g., poker). While I have not had real-world experience in the financial industry, I have gained experience researching potential investments in the Core Trading Consultant Investment Club at Ithaca College. I also have experience trading stocks with my personal online account. Through trading online, I have learned the importance of using stop-loss and limit orders to manage risk and lock in trading profits.

Attached is a copy of my resume. I would be delighted to speak with you further about the position after you have had a chance to review it.

Thank you for your time and consideration.

- This is a polite, nice, and well-written letter—one that would never stand out on the Street.
- The candidate did not graduate from an Ivy League school.
- Where is the perfect math SAT score?
- He didn't play DI sports, like so many hired new traders.
- That small online account didn't add up to much.

Yet this letter started our road back!

This young man would in two years become a consistently profitable trader, and a d*** good one for that matter. But he meant so much more to us. He showed everyone that you could make serious P&L as a discretionary trader during market conditions where many were failing—even the scores of consistently profitable experienced traders across the Street. He showed you could succeed without some of those experienced traders we had lost. He was the first new solid trader we developed after all our recent challenges. Through his actions, he proved trading skill could be built through hard work.

Meet Shark, who will teach you

- The importance of a detailed daily trading review
- The power of embracing a mindset to improve every day
- That anyone with the passion to work at this game of trading can compete
- The importance of adding value to your surrounding traders
- The necessity of controlling your emotions
- The significance of being self-actualized
- How a relentless determination adds P$L
- How to find the best stocks
- That good traders focus first on the process

I teach my guys that if a quality trader goes to grab lunch, follow him and start a trading dialogue. If he is going for drinks with the boys, show up and talk trading. Heck, if he hits the john, head for the john. So my advice to you is absorb every possible detail of what made Shark successful.

Take notice that none of these attributes are highlighted on a financial market TV show, yet this is the information that leads to consistent trading profits. Imagine this: “Next up is Shark from SMB Capital, who will detail his PlayBook trade from today, live on [insert market show].” We supposedly live in the information age yet receive little information about what it takes to really become a profitable trader. What we get is this: “Next up, someone trying to make a name for himself, who has no idea where $SPY is headed but is going to overconfidently forecast its direction anyway, live next on [insert market show].” Ubiquitous predictions blanketing what we will call the Financial Media Entertainment Complex distract investors and traders from the real work of real pro traders. This chapter introduces you to a consistently profitable trader (a streak of 23 months and counting) and how he does it, our next outstanding trader, Shark.

The Work Output of a Pro Trader

I stood in our training room livid at the underperformance of our desk. The trading I had witnessed from my guys was unacceptable. There’s a standard for trading that’s required daily, and almost everyone in the room failed it badly. There’s nothing worse than having a good day of trading opportunity only to realize that the traders under you performed below their ability because of sloppy preparation. I address this immediately, sometimes with my voice raised. Communicating standards to my traders is my most important duty.

Rewind six months. I stood at the front center of our SMB training room and introduced a new review exercise for our desk to improve their trading performance. I called it the PlayBook (unaware this would make a great title for my next book or that I would write). All the traders voluntarily would archive their favorite setup of the day that made the most sense to them. They would record this setup in our proprietary template form we coined the SMB PlayBook.

My directive was simple: “Send me a trade in SMB PlayBook form; I will review it and give you my feedback.” Each night I would edit these PlayBook trades, send them back to our students, and then have them placed in a new training section of the SMB Foundation, the SMB PlayBook, which all of our traders could access. Each of our traders could see any PlayBook trade by another trader, improving their learning opportunities.

In a short six months, something became both impressively and disappointingly clear. This one kid kept sending me play after trading play. He had not stood out to me beforehand. Who the heck was this young man? My informal evaluation of him was “on track” at best and “no opinion” in truth. The partners never took extra time to daydream about his unlimited potential like we did for a few others in his class. Of one classmate, Spencer touted, “He holds things better than anyone we have trained. We are going to make a fortune off his trading.” This rookie was good. Steady. Consistent. Improving. Likable. But one thing about him stood out like Kate Upton adorning a red dress at a cocktail party. Above all others, after we introduced the SMB PlayBook to the desk, his work output was unmatched.

So there I was, furious at my guys for their underperformance. My blood pressure had to be at a danger stage. I suffer from the beginning of inherited heart disease so I could drop dead at any second during a talk like this. I stopped and paused a little too long, having found an epiphany after my anger. Everyone now was focused on me and my next words. I scanned the room looking into the eyes of each trader, pausing even more. I continued (in a low, soft, and concerned voice).

“One person has done more PlayBook trades than everyone else combined in this room. One person. More than everyone else in this room. He has improved the most. He hasn’t been underperforming. Shark has done more PlayBook trades himself than all of you combined in this room. You want to get better? You want to eliminate days like this? You want me not to stand up here and rip you for your underperformance? Do the work that needs to be done. You should be sending me a PlayBook trade every day before you leave the office. Going forward, no one is to leave the trading desk without first sending me a PlayBook trade.”

And that was that. Archiving a daily PlayBook trade became mandatory. This was now an official, integral part of our trader development program. It was all because of Shark’s work output. Not only did he lead our desk in PlayBook trade submissions, but he also encouraged us to rework our daily review.

The Shark Daily Review

There is nothing spectacular about Shark’s daily review, which you can access in this section. Simply put, it represents the necessary work to improve as a trader that Shark does after every close. What I will say about this review is twofold:

1. He improved the original SMB daily review without prompting.

2. He does this review in detail every day without fail.

He didn’t complain that our review was not good enough. He didn’t wait or rely on someone else to fix this review so that it would be better for him. He took the good parts, improved them, and added some new ones that made the SMB daily review better. You are either part of the solution or part of the problem.

The hard part about these reviews is the ability to do them in detail every day no matter what your mood or energy level after the close. Take a few rips and finish decidedly negative, and it’s easy to want to skip out after the close. Spend six and a half hours fully immersed in an ocean of cascading numbers and you may want to head home right after the bell. The greatest value to this work is that with each successive day, the work compounds, leading to slow but meaningful improvement. Miss a day or bring low energy to a review, and you have squandered a trading session of maximum improvement. Shark doesn’t have many days like that.

The goal of this daily trading review is to

- Find the plays that make the most sense to you
- Eliminate your mistakes
- Internalize your best trades
- Set up a process for me to give a nuanced response to your trading

This is an oasis of specific critical feedback for the developing trader. Also, it's this recording of your best trades that helps you trade these setups better in real-time. You are starting the slow process of internalizing your best setups and building intuition, the gift possessed by only the experienced trader. You make these trades your own so that you can instinctively execute them in real-time. This is opposed to copying some canned setup from a trader more famous than you and worrying whether you have his damn trade right while market data is flying by. It all starts with your work after the close. These are the moments when you are becoming great.

Here is a review Shark sent to me after a solid day of trading, which may give you an idea of how to review your work daily. This is more important than any setup I or someone like me might share. Stock by stock, our traders review their work. The SMB Chop Tracker is implemented into this review, crunching the daily trading statistics for the trading session and each stock traded. (Note we have recently changed our daily trade review incorporating Evernote, which helps us take screen captures of chart setups most interesting to us and add quick notes about the trade. Check out Evernote as a tool to categorize and compile your best setups with powerful note-taking functionality.)

I ask Shark and traders like him to focus on the following during their trade review:

- What setups worked best for them?
- What did the setup look like that worked best for them? Was there a catalyst before the big move in their best setup? If so, we want the trader to replay this by archiving exactly what the stock looked like before the big move.
- Where could the trader have been bigger responsibly?
- What is not working in his trading and should be eliminated?
- What stocks are they trading well?

- What stocks do not fit their trading eye? (I can’t trade SNDK. I trade GS worse.)
- Are they trading better during the open, midday or close? If so why? And what adjustment should be made to correct timeframe underperformance and maximize time frame overperformance?
- Are they trading efficiently by adding enough liquidity? Are they bidding and offering to buy stock or just hitting the bids and taking offers? The latter is sign of bad trading.
- Are they keeping their losses small?
- Overall, how can they improve?

Do not worry if you do not understand every term he uses or grasp every trade reviewed. Take away the importance of developing a detailed trading review after every close.

Shark’s Daily Review: An Example

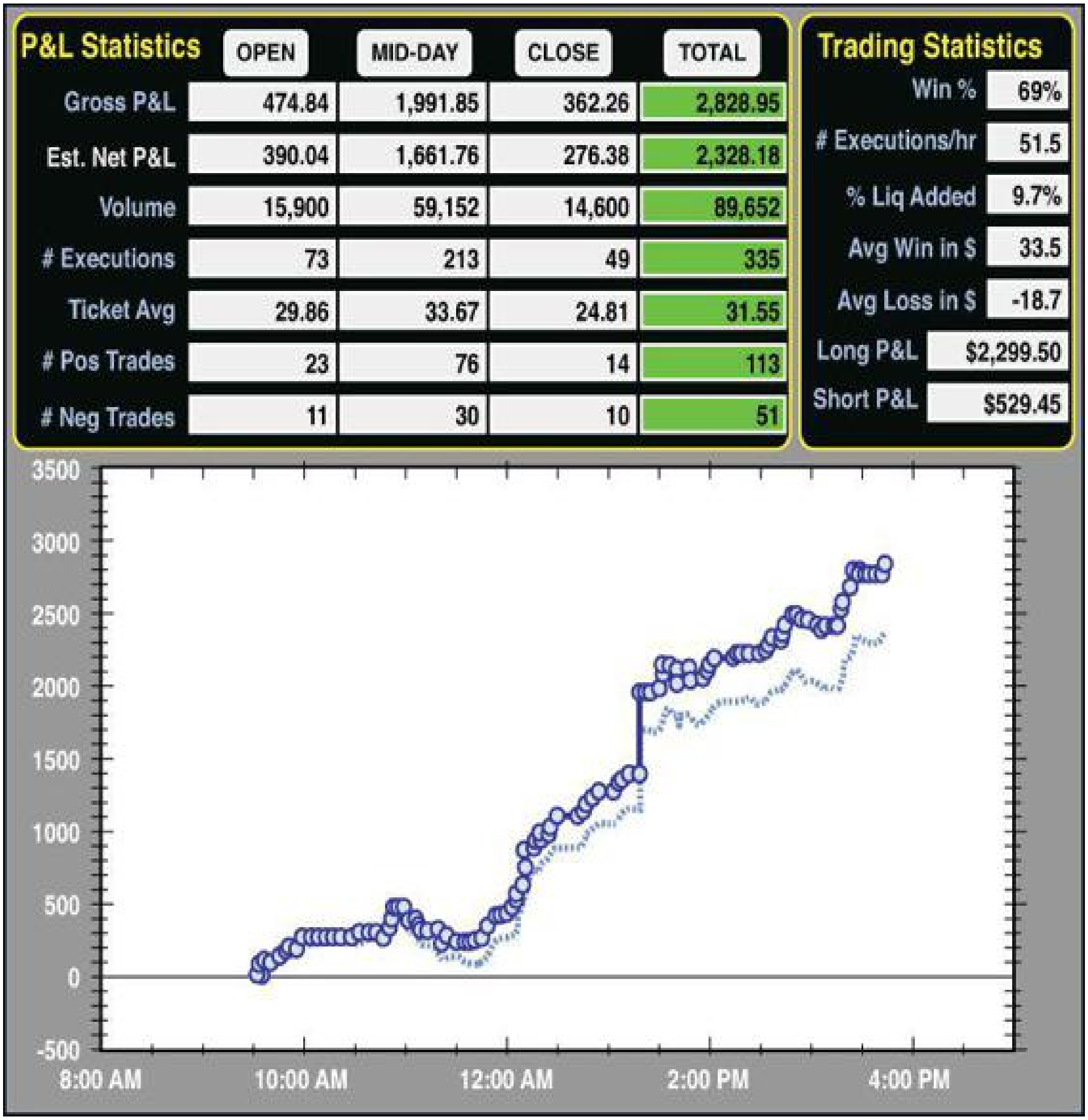


Figure 2.1

Overall, I see myself cutting out the stocks that aren't moving and that is really helping me increase my results. A lot of times I'm just cutting size right away if things don't work in my favor, and that is really helping me stick to the better stocks.

I am staying aggressive but selective to what has potential—and staying with stocks that can make my day, and there has been enough opportunity to put together some good days. I'm really eyeing the five grand day that I think is in my grasp. This next earnings season I'm gonna focus on not letting any sort of overconfidence creep into my trading as a main goal going forward this next week, to just take what is given and to continue to work on getting bigger in things that have good potential.

HSH

I messed this up by getting impatient and buying too soon into the pullback (see Figure 2.2), but I did do a good job recognizing this stock and trading it with size, recognizing that I can trade it actively by just working hard to find the right stocks. You never know what you might stumble onto, and I'm doing a better job to recognize what has potential lately and sticking to the better stocks.

P&L Statistics	OPEN	MID-DAY	CLOSE	TOTAL
Gross P&L	0.00	945.60	-13.48	932.12
Est. Net P&L	0.00	867.38	-24.46	842.92
Volume	0	14,560	1,800	16,360
# Executions	0	56	3	59
Ticket Avg	0.00	64.95	-7.49	56.98
# Pos Trades	0	32	0	32
# Neg Trades	0	1	1	2

1200

Figure 2.2

BBY

On the open, I think I could have done better off the 70c buyer, but it was hard to trust (see Figure 2.3). I did a decent job with my sales for the most part getting light into the spike. But the thing I am most proud off on the day was my ability to react and trust my skills when I saw breaking news hit the tape. I just knew it right away and ended up just hitting the bids for 1,000 shares long and getting short 800 and making a really quick chop. That was pure instinct, and that's why it pays to be at your seat and watching your stocks. This is definitely something I would not have been able to do probably just three months ago.

P&L Statistics	OPEN	MID-DAY	CLOSE	TOTAL
Gross P&L	342.68	526.39	0.00	869.07
Est. Net P&L	293.32	493.05	0.00	786.37
Volume	8,700	5,900	0	14,600
# Executions	31	20	0	51
Ticket Avg	39.39	89.22	0.00	59.53
# Pos Trades	11	4	0	15
# Neg Trades	3	4	0	7

1000

Figure 2.3

VHC

Nice pull in trade here starting at 85 cents then using the time of day and an offer at a nickel to get up to 900 shares (see Figure 2.4). That is a decent size position for how sketchy this stock is. I think I scaled out a little too early, eventually holding just 100 shares to 38, but I did a good job recognizing the trade and getting in.

P&L Statistics	OPEN	MID-DAY	CLOSE	TOTAL
Gross P&L	0.00	0.00	429.94	429.94
Est. Net P&L	0.00	-0.77	422.22	421.45
Volume	0	300	1,700	2,000
# Executions	0	2	11	13
Ticket Avg	0.00	0.00	252.91	214.97
# Pos Trades	0	0	8	8
# Neg Trades	0	0	0	0

500

Figure 2.4

GDOT

I noticed this consolidation around 50 and 60 cents, bought a chunk, and was just too big for the share volume, so I bailed on in light of it (see Figure 2.5). I ended up trailing this eventually and stopping myself out below 20 cents. Good job using the radar here, but maybe I could have tried to hold a bit more.

P&L Statistics	OPEN	MID-DAY	CLOSE	TOTAL
Gross P&L	0.00	264.94	0.00	264.94
Est. Net P&L	0.00	241.44	0.00	241.44
Volume	0	4,200	0	4,200
# Executions	0	20	0	20
Ticket Avg	0.00	63.08	0.00	63.08
# Pos Trades	0	10	0	10
# Neg Trades	0	0	0	0

300

Figure 2.5

NKE

Nice opening drive, though I was a wuss with my size (see Figure 2.6). Bought the pullback well and later tried the short, holding it under 20 cents. I got long above 80 cents but overtraded the pullback and ended up giving way too much back.

P&L Statistics	OPEN	MID-DAY	CLOSE	TOTAL
Gross P&L	256.90	63.19	-104.92	215.17
Est. Net P&L	245.49	38.59	-128.18	155.90
Volume	3,000	4,554	3,900	11,454
# Executions	20	27	15	62
Ticket Avg	85.63	13.88	-26.90	18.79
# Pos Trades	8	6	0	14
# Neg Trades	3	5	5	13

400

Figure 2.6

Overall I think I did okay here, but I needed to be bigger off that 20c lift on the open that was an absolute layup.

STZ

I had a hard time with this one on the open (see Figure 2.7). I finally I got in above 50 cents and was able to hold it and add at $28. But if I was a little bigger from the get-go, I could have been bigger around the 28. I eventually stopped out under 35 cents and didn't revisit, but I did a good job at last turning profitable after getting wicked out a few times in this one.

P&L Statistics	OPEN	MID-DAY	CLOSE	TOTAL
Gross P&L	1.14	201.96	0.00	203.10
Est. Net P&L	-5.57	164.59	0.00	159.02
Volume	1,100	6,300	0	7,400
# Executions	4	27	0	31
Ticket Avg	1.04	32.06	0.00	27.45
# Pos Trades	1	7	0	8
# Neg Trades	0	8	0	8

250

Figure 2.7

I cut the Shark trade review short, as you get the idea. There were 13 more stocks reviewed by him like this.

Other traders have improved on the daily review tablet described here. Things like this happen when you have someone like Shark work so hard on his or her game; others want to as well. For example, Alabama, two seats from Shark, added an important checklist to the SMB daily trade review, which many traders have inserted into their reviews.

Trading Checklist

- Was I in control of my trading?
- Did I manage my risk correctly?
- Did I stay with my winners?
- Did I add to my winning trades when they started to work?
- Did I have enough size in my conviction trades?
- Did I break any of my trading rules and, if so, why?

And they also keep a psychology journal. I share one example here, also developed by Alabama.

Psychology Trading Journal

The Big Money is made in the sitting. Patience = Profits

What I Am Working on This Month and Where My Focus Is

This month is the first month of the trading year and the first month that I take my game to a new level as a trader. I am entering my tenth month and I am ready to start making consistent money. This month I am focusing heavily on deliberate practice in everything that I do, and I am devoting everything that I have to mastering my craft and improving my trading. My mind has never been this right and ready for something. I hear from people that sometimes you just “know” when you are ready, and I have that feeling. I am ready to let myself be successful and become the trader that I know I can be. I am focusing this month heavily on trading psychology and am working on acquiring the ideal trading mindset. This will take time and a lot of hard work and self-observation, but I am ready to look at myself in the mirror and ask myself the hard questions.

This Week's Goals

1. Take every trade that I identify as having an edge in.

2. Add and hold on to my winnings.

3. Work on getting more size on my initial entries within my risk parameters.

4. Improve trading around a core.

Morning Thoughts

I am so unhappy with my performance in holding on to my winning trades that I am just done with that part of my trading for good. The only way that I will get paid is if I hold on to my winning trades to get paid. I am doing so much better with getting size now it's the holding that I will master. Boom Fridays are my best days, and I am looking forward to holding on to my winners.

Trading

Trade	Self-Talk	Consequences	Coaching Talk	Emotions
Traded WFC around the major level of 35.00	I think this is an important price to be involved in, and I was looking to add and get bigger for the trade.	Lost $17 playing it both ways for a potential chop.		
Long small WFC at the same level	Thinking about this trade on a bigger time frame, and it touched the hourly. I think it's going back to 36.00 by the end of the day.	Wrong. Lost $8. Good trade.		
	I am going to make a lot of money this earnings season.			
	I really hate getting shaken out of positions.			
	When I inflate a position before it triggers, it usually results in losses.			
	I need to take a break. I am just not trading well trying to keep my stop too tight when I know my idea is still valid and I do not give things the right stop.			

I have traded next to and taught hundreds of traders. I cannot recall a trader with such an outstanding trader mindset as Shark. If you adopted his trader mindset, your trading would improve dramatically. Let me explain.

The Language of the Successful Trader

Consider Trader A. He has overperformed since his start at SMB relative to his experience and peers. Trader B, by contrast, has underperformed relative to his experience with us. Trader A went to a middle-of-the-road school; Trader B went to school with the sons of senators and CEOs. Both love trading. Both are guys you can build a firm around.

So what separates the two? Their language. And this is found curiously in their daily trading reviews. Here is a daily review sent to me by Trader A. Notice the language emphasis on daily improvement and what he learned from the trading session. Take particular notice of the new play he built that made sense to him.

> I am happy and disappointed at the same time. Here's why:
>
> - I felt like there was so much money out there today. Stocks were
>   moving so significantly, and the worst thing is that I was involved in a bunch of them and didn't truly capitalize on the opportunity.
> - With TSL, SHLD, RCL, and SWN, I hit out a few cents before over 1-point moves. I gotta be a little more lenient. Were my ideas truly busted? That and I have to be able to get back in things.
> - This was a day to make (more) and in the stocks I was in, so I ended the day really disappointed.
>
> With all that said, there were some things I felt good about:
>
> - I did hit many lows and highs and still made respectable money.
> - **I finally put together a positive close, and that was through a strategy I thought of yesterday.** I put together a five-position basket and a one-position kind of worked, while one really worked in which I made $400 in it. So I am going to try to get back to that in the 2–2:30 hour to build my basket.

> I really leave today thinking it was a total missed opportunity but really optimistic about the next few weeks. While the market volatility has decreased, individual stocks are breaking out, and I'm following through on them. Things are cleaner. It just seems like trading is a bit easer the last few days.
>
> I am also trading larger share size, and I am not jumpy. I can hold 1,000 shares for the real move.
>
> I am losing the desire to take 10 cents in every trade because I know I can spread myself out now and only need a few ideas to really work. The goal for me today was to not become overconfident and force anything. I let things come to me, I got into my setups, and I am chasing the easy money lately, whereas I see a lot of people around me trying to stay with things that aren't moving, or trying to buy steep pullbacks. I am sticking to my guns: working with consolidations in stocks that are trending, and I will continue to do as we get into earnings season.

And now let's take a look at the daily review language from Trader B, who was underperforming. Notice how much attention is paid to his lack of P&L. Catch that there is less learning from the day than Trader A learned. Spot the lack of specificity to his reasons for underperformance:

> Bella, I am absolutely disgusted with my executions today. **I barely made any money.** I churned and wrote more tickets than I have ever written, I did not pick my entries well at all, and I didn't lay on the risk at the right times. **I am so upset at myself for not making more money on a day like today;** this was the best day the market has had since Xmas. **I made ($XX) net.** That is absolutely unacceptable. **I can't get over this ($XXX) mark.** In November, I had no problem hitting those kind of numbers on a regular basis, but I have this mental block. **I haven't had my gross P&L over ($XXX) since the first week in December.** That is unacceptable.
>
> Tomorrow I am not trading before 9:50. No excuses for not learning from the past two weeks. I make all my money during the middle of the day and lose money every open. I write in my review about being more thoughtful in my trading, and that is a huge part of improving my results that I need to correct. I am very excited

> for tomorrow, but I really need to focus on not making the same mistakes that I made today. Let me know if you have any thoughts on my review. Thanks.

Trader B can go on to become a successful trader, but he won't if he continues to use the language in this example. We pointed out his language to him with suggestions and penalty threats unless there were more constructive future trader reviews. Since then, he has made progress. Providing guidance to traders, with repercussions if they do not correct their behavior, can improve their underperformance. Underperformance is a data point that can be reversed.

As expected, Trader A continues to outperform his peers. So, guess who Trader A is? Trader A is Shark!

At SMB, we preach the importance of developing the proper mindset: improve every day. Our influence is Carol Dweck, author of the game-changing book *Mindset*. It is easy for me, or a fellow trading coach, to throw on some slacks and a dress shirt and talk at traders daily about improving their performance. But only the special trader can live their trading life perpetually focused on getting better every day when it is so easy to be distracted by a scoreboard of money. Shark does!

Some are attracted to trading for the unlimited upside and freedom. "I can come and go whenever I want," think most people. "Shorts, flip-flops, t-shirts, right?" Oh boy! Not if you want to be the best trader, and not if you want to trade on a professional prop desk.

What also gets left out from this poppycock is the real-time relentlessness of the outstanding pro trader. Some traders can make a consistent P&L, but only a much smaller few can generate serious P&L. One undervalued skill necessary to achieve this P&L height has everything to do with relentlessness. You cannot enroll for this class at Wharton. (I had Spencer and Freudberg both check.) This escapes the financial media's attention. It is a skill of the elite and soon-to-be elite traders.

Good Traders Are Real-Time Relentless

Spencer entered my section of our trading desk and chirped, "Bella." That's code for "Meet me in your office." My office because it sits right outside the trading floor and is nearest to the traders, the cash engine of SMB Capital. Spencer sports a palatial office that I quip is closer to New

Jersey than our trading floor. Even worse, his previous office, before it was put to more efficient use, was 18 feet across of almost floor-to-ceiling glass, with a lounging couch for interviews and talk of an 80-inch plasma. There are smaller apartments in NYC compared to that former office. But I guess when you are a pretty boy, media star like Spencer—Fox Business, Bloomberg, the *Financial Times,* the *Wall Street Journal,* CNN Money, the BBC—you get digs like that. Diva.

Spencer started, “Do you see what Shark is doing today?”

What, did he think I was playing Words with Friends all day?

“He is relentless. He keeps making more. Every hour he is up more money. His P&L is a steady climb.” And then he said that something I could never forget: “If GMan doesn’t step it up, Shark is going to pass him as the best trader on the desk.” (Insert dramatic *CSI* music for added effect?)

“Is that it?” I asked.

“Yep,” finished Spencer, with a look conveying I was dense for not understanding the importance of Shark’s progress.

Ignoring the look, I went back to trading. I didn’t need results to confirm what was ahead for Shark. Work begets results. “The only place success comes before work is in the dictionary,” said Vince Lombardi, legendary football coach of the champion Green Bay Packers. No one works like Shark; therefore, no one is going to be better than him until they work like him.

Shark’s Best Trade Ever (NKE)

Before this conversation with Spencer, Shark had just made his “best trade ever,” in his words, thank you NKE. (This was about 18 months into his trading career, when he was exclusively trading short-term intraday setups, and perhaps 20 names everyday.) Soon after, a gaggle of other traders were celebrating similar chops in NKE. As others on the desk soaked in their moment of market domination and relaxed, Shark then found a new chop, a short for a point in NKE. Riding the long for over 2 points was not enough for Shark. SMB trader Jersey Shore, who called out the NKE setup to Shark, had his best day going but was gone from the floor by 3 p.m. Perhaps Jersey Shore in fact went out to the Jersey Shore for some GTL (gym, tanning, and laundry à la MTV’s *The Jersey Shore*), but Shark was seated, primed, and making more.

In a recent interview with the *New York Times*, Jeff Weiner, CEO of LinkedIn, points to several attributes that are effective for asserting strong leadership. One is to be more loving than right; another is the need to inspire people rather than manage them. But perhaps the biggest takeaway for traders are his remarks on two words that he learned from Coach Mike Krzyzewski of the Duke Blue Devils. As Weiner describes it,

> [Krzyzewski] doesn't want them celebrating that incredible alley-oop dunk, and he doesn't want them lamenting the fact that the opposing team just stole the ball and had a fast break that led to an easy layup. You can take a moment to reflect on what just happened, and you probably should, but you shouldn't linger too long on it, and then move on to the next play.

Have you read a more perfect summary of the proper disposition that every trader should have? *Next play!* Krzyzewski's two words are simple, obvious, and stunningly perfect because they beautifully sum up the proper frame of mind that every trader needs to have. It's all too easy to sour on the market or to scream at the computer or to descend into a quiet funk over a trade that didn't work. This is bad, this is wrong, it's counterproductive, and, worst of all, it's poisonous to the mind. The lesson here is important, not just for playing basketball but for trading as well: Don't wallow in self-pity *or* jubilation. Have your moment of frustration or celebration (go ahead, you're human) and then sit up and say to yourself, "Next play." Don't live in the past (which is different from recognizing and learning from an error you made). Always be looking for opportunities. Next play. Always be fluid in your mind, where a natural state of interest and enthusiasm keeps you open, not closed off, to the next opportunity. Next play. Make this your default mantra to every trade and you'll always stay in the game.

The day doesn't end until 4 p.m. When you are trading well, you keep trading. You may reach a new level in your trading that you never imagined possible. When you work hard at something, experience the power of your skill compounding, then you just might become better than you ever imagined. But you will never discover how good you can be unless you sit in your seat, stay, and trade. The difference between Jersey Shore and Shark may not be skill but relentlessness. Spencer tagged Jersey Shore early as the trader to be more profitable than Shark. And that has just not been the case, even though Jersey Shore is a pretty solid trader.

The weekend after this NKE trade, Shark, some traders, @speerothekid, @zmoose12, and I sat in PJ Clarke's on the Upper West Side of Manhattan via my invitation for brunch. I went with the no-carb steak and eggs, and the rest had PJ Clarke's signature burger, famously enjoyed at a moment in time by luminaries such as Frank Sinatra, Nat King Cole, and Jacqueline Kennedy Onassis. Shark, positioned to my left, walked me through his thinking about how he could have been 60 percent bigger in this NKE trade. He outlined in detail his entries, adds, and stops. He not only stayed and made more, but he did so on one of those summer Fridays on which too many are tempted to go to the Hamptons or Jersey Shore or play golf or hang with that pretty party girl. Now he sat there hours removed from the trade, over burgers, getting better with trading thought.

Now Shark and I work on his specially designed "Shark PlayBook." He has outgrown the standard SMB PlayBook. Each day we focus on the same: How could he have been really big, with 5K shares or more in his best setups? Highlight this next trading tip: When you make a great trade, you must go back and review it, focusing on how you could have been bigger responsibly. Here is a quick Shark's review of that NKE trade, his best single trade ever up to that point (since surpassed) and his work to find a way that made sense to him to trade this setup bigger.

Reversal Long After Exhaustion Gap Selling: NKE

June 29, 2012

Play Fundamentals

• Bigger-picture psychology drives a lot of the logic of this play. It is relevant that NKE is an institutional name, a "real stock," and therefore has more bounce capacity than a stock that institutions don't own.

• The first half of 2012, NKE spent trending up and then forming a top, failing to break out, and starting to roll over. The selling that precedes the exhaustion gap indicates that most of the longs have already gotten out of positions and the shorts are less likely to pile in right after such a large decline.

• In these situations, panic selling after the gap is a possible scenario, particularly in this case as NKE gets below longer-term support, but then if a buyer can be identified, good opportunities for countertrend longs can develop.

SPY: Big Picture

SPY 1days: 151.41
143.41
142.00
141.00
140.00
139.00
138.00
137.00
136.00
135.00
134.00
133.00
132.00
131.00
139.00
129.00
128.00
126.82
Volume: 38,695,497,728
200M
100M
0
2011
Apr
May
Jun

• SPY was in a bigger picture downtrend but had formed a bottom after a steep selloff in May and was turning up from there.

• On the day NKE made its move, the market was gapping up and strong, another check in the favor of the reversal long in this case.

• Institutions could view the steep dropout in NKE as a buying opportunity in a market that was showing some signs of turning the downtrend around.

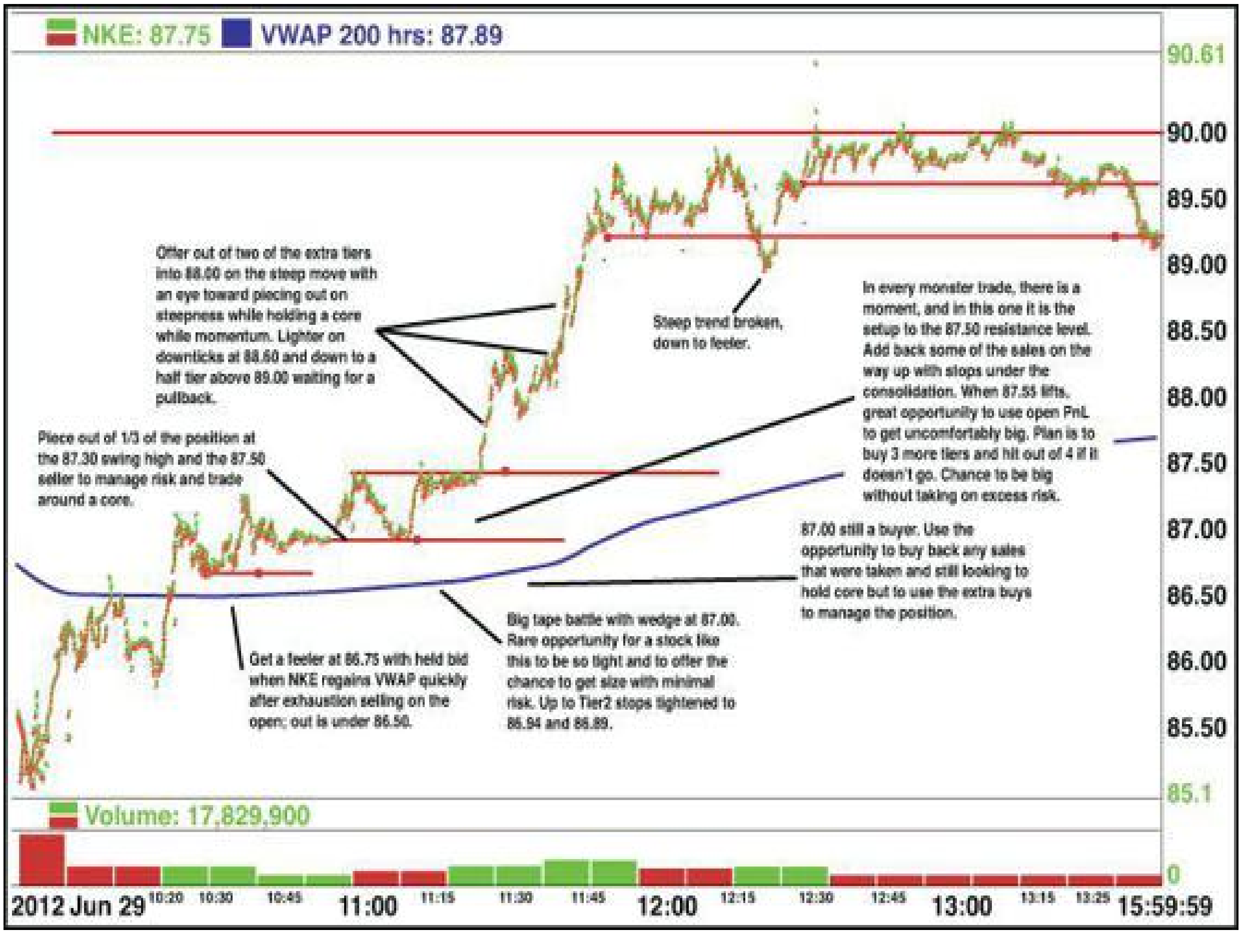
Intraday Fundamentals

• Earnings play, guided down EPS growth rate:

• **Thursday, 28 Jun 2012 05:00 a.m. EDT:** Nike, Inc. announced that for fiscal 2013, on ongoing basis it expects revenue growth at or slightly above the company’s high single-digit target range. on a reported basis, it expects mid to high single-digit revenue growth and expects to deliver high single-digit EPS growth in fiscal 2013. This is below the company’s long-term goal of mid-teens EPS growth as a result of the negative impact of weaker international currencies on both gross margin and translated foreign earnings as well as a higher effective tax rate.

Technical Analysis

Trade Management



Some are reticent to follow their dream of trading pro because they fear it is a playground of insiders or the genetically elite. This is nonsense. In the late 1990s, advances in technology created access and opportunities for all with trading skills. Translation: Almost all with the time and willingness to build skill can compete in the market. While Shark had many attractive personal attributes in his background, it was not obvious to HR, other firms, the partners, our traders, or me that he would become this good. He worked hard to get where he is today, and if he can do it, why can't you?

If Shark Can Do It, Why Can't You?

For those who have never traded, have a passion to trade pro, and do not possess a stereotypical Wall Street pedigree, let Shark be your inspiration. In Chapter 6, "Special Projects: Get Ready to Trade Pro," I implore you to gain trading experience before starting as a pro trader. I suggest your odds of success diminish substantially without building trading skill and acquiring trading experience before declaring pro. Shark defies this advice. One day in September, he just showed up and started. I ought to amend that to say that he showed up and started and started working.

Shark is from one of those small upstate New York towns where most people don't grow up thinking they will land in NYC. Let's be fair; most people from those towns find a day visiting Broadway and Carmine's to be a trip of wonderment. My wife is from one of those towns. Spencer and I are from one of those towns (though not the upstate part). A childhood in distant suburbia makes you appreciate everything that you experience in NYC that much more. "We can only be said to be alive in those moments when our hearts are conscious of our treasures," wrote Thornton Wilder, author of the classic *Our Town.*

Babbo replaces the Macaroni Grill, Paul Stuart replaces Banana Republic, the Sony Theater IMAX replaces the village multiplex. You learn that Times Square is a place no real New Yorker ever visits and that only tourists hold a fear of city crime. Great bands play in 300-person venues such that you can almost touch your new favorite musicians for a $20 cover. NYC isn't the Statue of Liberty, street vendor hot dogs, the Empire State Building, Joe's Original Pizza, and gridlock traffic. It's the coming together of so many ambitious people from all over the globe, in all types of industries, with diverse neighborhoods, 30 minutes to Yankee Stadium or a similar event, and Grimaldi's. Learning all this is a thrill. NYC surges a mutant strain of oxygen into your blood that never leaves. And Shark, that upstate boy? He lives here now and as a professional trader.

Shark is the example of how you can sit down without experience, work your tail off, get better every day, and become a successful intraday trader without previous screen time. Yes, we argue in other chapters this way is harder. But for those of you sitting in one of those pushing-around-paper jobs wondering whether a trading life is possible, well, Shark is your alpha dog.

The market is open to those with skill. Good training, hard work, screen time, and a passion for trading are your barriers to entry. If that nontraditional for Wall Street standards, upstate boy can do it, can't you?

Trading Calm

The day of the Supreme Court's huge healthcare decision (*National Federation of Independent Business v. Sebelius*), we were all trading the healthcare names. There was market-participant confusion on where healthcare stocks should be priced, so stocks in the sector shot up and down intraday like kids on a trampoline. Many of us were short WLP, a healthcare stock, after a 1-point down move, and we all had a sense that it might trend lower. Some on the desk found a seller at 66 and an identifiable exit above 66.15. Short and confident in our position, we waited. The result? We all got stopped out above 66.15.

"D*** it!"

"What a rip!"

"Mother ******!"

All these comments could be heard on the desk. And then from Shark to a mentee calmly after also being stopped out, "If you see a good trade, just make it. Keep trading. Your P&L will swing on a day like today. Just keep looking for good trades."

Shark took that rip in WLP. He took another with our trading area in VRTX. Open P&L in UNH was given back. But he also caught a huge chop in VRTX. He caught a nice move in HCA. Then he caught another one in AET. His P&L went up and down, but he kept his cool and had a very profitable day.

Disappointment is a certainty for the intraday trader, like ECN fees and commissions that you always feel can be lower. After disappointment, opportunity is present. The calm trader exploits that next opportunity. Opportunity that is sometimes greater than that first disappointing rip. It's the calm trader who can go from positive to negative to significantly positive in a matter of minutes.

We all come with psychological baggage to overcome, even Shark. While mostly calm now in real-time, the following blog post shows even the dream trainee Shark had to work on his emotions.

The Overanxious Trader

> As I was reviewing a monthly review from a mentee, Shark, I thought that I could use the thoughts of Dr. Menaker, a trading psychologist. Shark wrote:

Too excited on days I want to do well. I force too much. I had such high expectations for myself coming into earnings season that I started to force things. I didn't let trades come to me. I was too jumpy. I was too eager. I wasn't selective enough. Often I write too many tickets and don't select bigger picture plays that will actually pay me. I think this happened a lot where I would write a bunch of tickets and end up breaking even on a lot of days after fees.

Dr. Menaker wrote:

Whenever a trader mentions performance expectations, I take notice. Of course, we all want to do our best, and some of us perform best when facing a challenge, like a clutch-performing athlete in a way. But trading is a bit different. Having expectations is not a problem per se. It's what we do with the expectations and how we respond to the expectation that is critical. The issue here for some people is that expectations can become "demands." For such people, these demands become internal demands, narrowing one's field of awareness and easily translating into a rigid mindset. A rigid mindset is a dangerous mindset for a trader. We need flexibility and patience, not rigidity.

Another possibility for this trader is that writing too many tickets, or overtrading, is simply a way to justify oneself and deal with performance pressure from high expectations or internal demands to perform. In such a case, one needs to learn to tolerate the discomfort that comes with performance pressure. Many people will try to escape the discomfort by "doing something," like getting into a marginal trade. But that rarely does the trick and often leaves you more frustrated in the end. Learning to be patient, to wait for the fat pitch, is one of the most important skills a trader can have. Patience is not simply the ability to wait, it's the ability to have the right attitude while waiting.

One trading technique that Shark is able to execute proficiently because of his calm emotions is a Flip Trade. To flip a position means to go from short to flat to long or long to flat to short in a nanosecond. While too many on the desk waste energy with “oh, damn it! Stopped out of xyz,” Shark can withstand that stop out and quickly take the other side of the trade. I have noticed him catching a quick spike in the opposite direction than his original bias, while others are moaning about the stop out and missing the better next trading opportunity.

Shark has gone from no experience to positive to more. That more is a trader who makes others on the desk better. If the Street voted for Most Valuable Trader, I would submit his name.

Most Valuable Trader

It is rare to find a member of an organization, company, group, or team who adds value to all others. Their presence and work makes everyone better. Shark does! Here is an example that started with an e-mail from Shark to me after one close:

> The thing that kind of got me on tilt a bit is that I wasn’t in LNCR, and apparently I must have tunnel vision because people did mention it, but it was more like that they weren’t really calling it out and meanwhile I’m walking people through the trade I like, ORLY, mentioning it out loud and on the chat (SMB Real-Time) and letting people know I’m holding 30.
>
> With LNCR, I don’t hear people yelling. You have to be in this when it’s clearly an unusual opportunity. So that got to me a little bit. and it kind of made me force some stuff in the close and do a little too much.

Shark was p***** that others were not calling out trading opportunities like he was. Through back channels, it was made known that Shark was not happy with the lack of callouts in LNCR. Not an hour later this e-mail from TO was sent to the SMB master trader e-mail list:

> I’d like to personally apologize to the entire desk about LNCR today. I’ll confess: I absolutely dropped the ball on that one, both in managing my own trade and communicating the 29 level to the desk. I cost everyone a lot of money that they should have made. I thought I’d get stopped out, and I tend to clam up when my confidence wanes in a trade, and that’s wrong on both counts. I also should have called out that COG louder. I feel bad about this.

> Drinks are on me tomorrow if I don't get you guys into a good trade.

TO apologized because he did not want to disappoint Shark. He knew Shark had made his trading better with callouts in the past, and he felt terrible that he did not help Shark with this trade. That is earning respect from your fellow traders. That is one trader setting standards for the entire team.

Seth Freudberg, who runs our options trading desk and education department, is fascinated with how SMB consistently values its unique culture. I pinged him with an anecdote I knew he would most appreciate:

> I cannot say enough about Shark. It is one thing to surpass GMan on the desk and have the best results of the month. But he has also now helped a young trader, Chris, become a pretty good young trader. Chris is now entering Pippen and TO early stages of superior development. But he has a little more guts. This new nucleus of young traders may be the best we have ever developed.
>
> Seth responded:
>
> It is truly something to be proud of. I have great respect for the fact that it is not just about money for you. You really care about these guys and their success is fulfilling to you. You take sincere joy in seeing other people grow. That is a rare and wonderful quality. I am proud to be a part of what you and Steve are building.

So now Shark not only makes others around him better, but he also helps me inspire Seth. Seth now feels more pride working with SMB. Seth will tell this story to anyone he talks with who might partner with our options side. Shark's influence reaches further than just the traders around him.

Shark's reach extends to his work as a mentor to our most promising trainees.

Shark, The Mentor

Let's look at a snapshot of Shark on the desk. MQP, a former airline pilot, prepared to start her first trading day live. Spencer labeled her the most qualified person (hence MQP) we had ever trained because of her impressive background. Keep in mind that I sometimes refer to Spencer as Spencermistic, in that he can be overly optimistic. We placed her next to

Shark. For 15 minutes before the open, she got the manual for how to hit a run rate of 250K in gross revenue by the end of Year 2.

Shark sent her his template for his daily review. He suggested she do a PlayBook trade every day. He discussed how he rips through charts and makes notes on promising technical setups. He outlined all the helpful books he has read. They were mostly psychology books. Shark noted that trading is a performance game and counseled that these books were very helpful to him. He encouraged her to read *The Daily Trading Coach, Enhancing Trader Performance, Trading in the Zone,* and, "Oh yeah, there's this new one, *Market Mind Games,* by one of Bella's friends." This being a prop desk. you know what is coming next from the overhearers. "I heard *One Good Trade* is pretty good, as well, Shark." Two rows of traders cracked themselves up.

Shark continued, "At the beginning, you should watch your tape so that you get better trading the open."

"Yeah, I will do that," replied MQP.

"These are the things that I do. If they work for you, you can use them. But if you want to change them to better work for you, that is fine."

"No, I like these ideas."

This trader was juiced with motivation sitting next to a high performer. Now she will listen to whatever Shark says because she can see his P&L tick by tick. Now it is up to her to do the work. But she knows exactly how to become great, and all her motivation needed is sitting a couple of feet to her right.

A quick note here. Teaching other traders as Shark did here makes Shark a better trader. Teaching forces you to better understand your game as you must explain it. It also forces you to scrub your trading, as your thoughts may be challenged by another. Teaching improves your trading.

Not only does Shark make young traders better, but his reach extends even further. Think all the way up to the partner level.

Making GMan a Better Trader

GMan taught Shark how to trade. He sits right next to GMan and has luxury box seats to one of the most skilled intraday traders on the Street. In case you do not know, GMan was named one of the Top Three Traders Under Thirty, covered by Yahoo! Finance. Tick for tick for about a year, Shark has had the opportunity to listen to GMan in real-time and learn how he thinks through a trade. For soccer enthusiasts, this would be like having Cristiano Ronaldo, one the world's greatest players, right next to you on the soccer field as you grow up playing the game.

Shark's data as an intraday trader reflects the likelihood that he will become the best intraday trader on our desk. Traders make the most progress from Year 2 to Year 3 in our sport. He is still at the end of Year 2. He has become so good that he has forced GMan to become a better trader. How? GMan cannot fade trades the way he stubbornly used to and that harmed his P&L. If he does, Shark is gonna crush his trading results.

Also, Shark is wildly profitable playing the trend in the very stocks that GMan sometimes tries to fade. GMan cannot ignore the results of a lesser-skilled trader following the trend and making more than he does. GMan's inner drive will not allow him to continue to make these mistakes and be the second-best trader on the desk. GMan and his South American internal fire would quit trading before he allowed that to happen. His analytical skills will kick into overdrive, and he will acknowledge how badly his fading is costing his P&L.

It is one thing to hear criticism about fading from me and his personal trading coach. It is another to watch someone with less skill, like Shark, make more than him because the person is doing the complete opposite of him. The data doesn't lie.

The other day Shark announced he was taking a three-day weekend to see his family right before the start of earnings season. Guess who took off that day as well? Yes, GMan. We actually had a good trading day as a firm, even though the heavy hitters were absent. You know there were a few kids left offering guidance in the names of Spencer and Bella. But overall, the desk feels a huge gaping hole, like an offensive line without its center, if Shark is not on the desk.

One of the harder traits to amass as an "eat what you kill" intraday trader is self-actualization. Shark has that one covered as well.

Shark Is Self-Actualized

One of the most difficult aspects of intraday trading is being wrong so often. As an aside, and dispelling the myths propagated by the Financial Media Entertainment Complex, even world-class traders have a win rate barely above 50 percent. Most civilians do not spend their days being wrong 40 percent to 60 percent of the time. If they were, they would be fired. Psychologically, it is difficult to fail so much and move forward undeterred. Recently, I sent Shark a critique of a decision he had made. His response was striking. He quickly understood his error and admitted it. He is self-actualized.

Here's the e-mail Shark sent me on a beautiful spring Friday morning:

> I feel a bit checked out today. Going to take off early for the weekend and enjoy the weather. But overall, I just wanted to lock in the day but really should have done much better with that NAV again today. I'm gonna spend a good amount of time reviewing that one over the weekend.
>
> Also, I have my monthly review pretty much done. Going to work on reviewing some final things over the weekend and will send that over.
>
> The big lesson of today is that when I have so much info in NAV or any stock from the final day I have to be in it earlier. I really missed a layup just because it was a little thin, but with so much play money from the prior day I should be comfortable taking on a bit more risk there.

And then Shark left for the day. I think GMan talked him into heading out early. GMan misses no opportunity for potential fun. Las Vegas marketing very well could revolve around the potential hankerings of a GMan. When there's good weather, it's like the earth's core is pulling GMan to come out and play. Or like God himself paid GMan a visit warning a day of good weather squandered will be discussed on Judgment Day.

That NAV Shark was trading continued to follow through, drive higher and cleanly. Shark had walked away from a huge trading opportunity. I thought Spencer was going to lose it talking about this missed opportunity in my office. "I don't understand where these guys are going. How hard is it to sit in your f****** seat and trade?" he ranted.

I sent a brief e-mail to Shark and the other cutters:

> NAV layup?
>
> Some traders didn't respond. Two responded defensively. And then there was Shark:

> To be honest, I shouldn't have left. Maybe I let yesterday get to my head or something, and I thought it was okay, but I haven't had any sort of success to be able to do that. You have the right to be p*****, and I couldn't actually enjoy the weather looking at that stock go to 29. For me, I was so mad about not being in from 24, it was hard for me to stay in it that much of the bottom. And that far away from 24. But there was no reason to get out, and I'll imprint this stock in my brain.

What is so remarkable about Shark's e-mail is how quickly he admitted he was wrong. If you do not think this has a lot to do with why he is a successful trader, think again. Good traders admit their mistakes, learn from them, and get better. Many other traders, I hate to say, attempt to defend the indefensible as a way to maintain a level of personal delusional awesomeness, masking the reality of a trading account buried in red.

Let me offer you a trading tip: Save the defense for your driving; a good trader is self-actualized.

Another example of Shark's self-actualization was his approach to trading after returning from vacation.

Shark's Smart Trading after Vacation

Shark understood that a few days off would leave him a bit rusty and not as connected with the flow of the market. So the first day back, he took it easy. You can see that here:

> You know I think I did some good things and some bad. The damage could have been worse. I came in after vacation and made the conscious effort of taking things slow on the open, and as it turned out, all the opportunity was really on the open, so that backfired.
>
> Being a little slow, I missed a trade with JCP and WAG opening drive off 85 cents were really the two best trades, and me taking things slow kind of made me not capitalize like I should have. After that, I wanted to start ramping it up, and I think I got in some things that could have really paid: ORCL, JCP, WAG were all good opportunities. But I also took some iffy plays and botched some executions. And also didn't really truly capitalize on the one

> play that worked well for me. Those are the things that really stand out to me today.

Good traders are in tune with their ability, which can shift based on the markets and time in front of your screens. They catch the big rips before the big rips. So this is a healthy review of limited damage instead of the underperforming trader with regret and blood across his trading review. This reminds me of the applicable quote from Socrates, “First know thyself.” Sharks knows his limitations, which improves his P&L.

Sustaining traders focus on the process over their P&L. I offer Exhibit Shark as evidence.

Shark’s Focus on the Process

I noticed Shark starting to make money at the end of his Year 1. I talked with Steve about bumping his percentage payout. Let me be clear; we were under no legal obligation to pay him a higher percentage of his profits. In fact, he had a signed contract that stipulated his percentage split for the first two years of trading. But he had led the desk in work output, the firm’s risk was now considerably lower, and we reward those who improve our culture.

Generally, in the past when I have bumped the pay of a trader, they are noticeably pumped. Think of your favorite NFL team scoring a touchdown in the playoffs. This firm act improves morale. The best traders are happy, and this news leaks to the other traders.

I buzzed Carlton on our phone intercom to ask Shark to come see me in my office at his convenience. Just before lunch Shark knocked on my door.

“Bella, Carlton said you wanted to see me.”

“Yes, sit down. I have some good news for you. We are bumping your payout (it was a 20 percent bump to him). You have worked very hard. You have done everything we have asked and more. You have added value to the desk. You are active during our tradecasts. You offer great callouts to the desk. You deserve it!”

Shark’s reaction? “Oh.” He sat without expression, listening to what I was saying. Then he said, “Thank you,” without a smile or hint of excitement.

He then asked if there was anything else.

“No.”

Shark got up, closed the door, and joined his trading buddies standing outside my office waiting for him to head out for lunch.

I sat confused. What was that nonreaction all about? In baseball, they say you see something new every game. I was having one of those moments as a trading partner. How could he not be ecstatic? I couldn't stop thinking about his indifference. Was there some $5 Subway foot-long special that he was about to miss?

But then I got it!

That is exactly how he should have reacted. We teach for traders to first improve every day. Shark is to daily improvement as Beyonce is to hit records. Getting a bump in pay has nothing to do with his improving as a trader. It's just the money that we will wire to his bank. Completely immersed in our culture, he did what we taught: Go back to work and figure out how to get better. That is the true reward of trading. He reminded me what I was teaching him. Now having said that, just between us, I have to chuckle. Man, that was one powerful response, that nonresponse, from the ultimate elite performer.

In other words, this was just another example of Shark's focus on the process. It's a model for others in the trading community to emulate.

To Improve Your Trading Results, First Do This

Following is a conversation I had with an SMB trader who I thought should have been making more. I used Shark's emphasis on process as a guide for this rising trader.

Bella: Put up 15K in January and there will be a special surprise for you.

Trainee: I am trying to do that halfway through the month. I've hit that before in six days, but that was months ago.

I didn't get a chance to do the review today. Will get to it tomorrow. Have a doctor's appointment and got caught up trading RIMM and talking to my mentees.

Overall today was solid. I fought stocks and had a few P&L swings, which only gave me confidence. To fix my issue of having those holds with size, what I did over the last two days was treat 500 shares like it was 2,000. And today I caught more half-point moves than I usually do. So, I now know I am ready to make that big step that I have been so wanting to finally do.

Bella: In my opinion, you will more easily make that next step if you review your work like a TO and Shark. Adding some structure to your review and preparation is all you really need. This will brand the best plays for you in your trading head. Ensure you are best prepared for your best trades. Prepare your brain to be ready for your best setups. I see the first step being to add some structure, and then those better results you want will follow.

A few months later, that trader came back into my office with some details about his new review process. Writing down things was not for him. He had started doing a Skype call about all his trades with his mentees. "Bella, doing this review every day has been helping me a lot. It is why I have been doing better lately." I listened without the least bit of surprise.

You do not have to do exactly as Shark does. Even Shark says this to his mentees. We are all different with unique personalities and variant personalized reviews. But you do have to find a way to review your work that makes sense to you. It's this review process that helps you internalize your trading, which will get you to perform better. Without it, there is no increased P&L.

Shark has developed an affinity for picking the best stocks to trade intraday. You are only as good as the stocks you trade, but finding them is not luck. It is stock selection intuition accumulated through superior preparation over an extended period, after excellent training.

Shark Hunts the Best Stocks

Sharks can track large prey by following their low-pitch sounds. They can smell blood in the water from miles away. A great white shark could detect a single drop of blood in an Olympic-size swimming pool. Well, maybe our Shark cannot detect a good stock as well as a shark does blood, but he is adept at finding the best stocks to trade intraday. This is not some innate gift. He works every day to put himself in the position to trade the best stocks through thorough preparation. I asked him to send me an outline of his daily routine for this book and as an aide for you. Here is his response:

Daily Routine

Morning:

• Wake up and check quotes of indices.

• Come in and check news via seeking alpha/smbscanner.

• Look at volume advancers from day before.

• Look at chart for every stock that trades 1 million average volume and above 50c average true range.

• Journal: Write down my goal for the day; freewrite about how I'm feeling. Anything else that might affect my trading and ask myself the best strategy to do well for the day.

After close:

• Chop tracker routine I send you while looking at execution bubbles on my chart.

• Journal: How I did on my goal/what I did well/poor/different/my game plan for tomorrow, and a few annotated charts of things I messed up on.

• Separate journal about my general thoughts or how I felt about the day or anything else really I feel like writing.

• PlayBook: Usually about a trade that I should have done better.

• Sometimes I watch tape (used to do it more when I first started).

• Watch Brian Shannon's video/daily recap when I'm at the gym or at home.

So there you have it: an inside guide to finding the best stocks intraday from a great intraday trader.

Supplementing Shark's routine, I wrote a blog post on how to find the best stocks to trade throughout the trading day.

How Do You Find The Best Stocks to Trade?

Jan 9, 2013 | By Bella | Category: General Comments | Edit

Hi Mike,

Quick question... while you're probably constantly reevaluating throughout the day, would you say it's common for SMB to come up with another set of "in play stocks" for afternoon trading, or do you tend to stick with the original ideas from the morning?

thanks for all your advice and thoughts.

@mikebellafiore

> **1.** We are experts in choosing the best stocks to trade intraday. We are only as good as the stocks we trade. There is almost never a trading day without trading opportunity for our desk because we are expert at finding the stocks in play. Steve does an amazing job preparing our desk with the best stocks to trade with our SMB a.m. meeting. In fact, today he prepared the desk so well before the open that I got an e-mail from him explaining his awesomeness.
>
> **2.** We supplement our a.m. meeting with trading tools. Tools such as the SMB Scanner and the SMB Radar. We built the SMB Radar with Trade-ideas. These are professional proprietary tools that we have built to find the Stocks In Play.
>
> **3.** We supplement our a.m. meeting with our SMB Real-Time. Traders chat to each other about the most opportunistic stocks.
>
> **4.** Guys on our desk are taught to call out stocks that are moving best intraday. Sixty pairs of eyes are better than one.
>
> **5.** Some guys on our desk scan tools such as Finviz to find sectors that are hottest and start to consider trades in these sectors.
>
> **6.** A news feed is piped into most proprietary trading desks so that traders do not miss breaking news. One shop has this news feed built into its proprietary trading platform. With the click of a key, ours, you can see the breaking news on that stock from your trading platform.

So we are very good about picking the best stocks to trade. Often you do not need to trade more than what is shared during our SMB a.m. meeting. But we do supplement all of that with the above.

I hope that helps. Thxs for the question. Trade well.

Shark is the best of the best nucleus of young traders SMB has ever developed. After my dad's stroke, my mom's passing, and the exodus of some of our more experienced traders, it wasn't fun to go to the office. Like a Duke team without good players, SMB wasn't very good. I wasn't there mentally. I have to admit at my lowest points my mind sometimes wandered to perhaps doing something else. Seeing Shark succeed in an SMB environment that was after our past best days (or so I thought) helped bring the spark back into my coaching game. And he inspired others around him to follow his lead.

With The PlayBook, we made some educational changes to better train traders for a market that was harder to trade. Longer time-frame intraday trades were identified and highlighted. We added better trading tools to help our guys. We managed out of the firm anyone who did not fit our culture, without them even realizing this, getting even smaller. SMB had to and we did get a lot better. Shark was the fastest to take our new and improved training and infrastructure and prosper. His contribution to our firm cannot be understated. We made a comeback worthy of everything that SMB is all about, ignited by him.

For the reader at home, perhaps Shark's biggest inspiration is his lack of obvious trading talent. His blue-collar work ethic is why he is a good trader. For those without a world-class IQ and who dream to be a world-class trader, he is your model. For those without insider Wall Street connections, remember Shark. For those without a history of trading success, be mindful of Shark. For those who did not graduate from an Ivy League school, neither did Shark. For those who didn't star as a DI athlete, I offer Shark. Just understand this: To *be* like Shark, you must be ready to *work* like Shark.

Now let's take a look at a PlayBook trade Shark made in KCG (Knight Capital Group), right after their much publicized and notorious trading error that jeopardized their entire firm.

3. The Day Knight Capital Almost Fell (A Support Play)

This chapter reviews Shark's Support Trade in Knight Capital, right after their infamous monster trading loss. But first we need to do one more thing. We must explain a Reason2Sell, an exit strategy for winning trades. This concept is discussed in this setup and prominently throughout the book. It will help you write personal trading rules to best exit your profitable positions.

Have you ever cut your winners too early only to see the position trade much higher? Of course you have. How about hang on to winners too long only to see your unrealized gains evaporate as the position reverses? You are not alone. British economist Sir Alec Cairncross lyricized our dilemma best:

> *A trend is a trend is a trend*
>
> *But the question is, will it bend?*
>
> *Will it alter its course*
>
> *Through some unforeseen force*
>
> *And come to a premature end?*

Reasons2Sell will help you develop an exit system so that this occurs less often and only when your predetermined rules for selling manifest. Let's check out a recent blog post I wrote offering guidance on when to sell your winning positions utilizing Reasons2Sell. To all those who sell too early, take comfort; you will see you are not alone. And by the end of this chapter, we will offer a fix to all of this for your trading.

How Do You Know When to Sell a Winning Position?

> Jan 23, 2013 | By Bella |
>
> Dear Mike,
>
> I recently read *One Good Trade* and found it a quality read relative to all other books I've read. It has been immensely helpful as I am currently full-time employed and am at a point where I am thinking that that trading full time could be an option, provided I

can become consistently profitable and have the confidence of putting “bread on the table” from trading.

As a result of reading the book, I have adopted a methodical and disciplined approach and my results have improved as a result of this. What I’m finding however is I become indecisive when I’ve had some reasonable gains on a trade and now adopt a “bird in the hand” approach and take the money off the table once I am up a few percent in a trade and before there is a pullback. I understand this is the wrong approach as I am supposed to let profitable trades run; however, I have seen many decent gains evaporate or, worse, turn into a loss because I decided to hold. I’m not sure there is a question there, but in any case would be grateful for your views.

@mikebellafiore

I love how you are approaching trading pro. You are working on your game while you are employed and being very patient and gaining valuable screen time before deciding whether to trade pro. Too many just start, without any past trading experience, and expect to make bank immediately. As is true of any professional discipline, you do not reach the stage of competence until after training, concerted practice, experience, and review.

When do I know when to sell? How do I know when to cut my winners? I will give you some highlights. Also check out The PlayBook webinar series (www.smbtraining.com/blog/the-playbook-webinar-series-opening-drive-play-in-lnkd), where we discuss the trading concept that helps you answer these questions. That concept is Reasons2Sell.

When you are developing your PlayBook, an archive of trades that make the most sense to you, distinguish between Move2Move trades and Trades2Hold. An example of a Move2Move trade is a scalp, trading for the next move in a stock. Trades2Hold are our intraday swing trades, where we are trying to capture multiple points. With our Trades2Hold, we do not sell until there is a Reason2Sell.

Each trader must develop his own list of Reasons2Sell. If you spot a reason, then consider selling. If you do not, the position is not a sale. This is true even if the position trades against you and you give back significant open profit. Your job as a trader is to do the right thing. Judge your trading not by your P&L but whether you traded a setup well.

Reasons2Sell examples include the following:

- The stock breaks its uptrend.
- Breaking news.
- Overall market resistance.
- Technical resistance in the stock.
- The selling pattern dissipated.
- Breaking news in the market.

This is not our proprietary exhaustive list of Reasons2Sell inside the SMB Foundation, our training program, but it gives you a feel of the right thing to do with your positions. Develop your list of Reasons2Sell and start applying them to your Trades2Hold.

I hope that helps.

MHB

You cannot carp about an exit too early if you have not taken the time to write rules to exit a winning trade. All traders on our desk draft these rules, again we say Reasons2Sell. The idea is not to sell our position until one of these Reasons2Sell becomes present in the trade. If we do sell before one of these reasons materializes, we have made a trading error. If a Reason2Sell develops in a Trade2Hold, we sell, and then if the stock continues higher, well, that is no matter. We have done our job: trade the setup well. Our job is not: to obsess about every penny we could have taken out of the trade.

Let me give you a real-life example on a pro trading desk of how having developed your Reasons2Sell will positively impact your trading. KMay, a developing trader who sits diagonally behind me, got me into a Trend Trend Trade short for CRUS. I got short under intraday support at 19.25 and so did she off of her trade idea. It turned out to be the trade idea of the week, but had the real possibility of being cut short too early and then followed with distracting guilt, regret, and grief for a failure to capture the real move.

At about 19, KMay asked, “Bella what are you doing with CRUS.”

I detected a concern in her voice about giving back her open profits. I was puzzled why she was even thinking about covering because none of my Reasons2Sell had appeared.

"KMay, I am not even really looking at it. It just started. What is the next technical level?"

"18.75. And then 17.75ish after that."

"Okay, I will take a look at the stock when it gets there (18.75)."

At 18.75 CRUS blew through the technical support level. We both continued to hold the position. I was not even thinking of covering the trade until one of my Reasons2Cover materialized. And none had so I sat unconcerned about giving back open profits and KMay was now not focused on her fear of giving back unrealized gains but the right exit.

"KMay, let's let the stock tell us when it's done. I will cover when it breaks the downtrend on the 15 minute or perhaps near the next technical support area."

What happened? Well for you swing traders, by the next day CRUS was trading at 17.50. For you intraday only traders, CRUS dripped down in a beautiful trend to 18. So instead of being overly stressed about open profit at 19 and potentially covering too early based on irrational but all-to-human trader anxiety, we let the stock run and show us the exit. As it turned out, this exit was considerably lower than the first hint of trader anxiety from KMay about a cover. These are exactly the types of positions Reasons2Sell will help you trade better. Okay, I am excited for you guys to learn this exit technique, so let's dive deeper on how it all works.

Let's introduce some Reasons2Sell, which perhaps you can use to craft your exit rules for winning positions, with specific trade examples. It is not important what your exact rules are for your Reasons2Sell, but it is vital that you take the time to determine your Reasons2Sell for your winning positions. Doing this will dramatically improve your trading exits, your understanding of when to take quick profits and when to let them run, and your trading P&L.

Reasons2Sell

The most common Reasons2Sell include the following:

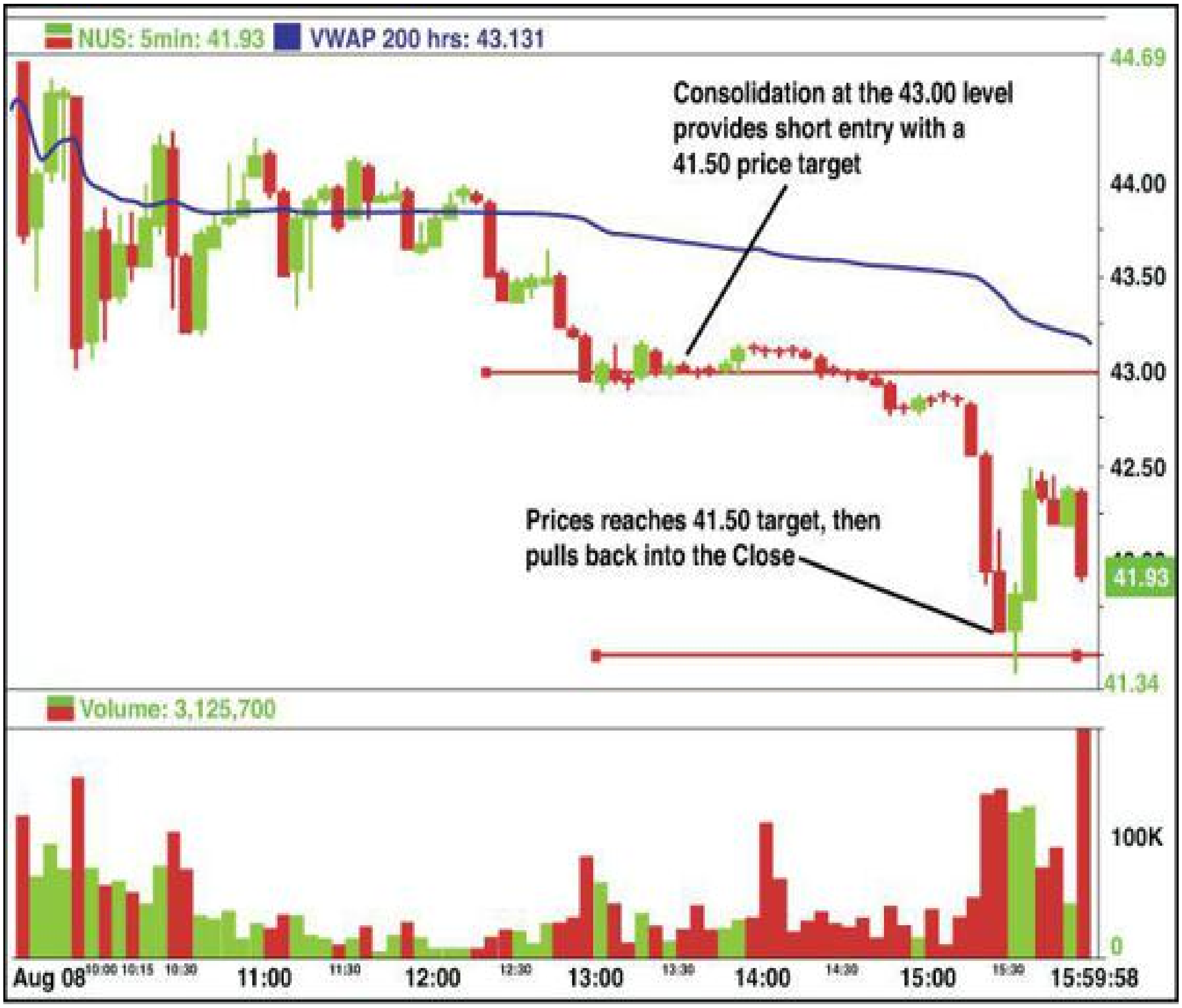
- Stock hits your price target.

- Intraday uptrend is broken.
- Breaking news about the stock.
- Market is at an important technical resistance level.
- Breaking news in the market.
- Unusual seller on the tape.
- Clear buying pattern dissipates.
- Time clock goes off in your trading brain.
- Too steep.
- Too much of a pullback.

Let’s examine each of these Reasons2Sell individually with actual trading examples for illustration. Also note that we will revisit Reasons2Sell with some of the trades discussed in detail later in this book.

Stock Hits Your Price Target

Have a target or set of targets before your enter a trade. Follow your plan and sell when your targets are reached. Targets generally are the next important technical level in the stock we are trading.



Intraday Uptrend Is Broken

Determine which time frame you will watch with your Trades2Hold. There is no right answer as to time frame; just be consistent with your approach, whether the 5-minute, 15-minute, 60-minute chart, and so on. If a stock breaks the time frame for which you are watching for this position, exit.

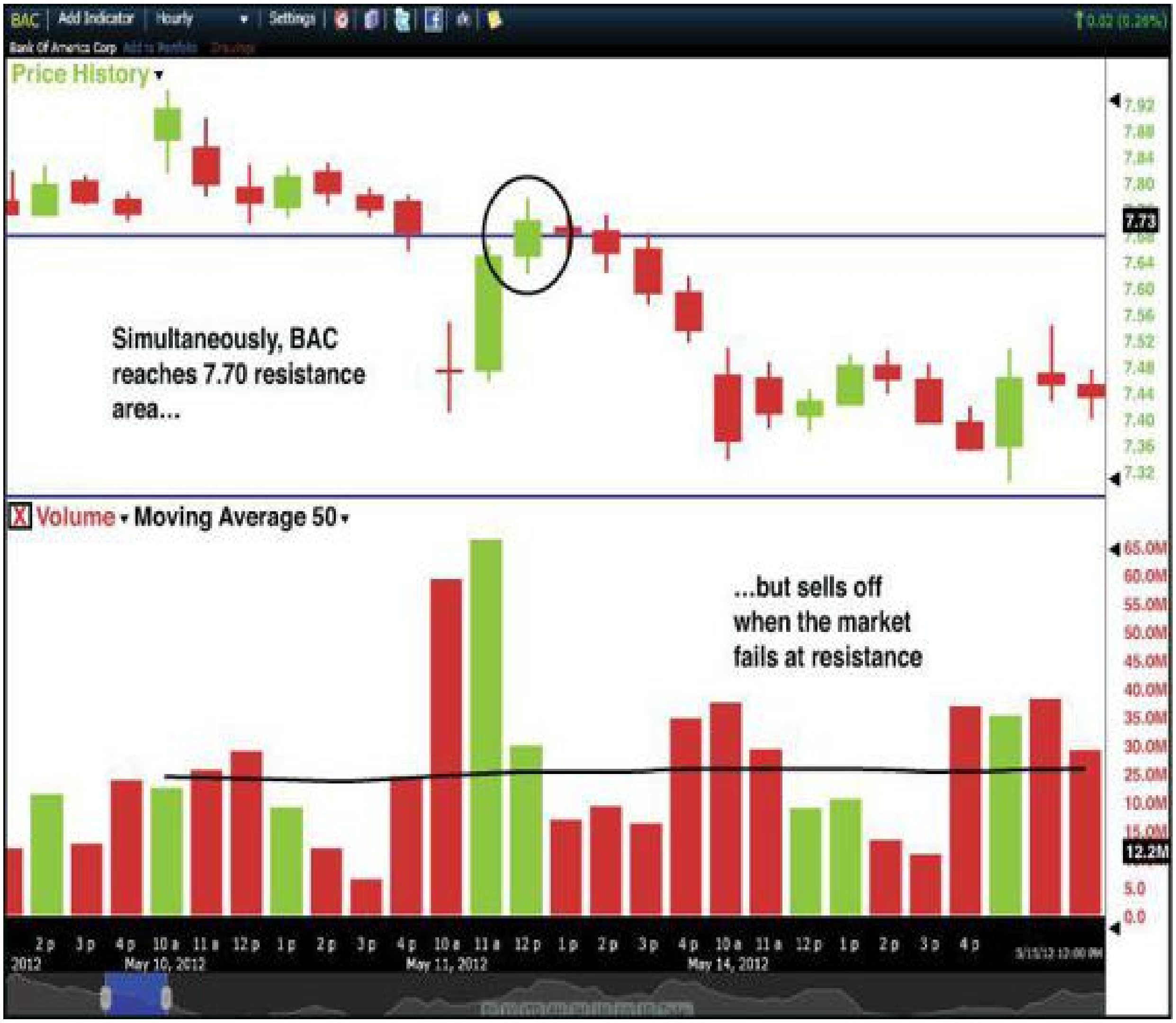
Breaking News about the Stock

If unexpected news suddenly breaks about your stock, you may want to hit out and then reevaluate. This breaking news could be the catalyst for a huge new move in the stock. All of the intraday trading data up to that point might now be less important than this breaking news.

Market Is at an Important Technical Resistance Level

Most stocks follow the overall market (although Stocks In Play have order flow independent of the market). However, an overall market level may mean selling will enter the market and cause your stock to trade lower even if it is In Play. You may consider selling or at the very least lightening up on your position at market resistance.

SPY 5min: 135.55
VWAP 200 hrs: 136.057
136.91
136.60
136.40
136.20
136.00
135.80
135.55
135.40
135.20
135.07
SPY reaches technical resistance area that it has failed to hold above for the past several days...
Volume: 111,657,520
2,500K
0
May 11
10:15
10:30
11:00
11:30
12:00
12:30
13:00
13:30
14:00
14:30
15:00
15:30
15:59:59



Breaking News in the Market

If a big event occurs, it might cause the market to move erratically, and therefore you may want to sell and reevaluate. Examples of breaking news include a member leaving the euro zone, Middle East conflict, or a government shutdown.

Unusual Seller on the Tape

If your stock tries to get above a price several times on outsized volume and fails, then consider selling. We will study the potential impact of unusual buying with the KCG trade below.

Clear Buying Pattern Dissipates

If a stock is showing a distinct buying pattern and that pattern disappears, consider selling. Reading the Tape skills are most helpful to spot such patterns.

Time Clock Goes Off in Your Trading Brain

If after a predetermined amount of time your position hasn't done what you expected, consider selling. You may develop a trading system where you want the bet to move in a certain direction and do so in a specified period of time. And if it doesn't, this will be your Reason2Sell.

Too Steep

If a stock spikes up too far and too fast, you may decide to sell your position or at least lighten up. Now the risk of the stock trading lower from this potentially overbought price may cause you to exit.

Too Much of a Pullback

The pullback in the stock you are trading may be more than you expected. If you see this, you might consider selling. Generally, strong stocks have shallow pullbacks.

Trading Day Ends

Because we are intraday traders, we might decide that the closing bell is our exit. (There are trades we will hold overnight.)

So, these are some common rules for selling a Trade2Hold long. We develop Reasons2Cover for Trade2Hold shorts, which generally are the mirror image of our rules for the long side. Please develop these rules that make sense to your trading and start deploying them to manage for better exits. Congratulations—you now have a smart and professional system to handle your winning trades!

Next up is Shark's PlayBook Support Play in KCG archived in the SMB PlayBook template style.

Support Play: Unusual Hold on the Bid Above an Inflection Point (KCG)

Shark

KCG

08.03.12

Strategy Description: Unusual Hold on the Bid

- Unusual buying on the bid.
- The bid just will not drop after repeated testing.
- Step in front of the bid and get long.
- If the bid drops, exit your long position.
- If the bid holds, Trade2Hold.
- Expect a big move.
- Foreshadows a huge buy order.
- Why isn't the buyer dropping?
- Above inflection point increases the win rate for this trade.

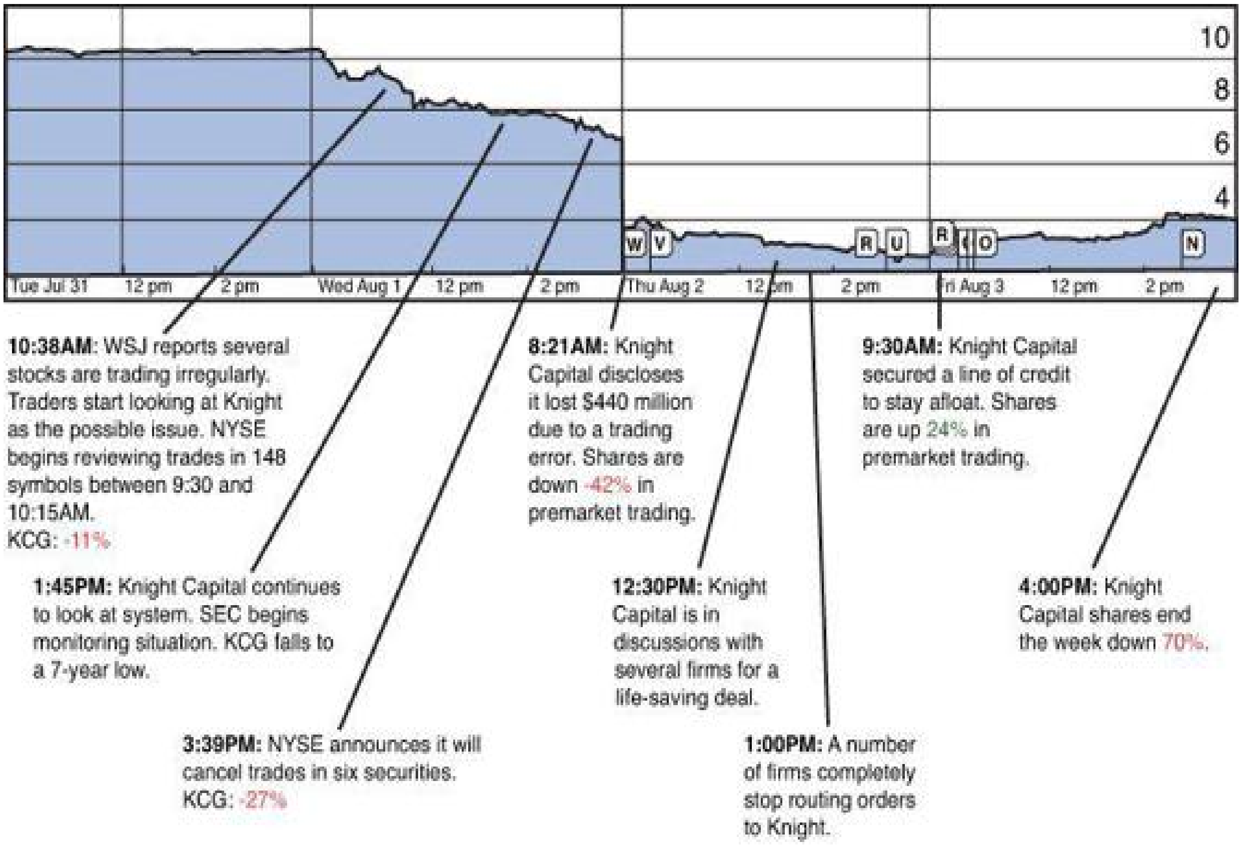
Big Picture

On the daily, SPY is in an uptrend channel. In the last week, we consolidated near the top end of the channel above 138, but broke below 138 and 137.50 the prior day. Today a gap up brings us above 138, and a good jobs number has us flirting with recent highs around 139. Holding above 139, looking for a move to 140–140.50.

Intraday Fundamentals 2nd Day Earnings

- Shares of Knight Capital, KCG, climbed 57 percent to $4.05 on Friday. For the week, however, they fell nearly 61 percent.
- Knight's shares tumbled in the previous two sessions. They closed Tuesday trading at $10.33. Knight said Thursday that exiting erroneous trading positions cost it $440 million, raising concerns about its capital position. The erroneous trades were caused by a glitch in the installation of trading software on Wednesday morning.
- The *Wall Street Journal*, citing unnamed sources, reported on Friday that Knight has received a credit line that will allow it to

stay afloat.



Knight Capital Group (KCG)

Knight Capital Group, Inc., a financial services company, provides access to the capital markets across multiple asset classes to buy- and sell-side firms and corporations; in addition, it offers capital markets services to corporate issuers and private companies primarily in the United States. The company's Market Making segment engages in market making in global equities and listed domestic options. It primarily offers client and nonclient electronic market-making activities in equity securities quoted and traded on the exchanges, over-the-counter markets, and option markets.

Average Volume: 8.1 Million

52-Week Range: 2.27–14.00

Short Float %: 11.0 percent

Average True Range (ATR): 0.40

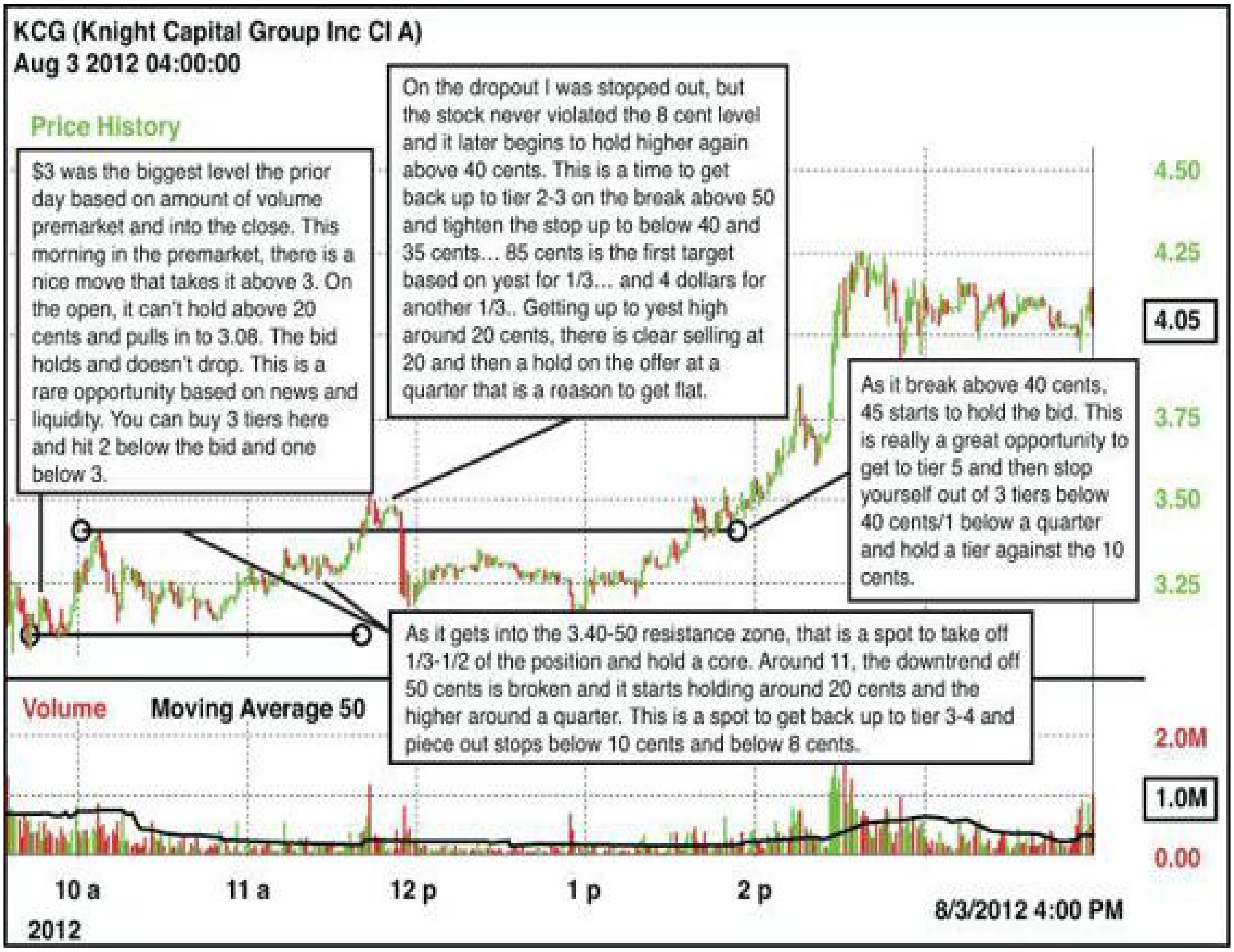
Long-Term Technical Analysis

Short-Term Technical Analysis

Reading the Tape

- Unusual hold on the bid at 3.08.
- Buyer was tested but would not drop.
- There was 20 times the normal volume done at the same price.

Trade Management



Trade Review

I like my aggressiveness the first time it started holding higher... was long 4,000 shares looking to add. The problem was that by buying on the way up, I was a bit top heavy and gave too much back on the drop of 40 cents. I should have been tighter with more size up there and longer originally from the 8c price. I think I gave 20 cents too much importance on the open, which made me want to buy less underneath the 20 cents when the bid held... when really 3 was the biggest level and that is the price to get amazing risk/reward. Good job sticking with the play after the failure at 50 cents and getting aggressive on the second break. Again, was a bit too top heavy but still made a decent trade. I like that I was willing to really size up and risk money on the play; just wish I had done it from a bit better price.

Trade Idea

Long above 4.25 tomorrow. Watch 3.50 and 3.

This is our favorite play found by Reading the Tape.

Next is a trade discussion on this Support Play with Shark, our desk, and me.

The comments in the columns are me trying to clarify the trade discussion for you and at times talk directly to you.

Most traders overvalue the importance of the trading day—their trading. The least important part of your trading day is your actual trading. The work you do after to improve and prepare for future trading opportunities is most important. This conversation after the close, on a past trade made, is an example of the work pro traders do on our desk to improve their game. These are the moments they are making the most progress with their trading. You are about to absorb a great deal of trading knowledge by peeking in on these trade review conversations with an SMB trader, our desk, and me on real trade made in real-time. You are about to improve as a trader.

From Our Training Room: A Trade Discussion with Shark

Shark: This is a trade from KCG on Friday. It's an Unusual Hold on the Bid Play. Just a brief description of the strategy. **It's a simple play where you see someone is buying on the tape; they're taking prints, and they just won't drop.** They get pounded, they get pounded, and the buyer just won't drop.

The characteristics of this play might indicate that the buyer has a large order; otherwise, why wouldn't they drop the bid and buy the stock lower? You'll see it all the time someone's buying on the bid: They keep buying, then they drop it, buy a little bit more as they drop the bid, and then maybe walk the stock higher. But if someone's just holding a stock at one price, it's unusual and might indicate that it might trade higher.

Bella: Just to clarify. You mean that someone just keeps buying the stock over and over and over again at the same price?

Shark: Correct.

Bella: As opposed to what normally happens, where they buy around a price?

Shark: Right.

Bella: Usually, they buy a little bit, they drop, they buy a little bit, and they drop a little bit more. Then maybe they step up and they buy higher. But when they are just buying at one price, you can almost hear someone on the phone at some big hedge fund saying, “Do not drop the bid. Buy 500,000 shares on the bid!”

> *A passive-buy algorithm (algo) buys some at a whole bunch of different prices without aggressively paying the offer and stepping higher to fill an order.*

And in this day of algorithms, everyone on the Street has bought some fancy algorithm to help buy stock at the best price, enabling them to very easily put in that order to buy 500,000 shares with an algorithm that they bought from, say, Deutsche Bank and they can just, say, buy 500,000 shares using the passive-buy algorithm at the best price. And when they choose not to do that, they just sit there and buy a stock at the same price over and over again. That’s unusual...that’s why we call it an *Unusual Hold on the Bid Play*.

> *There are many subsets of support plays, with this being one of our favorites. Which each trade, you develop subsets for your trading strategy.*

This Unusual Hold on the Bid foreshadows that there might be this monster buy order coming into the market. The buyer or buyers are anxious. They are afraid to drop the bid and try to buy lower. With this trade, they are afraid to see what would happen if they drop the bid at 8 cents and try to buy it lower. But I was saying to you before we came in here, Shark, that I almost find this to be an embarrassing trade. I am almost embarrassed to teach this trade. But the damn trade works, and it is worth learning. And it also helps us learn the principles of how to trade a Support Play, as this is a subset of a Support Play.

When we go to the bank to cash our profits in an Unusual Hold on the Bid Trade, the bank will take this check.

Shark: Yeah, it's rare. It's almost too simple.

Bella: That's what I meant. That it's so simple that it's almost embarrassing to talk about. But in this case, the Unusual Hold on the Bid sets up a very interesting trade. It's the catalyst for quite an interesting trade.

Shark: If the buyer drops the Unusual Hold on the Bid (UHOB), the stop is right below the buyer. It's a Trade2Hold if the stock starts working for you.

Bella: There's an important point to make about KCG being above an important inflection point, in this case 3. Can you explain that?

> *Buy above the important support level and not just below it (say, at 2.95).*

Shark: Sure. Well, in this particular instance, you always want to research what levels are around, and in this case, it was right above an important level, which really makes the trade much better. For example, 3 is a really important level from the last day. If the buyer is holding 2.95 and won't drop, won't drop, won't drop, this might interest me, but it would not be as good of a trade as KCG being above the level of $3. You always want to combine your checks. In this case, KCG is above the inflection point of 3 *and* there is an Unusual Hold on the Bid above 3.

> *Sometimes the overall strength of the market is not going to be a huge factor in your trade.*

Shark: The Big Picture in this play doesn't matter so much, but overall the SPY has been in an uptrend channel (see Figure 3.1). We were hanging around the top of the channel; then we broke down with the ECB comments below some immediate support levels. Then the jobs number gapped us back up, and we are taking out 139 and flirting with recent highs. So it's been a stronger market. It has not been the easiest uptrend market, but again in this particular setup, the play is more stock specific as opposed to pulled higher because of the strong market.

> *I know a firm that made 2.5 million on this trading glitch. They would have made 16m, if not for cancelled trades.*

Figure 3.1

Shark: For the Intraday Fundamentals, Knight Capital had this glitch in their computer system that sent a lot of orders that weren't supposed to be sent into a bunch of stocks, and the firm took a big rip. This glitch in their trading software actually put them in jeopardy of going out of business. They're not a huge firm, and they lost about $440 million. The glitch was a few days ago, and the reporting of their loss was the day before. Because of these events, KCG traded all the way down from $10 to $2 in two days. There was new big news coming in this morning on KCG. There were rumors about potential investors offering capital to the company.

Bella: So, basically, we are in a situation before this trading session where Knight was off over 60 percent, and there was a real concern that they might have to declare bankruptcy or go out of business?

Shark: Right.

> *Knight Capital accounts for 20 percent of all U.S. equity options volume and 10 percent of all U.S. equity volume.*

Bella: This is new news of a white knight offering a parachute for Knight. Knight is a terrific firm. Their technology is wonderful, and most of the Street uses it. So this was just a one-off error; it doesn't have anything to really do with KCG's core business.

> *Great job of using the levels the day before for this trade.*

Shark: Moving on. This is the longer-term chart, and you can see the pronounced decline (see Figure 3.2) in the last couple of days. The more important chart is the two-day chart because these are the only levels to look at since there has been so much activity the past two days (see Figure 3.3). So yesterday, $3 was a super important level to look after in premarket. Some guy just kept selling there at 3. KCG finally got above there, and it had a one point up move. Then KCG kind of reversed, and you will see some other levels. There was a big seller at 3.85 cents, 3.50 didn't lift the whole afternoon, and then that $3 was another battle area into the close. Those are levels of interest to me as a trader on this day. So coming in this morning, KCG was trading around 3, and that's my main level. That's where the most volume was done the prior day.


Knight Capital Group Inc Cl A Add to Portfolio Drawings
Price History
3.09
X
Volume
Moving Average 50
77.61
04
05
06
07
08
09
10
11
12
02:28:05
13

Figure 3.2

Figure 3.3

Bella: You have your levels from the day before, but we got very substantial new news. Coming in the day before, people were trading KCG like they were going bankrupt, and then now if there's going to be a capital infusion into the stock, what is your thought process about using those techniques levels from the day before?

Shark: I would just focus more on the price action because the prior day, people can be forecasting a buyout, and then the news comes in the next morning. So I would be looking more at the levels the past two trading days. I don't have a fundamental analysis edge. I do not know more than others trading this on the Street based on the news. **I just let the price action tell**

me where the stock is most likely to trade. As you say, Bella, I am a trader, not a fundamental analyst. But because of substantial news, KCG might go back up to these levels or even much higher.

Bella: I was thinking that the psychology the day before was ultra-negative, and today we have a really positive catalyst. We don't want to be unaware of those two-day levels, but we should understand that this substantial new news might be a catalyst to blow right through those two-day levels. A new psychology for KCG may take control and cause a steep up move, pushing easily through those two-day resistance levels. Those two-day levels might be less important than you think. *(Bella smiling)* Now, they turned out to be important, didn't they?

Shark (*smiling*): Yes, they did, Bella. That is why I was watching them.

(Traders laugh.)

Bella: Okay, good. I just wanted to present another way to look at this trading event. I was wondering that when we were trading it. The psychology from the day before was that they were potentially going out of business. The next day was that they were going to be saved. And would KCG trade so differently on this day of a new psychology. What do you have on the tape?

Shark: On the open, we have a nice move through 3. There wasn't that much resistance at 3. Then there's the Unusual Hold on the Bid we were talking about at 3.08. The guy just wouldn't drop. **He was there buying at 3.08 and buying and buying at the same silly price.** Also, this is important to note that 3.08 is an unusual price to buy a ton of stock. People usually like to buy at 10 cents, 5 cents, the whole number. So, yeah, there was a lot of volume at the same price, 3.08.

> *When you see a UHOB get big, if there is a way to exit below this price. Think Tier3.*

The 8 cents is obviously a great place to start your position. This sort of news, the volume, the liquidity in the stock is a good opportunity to get in with a lot of size. Maybe you usually start Tier1 on a previous day, but today maybe you would up your position size to Tier3. You have that 3 level under you that would be your protection, so maybe you do Tier3 there. Your stops are to hit two tiers below 3.08 and the last tier below 3.

I know for me it was a mistake not starting with enough size from the original price of 3.08 because in a lower-price stock like this KCG, it's not going to move 30 to 40 cents where you can work your price. You really need to be in from the good price where you want to hold.

> *For Shark, Tier1=1000 shares, Tier2=2000 shares, Tier3=3000 shares. It is up to the trader to determine the size per Tier.*

Bella: That's a very important point. Just clarify how you enter 3 lots (Tier3) long from 3.08?

Shark: Enter 3.09 for 3 lots long if you pay the offer.

Bella: Where are your stops?

Shark: 7 cents, and 99 cents. Or 98 cents, whatever you want.

So for me, 3.20 was a little bit of an inflection point on the open and the prior day. So right away I'm probably going to offer some up in front of that price. You have the option that if it comes back near 8 cents; you can play around with some of the position—maybe 1 tier you're just working up and down. But holding your core up into that 3.40, 3.50 area....

Bella: It wasn't really trading above 3.20 after it was holding 3.08. It really wasn't trading above 3.20, correct?

Shark: Right.

Bella: So that's why you wanted to take some off at 3.20?

Shark: Right, and 3.20 was also sort of an inflection point the prior day. It's wasn't an incredibly significant level, but it was a level to me. So if you want to be aggressive, you can add through that 3.20, but really the trade is from that 8 cents up to that 40 to 50 cents, where you want to start taking sales. In this instance, the first up move is pretty steep, so maybe you take 2 lots off up there and wait for some consolidation.

Bella: Let's talk about this in more detail. This is high-level trading you are doing, and I want to make sure that everyone in the room learns your advanced trading technique. So you are long 3 lots from 3.08. KCG gets up to 3.20. Are you selling some?

Shark: Yeah, I mean 1/4 or 1/5 of the position. I sell a little bit to cover my risk in the trade. After I cover my risk, now the whole trade is gravy. So then maybe if KCG goes back to 10 cents and it starts holding, I'll buy some KCG back, and I'll just do that to make cash flow.

Bella: And if it gets above 3.20?

Shark: Then I'm thinking maybe I want to get up to Tier4, depending on whether someone is holding the offer and then it lifts or someone is holding the 20c bid. This depends on what it looks like on the tape at 3.20.

Bella: Okay, so we're going to play the range, buying at 3.08, 3.09. And in front of 3.20, take some off; let's say we take 1/4 of a position off... so maybe that's 700 shares in this case. We were long 3,000 shares at 3.08, KCG goes back up to 3.20, and then we take off 700 shares on the offer in front of 3.20. If it pulls back and holds 3.10, we put the 700 shares back on, and if it goes back up to 3.20, we take the 700 shares off again. So we make the spread between 3.08 and 3.20 until the range breaks. **We make a Cash Flow Trade until KCG breaks.** There can be very good money in this Cash Flow Trade before KCG breaks. You might catch three spread plays and bank $300 before KCG breaks. That can add up quite nicely. And then, of course, if KCG gets above 3.20, we get longer.

Shark: I mean sometimes you can do that four or five times, and you'll make some nice cash. So KCG gets above 3.20, and it's pretty steep up into that next level of 3.40 to 3.50. You could see 40 cents just doesn't really lift when it gets up there. This is a change of pattern on the tape. You hit the bids when 39 cents drops. You get down to your Tier1, and then you wait. This is not the only way to trade it; this is just the way I traded it.

Bella: When you say you saw a change of pattern, what do you mean by that?

Shark: KCG gets above 20 cents, and there are a lot of people paying the offer. This is a sign of strength on the tape. Then KCG gets up to 3.40, and people stop paying the offer. They had paid the offer and paid the offer and paid the offer, and then they just stop. Next, 40 cents doesn't lift the offer, and then the bids start dropping. The trading decision to lighten up and exit some of your position is simple: 30.40, that's a level from yesterday. Combine that with the offers not getting paid, and a dropped bid at 39 cents, and you have your exit of hitting the bids.

Bella: Was there a held offer at 3.40?

Shark: I don't really remember specifically, but I'm pretty sure that those 40 cents wouldn't lift. They paid him for a little bit. I don't think there was so much volume, but you get down to Tier1 and wait to see if it holds up there. But KCG comes all the way back into that 3.08, 3.10 level, and you can buy a little bit back there. That is still an intraday support level to buy in front of. So maybe you just get back to Tier2 and wait. There's not much to do.

Bella: But you didn't want it to go all the way back to 3.08. You wanted it to hold above 3.20, right?

> *After a stock breaks resistance, you want it to hold above that prior resistance.*

Shark: Right. But you are just holding your Tier1; there's not much else to do.

Bella: Does everyone understand that? We got 3.08 buying, 3.20 selling. It breaks above 3.20 and goes and finds another resistance level at 3.40. But when KCG pulls back, we don't want it to be below 3.20; we want that to now actually be the support level. So it's not that the trade can't work or can't go higher. It's just not as good of a trading pattern as if KCG now held above the 3.20 level. We want resistance to become support and helping to confirm a likely push higher. Your win rate will be lower if KCG retraces all the way back to the 3.08 support level from where it started.

> *Advanced traders break up their stops into pieces and exit with a whole set of different stops for each piece.*

Shark: Also KCG needs more time to work if it's going to pull back that much. Okay, so say you don't like how much it pulled back; you hold your Tier1. You see around 11ish KCG holding around that 3.20 again. KCG is not really getting below 15 cents or 10 cents, so maybe you add another tier here and set your stops below 15 cents or 10 cents. Then KCG starts holding near that 30 cents, it's not really dropping 25 cents, and then maybe you get back up to Tier2 and set your stops below 20 cents or 10 cents.

Bella: What does that mean, *piece out your stops?*

Shark: It means, for example, if I have 2,000 shares, I put a stop at 800 shares at 24 cents, 800 at 19 cents, and the rest underneath 10 cents. To piece out of my stops means that I put my stops at different prices. **This increases my odds to catch the real move for at least some size while still being responsible with my risk.**

> *On the desk, I was stalking Shark to get really big if KCG got above 3.40. No Trader Wuss Syndrome here.*

So, KG gets above 3.40, and for me I thought this was the spot to get really aggressive. It didn't work out so well, but KCG gets above 3.40. It's our level, and you see a buyer at 45 cents. This is when you put on max risk. You cannot control the results.

Bella: I have to admit, I think I was encouraging you to get really big above that 3.40 because I really thought with a change of psychology that KCG was going to have a run. I didn't want you guys to miss that run. But, yeah, this is a great setup above 3.40. There's just one thing I was concerned that you didn't do very well. And I wanted to talk about that with you. But we can get to that.

Shark: Okay, so at that point holding above 40 cents, I'm pretty much Tier4, ready to add another tier through 50 cents. I put half my stop below 40 cents because it started to hold above that previous resistance and then half my stop below 25 cents because that's the last area where KCG held.

> *Basically the stock becomes messy and doesn't go up like we thought it would. But still the right thing is to be **big.***

Bella: Okay, so we talk about this a lot. **Your job is to do the right thing,** and this is doing the right thing. We talk about not being a wuss; **this is not the time to be a wuss.** We talk about that fact that you are actually costing yourself money with a really terrific setup if you don't put a lot of risk on. This is another example of when you must be big. So what happens?

Shark: The buyer at 45 cents drops, and KCG goes down pretty steep. I get stopped out in it. This is unfortunate but....

Bella: Where did you get stopped out?

Shark: Below 40 cents and below 25 cents. But when KCG stopped going down around that 20 cents, I decided it's still above that original hold price, so I bought some back.

Bella: Did you get stopped out for all of it?

Shark: For all of it, but at that point, I'm getting ready to buy back

Bella: Why would you be stopped out of all of it since it's still above 3.08, meaning shouldn't you be at least long Tier1 until KCG gets below that support level?

You shouldn't get flat here unless KCG traded below 3.08.

Shark: Well, in this case, I hit out. But I'm also thinking when KCG stops going down I'm going to buy it back. So I hit out at 24 cents. I got flat. That was my last previous support level. But I'm thinking KCG is still above 8 cents, so now when it gets above 20 [cents], 15 cents, I'm going to buy back. Probably not Tier1 in this case. Probably 1/2 of a tier because I don't like that candle from below 45 cents back to the first support area at all as far as for the long. But KCG does start to stabilize; there was a seller at 30 cents, so I get back up to a full Tier1.

A deep red candle means a sharp down move.

A failed breakout offers a lot of downside risk.

Bella: Question, sometimes when a stock gets above a really important level, you can have one of those deep red candles because too many people get long above this 40 cents and they get flushed out. And another way is a stock gets above this 40 cents, and it actually gets too steep. Sometimes when the candle is much steeper to the upside than it's been all day, you can have that candle to the downside—that's steeper than you've seen. The steeper up move causes the steeper down move, or pull in. But it looks like what happened here is that KCG got above a really important intraday price, and sometimes when that happens you get that steep candle because everyone is buying above resistance. **So there's that risk; a failed breakout offers a lot of risk to the downside if it doesn't hold that 3.40** (see Figure 3.4). Is that what happened?

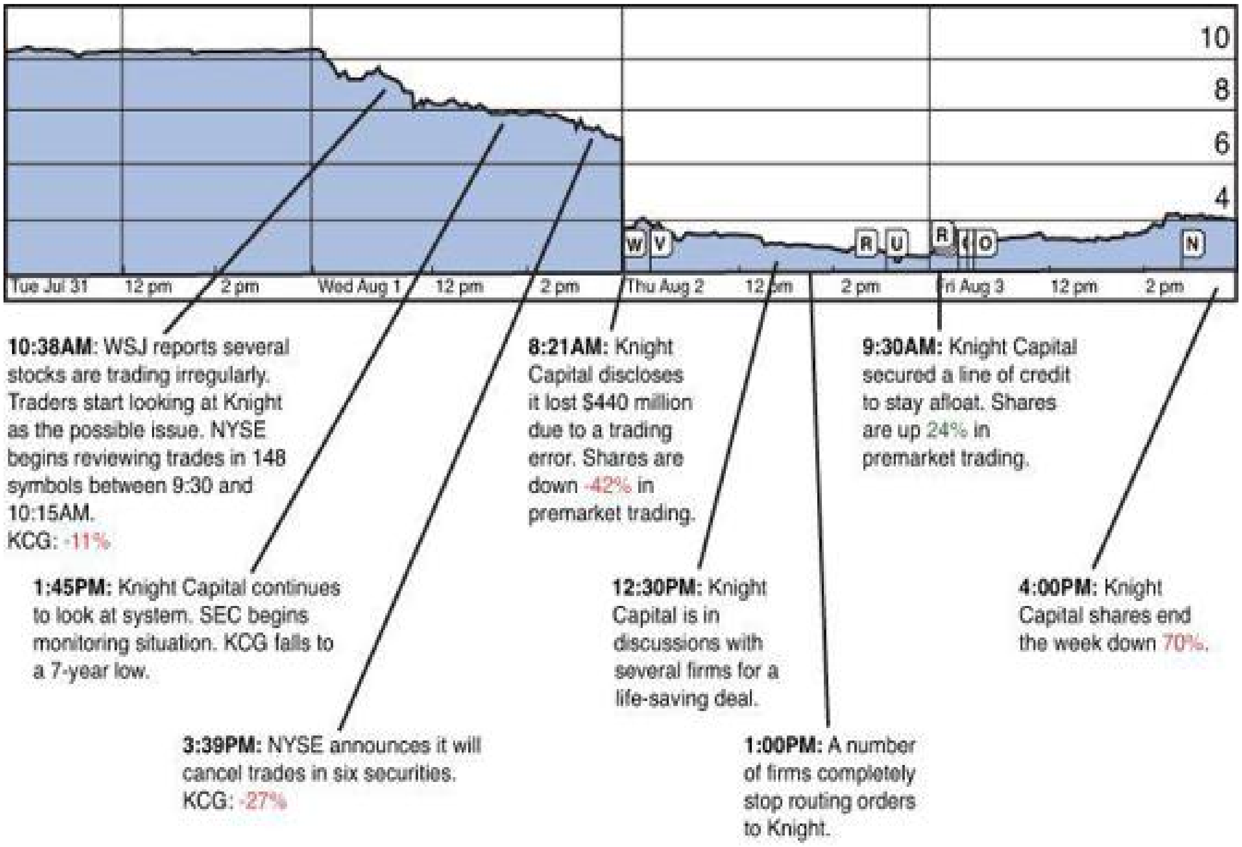


Figure 3.4

Shark: Yeah, so I didn’t like how KCG pulled in at all. KCG does start to recover above 3.30 again. There was a big seller at 27 cents. I remember there was a big seller there that wouldn’t lift, and then when that guy lifted, I got back up to a full tier. I just kept my stop below the original hold. We get back above 3.40 and then up to 3.50. Finally, KCG starts holding a little above 40 cents. So that’s another spot to get up to Tier2, Tier3, and once it finally got above 50 cents, it took a few tries. There’s nothing really to do until it gets up to 85 cents. I thought KCG got steep to that price.

Bella: Okay, let’s just talk about something that I think needs to be discussed. You’re looking at that 3.40 level. It’s an important level, but if I were to critique some of your mindset in this particular setup, I would say that you were too married to the idea that it had to go up above 3.40 and go find 4ish the *first time* it got above 3.40.

Sometimes it takes a couple of times. Sometimes the stock is not ready to actually break out the first time. The stock may not be ready to break out when psychologically you want it to break out. And did you overvalue that it just didn't work the first time? That happens. Were you psychologically prepared to be really big again or big, maybe really big when it got to 3.40 the second time?

Shark: I actually got pretty aggressive again at 3.50. I was probably holding Tier1—1,000 shares or 1,200, something along those lines. And KCG got up to 3.50 and I paid for a lot, through 3.50. I hit out of some, and then when KCG got below 40 cents, I hit a little more. But I kept trying through 50 cents, and then it finally started looking different, so I got back up to a Tier2, Tier 3, and was able to hold it pretty well for the up move.

Bella: So you did get back into Tier3?

I stand corrected!

Shark: Yeah, well, it went through 50 cents like three times and didn't go up. So I kept paying for a thousand shares and then hitting out for a couple cents less, paying for a thousand shares and hitting out, and then finally KCG got a little higher through 55 cents and hadn't gotten above 55 cents, so then I paid for a few more thousand shares and dropped 50 again. Then I got down to 1,000 shares, and I caught it for another 2,000 shares when it finally went. *(Shark smiling)* I can't say I didn't try.

(Traders laugh.)

Bella: Okay, so what you are saying is that for this setup, it wasn't a clean enough intraday breakout above 3.40 for you to really crush it?

Shark: Right.

Read carefully please.

Bella: You have to protect yourself and play defense first with all trades. If the stock doesn't act a certain way, you will continually get stopped out and not crush it. **But it is more important to play defense and control your risk.** So, you take the small losses before catching the big up move. Professional traders take losses all the time. **Professional traders are first interested in controlling their risk before being right about a trade. Keep your losses small, and let your winners run.** That is the life of the pro trader. It can be frustrating at times. You will find yourself wanting to say the heck with taking that small loss, the stock will go higher. But that is not the mindset of a pro trader. A trader is mostly a master of risk management.

Shark: Exactly, and after what happened the first time with the failed breakout, I have that in the back of my head.

Bella: You were doing the right thing, but it just wasn't clean enough for you to crush it, which happens. It happens.

Shark: So in the rest of the trade, KCG got steep to that price. Again, it's sort of the thing that happened the first time at 40 cents, holding the offer at that price. It was like 82, 83 cents, so I sold a third of my position there. I think I might have tried buying on the pullback at 60 cents. Four was the next level, so I got pretty light there because I thought it was pretty steep and then at 4.20. At 4.25, there was clear selling on the offer, and then 25 cents just didn't lift.

Bella: Was 4.25 as much as an Unusual Hold on the Offer as 3.08 was an Unusual Hold on the Bid?

Shark: It might have been. There was a tremendous amount of volume at that price. It didn't lift.

Bella: You sold in front of there, 4.25?

Shark: Yeah.

> *A Trade2Hold means you are holding until there is a Reason2Sell.*

Bella: Okay, so that can be a reason to get out of a Trade2Hold. If you see massive selling at a particular price that you had not seen previously, that can be a Reason2Sell. You might add that to your list for a Reason2Sell: a Trade2Hold.

Shark: Yeah, combined with the fact that it was really steep and it was at a price from yesterday: 4.20, I think was the high from yesterday. So it was combining all those factors.

Bella (*holding up fingers to enumerate the combining factors*): Too steep, massive selling, and a level from yesterday.

Shark: Correct. So then my next mindset was I'm going to buy the pull in, depending on how it looks. But KCG really didn't do much the rest of the day.

(*Trade Review slide shown*): I think I was aggressive, but the main thing that tripped me up was not being Tier3 from the beginning at 3.08. I think I only started with 1,000 or 1,500 shares there, and I wasn't really afraid to buy on the way up. But when KCG dropped that 40 cents and had that red candle, it made me much more hesitant the second time to load the boat.

In stocks below $5, buy mostly on the bid. And fight for the best prices; otherwise, you will not make money consistently.

Bella: I think that is a very important part of this trade. So if this were a $50 stock and the levels were 50.08, 50.20, and 50.40, the way that you ended up attacking the trade probably makes more sense. But you made a really interesting point: It's a $3 stock. So a move from 3.08 to 3.40 is a big move in a $3 stock. A move from 50.08 to 50.40 is the spread sometimes in those stocks. **You really have to fight for your prices in something that's as cheap as KCG.** A move from 3.08 to 4.25 is massive.

Shark: It's like 30, 40 percent.

Notice his mindset: He focuses on what he gained from this trading experience. Superb quality to emulate.

I like how aggressive I was. I was ready to hold 4,000–5,000 shares in this position, no problem. It was a good experience being able to give back $1,000 of open P&L because at least I can say I did the right thing. And when it does happen and it works above 40 cents the first time, I'm going to have a good trade.

Bella: I actually feel better that you went through this review because I thought you gave up on it a little bit because it didn't really work that first time. But obviously, it just wasn't clean. Okay, good trading. Thank you, Shark.

Postscript

We have been having internal discussions about a path, in time, for Shark to become our next head trader. It is not a coincidence that the traders he mentors are some of the hardest workers at our firm. It's Sunday as I am editing this chapter. Two of his mentees are in our Midtown office with me. New traders doing work like Shark is how you build a desk. The daily work of Shark is how you build a trading career. There will be more interesting trading strategies to come in this book, but not a more important lesson to be learned about how to become a successful trader than by emulating the daily work of Shark.

4. TO: How Good Can *You* Be?

Football fans will remember wide receiver Terrell Owens, or TO, mainly for his over-the-top antics. On the field, with his talent and diligence, he established himself as one of the best ever at his position. But he just couldn’t keep his mouth shut and often let his ego get the best of him. As I write this, the more famous TO has hit rock bottom, is broke, divorced, and has just been cut from an arena league team in Texas that is mostly unknown to the general public.

But the young man we will call TO embodies all the on-field excellence that Owens showed for years but without the drama off it. Call it TO talent without TO attitude but with all the competitiveness of an NFL pro.

I remember vividly TO’s video Skype interview to gain entrance into SMB. I sat in my small office at One State Street, a block from Wall Street, walls covered with the Golden Bell, #12 of the Masters, Derek Jeter diving into the stands stopping his momentum chin on the stadium seat, impressed I actually had executed on this technology experiment. For me, technology tryouts often lead to disappointment.

TO and I had scheduled a call during his senior year of college. The call went like this:

> TO had been trading on his own with his teenage poker winnings.
>
> *I became more interested.*
>
> He had started an investment club at his school.
>
> *I became more interested.*
>
> He was marginally profitable.
>
> *I became more interested.*

He had been following our blog. He had read my book. He knew Steve, GMan, and the rest of our cast of characters.

Okay, you get the point; I was interested.

“TO, can you tell me a little about your trading strategy?”

There was a pause. He collected his thoughts. Later, I would learn he does this before answering any question, as he is wonderfully introspective and thoughtful with his responses.

"I like to fade stocks on the open," and he was off with specificity to his trading style. He was a senior. In college. Five years ago, I wouldn't have heard something like that when I vetted a college kid. This was no "I read the *Wall Street Journal* daily and watch CNBC" pat deja vuish interview.

In *One Good Trade*, we had introduced the Franchise, SMB's equivalent of the number-one pick in the NFL. The Franchise has since moved on to his own firm, but all good organizations must find ways to replace elite performers. That seat is now occupied by TO, literally. There is so much you can learn from his journey to consistently profitable. TO is the ultimate competitor. If anyone reads this chapter and can honestly say you compete like TO, I would like to meet you. First, I do not believe you. But second, please look me up, give me a ring, and I will probably hire you for our prop desk. And there is more about TO, a truly complex trader/person. This is a story of depth, layers, awesomeness, grit, fragility, flow, and self-fatiguing perfectionism. He is one step ahead of the competition, does the detailed daily work to build intuition, could fail at any moment, but is already a success. Let's see how.

TO: The Ultimate Trading Competitor

Often, traders (people?) mistake ego for competitiveness. Competitiveness is not trying to make more than another trader. Solely, it is becoming your best trader. This requires daily and detailed work. Work that TO has done. We will share the detailed trading work that he does and you can copy to make significant improvement as a trader. Competitiveness is being as good as you can be at your passion. Trying to win at anything else is ego.

- "I really want to be a good trader."
- "I really want to make more than (such and such) trader."

If you are not reviewing your work after every close, being prepared before every open, spending the day immersed in getting better every day, then, no, you don't. You don't want to be those things. You want to satisfy your ego. Find another game for that and leave professional trading for guys like TO.

Sitting on a trading desk and saying you want to get better does not make you better. That is talk. That talk has nothing to do with your individual skill development. Notice how the New England Patriots don't talk before the Super Bowl. What does their chirping about wanting to win the Super Bowl have to do with winning it? They must prepare their bodies with strength training. They need to protect Brady (their star quarterback) better. They need to watch hours of film to find the schemes to do this. They need to practice these new schemes so they can execute in game time. These are the things that will help them win. Not talk. Not ego. All of this before the game ever starts is their competing.

I cringe when people spout wanting to win at something like table tennis, which they might play once a year, shows they are competitive. Those stories about Michael Jordan so desperately wanting to win at ping pong are not examples of his competitiveness, but rather his large ego. Or the vacationing golfer who wants to beat his buddy because he feels he is a competitor. If you are not spending 30 hours a week on something to improve your craft, then winning at that something is to satisfy your own ego. Please do not confuse that with being competitive.

This is what competitive looks like as a trader.

Timeline: It’s 7:00 p.m. on a Thursday. I close my Internet browser, grab my North Face backpack, lock my office door, and look forward to a short subway ride home to see my wife. I am tired and hungry. My brain cannot process any more information for this day. I peek through the clear glass door that encloses our trading floor, expecting it to be empty. I am wrong. There is one trader left working on his game. It’s TO.

TO competes.

Timeline: It’s around lunchtime, and I exit my office to go grab some Sophie’s, the best Cuban food in downtown Manhattan. I can almost taste the marinated chicken, yellow rice, and pinto beans with their special hot green sauce as I walk quickly to the elevator. In front of me in our narrow corridor is TO and his sidekick Pippen. (We will call him Pippen because, well, Scottie Pippen was perhaps the best “sidekick” in professional sports history, playing second fiddle to Michael Jordan on six NBA championship teams. And Pippen is TO’s sidekick.) You might expect TO and Pippen, as young twenty-somethings, to be talking about last night’s beer blast and a pretty girl they chatted up. Nope. They are talking CHK. TO is explaining with supreme focus how he should have gotten shorter at 18, as a clear bearish flag pattern had developed. Pippen nods, absorbing every trading nugget of TO’s description. I check my BlackBerry, answer an e-mail from a trader in Australia, and share the elevator down to our lobby. They talk CHK the entire ride down. And then out the office. And then heading right as I veer left to grab my lunch.

TO competes.

Timeline: It's 7:15 p.m. on a Wednesday, and our principals meeting is complete. With 90 minutes of discussion now over, I slip onto the almost empty trading floor. There is TO again. He is watching a trade back in VRTX that he recorded via screen recording technology Camtasia 8.0. I ask him what he is watching. He responds he is trying to decide whether he should have faded a double intraday top. We watch back a particular segment of the recording together. This is his tenth viewing to my first.

"I don't have a problem with your skipping that short," I say.

"Yeah," he replies and then watches the segment again.

TO competes.

Timeline: On a typical day sometime around 9 p.m. EST, I receive the last daily trading review from the traders I work with one on one. If I recognize a trader who is working hard, and he or she starts to become profitable, I ask that trader to send me a daily review to which I respond with feedback. We do this every day. My BlackBerry buzzes, I am lying on my couch watching *Pardon the Interruption* via DVR, and it's TO's review. I immediately pause the show and open my laptop. I have come to look forward to TO's daily review like a delicious dessert. It's as if he wants me to know the best comes last. It often does. His reviews often read like an academic white paper—brutally critical yet brutally honest and factual at the same time.

Here's an example of one of TO's reviews, giving you an inside look at the detail of review for an elite competitor. Your P$L as a trader is determined by the work you are willing to do after close.

> Really nice day. I was very defensive too. I didn't need a whole lot to make money today. Can't say it was an amazing day in the market, or that there was a ton of opportunity. I just maximized what was given to me. I was worn out from scalping all day yesterday, and I made an effort to try to guide my day in a different direction. I just didn't want another open where I had to dig my way out of losses and grind all day. I made 5x more than I did yesterday with 1/5 the effort (see Figure 4.1).

Figure 4.1

1. I pressed my best stocks for the day by putting on size or trading/holding them throughout the day.

2. I avoided racking up gross losses by passing up 50-50 trades, stocks that didn't move, weren't clean, or weren't clearly directional. $220 in the loss column on my chop tracker—that's gotta be the lowest for me in ages. Now that's patience.

3. I stayed in observation mode. I wanted to stalk trades and trade ideas when they were ready. I didn't even want to put on a feeler 100 shares because I knew that would commit me to the play and lead to taking additional risk, because my personality is to make everything "perfect"—getting back in the play, trying to add, trying to scalp around a core, trying to improve my price, etc.

I had a nice safe stock in WIN on the open. Although I had 300 shares on below 11 as a feeler and it traded down to 10.30, I didn't make most of my money on the initial drive because there was hardly any trading volume in the stock. There was absolutely no reason, tape or news, to think a stock that traded so thick with so little ATR would get struck so hard. It was a surprise move from a conference call, and I covered early at 10.50. The real money came after the drive shows weakness, and it starts to hold lower below 10.40. So I don't need to get the first 50c to make money. I'm trying to remember this because trying to be the first guy in a move keeps getting me cracked on the open.

I need to learn to how to better flip the aggression switch on. I wasn't big enough in SGI. I was trading based on the results of the last few trades, and the prior two days, I remember getting burned by thinner stocks under the uptick rule. So I only had 400–700 shares on this stock. There were spots where I should have capitalized on getting huge with 1–2c risk, but I wasn't certain if it would work or if I really did have 1–2c risk. I should be risking $50–100 in SGI to be consistent, and I didn't. Then there are stocks like KRO yesterday where I just pile up losses more than I anticipated due to slippage, waste, getting back in, adding at random spots, etc. (see Figure 4.2).

long trades

Time	Symbol	Volume	Execs	P&L
10:30:20	WIN	2000	11	$61.00
11:23:40	LYV	4800	23	$-2.50
12:27:45	GMCR	200	2	$4.00
12:57:30	MDRX	600	2	$0.00
13:06:11	GLUU	800	2	$-12.00
17:33:55	JPM	1400	13	$60.00
18:00:45	ARNA	1200	10	$-12.00

short trades

Time	Symbol	Volume	Execs	P&L
09:33:24	WIN	12000	63	$344.20
10:34:42	WIN	2000	12	$-31.00
10:43:14	SGI	1806	16	$167.54
12:31:07	GMCR	400	3	$-10.00
14:46:28	SGI	1600	12	$127.00
14:51:02	ADY	1000	8	$-12.00
16:53:01	JPM	2000	20	$72.00

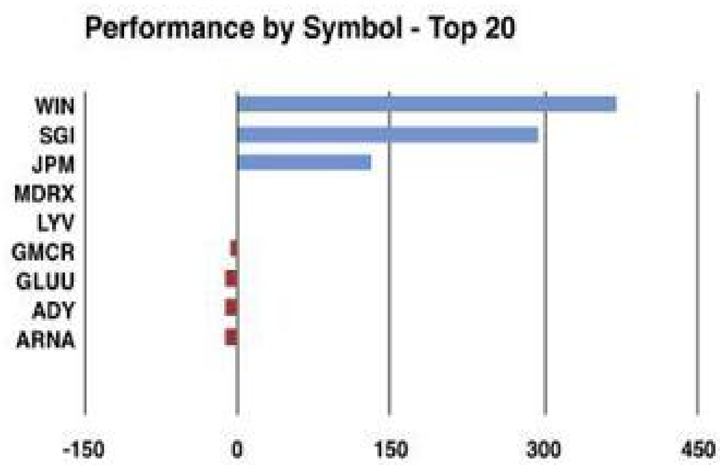


Figure 4.2

WIN was a stock where you could (erroneously) hit the bids like SGEN. It was thick and liquid. So I got huge in this play: 1,000–1,500 shares. Everyone on the desk missed the easy money from 10 to 9.40. I kept trading the ticks in that move, knowing I could hit the bids. I don't think anyone took advantage of this enough; we all thought it was overextended. It's always easier to "get back in" for the panic move when you see the stretch move and you can hit the bids and keep it tight. Either you sense the panic or you don't, and you can get out quickly and safely, especially on this stock. I also got long for the bounce at 9.60, sensing the difference in pattern change. I didn't really try to make a whole lot on this play, trading 400 shares and selling most of it before 9.85. But the trade was actually really easy, and it's not scary like most bounces because WIN was a clean, liquid stock.

Later in the day, everyone was consumed with playing the reversal play in WIN. I'll admit I was a little annoyed. I wasn't in the play because I didn't think the stock would move much. I thought most people were drinking the Kool-Aid on the play and chattering about how they're gonna be super, super big. I thought they were getting big because they could, not because the play was amazing. It was barely moving. I had to resist the urge to get in just because everyone else was in it. I ended up being right when after three hours in the play, it didn't get past 10.15, and everyone got stopped out at 10.09. I was trying to be consistent. This was not ROVI or HOLX or AET or SGEN or BIG—all similar (uptick rule, stops going down, reverses) plays but better, where I followed the desk. We've talked about using the desk's information better, and this is the balance I want to achieve. I made $500+ on ROVI last Friday following the desk, and I thanked everyone for it. But at the same time, I don't want to drink the Kool-Aid, and I don't want to feel like I'm in this competition to trade more size in a play. My intuition was telling me this was one of those spots, that the play wasn't that good, and I avoided it.

SGI was a stock at 52-week lows and held below $7, traded down to $6.10. I covered my risk too early for 5–6c on 200 shares, not trying to hit the home run, and kind of compensating for being 10c late in the play (the initial entry should have been the consolidation at 7.20), I got in 10c late. I'm kind of managing risk according to my emotions here, being overly concerned that SGI is another dud like KRO from yesterday, rather than trying to maximize the real trade. I did get back into the close at 6.45, even though the best entry was 6.70, and I took another $160 out of this trade. So that's a positive.

I also tacked on another $120 after-hours trading JPM. Tape was surprisingly easy and clean. I have to say, I have zero confidence reading the tape on large caps or big financials. I was actually hesitant to trade it at first because for a stock with 25 mil trading on average, it was a bit spready and illiquid, which made me not trust it. But that's actually better sometimes. There were no programs playing games. It traded below 40 and traded dollar to dollar, never found 40.01 again. I didn't get involved until 38.50–39ish. Only traded 200 shares at a time. I'm starting to learn from GMan in finding a balance between being too reactive vs. holding too long.

TO competes.

TO is such a world-class worker that he inspired me to write this blog post about doing detailed work to improve as a trader.

This New Trader Is Improving

Nov 17, 2011 | By Bella | Category: Mike Bellafiore's (Bella's) Blogs

I should facetiously title this post "The glamorous life of a managing partner." Yesterday Leo, who runs our active trader college program, and I drove eight hours back and forth to Bentley U, arrived back home at 1 a.m., woke up at 5 a.m. to scoot to the airport for a 6:50 a.m. flight to Vegas. We had a blast at Bentley and worth every driving mile. Some really wonderful conversations with young students with very bright futures. I am presenting at the Las Vegas Trader Expo on Friday. Which reminds me if you are in the area, please come by and say hi. On the flight out, I worked on my PowerPoint presentation and tried to make a dent in the two days of behind e-mails. Drinking lots of water to stay hydrated as I recognize travel, with a lack of proper sleep like this, can bring a nasty flu.

A fun part of the flight out west at 35K feet on my Gogo Internet connection is going over some trainees' reviews from yesterday's trading session. TO sent me his work, which fits nicely into my thesis I shared at Bentley U last night. TO showed up for training with a nice background of college trading. TO stays till 7 p.m. on most nights and does an all-star job of reviewing his work and focusing on getting better every day. He is a catalog perfect model for the aspiring young trader.

From TO’s review:

“Positives:

“Put myself in a position to win at the open by focusing on a big picture play that made sense to me—in this case, PEIX. I’ve come to realize that it no longer makes sense to favor a stock just because it has earnings...if the gap is too small, if the premarket volume is too light, if there’s a conference call, if I can’t make sense of the long-term story, or if the uptick rule just makes it too difficult to trade....It’s these details that make a CECO or a QCOM or an APOL...can’t count how many times I’ve invested time in an ordinary gap down, hoping there will be an unusual hold to give me a 100-1 R/R trade and it never comes and I just churn....

“My stock selection continues to be pretty good for those accumulation-breakout setups. VIT was a good one...execution still isn’t perfect, but if there was one long into the close that worked in the market downtick, it was this one.

“I was patient and mostly traded the stocks I prepared for from the morning.”

Traders often talk about their intuition. Well, you do not build intuition without screen time and purposeful practice. TO is now able to find the better gap setups because he has spent numerous opens fully prepared and carefully considering the best gaps to play. He could have walked in on most trading sessions in his first eight months, blindly listed to our a.m. meeting, not internalized a best setup on the open for him, and now be sitting without the skill to find the best stocks for him.

But now that is not the case. It was his pre-open thought preparation. It was his after-the-close review of the stocks he chose. It was quietly thinking about his trading. Hours of journaling. It was talking to some other traders and getting their feedback. And now he has improved.

My days are packed with learning meetings in Vegas. Should be a fun two days!

One of the great ways to improve as a trader is to think about your trading after the close. *The Talent Code*, written by Daniel Coyle, teaches us how our brains develop circuitry for our skills. Your brain, developing this wiring, makes no distinction between doing and just thinking about doing. TO is always thinking about his trading and building this connectivity in his trading brain—so much so that we used his post trading thought for a guest SMB blog post. Doing a daily PlayBook trade is one way he builds trading connectivity in his trading brain. You can do a PlayBook trade daily to just get it done. Or you can do a PlayBook trade with all your effort so you get the most out of each trading day. As you can see, TO, the gritty performer, gives his best effort each day, taking away as much knowledge as he can from each trading session.

Making Decisions How to Enter on MOS

Oct 3, 2011 | By smbcapital | Category: General Comments

A guest post from an SMB trainee, TO:

Bella has the entire floor working on their PlayBooks on a daily basis, to take in and internalize our best plays. Here is one of my plays on MOS last week:

1. Big Picture: The SPYs were in an intraday downtrend in the 116s and next support was 115.

2. Intraday Fundamentals: MOS was in play off earnings. Q1 EPS was 1.17 vs. estimates of 1.29. There was a slight gap down.

3. Technical Analysis: MOS was in a downtrend and consolidating at the lows near 55. The next support level was 54.50 (the six-month low) and after that, it would be 53. A new six-month low could have considerable downside.

4. Reading the Tape: There was some selling at 55.10, maybe a held offer.

MOS 2y D
D: 9/30/11
O: 53.14
H: 53.14
L: 48.49
C: 48.97
R: 4.65
Y:
Hi: 89.24
90
80
70
60
20 year
long term support at 53 level
6-month lows at 54.50
48.97
Volume: 18,900,122
<millions>
40
20
Aug
Oct
Dec
Feb
Apr
Jun
Aug

Figure 4.3

MOS 4d 1m
D: 9/30/11 7:59 PM
O: 48.82
H: 48.82
L: 48.82
C: 48.82
R: 0
Y:
short signals:
1) gap-down and downtrend off earnings
2) trading near 6-month lows
3) rangebound at the lows from 55 to 55.75
1st entry signal:
held offer at 55.10, tightening the stock at the lows
58
57.75
57.5
57.25
57
56.75
56.5
56.25
56
55.75
55.5
55.25
55
<thousands>
200
20
150
100
50
0
9:30
9:45
10:00
10:15

Figure 4.4

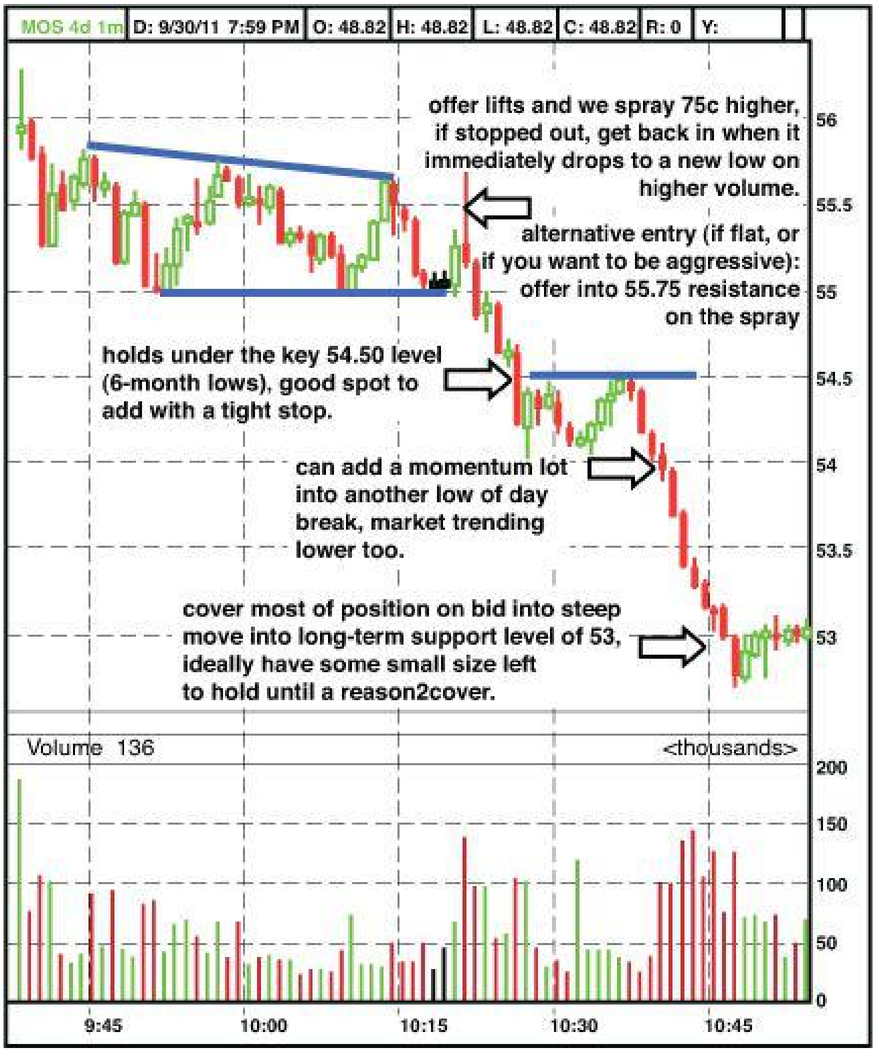


Figure 4.5

This is simple bread-and-butter strategy at SMB: getting short on weak stocks that are In Play. Trading with the market on a market stock is a bonus. I have many other PlayBook entries with very similar variables. However, in this scenario, I chose to watch the stock rather than jump in short when we print a new low by 1c. I'm not saying this isn't a good trade, as I very well could have missed out on profits for the times when MOS has a clean break away from 55. But there were two factors that made me wait:

1. I did not watch MOS trade at all until that point. I knew from premarket discussion with other traders that it can be a spready stock with some vicious algo trading.

2. It wasn't yet long-term broken until we were below 54.50, so there could be some accumulation between 54.50 and 55.

There was sideways price action which defines my risk, but was that really my true risk? Yes, if I'm just hitting the new low for a scalp. But if you're trying to trade a bigger picture idea (and that's generally what our PlayBook consists of), sometimes the real risk is having to maneuver in and out of a stock and getting stopped out on multiple tries before finally having a clear signal that your idea was right or wrong.

There are other subsets for a short entry that were still possible. We could hold under 55. We could break 54.50 and I could hit the new low there. And sometimes waiting for "something to happen" in a stock can really show you the true risk and give you the best entry. In this case, the "something to happen" was a not-so-nice (for early shorts) spray move to 55.75 after we printed a new low by 1c at 54.96.

Some background: One time I heard my mentor Sammy mutter on one of the stocks he had traded, "I should've got back in; the offer lifted but then came right back and held lower—that's an even better short." He was talking about a certain pattern where one should get back in if they got stopped out on a Held-Offer Play. So this PlayBook setup is about a particular squeeze-then-we-go-lower subset—the buy-the-new-low program steps in and squeezes out the weak shorts and (and buyers at support get excited) extra liquidity and better prices immediately attract sellers to return to the market and bring it lower. This is what happened little over a minute later on MOS. This time, I got off the sidelines and hit the bids.

MOS reached my target of 53, and I covered on the bid at 52.88. I did not crush this trade by adding size (alas, this is the downside of my cautious approach to this stock), so I went back and reviewed good spots to add size responsibly, something that Bella mandates we do on our best trades.

Timeline: The Friday before St. Patrick's Day in NYC TO is huddled with GMan and some newbies talking about an ITMN trade. GMan is walking through his thinking tick by tick and explaining how and where he got big.

“Yeah, but weren’t you concerned that the market was getting weaker, GMan?” asks TO. GMan, an original cast member of the Go Big or Go Home Trading Network, responds, “Nah, it was showing relative strength to the market.”

Do not jabber you want to be a better a trader. Do the work daily that determines your trading success. If you are not competing like TO daily, imagine how much better you can be as a trader if you did.

What does it mean to compete as a trader?

- Review your trading/trades.
- Think trading.
- Watch film of your trading.
- Talk trading.
- Review the trades of your mentor.
- Talk with your mentor about trading.
- Watch film of trading in a group.
- Archive a setup that made the most sense to you in your PlayBook.
- Keep a trading psychology notebook.
- Ask questions about the day to a trading partner.

Do you do this every day as a trader? TO does. If not, then you are not competing like he is.

TO does more.

TO Is One Step Ahead of You

One of the things that frustrates me about new traders is that too many expect someone like me to give them *all* the answers. Then they just do the work that I proscribe. That is not good enough. You need to do all the work that a good training firm demands *and* more. News flash: I do not have all the answers. Oh man, whatever you think of Coach Cal, go watch ESPN’s All-Access documentary on the 2012-13 Kentucky Wildcats. See how hard it is to compete at the highest level of D1 college basketball. For every possession, every screen, every pass you must compete. There are a lot of things that future elite performers just have to figure out. As a trader you have to be thinking of ways to take that trading base you learned from your mentors and make it stronger. Be one step ahead and do more. Like TO does.

After the close just after social media stalwart LinkedIn, stock symbol LNKD, went public, I marched the firm into our training room. Just before, there was pound 263, speaker on of me punching my phone.

“Carlton, get everyone in the training room right after the close,” I barked.

“No problem, Bella.”

Playing Coach Bella, I pounded the table for our traders to start watching social media stocks. They were hot right after the Facebook IPO was announced. For a few weeks, they were a basketful of opportunity. RENN, GRPN, LNKD, and ZNGA were some stocks that were moving. So what did TO do? He went back to his desk, logged onto FinViz, and started mapping out a basket of social media stocks to watch. He shared his watch list with me, which I then shared with the desk. Fast-forward four months, and I sat in the Marina Mandarin Singapore preparing my presentation, “Opportunities in U.S. Equities for the Asian Investor/Trader,” from that list that TO compiled.

Don’t wait for someone else to give you all the answers. You will never make it as a consistently profitable trader if you do. Find ways to improve your trading game.

When a sector gets hot, it’s time for you to develop a hobby of reading everything you can about that sector. I hear there is something they invented called the Internet for such information. Learn the Tier1, Tier2, Tier3, Tier4 (companies not in this hot sector pretending to be). Here is how they move. Tier1 stocks find a bid, then Tier2 shortly thereafter, then Tier3 shortly thereafter, and then Tier4. Patterns emerge with this hot sector. Learn these patterns and develop trades that make sense to you to exploit these opportunities. If you need to wait for someone else to develop a watch list of a hot sector for you, I can only advise for you to find another sport.

Here is that watch list TO created: http://bit.ly/xsjgoW (see Figure 4.6).

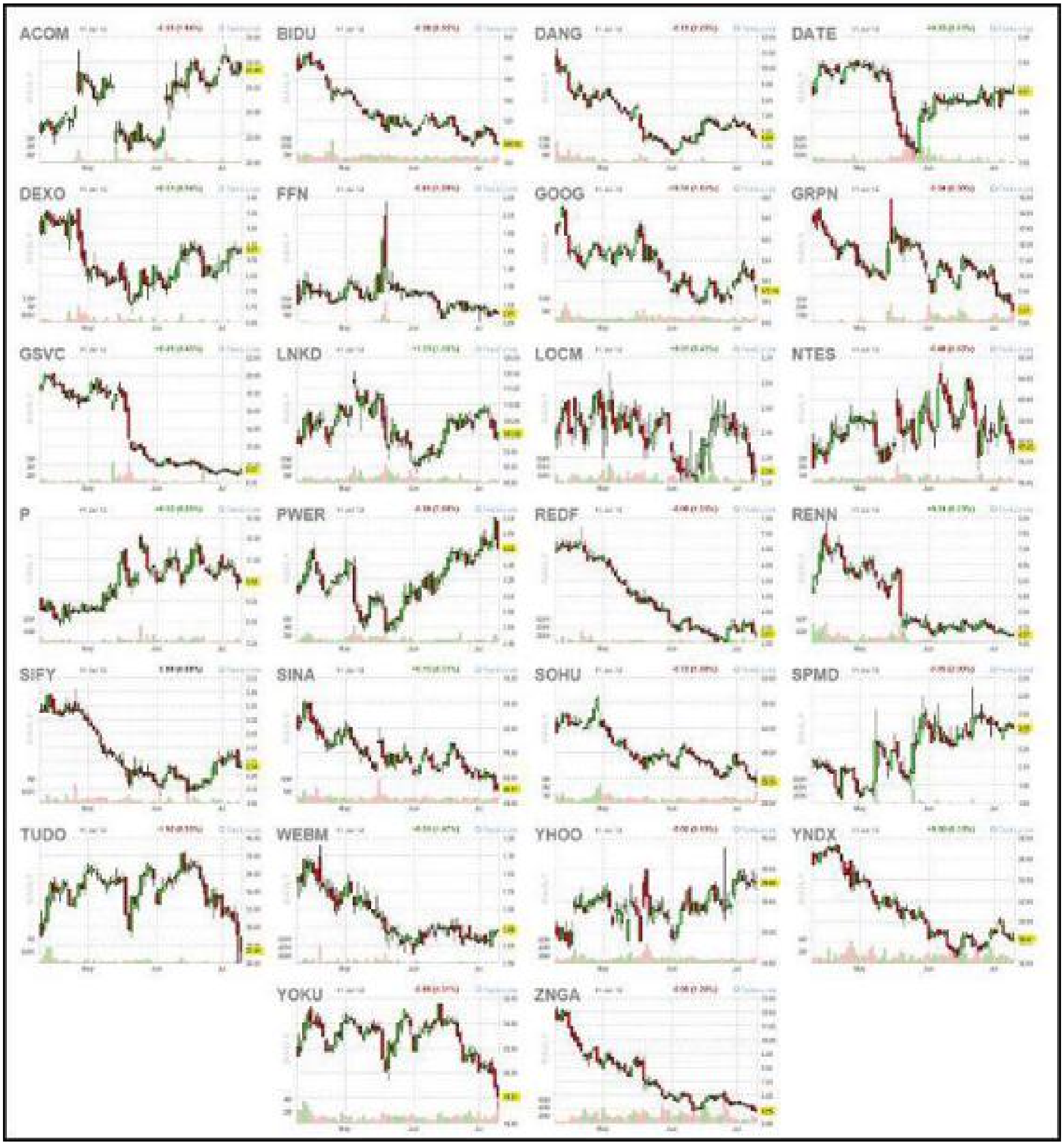


Figure 4.6

And TO does more.

TO Knows Tools Before the Rest

One afternoon, I start playing around with a beta version of Tradervue, created by my friend Greg Reineker. Tradervue helps new and developing traders review their work. Perhaps he was just being nice, but Greg credited

One Good Trade as his inspiration to build Tradervue. Greg is a super-talented technology coder and entrepreneur in the Colorado area, a.k.a. Brad Feld territory of Zynga investing fame and the awesome Tech Stars on Bloomberg TV.

Greg had sent me the first beta version of Tradervue. I wrote Steve this simple e-mail with the beta link: *Find out how we can work with him!* I mentioned Greg to my good friend Leigh Drogen, who created the game-changing Estimize, the first open financial estimates platform, and he confided, "I tried to get Greg to work with me on Estimize. If you can work with him, just do it." It's a great trading tool for you to check out.

So this is how awesome of a worker TO is. Steve and I are talking to Greg about working together. Greg releases his product. And on day two of the Tradervue launch, I pass by TO's desk and peek at what he is up to. Guess what that SOB is doing? The SOB is playing around with Tradervue. And he loves it. Further, as time goes by, TO exchanges e-mails with Greg and offers suggestions to improve the product, which is like getting input from David Beckham on free kicks.

Here is an example of how TO took our existing monthly review and incorporated Tradervue in only his first few months of trading (see Figures 4.7–4.13).


P&L Statistics
OPEN
MID-DAY
CLOSE
TOTAL
Gross P&L 1,465.91 1,844.36 882.47 4,192.74
Est. Net P&L 466.71 963.26 706.15 2,136.13
Volume 224,060 206,520 40,644 471,224
Executions 1,682 1,376 276 3,334
Ticket Avg 6.54 8.93 21.71 8.90
Pos Trades 432 386 84 902
Neg Trades 352 306 60 718
Trading Statistics
Win % 56%
Executions/hr 17.7
% Liq Added 25.2%
Avg Win/Share 0.11
Avg Loss/Share -0.06
Long P&L $2,422.44
Short P&L $1,770.30
Best/Worst Stock
Symbol P&L Tkt Avg
Best TSL 626.01 24.9
Worst CTRP -91.99 -12.8
Liquidity Statistics
Added Liq Removed Liq
BATY 40,119 89,036
ARCA 3,611 82,891
BATS 60,003 22,476
Holding Patterns
Total # Wins
Total Profit in $
% of Total Wins by $
.01-.09 543 3,103.64 28%
.10-.24 274 4,682.47 42%
.25+ 85 3,322.85 30%
Total # Losses
Total Loss in $
% of Total Losses by $
.01-.09 588 -3,774.13 55%
.10-.24 120 -2,704.11 39%
.25+ 10 -437.98 6%
5000
4000
3000
2000
1000
0
-1000
29-Jan
3-Feb
8-Feb
13-Feb
18-Feb
23-Feb
28-Feb
4-Mar
2/1/2012 to 2/29/2012

Figure 4.7

Total gain/loss:	$4,174.78	Largest gain:	$377.00 (show)
Average daily gain/loss	$208.74	Largest loss:	-$117.00 (show)
Average daily volume:	23531	Average per-share gain/loss:	$0.02
Number of winning trades:	183	Average hold time (winning trades):	44 minutes
Number losing trades:	248	Average hold time (losing trades):	17 minutes

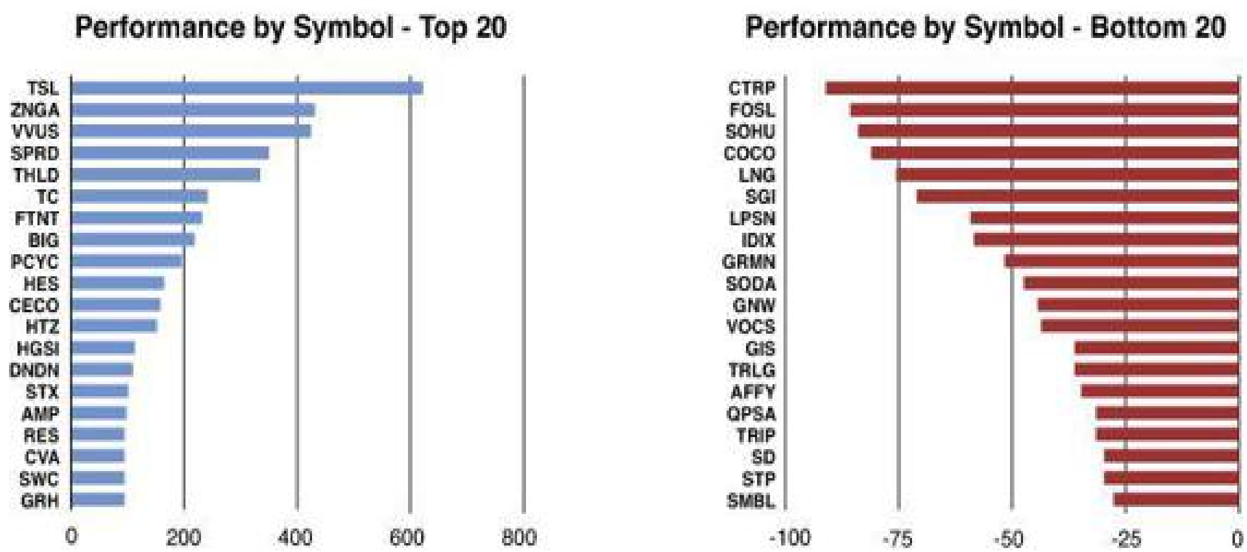


Figure 4.8


Trade Distribution by Day of Week
Mon
Tue
Wed
Thu
Fri
0
30
60
90
120
Performance by Day of Week
Mon
Tue
Wed
Thu
Fri
0
400
800
1,200
1,600
Trade Distribution by Hour of Day
6:00
7:00
8:00
9:00
10:00
11:00
12:00
13:00
14:00
15:00
16:00
17:00
18:00
19:00
20:00
0
30
60
90
120
Performance by Hour of Day
6:00
7:00
8:00
9:00
10:00
11:00
12:00
13:00
14:00
15:00
16:00
17:00
18:00
19:00
20:00
-500
0
500
1,000
1,500

Figure 4.9

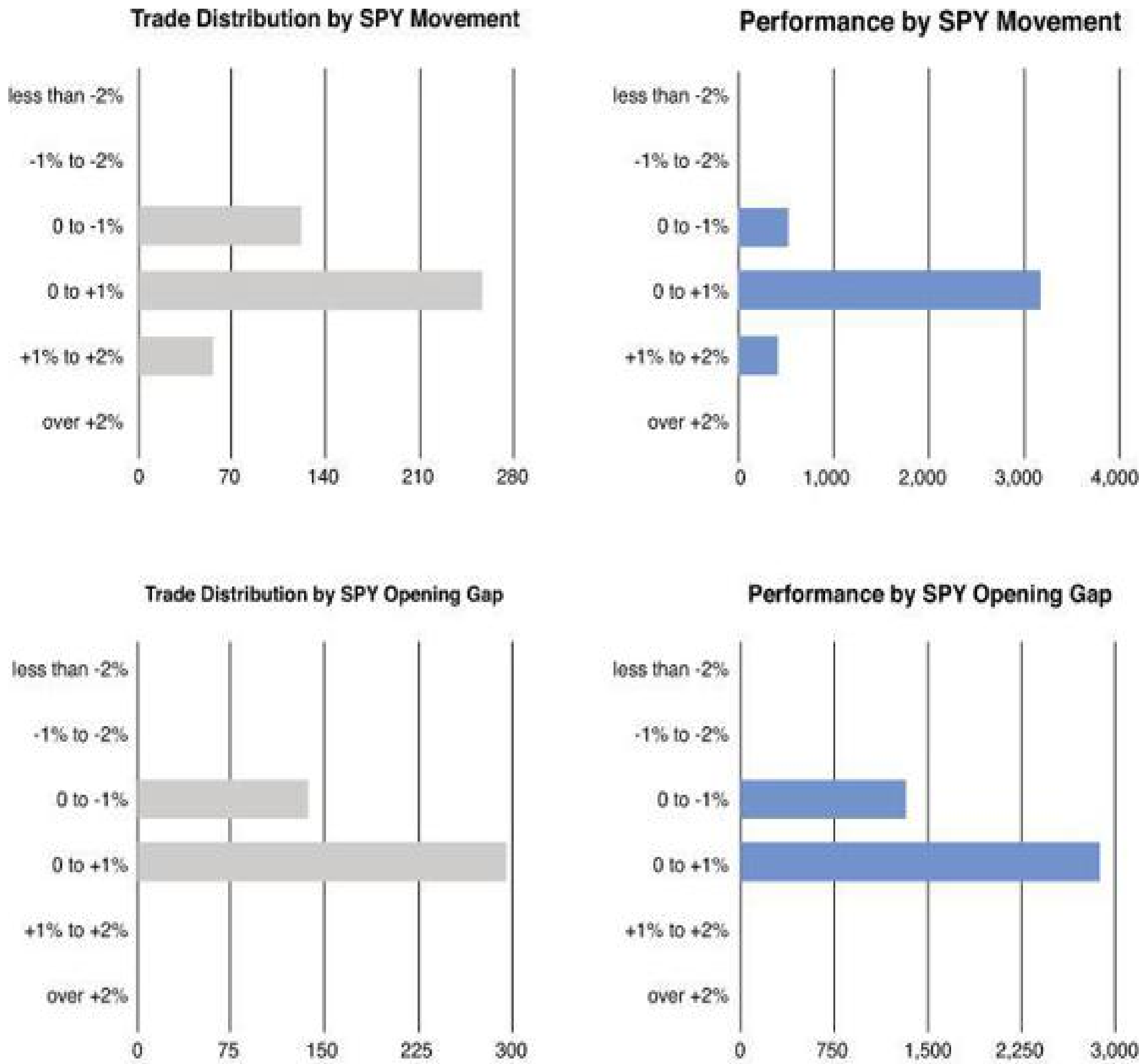

Trade Distribution by SPY Movement
less than -2%
-1% to -2%
0 to -1%
0 to +1%
+1% to +2%
over +2%
0
70
140
210
280
Performance by SPY Movement
less than -2%
-1% to -2%
0 to -1%
0 to +1%
+1% to +2%
over +2%
0
1,000
2,000
3,000
4,000
Trade Distribution by SPY Opening Gap
less than -2%
-1% to -2%
0 to -1%
0 to +1%
+1% to +2%
over +2%
0
75
150
225
300
Performance by SPY Opening Gap
less than -2%
-1% to -2%
0 to -1%
0 to +1%
+1% to +2%
over +2%
0
750
1,500
2,250
3,000

Figure 4.10

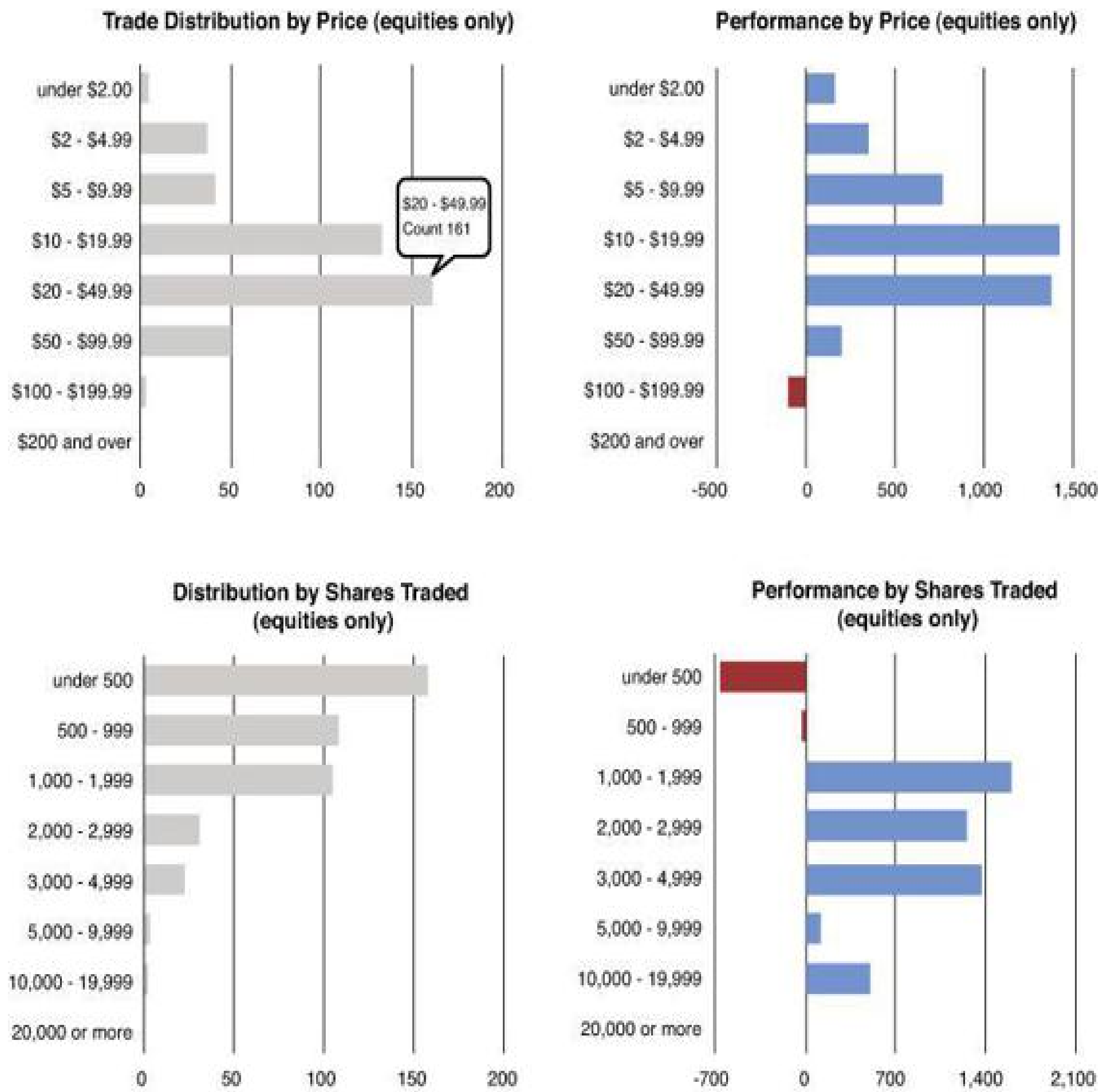

Trade Distribution by Price (equities only)
under $2.00
$2 - $4.99
$5 - $9.99
$10 - $19.99
$20 - $49.99
$50 - $99.99
$100 - $199.99
$200 and over
$20 - $49.99
Count 161
0
50
100
150
200
Performance by Price (equities only)
under $2.00
$2 - $4.99
$5 - $9.99
$10 - $19.99
$20 - $49.99
$50 - $99.99
$100 - $199.99
$200 and over
-500
0
500
1,000
1,500
Distribution by Shares Traded (equities only)
under 500
500 - 999
1,000 - 1,999
2,000 - 2,999
3,000 - 4,999
5,000 - 9,999
10,000 - 19,999
20,000 or more
0
50
100
150
200
Performance by Shares Traded (equities only)
under 500
500 - 999
1,000 - 1,999
2,000 - 2,999
3,000 - 4,999
5,000 - 9,999
10,000 - 19,999
20,000 or more
-700
0
700
1,400
2,100

Figure 4.11

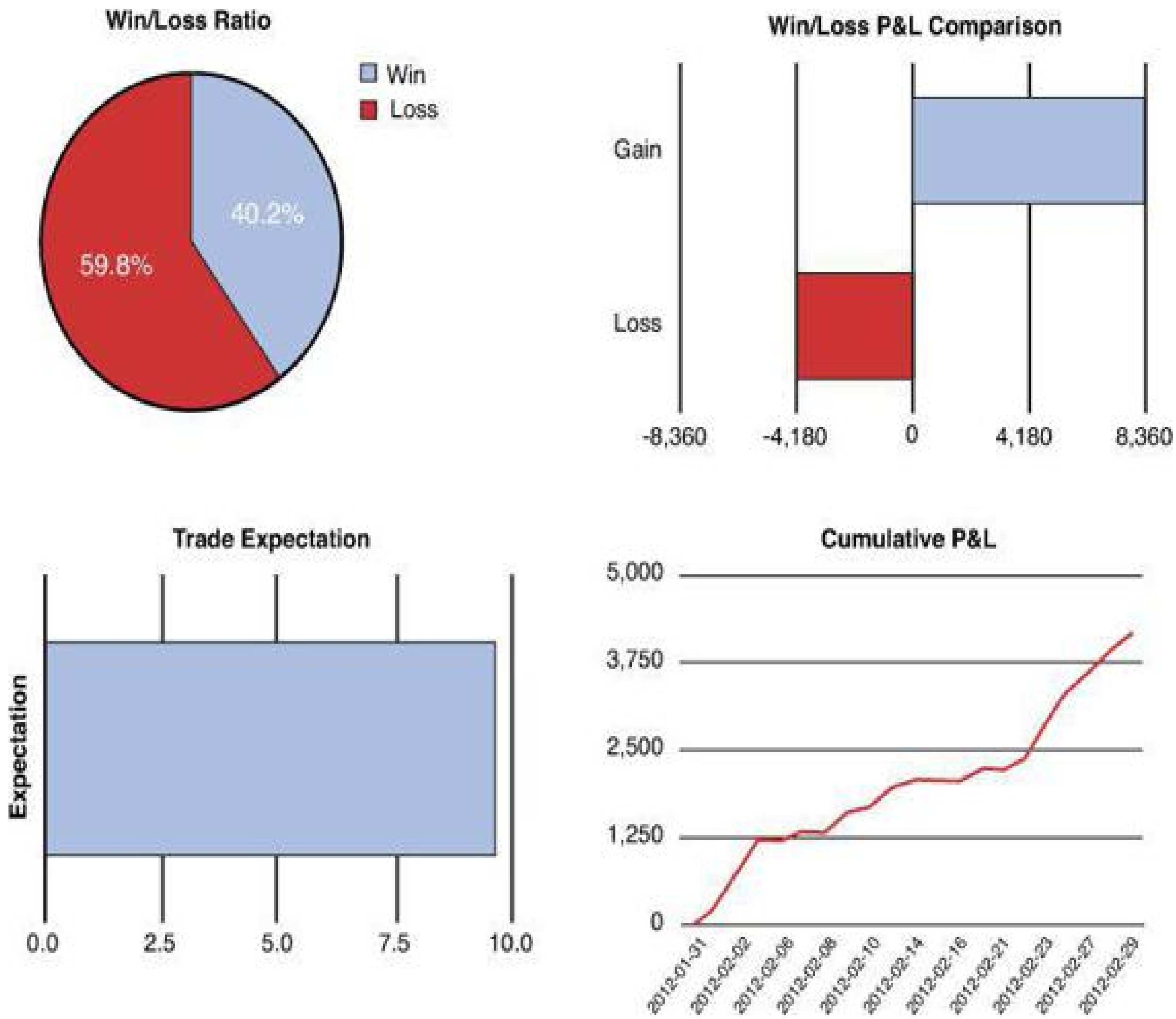


Figure 4.12

Worst trades sorted by PnL:

Date	Symbol	Volume	Executions	P&L
2012-02-29	WUS	1600	11	$-117.00
2012-02-03	GILD	3000	27	$-78.00
2012-02-06	SOHU	400	3	$-64.00
2012-02-14	LPSN	800	3	$-60.00
2012-02-15	ZNGA	3200	19	$-58.00
2012-02-08	SGI	1200	9	$-53.00
2012-02-15	WTW	400	3	$-53.00
2012-02-22	GRMN	400	3	$-52.00
2012-02-16	WUS	2000	20	$-51.50
2012-02-17	GILD	400	3	$-51.00
2012-02-28	LNG	1200	6	$-51.00
2012-02-15	FOSL	200	2	$-50.00

Date	Symbol	Volume	Executions	P&L
2012-02-02	AFFY	600	2	$-48.00
2012-02-06	SODA	600	4	$-48.00
2012-02-01	COCO	2600	10	$-46.00
2012-02-06	HCA	600	5	$-46.00
2012-02-21	GNW	2000	5	$-44.98
2012-02-27	WUS	1000	9	$-44.00
2012-02-29	WUS	4000	25	$-44.00
2012-02-29	CTRP	800	3	$-44.00
2012-02-29	VOCS	400	3	$-44.00
2012-02-17	TSL	2600	15	$-43.00
2012-02-28	WUS	1000	8	$-43.00

Figure 4.13

Other stats:

ECN fees: 1.70 per ticket

Net positive days: 13/20 (65%)

Gross positive days: 17/20 (85%)

Net PnL: $2048.82

Daily avg volume: 23,531

Net positive tickers: 71/184 (38.5%)

Positives:

1. Trading certain sectors—biotech, social media, and solar—accounted for a large chunk of my revenue stream. TSL, THLD, RENN, ZNGA, and VVUS are five of my best stocks. I’ve learned a lot about what drives these companies, who participates in their market, how interest flows in and out, and how it’s visually represented in price and volume.

2. Not playing tug-a-war with any given stock; no stocks beyond –100 in gross.

3. Increased my ticket average month to month by almost 3.3 points (5.62 to 8.90)—substantial improvement.

4. Increased daily average volume by about 3500 shares (20,000 to 23,500)—probably not as much of an increase as I'd like considering how much I improved my efficiency above.

5. Positive every hour of the day.

6. Rarely gross negative, cumulatively, my three gross negative days accounted for –$35 gross. When taking this into consideration, I'm probably not taking nearly enough risk on a day-to-day basis.

Negatives:

1. Win ratio is still too low; 40 percent just doesn't psychologically bode well with me. It's not the most important stat though. I attribute this to a lot of feelers and scratch trades where I took a very small loss.

2. Too many negative stocks; 38.5 percent rate. Suggest I'm in too many plays where I don't have enough of an edge, either not moving enough or moving too erratically instead of cleanly.

3. Went through a dry spell for two weeks in middle of February where I was net flat. There was some inconsistent trading here.

4. I pretty much don't have any notable big chops on a trade initiated after 1 p.m....I need to alter my PlayBook for this time period and reduce the volume I'm doing in this time period relative to other time periods.

5. ECN fees were just terrible this month; 1.70, worst since I've started trading.

What to improve on:

1. Trading high price and large spread stocks—stocks such as WTW, FOSL, SOHU, SODA, GRMN, CTRP—these were my biggest losers or my most frustrating trades. I traded them when they were in play, and I do think there was an edge to be had trading these stocks, but execution and trade management were very difficult for me.

2. Risk aversion on the open—I was passing up too many good plays on the open during the two middle weeks of February where my performance dropped off a bit. I overcompensated by taking the risk during lower opportunity times of day. It makes no sense to allocate risk like this as an intraday trader. I should be willing to lose the same amount of money when things are moving on the open. In general, all my losing streaks (4–5+ losing trades in a row) almost always come after 1 p.m., not the open, so there's no proof that I'm even experiencing a lot of negative variance on the open. (The possibility that a few bad trades can push me close to my stop on the day.)

3. Open drive play during earnings season—I don't think I made enough on these patterns, relates to the above issue. Will be looking to add these to my play for next earnings season—numerous trades on VVUS are a good template to start with.

4. Dealing with my emotions—rough stretch in middle of February where I felt I was underperforming, probably exacerbated some losses by staying at the desk while on the tilt, forcing trades.

5. Trading with the market—specifically this market that is long-term strong but occasionally weak intraday—too much money lost on long exposure when the market was going down, trying to force second day support plays and relative strength plays while the market was going down because I missed most of the shorts. I think I adjusted for this well.

6. Profit-taking short setups—usually my bread-and-butter setups on the open. I usually have the right sense of timing, but I don't think I take enough out of these plays. VVUS on the move from 24 to 22.50 is a good example of a trade where I had the right entries but chickened out of the play early and didn't take enough. I want to improve on trade management here. The key is knowing the difference between the ticks on a stock with a lot of upside momentum undergoing some profit taking and a weak stock. There will be a transition where chasers or late comers have to see the stock is done and then shorts take control. There's a lot of battling on the ticks. It's important for me to understand this when I'm in the trade and not get out of the play too early on some momentary strength—they're just going to have to control the stock and go all the way to take you out of the position.

7. Better win rate; 38.5 percent net positivity on tickers and 40 percent win rate on ideas don't cut it for me. These aren't the most important stats, but I'd like to have a better baseline—too low means I'm overtrading or overextending myself into too many positions.

8. Most important: Trading with more size, increasing my $-risk per idea on the open, increasing my tier sizes, getting to Tier2 more often, taking more risk in general as a percentage of my daily stop. I should lose more money on my subpar days (usually it takes an obscenely low win rate to come even close to my daily stop), just as a function of increasing risk across the board. I'm in the process of planning how I will do this on a day-to-day basis; I think this will be divided into weekly goals.

Goals for March:

1. Ticket average of 10+

2. Position sizing—get to 700/800 shares Tier2 more often on my best plays

3. First $1,000 gross day

4. 80 percent net positive on daily basis

5. Gross $5,000+

I think I'm going to have an "add 100 shares" rule. Any time I'm in a position with at least 300 shares and I decide that's how much I'm going to risk, I'm going to add another 100 shares just on top of it. It's like a +1 rule to build the habit of a higher tier size, but incrementally, and not in any plays where it could double my risk (like if I'm trading SINA on the open with 100 shares).

Overall, this month represented a real positive step in the right direction. After an inconsistent December and January where it was hard to string together back-to-back positive days, this month felt good. It represents my highest gross/net to date, so I'm happy with my progress so far. Lots of valuable screen time generated from my second earnings season, augmented by a stacked FDA calendar and Facebook's IPO announcement—good confidence builder to precede my effort in trying to trade with more size.

Then TO took the SMB daily review that Shark developed from work by GMan and me and incorporated Tradervue to make our daily review even more powerful. He reached out and made a new, awesome product more awesome. Then he took a pretty damned good daily review process and made it better, helping his deskmates and himself improve even more. You want to know why you want to sit on a prop desk? To sit next to a TO.

He Already Had a Psychology Coach

I reached out to TO and asked whether he wanted to see one of the psychology coaches who work with our traders. I noticed from his daily reviews and private conversations that he could be a little too hard on himself. Also, he started to write in his daily trading reviews, which I reviewed, that he got mentally exhausted at times. This reminded me of one of the brightest traders I have ever trained, Dr. Momentum, from *One Good Trade*. He had this same issue at the start of his trading career and worked with Dr. Brett Steenbarger, legendary trading psychologist, to improve. Deservedly, Dr. Steenbarger left us and his top hedge fund clients for a gig at this hedge fund you might have heard of called the Tudor Group and its approximately $11 billion of assets under management.

But not to be outdone, today we work with Dr. Jonathan Katz, who has worked with top hedge funds and professional sports teams such as the New York Rangers; we also work with Dr. Andrew Menaker, who has worked with major banks and even the U.S. Navy. Upon my suggestion of his working with a coach, TO promptly sent a response: "I already work with a sports psychologist, though he's not a 'trading psychologist' per se. We do exercises on a biofeedback machine every week. It’s pretty neat.” Should I have been surprised?

The Failure Rate of a Prop Trader

Let me pause here and remind you that not one of these TO anecdotes is later than 18 months into his trading career. Traders do not even get really good until Year 3. We may look back at this book in ten years and see the documenting of the start of a future star trader. Having said that, this book is not Trader Disneyland. Even the future stars struggle.

After a solid day by our desk, I pinged our floor manager, Carlton, to have some of the guys who made chops intraday discuss their trades in our training room. After the close, Carlton found me.

“Bella, do you want to be in the room when they discuss their trades?” asked Carlton.

“What the hell do I need to be in the room for? TO made two points on the YOKU trade, and I made 50 cents. What do they need me for?”

Later that evening, I received a near-despondent e-mail from TO, pissed at himself for not making more in this trade.

One of the most popular blog posts I ever wrote was *The Failure Rate of a Professional Trader.* After I wrote it, our former head of sales came storming into my office cautioning me not to be so honest. Let’s double down with that openness.

So TO has done just about everything you could ask from a developing trader. He even traded in college. So if you work as hard as TO, you are destined to become the next great trader right? Let’s get TO’s opinion of his chances of success:

> It’s not blind optimism that gets me through the doubt. It’s honest introspection and realism. No matter how hard I work, how responsible my risk management is, there’s a good chance the markets are just too hard and the cost of business becomes too high for me to keep playing. In that case, I will just go home and trade my own money. And if I go broke, I will call up my best friend to loan me $5K (and he gladly would) to trade. I’m going to trade anyway—this is what I remind myself when I start to dwell

> on the possibility of failure. You have to be a little crazy to want to be a prop trader.

Oh, so you do not come to Wall Street, join a firm, and instantly become a millionaire?

One Day in the Life of a Pro Trader

TO has been challenged mentally by the market to become a pro trader. He has had some bad days.

I received this e-mail from TO, disappointed after a tough trading session. I chuckled when I read it. Man, have I felt like TO like every year of my career:

> I really got my a** handed to me the last two days. I think they are my two worst trading days in terms of net P&L. I basically gave back all of Wednesday's gains (my best day), and some extra change to boot. Not to be over melodramatic but these two days really produced a lot of anguish. It's not so much the $$ amount but the sense of positive progress and consistency being "squandered away." Now I'm left wondering if I can meet my goals for the month and whether I have to, again, take a step back in my efforts to trade more size. I'm wondering if I have to be more humble with what I can do in this market.

Trading can be one step forward and then two steps backward. Then a few steps forward. There is never going to be a time when you are not going to run into a wall of progress impeded. So now from this psychological doubt and disappointment can you find a way to make new progress? That is the game. That is the challenge. That is the world of a veteran pro trader.

I feel as though I will never make money again.

TO was also the sender of this e-mail of frustration:

> I don't know what's wrong with me the last three days, but I am not trading up to par. It's much more eye-opening when the market is actually decent and others around me are making money. I'm disappointed (to say the least) by today, but I didn't do anything fundamentally wrong at first. I even made money initially.
>
> I don't know how to explain it, but from the opening bell, I was very unhappy before making even one trade. I was probably a 1/10 in confidence. I had no go-to idea, so I was thinking negatively:

> "I'm probably going to be stuck in all the wrong $hit again. Watch me start off all red in my first five stocks. I just don't get trading."
>
> I missed just about every money-making trade for no other reason than just not believing it will work and this bled past 10 a.m. too. Then when they all worked (CAR, AEM, CF—which I was the one to alert on the VTF, GM), I couldn't stop beating myself up and questioning everything I was doing. I took a one-hour break from the desk, then came back to make random 100 share piker trades...but eventually got into trouble trading a breaking news stock in VVUS and turned my day gross negative.
>
> These aren't my worst results, but I feel embarrassed to be negative today. If I sat down and analyzed the patterns that I saw, I could probably come up with objective answers why A was a trade and B wasn't, but I don't know if that's the big problem for me right now. It's doing it in real time and not getting stuck in BS worries like "Well, I just brought it up and now it's 10c away from the ideal entry; I can't feel comfortable in this, and it's probably a worse pattern if it actually gets back to my offer." Maybe I'm just too slow on top of being too scared. My psyche is just a train wreck right now, and I'll be thankful tomorrow (or at any point) if I just have fun trading at the open again, regardless of results.

I responded to TO via my iPad from Singapore.

Before I share my response to him, I must add that I have had these same thoughts. I have had them every quarter that I have traded. I will have them again.

Sometimes you feel the markets are too hard. That you just do not get it as a trader. And then there are streaks where you feel you cannot do anything but be positive. The truth is those streaks end, as well. You are not as bad as you think when you feel you cannot make money. You are not as good as you think when you believe you will never have another losing day.

Here are a few of my comments (some made to TO) in response to his preceding e-mail:

> Do not concern yourself with how anyone else is doing. Ever. The bank takes your trading check. It is does not cash your trading partner's. This is a journey about your trading. Do not worry about anyone else, or anyone else's trades.

Second, you ought to create a roadmap for the open. But you cannot predict how you will make money. You do not want to put pressure on yourself that you must be able to predict where and how you will make money. Trade with an open mind. Have some ideas on how you might make money, but then let the market confirm your bias.

And be ready for easy plays to present themselves. Often, an easy trade you never knew was coming enters and can make your day. Remember MHS and ESRX from recently? But you must be open to it coming to capitalize.

You will have bad streaks. It is the life of a trader. Keep doing the work the market requires to improve every day. Keep searching for the patterns that make the most sense to you. Do not be so hard on yourself when you are just a little off. There is a fine line between crushing it and underperforming. You are not selling iPads at an Apple store here.

When you are feeling like the trader above, make the game easier. Lower your tier size. Trade your best setups. Trade your best time frames. And just put up a positive number. And then repeat the next day. A lack of confidence can infect every future trade. Rebuild it. Soon you will forget you ever were in a trading bad streak.

Finally, channel the negative feelings above into energy to improve. Embrace the pain. Use it to rip through charts so you never feel like this again. Use it to archive your best patterns so you never feel like this again.

Bella

So look, even if you have quick trading success like TO, you will doubt, worry, and consider failure. Welcome to the highly competitive world of a professional proprietary trader.

The Standard Is: How Good Can You Be?

TO keeps working on his PlayBook that melds his talents and interests with his skill. Admittedly, I would prefer that he followed the trend more, but he is most comfortable, in his own words, as a “contrarian”. This and his trading past pulls him toward Fade Trades. My job as a coach is to help him be as good as he can be not meld him into my trading system. I serve him, he does not serve my system. I frown at those firms who teach everyone who walks in the door to intraday momentum trade, historically the most successful intraday trading style. As long as TO is making fundamentally proper fade trades, he is good at them, and this is not detracting from setups of more opportunity for him, then I help a trader refine *his* strategy.

When a trader starts, I feel strongly that most should begin with the Second Day Play, and then the Trend Trend Trade (T3), and then the Bullish Flag Trade. These are the three easiest trades to start with as a new and developing trader. Become proficient and profitable in one trade, demonstrate that to your mentor, and then and only then should the new and developing trader move to the next trade. One trade at a time, traded profitably and proficiently before the next. But traders come in all stripes, so with TO, we expose him to these easiest trades, and then work with him to improve the trades that his trading brain find most interesting (in this case, Fade Trades).

TO loves to fade and he is good at it. Later we will see GMan force fade trades that were harming his P&L. Also we will take a peek at South African traders who were attempting fade trades when the fundamentally proper trade was to trade the trend. None of this is the case with TO. He has a history of working at his successful game as a fade trader, while also following the trend when that is the fundamentally best trade. The Fade Trade is just a part of his PlayBook, but a section that he naturally finds more interesting. So my job is to help him build the best PlayBook for him. That means helping him craft his best PlayBook of Fade Trades. Let me share two anecdotes, a morning breakfast, and an e-mail exchange that demonstrate how I worked with TO on his fade trading so that we can learn how good *he* can be.

The Breakfast of Fade Trades

On a Saturday morning, we met on the Upper West Side of Manhattan for brunch at Lenny’s, a popular eatery in my NYC neighborhood. I ordered a whole wheat bagel with tofu cream cheese, and, well, he some pastrami heart attack special. TO sat underweight and double layered on an unseasonably warm winter day, as we got around to trading talk after hack analyzing the NBA like a bunch of sports talk show callers from Piscataway.

“TO, is there really a rivalry between the Clippers and the Lakers?” I asked.

“I mean not really for Lakers fans. Maybe for Clippers fans.”

Stuff like that as an unusual proportion of twin carriages, egg white wraps, and Patagonia fleece jackets pass us by.

The day before, after the close, TO had asked to meet in my office for a talk, but I was unavailable. I was on one of those conference calls from managing partner hell. Oh, do I miss the days of just trading and coaching my desk! Heck, I miss the days of just trading, heading to the gym, playing two hours of basketball every night at the Reebok Sports Club, and weighing 20 pounds less (okay, 25; okay, 30). Gathering my things after the bell and walking through Central Park from the East Side to the West Side of Manhattan, in time for a 4:30 p.m. run till dinner. Not anymore. SMB and all its entities do not run themselves.

So we met for breakfast on a trading off-day. I was in And1 black sweats, a white tee, a gray Old Navy pullover hoodie (Mark Zuckerberg style), with a laptop powered by a Verizon hot spot, the *New York Post* and the *New York Daily News* situated smartly on my breakfast table, sitting with this potentially next great SMB trader. (I should also mention that TO made $20,000 in online poker before he was 18. He wasn’t supposed to be playing, obviously, but who cares?)

TO had made a Fade Trade for which he wanted my input. A Fade Trade means to take a position against the trend of the stock. So if a stock is trading up, you get short. If a stock is trading down, you get long. TO wanted to discuss a specific type of Fade Trade; we say a subset of a Fade Trade. Here goes: A stock gaps up; it quickly trades up 80+ cents without any discernible buying support and slows on the tape. TO wanted to fade this setup. TO japed that he wanted to make more plays like this. I like him thinking about the plays that make sense to him, although I am not a huge fan of this setup overall.

Sipping Diet Lemon Snapple Iced Tea in a large cup of ice, back against one of those orange plastic cushion backstops, I asked whether he had archived these setups in his PlayBook. No. These were just the loose thoughts of a new trader who needed more nuance. Time for me to encourage a higher standard of trading thought. I shared that I am not a huge fan of this trade. Yes, these setups could be a part of a PlayBook, but there are better fade/reversal patterns to make. We discussed the gap-and-go on low volume with a flag that fails. "You can make your month with plays like that," I encouraged. "But limit, limit, limit your PlayBook to the very best plays," I counseled.

During our breakfast trading summit, I had to communicate that there was a lack of quality thought with his fade play, while not diminishing this new trader's confidence.

I asked, "Is there a way you determine if a stock has gapped up too much?"

He should.

I asked, "Is there a way to set alerts for these gaps and then low-volume spikes near long-term resistance levels?"

There was and he hadn't thought of this.

I can see the patterns for this trade in my mind that are worth his attention. Like our brains search for a lost memory, my trading mind searches for profitable fade patterns for this young trader to master and me to encourage. His mind cannot yet see them. The natural interest is there for fade trading, but the domain knowledge for the best of these kind is not. I needed to feed his trading brain with the best of the fade plays. And how about the spikes that are especially hyperbolic? How about limiting his new Fade Trade to those?

For me, the trade to make is the gap that makes no sense to you, combined with an especially hyperbolic low-volume drive on the open that pauses on the tape near real long-term resistance. I encouraged alerts set for these plays. I persuaded TO to limit his new Fade Trade to these variables and suggest spending more time internalizing this reversal pattern—the gap with an overextended open that flags and fails. Here is where the real money is.

TO takes my domain knowledge on Fade Trades and then considers whether they will work for him.

And after that we went back to talking about his Lakers.

Three Fade Trades for You to Master

After trade discussions like ours at Saturday breakfast, there are follow-up questions on fade trading, like in an e-mail that led to this blog post that follows. My response reveals three Fade Trades that you might consider for your PlayBook and again highlights the importance of each trader finding the patterns that work best for him or her.

Would You Make This Fade Trade? $APOL

Jan 10, 2013 | By Bella |

I received this trader question via e-mail on fade trading. Here goes:

After the (well-known trader coach visit) meeting, I've come to realize I don't ask enough questions from the people who are more experienced than I am. Today was a dull day, lost about $150, I don't have a lot of talk about except this APOL trade.

I'd like to know what you think about how I traded this APOL trade:

My idea was to get long on any kind of failure test of the 52 week lows and position myself for a short-covering bounce. The 52 week low was 18.36. The premarket low was 18.62. The stock made an opening low of 18.52, which I thought was pretty marginal. It didn't really stick and hold lower.

What do you think is the better approach, getting a price close to 18.50 (fading the down move, since the tape is telling me they can't really stick) and trying to stay in the trade all day against that inflection, because that's the real big picture level where I'm wrong, or being "safe," waiting for more confirmation, trying to trade with the momentum on my side? I kind of did the latter. I got into the trade at 18.85, 19, and some lots above 19, and little did I know, I walked into a battleground that touched a lot of prices. Above-below, lots of quick short-covering bursts that failed to hold, overly aggressive low offers...but generally ticking my favor. I don't like establishing my position in spots where my intuition tells me it's 50-50, but I didn't want to miss a trade I prepared for either. At some point, I just felt like my price average (19.03) was too high for me to give it to 18.50, it became a pseudo-"hold higher" trade rather than a support trade, and after two failures to hold above 19.25, I just hit it below 18.90. My active trading (getting bigger/getting lighter) was awful on the stock to boot; I kept killing my core average.

I also think this trade would've been a lot better if the stock didn't put in an opening high at 19.48 in the first 10 minutes...that just makes the psychology of the play much different than, say, if there was only one move on the open—down—and the offers just tried to mow it down, but it couldn't get below 18.50. You could argue this is too crowded/hard a stock and I shouldn't focus my time on it.

I don't think there's a right/wrong answer (I'm positive that this will be your response, in that there's only the right way for *me* to trade it), but I'd like a compass so that I have more direction in evaluating my execution. Any thoughts?

@mikebellafiore

I have been a fade trader and a trend trader during my trading career. It is too stressful for me to fade trade now. This doesn't fit with my present lifestyle. And we do teach many new traders globally for whom it is much easier to start as a trend trader. But at this point you have more experience and fade trading is appropriate.

There is no best way to trade this set up. There is the best way *for you*. You were correct. Having said that, there are three intraday patterns that I see for a Fade Trade:

1. The puke

You see a steep down move on heavy volume that looks to you like the end of the move. Some call this capitulation. The play here is to get long with a stop below the low and hold for a real up move. This is only for advanced traders.

2. The *clear* bottom from the tape

I like this trade for an intraday, active, superior tape reading fade trader. I would caution that you wait for the tape to *clearly* show you something different. Wait to see clearly that the tape is different and that the stock clearly is not going down. This will be the key for this trade. Having the tape reading skills and discipline to see that the tape is clearly different and clearly not going down anymore. And passing on this setup when the tape is kind of indicating the stock may be done going down. This is a very important distinction, one that you must make to trade this pattern successfully.

3. The Reversal Trade after confirmation

I love this trade. This to me is where the most money is for most traders. Now the downtrend is broken, now the stock is holding above the intraday downtrend, we have confirmation of a potential reversal. What is most important here is a higher confidence level in our trade. Therefore, you can get bigger. In fact, to play this trade properly, you have to get bigger when the trade starts to work. What is terrific about your trade here is you add through 19. This is spot on. What is awesome about your trading here is your hold for the *real move*. You cannot be a successful fade trader without capturing big chunks of moves when you are correct.

TO's competitiveness has allowed him to build skill so that he can use another important indicator for each of his trades: intuition.

Building Intuition

Arggh is the topic of trading intuition misunderstood. Newbs think they are born with a “feel” for the markets and trade accordingly. Yeah, so it doesn’t work like that. Intuition is your trading brain telling you when to buy and sell. For the experienced trader, this is an invaluable indicator. One to be listened to and honed. If you are a newb, tell that voice in your head to, as we say on Twitter, STFU. It’s like a crazy old uncle you want to avoid at a family picnic. You will develop intuition through screen time, experience, and trader thought. Like TO did. There is no other way it gets developed.

When the Facebook IPO came to the market in May 2012, it failed miserably. Its IPO open price of 38 did not hold. During a discussion after the close, TO critiqued our desk during a trade review for not being prepared to short social media stocks. He made his points clearer in this e-mail:

> I really think the desk blew an opportunity not getting short social media plays. We all know we can only make money if FB goes up, but we should be prepared if the IPO sucks...and that’s where you go, to stocks like RENN and ZNGA...especially when they show their relative weakness right off the bat. They were *crushing* ZNGA in the premarket, flashing huge size on low offers. There are so many trapped longs who were long for no reason other than for today. Hey, I wanted the IPO to be good, too, but there’s no reason not to think of ideas to make money off of if it sucks.
>
> I am beating myself up so much for not being the one to make a massive amount of money shorting these things. I have a contrarian radar in my head and for weeks, I avoided the social media sympathy plays because the price action was so bad. (I’m actually being contrarian by following the trend, how ironic.) Then GMan banks huge on FFN, and I can’t help but drink the Kool-Aid as well. I lost close to a grand on my personal account by getting long a few of them premarket on gap-ups. (Trading small! I just let them all trade against me because I was stuck thinking “wait, WTF is going on?”) We were all drinking the Kool-Aid on the open, trying to get long ZNGA with a very wide stop, thinking, “Wait, this makes zero sense; how much can this really go down?” I mean, if you were paying attention, you could have seen this coming for weeks...ZNGA was making new lows into the IPO

> date...nobody wants this piece of $hit. Even a leader such as LNKD looked very weak. Didn't follow my intuition. I'm not time-machine trading; the foresight was there, but I didn't listen. That's why you have got to trade price action and not blind hope. If anyone should've nailed it, it should've been me. Hyped-up sector, speculative stocks, contrarianism—those are my roots as a trader.
>
> Today was classic Wall Street "buy the rumor, sell the news," with a different twist. The only reason anyone had to buy a garbage company like RENN was for *this day,* and the IPO can't hold its opening price and traded dangerously close to getting below the IPO price as well. None of these companies had the right type of chart coming into Friday, save for FFN.
>
> Anyway, I'll get off the soapbox now.

I responded:

> You are not on your soapbox. You are totally right. Your ability to properly critique this day started when you created the FINVIZ list of social media stocks and started watching how they traded, which were the best, which were dogs, which moved together.

The trading lesson here is that TO developed the ability to accurately critique this day's trading because of the prior months of work he had done. You build intuition through screen time and study. He had paid his dues to gain the insight to offer a better plan of trading attack.

And the Winner Is...TO

Fast-forward to a year later and see the contrast between a failed trader and TO. Fail Boy sat in my office taking the time to explain why he was leaving. He volunteered a list of things he thought SMB could do better. As way of background, about five minutes earlier, SMB had an internal discussion about letting him go. I fought with my partners to give him another month. Turns out this was not my best moment running the firm.

Fail Boy started, "Bella, I run a small business, as well. I am doing this for your benefit. I thought you would want some feedback on how SMB can do better."

He was the third-worst performing trader on the desk. We do exit interviews when a trader leaves the firm. Why was he assuming we wouldn't ask for this feedback proactively?

"I know I can go get a job where I am paid a salary and run the algo I have developed," Fail Boy boasted.

"We will run your algo and fund it if you show it to us and it backtests well. We are happy to back your model and are more than willing to back it with significant money as it performs," I responded.

"It still needs to be tested some more. I need to see how it performs over a few more months."

"Okay, well, we can help with that if you want," I replied. (We have quants that help with this.)

"My algos are much better than yours, and there is no one here to help me with mine."

"Our best algo is built to run at a $100 million capacity and has a ten-year track record. And the developer sits on our desk every day and is the most open person to new traders you would ever want to meet. Why not talk with him?" (Or for that matter our other quants.)

"My algo is not a simple trend-following system, Bella."

As if ours is. Sometimes I feel as though I have taken crazy pills. Am I really sitting here having this conversation?

Fail Boy didn't create an algo that works, was one of the worst traders on our desk, and when I offered him help, he was too good for that.

"TO was in your class, correct?"

"Yes."

"Why aren't you doing as well as he is?"

This next answer sums up why he was talking to me about leaving and TO was on the desk making money.

"Bella, he has an unusual work ethic."

And there it was. The mind of a guy who can never become a successful discretionary trader. Fail Boy was in my office correcting my firm before heading to imaginary greener pastures because he did not possess the secret sauce of TO. It turns out a firm notorious for poaching SMB traders had offered a salary to poach him. On a positive note, Poach Firm used to steal our better traders, but now through some SMB adjustments, they take the worst off of my hands. Of course, Poach Firm thinks they are stealing our best.

Yes, TO competes very hard. Yes, TO has competed harder than most who have ever entered the doors of SMB. I felt a case of déjà vu as others had said the same about the better traders we have developed. Is TO a possessor of an unusual competitiveness? Or is TO's competitiveness a standard you must match if you want to find out how good you can be as a trader?

The market data that I have demonstrates that TO is very special. He is a gift to me and my firm. TO inspires me to teach better, develop better trading tools, find better technology, and knock down doors for new trading opportunities for our desk. But the market is very clear in what it demands. Compete like TO, or else you will be eliminated.

> Success is peace of mind which is a direct result of self-satisfaction in knowing you did your best to become the best you are capable of becoming.
>
> —John Wooden

Honestly, it is not most important from TO's story whether he is trading in five years or not. I am already proud of him. He has done the work to learn how good he can be. He is a success. Having said that, I bet you a Coke Zero he is an elite trader. If my firm does its job, he will still be on our desk working with and sitting as a role model for the next generation of SMB talent. If you compete like him as a trader or anything else important to you in your life, you should be proud of yourself.

Let's peek in on a trade review of one of TO's fade setups that fits his individuality, highlight a plethora of important market principles, introduce a new trade, and enjoy a high-level market discussion.

The "Sell the News" Trade

TO

Ticker: AMRN

Date: Friday

July 27, 2012

Biotech Fade Trade Strategy

This trade has multiple components:

• Biotech key event Rug Pull Trade

• Open Drive/Momentum Trade

• Contrarian-style “Sell the News” Trade

The third is the most important. This is a textbook template for the “oldest game on Wall Street” story: smart money guys pulling the wool over everyone’s eyes and leaving retail suckers holding the bag by selling into positive news.

Big Picture

It’s been a biotech bull market this summer. Lots of impressive run-ups: ARNA, PCYC, OREX, ONXX, AMGN, MDVN, etc.

What’s important to understand is that AMRN is a biotech with a fair amount of coverage and following but it is not one of the leaders because it did not trade to new 52-week highs.

Intraday Fundamentals

AMRN got PDUFA approval for AMR-101 but it opened negative in premarket trading.

Just from following the stock, I knew a few things:

• Everyone on Stocktwits was pumping this thing, saying approval was a lock.

• Canaccord/Wedbush/etc. were raising price targets to $18/$20 and pounding the table with buyout calls.

• AMRN often had technical breakouts, gap-ups, and breaking news spikes that had less-than-impressive follow-through (e.g., late June when it gapped up to $15 but faded all day). The long-term price action was in an uptrend but it felt heavy at current levels.

That, and knowing this was a crazy bull market in the sector, makes me think everyone was long into approval (overcrowding) and that there's nobody left to buy = *Sell the News!*

Technical Analysis

AMRN chart prior to approval. 16 = top of range, 13.60 = bottom of range. I try to gauge sentiment by looking at the gap relative to long-term levels. If an extremely positive catalyst can't get it above 16, my outlook is that the news is priced in and it's a big picture short as the smart $ takes profits.

Reading the Tape

• The 8 a.m. volume came in and it rejected the 15 level. There was a seller 14.60. It was initially a weak tape.

• However, once it reached 14, a 14.15 ARCA buyer stepped up. He'd eat a lot of prints, drop, and go high-bid/cross the book to trap bid-hitters.14.60 was not defended. The stock was a long on the tape at this point.

• I had to take the liquidity at 15 to get out of my position short and preserve my risk/reward, knowing 16 was the real out for the bigger idea and the short-term momentum was against me.

Later on, there's an unusually tight consolidation at 15.75. Mr. ARCA was eating up prints, he'd drop, and nobody would hit the bids lower than 15.70, and he'd come back. This felt "trappish" and made me think short squeeze on the open. But they wouldn't get past 15.85 when offers were paid. And 16 is key resistance.

But two minutes before the bell, somebody threw a brick (a large block order at market), the buyer dropped, there were print-throughs to the half, best bid was 15.67, and the book was now considerably thinner. Now I was anticipating the Rug Pull pattern where the premarket tape was fake strong and then the real volume comes in when sellers soul-crush the stock.

I hit it, and it tanked immediately (not to imply that I was the guy who caused that drop).

Trade Management

Trade Review

My covers suck. I covered 15.01, 14.91, and 14.70 on a 300 share position. Several reasons:

- Still new to the Open Drive Play
- Hard not to take profits with such a quick move
- Did not mean to get flat at 15.01/14.91
- Too picky in getting my shares back
- Never gave me prices I wanted to reenter after flat

I'm still deciding how I want to trade this play. Everyone has a different threshold as to what is needed to prove them wrong. There is balance I'm trying to figure out between trading the price action and intraday momentum and trading the bigger picture idea.

I had to be short early because sometimes they don’t drive it up and pull the rug. Sometimes it will just fade smoothly and trap longs on the shallow pops and I did not want to miss the bigger trade.

I should’ve taken a lot more risk on this idea, but they made me squirm a little bit, so I couldn’t build the position as originally planned.

Definitely have to hold this trade better, especially considering the conviction I had and the pain I initially took. Went straight to my target: 13.50.

From the Training Room: A Biotech Fade Trade Review with TO

This is a Fade Trade. Some say a Contrarian Trade. We take a position counter to the direction of the stock.

Bella: TO, why don’t you share with us your trade in AMRN.

Rug pull *means there is buying and buying and then the buying just stops and the stock plummets.*

TO: This trade in AMRN is called a Sell the News Trade, and it was a trade that I made last summer in July, on a mid-cap biotech. This “Rug Pull” Trade has multiple components. Let me break it down. The first component is a key event in a biotech stock. This is a sector-specific event, and this type of price action is most common in the biotech sector. The price shoots up out of nowhere in premarket action or right on the open things seem very liquid (meaning that it appears you can exit the stock easily if you want to), and then the stock just drops much more than you think and with extreme difficulty of exiting your position. This down move can be temporary or it might be the start of a bigger downtrend. The second component of this trade...

Bella: I just want to ask you a question to clarify a point. So when you are talking about this type of setup, you are referring to a biotech stock gapping up too much.

TO: True. Although, they don't have to gap up, this can even happen all before the event, before the results from the biotech stock are out.

Bella: Okay, and so, you are saying that these types of stocks more so than other stocks have a history of mispricing?

TO: Right, and imbalances come out all at once or in a short period of time, and there are very quick bursts near these companies' key events such as FDA approval or phase-three data or other research announcement.

> *Biotech stocks may rely on the success or failure of just one drug. This causes tremendous price fluctuation, or as we say, volatility.*

Bella: Would you say that understanding the fundamentals of the biotech company or the story that's driving the company is particularly more important in biotechs than other plain vanilla type of stocks?

TO: Absolutely, I just feel in this sector that the participants' emotions are a lot more volatile. As the swings get more abnormal, these emotions exacerbate. So, you want to know the story in the sense of what people are expecting, what might be baked into the stock.

Bella: Let's discuss the second component of the trade.

> *Sometimes news is already priced into a stock.*

TO: I will just go over the second component quickly, and I actually kind of covered it in the first component. These components overlap, but the second one is the Opening Drive. It's strictly a technical trade where you know something's going down, price action is weak, and we are just hitting the bids and getting short because we can expect a large opening drive on the stock and that goes hand-in-hand with what I tried to describe in the first component of the trade. So it always goes together, that's more like how to execute part of the trade. And going back to the third component, Sell the News. Basically, the Sell the News Trade is when you determine that news is already priced into the stock and there are no real buyers left. Therefore, you deduce that the stock has to go in the other direction. It's as simple as that. They say the oldest game on Wall Street is the smart money guys leaving the public holding the bag. The smart money sells into the positive news, they sell into strength, they already anticipated; by the time it's too obvious and it's in all the headlines, they are done with it.

The "smart money" is the sophisticated pro traders. The public are retail traders.

Bella: So, I have a question about you personally. Do you gravitate toward Fade Trades more so than the typical intraday trader?

(TO pauses and then answers.)

TO: Yes.

Bella: Maybe the question would be easier if I asked whether you gravitate more toward Fade Trades than a typical SMB trader?

(TO answers quickly.)

TO: Oh yeah, absolutely. That's easy to answer. Because I don't know every day trader and how they trade, so the first question was hard to answer. I know there are a few firms where they like to play bounces or fade short-term parabolic moves. I would say I fade more than most other traders on the desk, although most of my trades are not fades.

Bella: We have talked about fading in the past, and you actually sent me a question about a particular APOL trade [discussed earlier in this chapter]). You asked me whether I thought you actually traded it correctly. And I came up with three Fade Trade patterns that are worth consideration. One that I talked about is *the puke*. There are a few prop firms making good money on the puke. There's a steep down move and capitulation. These firms have filters that search for these types of moves, and their traders are taught to fade them with pretty big size and then play for a bounce or retracement.

What I try to get our traders to think about is this: Where is the most money? Psychologically, I think it's very hard to buy something at the bottom and hold it. You are basically sitting there and you are saying, "Well, I think this stock is done going down because I see something on the tape and I think it's going to reverse because I'm seeing something on the tape." The problem with this trade is that you have to hold it for a significant move; otherwise, it doesn't intellectually make sense. But what happens is that you over-remember how bad this stock looks at 15.50ish (when it is going down), and when it goes up, you sell it too early. It's just too hard for most to get out of their head how bad the stock looked while going down.

TO: That's true for me on a random play. But on these trades I am able to hold my long.

(Bella laughing.)

Bella: So you are much better person than me and other people.

TO: Yeah, if it's random play and I probably just....

Bella: I like the Reversal Trade better. Here's why. The stock stops going down here near 18.50; it clearly breaks the downtrend and holds higher maybe around 18.70ish. To me, here, I'm more confident that APOL is actually now going to go up. To me, my thoughts are not as bearish as what it looked like in the 18.50s. To me, there's going to be more people stepping in to buy it because now it's easier to determine that APOL will trade higher. So I think the Reversal Trade is going to be an easier trade. To me, I think that's something easier for me to hold for the real move.

When you and I trader chat about fading, I have to admit, I try to encourage you to make the Reversal Trade. It's an easier trade, and there is more money in it. Having said that, you have your own style. And if you enjoy The Puke or another type of fade, then go for it. You do like to trade biotech stocks; in fact, you like to trade cheaper biotech stocks. We stay away from cheap biotech stocks. But if these stocks work for you, if you can find patterns that make sense to you, then stick with them.

Find the product, trade strategies, and time frame that works best for you.

We teach on the desk, particularly in the beginning, to trade with the trend. You like to fade. My job is to point out the patterns to you that may help you make money when you are fading. I showed you the patterns and the subsets of the fade trade that are best for you to try. It's not for me to tell you which one you are going to like the best. That's not my job. In fact, if I tell you that you have to make certain trades, I am probably not doing a very good job.

This trade represents allowing a trader to be his own person. Agree or disagree?

TO: I agree.

Bella: So the Big Picture for AMRN is?

TO: The Big Picture that summer for this sector was the biotech bull market. It actually is a bull market right now as well. Lots of impressive run-ups in biotech that people are talking about: ARNA, PCYC, ONXX, etc. AMRN was getting a fair amount of coverage, but it never acted like one of the leaders. It never had a run-up where it consistently made 52-week highs.

It just went up slowly to some resistance levels and stalled. People keep talking about it as if it's going to be like the next big thing, which leads me to the next slide.

Bella: So, just to highlight a trading principle. There are certain stocks that make up a sector. And the sector in this case, the biotechs, is hot. And when the sector is hot, you are going to see patterns.

TO: Let's just say uptrends becomes the norm, powerful uptrends become the norm. So when a stock in this hot sector gets talked about, you want to watch it for an explosive upmove, if it has not made an explosive upmove yet.

Bella: What about looking to the leader in this sector as an indicator for when you are trading another stock in the sector? Let's say that MGN is the best stock in the biotech sector, and you were trading ARNA. If MGN is really strong on a particular day, you might use that information when you are trading ARNA.

> *This is a much better and nuanced answer here from TO than me about using other biotech stocks in the sector as an indicator.*

TO: Possible, it depends on what day you are talking about. Biotech stocks do different things. If one biotech stock treats a certain disease and is outperforming on the day, then other stocks that have a similar drug may trade higher as well. I will use the leader for each drug in the biotech field for other stocks that have drugs that treat the same disease. Move on to Intraday Fundamentals?

TO: Okay, AMRN had a major key event. They received approval for one of their drugs, AMR 101. AMR 101 significantly reduces the bad cholesterol of the patients, and it's a prescription grade omega three fatty acid. So that's the kind of drug it is. There is a lot of money to be made in this space because heart disease is a major health problem in the United States and worldwide.

But AMRN opened negative in premarket trading. And when I see that the initial reaction from the market is negative, that is meaningful to me. I start to wonder if this news is already priced into the stock. Or I wonder if there is something I didn't see about the approval, something in fine print that suggests that this isn't as positive of an event as it might seem on the surface.

Just from following the stock for the past few months I knew a few things. Number one, everybody was saying approval was a lock. Second, analysts who were tracking the stock were raising their price targets to 18, 20. They were pounding the table with bio calls. Analysts were saying once it gets approval, they should be looking for a buyer, putting out valuations in the 20s. Number three, gap up, technical breakouts, have failed in this stock in the past.

There was a day in late June when AMRN had positive news. We were actually trading it on the desk. AMRN gapped up to 18, but then traded lower all day. It didn't completely fill the gap, just a very slow downtrend. There was not a lot interest, not a lot momentum in the stock. Even though it was in an uptrend, it did feel a little heavy, overbought, every time it has had good news.

Very nice job here of spotting a pattern that may give you an edge.

Bella: So were you remembering that day and using that information on this day? You were recognizing a past pattern with this stock to give you an edge on this day?

TO: Yeah.

Bella: Okay, good, I like that. Alright, give us a summary of your Technical Analysis for this play.

TO: Well, it's pretty simple. Prior to this drug approval, AMRN has been trading in a range. 16 is the top of the range, 13.5 is the bottom of the range. I'm just trying to use these levels to gauge sentiment. I am trying to look at the gap relative to long-term levels and trying to determine if the news is priced in, if it might struggle with 16. How specifically that happens, there are a lot of subsets for that. But in short, any type of price failure at 16 is a good confirmation that price is confirming my thesis: AMRN is a fade. So 16 is the level I'm looking at to try to define my risk and to gauge the probability of my Fade Trade.

Bella: So you said something interesting. Your thesis is that it's going to fail.

TO: It can happen in many ways. It could gap up to 16.50 and fail quickly on the open. Or it could start somewhere within the range and fail from there. It could reach near this 16 technical resistance level and then just fail from there.

(Bella smiling and setting up TO to highlight an important market principle.)

> *If a stock leaks above a key technical level, this is not a confirmed breakout. Time above the level and volume confirm the breakout.*

Bella: I'm confused, if the top range is 16 and it gets above 16.50, doesn't that mean the stock is going to go up? The stock is now above the important technical resistance level.

TO: As you said, Bella, time is an important variable in reading the price action. And you will see all the time premarket price breakouts on very low volume that fail miserably. They print above the technical level but do not stay up there for a lot of time or do a lot of volume above the level. If a stock is not above the technical level for a significant period of time, or does not do a significant amount of volume, it has not confirmed it is ready to break out.

> *Capitulation is heavy and desperate selling potentially indicating the end of the sell order.*

Bella: Let me go back to trading the puke because there are some important points I want to clarify to you. Spotting that puke is a legitimate way to trade. Some firms make a lot of money doing that. They have deeper pockets than retail traders, so when they are wrong they can handle the loss. When you fade the puke and are wrong, this can lead to a serious rip that most retail traders cannot afford. This is an advanced trade that I do not advise a new trader to start with. Because when they are wrong, they are going to lose a lot of money. I recommend starting new traders with easier trades and have them built from these. But that's a legitimate pro trader trade, playing for the puke.

The Reversal Trade is something that I would prefer my new traders make more of rather than trying to catch the bottom. There are three legitimate fade patterns from this APOL setup that you sent to me.

First master the Reversal Trade pattern if you want to add a Fade Trade to your quiver.

TO: I'd like to point out that in that APOL setup, I feel like I had a good level to use as a guide.

Bella: In this case, your question was more about, you saw something on the tape, you saw it not going down anymore, the question is if you see that is that a legitimate way to start your position. And I don't encourage most to make this trade, and I certainly don't encourage new guys to make that trade. Because again, I think it's a harder trade.

First learn the easy trades and then build from there.

But I think you TO can make the trade. I think Spencer would make this trade. Gman would make this trade where the stock is not going down any more. Gman would see that on the tape, start a long position, and whack it if it violated this level. And because the stock isn't going down any more, you are willing to get long, and your stop is below the bottom of this level.

The big money is in catching the real move.

Bella: Okay, let's get back to your AMRN trade. And as you mentioned before, these stocks, the biotech sector, have a history of opening up and opening down much more than other stocks. So we are more skeptical about a biotech opening up above a technical resistance level than other stocks. What's next?

TO: We can talk about Reading the Tape. I was watching the stock right when the premarket opens, at 8 a.m. Volume came in, and there was a seller at 14.60. So there's initial price action that shows weakness. AMRN was not at our key levels; 13.50 and 16 are the key levels. It would have been better to spot a seller closer to 16, like at 15.80, for example. That would have been safer. And there's still 90 minutes to go to the bell, so we are still in the price-discovery process. But I couldn't help myself. I got short near 14.60 once I spotted that seller. It looked to me like there was tradable volume, such that if I was wrong I could cover quickly.

Bella: Wow! 8 a.m. is very early trading. That is very early premarket trading. Usually volume does not pick up until close to 9 a.m.

TO: I got short initially at around 14.60, and AMRN traded down to 14. And at 14 it started to change. There were some signs of buying at 14.15.

Auto buyers stepped up. A buyer took the prints on the bid and then stepped higher. When this buyer stepped up to 14.60, no one hit the bids. And I think the stock was a long on the tape at this point purely from a momentum standpoint.

And this is where I made one of my mistakes. AMRN now offered a decent momentum scalp as a long. I was overcommitted to the short thesis at this point. Instead of taking a small profit when I spotted that buyer around 14.15, I just decided I was building a position. I had that plan, built a small short position, and got taken out above the 15 for a small loss. I made the spread a few times to try to improve my average price as it was going up, but at 15 my shorts were wrong and I had to cover.

My plan was to restart my short position at higher prices if I saw a good shorting opportunity. I would have had to hold all the way up to 16 if I decided not to cover above 15 for my short at 14.60, which made no sense. So my covers were good.

> *I do not know any great traders who do so by hanging onto trades that trade against them. Pain is for the hospital not trading.*

Later on, this is still premarket, there was this unusual tight consolidation at around 15.75. AMRN is already up 2 points with that auto buyer still eating up a lot of the prints. He would drop, but nobody would hit the bids, so then he came back. This actually set off an alarm in my head. It made me think AMRN actually could be a long from a momentum standpoint (even at this level). Because the buyer was dropping, he's the guy who drove up the stock and nobody was hitting the bids when he dropped. That kind of concerned me because this relates to my short thesis. It was just so strong on the tape.

Bella: That's a big tell on the tape, right? When the identifiable buyer drops the bids, you would expect A) the stock to go down quickly and B) the seller to hit the bids pretty hard.

TO: Yes, especially after a 2-point run-up premarket. But AMRN wouldn't get past 15.85 either, so there was no reason to get long. And 16 was the key resistance level looming overhead.

Bella: Even with such strength on the tape, that's not really a long until it's about 16. So what are you thinking? You are thinking on the tape this is a very bullish signal. But it's such an important level at 16, such an important technical level. It's a better trade if it holds above 16, but not a good risk/reward here at 15.75?

TO: Yeah, at this point I'm just looking for more information. But I am ready to act.

Bella: If 16 wasn't the resistance level, you would get long. If 15.50 was the key resistance level and you saw what you saw, the buyer step up to 15.75, then you would have gotten long. Alright, so what happens?

TO: Two minutes before the bell, somebody threw a brick into the stock. That's what I refer to when there's a large block order that enters the market. They just kind of cleared the book, or the bids with one large order. And our buyer dropped. He didn't drop on his own this time like the last time. He was forcefully dropped. They smacked him basically.

AMRN got below this key 75c level from the tape. The book looked better for the shorts. You didn't see as many prices on the bid any more. And now I started to anticipate the rug pull pattern where, you know, they ran it up on low volume and then right before the bell they drop the stock out. I expect the stock to fall quickly.

Bella: The key is low volume. You must have low volume. If the volume had been higher premarket, this is not a rug pull. It's the lack of volume in the premarket how much it has actually gone up in the premarket that got you interested, right? It's got to be low volume, it's got to have some room to actually go down.

Oh, and the student disagrees with the teacher. I kind of like that.

TO: Depends on what you mean by *low volume*, because I feel like it has to be volume relative to the larger volume that comes in when they start hitting the bids and showing the selling balance right before it opens. Because I have seen opening drives lower on high volume trading that gapped up about 100 percent, so it has to go down a little bit. That was kind of different. So I don't know.

Bella: Anyway, you thought that was a very significant signal at 75 cents when the buyer got smacked?

TO: Yeah, you can see it on the chart, the volume candle and the downturn; the chart is lower.

Bella: So where did you hit it? Where did you get short?

TO: Yeah, I hit it at 15.67.

> *Wow! That is some very fast trading to hit that right below the seller at 75c.*

Bella: And what would be your cover above 85 cents or above 16? Or to be even more nuanced, half above 85 cents and half above 16?

TO: On these trades, it depends on what happens right afterward. If I do not like the way the stock went down, I might cover or lighten up. But above 16 you have to cover.

(Bella presses TO to be more nuanced with his covering.)

Bella: What about above 85 cents? You said AMRN couldn't trade above 85 cents. It was 75c that it could not trade below, but AMRN couldn't get above 85 cents. To me there are three covers to consider. You hit it and you are playing momentum, and the cover is wherever it slows on the tape. You are playing it for momentum; that's how you play momentum. The guy drops, you hit it, it goes down 30c and slows, and you cover, that's cover number one.

Cover number two is above the top of the range at 86 cents.

Cover three is above the important longer-term technical level. That technical level in this case is 16, and so you must cover above 16. *(Bella raises his voice.)* You must cover above 16.

> *Not covering above 16 is bad fundamental trading. It's just bad.*

If you want to be really sophisticated, you can do a little of all. You can get short three lots; play one lot as a Momentum Trade and cover that one when AMRN slows on the tape. Keep the other two lots for a bigger down move and split the atom with your covers. Cover one lot above 86 cents and cover the last lot to get flat above 16. You could trade that setup this way.

Admittedly, that is some very advanced intraday trading. That's probably the way I would look at the trade, the way I would have done it. But that's sophisticated. But something for you to think about. Alright, so tell me what you do.

TO: I hit three lots at 67 cents. And I just covered way too early. I cover 15.01, 14.91, 14.70. I was surprised by how fast it dropped so I just covered.

Bella: This is right on the open? So we open, and that's when the buyer got smacked?

TO: No it actually happened right before the open. But more volume came in, and AMRN spread out on the open. So, it was hard not to take profits from that quick down move. My eyes lit up to just take profits. I didn't even want to get completely flat. But I talked myself into a what I call *fancy play syndrome*. I was too cute. I thought maybe I could take a quick cover since it went down so quickly and then reshort it higher.

> *Oh I really like this fancy play syndrome. Great way to express being too cute with your trading.*

Bella: So you wanted to reshort at 15.10, and AMRN only got to 15.06? So if it's 15.10, you're going to short some more?

TO: It was really difficult to read the tape on that first minute. Because it's flashing up and down and so fast. All I am thinking is this is uncertain. So I reacted as if I didn't have control over the position. But that was my reaction. It was like chaos right on the open. It wasn't like I could read the tape. The stock was moving too fast. The spread was too large. There was not an easy way to spot a reentry.

Bella: Been there.

> *This is such a great example of the inner re-analysis that a trader must go through about a bias or thesis. Keep asking yourself the right questions.*

TO: There's also something to mention, my psychology. I started shorting at 14.60, watched it trade down near 14 and road it up to 15. I took a little bit of loss on the play. And then I watched it trade all the way up to 16. I started to feel like maybe my thesis was wrong with that buyer at 15.75. It was hard for me not to take profits into the down move after seeing the premarket action.

Bella: It seems to me two things have to be going on here with our Intraday Fundamentals to help us with this trade. Either A) the news is built into the price of the stock or B) the news really isn't as good as the market thinks it is. So, a lot of times with biotechs the drug is not far enough along for people to be excited. It's too early in the research stage for a new drug for traders to be that excited. In this sector, the information flow is not as efficient as with other stocks. There is more opportunity for these stocks to be mispriced. And therefore, there are more crazy moves in biotechs than in other sectors. If you really follow the news in such stocks closely, you can gain an edge more so than with other sectors.

TO: That's why I like to trade biotech small caps. I mean there's only so much money that can go into these companies. A lot of big players like David Einhorn might not be interested because he cannot get big enough in these trades for the size of his book. So I am competing against lesser competition in these names.

Many big hedge fund, mutual fund, and institutional traders cannot trade stocks under $5.

Bella: And many big players have rules about trading cheaper stocks. It's just not as sophisticated a market sector as trading AAPL.

Alright, good. I like the way you put together a lot of different indicators for this trade. I always love the pattern where a stock is close to resistance and there's a clear buying pattern on the way up or there's a very significant buyer you can spot very close to the technical resistance area. And then that buyer dissipates, so then you get short. This is a very compelling risk/reward opportunity.

As I actually listen to you explain the trade, I see the next level below 15.80 as that 14.60 level from premarket that we saw at 8 a.m. I'm thinking I could probably get that down move at a minimum. At best, I may catch a move all the way back to the bottom of the range, which is 13.50ish. That's a great trade. I can cover above 85c and 16 for a potential down move of over a point very quickly and maybe even more with the setup. What a powerful trade.

TO: You can also see this opportunity as more than one trade. You have that Opening Drive Play that I made. But you also have an easier trade. If after the open this stock is trending intraday, you can make a trend trade for AMRN to trade to the next important technical level. This news event can be the catalyst for the stock to make a large intraday trend move. So if you are not as fast as us, you can make an intraday swing trade for this play as well.

Bella: Okay, I like people finding trades that are interesting to them, as you have clearly done here. And as long as the trade is fundamentally solid, I have no problem with you gravitating toward fade trades. However, above 16 and AMRN is not a fade. That is fundamentally the wrong trade to make. Fading above there is just plain bad trading.

(Bella smiling.)

This is a wonderful example of an elite developing trader being more individualistic about how he looks at the markets. So, TO, thank you.

TO: It was my pleasure, Bella.

Postscript

TO continues to work hard and be hard on himself. I worry about him putting too much pressure on himself, burning out, and not enjoying the process. I do not worry about anything else with someone like TO. After all, he is now one of the larger holders of bitcoins, a peer-to-peer cash system. He applied his Reading the Tape skills to dominate trading in that product. And he used the same tape reading techniques to crush FNMA, Fannie Mae, ending up recently with a 50k plus month.

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5. Follow the Trading Path of Pippen

The next trader I will introduce, Pippen, followed a trading path to copy. Think of him as the leading actor in the big movie production *Optimal Trading Start*. It is a course I have seen most of my sustaining, consistently profitable traders take. Let's meet this outstanding young man and discuss the steps to Consistently Profitable Trader and then more. It is one shared day by day, trade by trade, tick by tick, review by review with his sidekick TO.

A few days before Christmas, Pippen knocks on my door and hands me a card before flying west to Southern California for the holidays. The card reads as follows:

> Dear Bella,
>
> Thanks for being a leadership role model for us and tightening up our culture. Thanks for being with us during our development as traders. I wish you a Merry Christmas and a Happy New Year!
>
> See you soon!
>
> Best,
>
> Pippen
>
> Dec. 16, 2011

He is the politest trader I have ever trained, impossible not to root for.

Another time, we're eating lunch on a Saturday at the Landmark Grill inside the Time Warner Center in Lincoln Center, NYC, with his trading buddy TO. Pippen lets TO and me dominate 90 percent of the talk. You almost get the sense that a good story from Pippen would have diminished TO's Friday night recap, so there is none from him. We could rename him Mr. Polite.

Pippen is a desk favorite. He talks with a most unusual time delay, with English not being his first language. He thinks constructively first about what he is going to say, then starts to move his mouth, but the words come out as if there's a slow Internet connection. Think of the old AOL dial-up connection of the late 1990s. Most find this quality endearing. One summer night in NYC it rained as hard as anyone had ever seen. The next day, Pippen cracked the desk up with: "It was raining so hard yesterday, I saw a baby flying through the air." To this day, none of us have any idea what that possibly could have meant. But any reference to it now yields full-belly, gasping-for-air laughter on the desk.

The trading gods must have built Pippen just for the trading teacher. Pippen obsesses about a good ticket average the way a Type A college student does his GPA. His monthly reviews begin and end with goals for more efficient trading. Pippen is mellow even for Southern California. He's never late, never loud, and never a problem. He displays an all-star attentiveness during tradecasts, which is always the signal that trading is one's passion. He looks at you, the mentor, like the deeply religious their priest, as if he is listening to the Word of the Markets.

Why do we call him Pippen? Because he is so deferential to TO, like Scottie Pippen was to Michael Jordan. I will let TO tell the story of how they met and then later on how they became trading's version of a Mantle and Ford, Seinfeld and Constanza, Jack and Bobby, or Batman and Robin:

> I actually met Pippen, the guy I sit next to, before attending the training class. He found my cousin in a game of *Defense of the Ancients* (popular *Warcraft III* game), and they chatted a little bit. My cousin found out he was also a trader who was going to trade at SMB Capital and he told me about it. We exchanged some pleasantries over Facebook. Now I sit next to him. We're the top traders in our training class. Small world.

Pippen hardly begins a sentence when asked about his trading without breaking into "TO got me into..." or "TO and I were big trading...." Our trading halls often find Pippen walking in and out with TO. They can be found well after the close in their seats reviewing their trading, often together—and subsequently making each other better.

Your start to trading a new market product should follow Pippen's. In this trader's first two months, he was negative, but barely. He made some progress, losing less in his third month but was still in the red. Then in month four, he made a little money. In month five, he made a little more. And this trend has continued. Many traders believe that they quicken their path to success by imitating the techniques of a star trader that they have heard about or know. Gathering around a firm's star trader so they can become like him is a common exercise among new and developing traders. Not a chance. Trading is a journey. You climb the P&L ladder dollar by dollar, daily lesson by daily lesson, trade by trade made your own, added screen time by added screen time. You want a trader, a path, to copy? Let that circle form around that firm star trader without you. Be like Pippen.

Pippen is not the best trader on the Street. He is not the best trader on our desk. He was not even the best trader from his class. He is now. He was not one of the top three traders in his row for most of his career. He is now. He has responsibly and steadily improved his trading game. He has developed a base of profitability from which to build. He has done the work, built the skill, and developed a PlayBook that makes sense to him. The young man can flat out trade and is perhaps the best momentum trader now on our desk (the hardest strategy to learn after the influx of HFTs). And from this point, he can grow to become an elite trader. Most importantly, few traders in my space ever became great without first starting like Pippen.

From Pippen's story, you will learn the following:

- The steps to profitability
- How to stop losing money
- How to recognize the delusional trader
- The massive importance of finding the right culture
- The value of master coaches
- That each trading session is first an opportunity to learn

Also, stick around for the intriguing end of this chapter where we review the historic IPO of Facebook, how Pippen traded this opportunity, and how to trade an IPO.

A Path to Profitability

Let's start with a common and erroneous refrain I hear way too often with new traders: "If I increase my stop, then I will start making money."

This just might be the single silliest and most dangerous thing an unprofitable trader can say. Correction: "Trading is in my genes" is. If you increase your stop from a position of being consistently negative, there will be only one result. You will lose more money. It's not your stop. The trading truth is that most winning trades start to work for you quickly. Mastering the trades that need that bigger stop is Ferrari acceleration to larger losses, inefficient trader review, and trader frustration. This is due to not having a consistent book of profitable PlayBook trades that you can execute in real-time. Until you do, you will be caught in a web of losses, deluded by a hope of better days ahead (as discussed in the blog post here).

This Trader Is Delusional!

Jan 13, 2013 | By Bella |

On Sundays, some SMB traders send me their weekly results. Here is an example from one trader, who I like a lot and am rooting for, that p***** me off.

> This week could have big a big week for me and one that has really set in on me bc I lost $1,000 and I wanted to know what happened after all the preparation that I took. If I took trades that conformed to my edge, added to trades that were working, and let my winning trades play out: I would have had my best week to date and that is really interesting. Two days would have been over $1,000 and the rest around breakeven. going over my trades, **it really is amazing how many trades I took that didn't conform to my strategy**. I think that I **went on tilt** after losing money on Monday when I had 3 trades that I put myself in a position to make real money and **I didn't take the AAPL trade** in premarket. **I tried to compensate** for this by getting in trades that were not my own, and I will definitely be looking to improve on this week. I now realize that I cannot try to make money, all I have to do is follow my strategy and the trades that work are the trades that I look at right away and say to myself "I have to be in this" not the trades that I think "might" work and I try to anticipate and ignore my signals.

I will be a consistently profitable trader if

1. I only take trades that I have an edge in.

2. I let my winning trades play out and tell me when to exit.

@mikebellafiore

The trader is delusional! I write about this issue more extensively in my next book, *The PlayBook*. He is not anywhere near close to having a big week. Traders do not go from underperforming to a big week, unless they are lucky. Trading is a measurement of doing all the little things well. This trader is making four big mistakes that he must correct just to get flat. Flat should be his singular goal because he is underperforming.

Here are his next steps:

1. Not so drastically underperform
2. Flat
3. Make a little
4. Expand his PlayBook
5. Get big in his A+ setups

There are five steps before he will have a big week, not only if he did a few things differently.

To achieve Goal 1, he must address these problems:

it really is amazing how many trades I took that didn't conform to my strategy

You do not just decide to solve this problem. This is an issue of preparation, visualization, and trade review. All of these are lacking based on this statement.

went on tilt

You cannot just change going on tilt. You have to work to lessen the frequency and damage of these periods. Self-actualization, a psychological journal, and a walk to calm down in real-time when you sense you are on tilt are essential.

I didn't take the AAPL trade

Again you are not just going to take the next such trade. Pulling the trigger is performance anxiety. Generally it results from a lack of practice with your best setups. Think trading, talk trading, review, talk to your mentor, watch tape, create a PlayBook, etc. are all ways to help you execute on your favorite setups in real-time.

I tried to compensate

This trader is going on the demo next week. He can work on not doing this while not trading our money.

*****postscript: This trader above actually got the message. Four months of struggle and work later, he has turned the corner. I

> expect him to be one of our better traders going forward. It is rare to go from delusional trader to CPT. But you can do it!*****

I will offer a path to profitability to consider: the path of Pippen and the many sustaining and consistently profitable traders that I have trained. Look, there is no one right way to achieve your goal, but there are definitely wrong paths. Adding risk when you are losing money is a flight plan to trader crash and burn, and, worse, the blowup.

I was talking to a group of trainees recently about the potential power of building from a positive P&L trading base. Notice my use of the word *potential* here. Positive traders have potential, even if only minimally profitable. Unprofitable traders have a PlayBook to build, and flaws to correct, and for them, the description of potential is not yet ripe.

If you can create a PlayBook of profitable setups that make sense to you, there is an ocean of possible growth. Here is what Coach K said to one of his star players, Austin Rivers, now in the NBA, about adding to his game:

> When Austin came to Duke, I told him that every player is like a house: The more skills you learn, the more windows you have on your house. When he came to Duke, he had one really big window. He was an amazing scorer. The goal was to add more windows to his game. He's in that process right now.

If you are just losing money week after week, you have many issues you need to resolve as soon as possible—namely, impatience, overtrading, lack of discipline, and work ethic. Believing you can go from consistently negative to decidedly positive is delusional for almost all unprofitable traders. How about first just stop losing money? As Coach K says, you have some windows to build.

My good friend Michael Martin wrote in *The Inner Voice of Trading* that you are not going to be great at this game called trading for many years, but you can enjoy the journey as you build your skills. In Denise Shull's *Market Mind Games,* she wrote about the trading reality of one technique being gamed out of the market and the psychological challenge of finding that new edge. And that is for the profitable traders. The single greatest failure in trader education just might be the unwillingness of teachers to share realistic learning curves for fear of diminished sales or understand their true expanse from a lack of knowledge. As Denise writes, even when you get "there" (consistent profitability), what do you really know? She shrieks at the idea of traders thinking they have cracked the code of the markets. So with that said, where do the new and developing traders think they are going so quickly?

The Folly of Overconfident Market Predictions

Let me make a point about the overconfident know-it-alls on the Financial Media Entertainment Complex, Twitter, and now StockTwits. Stop pretending you have the markets licked, with your "APPL is going here and SPY is going there" pronouncements of certainty. Or your pats on your back after a correct prediction. This does a disservice to all who are trying to improve at our game, because they enter thinking they have to be able to predict stock movement. As a trading teacher, I have to power-wash this financial media propaganda from their trading brains. Spencer tells me how pro trader and straight-shooter @Gtotoy DMs him in disappointment at these punters. This tweet sums up this struggle between pro trader and the predictors:

Fitzstock @Fitzstock2004 @Sissine27 @jcmbama1 you don't get it. You don't predict price, you trade it. When we start a downtrend, I will change my tune. $study

Overconfident market predictions are folly and dangerous folly to the followers who do not know any better.

Let's reflect on all the financial predictions that were thrown around in 1999 and 2000. Here's one from December 1999: "Most of these stocks are reasonably priced. There's no reason for them to correct violently in the year 2000." Thank you very much for that, Larry Wachtel of Prudential. Here's another: Charles Kadlec said in August 1999 that "The DJIA will reach 100,000 in 2020" after "two decades of above-average economic growth." Well, good luck to you, sir. Let us know how that turns out. Hey, we're only seven years from 2020. Maybe we'll find gold on the moon by then, too. James Glassman, in October 1999, was adamant about the riches that were in store for all: "What is dangerous is for Americans not to be in the market. We're going to reach a point where stocks are correctly priced... it's not a bubble...The stock market is undervalued." Oh, the name of the book he wrote?

A real knee-slapper called *Dow 36,000*. Hold on, I have another book title for you: *The Roaring 2000s*, by Harry S. Dent. Oh, poor Harry—and I mean that literally, if he happened to stay on the wrong side of the market.

And then there are the television pundits. I'm speaking primarily of the folks over at CNBC. They held their first annual CNBC Stock Draft on April 26, 2012, with the proviso that each contestant hold the stock until the Friday before Super Bowl 2013, February 1. Well, that date has come and gone, and the stock picks, while they weren't uniformly bad—Reggie Middleton chose GOOG, up 26%; Herb Greenberg chose JNJ, up 14%—they were, without question, *mostly* bad. To name just a few, Pete Najarian thought Starbucks looked great at $60.59; it pulled back 6%. Paul Adami chose RadioShack, thinking that at $5.50 the stock was headed for $7.00; it went negative as well, down a whopping 44%. Jim Cramer, to his credit, mocked Adami's choice and chose Microsoft; alas, it ended down 13%. Abigail Doolittle, who chose Dell at $16.56, saw that stock go down 17%. (She believed it was headed to at least $22 and maybe as high as $26.) The worst pick? That honor goes to Paul Hickey, who chose JCP, down 45%. While this made for some lively TV, this game of the predictions is not the one we play.

I could go on with all the picks (you can easily find the video online), but the point of this missive is that we can't know what the market is going to do in an hour, a day, a week—or a year. Trading is about controlling your risk/reward and constantly evaluating your positions. But there's a meta-problem here: Most TV financial pundits exist to fill up air time, entertain, and sell advertising. You may think I'm painting with too broad a brush, but it's only to say that our sport is not the business of entertainment, or offering up pithy one-liners, and we're not in the business of hollering and screaming. (Okay, you might be able to figure out who I have in mind at CNBC.) Trading is a serious business, and to succeed at it one must not only have the developed skills, but the mindset our job is not to be right. So be careful to not become mesmerized by the Financial Media

Entertainment Complex and try to understand their agenda. You are a trader, not an ads salesman.

Skill survives. The ability to find new patterns that work in changing markets endures. Trading plays come in and out of favor like significant others in your early twenties. We all do not know that much about the markets, even after 15 years of trading, because our market's data is always changing. For example, I had never traded against algorithms for most of my trading career, and then they just appeared without warning dominating a new trading reality. How I pulled money from the markets in 2003 or 1991 or even 2009 is distinct from how I trade today. Having said all of that, then isn't it best to pick a path that is most responsible and builds a trading base to adapt to ever-changing markets? Think about this path, the path of Pippen:

- Lose money.
- Lose less money.
- Flat for the month.
- Slightly positive for the month.
- Consistently positive for the month.
- Find more opportunities in the setups you are consistently profitable.
- Build from this positive base by adding other trading plays.
- Focus on getting bigger in the plays that make the most sense to you.

This path of Pippen contextualizes a common challenge for the new and developing trader: constant trading losses.

How Do I Stop Losing Money?

"Bella, how do I stop losing money?"

I get asked this question via e-mail often. What are my thoughts?

There isn't one single thing I could say that would make a difference. There aren't even a few things I could write that would make a difference. I have no Advil for your trading headache. We do know that Einstein said, “We can’t solve problems by using the same kind of thinking we used when we created them.” Let’s see if we can offer some ideas for solutions.

First, if you are consistently negative, you should not be trading live. You should be on a demo. If we work with students who are consistently negative, then they are placed on the demo and asked to work on their PlayBook and trading skill development. Every day they should catalog a setup that makes the most sense to them in SMB PlayBook template form. The idea is to focus on the trades that you can make at this stage in your career profitably. Get good at one trade, make money, and then move on to the next trade.

GMan developed a risk analysis sheet that crunches how trainees should bump up their trading size. You start at 100 shares and do not get bumped until you are net profitable at this level. This severely restricts how much money you can lose intraday when you begin trading. Perform well at one level, and then and only then push yourself to that next level.

New traders undervalue the power of being consistently positive. Perversely, some new traders would rather lose $1K in a day than make $200. Their logic is this: At least with these losses, they are trading bigger. Trading bigger makes them feel more professional. This trading is more entertaining to them. But this mentality reminds me of the Sean Penn warning on how movies should not be merely entertainment: “If you want entertainment, get two hookers and an eight ball.” There is nothing professional or entertaining about losing money consistently as a trader. In fact, that could be the very definition of amateur, or as we say *piker* or others say a *punter.* Respect your trading losses.

Recently, Carlton, our floor manager, and I talked with a trainee about too many negative trading days from his prior month. To me, this is a lack of respect for money. A good intraday trader ought to strive to pull money out of the markets four out of five days a week. If you are negative two days in a row, you ought to hold an emergency trading summit with yourself. Negative three days in a row, and that trading summit gets extended and you bring in outside speakers. Ask yourself and mentors: What can you do tomorrow to ensure that you make money? And then stick with those plays and quickly lock in your gains the next day. Do not expand your trading outside those setups.

This hyper-focus on making money forces traders to hyper-focus on the setups that are best for them. Sticking to these setups while trading live will improve their results, and better results builds their confidence. Improved confidence then allows traders to find more setups that are best for them. It is a delicious cycle of profitable trading breeding further profitable trading.

Remember, a typical pattern for the successful beginning trader is this:

- Lose money.
- Lose less money.
- Flat.
- Slightly positive for the month.
- Consistently positive.
- Find more opportunities in the setups with which you are consistently profitable.
- Expand your PlayBook with other trades.
- Add size to your best trades, which grows your P&L.

But if you are just at the stage of losing money, you should not even be thinking about adding size. There should be no delusion that you are close to breaking out as a trader. You are not. Your next steps are the ones shown here. And you are not going to get to the stage where you should be sizing up for many stages. So be realistic and patient about your work ahead.

My thesis on how to start as a trader is not supported by everyone. I have had personal discussions with the head of a very successful prop firm outside NYC who gives his new traders much more latitude when they begin. Traders are quickly bumped to trading 1,000 share positions. It is important to note that this other firm head has deep pockets to withstand drawdowns on his traders that you may not have in your personal account. I might add that developing new traders is not a strength of this other prop firm; it's more an outfit continuing to profit from many legacy traders. This trade-big-early position is also supported by one of our senior traders, with over 15 years of trading experience, who is always in my ear questioning whether new traders should start trading bigger at the onset.

I find, at best, this leaves your better new traders in an outsized hole they must dig out of to take home a paycheck and, at worst, trading losses unnecessarily big on losing traders. Also this added size distracts from the trainees primary goal of building skill and a PlayBook and focuses attention on insignificant early P&L. Giving traders a large number of shares to trade at the start is not the most direct or efficient route to build a well-rounded career as a consistently profitable trader.

The key is to setup an infrastructure to allow new and developing traders to build skills as fast as possible so they shorten their learning curve. I view the normal curve as developing a PlayBook of trades that traders execute in real-time. New traders can build this PlayBook after the close by archiving their best setups and then building from their best trades. It is not necessary to rip up a bunch of money when you are learning to understand which setups are best for you. Perhaps I come from a history bias of almost always trading my own money and fronting traders. So I see those beginner losses based on size that's too large as a case of taking on unneeded risk.

Let's study a better way to start.

You *Must* Be Big in Your A+ Setups

With Pippen, we took his consistently positive trading base and pushed him. We bumped up his max trading size and intraday loss limit. A few weeks later, we rinsed and repeated. A month later, we rinsed and repeated. One time, Steve bumped him up to a level that so surprised Pippen that he took the news like a giddy teen, but then he quickly assured Steve that he would be responsible with this added risk. Steve quickly corrected in a stern voice, "No, we want you to take on more risk."

On every daily review sent to me thereafter, I checked to see whether Pippen had taken on enough risk with his best trades. If he hadn't, I would ask him in an e-mail, "Where could you have been bigger in *xyz* stock?" During tradecasts, I stressed with all my teaching passion, "In your best trades, it is your job to be as big as you can in your A+ setups responsibly. If you are not as big as you can be, then you are not doing your job."

It took some time for Pippen to trade bigger. He needed to be pushed. A negative of only allowing traders to get bigger from a positive trading base is that many will be slower to get bigger. They are so accustomed to controlling their risk that they can become reluctant when it's suggested to them that they increase their level of risk.

Further, they also can overvalue being positive every day. See this e-mail from Pippen:

> Hi Bella,

> Tomorrow will be one of the *most* important days to me as a trader. And it will mean a *lot* to me.
>
> Today is my 29th consecutive positive day. I have been positive every single day since last month, from 4/24/2012 to 5/23/2012 (today). If I have one more positive day tomorrow, I will be positive for 30 consecutive days. [further review deleted]
>
> I will be preparing for tomorrow. I want to close at a perfect record. That will be a huge personal achievement for me.
>
> Fingers crossed. Focus on one good trade.

While this streak was impressive, your goal as a trader is to be as big as you can in your best setups and not to be profitable every day. This point was reemphasized to Pippen.

Some consistently profitable traders won't trade bigger until you push them. You must point out the harm, the risk, in not adding size when they can. But eventually, they get more comfortable with the added size and risk, particularly when they remind themselves that they now have trading skill that they have developed from a positive base. Most importantly, they have the trading setups to trade that led to their positive trading base.

Even after they begin to trade bigger, there can still be work to do focusing on getting even bigger. Pippen is making improvement, but he still needs to keep at it. See his e-mail here and notice in bold his readjusted emphasis:

> Hi Bella,
>
> I will be taking this July 4th week off to spend a week with my family back in California.
>
> Before I head to the airport, I'd like to work on my monthly review and send it out by tomorrow. There will be many things and goals for this earning season. For example, one of the major things I want to work on is to **get up to an uncomfortable size at least once a day on very good trades.** I've prepared my entire month and practiced on sizing. It is about time to put them to work while controlling the risks responsibly. I'm pumped!
>
> I wish you a wonderful holiday, and a wonderful time with your family. I will see you next week.

Pippen’s story also shows us the importance of traders fitting into a firm’s culture and a firm having a culture best for that trader.

Be in Your Right Culture

How you start and what you decide is the best way to begin your trading career are questions of culture. Our culture is that of working hard, building skill, and improving every day. We work as a team. South Africans call this Ubuntu: “I am what I am because of who we all are.” Nelson Mandela explained Ubuntu as follows:

> A traveler through a country would stop at a village and he didn’t have to ask for food or for water. Once he stops, the people give him food, entertain him. That is one aspect of Ubuntu, but it will have various aspects. Ubuntu does not mean that people should not enrich themselves. The question therefore is: Are you going to do so in order to enable the community around you to be able to improve?

Those who want to cut corners do not fit well in our culture. There is a dress code. Head out early without prior approval, and that is not permitted. If you do not buy into the work we believe is necessary to become a great trader, we are a bad fit for you. If you think you are going to be the best trader on our desk in month 3, we are a bad fit for you. Further, we identify those who do not fit our culture and manage them out of our firm.

To give you an example of how seriously we take our culture, let me introduce Talks a Good Game. This gentleman was an experienced trader of 9 years, who was a good friend of a core trader on our desk. In the past, he had surpassed P&L of 500k for the year. Talks a Good Game was talked to on several occasions about doing trade reviews to improve his trading game, as he was underperforming relative to his experience. After about the fifth failed attempt to get Talks a Good Game to fit into our culture and do the work necessary for him to improve, our floor manager let him go.

Talks a Good Game sent me a testy e-mail (edited):

> Maybe you had something out for me...Work ethic?
>
> You just let your best trader go.....
>
> I responded:

> I am sorry you are disappointed. Carlton was very fair with you. He gave you many chances to do the work that we think is important for our traders. For whatever reason, you could not sustain the energy to complete this work. And when you did the work, the effort was well beneath that of our other traders. It wasn't fair to you, to our traders, to our culture to continue.
>
> ...We were clear with what we expected from that first conversation I had with you. And you chose not to fit in to what we outlined as important.
>
> This was not a decision made by Carlton about your ability, what we think of you personally, or your trading prowess. This was a decision made strictly on culture. We value our culture. We feel everything starts there. We do not feel we have the infinite wisdom on the best culture. We respect those who feel ours is not the right culture for them. It is just our culture, you were not fitting in, and we felt it was best to move on.
>
> I wish you nothing but the best in the future.
>
> I look forward to you checking in to tell me you are crushing the markets.
>
> All the best,
>
> Mike

Many traders do not value or have not yet recognized the importance of a trading culture. Where is the best deal? What is the cheapest or easiest way into the world of prop trading? To survive in our business, you must develop rock star trading skills that are sustainable. That only happens through hard work, good coaching, support from others traders, and the help of a firm. Picking your best trading culture is perhaps your most important decision that will impact your trading future.

Pippen fit into our culture, and our culture was a best fit for him. He thrives in an environment where he is challenged to work harder. He sent me a review one day that was not complete. I responded:

> This is not an example of the type of review work I expect from you. You can do much better. This is not detailed enough.
>
> Your progress each day relies on detailed thought and review of your trading.

> Should you have been in NAV? SMG? REGN?
>
> Your progress starts with these reviews. Do better ones.

He sent another one that was worthy of our culture and his work ability. Some would have been angered by my calling them out. If your first reaction to getting criticized is to feel defensive, then you're not likely to last in our culture. As for Pippen, he took the feedback as a need to do better work...and he did that work.

A few months later, Pippen sent me an email sharing an awesome anecdote representing the importance of learning from our failures. The fact that he sent me this email showed he fit our culture. Pippen wrote:

> I was watching Spain vs. USA basketball on Sunday morning, and this short advertisement really tickled me. Every single day, there are countless people failing to make it to their dreams. But this little kid, called Timothy, was very special. His thinking process, and how he perceived the world, was so unique, so different from many other ordinary people. When he fell on the ground playing basketball, he laughed.
>
> His coach curiously asked him, "Why are you smiling?"
>
> Timothy answered, "I can only get better!"

Are You in the Right Culture as a Trader?

Do you think you should be doing better as a new or developing trader? The concerns of one SMB trader and my e-mail trail with him can provide some insight into the best start to your trading career:

> Bella,
>
> I've been thinking about what you said yesterday about being properly prepared. I have been getting better in my preparation and daily commitment to improving as a trader, but I feel like something is missing. I keep a detailed journal, have a detailed review at the end of the day, record my screen and go back to watch the trades that stood out to me, and watch them at the end of the day. I get Shark to send me his daily review so that I can see how he traded certain stocks because chances are I was in those same stocks and that helps a lot. I go over my review when I get home at night, but I am just getting frustrated with my improvement.

> It's not the fear of losing money or being wrong, but I am still struggling with several mental aspects that relate to trading. I have been talking to Shark about that, and he said the main thing that helped him was working on his psychology and how he read every book he could about that.
>
> I know that I am still new to this, but when I played basketball, it was usually a steady slow improvement and trading is very different. I can go from being super-disciplined one day and extremely confident to feeling unfocused and feel like I have no clue what the h*** I am doing the next. I am not tied up in my results by any means, but I believe that I should be doing better than I currently am.

I responded via an e-mail:

> So if we take basketball, which I love and have played most of my life, and then compare it to trading, you'll see a significant parallel. The hardest part about getting good at basketball when you are a kid is getting strong enough to really improve. When you get stronger, there are a lot more shots you can attempt and thus make. This opens up your game to much more opportunity. Same with trading.
>
> You are still in the getting strong stage.
>
> You cannot make enough shots yet.
>
> So to reach this analogous skill level with trading takes time—and screen time.
>
> How long have you been trading?
>
> I generally do not see much from a trader in their first four months relating to results. What I see is them working hard every day. What I see is them doing a daily review, going through their work, doing a PlayBook trade every day to archive, finding out which plays they like the most and why.

The new trader responded:

> That's a good way of putting it in a basketball sense. This is my third month to be trading actively. I position traded in college but had a very small account so was limited in capital and thus in the decisions I was making on a daily/weekly basis. I am not getting

discouraged in my results and am very aware that I have a long, long way to go before I can be upset with my P&L, but what I can be frustrated at is my lack of focus on certain trades and not being prepared at certain levels in stocks. My trading skills are very novice right now, but I know that if I put in the effort, every single day, day after day, for an extended period of time, the results will follow. I can barely hold a conversation with someone at the end of the day because I am so mentally wiped.

Bella:

Mainly the first four months is about culture. Do you fit in? Do you work? Do you ask good questions? We don't really care about your results.

New trader:

I absolutely love the environment and the people here. Everyone is so different, and I am beginning to notice everyone's style. I probably have one of the best seats in the house sitting next to GMan and Shark. Even though I have rarely taken any of GMan's trades, it is such a great learning process sitting next to him and seeing what he is in/why he is in it and running my trade ideas by him. It is really nice to be able to make money off of his ideas and him making money off of some of mine. That is what a prop desk is all about, helping each other make money and pushing each other to get better.

I like it when Shark tells me to hold something for the bigger move and wait because he expects this or that to happen. This I feel is really speeding up my learning curve. I sometimes wish my class had more trainees at my current skill level so we could discuss certain things we were doing well/struggling with at this stage but that might even be better for me in the long run to be thrown into the lion's den with the best traders. It's kinda like when you were growing up playing basketball with the kids who were older than you. I think that it's a good thing.

I am trying to ask as many questions as I can during the trading day. Iceman is really good at holding stocks for the bigger move; Ryan is very patient; when Prep has conviction in an idea, he has *conviction;* Shark is very good at being in the right stocks and

> always being in a stock for the real move no matter how many times it takes him to capture it with size. I am trying to see what everyone is best at so that I can ask them specific questions that are their strengths.

When you begin as a trader, it is very important to find the right culture for you. It is essential that you develop a personal work culture. You are not going to be any good in your first four months of trading. But you can develop good habits, learn a ton, develop parts of your PlayBook, gain screen time such that your tape reading skills improve, learn which stocks are not for you, find those whom you can learn from, and so on. Every step along the way in your trading career, please take the time to ask yourself: Am I in the right trading culture?

Seek the Master Coaches

Trading firms and even individual traders have to be cautious not to grow too quickly and with the wrong people. For example, there were two traders we had to manage out of the firm because they do not fit our culture. One of these traders was an experienced, profitable trader who would mess with morale, so we decided that he could no longer stay with us. All of us have a right to feel disappointed and frustrated, but when an individual is constantly complaining, then it's time for that person to leave. As a side note, we can all point to choppy or sluggish days, but when a person incessantly complains about the markets or your firm, he's really just vocalizing his own inadequacies or ineptitude. But as for traders who sincerely want to get better, they have to be sure that they have found a learning culture that is best for their long-term growth and that they personally have to spend a great deal of time reviewing their trading and making daily improvements.

I received an e-mail from an SMB reader that emphasizes just how fragile creating a trading culture can be for traders and the firm:

> Mr. Bellafiore,
>
> The reason for this e-mail is somewhat off the topic and a bit out of *The Talent Code* that I read a little while ago and I just realize how much SMB Capital could relate to the book. For example, many good prop firms have multiple offices in multiple cities and even countries. However, you guys being one of the best have only one.

> But I believe there is more to it and that is you truly understand how skill building works and how to ignite them. By having only one office, it gives traders a sense of scarcity. Therefore, they prepare and work hard every trading day so they don't get kicked out. Then, your well-known trading education and mentoring subconsciously deliver a message to the trader that it is not only about the money but rather they can learn a skill that will stick with them for the rest of their life. These two create a very powerful trigger that enables traders to pour vast amounts of energy into learning how to trade. A combination of scarcity, education, mentoring, unselfishness, and constantly stressing the importance of practice, it is no wonder you guys have a huge group of talented traders. Somewhat like the "Talent Hotbed" the author mentioned in the book and to my limited knowledge these advantages are more than any prop firms I know.
>
> But my question is this. Did you purposely structure your firm the way it is or is it really too much work to open another office? Oh and great job on your book; it was an awesome read.

I asked the opinion of the true expert on this subject: Dan Coyle, author of the must-read for all traders, *The Talent Code.* Dan generously shared via e-mail:

> Hey Mike,
>
> Great question.
>
> I think places that have had success in branch offices are ones that have an incredibly strong culture along with a fairly narrow skill they're teaching. Suzuki violin is probably the best example. He developed a curriculum, a detailed ladder of pieces, a nearly cult-like philosophy that he could use to teach more master teachers. Then it worked. Far more common, I think, are examples where branch offices fail because the assets that make the home office a success reside in the personality/character/drive of one person. It's all about the master coaches.

A good culture is hard to find. Search hard for it, and if you do find it, treat it as a gift.

Continuing on our theme of Pippen fitting our culture, he showed us another way how.

It’s Not How Much You Made, But How You Traded

After a trading close, Pippen sent me a daily review expressing an important trading principle: It’s not how much you made, but how you traded that matters most. In other words, do you only judge your trading by how much you have made after the close? Not Pippen, who is now first concerned with what he can control. Here is his review:

> Doesn’t matter that I’m green today; I really hated the way I traded. There were so many opportunities intraday. Today was a day to make $1,000 if I had traded properly. This was a day to turn a week into a very positive week if I had taken on some good risks. However, I did such a poor job today for not capitalizing on these opportunities. There are so many things to review from today. [review cut]

And then Pippen showed he totally had grasped this principle by sending me this must-read e-mail:

> I came across this picture while browsing on the Internet, which I thought was worth sharing. As shown on the pie chart, 90 percent of the population lives in the Comfort Zone. They are average, living a mediocre life. They are settling just for survival. They are depressed, tired, fearful, and often ask, “What if I can’t?” These descriptions are spot on.

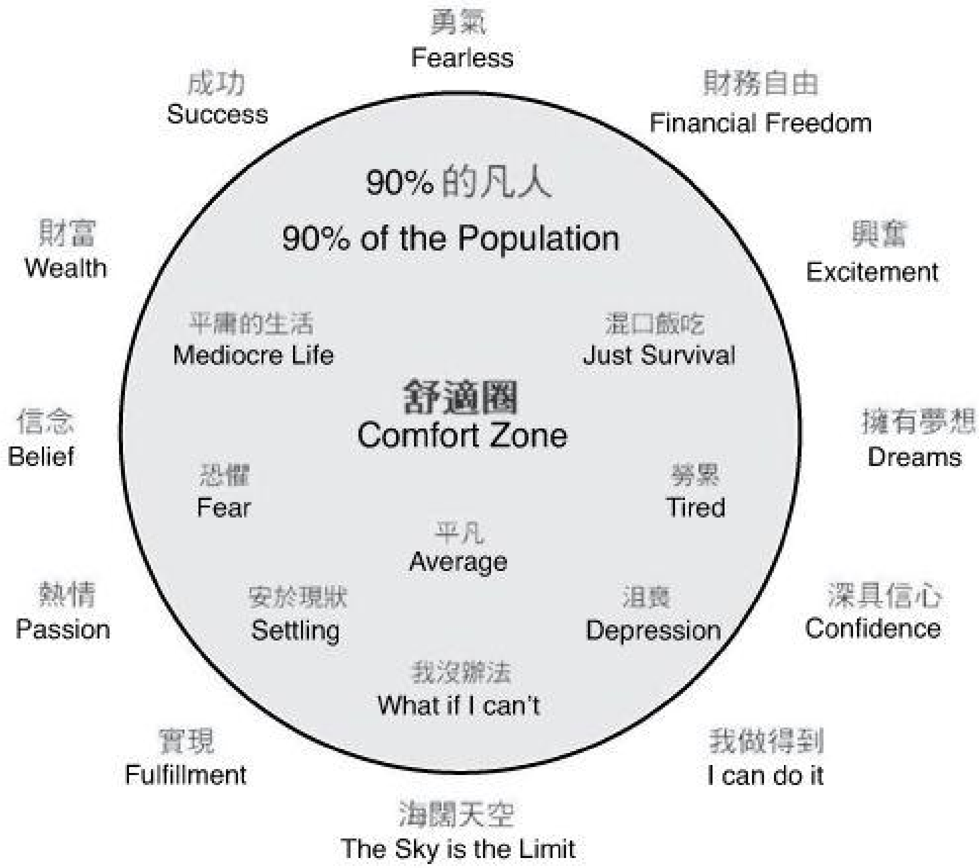

Figure 5.1

I'm going to be very honest, I identify myself with a couple descriptions mentioned above. Sometimes I'm fearful. Sometimes I doubt whether I can do it. But in the end, I managed to stay in the game and fought to conquer the biggest enemy, myself.

So, what do I need to do to get out of the 90 percent, and become the top 10 percent? What characteristics do they possess?

They are fearless. They have dreams. They are confident, always thinking "I can do it." The sky is their limit. They have belief and passion. They seek wealth, success, financial freedom, fulfillment, and excitement. What makes those 10 percent so special is that they're not mentally confined. They look to get better each day. They know they can get much better.

I'm still very young. My priority should be looking to learn as much as I can, not how much I can make in the next week or two. I wouldn't say I'm currently the 10 percent outside the 90 percent now. But I would say that I have improved a lot. Comparing myself with when I started, I have grown to be a better risk taker. I have strived to step outside of my comfort zone. I'm not settling like before. I'm more fearless than before. And I have bigger dreams than before.

Yet, I still have a lot to improve and accomplish. Every day is a learning day for me.

Earlier in the week, I continued to struggle. It wasn't that I was losing money. It's just that I couldn't get anything right with my trades. It was frustrating. However, things turned around on Thursday and Friday. There were stocks that actually traded cleanly and moved a lot for me to capitalize. Friday was by far one of the best days I have seen this year. I only had to be in one stock, just one stock, ADSK.

Initially, I was very doubtful whether I should trust the movements in ADSK. I was worried that the slippage could be extremely bad. 28.05 held. 28.10 held. 28.25 held like the buyer was so desperate for the stock. After seeing that ADSK had proven itself worthy, I began to take on more risk and trusted it more. 28.25 was where ADSK unusually held the bid. I got up to 1,000 shares above 28.30, but ADSK quickly dropped down to 28.25. Below that 28.25, I was thinking 28.10. 1,000 shares would be around $150 of risk. I quickly lightened up down to 500 shares and watched how ADSK behaved. ADSK never dropped that 28.25 and proceeded to go to 31 very quickly.

There were good and bad things about this trade from 28.25. The good was I recognized the risk below 28.25. The bad was I should have just manned up and got long 2,000 shares after seeing how ridiculous 28.25 was buying on the bid. It is hard for me to judge how big I should be. I was concerned about the risk below that 25c. If he dropped, I'm 50 percent done for the day. It was hard. That 25c really got hit pretty hard, and it was really tough to know how big I should have been at that place.

In the end, I chose to keep 500 shares against that 25c buyer and captured really good moves in ADSK. I was able to quickly accumulate $500 for the first 30 minutes of the opening drive. This was by far the best open I have ever traded.

ADSK was pretty much the only stock I traded on Friday. I even skipped lunch because I knew there was a lot of money to be made in ADSK. I did not want to miss a chance to make my entire week. I stayed in front of my PC and traded ADSK until 4 p.m.

The entire firm, including me, was killing the stock. I was up to my personal best by 1 p.m. I was so tempted to just close out and call it a day. But I did not. I chose to risk more and tried to hold ADSK for more. I was thinking $2,000. It did not work, but I felt it was the right thing to do.

I was a little bit depressed that I gave back my personal best. But honestly, what is that $250 going to mean to me in my trading career? I think I made the right choice for not settling. Now I know I'm capable of a new personal best. One day I'm sure that that new personal best will come.

Pippen fully grasped what we believe, which is his daily calling to do the right thing was paramount over money. In return, this made him better.

Your Job Is to Make Good Trades

We created the daily trading review and a monthly review for our traders. But then Pippen created the weekly trading review. One Sunday he sent me his weekly trading review, and it seemed like such a good idea that we asked others to do it as well. This is a good example of building a culture of daily improvement and then having those who buy into your culture make things better. You leverage the talent from those who buy into your culture and build an environment far superior to what you could have built.

When you develop the right culture, you set up an infrastructure where traders can help themselves and those around them. Pippen sent me this wonderful lesson from Scotty Brooks, coach of the NBA Oklahoma Thunder, that helped him develop a better perspective to trade bigger. This e-mail was then shared with the trading desk to help others trade bigger. Pippen's e-mail:

I was watching Oklahoma Thunder vs. San Antonio Spurs last night. It was such a competitive and thrilling game. The Thunder had Kevin Durant and Russell Westbrook for a pick and roll, while San Antonio had superb passing skills. The Thunder had James Harden for controlling the ball, while San Antonio had Manu Ginobili who pretty much made the difference for the Spurs' in game 1. It was very hard to tell which team could win the fourth quarter given the competitiveness of both teams.

During halftime, Thunders coach Scott Brooks mentioned something to his players that really caught my attention. Brooks said, "Keep making the good plays and taking the right shots. I don't care if you score or not. Keep making them." This mindset is exactly what professional traders should also possess. Keep making the right plays. Keep at it. The results do not matter as long as you are making the right plays.

If it is a $100 play, go for 200–300 shares. If it is a $300 play, risk more, and go for 500–600 shares. If it is a $500–$1,000 play, it is very crucial to risk more and a make bigger-sized play. Go for 1,000–1,500 shares. The results honestly do not matter. Risking bigger on better plays is good trading.

I went to the desk on Friday. A lot of people took the day off due to the long weekend Memorial holiday. Only TO, Shark, Ryan, Prep, and me, along with a couple traders, were on the desk. The day was long. Nothing was moving. By 11 a.m. I had only traded three tickets. SPY was stuck in a 50c range for most of the day.

Around 12 p.m., a good setup in VIP caught everyone's attention. VIP is broken long term and short term. VIP consolidated at the low. It was a great trade to put on 1,000 shares short. But I only took 500 shares short. I didn't think it could move. It was Friday. It was noon. I didn't think it could move, so I only put on 500 shares of risk.

VIP turned out to be the best stock for the day. But I only managed to catch a nice move with 500 shares.

This is the mindset I need to learn. "Keeping making the good plays and taking the right shots. I don't care if it works or not. Keep taking them." The results do not matter. VIP was a trade to risk 1,000 shares. I need to recognize that.

Well said, Pippen.

Did You Learn as Much as Pippen Did Last Week?

Pippen quickly became one of my new mentees to watch. Because he is a student of elite performance, there is so much right about the following e-mail. The work. The concentration on improvement. The self-reflection. The detail to his learning. The depth of it. New and developing traders too often seek to copy the trading of that big trader. It would be wise for you to copy the work, mindset, and competitiveness of this new trader if your goal is to become that big trader. Also, it is a great example of the weekly review that Pippen created.

> Hi Bella,
>
> The following is my weekly review from October 3, 2011 to October 7, 2011:
>
> Friday was one of my better days in terms of consistency and probability. After reviewing my trading, I noticed several things I did differently:
>
> Have a time stop: Scratch a trade that does not work for me after a given period of time.
>
> Be ultra-selective: Trade only radar/in-play stocks, which haven't moved out of their ATRs, and still have room to go.
>
> Cover risks: Initiate with two lots on higher R/R setups, and covering risks with one lot into the next up move/down move.
>
> Internalize "second rat gets the cheese": It is okay to miss the first 20c; you don't have to be the first one in. Let them do the battle, confirm the price action, and then I enter with more confidence.
>
> Of course, one-day data cannot serve as a conclusion on my results, but they will be something to keep in mind for the following weeks.
>
> Several things I picked up this week, and things to remind myself in my trading game:
>
> If you get stopped out a lot in a stock, ask what's the real stop? Is your bias wrong?
>
> Always know what time big/important economic numbers come out.

It is not 2008 now. Know where has the market come from, and what is your risk/reward in today's market.

If you see SPY touching too many prices, and you weren't making money on both longs and shorts, you should slow down and see where the market now is in longer time frame.

Consider how you could have traded the bounce better.

If you hit the decrementing big bids as a momentum lot, and buyer rebids, you have to get out right away. You can easily be squeezed out by algo.

To add to above, you should always have a time stop. You do not treat momentum lot as trade to hold, and set a stop too far from the entry.

To add to above, stops for momentum lot if time stops, the stock slows, or ticks against you.

To add to above, unless it really moves away quickly from your entry, then you can consider putting a price stop.

Quality not quantity. The bigger day will be where you crush your setups in one or two plays.

Don't overtrade levels during midday. Algo can easily outplay you with above/below program. Rather, look for a level to hold during mid day.

If you miss a trade, you miss a grade. It is worse if you get in at a bad price, and you couldn't manage your R/R.

When playing a slow grind up, you really need to find a great price to reduce your stress level. You can easily get shaken out trying to play a breakout. The better play is to get positioned against a good stop.

To add to above, the better way to trade is taking profits into the up moves and down moves.

To add to above, remember, there were too many occasions where I was 25c in the money, trying to hold my slow grinding position, and eventually had my positions went against me as time passed by.

Know ATR. Be careful when stock does 2x ATR already. Reevaluate your R/R.

You should look for longer consolidation to initiate trade if move is already extended.

Don’t trade everything. Don’t take every trade. Focus on better setups.

Don’t trade SPY unless it’s a big level. It’s difficult to fight with programs with ticks. Trade SDS instead for areas of support/resistance.

Don’t be too tight on good plays.

Put more risks on higher probability trades, which have all the checks on your side—trend, tape, technical, fundamental.

Put less room on lower probability trades.

Get better in your PlayBook setups!

Be careful of whole number trap. Let them have the first 10c–20c. You want to short below the real level, or long above the real level.

Patience—wait for your setup. You don’t have to be the first one in.

Instead of getting in/out, and risking so many 2c, 5c, 6c, find a best spot and risk 20c (real stop) on better setups.

Don’t trade against a trend thinking you’re fading resistance. You want to see failure at that level first, unless it’s a big, big level.

Sometimes if you like a price, you can wait for it to stabilize before placing a bid/offer. You’ll get more info and confirmation. Or you can put on a very small position as a feeler.

Don’t trade minor levels in every stock. Trade clearer levels in better stocks, with fresh order flow.

You need to find something that can trend for the rest of the day. Be selective on stocks. Spend your attention on this. Don’t be in a stock if you just want to make 30c–40c.

To add to above, when you have an idea for an entry, ask: “Is it worth your time for that trade? Is it going to trend?”

In an uptrending market, shorts are scalps until market proves it’s a downtrend.

> Trading is not about trading every minute from 9:30 a.m. to 4:00 p.m. Trading is about taking good trades. If there's no good trades, don't overtrade. You'll be wasting your time, energy, and money. Do not be stupid.
>
> To add to above, do not be delusional and think that you're making one good trade. Think twice on what kind of trade you're making. Is it really One Good Trade?

To close our introduction of Pippen, let me tell you about one good trade I made with him. It was my best trade of the year.

One Good Trade

Sitting in my office talking firm financials, Steve lifted his chin, unconcerned about future cash flow for the first time in 18 months for one reason. "This is the best group of young traders we have ever developed," trumpeted Steve. "They are better than the traders we developed through '09. They hold stocks longer. They believe in our culture. They are more skilled."

I responded, "That is because we make them do PlayBook trades every day. They have internalized better the setups that make the most sense to them. They can trade bigger than our guys in the past because they have setups that they can trade on a longer time frame."

This same day Pippen knocked on my door and asked to start receiving a draw as he was running low on funds. I told him I needed to ask Steve. We checked his numbers, and at that time he wasn't making enough to cover his draw. We had noticed him doing all the things he was asked to do and then more. I stopped my financial analysis on the spot, realizing how foolish it was. Two minutes after he had left, I called him back into my office. "Your draw is approved," I said. Since this time, he has never caused a month of financial strain on the firm and only gotten better. But besides that, Pippen is the trader you back and help more if necessary.

In 2010–2011, our firm got a lot smaller than it had been in 2008–2009. At the same time, it got a lot better. We made more money, Steve and I enjoyed going to work more, and our traders were more appreciative of what we offered.

Pippen is one of our better young traders. He made himself the trader he is by buying into a learning culture, being an all-star listener, learning from his buddy TO and others, following the perfect path to trader profitability, and doing all the work necessary to develop his trading PlayBook.

Traders like Pippen inspire partners to make their firms better. I hope he inspires you to take the right path to consistently profitable, and in an affable and polite way while you are at it. What can I do to make my firm better so he has the more that he deserves? First, I pushed him, and now he pushes me. I am really proud of him and to run a firm that attracts such a quality person. I will end with this suggestion for a star start to your trading career: Choose the path of Pippen!

Let’s take a look together at the historic IPO of Facebook and a trade Pippen made in it.

FB IPO Support Play

Long at IPO price with buyers on the tape

Trader: Pippen

May 18, 2012

Big Picture

- SPY had sold off five straight days from 137 to 131, which could attract some speculation money coming into the market with FB IPO.
- FB IPO is very important to the market because this means a large influx of new money into Wall Street from the investors.

Intraday Fundamentals

- Facebook was one of the biggest and most exciting IPOs.
- Facebook IPO priced at $38/share.
- Facebook IPO scheduled to open at 11 a.m., 05/18/2012.
- Facebook is unlike many other IPOs (ZNGA, QPSA, etc.). This is an actual company that many are involved in.
- It is extremely important for the underwriters (Morgan Stanley) to protect $38/share IPO price level for a successful IPO.

• There's a very low percentage that the underwriters would not protect $38 price level on the first day.

• How successful the FB IPO was will mean a lot to underwriters' reputation in the future.

The IPO Trade

• Buy in front of IPO price.

• Buy new highs. (Keep track of important levels.)

• Buy important technical levels.

• IPOs trade more cleanly—few price points.

• Principles apply to all IPO trades globally; human psychology will never change!

Technical Analysis

Reading the Tape

Trade Management

Trade Review

Good:

1. Looking back, I want to get really big at $38, but I felt I made the right choice. I couldn't get too big because I did not know the liquidity below $38, and there's the risk of someone clipping all the size before me being able to get out.

2. I managed to take some sales around $42 into the spikes.

Improvements:

1. I was too light into $40 and did not have enough size from $40 to $42.

2. I was too big above 41.25 and risking more than I should. Instead, I should wait and then be big if FB shows that it can hold above $42.

3. I should have been bigger at $38 IPO price level, knowing that this is an important level that FB has to defend. I should take on more risk and let FB prove me wrong.

Gratitude

- The most historic IPO since GOOG.
- Did you trade the FB IPO?
- You were fortunate enough to trade it!
- How cool is that?
- Learn to be grateful for the opportunity to trade—Dr. Andrew Menaker.

Next is a trading discussion on how to trade this IPO FB opportunity with Pippen and my desk.

From the Training Room: Trading an IPO (FB) with Pippen

The FB IPO trading session was a historic event, which traders will remember forever. This trade takes you through that day!

Bella: I got an e-mail from someone in this room who I may mention or may not. His e-mail triggered for me a really important trading fundamental about our preparation that we should discuss. On Friday, we were discussing how to trade Facebook (FB). Today, before the open, we were thinking about trading FB and some other social media stocks. Coming into today, what were the two Big Picture thoughts that you needed to think about this weekend to be properly prepared to trade today's open?

(Someone raises his hand.)

SMB trader: If the market bounces and if FB holds above $38.

Bella *(smiling):* My e-mail right before this review might have helped you with that answer. So this weekend, where did you guys go out? Lucy's?

(Traders talking and laughing about Lucy's.)

Bella: So look, you guys are at Lucy's, and one of the things you should be doing is talking about trades for Monday. Unless you get distracted by someone who should distract you and you need to take care of that. For any tips on that, please see Iceman.

(Traders laughing.)

We have been down 11 out of 12 days? We had been strong for a while and now we are incredibly weak. You need to be thinking about whether we are going to bounce.

(Bella raising his voice.)

> *When playing a bounce, I wait for SPY to bottom and then hold higher. After SPY holds higher I load up in my market stocks. It takes time to become a good bounce trader.*

It's not good enough to sit at your desk on Monday, scrambling to figure out what to trade and do. Gentlemen, that's not good enough! Over the weekend, you *must* be thinking: If we bounce, what would a bounce look like? Above what S&P futures price will you get long market stocks? And which ones? And at what prices? Above what SPY price? And you must not stop there guys.

What kind of an open makes it more likely we will bounce? What if we open, tank, and this appears like a blow-off bottom? What is we open and hold above an important technical level in the market? And then gentlemen, you should be mapping out, the stocks you would trade, the prices you would trade them at for each possible market iteration. You should be prepared to trade each market iteration. Ideas like if ADSK holds above 30 and SPY holds above *x*, I will get long ADSK. These ideas should be written down, over the weekend, and sit closely next to you on your trading desk. It's called preparation. You win the game with your preparation before the game is played.

The most money for a bounce is trading multiple market stocks, and you must prepare for that scenario. I have said this at least 30 times in this room. Market stocks are traded on market days. A bounce is a market day. So maybe it's CAT, maybe it's IBM, maybe it's AAPL, maybe it's JPM, maybe it's a couple of those stocks, maybe it's C, maybe it's NFLX. Whatever stocks you think you can trade the best, over the weekend, you must rip through the charts; and find prices that offer an excellent risk/reward if we bounce. Rip through a lot of charts, and prepare for multiple scenarios.

Why? Perhaps a JPM isn't setting up at a good price for a bounce, but maybe an FCX is, or a NFLX is. Okay?

In this market, the best bounce candidate is Apple.

> *Add some high beta stocks to your trading, such as AAPL, GOOG, LNKD. You will take some losses first but then be in position for serious gains after you master their movement.*

It's awesome to see some guys learning to trade AAPL because that time and money investment was rewarded with opportunity today. I know DB took a couple of nice losses in Apple learning to trade it, but this is the day where those paper cuts pay dividends. Today you get in there, and AAPL went up 30 points. Not only did it go up 30 points, it went up 30 points above a pretty tight consolidation chart pattern with the market bouncing, right?

(Bella smiling.) That is an amazing opportunity there. And TO sent me an e-mail over the weekend. I did say that I may use the person's name. *(Bella smirking and looking at TO.)* Is it okay that I use your name?

TO: Well, you already used it.

(Traders laughing.)

Bella: Yeah, that is a good point TO. But if it's not good, I actually won't use your name anymore.

TO: Well it's too late now Bella. You already did. But that's fine. Not that I had any choice.

(*Traders laughing.*)

Bella: TO e-mailed me on Friday, and he said it actually after the close in our discussion on Friday too, we were overly bullish on FB. And we should've known that FB wasn't going to be that good because social media stocks were crap going into FB.

TO: I didn't say that. I said that we could only make money going long FB, but if it's not a good IPO, there should be an insurance plan, Plan B.

> *At times trading rules are not clear. Some firms make aggressive interpretations of a rule, and others can be more conservative, causing a disparity with short locates.*

Bella: I was on the phone, not too long ago, with a firm that was able to short FB because they have a relationship with Goldman. And they were able to short FB today, which we aren't sure was legal or not. There might be a situation where Goldman is giving out shorts, and they shouldn't have been. Or Goldman has it right and others are a few steps behind. We will learn more soon. But I was literally on the phone with the firm, a solid prop firm, and they were able to short FB. Steve got pissed and asked, how can you short FB? Compliance at our BD is telling us we cannot in the first three days. (Goldman had it right by the way.)

(Traders mumbling.)

Bella: Sorry to incorrectly paraphrase you. But you said we should have been more prepared if FB did not hold its IPO price?

(*Bella looking at TO.*) Right?

I agree with you. You must consider what you are going to do if FB is really weak? Are you going to trade Groupon, Zynga, or NetEase? Are you going to trade that FriendFinder that you guys crushed the other day? I said that months ago, in this very room, after LinkedIn came public.

I said the LNKD IPO is not going to be the last opportunity you have to trade social media stocks. I urged for you to go make a list of all the social media stocks and start learning about them, start reading about them. I advised you to learn the social media stocks, the good from the bad. They are not all the same. And there is a market principle to trade hot sectors to game. Sometimes the Tier1 hot sector stocks go up. Sometimes five of the Tier1 hot sector stocks go up and three of them don't. Sometimes Tier3 hot sector stocks go up after the Tier2 hot sector stocks go up. Sometimes the Tier4 hot sector stocks go up, and you have to be very careful about intraday reversals because they are normally garbage stocks.

> *Generally hot sectors move like this: The Tier1 stocks go up, then the Tier2, then the Tier3, and then the pretenders, Tier4. Strong sectors tend to be hot for a three to four day period and then rest. Tier4 stocks can be faded for reversal trades.*

This is important: Hot sector patterns develop. There are divergences with these different types of stocks in these hot sectors. You must learn which social media stocks are crap and which ones are awesome. Or maybe there is an opportunity where all of them are overhyped and ready for a decline. Patterns will form for hot sector stocks. Your job is to learn those patterns.

TO was the first person to develop a list, a list of social media stocks for him to follow. The reason I know that is because I used *his list* when I was preparing for a presentation in Singapore to share a list of the most popular social media stocks with them.

I was invited to talk about opportunities in the States for Singapore investors. At the time social media stocks were all the buzz as the FB IPO was coming. Here's what I found most interesting about TO's comments:

1. TO was right.

2. TO did the work that enabled him to be right.

TO started doing the work months ago. He actually started putting together a list of social media stocks, and he started following them every day so that when this FB opportunity came out, which the whole Street's been waiting for, he was able to say, Bella, we should actually be ready for the bearish case. He could make this critique because of the work he's been doing.

Steve wrote an article over the weekend stating that trading is not rocket science. It's not that difficult to understand the difference between the Tier1 and the Tier4 stocks in a sector.

(Long pause.)

If you did not come to work today with written notes, all the stocks you were going to trade if the market bounced, ripped through 150 charts over the weekend of your favorite market stocks, you are not a professional trader.

(*Long pause.*)

If you haven't thought about trading the bear side of this social media opportunity, and you haven't been following this sector for the last six months, you are not a professional trader.

It's unacceptable to walk onto our trading desk if you haven't done those things. And you have to keep doing this kind of preparation. The market doesn't have to bounce like it bounced today. Apple doesn't have to go up 30 points. There's going to be years when we are going to sit there, and the bounce of Apple is only 5 points. *(Bella now raising his voice.)* Guys, you have to make the most of these opportunities!

On Monday, Carlton and I were sitting in our office going over the numbers for everyone in the firm. There are a dozen newer guys who keep getting better, and we see this in their numbers. There are six newer guys who are kind of up and down, and I can see they can get better. There are some guys whose numbers are terrible; they are never going to be good.

For the newer guys, let me give you some advice. There are three guys in this firm who really do a lot of work. If I was a young trader, I would just follow Shark wherever he went. If I was a first year, I would just follow TO wherever TO went. Shark has done the most work over the last couple of years. Every day I get a detailed report of how he traded. He's always working on something. He's always trying to get better. Every day the work is there. I don't even remember where he went to school, but I'm pretty sure he didn't go to an Ivy League school. Look how he works. He is going to continue getting better. TO came up with this list of social media stocks, and Pippen came up with the weekly review. I don't think we even had a weekly review until Pippen, and TO made the daily review better. I think Shark made it better first, and TO threw Tradervue in and made that better.

If you didn't make enough money today, I promise you it's because you didn't do enough work before today to be prepared. You did not do the work that allowed you to believe you deserved to make more. It's not that you are not smart enough. It's not that you are not good enough. You guys have very advanced and developed trading skills. You were taught at a very high level that very few people on the Street will ever obtain just because of the way we trade. We trade so actively you have to be better than 99 percent of the traders on the Street. You would be amazed if you talk to some professional traders who have no idea how to enter positions at a good price. It's embarrassing. You guys actually learn how to trade.

(Bella speaking intensely.)

I was talking to a trader on the desk today and he was all impressed with himself for having what he termed "a good day." Bull****, you are having a good day! The market bounced a ton, and you are trying to make a few thousand dollars? Come on. I know many of you are new traders. But seriously, there's real money out there to make. Just to be clear, you should expect better from yourself. If you do not know this yet yourself, then I will tell you. You guys are so much better than this. This is a wonderful core group of guys. Maybe the best we have ever developed. You can do better.

You have the opportunity, and that's the good thing. You guys do the work. You will get better. You will start to make more money. You will. This is not rocket science. You just have to keep rehearsing, preparing, and practicing every day.

(There is a long pause.)

(Bella smiles.) All right, let's go over this Facebook (FB) trade. So this is Facebook. This is Friday. This is a trading session you will never forget. Pippen, the floor is yours.

Pippen: SPY went from 137 to 131, which could attract some money into the market, into the FB IPO. The IPO is really important for the market because that means a lot of money is going to come into the market for this IPO.

Bella: I actually can't think of a bigger IPO that's come to the market since Google (August of 2004 at $85). I still remember that IPO, where I was sitting and the excitement of that day. There was no SMB then. It was just Steve and me trading our money at some BD, which I think is no longer in business. This was a day of history for us as traders. It was a trading day never to forget.

So FB is a very important IPO. One very important thing about this IPO is it had been priced very aggressively. Morgan Stanley was trying to get FB as much as possible out of the deal, leaving FB very little margin for error to trade above its IPO price. We are not fundamental analysts, but that's the long risk you need to understand. Pippen, what were the Intraday Fundamentals?

Pippen: Facebook is one of the biggest IPOs out there that everyone's been waiting for. The Facebook IPO is priced at $38/share. Facebook's IPO is scheduled to open at 11 a.m. on Friday. This is very different from other IPOs like ZNGA or QPSA. This is a Tier1 deal for an actual company that a lot of people are involved in. The $38 price can be very important for the underwriters like Morgan Stanley.

> *The IPO price is a huge support level when trading any IPO. We used 38 as a huge support level for Facebook. The underwriters must support this price or else the deal they lead will be seen as a failure. This decreases the chances of future investment banking deal flow.*

Bella: Let's slow down. It's embarrassing and bad for future business for the underwriters if FB gets below the IPO price because now their clients are underwater. FB below 38 may harm the reputation of the underwriters, particularly the lead underwriter in Morgan. Second, there are new concerns on the Street about Facebook. It's a great platform that a lot of people use, except for me. Is there anyone in this room who doesn't use Facebook?

(Someone raises his hand.)

SMB trader: I don't, Bella.

Bella: So, you and me can hang out after this meeting and talk about who is less tech savvy. Cool?

(Traders laughing.)

Bella: Look, I don't understand why people want to look at pictures of other people they haven't seen in years, but apparently that is just me. Do you use it, Pippen? So everybody uses it. It's obviously an amazing company, but their challenge is what?

SMB trader: They don't make that much money.

Bella: Specifically, what is their biggest challenge?

SMB trader: How to get people to spend their money.

Bella: Their specific challenge is advertising revenue. Just before this, GM pulled their $10 million ad account because they didn't see a lot of bang for the buck. It is not clear that FB is going to make a lot of money through ad revenue.

FB and GOOG employ very different models. FB put up ads on their site like GOOG, but it is not clear these ads with be as effective as Google's. When you use Google, you are in an active search. You are looking for something very specific with the keywords you choose with your search. [So, for example, you might do a GOOG search for "trader training." You will see SMB pop up on the free search and then ads for trading educators.] When you are logged onto Facebook, some algorithms are unleashed to figure out what you might want to buy based on your past behavior. You are not actively searching for what you want to buy. You are just looking at the page of one of your buddies. This is a big distinction between Facebook's and Google's effectiveness to help sell product, and thus their ability to sell ad space.

> *Strategy for trading an IPO: If it holds above the IPO price, buy. If it holds above the IPO price and then holds higher, buy more.*
>
> *If the stock forms a bull flag above the IPO price, and you can control your risk if the stock fails, buy.*
>
> *If a stock approaches the IPO price, buy in front of that price. Sell if the stock trades below the IPO price. Sell into a strong up move if the IPO price holds.*
>
> *Observe prices where more volume is done. These are your first technical levels. Trade off of these technical levels, as they are very significant with IPOs.*

Bella: So that's one of the issues: Are they going to increase their ad revenue? The stock would go up if they start to solve this problem. The stock will go down if they don't. There are other challenges, like how the platform will play on mobile devices, but I just wanted to illustrate one and how that might affect trading in FB. Know the story for your stocks and what may move them.

Pippen: This is the Technical Analysis for Facebook on Friday. As you can see on the chart, the key level is $38 (see Figure 5.2). My plan is to buy Facebook in front of the IPO price at $38, if I see a buyer on the tape.

Figure 5.2

Bella: My first buy is right here at 42 *(Bella pointing to 42 on the FB chart)*. FB opens at $43, showing strength as it opens *above* the IPO price. We are playing the short-term momentum with an IPO and not where we think the stock might trade in 6 months. This IPO is different from LinkedIn in that there was much more liquidity. [FB had a float of 421 million shares, while LNKD 7.84 million shares.] FB pulled back to $42. I saw some buying on the bid, and I bought some. At this moment it is above the IPO price, the short-term momentum is up, and there is support on the bid at 42. At this moment in time, it is a long using a momentum IPO strategy.

What must I consider before getting long at 42?

(*Bella waits for an answer*.)

SMB trader: Where can you get out if 42 drops the bid.

Bella: Yes, very good. If 42 drops the bid, where can I get out. There were a whole bunch of problems with Nasdaq trading data. Nasdaq is getting a lot of heat about the data being messed up for this IPO. We are trading FB. You couldn't tell where anything was. It was really fast. I just bought 300 shares near 42 because the data was so jumbled. I just "wanted to be in it" in case it exploded. Hot IPOs can get irrational and explode to the upside. You buy just a little bit because you don't know where you can get out if the 42 bid drops. FB dropped $42. I exited. It was pretty easy to exit. FB went to $41, and I bought 300 shares again. There was buying again at 41, so I bought; 41 dropped, so I hit the bid. At $40, I bought a little bit more this time, and it held there for a little bit longer. And I actually bought a little bit more.

My trading plan was to buy a lot if FB actually held higher. I just "want to be in it" and get a feel for it. We couldn't short it at the time. All we could do is play FB on the long side, so if it holds the bid nicely, I would try to buy in front of that bid.

I was trading for a hot IPO pattern. Maybe this will be a great IPO. If the trade started to work, I would have bought more and held for a significant up move. This is not buy and sell 50 cents higher. This is buy and hold for a potential explosive up move based on the way hot IPOs can trade. Who knows which way it's going to go, but that's how I was managing the position. So I bought a bit more at $40. You were actually able to overlap and hit out with the ECN NASD pretty easily at this point. The more comfortable I felt that I could get out if 40 dropped, the more time FB would trade sideways; then the bigger I was getting. First I needed to test whether I could control my risk. As I learned I could control my risk better, I got bigger.

When FB got below $40, I got out at about 94 cents. It was really easy to get out. I probably should have been bigger there at $40 because it was so easy to exit. Remember that we are just trading a pattern, The Hot IPO Momentum Trade. You do not want to be the guy on the desk who could have bought at 40, watching FB trade at 60 by the end of the day. We are not trying to be right. This pattern is this: Long in front of intraday support and hold for a potential explosive move, and out below the intraday support. So the risk/reward is 5–25 cents on the downside depending on where you can exit and points to the upside. I like this risk/reward.

Now FB pulls in to the IPO price of $38. What must we ask at this level?

SMB trader: If FB drops 38, where can we exit?

Bella: Yes, very nice.

I bought in front of 38 after this level held. I had a conversation with myself about how much I bought at this level. I was not very nice to myself.

(Traders laugh.)

I should have been much bigger. How much did you buy down here Pippen?

Pippen: I only had Tier1 because I wasn't sure what would happen below $38 (see Figure 5.3). I saw size on tape. Everyone saw size on the Level II, but I wasn't sure what would happen if FB traded below that price. There's a chance that's someone would clip that bid, and you wouldn't be able to get out. So I only had Tier1 at this price.

Figure 5.3

Bella: So your thinking is, "What's the likelihood that it's going to drop the IPO price and if that happens, where can I get out?" Actually, I think I should've been bigger because

- It was the first time down to the IPO price.
- They bought it on the bid.
- It had been easy to exit on the way down.

• The underwriters should try and support this level at least the first few times at this price.

And then what happened? It went up. IPOs don't have a lot of price points, so they can be easier to trade. Their technical levels are more important than regular stocks. It started to work for you? Where did you think the stock would go to?

Pippen: $40.

Bella: At least $40. I'm thinking of $40 or $42. So I was slow to sell, and it went up to $42. Please, tell me what you did.

Pippen: I was at Tier1 here in front of $38. I actually sold some in front of $39 and some more at 40, and I was down to 50 percent of my position at $40. I tried to buy back, but I missed the spike down buying opportunity, so I only had 50 percent from what I bought at $38 (Figure 5.3).

Bella: What percentage of your position do you want to sell at $39 and $40? I agree with you that you should be at 50 percent of your initial position at $40 because that's your first resistance level. That's your first level because that was the most important nearest level that we saw on the way down. The trading in FB gave us this important price points. 42 dollars is the next important level above 40.

Those sales at 39 are not right. You are just selling to make yourself feel comfortable, and that is not a good reason to sell. If you are going to take the risk of buying at $38, you have to do a good job of banking the reward and selling at the right price points. And you should determine what percentage of your position makes sense for you to sell at this next resistance level of 40.

I definitely think it makes sense for you to take some off in front of $40. I actually can't give you an argument for having more than 50 percent. The question is how much to buy above $40, for a push to 42. That's for you to decide.

Pippen: So I bought some back between $40.00 and $40.50 and made some spreads. I was holding 50 percent as my core from $38.00 for a big move. I bought more at $41.00 (Figure 5.3).

Bella: Let's take a step back. TO, I think you made the spread a bunch of times, right?

TO: Yes, a bunch. More than anyone here.

Trade around your core only if you are an advanced trader. If a newb, just sit and manage your core.

Bella: Showoff *(Bella smiling and looking at TO)!* That is very advanced trading. Excellent. When you see a held bid at $40, you can buy in front of $40 and put it up at 13–19 cents to make the spread and then immediately rebid in front of $40. If you get hit on the bid, then immediately re-offer in the 13–19 cents again. Keep your core position for a bigger play. But buying some extra shares and making the spread is an excellent trading technique to make cash flow. It's called trading. Use your superior trading skills to your advantage here. If you do this, you will guarantee making money in FB even if it your bigger trade does not work. You trade around your core position by making cash flow trades. Other people would call that a scalp.

Pippen: There were multiple occasions where I made 20–25 cents for scalps. This covered my risk with my core position. There's one point around here (2 p.m. area), between $40.80 and $41.50, where I get big (Figure 5.3).

You actually have to determine the proper reward to determine the risk/reward in a trade. Our guys had the reward all wrong.

Bella: That's where I wanted to bang my head on the desk because you guys were making up the reward on that trade. You were making up the reward for that trade. Do you guys understand that? You were making up the reward for that trade.

The problem is at this consolidation between $40.80 and $41.50, there was not the reward that you guys were claiming. What I heard from the desk was if it gets above $41.25, it's going to explode. I scolded the desk that you guys were making up that reward, while you were chirping that nonsense. It's not going to explode until FB gets above $42, our next important technical level. So the reason for that is IPOs really respect levels and that $42 is a really important level. We learn that by watching the price action after it opens and noticing a first battle there at 42. When FB opened up, there was buying there, but that buyer lost. That became an intraday technical level or point of interest that you have to remember.

FB wasn't going to explode and go to the prices you guys were talking about until it got above 42. It was not going to 45 like you were chirping until it got above 42. So, I love the aggressiveness. I love the thought about whether to get long above this consolidation. Nice job communicating with each other on the desk about this opportunity. You just need some more domain knowledge about how IPOs trade.

What did you have to see to add above 41.25? So if you are Tier1 or Tier2, at 40.80, I still don't like that trade, but okay let's review your thinking from here. When you add above 41.25, what did you need to see to add above that intraday level?

Pippen: There should be a buyer above 41.25 on the bid.

Shark: Or we want to see FB just move away from that price of 41.25 showing us its strength.

> *A sign of strength for a stock is when it gets above resistance and then moves away from this price quickly.*

Bella: So you want to see FB get above 41.25 and explode away from that price. This explosion away from this price is a signal of strength for FB. Or you want to see FB clearly holding above 41.25. If you do not see that, you really should exit the extra shares you are buying above 41.25. And it really didn't make much sense to me to say I'm going to buy 41.27 or 41.30 and give it a stop below 41 with an upside of resistance at 42 for FB. That's not a great play.

(Trader raises his hand.)

Bella: Yes.

Shark: I didn't pay through 41.25, but I did see something subtle on the tape. FB traded between 80c and 25c three times. But then FB tested 41 and held cleanly above 41. Although this was only a subtle signal there, I thought it was kind of significant.

Bella: I like you trying to look for clues on the tape. What is one thought that mitigates your idea?

(Traders mumbling.)

Bella: I like your idea. I like that. What I like about that idea is that if I see something subtle, maybe that's a way to get really, really big, or bigger, in your position. But then keeping your tights *very* stops.

(Traders laughing.)

SMB traders: Stops tight, Bella.

Bella *(laughing):* Keeping your tights really short.

(Traders laughing as Bella continues to mangle the English language.)

Bella *(laughing at himself):* So keeping your stops really tight. That's fine...if you see something clearly different on the tape, just keep your stops tight. Why?

> *SMB conspiracy theory states that when many of our traders are big in the same trade it never works.*

SMB trader: Because the dropout is going to happen. *(Traders laughing.)*

Bella: One is a dropout may happen. But two, there is something about your analysis that you may not be considering. Anyone?

SMB trader: I think that's the play that now you are saying that if it's holding above 41 you have to stick to your guns.

Bella: But think about that rationally. What about the data you have should breed skepticism?

SMB trader: FB was in an upswing for ten minutes as opposed to it failed miserably at a bunch of levels previously.

(Bella looking out at the traders waiting for the right answer.)

Bella: There's so much volume in FB. It's hard to glean something significant from the tape. It is easy to think you saw something significant.

Who knows what people are doing. Maybe some big seller went to the bathroom; now it's going up, and now they came back from the bathroom...I don't know. All right, so FB got above 41.25, then it kind of went up but didn't get above 42. Then they dropped FB out below that 40.80 intraday support consolidation level that you guys all were in love with, and so FB went back to 40. So you guys all got screwed?

(Traders laughing.)

Bella: The bid dropped 40.80. It was hard to get out, right?

Pippen: I actually took a sale in front of the 42 level.

(Traders laughing.)

Bella: You sold the top.

Pippen: 84...41.84...

Bella: You did.

Pippen: I did.

SMB trader: It dropped a point right after. *(Traders laughing.)*

Bella: That's the highest print, Pippen. Did you get flat?

Pippen: No, but I did sell most.

Bella: Because you wanted it to be above 42 before getting very big?

Pippen: I mean the add above 41.25 was just a momentum scalp for me.

Bella: Okay, good. Wow! Excellent trading.

Pippen: The real trade was above 42.

Bella: Okay, good. That's the way to do it. You play the momentum [this is a Scalp Momentum Trade for advanced intraday traders] above 25 cents, and then take off most in front of 42....So 40.80 dropped, everyone hit the bids, then the next level is 40; that's the technical level, right?

SMB traders: Yeah.

> *When a stock fails at technical support, we assume it will continue to the next technical support area.*

Bella: And then you can buy some there. I have no problem with that. But it didn't work. FB went down to 38 again. Let's talk about that. Once FB gets below 40, I want you thinking it's most likely going to 38, right? 38 is the next technical level. FB goes to 38 again, and it's very late in the day. The thing I didn't like about it going to 38 was what?

SMB trader: It holds lower every time.

> *It is better for a stock to drop to 38, an important support level, quickly and on low volume than to slowly find this level if you want to get long at 38.*

Bella: It slowly gets to 38. I hate that. It was slowly holding lower and spending time close to 38 as opposed to dropping there quickly on low volume. It was at 38, and it was getting late in the day. They were whaling the bids.

Pippen: They were hitting the bids so hard.

Prep: I thought the bids were going to drop.

Bella: I mean they were crushing those bids. They were hitting them so hard, you thought the 38 bids would finally drop. But FB held the 38. It's a buy there, right? I remember tweeting I was buying again for a potential end of the day move to 40.

FB went up 40 cents. You could've made cash flow trades buying it at 38 and selling it at 40 cents, like TO was doing, making the spread. You definitely can make the spread there. But FB didn't go up to 40.

Just a quick thought about this. FB really could've gone up to 40 in the last minute. With an IPO play like this, FB really can do that. You guys have not seen this yet. Just like you have not seen a hot IPO hold 42 and then be 60 by the end of the day and then three months later 25. These plays can happen. After you see them a few times, you will understand the importance of just "wanting to be in the stock" at times. So just keep that in mind. Above but near 38, it's not a great setup, but it's still a long. 38 is still a big level. Today some new prices were developed as it traded terribly. How much was it down today?

SMB trader: Eleven percent.

> *If an IPO trades below its IPO price, we short the stock and wait for the stock to show us it has found a bottom.*

Bella: And if you could have shorted it, you would've shorted it below 38, right? FB can now trade as low as until it shows you the downtrend has been broken. Now we focus on the short side right?

SMB Traders: Yeah.

Bella: All right, any questions about trading this IPO?

> *Always remember it's a privilege to trade. Be grateful for every trading day.*

Bella: Good. That was fun, right? Look, this is important; be grateful for this trading opportunity. You just got to trade the most historic IPO since Google. And that's really cool. There's still plenty of money in these social media stocks, plenty of money in FB going forward. LinkedIn had offered us tons of opportunities; even today it was a great play, right? GRPN and ZNGA are setting up for some excellent shorting opportunities. So learn these stocks, and along the way start to decode the social media trading patterns.

One day someone is going to ask you about the FB IPO, and you are going to be able to say, "Yeah, I traded the FB IPO." Be grateful for the opportunity to trade something so historic. All right, thanks guys.

(Bella turns around and leaves the room.)

Postscript

I have noticed especially of late that Pippen can flat out trade. He can momentum trade anything with the best of the intraday traders. I have been encouraging him to build from this strength and step into more momentum opportunities, even though most on the desk avoid them. Although most cannot intraday momentum trade of late because of HFTs, he can. He processes the tape and makes good decisions so fast that he can excel at this strategy. It’s very impressive. And he does it all, with never a banging of the desk or complaint about the firm, market, or trader mate, and always with graciousness.

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6. Special Projects: Get Ready to Trade Pro

I am sitting in a conference room in the American Southwest with my partner Steve Spencer. Actually, it’s a massive boardroom, and we’re negotiating a potential *joint venture* (JV) between SMB and a hedge fund. Three on their side, two on ours. The former star trader and now owner/partner of the hedge fund has instructed outside consultants to build an elaborate financial model to determine his potential profit and risk for the JV. The financial model is displayed on a projection screen, which we all now stare at. He asks, “So, what is your success rate for training new traders?”

We almost never made the meeting. Even worse, we almost didn’t make the meeting with proper dress attire. Our Delta flight through Atlanta was delayed, and after landing, Steve and I had 15 minutes to board our connecting flight. Of course, 15 minutes to board is 14 minutes of margin for Steve, who prides himself on efficiency. We caught the flight, but then landed on that island, Business Travelers’ Hell. There was no space for our carry-on luggage in the overhead bins. Awesome. Next, an attendant came running toward us to “help,” evading passengers like a hurdling O.J. Simpson in those old Hertz commercials.

Knowing Steve as well as I do, since we were 5 years old, I could read his mind: “This is not a good idea, Bella. We cannot give up our bags to this strange person.” Like hostages being held captive by airline regulations and their enforcement staff, sometimes referred to as flight attendants, there appeared to be no exit. We handed over the bags. Steve’s mood immediately soured to exasperation. He went to a dark place, convinced that our bags would not meet us at our destination. I didn’t really care, as a lack of a connection would mean Steve mocking the attendant and airline industry for the rest of the weekend. Steve can be quite entertaining when it comes to lampooning incompetence.

Our connecting flight landed, and we headed for baggage claim. After witnessing other people getting their bags for 20 minutes, Steve and I looked at each other as if the joke were on us. Were there hidden cameras somewhere and a TV host about to burst out laughing at this orchestrated prank? Steve’s brain was practically exploding at the ineptitude of that flight attendant. “Don’t say you are going to help if you are going to make things worse,” snapped Steve.

Eventually, we found that place where you yell at the airline because your bags didn’t arrive and pleaded for a possible quick fix since we had a business meeting in the morning and no clothes. This would give new meaning to the expression “the emperor has no clothes.” Here, I learned something new. The agent explained we could replace our business attire with new purchases at a nearby retailer, keep our receipts, and mail them in for a redemption. Hmm. I didn’t know the airlines did that for you.

So, the next morning we opened Neiman Marcus, found two sales associates, asked them to find us some slacks and shirts, and retired to the private-shopping dressing room. What would you expect from two busy partners? Steve has a taste for finer clothes, so Delta was in some trouble here. I ended up with an all black Armani Exchange dress shirt, and Steve found some fancy Hugo Boss slacks and a designer shirt. Delta caught a break when he couldn’t quite pull the trigger on the Ferragamos that the “cute” southern sales associate was pushing.

In the boardroom, and picking at my too tight, new, European sport shirt, I answered, “If you hire ten of the right people, three will do very well, and two others will have a chance. One of those two might make it. Five will not be worth much attention because they will not do the work required by the market.”

So who are those “right” people? How do we get more people succeeding as pro traders who enter the field?

Do You Fail as a Trader, or Do You Learn It Is Not Your Passion?

An e-mail:

> Morning Bella,
>
> I’ll try to keep this brief because I know you’re extremely busy. I just finished reading *Talent Is Overrated* by Geoff Colvin along with *Mindset* by Carol Dweck and was interested to know what drives you and Steve to be successful traders and teachers. Where does your passion for trading come from? Where did it start?

Colvin talks about passion initially coming from an extrinsic factor but over time it turns into an intrinsic motivator.

From page 204 of Colvin's book: "What would cause you to do the enormous work necessary to be a top CEO, Wall Street trader, jazz pianist, courtroom lawyer, or anything else? Would anything? The answers depend on your answers to two basic questions: What do you really want? And what do you really believe?" That second question is easily answered by your mindset. Do you have a growth mindset? If so, then you believe with "deliberate practice" you can improve dramatically and achieve your goals. If you have a fixed mindset, well, we know where that leads.

I was watching your StockTwits videos, and Steve mentioned that the whole concept of why you guys started SMB as a desk was because you can make more money working as a group sharing information and working together opposed to trading/working alone.

I responded:

My passion today is to build training methods to shorten the learning curve of new traders, build our desk, expand our training, and share what the market has taught me. This means building SMBU, mentoring passionate trainees, and to write/blog. There is another great book I recommend: *Flow,* by Mihaly Csikszentmihalyi.

When you are doing what you love, time stands still. Often I awake on a Saturday morning and immediately start writing a blog. I do not want to watch TV. I do not want to eat breakfast. I want to write. I can work for an hour on a trading topic I want to share with the trading community and lose all track of time. When I was younger, I could shoot baskets for hours outdoors in the Long Island winter chill and lose all track of time. When I am thinking of a new way to teach traders, a better way, I can get lost in this mental challenge. Elite performers refer to this state as *being present.* James Lipton teaches this state of present to his student actors at the Actors Studio. When I start to think about expanding our training to another product, I get lost in my thoughts. None of this is work to me. There is a peace that

> overcomes me when I am so deep in thought. It is a state of flow. It's the deepest form of happiness that we can reach, according to Professor Csikszentmihalyi.
>
> The truth is that trading takes a lot of work. Staying till 7 p.m. is hard to do every day. But TO, one of our developing traders, does it. It's a grind to write a detailed trading review after the close every day. But Shark does it. It's hard work to crunch your trading stats in depth everyday. But GMan does it and has been doing it for more than five years. Are these traders doing hard work or are they just in a state of flow, doing work that connects with something inside of them?
>
> I had a conversation with a new trainee recently who emphatically claimed, "Bella, I really want to get better." I asked him to develop a plan of attack on a specific adjustment we identified. He followed up with a two-paragraph e-mail. This new trader will never make it. This work product is short of the work necessary to succeed. It is not that this trainee is lazy or a bad person. Trading is just not his thing. There is no flow for him when he studies trading.

What can be confusing is that a new trader may think he is working hard. And then he really isn't. People who work hard think about their passion all the time because that is what they want to do. As I write, Kevin Durant is about to face LeBron James in the NBA Finals. Our two best young basketball stars head to head perhaps since Larry Bird and Magic Johnson. Do you think Durant has any struggle daydreaming/visualizing possessions against LeBron? If you cannot daydream about trading, how can you expect to be an elite trader?

We run an internship program year round for aspiring traders. We teach them how to trade, and they give us a peek at their interest in trading. I can tell within two minutes if interns are sincerely interested in trading or just filling in a few lines on their resume. How? I ask them to run the charts during a tradecast. The nontraders don't know the symbols. My asking for Ren Ren (stock symbol RENN) to be displayed on our 60-inch flat screen in our training room leaves them confused. Zynga (stock symbol ZNGA) brings a blank stare to their face and maybe a "what stock?" Actually we ought to use this as a test to hire traders. Instead of the Q&A interview, we should have them sit in the back of our training room and man the charts during a tradecast. We could find the trader fakers within two symbol requests.

We spend too much time in the trader blogosphere discussing why traders fail, with a thousand theses abounding. I am told anecdotally that there is way too much wasted negativity about this across trading forums. Pro traders tell me these forums are disproportionately visited by failed traders or frustrated wannabe traders who mostly leave an oasis of misinformation about trader development. But did they really fail or just learn that trading was not their passion?

If I teach a new trader and he does not make it, this should be his exit (and this actually happened):

There is a knock at the door to my office.

“Come in.”

“Bella, do you have a minute?” says one of the smartest new traders in his class and someone I have been working with very closely for the past two months, since I see he is so close to turning the corner to consistently profitable trader. In fact on some opens, I stand behind him and coach him in real-time offering critical feedback of his trading. At the moment he is mostly flat, but with his sharp mind, and pretty solid work ethic, it is my sense he could be very good.

“Yeah, shoot.”

“I want to thank you for everything, but it is time for me to move on. Trading is not my passion. I am going to go work at a start-up. This is what I really want to do.”

Okay, I can live with that. I gave it my best effort. He gave it his best effort and found out this wasn’t what he wanted to do. Trading history will record him as a failed trader. But was he?

Trading is a craft. One that you work at for years to develop. Thing is, few are willing to do the work required to build the skill to become a great trader. That is no issue to me. It is just not for them. But please, can we stop kidding people into thinking pro trading as your job can be for the masses? It’s not. It’s for those who, for whatever reason, have an unexplainable inner desire to work at this silly game we call trading.

So you think you have a passion for trading? What can you do to improve your chances to become a great trader? And what can young traders do to advance their chances of success that too few are doing? We explore these questions and challenge college curriculums while we are at it in this chapter.

The GM Test

I am one of many guys you might pitch for your "dream job" as a proprietary trader. But you know this whole trader-recruiting thing is inverted. You should not be pitching me. My desk and others like mine should be pitching you. But you need to do some work before this would happen. Like start developing a track record now!

During a recent *MoneyShow* interview at the Las Vegas Trader's Expo at the Paris Hotel, I revealed a test for new trader hires. I call it the GM Test.

Imagine that I am the general manager of the NY Knicks, and I tell you this story about a ballplayer's pitch to draft him in the first round. Sitting in my palatial office overlooking the court at Madison Square Garden, this hoopster said, "I really think I would like to play basketball professionally. I have been playing a lot of pickup basketball with my buddies from Beer Pong Dorm. We just won the school intramural championship. I have been hitting the weight room and put on a few pounds of muscle with Myoplex Mass Gain. I even cut back on the Pabst Blue Ribbon, ditched this psycho foreign exchange student, and am thinking I would be a nice pick for you in the first round."

What would you think? You would think I was soon to be the ex-GM of the NY Knicks. You think this is an absurd analogy? This is what we do in the prop-trading world. In our prop-trading world, some bright, ambitious, sometimes suit-challenged candidate sits in offices all across the country and declares his love of trading. His proof? Wait for it....

"I watch CNBC. I read the *Wall Street Journal*. I have made a few trades in my [*insert discount broker*] account."

Respectfully, this is insufficient preparation for your life passion.

Now, if I were the GM of the Knicks considering a potential draft choice, I could have watched you play in high school, Amateur Athletic Union (AAU) ball, college; had you in for drills; thrown you into one-on-one and three-on-three scrimmages with like talent; done interviews; checked your body fat; and so on. In trading parlance, I would have data to *model your potential* as a pro.

Think of just the commitment an elite basketball player makes to a portion of his high school playing. Being a key player on an elite AAU basketball team can be a demanding task on and off the court. While the AAU season is very quiet during the regular high school basketball season due to school sports, teams become extremely active from March to June, even playing throughout the summer. While the benefits of playing on a high-caliber team are extraordinary, several large commitments must be met. The cost to be on a team can be well over $1,000, not including travel, food, and hotels. Travel alone can be the greatest expenditure, with elite teams even flying to a tournament or two. The largest commitment, however, is time. Several of the teams practice at least twice a week and usually will have two or three tournaments a month on the weekends. Even college programs have more data about a player than prop firms of a new trader.

I used to take a lunch/workout break at the Sports Club/LA when I traded at E*TRADE’s prop desk on 57th and Lexington. During the summer and right before the draft, you can find some hopeful first-rounders working on their game at this gym. The basketball courts of this multilevel facility are open to all members. You can be shooting hoops a basket away from future stars and watch them work out. I have seen Mike Dunleavy, Sr., the former NBA coach and GM of the Los Angeles Clippers, scouting some of these hopefuls. I watched Ben Gordon prepare here daily before he was drafted by the Chicago Bulls in 2004 as the third overall pick. These hoops stars all have personal coaches, and they’re watched by their agents, who prepare them for individual workouts with NBA squads.

The effort exerted by these pro prospects during these training sessions is memorable. They lose a bucket of sweat per workout. The shape these guys are in, the skill, the speed, the explosiveness. It’s beautiful to watch, art in creation.

There is meaningful and substantial data available that I could study as the GM of the Knicks to predict how you will do in the future. In *MoneyBall*, by the wonderful finance writer Michael Lewis, we learn that some Major League Baseball teams shun drafting high school athletes because this playing data is too limited to make an investment in a player. And with canned, “I watch CNBC” answers, what can I model about your ability to trade pro? More to the point, what can you predict about your trading pro potential?

Trading is a skill. You were not born a great trader. The insightful books on elite performance such as *Talent Is Overrated*, *The Talent Cod*e, and *Outliers* teach us that to become great at anything requires purposeful practice over an extended period of time. In *The Inner Voice of Trading*, Michael Martin writes it takes a person about eight years to become an expert trader. In 2009, serial money-making intraday trader Marc Sperling stopped by our shared and overly crowded conference room at our former location, 417 5th Avenue, to address our desk. Self-actualizing Marc exclaimed he had finally surpassed the 10,000th hour rule as a trader, so he was now an expert. After all the money he had pulled out of the market before this talk, he only now was finally comfortable claiming expert status. You need screen time to become a Consistently Profitable Trader.

Trading is a performance activity for which we can find learning opportunities for traders from other sports. Using the GM Test, I ask potential future trading candidates: Where is your trading track record? Whenever I have a bully pulpit speaking to new or wannabe traders, I say the same thing to all of them: Start trading now!

In that spirit, I penned a blog for SMBU playfully envisioning the future stars of trading. This blog introduces some themes that we will expand upon in this chapter: the need to start trading early, the need for better trader education for college students, and the need to recognize trading as a performance sport that should require early skill development to best prepare for the profession.

First Team Wall Street: The Next Generation

Aug 21, 2010 | By Bella

Give me six hours to chop down a tree, and I will spend the first four sharpening the axe.—Abraham Lincoln

An extensive FX training program is being created for a college investment club as I write. The creator is a junior in college. A bright young trader visited SMB for a tradecast from the Midwest during a summer vacation. He had just graduated high school. I get an e-mail every week from a developing trader who is killing the market this year. Not a month has passed without him netting 30K. He is entering his senior year at college. @zmoose12 has caught the eye of the best @stocktwits and will be attending Bentley

College in the fall. @thearmotrader, a senior at UCLA, just spent part of the summer training with us and is one of the rising stars in the trading community, already with his own blog on StockTwits. *And* watch out for @ramblin_rebel13, who runs the Georgia Tech Investment Club.

I have written extensively and repeatedly that we have learned from the trilogy of performance literature *The Talent Code*, *Talent Is Overrated,* and *Outliers*. The collective wisdom of these three books is that no one becomes great at anything unless they engage in purposeful practice for many years at their craft. For example, many people incorrectly think that the Beatles were an instant sensation when they arrived in the States, when in fact they had nearly 10,000 hours of hard work behind them playing in clubs throughout Liverpool and Hamburg. Bill Gates is another one: By the time he dropped out of Harvard, he was already a stud programmer because of all the time he had put in writing code since he was an early teen. If you want a tongue lashing from me, go ahead and sit in on one of our trading film sessions with a month of experience and tell me you "just had a feeling the stock was going up." If you want to lose my attention during an interview, tell me that you have a good feel for the market even though you have never placed a trade. Don't misunderstand. You can indeed have a feel for the market. It's called trading intuition, but you only develop this intuition after years of screen time.

Tiger Woods started playing golf when he was 2 years old. Andre Agassi was starved of a childhood save hitting tennis balls. LeBron James played more basketball before entering the NBA with AAU, camps, and an ambitious high school travel schedule than others already in the league. Why do newbies try to pick up our game of trading without any experience, without any trading skills, right after college? How silly would you think LeBron if he showed up at Danny Ferry's office, former GM of the Cleveland Cavaliers, requesting an interview for an NBA spot without ever having played? How about Agassi knocking on Phil Knight's door, founder and chairman of Nike (NKE), talking a Nike endorsement without the skill to hit a backhand?

Just in case you missed the other thousand times I have written or said this: Trading is a skill that must be learned and honed. You must develop a PlayBook of trading patterns that makes the most sense to you. To become great at these setups takes experience, practice, and a love for your game. Only then can you join First Team Wall Street.

Future trading stars should start trading in high school with a small size and an emphasis on risk management. They should be scouring the blogosphere for knowledge. They should laugh with an @thereformedbroker's irreverent post; learn technical analysis from YouTube trading king @alphatrends; peek in at a prop firm at SMBU blog; argue under their breath at a call by @DougKass, DM @afraidtotrade about the structure of a trading day; read every last post from TraderFeed.com to develop their mental game or classics like *Reminiscences of a Stock Operator;* and ping trading questions to pros like @thekirkreport (we will respond). They should work to build their trading PlayBook like @speerothekid has done before graduation.

Further, future traders should attend universities with trading labs. During the summers, they should study at the highest quality trading education schools. They should dabble in different products and markets. Dr. Steenbarger famously wrote that a new trader should trade all products first before deciding on one. Future traders should intern at prop firms and institutional banks. A Harvard sophomore took our five-week summer training class, loved it, and then asked me what else he should do before graduation. I counseled, "Next check out what it is like at a big bank." Most importantly, future traders should develop a track record.

After developing a track record, then you will have the power to pick where you want to trade, what you want to trade and how big, and not have to rely on someone like me to let you in the door. You will have developed your trading skills so you can become the next king on the Street.

In June 2011, SMB started its summer training class with ten students. As I write, the top three performers traded in college.

They started faster, performed better, learned more, added more to the desk, and were most enjoyable to coach.

Although my thoughts in the First Team Wall Street sidebar were just an early vision and a hope for the future of Wall Street, this is all starting to happen, for a variety of reasons. I see a rise of college traders—and with that a potential disruption in college curriculums.

The Rise of College Traders

SMB had five traders for our June class who already had proven active trading records in college. We get e-mails from traders making serious money consistently and yet are in college. I was on the phone with a college trader who thought last year's $3,000 gain owed him entrance into my firm. I explained as politely as possible, and not wanting to harm the young man's confidence, that I would be impressed if that number was $10,000 a month given the results from other college traders sent to me. I have never seen results like this before. And do you see how many young traders are out there writing awesome blogs?

I wrote an article recently about the thirst for trading education at universities, and my inbox has just been littered with very solid college traders sharing their stories. I love it! Who says you cannot start trading in college? How is that any different from Cam Newton, star college football player, working eight hours a day on his quarterback skills to gain a top draft spot? Or Jimmer Fredette, leading scorer in all of NCAA Division I basketball during his senior season and winner of every major National Player of the Year honor, including the Wooden Award, the Naismith Award, the Adolph Rupp Trophy, and the Oscar Robertson Trophy, working hours every day on his basketball skills? Which takes us to my next blog post.

Stealing from Jimmer Fredette

Jan 27, 2011 | By Bella

Jimmer Fredette is considered one of the leading candidates to be named Naismith College Player of the Year. I watched him play last night against SDSU. What a treat to watch someone with such advanced skill compete in an important game. Recently I caught

> his interview on *PTI* and was struck by his training practices to become one of the country's elite basketball players.
>
> Here are two things you may not have known about Fredette. One, his brother and Jimmer developed a unique drill of dribbling in the dark to improve his handle. Two, his brother organized games against prison inmates, which helped make him more "mentally tough." Lastly, I like this: a "contract" that Jimmer signed as a teenager:
>
>> I___________________ will make all necessary and proper sacrifices to reach my ultimate goal of making it to the NBA.
>>
>> _________________ _______________________
>>
>> Name (Signature)   Witness (Signature)
>
> This contract was taped above his bed and he looked at it every night before he went to bed, and as he fell asleep he visualized himself playing in the NBA.
>
> My plain advice: Consider stealing some of Jimmer's training techniques for your trading.

I sent a recent blog I wrote on the thirst for more university trader education to a host of colleges, some with whom I am very friendly. Not one school showed any interest in improving its trading education. I know of a few students working behind the scenes to make this happen and have hit some early roadblocks. @zmoose12 is very close to making this happen at Bentley University, home of one of the first trading labs in U.S. education history. Iceman, who runs our college training program, has made significant inroads at some schools, getting college credit for our summer trader training program.

Now I understand that most schools are facing very real cuts in all departments, which means selling a new educational program can be very difficult in this environment of cutting. I was a trustee at the University of Connecticut and remember sitting with Dr. Mark Emmert, now president of the NCAA, when he was the chancellor at UConn, explaining the difficult decisions he was forced to make on budgeting. I was pressing Dr. Emmert to allocate some more money to a project at UConn Law School, which he thought was a terrific idea. The problem was he had ten other as terrific ideas that also deserved funding. So I left that lunch without a commitment for UConn Law School but promised my vote for UConn moving to Division I Football. Wait, how did that happen? I went to get money, didn't get it, and left giving Dr. Emmert the vote he wanted. Well, it was a nice lunch and chat anyway.

Budget decisions at universities are a tough job! All of that does not take away the tremendous new interest in trading from college students and need for them to succeed upon graduation at this profession. Demand always creates change. I see a potential disruption in college curriculums if higher education does not figure out how to service the growing demand for trader training.

If Colleges Do Not Adapt, the Market Will Extract the Demand

Peter Thiel, cofounder of PayPal and angel investor in Facebook, recently made a new investment. The Thiel Fellowship announced it would be awarding $100,000 each to 20 kids under the age of 20 to drop out of college and start their own businesses. Mr. Thiel is on record that a college degree isn't worth the giant debt burden with which it now comes. Thiel sees higher education in a "bubble."

"I believe you have a bubble whenever you have something that's overvalued and intensely believed," Mr. Thiel said. "In education, you have this clear price escalation without incredible improvement in the product. At the same time you have this incredible intensity of belief that this is what people have to do. In that way it seems very similar in some ways to the housing bubble and the tech bubble." Bill Gates, for one, predicts a time when top-notch Web-based degrees will be available for $2,000. Will colleges be forced to adapt to a more world-specific curriculum? Are certain performance fields like coding, entrepreneurship, business, and trading going to disrupt traditional education with new learning models?

John Carney, senior editor at CNBC.com and former editor of Clusterstock.com and DealBreaker.com, brought to light the idea that graduating from college isn't a prerequisite for future success in a recent article. The technology space is littered with examples of uber-rich dropouts. Tech moguls such as Paul Allen, cofounder of Microsoft; Michael Dell, founder of Dell, Inc.; Larry Ellison, founder of Oracle; and Steve Jobs, founder of Apple, Inc., never received degrees from their respective colleges. Leaving just a semester after starting, Jobs was considered one of

America’s most successful and important business leaders before his passing. The recent social media boom has created a new generation of tech dropouts: David Karp, founder of Tumblr; Kevin Rose, founder of Digg; Mike Hudack, founder of blip.tv; and hoodie protagonist Mark Zuckerberg, founder of a company you may have heard about, Facebook. Other notable dropouts not specifically in the tech space include Richard Branson, founder of the Virgin brand; Ralph Lauren, founder of Polo Ralph Lauren; and Jack Taylor, founder of Rent-A-Car. None of them seem to be sweating that piece of paper that hangs on a wall or is somewhere buried in a box.

Though Mr. Thiel’s grant comes with no strings attached, the young individuals are still provided mentoring that is essential to success. As Thiel’s Fellowship Web site states, “They are mentored by our network of visionary thinkers, investors, scientists, and entrepreneurs, who provide guidance and business connections that can’t be replicated in any classroom.”

National sports associations and Mr. Thiel aren’t the only organizations these days encouraging undergraduates to leave college early. The boom in technology and social media (think Instagram and Facebook) has left myriad companies yearning for young and bright talent. As early as their freshman year, students are being plied with internships or even full-time offers that include fat signing bonuses and other lucrative perks. Starting salaries for these graduates and nongraduates range from $75K to $100K, plus signing bonuses of $5,000 to $15,000. Amazon recently offered a Brown student $5,300 a month plus a one-time $3,000 housing stipend for a summer internship. She passed for a better offer.

Companies and alumni in this space are treating the students who decide to stay and graduate like rock stars, providing freebies, cash, and prizes. Some tech superstars can command a 1 percent equity stake of the company. Even after Facebook’s disastrous IPO, which Spencer characterized as botched badly by JPMorgan and Nasdaq on Fox Business TV, many students still see a giant upside in the tech space.

James Altucher, a former contributing writer for the *Financial Times* and TheStreet.com; founder of Reset, Inc.; cofounder of StockPickr; and managing director for Formula Capital, has written extensively on why a young person ought to skip college. First, Mr. Altucher considers the rising cost of a college education. With the average cost of college around $104,000, he explains that even though college graduates make an estimated

$800K more than noncollege graduates, one can make nearly $600K more over a 50-year time frame by earning 5 percent yearly on your money if that money is invested instead of being spent on college. Next, Mr. Altucher cites the lack of experience that young people receive while at college. By forgoing college and starting your own business, you learn how to develop ideas that will be accepted by others, sell them, build and execute on an idea, delegate and manage, and most important, eat what you kill. Mr. Altucher suggests instead to a youngster: Travel the world, spend time being creative, start writing, learn how to communicate with people, work in a charity, and master a sport or game (like trading?).

While I am not advocating skipping college to turn pro trader, we should at least place pressure on universities to adapt. As higher education may be in a bubble, as college students are thirsting for better trading education, as trading is a performance activity like professional sports, as traders should develop a trading track record early, colleges need to offer a better trading curriculum or risk losing traders from their rolls. Perhaps a Steve Cohen, of SAC Capital, will pull a Peter Thiel and start grabbing young traders out of college. Perhaps other hedge funds will then follow.

Professional trading firms in our space can help a little. SMBU initiated a summer training program for college underclassmen during a five-week summer session. There will be two such sessions. Steve and I allow active college traders access to our trading tools and our SMB a.m. meeting for free. College writers should continue to open up their new blogs and share. College traders should continue to create trading groups at their schools, following the work at Penn State, Bentley, Baruch, Indiana University, and Georgia Tech.

“I do not have enough money to start trading.”

Trading coach Dr. Brett Steenbarger, before leaving the trading blogosphere for a top U.S. hedge fund, used to saturate his must-read TraderFeed blog with the importance of working on your trading game. Paper trade. Trade a small account. No matter. Just trade. Steenbarger concluded that if trading is your passion, there is no excuse in this hyperconnected online age to not develop a track record.

If you need some inspiration, meet Cortez, Travis, and another Cortez.

Make It Happen!

Cortez, a nontraditional college student, was not a fan of the misinformation about trading disseminated on his campus. He was equally disappointed with the sparse selection of trading lectures at his school. You might say he was downright p*****. So he made it happen. He reached out to a prop firm (SMB), convinced one of its partners to visit (okay, me) and address some future traders, organized multiple student organizations to spread the word of a visiting trader (not easy), and hit up some internal departments (harder).

I would imagine many Ivy League students have had similar thoughts (complaints?). I have always found the trading community to be very generous. So you have a choice: You can do nothing, or you can be like Cortez. I gave a visiting lecture to some future traders from Rutgers–Newark. Make it happen!

On November 1, 2010, a community of young traders launched a promising new trading blog, Young Guns Trading. Make it happen!

Last year, I Skyped with a student at *University of California, Irvine* (UCI) who helped grow the school's trading community to 70+. Make it happen!

Three students have sent me information on their impressive student trading organizations and asked us to visit, which we will. Make it happen!

One SMB reader, while still in college, used to send me e-mails every month on his progress. The young man is absolutely getting better every month as a profitable, self-sustaining trader, not yet 22. Make it happen!

Be Like Travis

I talked with a recent college graduate the other day. Nice kid. Well-spoken. Polite. From one of those upper-middle-class, lacrosse-playing Long Island towns. After one minute on the phone, I could tell he was not interested in trading. I cut off the call after five minutes. At dinner later that night, my friend gave me grief about not at least interviewing the kid. I suppose that was a good point, but let me be clear, the purpose would have just been to build this recent graduate's interviewing skills. Because there was not going to be a second round at my prop firm. This young man had no business being on a trading floor, considering being on a trading floor, or hoping to be on a trading floor. He was not interested in trading.

How did I know? Because he didn't do anything, hadn't done anything, and wasn't thinking of doing anything to learn about trading. I got the old, I-find-myself-watching-CNBC answer to the question of an example of how he was passionate about trading. Please. Come up with a better answer if you want a job at a prop desk.

And by the way, I banned CNBC from our trading desk because it stresses me out. (Well, only temporarily as some of our guys insisted it be turned back on.) All that breaking news, breaking stories, and loudness. Bloomberg TV is much more soothing and civilized. Bloomberg TV is like reading a great book on a pristine beach. CNBC is like getting caught in midtown traffic with a cab driver who won't stop talking at you. Please, do not sit in front of me and use the old CNBC line when I have a pile of candidates who have traded, read trading blogs, and can reference one of my previous posts.

And then there is Travis. Travis is in high school. He and a friend came to visit SMB to learn more about trading. Let me repeat: He is in high school. His friend already trades. Travis and his friend flew from Middle America, over a holiday weekend, to learn more about trading. Most kids his age are masterminding new ways to score beer.

Come to think of it, how the h*** did Travis get invited to one of our tradecasts if he was in high school? Carlton! That must have taken some maneuvering. How would Travis even know what SMB was? How would he know whom to contact at our firm to get an invite? Carlton! I need talk to our floor manager.

Think about Travis interviewing at a prop firm after he graduates:

> HR: What in your past demonstrates your passion for trading?
>
> Travis: I have traded since high school. I read alphatrends.com, SMB's Blog, The Big Picture, Mish, Jeff Miller, Abnormal Returns, Steven Place, the Kirk Report, Seeking Alpha, Kass, Tickerville, Dr. Brett, etc. I run our school's student portfolio account. I interned at SMB one summer, then JPM's prop desk, and Morgan Stanley sales trading during the school year. Right now I am long gold, short SPY, short the euro, long treasuries, long AAPL, long BIDU, with some options positions in the VIX.

Talk about a *wow* answer!

So be like Travis. Life offers too much opportunity not to be the best at what you do. And to be great generally means starting early, working hard, having a passion for your work, and doing everything you can think of to succeed.

Be that candidate who walks into an interview and drops a few profitable years of trading records on the desk of a partner. Then sit back and wait for him to pitch you.

Burn the Boats!

On YouTube, you can find a mesmerizing video of Andy Andrews on Hernando Cortez, Spanish conquistador. It's called "Burn the Boats."

Andy Andrews, motivational speaker, tells the story of Hernando Cortez, who in 1519 sailed from Cuba to the Yucatan Peninsula to take the world's richest and most elusive treasure. For over 600 years, no conqueror had been able to capture the treasure, but Cortez was set to change that. Knowing that several had tried before and failed, Cortez changed his approach with gathering soldiers. Instead of just signing them up, he told them about the treasure in detail, explained how wealthy they would be, and described how well off their families could be for generations to come.

Cortez knew that he would have to build a most powerful commitment from his soldiers. When the crew of more than 600 landed, they all gathered around Cortez to hear one final speech on how they would take the treasure. The charges expected a strategy session of "go here and do that." Cortez changed everything with only three words: "Burn the boats."

The soldiers thought Cortez had gone crazy. How would they get home? But Cortez knew that when the only two options were to die or take the treasure, the soldier's sole commitment would be to capture that treasure and ride home on the enemy's ships.

The soldiers fought well...and they took the treasure. They had to.

Burn the boats!

So if you're a college student who doesn't have enough capital to trade with your discount online broker, burn the boats! If you are at a school that doesn't have a trading lab, burn the boats! If you are a student at a college that does not offer quality trader education for your passion, burn the boats!

After I watched this video, first referred to me by David Blair, @crosshairtrader, I couldn't stop thinking about it. It will change the way you view a future challenge. If you're a serious market participant, you have to watch it.

When I first started trading, we had one CRT monitor. We had no charts. There was no newsfeed. Our trading system would go down for hours regularly. There was no help desk to call to close out our positions. You just hoped and prayed your positions traded in your favor. I was on the phone with Seth Freudberg the other day listening to him complain that he was not a fan of a certain options-trading platform because it went down all day. Seth asked, “Does this happen on your platform?” I laughed because platforms do not really go down these days, but I remember when that was as common as the opening bell.

When I started, you could trade only Nasdaq stocks. We were in the middle of the Asian Financial Crisis. I have written about this previously. I personally was new to trading, and my account was at negative $36K. I was just out of law school and needed to make money immediately. Twelve years later, I have learned one simple truth about the market: You either find a way to succeed, or you find a way to fail. Burn the boats.

Andre Agassi hated tennis. Older than most retired tennis players, he faced a career crossroads: Retire or find a way to motivate himself. He envisioned an academy that offered the best of education to those less fortunate. Tennis would help him raise the money for his dream. He ran and lifted and hit and practiced to build this school. He went on to have the most amazing close to a career in the history of tennis. Burn the boats.

One Thursday, BIDU opened at a long-term technical resistance level of 76.50 and steadily traded down 4 points on the open. That was our one opportunity for that trading day. Burn the boats.

One Friday AMZN gapped down and bounced 13 points, holding a most gorgeous intraday uptrend. That was our opportunity. Burn the boats.

If you have the privilege to hit a buy and sell button in the market, that is more opportunity than most. Burn the boats.

As traders, we must find the time to visit campuses and share our experiences, like Tadas Viskanta—of the awesome abnormalreturns.com, blogger, author, investor, keen observer of all things financial—recently did at Indiana University. The StockTwits U blog, #study, are awesome destinations for interested young traders. And students on campuses need to keep working behind the scenes, showing great respect to the decision makers, to garner more trader curriculum.

As the markets become increasingly electronic, as foreign markets become more important and liquid, as more learn how to trade at a younger age, as a new generation of students with amazing coding skills invade the markets, electronic trading will be an increasingly attractive career. Because developed trading skills will be necessary to succeed, college traders will have to start sooner, trade more, and gain access to better education to compete. Just like Division I athletes seeking to turn pro. Now we just have to get them the education and the ability to practice that they need and deserve.

Although this chapter is mostly about college trader training, I hope this message resonates with the other wings of the trading universe. I hope the transitioning professionals who want to trade pro understand their challenge better, prepare, and are more realistic about the learning curve. I hope the underperforming traders with a passion for trading are more patient with their growth. I hope the experienced traders see how much better they can get with more time. Our challenge is nothing less than that of the classical pianist, master painter, world-class chef, or PG for the New York Knicks.

Why Aren't Universities Teaching Trading?

I visited Penn State in the late winter of 2010 for a talk with some students who were considering a trading career. Some serious college traders inside an investment club had reached out for my visit. One of those traders trades on my desk today. My charge? Discuss what it is really like to be a professional trader.

In a recent article the *New York Times* highlighted the rise of trading labs. According to Rise Display, only three business schools had such operations in 1997. Now, more than 200 institutions around the country have them—from Ivy League universities to small liberal art colleges.

"These days it's a bling factor at many schools," said Richard D. Holowczak, who runs the trading floor at Baruch College in New York, which started its trading room in 2000. "It looks sexy, and it's a great way to have a donor's name literally in lights."

Feel-good trading-lab anecdotes circulate the media. Robert Berns logged more than a hundred hours on the trading floor in his senior year at George Washington—an experience he promoted in his interviews at Wells Fargo Securities. He landed their investment banker position.

Unfortunately, many of these trading labs are not trading labs at all judging by the e-mails I get. They are investing labs. During brunch at Isabella's on the Upper West Side of Manhattan, I was told by a college junior that the trading lab at his prominent college is the most underutilized room at his school. I asked him to think about why. He responded:

> A very wealthy alum donated more than $1 million to get this beautiful trading floor with more than 50 stations built on the top floor of our school of business. That one alum provided the critical learning environment for aspiring traders, but the school fell short in providing students the necessary training to trade. There is only investor education. Not only that, but none of the faculty have a true passion for trading where they would be led to mentor students who also love trading. Maybe that's where it has to be a student initiative to get things rolling.

Investing is not trading! All things fundamental analysis, too much buy and hold is not teaching trading. I do not want to paint broad strokes. I am just relaying the e-mails I get from college traders and my personal talks with them. I am just sharing my frustration at the frustration shared by college traders who have no on-campus training or mentors. How can they prepare for a career in trading without proper training?

Trading is a skill. There, I said it again. Just as Shane Battier developed professional basketball player skills at Duke, so must college traders. We wonder about the failure rate of traders yet keep asking 20-somethings to master the trading game without providing them the training they need. How many 21-foot jumpers do you think Ray Allen, the all-time leading 3-point shooter in the NBA, shot before declaring for the pros? Yet most young traders have made zero bullish flag pattern trades before they kick-off their pro trading career. What would the failure rate be if traders showed up at prop firms after years of high-level practice and game experience? Maybe we would not suffer an economy-threatening crash every decade if our traders were better skilled? How many years of experience did the average Credit Default Swap trader have under their belt before they almost brought down our entire economy? These traders move around billions of product that can destabilize our world economy in short order. Shouldn't we all be concerned about their actual trading skill?

Today we are finding a learning curve closer to 18 months before we see the greatest leaps in progress. Four years of trading in college would give a future trader the required experience and skill necessary to hit the ground running on day one of his career. Trading stars do not arrive on day one because, unlike college athletes, they have little-to-no skill.

A few new traders inspired this next section that demonstrates the long path to becoming a profitable trader. Let's stop a minute and just make a human point. College training, better college trader education, is really at its core just after one thing: encouraging you to have fun at your craft. It's no fun to stink at what you do, which you will if you start without training. It is no fun to be stuck at a job you dislike. And it's no fun to be trading if you do not like trading. So, why not first find out if you like it before you turn pro?

The First Lesson of Trading: Do You Like It?

A trader on our desk shared this e-mail sent to him by another trader on our desk. It's based on the work of Dr. Steenbarger, and it offers a great lesson to new and developing traders.

> I was reading the first chapter of *Enhancing Trader Performance* by Dr. Steenbarger today and I realized that I was going about my trading completely wrong. He describes that to get to a level of elite performance, you have to go through three stages:
>
> **1.** Early phase: having fun with this activity called trading and exploring it to find out if it truly speaks to you. Learning about trading in this time frame and being minimally involved because you are in an introduction phase.
>
> **2.** Middle phase: emphasize skill development, where you acquire basic knowledge and work on skill building and now put effort to learn specific techniques.
>
> **3.** Late phase: mastery of the performance activity that becomes a life focus and is met with intense mentoring, journaling, and self-observation to push you toward being an elite performer in your field.
>
> These stages made sense to me, but a couple lines really caught my attention:
>
> "Working our way through the earlier steps in the developmental process is necessary for moving on to the later phases."
>
> "Achievement of elite performance cannot begin with the hard core pursuit of mastery, yet that is what so many traders try to do."

"The implications are profound: To develop expertise as a trader, the imposition of discipline and deliberate practice is *not* the first step to be taken. **The first step, and it's often the one that's forgotten by new traders, is to simply have fun."**

This really got me thinking about how I have been approaching trading lately. I went from trying to get better every day in the training program to having this mindset that I have to make money or else I am not successful when I started trading live. Essentially, I am trying to be at step three instead of working my way through step one and two. After work, and if I made money that day, I start thinking how awesome I am and that I am going to be a multimillionaire in a few years, to where if I lose, I begin to think that I'm a terrible trader and how could I have made some of those trades during the day when I know that they were bad in the first place and were strictly emotional trades? I really don't know what caused the sudden shift in attitude or mindset, but I know now that I need to get back toward the process of skill development and simply having fun by learning new things each day, rather than being focused solely on results (which really means nothing for me one month in). So instead of focusing on P&L, I am going to begin each day with a question that I will always ask myself: Am I better than I was the day before?

I need to focus on learning the craft of trading and to not worry about making money. When your skills are in place, the money will take care of itself.

I am going to trade the open on the demo for the first 30 minutes until I feel comfortable trading it live. There is so much opportunity, but I need to develop this skill first.

I am going to trade much less than I have been. I have been glued to my screen pretty much all day and I have no energy left at the end of the day to review trades and to ask traders questions because I am mentally wiped. I am going to review my morning trades at lunch and watch tape of my trading. This is where I will get better, and not by trading so many stocks that it is impossible to really know what I did well or what I need to eliminate. If I am in a position, then I will monitor it, and if I miss a trade, so what.

Perhaps the greatest contribution of this chapter will be many more trying trading and discovering they do not like it before they turn pro. Perhaps it will cause you to pause and consider whether you really like what you are doing.

We Need More Female Traders

While we are dicussing how to improve the composition of trading desks worldwide, let me address another serious flaw. I wish there were more women prop traders. Sheelah Kolhatkar in an article for *NY Magazine*, “What If Women Ran Wall Street?” postulated that our banking crisis might not have happened if there were more female traders because they handle risk more responsibly. When I first started trading, I sat next to a terrific female trader who taught me a great deal about trading. Right now our best new trader is female, and our best developing trader is also female. I was recently asked to speak to the investor’s club at Baruch College. About a third of the room was female, and most who approached me after my lecture with questions about our college training program were women. In the summer of 2012, both of our five-week summer college training program sessions were well attended by women, some even from abroad. I will keep encouraging females with a passion for trading to train and trade. But in a mostly male environment, we must be cognizant of anecdotes like the one described here, from a former prop female trader. Until most desks clean up their language and behavior (I would like to think ours has), women we will continue to be underrepresented on trading desks (to the loss of all traders and firms).

From the Prop Desk: A Woman’s Perspective

Jan 31, 2012 | By Bella

Hi Bella,

I finished your book and it was so wonderful and inspiring. As a female trader (back in the game after a year and a half away, used to trade on a prop desk), I loved that you addressed the issue of women in trading. You sound like a great guy to work for. I would like to share my experience as a female trader with you, since you expressed interest in the book. When I worked on a prop desk, I worked for the loveliest, most talented trader I’ve ever met...and with his unruly employees. When I first started, traders would refer to the stock as a bitch, a whore, a slut, the list goes on. They would say they got raped in a stock if they lost money. I am not like CDT (from your book), I can't tolerate that kind of thing. My head trader put a stop to it after I went to him (like I said, he is a great person), but my fellow traders ostracized me after that, they hid callouts via AIM, etc.

I would never blame them for my trading weaknesses, but I hated working there and doubt I will ever go back to a prop desk. I stuck it out for almost three years, and that was enough. The sincere disdain they had for me was just so unprofessional. On top of that, their trading was undisciplined. I'm trading by myself now and loving it, but I'm looking for a trading community online that may be more suited to my style and personality. Again, I want to emphasize that I have nothing but respect and admiration for my former head trader; my issue is just with his employees. Anyway, that kind of experience is what many women fear they will encounter if they trade, and it is probably part of why you haven't gotten many resumes. Just my thoughts.

The Future Five-Year Career Path

With schools pressed to raise money, how about this idea? Go pitch some wealthy alumni to pledge for a new Rich Ex-Donor Trading Center. Those who crush it after graduation with the help of this training center should then give back to the school, thereby creating a new stream of alumni giving. And the students will be exposed to trading, enriching their college learning.

If you are on campus and you like the work being done at Penn State and Rutgers, start a trading subgroup inside the investors group. After a recent lecture at a university, a student approached, making the four-hour dive down and seven-hour drive back in a torrential downpour worth the trip: "The reason more students are not trading is they do not hear enough inspiring talks from people like you." So for the professional traders in the community, we should make ourselves available to college traders to encourage them to work on their game and help them build their trading communities.

As our world becomes more niche focused, with a future where we will watch the Internet from our iPad-controlled TV, education will be forced to cater to what the students want. I see college students thirsting for a real trading curriculum. When will the universities listen?

My hope is twofold:

1. College students who really want to trade will learn about it in school and that those who do *not* have a passion for trading will come to this realization before they wade too far into the waters.

2. The Street will become populated with better traders because they will have better skills from years of practice. Let's regard trading for what it truly is: a performance sport. It's one that very few people will be able to play pro but that those who have a passion for it and develop the necessary skills will play at a higher level.

The market doesn't care whether you went to an Ivy League school. The market doesn't care who your dad is. The market doesn't care where you grew up. It cares that you have skill. And that takes time. So why not start early to give yourself the best chance of being a professional trader?

When new traders came to SMB five years ago, we offered the career path of only intraday equity trader. Today this is not the career path. In the future, proprietary traders might learn as intraday equity traders but then pick up options and then futures and then *foreign exchange* (FX). In addition, those prop traders should develop a strong knowledge of other markets. They should have cutting-edge tools that spot the patterns that they like best and feed them these opportunities with signals. In short, discretionary traders should become more bionic. Finally, they should be taught how to build trading models. They will be multiproduct, multimarket, bionic discretionary traders with automated models.

To do all of this in five years requires traders to walk onto our trading floor on day one as traders with a track record. Teachers, traders, and our education system all can do better. This new career path is too exciting not to.

Let's meet an SMB intern who started working on his game before receiving his college degree, and highlight his trade in ORCL. And let's give him the nickname Special Projects.

Reversal Play in Oversold Stock

Special Projects

ORCL

12/21/2011

Big Picture: QQQ

So all markets had a nice +2 percent rally yesterday after our multiday sell-off, coming into the holidays. However, today markets could not hold their gains from yesterday, and trended down for half the trading day and reversed some of their losses into the close. The markets are still susceptible to Europe news and our own economic and political dilemmas. Specifically, the Nasdaq was among the worst of the other indices as Oracle’s (ORCL) uninspiring earnings report (missing revenue quite marginally) last night caused most other big-name tech stocks like Citrix Systems (CTXS) and VMware (VMW) to sell off in conjunction.

QQQ 15-Minute Chart

Intraday Fundamentals

ORCL was definitely under pressure from its bad earning report last night, missing revenues quite significantly:

"Oracle, which has operations in Rocklin, said its net income rose 17 percent to $2.2 billion, or 43 cents a share, compared to the same period last year. Its second quarter revenue was up 2 percent to $8.8 billion. Excluding items, the company would have earned $2.8 billion, or 54 cents a share on $8.8 billion in revenue. Analysts expected, on average, earnings of 57 cents per share on $9.23 billion in revenue."—*Sacramento Business Journal*

SMB TRAINING

My Trade Plan and Intraday Technical Analysis

I traded this stock a little in premarket, but I didn't get to trade the open. During midday when I had time to check how the stock was trading, I noticed it was down over –11 percent and had done over 4x its ATR. I also noticed it was consolidating between 25ish and 25.26 and making slightly higher lows (ascending triangle). All this signaled to me that the selling was out of steam, at least temporarily. I set an alert for if the bid was "at or above" .27. My alert went off around 2:00 p.m. and I quickly pulled up the intraday chart and saw it did a spike out of its range and topped out at .29. After the quick spike up, it traded in tight consolidation for about 20 minutes. Then it popped up and held, instead of wicking. This gave me a signal that the stock might be ready to reverse for at least a .30–.50 move above .26. My plan was to play a short reversal on the long side as the stock was definitely oversold. If it could break and hold above .50, I was going to add and hold to maybe .75 to the whole number ($26).

ORCL 15-Minute Chart

Reading the Tape

As this stock does quite a bit of volume, to me nothing distinct about who's selling and who's buying helped me get into this trade. What I did identify was a pickup in speed of the prints and more offers being printed than bids, giving me some indication that there was definitely some buying pressure with the bids not dropping. In addition to the tape, I used my charting analysis with my other underlying indicators to aid me in getting long the stock.

SMB TRAINING

Trade Management

1. I got long 100 shares at 25.27 once the .26 bid, which was the offer that kept the stock down for most of the day, was holding

- **A.** My stop was .19 (below the low of the late day tight consolidation range).
  - **i.** Plan was to move stop to breakeven once I was in the money.
- **B.** My target was set to .50 (most important resistance intraday).

2. I added another 100 share lot to my position once .50 was breached and held with conviction with the bids not dropping for a few minutes.

- **A.** My stop was set .46 (below the close and opening one-minute bar after the .50 breach).
- **B.** Target was set to .70–.75, but would hold if price action and the chart showed me we were going to $26.

3. I took my first sale of 100 shares at .63 once the stock wicked to .66.

4. I got flat at .78 (below the consolidation after the pop to .83).

- **A.** This break below definitely made me think the reversal was over. As you can see on the chart, that’s a pretty big red candle.

ORCL Intraday Chart

Trade Review

I felt like I stayed very objective and let all my indicators (i.e., tape, moving averages, and my overall chart analysis and the patterns I was witnessing on the chart) give me an edge into getting long in a stock that was overly beaten down. The only thing I did wrong was shorting the stock after it made a second attempt at .83 (double top?). Especially when I saw a significantly bigger offer for 100K shares at .83 getting hit and soaked it up without lifting. My stop was tight (at .84). Other than trying to flip my position, I feel I did well sticking with the reversal and took sales when it seemed apparent that the reversal was over. But it's always funny to look back at the chart and see what I missed in terms of the patterns that were forming that could have enabled me to reposition at around .56–.60 and taken the stock up to $26 (my ultimate target). But that's after the fact. All in all, I would consider this a good trade/scalp.

Now let's let you peek in on the trade discussion had between Special Projects, our desk, and me on this ORCL trade.

From Our Training Room: A Reversal Trade Review with Special Projects

Special Projects: Okay, this is my PlayBook for Oracle from yesterday.

Bella: First intern ever to do a tradecast, right?

Carlton: First, first! (shouting from the back)

Bella: First intern ever to be on camera and to do an SMB Playbook trade.

Special Projects: I am very honored.

Bella: Well, this probably means that this will be a very long session, Carlton. It's good that I have a 4:30 phone call, or we would be here for hours, right?

Carlton: Oh, yes we would.

Bella: And, you would really get in there and dig at him, too, right?

Carlton: Of course, you have to haze him.

Bella: All right, so I would tread very, very carefully here, young fella.

Special Projects: All right, All right!! (understanding the pressure of the situation)

Bella: So, let's see what you got.

> *Look at Special Projects with special information about ORCL.*

Special Projects: Okay, I traded Oracle for the last hour or two of trading, yesterday. As you know, they reported earnings the night before, or after the close on Tuesday. And, their revenues missed expectations, and they usually don't miss. I think it has been ten years since the last time they missed estimates, and the revenues were off marginally.

You can go to the next slide.

So, "Big Picture" of the markets: The day before we had a really nice 2 percent rally after we had somewhat of a trend-down range, and then we had a nice pop on Tuesday. As you know, Europe is still part of the headlines, and they are moving the markets. And, the holidays are around, so the volume is a little light and you have to be careful trading. And, the tech sector was pretty much murdered yesterday because of Oracle's earnings.

And, you can go to the next slide, Carlton.

Bella: Okay, good: holiday trading, Europe, Tech. So, three big headline events when you are trading Oracle. Okay, so we are looking at the QQQ (*ETF index tracker for the NASDAQ 100*), good. We can use this as an indicator while trading ORCL. Very good. Did you teach him that, Carlton?

Carlton: No, I think he must have picked that up from Steve's morning call.

Bella: So you are saying he couldn't have learned it from me? *(laughter, as Bella stares at Carlton)*

Carlton: No. Sorry. It probably was from you. *(laughter, as Carlton keeps his head down)*

Bella: I am not saying he had to learn it from me. I am just wondering why you didn't think he could have learned it from me? *(Bella moves toward Carlton.)*

Carlton: I am sure he learned it from you, Bella. *(whispers Carlton)*

Bella: Okay, I am glad we straightened that out *(laughter, as Bella takes a step back)*. Please continue.

Special Projects: Okay, so this, right here, are the QQQ's *(cues up the QQQ 15-minute chart; see* *Figure 6.1**)*, and the highlighted area is the day before when we had the gap-up and the nice trend. Then followed by a gap-down and trend. As you can see, toward the end of the day, QQQ started to reverse, and I think that helped Oracle and other tech stocks cover some of their losses from the day.

Figure 6.1

So, as I said, the Intraday Fundamentals for Oracle were that they missed earnings. They reported 43 cents a share of revenue, but analysts were expecting 57 cents, so that is a pretty big margin to miss by, especially considering a company like Oracle. Everyone has very high expectations of a company like this.

So, they got hammered pretty much from premarket into the trading day.

> *When a big company misses so badly this shakes the confidence of the Street. Traders tend to sell first and then ask questions later.*

Bella: So, they missed big time on revenue, right? And, they missed big time on the bottom line. I mean, that is a terrible revenue number for such a big company, right? So, good point. So, big company, has a history of doing well, and to miss by that much is a big problem. Okay, good. Let see what we have next.

Special Projects: So, my trade plan and intraday technical analysis: I was doing other things throughout the day, but I was watching the stock during premarket and traded a little bit premarket but had to do something else but I noticed that it did over four times its ATR *(average true range, or the amount a stock generally moves from close to close, including overnight gaps).*

Bella: Carlton, did you make him do something? What else would he be doing?

Special Projects: I had to fill out a broker-dealer application. *(Audience begins to chuckle.)*

Bella: What else did you have to do? It sounded like he was complaining there. *(Audience laughs.)*

Special Projects: No, I wasn't, I wasn't!! I am just saying I needed to trade it.

Carlton: Don't throw me under the bus!

Special Projects: No, I'm not. It's not you. I am saying, I was busy.

Bella: What? Did you have to get Carlton lunch? Did he ask you to wash his car?

Carlton: Don't throw me under the bus. We just have to break you in.

> *Always check the ATR before trading a stock. You will learn to use this as an indicator to tell how far a stock might move intraday.*

Special Projects: So, anyway, I noticed that it was doing four times its ATR, which is something to think about. Most stocks, when they are beaten down, there is some point when they will begin to do a little bit of a reversal. And, it is the same thing when a strong stock has a tendency to pull back.

Bella: All right, stop there! What do you mean by that?

Special Projects: What do I mean by what?

Bella: "Most stocks, when they are beaten down, have a tendency...?"

Special Projects: Okay, maybe I misspoke.

Bella *(smiling)*: Wow, you have got to be careful right here. *(Audience begins to laugh.)*

Special Projects: Based on my observations, I feel that stocks have a tendency to retrace at certain levels and at certain measurements. I use, in my technical analysis, Fibonacci retracements to see how much something has pulled back or retraced, and confirm a trade from those levels.

I know you don't like technical analysis. *(Audience chuckles.)*

Bella: If you are watching at home, I am actually taking my head and slamming it into the wall. *(Audience laughs.)*

Carlton: Don't worry; I have you on camera.

Bella: Slamming it into the wall. All right, hold on, stop, because we have to correct a *huge* Special Projects mistake. So, you said, "Most stocks that are down a lot have a tendency to reverse"?

Special Projects: Yeah.

Bella: Well, first of all, this is A stock on A day trading in A particular pattern, and IT will have A way that IT will actually trade. So, if this stock, if Oracle, has such bad fundamental news, has such bad Intraday Fundamentals, then it should trade very differently than all of the other stocks you just mentioned.

Okay, so it is important what the Intraday Fundamentals are. If ORCL misses revenues by that much, that is no good. If stocks get below really important technical levels, they don't tend to bounce either. During light holiday trading, that becomes another factor to throw in there, and there may be fewer people willing to throw some money into Oracle to buy it.

So, here is the thing: When a stock's fundamentals get worse, it is not true that they normally bounce. It is factually incorrect to think that they will bounce. It is factually incorrect that they will bounce off of levels. It is factually incorrect that they will be worth your time to get long. All of that is untrue.

And, the reason for that is...why?

Because there are a lot of people getting the f*** out of the stock, and there are a lot of people on the short side. And, it is just supply and demand, and people do this all the time. They sit around and try to play off of bounces, and it is very unlikely, unless a stock acts in a very specific way, that it is going to bounce. For instance, if something is very steep to the downside and shows some sort of blow-off bottom, that is a particular subset of plays where it may be likely for it to bounce.

Okay, so, if the news really isn't so fundamentally bad as Oracle missing revenues that you noticed, then it is more likely, in that case, for it to bounce. So, you just have to be careful. And look, maybe it will bounce and that is fine. I am not saying don't look for bounces. I am not saying if it gets to a particular support level not to get long. Or it is completely wrong for you to see that as a Support Play that you might put into your PlayBook. But, I don't want you to just sit here and say... *(Special Projects interjects.)*

Did Special Projects just interrupt me?

Special Projects: I think you are misreading my intention. I was watching it and I wasn't thinking, "Oh, get long because it has been sold off." But if a bottom was confirmed based on the price action, I might look to get long. And, I also noticed on the chart that it was having a hard time going lower. It was actually making higher lows.

Bella: Good.

Special Projects: And, I noticed 26 cents was the level to watch, so I set an alert for 27 cents. I mean usually I like to set my alert a little bit higher with an important level, but since it was such a tight range, I decided to set it 1 cent above the important level, and then I got the alert.

Bella: Okay, I just want to be clear. What you just said is a reason for a stock, a lot of times, to go back up. Which is: It is having trouble going down lower. It is holding higher. That is a really good reason to get long in a stock.

Trading strategy for a bounce in a stock: Let the stock stop going down, let it hold higher. Then get long with a stop below the low. Do not sell until a significant up move.

I don't care how you actually trade this; I really don't. I just want you to think through it the right way. Make a fundamentally correct trade. And I do not want you to develop a PlayBook that is based on information that is not true.

Special Projects: All right, yeah, so besides where I said that "most stocks bounce after they have been sold off," I wasn't going to make a decision, especially when it sold off and where it was ranging between 25 cents or so, 35 cents, all day long. And then, I got the alert that it spiked out of the range that it was in for most of the day. I noticed that the lows that it would break through were not as low as the previous low.

Bella: That is an A+ setup. I love that setup: Stock In Play. It shows you a range where it can't get above a certain price, the stock stops going down, the volume breaks above the range, holds above the range. A+ setup. Great trade.

Special Projects: And then, the next slide is the 15-minute chart *(cues up the 15-minute chart)*. As you can see, premarket the day before, when ORCL reported, ORCL fell off of a cliff. Then, ORCL popped back to around 27, but obviously there was no volume, so this isn't a trade to consider. And, as you can see, premarket the following day ORCL continued in a downtrend and then ORCL opens up and just gets pummeled. And, as you can see, for most of the day, ORCL trades in a range followed by a reversal.

Bella: So, are you saying "right above here?" Carlton, can you show the one minute*? (One-minute chart is cued up; see Figure 6.2.)* So, are you saying, when it gets above here? *(Bella pointing to the range between 14:00 and 14:15 on the one-minute chart.)*

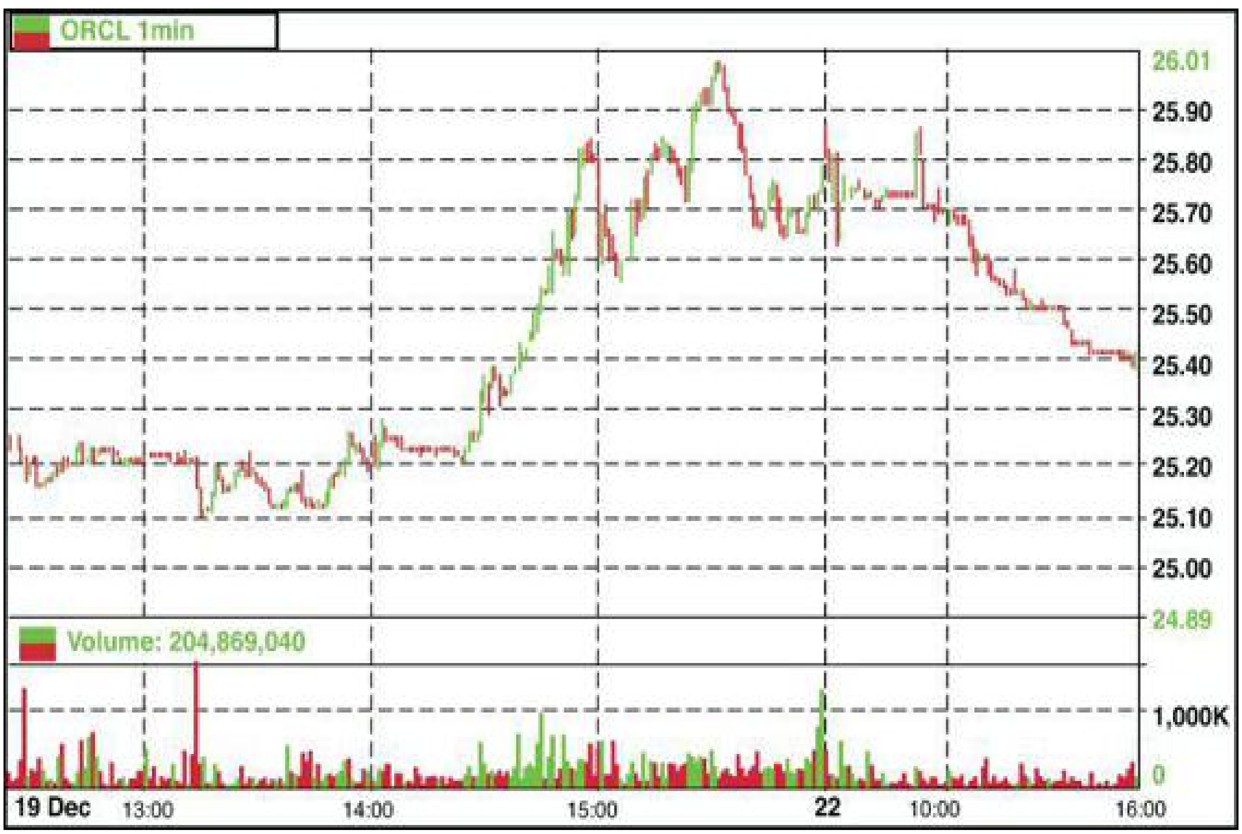


Figure 6.2

Special Projects: When it got above there, you see it spiked and came back and consolidated really tightly, right here. *(Special Projects pointing to the range between 14:00 and 14:15 on the one-minute chart.)* What really got me interested was when it dropped out and hopped up a little spike in volume, then followed by a higher....

Bella *(interjects):* So you mean when ORCL actually broke to the bottom of consolidation, ORCL did not go down. That is important, right? You got something tight that breaks below the bottom of consolidation, but does not go down.

Carlton: Can you please stress that? Because a lot of people fail to realize that.

Bella: So, when something is real tight and it breaks to the down side, and it fails and then actually breaks to the upside, that can actually be a better play. Why?

Audience: You have confirmation that it actually failed to the downside.

Bella: Yeah, so you have confirmation that there is not going to be a lot of sellers piling on when it breaks to the downside. It’s tight and it breaks to the downside, and there are no sellers getting ready to pile in. So, now the sellers show you they are not ready to be aggressive and the buyers are...what?

Aggressive. We have to buy this higher because when it broke to the downside there wasn’t a lot of people willing to sell it. So, if I now want to buy or cover, I need to step up higher. So, psychologically, that is very important for the stock. So, that in and of itself is a good pattern. And, look, what a lot of people will do in this situation is they will get short and they will be all pissed off that the stock didn’t go down, when what they should do when they get short is ask themselves...what?

In this tight consolidation, you should get short, right? But, when you are short, you should be thinking....

Special Projects: Where is the follow-through?

Bella: Yes! Where is the follow-through? The short didn’t work. Get out, take your loss on the short, be open-minded, and consider whether or not you want to get long, if it actually holds above the top of the range. Nothing to get upset about, nothing to say, “The stock had to go down! Why didn’t the stock go down!? This *f****** stock didn't go down. I'm short." All right, so the stock didn't go down. There was no panic selling. You cover, if it holds above the top of the consolidation, I actually think that is a better play because you have a lot more information.

Sometimes the best trades come after disappointing trades.

Special Projects: Okay, the white oval is my initial stop from where I got in (see Figure 6.3), which was when the bid started to hold at 26 cents, which was the level that was the high of the range throughout the whole day. So, I got long 100 shares there. And then, my plan was just to hold until 50 cents, but ORCL blew through 50 cents in the price action.

Figure 6.3

Bella: I think this is a Trade2Hold, unless there is a technical resistance level near. It is late in the day. ORCL has gone sideways and consolidated for a long period of time. ORCL is down a lot. The market has been very strong, buying real companies that have traded off considerably. ORCL is the type of stock that a lot of people own and are going to want to own. ORCL is the type of stock where people are like, “Well, I want to own this” or “I want to build a position in this.” A lot of people like to own Oracle. So, you can buy a lot of it. It is an easy story for investors to understand. People have owned it for a while. It is one of those stocks that people will actually think about supporting. And you have a clear signal from reading the tape to enter with a definable stop and room for a nice reward. So, you buy that stock, and I think you have to let it go. You have got to let ORCL go. It is a good pattern. It is a Trade2Hold pattern. And you can use this pattern to construct 3-5 day swing trades as well.

Special Projects: I did hold it, and I got long another 100 shares around 52 cents; 50 cents was kind of the level intraday. So, it pretty much blew through this level, dropped for a second, but....

Bella: *(Interjects)* Okay, so, there is the most important point about trading this setup that I would like somebody to explain to us. *(The room goes silent.)*

So, there is one most important point. What is it, J-Rod?

J-Rod: In terms of....

Bella: In terms of this trade, what is the most important point? What is the most important point*? (Bella addresses the entire room.)*

J-Rod: What point are you talking about? The entry, the execution, the exit?

Bella: Most important point of this trade. Ryan?

Ryan: Look at it as Trade2Hold because you waited so long for the consolidation that when it finally makes its move.

Bella *(interjects):* Yes, I think that is important, but there is something more important. It is a Trade2Hold, but I think there is something even more important. Jack?

Jack: I was just about to say that.

Bella: Okay. Anyone else? Carlton, what do you think is the most important thing? Pass?

Carlton: Pass.

Bella: GMan, what is the most important thing? John, what is the most important thing?

John: That, since it has been consolidating for so long that when it finally breaks outside of its consolidation, that you have confirmation that the probability of it breaking lower is low.

Bella: Yes, that is all right, but no. So, the most important thing is to see if the stock will hold higher, and if it holds higher to do what?

Audience Member: To add more.

Bella: Yes, that is the most important point of this particular trade. Whenever you are playing a bounce in a particular stock or playing a bounce in the marketplace, when something stops going down, it shows you that, and holds higher; that is when you get aggressively big...and hold. Not at the bottom. The better trade than the bottom is this: Hold and hold higher. Get bigger.

> *If you are making a bounce play, you must buy more when the stock holds higher. If you cannot, then eliminate this trade from your PlayBook. The math will not work for you then.*

Okay, let's go to the last chart for your review. *(Trade Review slide is cued up.)*

Okay, trade review. Go ahead.

Special Projects: I felt like I stayed very objective and let all my indicators (i.e., tape, moving averages, and my overall chart analysis) give me an edge into getting long on a stock that was severely beaten down. The only thing I did wrong was shorting the stock after it made a double top at 83 cents.

Bella: Okay, let me give you the review for this trade because this spot on highlights the trading principle that *the stock talks to you.* And, if you listen, you can find a very easy trade in a stock that a lot of people are scratching their heads about, thinking, "Is this stock going to go up or down?" Okay, it stops going down, consolidates, tries to break lower, it doesn't, holds above the top of the consolidation, Tier1: Buy one lot.

It is talking to you, it's saying, "I did not go down; I am busting above this level. It is time to actually put risk in on the long side." It is talking to you. When it holds higher, it is talking to you and it's saying, "Look, I am showing strength. I am showing strength, I am showing strength, I am showing strength. Buy more, buy more, buy more, buy more. Buy more, Special Projects. Buy more, Special Projects. Buy more, Special Projects. Buy more, Special Projects. Stop being such a wuss, buddy.”

And, in all of the data and news about Oracle, these are just patterns. There is the consolidation pattern. The specific one that you saw is a failed breakdown, hold above the top of the range subset. And that is a pattern that you will see for the rest of your trading life. And, there is a lot of money to be made in that pattern. It is a very worthy pattern. And then, hold higher. Something that had bad news, was down a lot, that you can play. That is it. Lots of numbers, lots of data, lots of opinions become just trading patterns. You can make your own trades from these patterns and figure out how to make a lot of money.

Anyone have any questions?

Yes?

Audience: How do you close your position?

Bella: Develop a list of Reasons2Sell. You work on that. We come up with ways to do that. If it breaks the uptrend, fine. If it goes and finds the next technical important resistance level, you might want to take it off. If the market comes to an important resistance level, you might want to take it off. If ORCL gets too hot on the upside, so, if it has a blow-off top that is too steep to the upside, you might want to take some off. But you work on, for yourself, developing the ways that you get out of a Trade2Hold and this pattern.

I can’t give you that answer. I can just give you the things to think about and you have to work that out for yourself.

All right? All right, thanks. Not bad for an intern! *(Audience laughs.)*

Seriously. Very nice work!

7. Prep

> There is "easy money" and there is "hard money" in trading. Your longevity is determined by which one you choose to pursue. Some folks don't make this easy for themselves.
>
> —Steve Spencer, Co-Founder, SMB Capital

Simply put, Prep is the most frustrating trader I have ever mentored!

He is #1 in SMB history for most trading flaws.

He makes the same mistakes over and over again.

He can make money; he just cannot keep it.

He loves trading but this has not translated into enough improvement.

We have poured significant resources into his trading with a decidedly negative return.

Prep has one of those backgrounds a big bank would drool over. He went to Choate, a prestigious private, college-prep boarding school in Wallingford, Connecticut, that boasts President John F. Kennedy among its alumni. Following Choate, he went to one of those ultra-small liberal arts colleges for those who just miss the Ivy League. Prep is also a former high-level hockey player. Before going off to prep shool, he grew up in one of those New Jersey commuter towns where most of the fathers have Wall Street jobs, and there damn sure has to be a magnificent country club. Boyishly handsome, athletic, polite, and with a bright demeanor, he seems the part to work in "the business." He would look just as comfortable at Goldman as he did with us.

There is a lot to learn from Prep's trading journey. I have to admit that although he has made a series of avoidable mistakes during his short trading career, requires a great deal of daily care, and consistently loses money for the firm, I just love the kid. He works, cares, has a passion for trading, and leads the desk in sharing trade call-outs. You just want him to make it.

How can we learn from Prep? Many traders in our game make the same mistakes. And there are numerous traders right on that default line from becoming consistently profitable to finding a new job like Prep. (I certainly would never fault him for ending up in institutional sales at an investment bank. I'm sure he'd be great at it.) If he could just get out of his own way, he would succeed as a trader. If you see yourself making some of Prep's mistakes, take comfort that all this is correctable. Prep finally reached the point where he made serious P&L. Prep got to that point where we all knew he could do it!

If you are right on the edge of making money consistently, then Prep is your champion.

If you make the same mistakes as a trader and wonder if you will ever stop, remember the story of Prep.

If you have months of negative trading data and wonder if you can succeed, then Prep shows you *you* can.

At the end of Prep's story, there is an all-too-real plot twist.

First, we should run through his mistakes so you don't make them.

It Is Everyone Else's Fault But Mine

I could fill Yankee Stadium with traders who are experts in blaming everyone and everything except themselves. Prep at times was no exception. This is the mindset of the underperforming trader that needs to be eradicated.

Prep sent me his daily review after one trading session. It started:

> ***Pretty tough day not to have my full size***, this was the best trading day I have seen in a while, LULU premarket was great, NAV was the best trade of the spring so far, AAPL I was stopped out a few pennies away from making 4 points, MOH was just a difficult stock to trade...

The words in bold italic caused my angry Coach Bella side to awaken. We had recently cut his trading size for distinguished underperformance. I responded via e-mail in the bluntest of tones:

> Hey, Prep, we cannot give you your full size back until you are profitable.
>
> It was not a bad week that got you lowered.
>
> It wasn't Carlton.
>
> It was me.
>
> It was not just last month.

> It was the month before as well.
>
> You do not deserve to be trading with full size given your results.
>
> The firm is down a ton of money on you.
>
> In fact your results are such that you would be asked to leave pretty much anywhere else.
>
> I do not send this e-mail to be hard on you.
>
> It is not that I do not support you.
>
> But STOP BLAMING THE DAMN SIZE THING!
>
> Your performance caused our firm to be responsible with the losses we can take on you right now.
>
> That is what has happened.
>
> We do not complain at SMB.
>
> We take responsibility for our results.
>
> Be more consistent.
>
> Do a PlayBook Trade every day.
>
> Do a very detailed trading review.
>
> Make notes about your psychology challenges.
>
> Put together a good ten days of trading data and come find me and I will bump you up.
>
> For now it is up to you to create those ten days of results.
>
> I am rooting for you!

Prep apologized and went on to produce seven out of ten days of solid trading. One thing about the young man is that he responds.

The trader who blames others is the losing trader. Prep is not the first nor the last to blame another for his lack of performance. Heck, even a reader of our FREE SMBU Blog went there.

Trader Rant

The reader wrote:

> I had something that worked for me, but I have lost my conviction because of listening to too many other people. The more I trade, the more my emotions get in the way, and all I learn is that

everything I think I know is subject to change. Computers have changed the way stock prices react to patterns so that you cannot predict what people will do, so much as you must now attempt to figure out how the computer is going to try to screw the herd, and ride its wake?

I have oftentimes wondered if your recommendation of the morning makes a good target for powerful contrarians guaranteed a fresh supply of weak hands, and yes, I've wondered if that was in fact SMB Capital. Not only were GMCR and SODA GREAT shorts, but they were some of the best of their rec.d days (rec.d as longs, made championship, killer shorts), and I don't believe it is a coincidence. Weak shorts make $NFLX so strong, and what better way to corral a bunch of weak longs than to offer a rec for the day, creating a possible easy takedown.

I do not know everything, and the scale of influence of investment firms is not an area where I have expertise. I just think if somebody was going to be able to decipher this market, it would be those that have written books, blogs, and have proprietary trading firms. That is why I trusted your recs two days in a row, and those just happened to be the worst plays for those days, and those days just happened to be critical for my trading, which I can no longer do because of the damage to my account.

Bella responded:

We encourage debate on our blog and to us and certainly SMB is far from perfect, but there was a lot wrong with the comment above. Let's see if we can learn from these mistakes.

1. Do not copy the trades of others blindly. See if you can make them your own and if so, then make them your own.

2. For all trades, first determine your stop if the stock trades against you. No one trade should ever so much as even stop you out for one day, let alone do serious damage to your trading account.

3. Trading ideas are ideas. If the market trends against your idea or in this case our ideas, then take the other side of the trade.

4. Never blame anyone else for your losses. Never.

5. After each losing trade, determine what you learned. Thank the market for its learning opportunity.

6. Judge your trades on the process and not on your results.

7. Do not get lost in an endless opportunity to find conspiracies in the marketplace.

8. If you spot a pattern, no matter how it develops, exploit it. If someone was fading our AM idea, then fade it as well. That would be awesome if that were the case since all you would then have to do is do the opposite. Think Opposite George from *Seinfeld*.

9. If you cannot control your emotions while you trade, then work on that first, and leave your money in your bank account.

10. One Good Trade, and then One Good Trade, and then One Good Trade.

There is still hope for that same trader. We can always choose to change our mindset. A few hours later he sent us this:

> Sorry. Didn't get much sleep the night before I wrote this comment, and I was really mad at myself, but had not realized this fact. I don't actually blindly take these recs, so much as try to make them work for me, and that did not work. I take the blame for my stupid trades. Everyone who is getting on my case here is right; I don't really have a leg to stand on. My apology to SMB.
>
> Yes, I have bad risk habits. Yes, I'm trying to make back money and it is driving me crazy. Yes, I am trying to convert to an open-minded trader from a pure bear, and at the worst time ever. Yes, I'd probably be better off taking the money I might put in my account and go on a vacation.

Ah, no worries. Well said!

Prep not only struggled with blaming others for his underperformance but a common cause for overtrading, which we call FOMO, a fear of missing out. FOMO does not just apply to trading or investing. It can apply to just about everything in life that seems popular at the moment. It could be a hot night spot or a destination beach town or ski resort generating a buzz. We had to address this psychological issue. Many traders struggle with FOMO without recognizing their ailment.

Fear of Missing Out (FOMO)

The day before leaving on a flight across the world for a presentation for the Securities Investors Association (Singapore), I had a trader chat with Prep in my office.

He knocked on my door. “Bella, do you have a minute to talk about my trading? I am really struggling.”

“Yeah, come on in.”

Prep continued, “I am so overtrading. I think I have a fear of missing out on trades and things. Even in my personal life.”

This was a teaching opportunity. Dr. Andrew Menaker, one of SMB’s outside trading coaches, was in town filming a psychology training program with me for SMBU. There was a planned dinner with Dr. Menaker and some of our traders, so I had Prep added to the guest list.

Prep joined the dinner with Dr. Menaker, GMan, and traders from the desk at Adrienne’s Pizza Bar on Stone Street. I suggested Prep discuss this issue with Dr. Menaker and the boys over pizza and then send me his notes on the working dinner.

As expected, Prep sent me an e-mail later that evening outlining the dinner conversation, which was saturated with trading psychology nuggets. Prep wrote:

> We actually had a great dinner, talked about a handful of topics. The first I’ll mention is what I brought up with you in our chat today, the fear of missing out. Dr. Menaker had definitely addressed this topic before, judging by how complete and preordained his thoughts were. He basically said that before every trade I should use a “FOMO” scale. And this is basically a meter of how much of my desire to make this trade is based on the setup and how much is based on a fear of missing out. Anything over 50 percent and I should not make the trade.
>
> This led to GMan’s thoughts on putting 100 shares on to fulfill his desire to make the trade, even if he knows it is wrong or he is paying the top or hitting the bottom. GMan will put 100 shares on to (a) keep an eye on the stock and (b) to just satisfy his desire to make the trade. I found both of these concepts really interesting and I am definitely going to consider them in my trading.

> Next, we talked about making the jump to bigger size, and the biggest thing I took away from this portion of our talk was that we should not be looking at our P&L and that with more size the methodology is by far the most important issue. Sticking to a system and disregarding the P&L. Why am I making this trade? Is this within my risk parameters?
>
> Shark wanted to talk about daily routines. One of the things Dr. Menaker brought up was each morning he has his mentees write for at least five minutes about how they are feeling and why they are feeling it. This helps relieve angst and anxiety and puts you in a much more objective mood. I think this is really good and I am going to start doing it.
>
> This led us to talking about dealing with trading because of our emotions. An interesting notion that Dr. Menaker brought up was that if he can’t turn away from his screen and take four deep breaths, then he is not objective enough and he needs to walk away. Whether it is to get some fresh air or go to the bathroom or whatever. I think taking a break is something that is super important and that I should probably do this to keep from churning during the middle of the day.
>
> That is a problem I have.
>
> We briefly talked about breathing and ways to calm yourself down and psych yourself up. Music was discussed as well. I think all in all this was a really positive dinner and I took away a lot from it. Let me know if you have any questions. TO and Pippen were also there.

In more detail, Dr. Menaker and I collaborated on a blog post for the issue of the impatient trader.

Stop Being The Impatient Trader

> February 19th, 2012
>
> Greetings from Singapore.
>
> Today is my last day here in the new gateway to Asia. I have a day packed full of some more learning meetings and then take a 2:30 a.m. flight to Johannesburg, South Africa. I arrive in JNB, will

shower, and then head to meet some top South African traders in Johannesburg. I have been tasked to talk about improving your patience as a trader. I had better sleep on the plane.

As preparation for my discussion, I sought out my friend Dr. Andrew Menaker, trading psychologist. I have traded for 13 years; read everything on trading psychology from the greats like Dr. Steenbarger, Mark Douglas, and Ari Kiev; written extensively on the topic, but wanted to improve my preparation and gain input from a specialist. You have seen some of this work on our blog in the past. SMB has been working with Dr. Menaker the past six months to create a comprehensive trader psychology training course. To create a quality program takes time.

Below are his thoughts, which I wanted to share with you.

Dr. Menaker:

> What to tell an impatient trader?
>
> When talking to an impatient trader, I always begin with FOMO—fear of missing out. The impatient trader is experiencing FOMO and is unable to manage the emotions that come with FOMO. Strong unmanaged emotions can easily trump one's will-power—or conscious decision to do or not do something.
>
> It's very possible that impatient traders will continue to be impatient even after various attempts to deal with it including mental rehearsal. If that's the case, and it often is, it suggests that the impatience is a reverberation of something deeper, something subconscious—out of present awareness. So, then the question becomes, what's going on in the trader's subconscious process that is producing such emotions that can trump will power and intellect?
>
> When I work with such a trader what I almost always find is some type of unmet developmental need, perhaps a feeling of needing acknowledgment or wanting their sense of self-worth validated, etc....lots of different possibilities here. What's usually happening for the impatient trader who has not responded to mental rehearsal or other cognitive-behavioral techniques and continues to be impatient is that they are not

trading the market; they're actually trading their subconscious need for validation, etc. This is where a trader can often benefit from guidance, such as coaching. It's important to identify the unmet developmental need(s) and to develop a strategy that deals with the core issue, not just the symptom; otherwise, the problem will continue.

The interesting thing is that no one is perfect; we all have some unmet developmental needs, but for some people those issues are stronger and more easily triggered by the environment—and for a trader the environment is the market. Traders may understand on an intellectual level that the market generates a lot of opportunities, but FOMO and the emotions that come with FOMO are often associated with an unmet developmental need that can easily overwhelm one's intellect—which is where willpower comes from—the pre-frontal cortex. Although our pre-frontal cortex—our intellect and willpower—can do many wonderful things, most of our mental functioning is outside of present awareness, subconscious. Think of an iceberg. The part you can see above water is just the tip; most of it is below the surface. Mental functioning is similar.

Another way of approaching impatience is looking at it from the perspective of why does the trader have such a strong need for immediate gratification? If our life is not very satisfying, if we don't experience much contentedness outside of trading, it greatly increases the chances that the trader will have a higher need for immediate gratification in trading—which is often expressed as impatience. I was talking to a neuroscientist I know at Stanford, Jodie Trafdon, PhD, who has identified specific types of neurons and levels of key neurotransmitters associated with the need for immediate gratification—brain research with rats, monkeys, and humans all show similar results—the experience of low satisfaction or low contentedness in life is associated with impulsive behavior that is an attempt to grab a reward. The remedy with this approach is to teach the trader specific ways to increase the experience of gratitude in their life to counteract the need for immediate gratification. Gratitude will slow down an impatient trader.

What awesome advice for the trader who suffers from FOMO!

And the hits just keep on coming with Prep. Prep was not only impatient and guilty of blaming others, but he also failed to follow his giveback rule.

Follow Your Giveback Rule

Traders should develop a giveback rule; that is, if you give back a certain percentage of your profits on the day, then close your positions. No trading should take place for the rest of the day. Yes, swing traders and hedge fund traders should also adopt a giveback rule.

This rule should be developed by the individual trader, in consultation with the head of a firm's risk management, and based on how that individual trades. Then the trader should trust the risk administrator to enforce this rule, protecting the traders from themselves. Some traders swing more and thus should have a larger giveback rule, and others such as scalpers should have a tighter giveback rule. A good giveback rule for most traders is 30 percent of your closed P&L.

At SMB we ask our traders to close out their intraday positions if they have given back 30 percent of their trading profits for the day. We do this only after they have had a profitable open. So if an SMB trader is flat or barely positive after the open, then this rule does not apply. But say a trader is up over $1,000 on the open, then he should not give back more than $300.

A profitable open varies among traders. For some not yet consistently profitable traders like Prep, $500 on the open may be considered a profitable open for which now the giveback rule should be followed. Our analysis of trading data suggests if our traders follow this rule, they will take home a significant amount more at the end of the month.

More advanced traders may amend the giveback rule to a mandatory 10-minute break after they have hit their giveback rule. And then the ability to trade again after their self-imposed break with a very tight stop. Having a rule that makes sense to you and is monitored by your risk administrator is more important than the details of the rule.

Prep struggled with his giveback rule more than anyone on the desk. He could make PnL; he just couldn't keep it. Do you struggle with this? Worse, he often ignored his giveback rule. The following is an e-mail exchange between Prep and me highlighting his failure to follow this rule.

Prep:

> Bella,
>
> Today was a very tough day for me. I need to cut my size in half tomorrow. My trading confidence is very low right now and I am really frustrated with trading right now.
>
> I was having a great morning and trading a few opening drive plays (DIS and BWLD). I have definitely improved on trading opening drive plays over the last couple of months. Within three or four trades, I went from positive to negative and I couldn't make a winning trade after that.
>
> I need to stay away from extremely tight consolidation plays. When something consolidates within a few cents for more than 15 or 20 minutes, that is a death trap; these plays do not work. I was sizing up in plays that make sense to me and losing in them. Short TWX into a pullback rollover, short CVH consolidating at the low with a seller below the previous buyers' dropout. Plays that worked a month ago are just not working; I don't know what else to do but to lighten up and wait for the market to show me what is really working.
>
> I don't see many plays from this week that really make sense and have worked out. I am just very frustrated with trading right now. I don't even attribute my losses today to not being disciplined to the giveback rule; I lost so much in just a few minutes I had no chance to be concerned about the giveback rule. Also I was having a good day really early and I wanted to try to press it to have a great day. I don't know; I need to get my head on straight. Let me know if you have any thoughts. Thanks, Bella.

Bella:

> Weren't you up 500 today? How is it possible you then were not positive?

Prep:

I was up with an open P&L of 500 *(this means he had not yet closed his open position but was marked as up $500)*, most of which was BWLD, which I took a 150 rip in; my highest closed P&L was just under 300.

Bella:

l looked over after the open and you were up over $400.

Prep:

I don’t think that is correct. Regardless if you think I am okay with my actions, I am not. I am beside myself, Bella. This is unacceptable and I will not let this happen again. I know what I did, but I also know that dwelling on my mistakes today when I come in to work tomorrow is the last thing I should do. I should learn from today, move on, and get better.

Bella:

Yeah, but the giveback rule is not voluntary. Look at the effect at not following this rule. You went from positive almost 500 net to negative 650 net. You went from positive for the month to negative. You should be sitting with a positive 300 day.

This is not an e-mail about P&L. This is an e-mail about progress. You must have a giveback rule that you follow. I am merely pointing out the effect it had on your month.

With Prep, it takes a few times of asking before he gets it. The next month after he failed to follow his giveback rule, I asked him to come talk to me.

Bella:

You were following a rule away from having a $2.5k week. Which is 10k for the month.

Prep:

What do you mean?

Bella:

Come talk to me and I will explain. Bring your numbers from this past week.

I sat with him and showed him the data that proved if he had followed his giveback rule, he would have had a solid week as compared to his reality, a negative trading week. He received a few days on the demo for his lack of compliance. Others on our desk have struggled to develop the proper giveback rule for their trading and follow it.

What Is Your Giveback Rule?

In his daily trading review, a trainee wrote with disgust about giving back too much of his early profits:

> I really hate what I did today. Basically gave back 90 percent of my net on the day by trading like a jack***. It just started with one bad trade and snowballed into a few more, and before I knew it, I just quit for the day. It's a shame too; I thought I was trading really well with CIE and ORCL. Mid-day, I nailed that CIE reversal and I called out the 14.80 breakout on INCY, and it seemed like I wasn't doing much wrong. Then I made my worst trade with too much size (buying immediately into a pullback on INCY) and it just got worse from there.

The rest of his review consisted of a lot of "I am a jack*** this and that." He's not, and my response was:

> This is not an issue of you being a jack***. This is you not having a giveback rule. You were up $$$ *(P&L numbers redacted for compliance reasons).* Lose $$$$. STOP TRADING. TIME OUT. Create a rule for yourself.

Earlier in that day, Steve told me about coaching an experienced trader to shut it down. He was up nicely, lost some, and then lost some more. Steve pinged the trader, cautioning not to give back more. The trader gave back more and then a little more. Steve personally went over and suggested to close it out for the day.

Later I wrote this to our desk:

> Guys, I am seeing the same issue and spotting the same problem on the desk. If you have a positive open and you give back 30 percent, shut down your trading for the day or at least until after a long time out. It is very common for HFs to shut it down for the month or week or quarter after such a giveback. Develop a giveback rule for yourself and send your personal rule to us.

One trainee responded:

> As a developing trader, I will not give back more than 50 percent of what I earned on the open. In the event I breach the 50 percent

> rule, I will close my Lightspeed account for the day and analyze what I did wrong. As I increase share size, this rule will be reevaluated.

So I ask: What is your giveback rule? And if you do not have one, shouldn't you develop one?

Now you can overhear Prep consider his giveback rule into the close as he talks to himself. "I am $80 away from my giveback rule. That trade is not worth it for me." That is excellent progress by Prep.

So now for Prep's next big challenge.

Consider the Big Picture

At the start of our SMB AM meeting, we discuss the Big Picture. For us, this means the important SPY levels, what is most moving the markets and each stock we discuss. You cannot make a good trading decision without also considering the Big Picture for the market and your stock.

As I write, it is June 26, 2012, at 8:27 a.m. EST and our morning meeting is 23 minutes from beginning. We will discuss the most important levels in SPY. For example, if SPY 137 is a huge technical resistance level and we are near that level, then you should consider trimming or closing your long positions no matter how strong they appear. The most important element of your trade at this moment is that the market is near important resistance. Most likely this will cause the market to pull back and your stocks to trade lower as well. We will update what is most important to consider in Europe for the week. We will mention that the U. S. Supreme Court is expected to announce its decision on The Affordable Care Act (ACA) and to watch healthcare stocks such as AET, CI, UNH, and WLP. I shot Steve this e-mail before the start of the week discussing a possible overturn of the ACA and its impact on the markets:

> You may want to mention for the desk to be aware to watch healthcare stocks if the Supreme Court ruling comes down this week. It is expected Monday–Thursday.
>
> Starting to hear that it could be overturned (would most take the SC seriously anymore if they did?)
>
> Not sure whether the whole bill or just a part (single payer).
>
> You may want to prepare the desk for this catalyst.

This is us covering the Big Picture for the market. If you are not doing this daily, you are not a pro trader.

Drilling down even further, when you are trading a stock, you must know its story. What makes the stock move? Is there a catalyst in the stock? If that catalyst changes, then all that price action that you have seen of late may be irrelevant. New prices most likely will be created for the stock since a catalyst has been removed. If you do not know what is moving your stock, then you cannot properly determine your risk. That is a fundamental trading error.

Before I proceed with how Prep screwed up again, combining analyses of the Big Picture with individual stock stories is not what Steve and I did when we started out together. I can't just follow individual companies and price action anymore. I have to read things about government policy and the balance of Congressional power that was once only the domain of DC policy wonks and political science Ph.D. candidates. I have to examine whether small countries with no industrial economies to speak of are going to default on their debts. I have to worry about the Federal Reserve throwing more money at too-big-to-fail banks, only to have the too-big-to-fail banks just throw printed money back at the Fed on deposit and not lend it out to those who need it. Can't I just trade? The background analysis I need to make informed decisions is substantially higher than ever before.

Back to Prep. He made such an error that Steve spotted and sent me an e-mail to get fixed. A few days before that, Prep had knocked on my trading door looking all dejected. Having experience with hundreds of similar trader psychology sessions, mainly Prep just wanted me to listen and tell him that things would be better. I did. But we teach traders to always find a solution. We teach our traders to learn from their trading mistakes. And we ask for them to analyze their trading objectively so they can fix problems that are holding them back.

The market does not have a vendetta against them.

Stocks were not created to screw them.

"I am just having the worst luck" is usually code for fixable trading mistakes. So after the Steve e-mail, I pinged Prep to fix that fundamental trading mistake that he had made.

Bella:

You keep getting all frustrated about trades, and then when we drill down, there are reasons why many of your trades aren't working. The mistake today in PGN CANNOT happen again. Attention to detail. Go talk to Steve.

Prep:

I realize that PGN was a merger and knew that going into it, but I thought negative comments on the likelihood changed that? I will go talk to Steve.

Steve:

Before we chat about this, please answer a couple of questions for me. One, why did you write in your PlayBook that it was trading higher Friday on a "rumor"? That is either sloppy on your part or not knowing the news.

Why would you trade a stock for a "gap fill" when its price action is not being determined by its gap but on the price action of a different stock?

Prep:

Okay, in terms of the news, I guess I didn't fully understand what was going on. The stock was gapping up because regulators considered new conditions for the takeover of PGN two days ago by DUK. Both drove down on the open yesterday, and I looked for news and found on my think-or-swim that JPM had negative comments on the takeover, so I thought that maybe there were merger/arb firms driving the stock down or firms that believed in the takeover that were selling their positions.

The intraday chart looked like a nice bear flag and there was a seller at the whole. The problem, which you pointed out, was that I wasn't aware that it was trading off DUK. I see the charts from yesterday and they are almost identical. When DUK popped off the low, I should have covered my PGN/should have just been trading DUK if I wanted to make that play.

I know it is pointless to trade stocks that are being taken over, but my thoughts were that it was a second day play and that someone didn't like the merger and it could drive back down to the price it gapped up from. It was in a clear downtrend, consolidating at lows

> and making new lows. I understand that I should have been watching DUK and I won't trade mergers like that again.

Oh, Prep, a year into his Wall Street career, and he's pretending to be one of the great arbitrageurs of the 1980s. If he wants to pretend to be Carl Icahn or John Paulson (the pre-2011 version), I'm happy to support his doing so with someone else's capital!

Fast-forward a month, and I was leaving my poolside seat in Bermuda on a four-day getaway. I piped back into the desk at the hotel lounge and found this e-mail from Steve pointing out another fundamental mistake from Prep not understanding the Big Picture.

Steve wrote:

> I was kind of surprised. Got this chat from someone who has been trading more than a year. The market had broken all recent support and was in a perfect downtrend.
>
> 2:32p Prep: Steve, thoughts on a bounce now?
>
> 2:33p (SMB) sspencer: Markets don't usually bounce on trend days.
>
> 2:33p (SMB) sspencer: There may be some type of retracement but bounce very unlikely.

Learning the nuances that move markets is the last lesson traders learn. With Prep, it was one lesson at a time after one bad trade at a time.

You have a choice as a trader. You can either do the work to find your mistakes and improve. Or you can become an expert in all the ways of all excuses: that the market, the financial media, your firm, its partners, the air conditioning, your trading computer, your trading platform, dark pools, algorithms, tech support, your clearing firm, your trading neighbors, regulators, the exchanges, the floor manager, your trading data, and your significant other are screwing you. It's up to you.

Negative Self-Talk

Prep also had periods of self-destructive review. This is common. I correct this flaw in almost every trader I coach. It infects every conscious trading moment. It can be the silent killer for the hopeful, consistently profitable trader. Following is an example of Prep caught in a web of negative self-talk that does not help you improve at anything. And it's a raw and honet look at what super-ambitious, developing traders experience during low moments as pro traders. Are you guilty of this?

> I am an ***hole. I had a comeback going. At 2:20 p.m. I was down $23 after being down all day. I was calm and selective and thoughtful all mid-day and into the 2:30 hour. I lost $250 of open P&L in 30 minutes in GNC, KORS, NKE SMG. I am such an A**.
>
> It is quadruple witching (*the day on which contracts for stock index futures, stock index options, stock options, and single stock futures all expire is referred to as quadruple witching)* Friday, and I am tick trading GNC and KORS. All I had to do was not trade today, and I would have finished my second week in a row positive. Now I am flat for the week and an idiot. I went way over my stopout and I am an idiot. I was putting together what would have been seven out of the last ten days positive, and now that is ruined because I am an idiot. The sad thing about KORS and NKE is that I was right and I couldn't stay in the stocks; I was right and I didn't give NKE and KORS the extra room for the shake.
>
> I am writing this review right now and watching my stocks rip up higher. It makes me sick to my stomach to watch this, but this is what I deserve. RIG, I had the right idea but it didn't look like it was going to move, so I timed myself out of my position. AOL, piker stock in the middle of the range. QCOM, I liked on the short side, but it was wrong and I hit out. NAV was pinned to 30 for options expiration. SMG, I thought was going to be great but reversed when the market popped. I can't wait to come to work on Monday, but I have all weekend to think about never making a mistake like this again. QUAD WITCH SUMMER FRIDAY, and I am pressing my positions at 2:45 p.m. after slowly grinding back and being so calm and selective all day. TIMING IS EVERYTHING, if I had waited 10 more minutes, I would have made chops in KORS and NKE. There are so many lessons to be learned from today, and I have all weekend to think about how to never make these mistakes again.
>
> **Things I did poorly today**

• I traded way too many names during the first 1.5 hours of trading. There was no reason to be trading, let alone during the first 1.5 hours. I tried trading NKE and lost a bunch of times. RIG was just in a range on the open. NAV had a nice opening drive that I missed. I tried to buy the pullback, but it was just above below.

• KORS, this stock was difficult right on the open. Step back and look at the big picture.

• I got so obsessive when I started to make a comeback that I wasn't thinking clearly. I worked way too hard all day to make a comeback and then p***ed it away.

• Stick to the game plan and that nonsense doesn't happen in KORS. NKE, you can't do anything about that; that is just terrible luck. Gave it 3 pennies extra.

• Traded way too many tickets, and I did half of them within 30 minutes, from 245 to 315. I get that it is a good time to look for stocks, but that is just unacceptable when I am trading 300 shares.

Things I did well

• GNC should have made a lot more but I caught 2 points in it, was down a chunk in it before that.

• I was in the right stocks: NKE, KORS, GNC.

Next Week

Next week is so important for me. I have a few goals. First, I want to be positive four out of five days. And I want one of those days to be Tuesday. I want to make sure to be extremely selective and that means trading six stocks until 3 p.m. I also want to trade no more than 20 tickets if I am trading with 300 shares. If I am down and not seeing anything good, I want to make sure to take a break. I get in trouble when I get fixated on stocks and do not take a break. I need to put today behind me and refocus and continue to make progress and get better each day, **I honestly felt like over the past two weeks my trading has improved, and today the market just taught me a lesson.**

Bella's comments:

In the future, let's stick with the facts and not vilify ourselves:

- I lost money into the close because of XYZ.
- I did that because of 123.
- Next time I will not do that because of ABC.
- There is a ton of good in your review to build on next week: the comeback, the recognition of how you could have improved your day, and a feeling of trading improvement supported by data.

Soon thereafter we ran into the same issue of Prep being unproductively hard on himself. I noticed after the close Prep cursing at himself under his breath for missed trades.

Bella:

> I kinda don't understand why you guys spend so much time beating yourselves up. After an underperforming day, reevaluate. Set a new daily improvement plan. Execute on that plan and you will improve. Why so much emphasis on the results of one day?

Prep:

> It has been three weeks of bad results. That is why I am so rough on myself. I realize that you can work hard without preparing. I don't know; I've just been super frustrated with my performance. I feel like I am making trades that make sense and they aren't yielding the same results that they used to. I also am rough on myself because I haven't made any money yet, and sometimes it's hard mentally to go a year without making money and still keep at it because it's what you love to do.

Bella:

> I guess I just don't see the world (trading game) that way. You are in a bad streak. You have to stop it. How do you do this? You aren't making money. How do you start making at least some? Do those things. I guess I just don't understand spending too much energy on anything else save doing those things.

Prep continued to work on this area of his trading game. It takes time and practice to learn how to talk constructively in real-time to your trading self.

> As if all of those other challenges were not enough, Prep faced yet another challenge.

You Are Trading Too Many Stocks

Carlton and I spend time every Monday around noon in my office reviewing the results of our desk from the prior week. We flag certain issues, such as overtrading and traders on whom we need to cut risk. Further, we focus on who is doing well and discuss how we can get them making more. Prep got flagged for overtrading one week, and we held a closed door meeting with him.

He'd had a nice gross profit week but barely kept any of his gains because of overtrading. Our core traders trade at our cost (we do not mark up commissions), and then they earn a profit split, so this was not a case of overly high commissions eating away trading profits. When we flag an issue, our first approach is to raise the weakness with the trader and then let him work on a solution.

A few days after our talk, we received this e-mail from Prep acknowledging the issue. The first step in solving a trading problem is acknowledging there is a problem, kind of like those 12-step programs. Goodness knows, I've done plenty of trader "rehab" with Prep.

> Bella, here is my review from today. I really need to figure out why I have been trading too many stocks and overtrading. I don't want to be scared to trade but I am really going to have to lighten up on my trading until this improves, **which means trading 10 or fewer symbols** and under 25k shares.
>
> It just needs to happen, writing all these tickets and losing in a bunch of crappy stocks is what needs to disappear in order to get me to the next level, which I think is becoming consistently profitable. I spoke to Steve briefly today and he suggested, strongly, that I see a trading coach because the problem is psychological and that I will never make money unless I figure out how to get rid of my overtrading/being in too many bad stocks problem.
>
> I am reviewing my trading from today. I had a pretty bad day, and out of the 13 stocks I traded, 2 were good setups that I made money in (not nearly enough size and didn't catch enough of the move), 3 were setups that with better execution I would have made money in, 2 were good setups that just didn't work and I would

make these trades 9 out of 10 times, 1 was a premarket trade that didn't work, 4 were just bad positions that I shouldn't have been in, and the last 2 were small plays that I was barely risking anything in and just wanted to see if they worked.

That means that only 1 out of 4 of my trades, approximately, were really worth trading and had the potential to move, 5 out of 13; I need that to be closer to 50 percent each day, which means being more selective, having better execution with fewer tickets, and really thinking before I make a trade instead of just jumping in.

Please let me know if you have any thoughts on how to fix this problem; I know this is something I NEED to conquer to get to the next level. Thanks, Bella.

So Prep identified the issue and started to think about a solution. The problem was his daily reviews did not show signs of progress. He was still overtrading commensurate with his P&L and skill level.

After a trading session, Prep sent me a daily trading review of the following stocks (see Figure 7.1). He traded 15 stocks. I thought: What is he running, a portfolio? This is intraday trading. GMan can cover that many stocks but not Prep. Not now.

Positions #2

Position	Symbol	Price	+/-Pos	Last Price	Cost Basis	Closed P&L	Executions
0	AMLN	24.87	0.00	24.2045	.00	+169.60	75
0	BBY	24.21	0.00	24.6146	.00	+6.00	26
0	BIG	43.08	0.00	42.9384	.00	+128.00	42
0	CHTP	2.65	0.00	2.693	.00	-40.00	16
0	CMC	14.13	0.00	14.39	.00	-20.00	8
0	CTRP	21.16	0.00	21.30	.00	-25.00	7
0	GMCR	48.35	0.00	48.18	.00	+76.50	29
0	ILMN	52.25	0.00	52.53	.00	+46.08	64
0	MHS	70.82	0.00	70.726	.00	+42.00	8
0	MOS	56.06	0.00	55.5460	.00	-6.00	12
0	PNR	47.18	0.00	47.14	.00	-160.07	59
0	PSS	20.13	0.00	19.9957	.00	-83.00	17
0	RHT	59.18	0.00	61.35	.00	-104.80	21
0	UNH	57.98	0.00	57.3403	.00	+81.00	27
0	WAG	33.82	0.00	33.9095	.00	-51.00	9
0	ALL		0.00			+54.31	420

Figure 7.1

I responded in an e-mail simply:

> TOO MANY STOCKS!!!!!!!!!
>
> TOO MANY STOCKS!!!!!!!!!

A week later Steve flagged Prep's overtrading on his risk monitor:

> Prep,
>
> As far as I am concerned, every guy on the desk can develop their own style that works best for them. But what traders should not do is repeat the same mistakes over and over and over and over again. When you continue to do the same things repeatedly that harm your results, the outcome will always be the same. I'm glad that you have taken the step to work with Dr. Menaker on your issues, which hopefully will get you over the learning curve to profitability.
>
> In the meantime, you have continued to do many of the same things that have prevented you from reaching your potential. Today should have been a profitable day for you as you made money in both GMCR and MCP. But you chose to be involved in an additional ten names and thus barely be net positive. The lack of a significant positive day today has a huge impact on your end-of-month numbers.
>
> Steve

A few trading sessions later and I caught the same nonsense. Prep was trading way too many stocks. I sent him this e-mail:

> There is no reason for you to trade more than eight stocks. Set that as a rule. You have to see the big picture and start concentrating on where the real money can come from. Just trading 15 stocks and hoping something works is not a good process. You have to learn what is more likely to work.
>
> Prep replied, "Understood."

A few days later, another review arrived with a dozen stocks traded. Perhaps I'd been too much of an enabler here, but he was just not getting it.

Bella:

> You told me recently you would keep it to eight stocks. You didn't today. Your results last week and to end the month are

irresponsible and cause for a timeout. You cannot lose money that consistently being an intraday trader without making changes that lead to making some money and stopping the losses.

You had no idea on the open today that we had been very weak the past few sessions and weren't even ready to consider that into your trading on the open until I brought it up. This is a lack of preparation both mentally and work-wise.

Why are you trading feelers when you aren't making money in stocks you are watching more closely? The way you go from losing to positive is to watch a smaller number of stocks more closely and find the very best entries for those stocks...like the MAT into the close that you mentioned. I am harming your progress if I don't bench you tomorrow. You have to follow rules to progress. You have to cut bad streaks.

You have to make changes when you are going badly so that under no circumstances will you be positive the next few trading sessions. Do not trade more than six stocks going forward.

Prep:

Bella, I understand what you are saying. Maybe I do need to be benched, but to say that there is a lack of preparation is a very frustrating thing to hear. I am literally the first person in the office every morning, and I have an extensive routine looking over nearly 300 stocks and reading several news sites, as well as reviewing my work from the previous day and writing in my journal for Dr. Menaker. Preparation is not my problem. I understand that I need to end this losing streak and that maybe I deserve to be on the demo, but it is frustrating to me that this is the day that it falls on. If you don't think I have been beating myself up over being on a losing streak and working my hardest to try to fix whatever is wrong, then you are mistaken. I know I said I would keep it to eight stocks, but I slipped up.

(A quick aside here: my guys hate it when I challenge their work ethic and preparation. Man I love them taking that personally. They should. Me saying you do not work hard is me saying you are not one of us. And our guys hate that!)

Bella:

Isn't it possible to work hard but be unprepared?

A week later Prep again exceeded the maximum number of stocks he could trade intraday. This was starting to get ridiculous. Had I gone from adult coach to kindergarten teacher here? Timeouts? Rules on the number of toys (stocks in our case) that he could play with? Was I going to stick him with the next training class as if I were holding him back before going to first grade because he needed another year of "maturity"? I swear these things crossed my mind. Didn't someone write a book called *Everything I Need to Know I Learned in Kindergarten* or something like that?

Bella:

Why did you trade seven stocks?

Prep *(knowing what is coming)*:

I hear you, Bella. Demo tomorrow.

I wrote about that in my review. It was a mistake; I didn't realize I had done six; I instantly realized it was wrong but didn't take the trade off because the risk was already laid out.

Bella:

Here's what I don't get with you and your buddy Ryan.

You guys want to trade more stocks as if this is some sign you are better traders, yet neither [one] of you consistently [is] big in your best plays and this is exactly how you make money.

AND to be big means you have to really watch your stock, so doesn't that mean it's better to trade [fewer] stocks and watch them more carefully and work on being bigger consistently and then growing the stocks you cover?

Prep:

I absolutely agree that it is better to be in fewer stocks, and I have been doing better because of it. I did not mean to trade that seventh stock. I realized it and regretted it instantly but kept the trade on. I realize that trading fewer symbols is the key and will continue to trade six symbols at the most.

Over time we allowed Prep to trade a few more stocks intraday. But his maximum was still eight stocks. Every so often he would knock on my door and ask, "Bella, can I trade one more stock? (*ABC stock*) is really setting up nicely, and I have been watching it closely." I give my permission. If he goes over by one stock, it is not an issue now. We have identified the issue, he has worked on it, he has made excellent progress not covering too many stocks, and we have a system in place to help him succeed.

And now onto our next issue with Prep.

Making Money Starts with Being Professional

Our desk had one of its better days of the year on a Thursday. Truth be told, there was a night of drinks after the winning trading session. The next day, about five traders from our core cut out early on a Friday. It was a gorgeous summer Friday that tempted them to leave after lunch. A guy like Prep, who had struggled to be net positive for his entire existence as an SMB trainee, should have stuck around. Unfortunately, Prep bit. A huge opportunity continued in NAV that these traders had crushed on Thursday and the start of the Friday trading session. They left easy money on the table. I was livid. I sent a personal e-mail to each of the traders who bailed early.

Bella to Prep:

> Why did you leave early today?
>
> NAV!!!!!

Prep to Bella:

> I didn't want to give back any more to be honest. Is that wrong? I felt like the right thing to do was to lock it in after a comeback from being down. How do you feel about that? Obviously, the NAV trade was a great setup, but I thought because I am trying to be more consistent it was better to be disciplined than to push it. I don't know if that was right and maybe I was trading my P&L too much, but I am less worried about missing trades right now and more worried about locking it in. Let me know your thoughts.
>
> Some advice: When you are in a hole, stop digging.

And this was me purposely nastier than I normally get.

> I was going to bump you up next week.
>
> Now I am not.
>
> You figure out if it was a good idea to leave on a Friday with an opportunity like NAV.

> If you want to enjoy the weather, move to California.
>
> This is a trading job.

Prep:

> But you are absolutely right; I should not have left. Period.

Teaching traders to be professional and what that entails is more important than teaching them trade setups. Trading mentors should overreact at a sniff of unprofessional trader behavior. Do not let a minute go by without ending this behavior. If you want to do what you want to do when you want to do it, then trading is not your sport. The market demands your consistent attendance. Unprofessional traders will never execute on the setups taught to them if they are not able to show up prepared and alert and committed to a full day of work every day.

First comes the professional trader. Only then can the trader become consistently profitable.

And then there was the issue of Prep trading on tilt.

Trading on Tilt

The most common challenge for the intraday trader is trading on tilt. "Tilt" is actually a borrowed poker term in which a player bets aggressively out of emotion and without too much pre-bet analysis.

There is so much failure in our business that it is nearly impossible to spend the entire time trading in the zone as Mark Douglas would recommend from *Trading in the Zone.* Traders must learn to decrease the periods they trade on tilt.

Prep sent me a review outlining his difficulty controlling his emotions in real-time:

> Completely undisciplined today. If this were sports, I would be doing sprints after practice. I am extremely upset at myself. MAKO really hurt me today. I made a great point and a half–two point trade in it and then gave it all back and then more being an absolute idiot. I gave back 50 percent of my highest unclosed P&L; that is way too much. My giveback rule is 30 percent, and I disregarded it because I was mad that I had given back so much and I wanted to make it back.

> That is trading on tilt and doing the wrong thing. Go for a walk and come back refocused. This is the second day in a row I have been stubborn and on tilt. DO NOT GET FIXATED ON A PLAY. Why are you doing this? Be objective and do the right thing. If you hit your mark, there is a 30 percent giveback rule. No exceptions. It is more important to be disciplined than to make money!!! GET IT THROUGH YOUR HEAD. I haven't been this frustrated with myself in a few weeks.

In another review, Prep again highlighted the issue of trading on tilt:

> Terrible trading day. Wrong on everything. JPM just bought four or five times and was wrong. ILMN, are you kidding me? Second day in a row I have been wicked out by some BS play even when I gave it the appropriate room and the stock just tanks. Such bull****. I'll show the chart in a minute. VRTX, I don't know what else to do there. I am right on the idea and I give it the real stop and it gets me out. I am so frustrated, and I am on tilt. This week was incredibly frustrating. I feel like I am doing the right things and just not getting paid for it. I probably risked too much in JPM and INFY, but it wasn't because I was trading with lots of size (I wasn't trading with more than 400); it was because I was just wrong a bunch of times. I am really frustrated with today, and I need to step back and look at my week and day when I am not ****ing angry.

After another review, I commented to him about working to control his emotions:

> My sense is Shark was on to something. The RSH trade was not a good idea. But then you got into some stocks that 1) had moved away from prices, 2) you could define your risk, 3) there was more room to go in the direction of the trend. You trade these plays well. Spend most of your energy on them. You have to make sense of this and internalize what you want to see. This seems to be where most of your effort should be. Also you have got to relax. You make me nervous sitting next to you. It's a long day. All the huffiness about the plays that you are in that are not working is such a waste of energy. Spend that energy learning why you were in a crap stocks. Spend that time searching and asking others for trending good stocks.

Trading on tilt often comes from being in the wrong stocks. That day after the Supreme Court ruling, Spencer offered feedback to those banging and screaming and complaining. It was simple and eloquent: “Some stocks are good. Some stocks are s****y. Stop looking at the s****y ones.”

I sometimes notice Prep overreacting to a trade gone wrong. It’s hard to miss as he pushes back his trading seat, puts his head between his knees, and grabs his hair.

“Why are you so upset?” I ask.

And then he explains how the trade didn’t work out because of this reason or that reason. He takes the negative trade personally. He seems to do a world-class job of being in all those moves that are screw jobs. I wonder what that means about his trading. That cannot be a coincidence or just plain old lousy luck.

“It was a good trade. You cannot control the results,” I continue.

“I know, Bella. You are right.”

If you sit near Prep, you can feel him place his personal worth into a trade. If it works, he is smart. If it doesn’t, he is a failure. This is a tough way to spend the trading day. Especially since we play a game in which we will be wrong an awful lot.

I recommended that Prep talk with Dr. Menaker about improving his mental game. I set up the call between coach and trader. A few weeks later, I learned that Prep had negotiated one session and only one session with Dr. Menaker. Arggggh. How would that help?

He needed a good six months with Dr. Menaker to improve his mental game. Dr. Menaker surely agreed to only one session as a favor to me and on the assumption that Prep would soon ask for more help. Dr. Menaker assumed correctly, and there were more sessions.

Dr. Menaker gave Prep some mental drills, like writing down his emotions before, during, and after trades. Dr. Menaker teaches his students that just the act of writing your thoughts on paper can calm them down and help frame a better context for their trading. The mindset is not to win on each trade or you are a failure. It’s how do students help themselves get in as many good risk/reward trades that make sense to them and then let the results take care of themselves. Evaluating with pen to paper your most important trades can help you see that a losing trade may not have been a bad trade. And it certainly is not a signal you are a loser.

Finding the Solutions

> "Never discourage anyone...who continually makes progress, no matter how slow."
>
> —Plato

Believe it or not, we were still working with Prep after all these mistakes. He was still not consistently positive. We scaled back our risk on him because the data didn't support added firm exposure. With a lowered intraday loss limit, recently Carlton flagged Prep. He placed Prep on the demo. (I've lost count of how many times I've placed Prep on the demo at this point.)

Next came an e-mail from Prep:

> Bella, I really disagree with your decision to put me on the demo. I realize that I went over my stop and I have not been making money for the firm, but it's not making me any better to put me on the demo. I would like to discuss this in person if you are available this morning. Thanks.

He remained on the demo.

Prep had been making progress from corrected flaw to corrected flaw. I could sense he was so close. And then it happened. He had the best day on our desk. And then again. And then again. He ran off three-plus weeks of best days bested. $1200, $1300, $1500, $1800, $2000. His mindset shifted from doubt to "how do I make 2k plus." In his personal swing account there were chirps about significant chops.

This was not just a trading hot streak, but, with this much data, a changed trader. His trading was cleaner. The outbursts quieter and shorter. He started leading other traders into the best setups. His trading was in control. His growth was growing the confidence of other traders. Even after all of those mistakes and time as an underperforming trader, there was no doubt that he had arrived and showed he was going to now be the trader I always knew he could be.

Now let's take a look at a trade in JCP that Prep prepared for us. It is One Good Trade that caused our desk to take a serious loss. I was sitting in the Chicago office of Linda Raschke, a legendary trader featured in *The New Market Wizards*, talking about the format of this book. Instinctively she directed, "Oh, show a losing trade as well. Readers should know not all good traders end well." For those who have never met Raschke, in person she is probably one of the more charismatic people you will ever meet in trading. So following the advice of this prodigious trader and magnetic individual, here is one awesome losing trade. And stay around for the plot twist right after the trade discussion.

Intraday Bear Flag Breakdown (News Spike)

Prep

JCP

6/19/12

Big Picture

- SPY has broken out of its range between 131.25 and 134. The market is grinding up slowly toward the 137 level. There is a reverse head-and-shoulders pattern in both SPY and IWM, and the momentum is to the upside.
- This is not a market play, though.

Intraday Fundamentals

- **Tuesday 11:31 a.m.** Deutsche Bank calls the surprise departure of J.C. Penney's (JCP –10.2 percent) President Michael Francis "a catastrophic blow" for the bull case in the stock, given the timing of the announcement and his short tenure. Mr. Francis was expected to play a key role in revamping the store's image and was considered vital to the store's recruitment of new brands. The firm maintains a Hold rating on the shares. 1 Comment
- [Consumer, On the Move]

• **Tuesday 9:47 a.m.** J.C. Penney (JCP –9.6 percent) takes it on the chin in early trading after its “Dream Team” of executive talent loses one of its marquee names. The buzz on the Street is on whether or not Ron Johnson will be given enough time to see his planned transformation of the retailer start to hit the company’s bottom line. (Earlier: Citi defends JCP) 1 Comment

• [Consumer, On the Move]

• **Tuesday 6:40 a.m.** Shares of J.C. Penney (JCP) fall off 5.5 percent premarket on the news that a top exec is bailing out from the retailer. Citigroup is out with a defense of the Buy-rated company, saying that the management talent pool is still deep and the transformation on track. 2 Comments

• [On the Move, Consumer]

• **Monday 4:33 p.m.** J.C. Penney (JCP) President Michael Francis is leaving the company, effective today, after just nine months on the job. “CEO Ron Johnson will assume direct responsibility and oversight of the company’s marketing and merchandising function.” Shares—down 5 percent in the after-hours.

Technical Analysis

JCP Long-Term Technical Downtrend

JCP Intraday Support 21.50

Reading the Tape

Massive volume being done in the range between 80 cents and 22.00. The stock starts to hold below 90 cents, and then the seller steps down to 85 cents; 80 cents has been support it gets below and starts to move away, takes out the swing low of 70 cents and starts to move; massive volume to the upside that looked like news. The stock reverses all the way to VWAP 22.40 and settles.

Trade Management

Trade Review

- I think the lesson here is that you have to have stops in just for incidents like this. I took terrible cover above 10 cents because I didn't have stops in for all of my size. I think even if you don't think a stock can make it back there, it will save you if you are caught in a news spike.
- The other thing I want to say is that this is an A+ setup and I would make this trade ten out of ten times. I don't think you can be fully loaded until it makes a new low, but until then I think you just have to stay in it with as much size as you can safely play. The target was a point lower and this is a thick stock with a story

behind it. Stay with this and there will be a place where you can really size up.

Trade Idea

JCP long above 22.50 and short below 22.80.

From Our Training Room: One Good Losing Trade with Prep

Know what the market players are most concerned about! In this case, someone leaving the Eurozone. Now this was less likely causing a stronger market.

BELLA: Now for the trade review with Prep, our desk and me. JCP yesterday had earnings. We'll just walk through the play and discuss this setup. It's a really good setup.

PREP: So in terms of the big picture. The market in general, we were kind of consolidating at 131 to 134. Two days ago, we broke out of that range to the upside. Over the weekend we had some news from Greece. That was kind of a big catalyst. So we were grinding slowly since then and the market had some upward momentum....

If you are not having fun while you are learning then someone is not teaching you very well.

BELLA: Let's just spend a little more time on that because my hair cutter asked about it. He asked, "What do you think about the market?" So I said, "It all depends on Europe." He said, "I don't think the market is going anywhere before the election. What do you think?" I said, "It all depends on Europe, hoping this wouldn't upset him and cause him to mess up my haircut."

And then he cut the three hairs I have left on my head. *(Bella says smiling and rubbing his bald head.) (Traders laugh.)*

What's so funny? (*Bella says smiling. Traders laugh.*)

Okay for our market, we all are concerned about Europe right now. For the big picture, we certainly have to understand the story in Europe. What news out of Europe can spook our markets? What news out of Europe will be received positively? So anyone wants to give us a rundown of some of the speed bumps with Europe? Again, we are not fundamental analysts. But we do need to understand what can move the market. What the market is most apprehensive about. Anyone wants to give it a shot? Memo?

He is our smartest trader!

MEMO *(originally from Turkey)*: Whether Europe has a bailout or not. That's the main concern we have.

BELLA: Is there going to be a bailout? Is Greece going to accept the bailout? There's concern about Spain and Italy as well. So a really bad scenario for the U.S. market, many people think would be if a bailout cannot be agreed to by Germany or Greece. If, for whatever reason, Greece says "I'm walking; I'm not part of the Eurozone any longer," then there would be uncertainty with the Euro. The market sells uncertainty. It shoots first and asks questions later. Meaning the big boys sell first and then reevaluate. That would be an interesting trading opportunity **almost certainly** to the downside. We are certainly focusing on that.

Never be certain about anything in the market. Almost certainly should be about as confident as you get.

There's news that Greece is going to vote for the bailout. It looks like they have a deal, in which case that's good for the market as this breeds more certainty for investors. Some people say price action is most important. Price is the only thing that pays, so goes the saying. Above 134, then, the market technically is strong, right? Then above there, 137 is the next resistance level. But we have had low volume of late, correct? So that dampens our confidence. With more volume, we would feel more confident about the strength of this market.

Think through the pros AND cons of your trading thesis and not just all the things that support your position.

BELLA: So low volume is not good. Good above 134. Next level is definitely 137. Low volume is not great, though. What do you got? What's next?

PREP: Just in terms of intraday fundamentals. The first thing with JCP is their CEO left their company after earnings. They are kind of replacing some of their guys with AAPL marketing guys, and basically it hasn't helped the stock at all. There was an initial bounce, but their numbers just weren't good enough, so they have been selling off the stock...kind of in a steady downtrend after that initial run-up. The numbers were not great. As you can see from the top headline number. The president of their company called it a catastrophic blow. So they reported numbers and the CEO left the company.

A well-respected CEO leaving a company usually receives selling from the Street. If this company is going to do well going forward, why would he leave is the thinking?

BELLA: Sometimes that can happen. **If somebody leaves the company that the Street respects, that can cause some selling.** Obviously, the underlying thought process is, "This is a talented person; why would they leave if this was a good opportunity for them?" Is there something wrong with this company causing this talented manager to leave? Maybe the company is in for some rough patches, and that's why he is leaving.

PREP: This is the multiyear. This is the two-year *(Figure 7.2)*. You can see this initial run-up last summer. Then it pretty much sold off back to the 35 level.

Figure 7.2

BELLA: So there's a longer-term support level that you guys are taking a look at, right?

PREP: Twenty-three?

> *When a stock is weak, go find the next important technical support level.*

BELLA: Twenty-one and a half?

PREP: Twenty-three was the upside.

BELLA: You have to go back a long way. So in September of 2010, we are sort of looking at this level. This 21.50 is where the stock seems to start a pretty nice move up toward above 40. And so when we take a look at charts, we want to look at the psychology of the market players. At what inflection points are a majority of the market participants voting this stock is strong? At what prices are a majority of the traders voting this stock is weak? At what prices are players confident the stock is going higher? At what prices are people psychologically selling the stock? Above this 21.50 and it has been relatively clean up toward 40 after it finally got above that short period of consolidation at 21.50. I don't think it's the best level, the most significant level. Anyone want to give their judgment from 1 to 10 on how important that 21.50 would be to them?

PREP: Probably like a 6.5 or something.

BELLA: Anyone with a lower number?

SHARK: Five.

BELLA: What do you think, Shark? Five?

SHARK: It's just so long ago.

BELLA: It's so long ago right?

PREP: But that's only level down there. Maybe it just gets run over, but that's the downside target.

BELLA: I don't think the answer is important, whether you think it's a 7 or 5. But I do think that every time you actually take a look at a level that you yourself should judge how strong, how important, that level is, and develop some skills and some experience with determining how important the level is for you. **So every time you find a level, ask how important it is from 1 to 10 to you.** Ask yourself that question. Give it number. So Prep gives this a 7 and Shark says 5.

I love when our guys challenge each other.

PREP: Well, in terms of the daily chart. I don't think it's a huge level, but in terms of intraday, this stock is down over 10 percent. So someone is going to look for some support to cover a position. Maybe someone is buying here, but here seems like a reasonable place to cover, at least some of your position, if it starts to work.

(*Bella sees Shark disagreeing.)*

BELLA: Shark?

SHARK: Why are they covering it?

PREP: I mean if you just look, there's no support until that level. For short-term traders, that is where they might look to cover.

BELLA: So what's next? We have a question about how important that level is. Good. That's for you guys to decide. *(Bella smiling)* And Prep, Shark would like to meet you outside after this Tradecast.

(Traders laugh)

PREP: I usually look at the six-month chart. In terms of like a 200-day, two years. But as you can see. There's no level, and it's in a downtrend. It can go down a lot harder. This is a pretty good setup.

BELLA: Definitely in a downtrend right? From 43.50ish.

PREP: This is the weekly and the 15-minute chart *(Figure 7.3)*. Just want to show you some of the action here. This is the premarket action. After hours and premarket, it kind of drops and the support is 23. That's the first level there. It really just hammered through there.

Figure 7.3

BELLA: So why do you look at that chart? Why is that chart important to you?

PREP: It shows the action last week. It's somewhat irrelevant in this chart since there's a big gap there. Maybe it holds above 23; I'm looking at this next support level from last week, the place where I bought it.

BELLA: But is it overall an important chart to you, the weekly 15 minutes?

PREP: I mean I just like to look at the price action over the last week or so. Especially when you look at stuff that gaps up and down. Just in terms of levels and maybe volume over the last week. Prices that people have been trading the stock at. But in terms of the big picture, maybe it's not as important.

> *Look at scores of charts with the same indicators and time frames for 6 months before determining the effectiveness for you of this technical approach.*

BELLA: Okay, great. **When you sift through charts, develop a consistent system that makes sense to you.** Repeat that system. This is how you will build skill relating to viewing charts for a trading edge. It is most important for you to be consistent. It is most important for you to develop a system of chart viewing that makes sense for your trading brain. As opposed to thinking there is some Holy Grail chart-viewing approach to the markets. There isn't. It's the daily and consistent work of viewing your charts that creates your trading edge using charts as an indicator.

PREP: *(Reading the tape slide.)* On the intraday, there's a massive amount of volume done this day in general between 80 cents and the whole number. Below 22, just holding below there. There's a seller at 90 cents, and it kind of just floated around there and lifted a little bit. The real out was above the whole number. But there's just a ton of volume. That indicates that toward the end of the day, maybe it's going to break one way or the other. And all those people who are on the wrong side of the trade doing all the volume are going to be wrong. Around 2 p.m. the seller is selling at 90 cents. Then he steps down and sells 85 cents, and you can short more and keep it tight. And then it breaks through the 87-cent level where all the volume is done. That's your confirmation to really get shorter!

The swing low is 70 cents. It gets to that 70 cents, and basically a buyer came in at 68 cents or so, reversed the stock, pumped in like a million shares, and there was a new spike. I got stopped out above the whole number.

Breaking news can change all the intraday data you have about a stock. Be connected to a good newsfeed.

BELLA: Just for the record. What was the news that caused JCP to spike?

PREP: Their sales forecast pattern looked good.

BELLA: And they announced that?

PREP: Yes.

BELLA: Okay. So there's breaking news, some positive breaking news. Okay. So this can materially change how the stock trades. **Every print prior intraday may now be irrelevant because of this breaking news.**

Our guys like to short at or near VWAP when a stock has pushed quickly below and then returns to VWAP on low volume.

PREP: So trade management *(Figure 7.4)*. JCP drives down on the open. I think it's actually the first trade below that 22.50 or whatever...well below the premarket low. The real trade begins when it drives down and then pulls back and holds the intraday VWAP. It pulls back and holds below this intraday VWAP and the whole number. So maybe you enter around here for your first lot and just kind of wait for confirmation of holding below this 20-cent range here. But you enter here with one lot, and your out is above these little wicks.

Figure 7.4

BELLA: What was the price to cover above the wicks, 22.05?

PREP: Around 6 or 9 cents. It continues to hold VWAP. It's just floating all day; you are waiting for it to either break out of the range or stop you out. It's holding and then...

BELLA: Let's just...I don't want you to lose your train of thought but...explain...if you take away VWAP and look at this chart, you see resistance at 22. So how are you using VWAP to help you be more confident that JCP is going to trend down?

PREP: I like that VWAP starts to hold below the whole (*Figure 7.4*). That means they are doing the majority of their volume lower and lower. VWAP is trending down. That means the volume is done lower and lower where there's a 95 cents or 97 cents. They are not doing it nearly as much at the whole as they were doing early in the day, which means there's a lot of pressure on the stock. I just like to use VWAP as an indicator.

> *A better short is when VWAP is trending down, or as we say curving down.*

BELLA: **VWAP is best as an indicator when it is curving to the downside.**

PREP: Moving in the direction, which I think it starts to do here (*area from 11 a.m. to 1 p.m. on Figure 7.4*). There's really not much going on during the middle of the day. You probably shouldn't be trading during the middle of the day right now anyway. Around 2 p.m. or so, around 1:35, this volume starts to pick up again on the five-minute. You can really see that JCP starts to hold this 90 cents. The seller just comes back and holds this 90 cents.

> *When you see a buyer continuing to hold the same level, we say that is an intraday technical level for which to trade off of. Below that level and we want to get short or shorter.*

Maybe you can enter again and have...I would take off a little bit above 90 cents...maybe just, if you have two lots, maybe take off a quarter or something. The real stop is still above that 5 cents. It could get back up, the seller could lift, you want to sell it higher, but...this 85 cents comes in and he sells again and I think you are still just holding those two lots. Then it drops 80 cents. I think that's your confirmation. It hasn't broken this range all day. It breaks the range, and that's your confirmation to really load the boat at that point on the short side.

BELLA: So we can look at the chart, and we can see that 21.80 is an intraday level. So the question for the trader is if we touch 21.79, is that enough for us add to our short, or do we need to see the seller hold below 21.80 before we add to our short? For you, how did you play that?

PREP: For me, I hit the 79 cents. JCP hadn't dropped that 80-cent level. There's enough volume and momentum that if you are long into this at 3:00 or 2:30 whenever this happens, they drop the 80 bid. I think if you are long, you don't want to see what's below that really. So you hit out immediately.

So I think it's more of a momentum play, and you can pile in there. You have the 85-cent seller to protect you if it doesn't go your way.

BELLA: Having said that, though, you're more of an aggressive trader than a conservative trader, correct?

(Prep nodding and smiling)

BELLA: Anyone in the room need to actually see JCP hold below 21.80 before they add to their position?

(Nate and MQP raising their hands)

BELLA: Okay.

(Traders laughing)

> *There are no right answers in trading. There is the right answer on how YOU want to attack a setup.*

MQP: Let's see if it holds below 21.80, and by the time it did show me that it was going to stay below...

BELLA: But MQP, having heard what Prep said, how would you feel if it just dropped below 21.80 and plummeted?

MQP: Yeah, I missed it. I did miss a chunk of it. Yeah, absolutely. That's something I need to work on.

BELLA: Well, I don't know if you have to work on it, but I just...you do have to think about the risk you are taking by not hitting right away below this important intraday support level, 21.80. Ryan?

RYAN: I'm more concerned with it too, but in that case I do agree with Prep and the uptick rule as well. So you might not get the chance to really get in there with the uptick rule. If it made the big move there, I would go for it...kind of get pushed down...so the uptick rule I like almost for a quick hit....

> *Please, Iceman would have been max short and not even caring if the stock ticked against him.*

ICEMAN: Also the time of the day.

RYAN: Yeah, in the time of the day, we don't.

BELLA: What do you mean by "the time of the day, we don't"?

ICEMAN: There has not been very good follow-through in the market place of late. The market has been terrible. And stocks have not been moving midday and following through.

BELLA: What about that fact that the market has not been following through of late? When Shark decided to go on his fancy cruise, for the last three days, we've had the worst three trading days in five years. It's like you have some sort of deal with the devil, Shark. I mean, he went away and the market just was miserable; he just took the market with him. It's all really strange.

SHARK: I have good timing, I guess.

(Traders laugh)

Golf not tennis.

BELLA: You alluded to this before, Prep. It's a certain time of the day we probably should not be getting short or anyway, but there is a thought process that we have three miserable days. The firm has done terrible, and the volume has been terrible. It has been very illiquid. You had to trade the market perfectly for three days not to get chopped up. It's like playing the U.S. Open; if you just break even, you would be a superstar. So that's the context of the three days before we traded this JCP. Having said that, does that give you a little bit more pause to hit 79 cents as opposed to waiting for JCP to hold 80 cents?

PREP: I would say no. There's so much volume done relative to how much the stock actually...you know, there's so much relative volume that this is the one stock that can maybe...you know, you can make your day and really make a big chop. I definitely agree that the market right now...you just have to look for that one stock each day if there is one. I thought we had three bad days...everyone was, there's a lot of volume done, there're some players in this.

BELLA: All right, anyone else?

SHARK: When you're on vacation, is the market going to come back?

I took a vacation? Now that I do not remember.

BELLA: When I'm on vacation? When I go on vacation, the market will go straight up. Everyone just get long. Hold until I come back on

Wednesday. Anyone else actually want to see the stock hold below 21.80 and have a reason why? Pippen, I thought you did that.

PIPPEN: I tried that. At 11 a.m. it went to 29 cents and I shorted two lots and I have to cover that. So after seeing that at 11 a.m., I kind of waited for a little bit longer around 79 cents. I really want to see time spent below 80 cents.

BELLA: Okay, so my...

PIPPEN: I mean I really want to see it spend time there....

> *New traders need to be more nuanced with their trading rules. Past failure may not mean another failure. Be skeptical of reentry but still willing under the best of circumstances.*

BELLA: So my question to you is, so you tried it before, tried to hit JCP when it got below 80 cents before and didn't work out. Because of that, you want to see it hold below 21.80?

SWANG: I want to see it spend time....

BELLA: But I guess my follow-up question to you is that was 11 a.m. and now it's 2:15; that's a lot of time. A lot of time has passed since you tried it and didn't work. Rethinking about it, not to get you to change your mind, but rethinking about it, should you as a trader say...I like your thinking, which is, "It didn't work; I want to see JCP hold below 80c"? But I wonder if a more nuanced algorithm for you is, "I have to see it hold below 21.80 unless three hours pass and a lot of volume is done and it never actually peeks below 21.80. Then after that, it's actually worth it for me to hit 79 cents again"?

PIPPEN: When you said you would drop at 79 cents because of the uptick rule, are you shorting beforehand or trying to sneak in an offer below 80?

BELLA: You just didn't answer the question.

(Traders laughing)

BELLA: My question is again, given the facts...I understand you are saying, "I tried it, it didn't work, let me adjust." Excellent, that's excellent trading. My question to you: Could you have been even more excellent and say, "I'm going to hit it again, or I'm trying to get short as soon as it gets below 21.80 again"?

Pippen: Yeah. I mean I shorted 75c; it's around the price.

BELLA: Okay, all right. Let's keep going.

PREP: So the news spike comes in.

(Traders laughing)

PREP: I actually...

BELLA: I'm sorry...just want to clarify this for the newer guys. So 22 is an area to short. A bending downtrend of VWAP at 90 cents is an area to short. Below 21.80 is an opportunity to short. Below 21.70 is an opportunity to add to your short.

What we want to do is keep adding to this position while it's working for us. You want to try getting bigger, right? Okay, so we've done that when JCP gets below 21.80. I think the firm is pretty big on the short side, right Carlton? I mean everyone's in it, right?

CARLTON: I would say 80 percent of the firm, Bella.

BELLA: And pretty big? So go ahead, so...

PREP: So basically you wouldn't want to hit more. Maybe cover some in front of the low. Then if it starts getting below the low then...

BELLA: Did it get down to the low?

PREP: No. It got stuck. It got to 68 cents or somewhere around there.

BELLA: All right. So no Reason2Cover.

PREP: No Reason2Cover, yeah.

BELLA: But thinking about if it got above that 21.55ish area to cover?

PREP: Definitely not all of it.

BELLA: But not Shark. Shark is not covering down there.

PREP: News spike comes in and I actually got stopped out of my position.

*Ah, s*** happens. It's all a part of trading.*

BELLA: Well, the stop didn't work, right? Did anyone actually have stops in and they actually worked?

SHARK: They worked for me.

PREP: I only got 100 shares.

BELLA: Shark, not only did you take the market with you, but you are the only one whose stops worked.

SHARK: If you actually put them in, they work.

(Traders laugh)

BELLA: But Pippen, your stops didn't work, right? Anyone else have stops that worked? Iceman? Memo? Pippen, how come yours didn't work? Anyone else have stops that didn't work?

(Traders discussing)

BELLA: Okay thanks. So you didn't have any stops in Prep?

PREP: I had stops in for half of my position.

BELLA: All right and how many? Considering how you trade, we will talk in lots. Each lot is a tier. So one lot or one tier. How many lots did you have?

PREP: Three lots and...

> *With a big position, often I put in automatic stops. This helps me handle the extra size. I know my risk is controlled with these automatic stops.*

BELLA: All right, let's just stop there. So you have three lots in a position. The question is should you have some automatic stops in? So that's my question to you. So next time you are long three lots or you are short three lots, do you think you should put in automatic stops, and if so, where should you put them?

PREP: As we discussed before, you should definitely have some automatic stops, even if you don't think you can get hit, just in case something like this happens. But I was a quarter in the money, and JCP really started to work. At the time I was like...

BELLA: But that isn't relevant, right? That's not relevant. The fact that you are in the money is not relevant. The question is, when you attack a similar pattern like this again, what are you going to do?

PREP: I'm definitely going to keep one lot, the initial lot, until above the whole. I think reasonable places to put stops are, above 85 or 90 cents for the second lot, and maybe above 80 cents for another lot. I usually give it an extra penny like 82 cents.

BELLA: So stops at 82 cents?

PREP: Eighty-two, 92 cents, and 2 cents.

BELLA: I think, Steven, that's where you had your stops, right?

SWANG: I got like 81 and above the whole.

Your job as a trader is to ask: What is the right thing to do? And then do it! It's not to make money in a position.

BELLA: So I just want to offer this idea. This is helpful to me, which is, a lot of times when you start to get bigger, you get apprehensive to cover. You don't want to give back your open P&L. And a really helpful thing to do, for me, is to set automatic stops and let the stops do their thing. **So if you are short three or four lots and you have an issue of covering too early, one of the things that's helpful is just to say "Look, this is either going to go to my target price, or I'm going to get stopped out. What's the right thing to do?"** The right thing to do is if I'm this big, it's to get stopped out. So I just put my stops in and I let myself get stopped out. (Move the stops up as the trade is working for you.) That's a very helpful thing when you are trading with bigger size. Not to cover too early in a position like this. Anyone do something similar?

(A few traders raise their hands.)

BELLA: So think about that. Anyone have any questions about that technique? It's too easy to sit there and think "I'm too big, I'm too big. Oh, my god, I'm up some money; let me cover it now and have a really good day." That's not the right thing to do, right? It's a cover when it's a cover. Covering too early in your best setups should be viewed the same as a trading loss.

And as you are actually learning to get bigger, it's really hard to hold a big position with all that open P&L staring at you. When you are really big in a stock, I promise you that you will find so many important buyers and important levels that you would never have found if you were just short one lot. It's important to come up with techniques to help yourself not cover too early. **If you cannot hold SIZE like you would with one lot, then you cannot add SIZE. If you cannot hold SIZE for the completion of the move, then you are just adding risk to your trading. Either learn to hold the SIZE, or else do not add the SIZE.** All right, so you got stopped out. What else do you got?

PREP: Flip it long. Not for a full three lot. Definitely for one lot.

Flip means to go from short to flat to long, in this case. The breaking news, the amount of volume done near 21.80, and *the clearing of 22 as a level made this a Flip Trade to consider.*

BELLA: Flip it long where?

PREP: When it started to hold above the whole.

BELLA: Above 22?

PREP: If you are some big momo fund *(momentum strategy fund)*, you are going to put in the squeeze right there. Some of the really big players down there get caught the wrong way. I think they can squeeze it to 23.50. But I think you can definitely get long for at least some.

BELLA: Good point. What else?

Well said Prep!

PREP: In terms of trade review, we talked about having stops in. The other thing is this is a really good setup you want to be in even if it's slow. **But this is an A+ setup, and I will make this trade over and over again regardless of the news spike**. If you do the right thing, it's about the probabilities.

BELLA: Good example because I don't think anyone since we have been doing the PlayBook exercise has sent me plays that didn't work out in their PlayBook, and you should get into the habit of including them as well. And I think it will help you understand that your job is to do the right thing. If the trade doesn't work, it's not a big deal. I mean there's nothing you can do about this play. There's no way for you to predict there was going to be breaking news in the stock. You would have had to violate some federal securities laws to know this was going to happen, which we don't do. Was there anything about the price action, was there anything in your preparation that could alert you that this breaking news might be coming?

PREP: I think TO called out there's news right now...like he just saw something different right away on the tape and then the offers were taken to 80 cents, and I was just not quick enough to get out. That was maybe the one thing I could have noticed.

BELLA: But there wasn't a stubborn new buyer below 70 cents demonstrating a character change in the stock intraday?

PREP: No, not at all.

BELLA: That foreshadowed news might be coming?

(Prep shaking his head)

BELLA: Okay. I mean, it's an A+ setup, right? Good. I actually just want to highlight one more thing, which is, all right, you got screwed. You had a big position. I know the firm took a big rip. But there was another opportunity there, above 22. If we had taken that opportunity, we would still have been very positive, right?

PREP: It was difficult for us to get long.

BELLA: I agree. I agree. What's your last slide for us?

PREP: Trade idea. Short below 21.80 if it's holding below there today and long above 22.50.

BELLA: All right, good. Any questions?

> *After a trading disappointment, keep an open mind to an even better market opportunity.*

(Traders silent)

BELLA: Okay, thank you. Newest guys, you can stay.

(Old traders leaving the room)

The Plot Twist

A few days after my feeling great about Prep's progress, I received an urgent text from him before one open.

"Bella, can I meet with you before the Open?"

At the firm, we met in my office.

"Bella, this is the last week I am going to be at SMB. I am not leaving for another firm. I have decided to go work for my dad. He owns many successful companies, and I am going to learn one of them and then hopefully one day run it."

Then he assured me he would continue trading—in his thinkorswim personal account.

My thoughts?

> God grant me the serenity
> to accept the things I cannot change;
> courage to change the things I can;
> and wisdom to know the difference.

8. We Are All Rudy

I worry that some think they are “special” before they turn pro. As if the day they walk onto a trading floor, they are on second base, far ahead of other new traders. Perhaps they have a high IQ, hold an 800 math SAT score, were a champion athlete, or possess the latest trending “special” characteristic, now poker player. If they do view themselves as special, this makes their trading journey more difficult. Worse yet, if we believe in this rubbish that the special have an easier path, this idea discourages those without these characteristics to mistakenly believe they have a lesser chance. Further, all of this undervalues the pro trader reality that you must be able to execute in real-time. Many who develop a PlayBook of trades that are best for them cannot properly execute these setups when the lights are turned on. Let’s meet a young man I trained whom many (including himself) would mistake as special and debunk some of these myths. This will give you a truer path to *Consistently Profitable Trader* (CPT).

My Gchat lit up with a message from Spencer: “I didn’t realize Rudy still works with us.” To not know that a trader is still with the firm can’t be a great sign for the trader.

Rudy is one of the smartest traders I have trained. He was raised in Middle America in a small town where no one was even close to as smart as him. He matriculated to a prestigious university to which Irish Catholic parents dream about sending their sons. Hint: think *Rudy*. For the first time in his young life, the smartest kid in his hometown met a community of thousands as smart as him, yet he still stood out.

In college, Rudy used his sharp mind to become a professional poker player. *The Leadership Secrets of Attila the Hun* just couldn’t hold his regular attendance. Interact with him on the trading floor, and it is hard to miss the ease of calculations for which he is capable. You talk with him about a trading setup and its risk/reward, and he gets it two sentences in and spends the next five bored with you.

Rudy is different. He looks different, with some unusually curly hair and old-school glasses, which give him the appearance of some hip 1960s rocker. I vote Buddy Holly and Rudy as look-a-likes. During a chat with him while strolling the streets of the Upper West Side after Sunday pizza with some new traders (my treat), you cannot help but feel the comprehensive thought he gives to each of your statements. Unfortunately, our trading data suggests this boy wonder mind might just not be enough in our game.

Let's remember how you become a CPT. Not only do you have to do acquire all of the domain knowledge that the market requires to be great. This is a matter of trading passion not high IQ or athletic prowess. But then you have to be able to execute. Even if super smart meant you could learn the patterns that would work for you more succinctly, which it doesn't, that would still leave you with the massive challenge of executing in real-time. Literally, you could read this book, develop the most amazing PlayBook for you, and still never make a dime because you couldn't execute. A firm can teach you well, you can be a great candidate on paper, but you still may not be able to play our game.

Spencer sat at our conference table with a glorious view of the Statue of Liberty, joshing with Freudberg about the realities of teaching new intraday traders. Freudberg teaches a systematic approach with options that present lesser frustrations for the teacher. Spencer asked, "If I outline a trade to make during our a.m. meeting, all of our traders will crush that trade, right?" Spencer waited for an answer that never came. He continued, "Wrong! And that is the essence of trading. Can you execute?" Spencer could have been thinking of Rudy during this diatribe. That Rudy possesses intellectual gifts is not necessarily a prequel to his being a franchise trader, possessor of solid execution skills.

Rudy's story shines a bright light on the nonsense that there can be special new traders. We will dive deeper into those considered special by the Street. Do poker players make for better traders? We will hear from some who have done both. Is possessing a mastermind enough to become a CPT? Then we will shift to pro trade execution and some challenges traders might confront.

The truth is most of us come to the Street more like Rudy (from the classic movie *Rudy*), the undersized, underdog, son of a steelworker, who achieved his lifelong dream of playing at football giant Notre Dame. The market only pays those who have developed a PlayBook. Coming without one (whether smart, athletic, or skilled in gaming) leaves us with a challenge of a lifetime. In a globally competitive market with landmines in every tick for our markets, this is a climb up Mount Kilimanjaro. Start with the mindset that you are a Rudy.

At the end of all of this, you will gain admission to a trade discussion between Rudy and me. Memorably, after this review, Special Projects approached me chuckling and said, “Bella, that was just brutal. You destroyed Rudy during that review.” I don’t see it that way. I critiqued a trader who required my critical feedback. Anyway, it makes for an entertaining review.

The Blue-Collar Trader

Your first test as a trader is to see whether you can absorb all the domain knowledge you must to become a fundamentally sound trader. This is not rocket science. This is a passion test. Do you love trading enough to take the time to learn everything about your subject to build a strong trading base? Think of your journey as a blue-collar trader.

A large swath of this trading base is your PlayBook. Will you take the time to develop a PlayBook that makes sense to you? You cannot just copy this PlayBook from a CPT. You certainly should co-opt trades from other traders and absorb their thinking behind these setups. But then you must roll up your sleeves and do the work to make these setups your own. Wear your hard hat as this is a daily grind sidestepping danger as you have seen from the ultimate blue-collar work ethic traders, Shark and TO.

The building of your PlayBook is an everyday event after the close—when you are tired, perhaps hungry or emotionally worn out from a day of trading combat. Staying in your seat and archiving the best trading setup of that session for you is the lonely work required. And if you are a newb, you should do more. Not only should you archive a PlayBook trade that made the most sense to you but you should also review other PlayBook trades from experienced traders. Learn how they think through a setup. See what setups they view as excellent risk/reward opportunities. Perhaps you can lift that trade for your trading and make it your own. Perhaps you need to ask that experienced trader a few questions about his PlayBook trade to fully grasp it. Building your trading coliseum, the PlayBook, is a Roman effort.

This work needs to be done daily and forever. Based on research and based on my experience as a mentor and coach, I worry for that trader who thinks he is special. If you think you are special, and I suggest that you do the daily work of building your PlayBook, you are more likely to think you do not have to do it. *Ah, that exercise is for the unspecial, Bella*. Worse, when those who believe they are gifted struggle at the start, research shows they will be more discouraged. You are supposed to be a talent. You expect to crush the markets from day one. Yeah, the market doesn't care. The market cares that you develop skill in her game.

Let's consider the spreading Street myth that poker players make for great trading candidates.

Do Poker Players Make Better Traders?

Inside the world of trading, a debate has ensued about whether poker players inherently make for good traders. The number of poker players trying or thinking of trying our game has increased. Rudy came from that world. In fact, Rudy's poker assets were frozen during the government shutdown of online poker. The Department of Justice seized the U.S.-based assets of the biggest Internet poker sites. Since 2006, it has been "illegal" to play online, but the feds didn't crack down on it until April 15, 2011. Rudy had his money with the second largest poker site, Full Tilt Poker. The site was mixing working capital with player deposits and didn't have enough money at the time to immediately pay back all players. Fast-forward to now, when FTP has finally found a buyer. The biggest poker site is acquiring FTP's assets through a deal with the DOJ. Rudy expected to get some money back before the end of the year. Hedge funds have considered hiring their game's talent. Blogs rage with discussions on the similarities between the sports and whether a poker player like Chris Moneymaker would excel as a trading moneymaker. Admittedly, we assumed poker players would make for better traders.

For those who do not follow poker, Chris Moneymaker, with a Master's degree in accounting, was just a normal guy living the suburban life in Tennessee until he saw the movie *Rounders.* In the movie, Matt Damon, as a former gambler, returns to the poker tables to help a friend in need of money. Becoming motivated to play, Moneymaker looked for local poker tables. Having no success, he went online and started to play. Starting with small amounts of money, Moneymaker started to win tournaments consistently on PokerStars.com, until he finally gained the opportunity to enter the biggest and most prestigious poker event in the world, aptly named the World Series of Poker in Las Vegas. The tournament is televised on ESPN, and winners become part of our pop culture. Moneymaker shocked the world by winning the championship in 2003 and instantly became famous for turning his initial

$39 deposit into millions. Could someone like Moneymaker or some high-level poker player turn his attention to trading and have a similar anonymous-to-star trader journey?

You Become Great at Your Passion

I asked an SMB trader whose brother is an elite professional poker player whether poker players would make for good traders. This trader has an inside seat into the world of prop trading and high stakes, professional poker. Here is his insight:

> There is certainly a good amount of overlap between playing poker professionally and being a professional trader. My brother, who has been playing professionally for about 12 years now, has absolutely no regard for money. This makes him an excellent poker player. When he sits down at the highest stakes games in the world where six-figure swings are commonplace, he is not thinking about making money. He is thinking about how to maximize value on every hand, and make good risk/reward decisions.
>
> I would venture to guess that a good poker player would make a good trader, but good traders don't necessarily make the best poker players. I hear stories of Wall Street guys coming to play in the underground NYC games and donating small fortunes to the pros on a regular basis. It makes me cringe when I tell someone I trade for a living, and their response is "Oh, isn't that like gambling?" First of all, let me preface my poker remarks with a quick detour by saying that pulling a lever and hoping for three cherries is gambling. Throwing your chip down on a spinning wheel is gambling. There is no *skill* to pulling a lever. But there is a skill to trading. Now, as for poker specifically, even if you're playing the game at the highest level, there is still an element of luck involved. There are only 52 cards in a deck. You can make all the right decisions and get unlucky. This is called *running below expected value.* And vice versa, you can make poor decisions and be rewarded for it. In trading, once you get to a certain point, there is little to no luck involved.
>
> In the economy that we are in right now, hedge funds and trading desks have an abundance of overqualified individuals from which

to choose. But once a year, these recruiters head to Las Vegas for the World Series of Poker to look for new talent. I even heard of one trading desk that requires of the candidates during the interview process to play a few hands of poker to see how they make decisions under uncertainty. After what is now known as Black Friday, when the world of online poker came to a halt, you can bet that a large percentage of these online players looked for employment on Wall Street. Instead of having 16 tables of poker spread across 4 monitors, they would now be looking at 16 charts of stocks.

These former online poker players are generally very analytical thinkers who excel in high-pressure situations. They also have an ability to control their emotions when real money is on the line. If you get steamrolled in a $1/$2 game, you don't move up to $5/$10 to try to get back your losses. This same principle applies to trading. If you make three bad trades in a row, you don't double up your size on the fourth trade.

It should come as no surprise that some of the top fund managers today started off by playing poker. After graduating from Princeton, Carl Icahn started his fund with his poker winnings. James Simons of Renaissance Technologies started off playing poker at MIT, and parlayed that into a hedge fund that is largely based on gambling-related concepts. Steve Cohen of SAC Capital played poker while attending Wharton, and said that it taught him how to take risks.

Bankroll management is a very important aspect of both poker and trading. I remember at the end of 2009, sitting behind my brother while he played heads-up $1,000/$2,000 against one of the best heads-up players in the world. Over the course of one hour, he lost $700,000. I was awestruck, but my brother just sat in front of his monitor with absolutely no emotion. As a result of this, I learned the importance of bankroll management, and it has helped me tremendously over the course of my trading career. I told myself that if I ever had that kind of money, I would never lose it. In trading and poker, often the most important element is preserving your capital and living to fight another day. The market will always be there, and likewise the casinos will always be there to gladly collect the rake.

It also really comes down to being passionate about what you do. In the same way prop traders stick around after the market closes to talk to their peers about how they traded a certain play and what they could have done better, good poker players are always discussing how they played certain hands and what they could have done to extract more value.

Rudy erred in assuming that his past poker gaming would provide him a significant head start as a trader, if not guarantee success. On his first day live, he overtraded. His trading volume exceeded our starting guidelines by 300 percent. That is like an NBA rookie strolling down the court and shooting every possession. He was immediately put on the demo and ushered in for a talk with Carlton and me. Well, this was another bad sign.

Nervously, he entered with a look of someone trying to escape this perceived sequestration. We had a calm conversation about the probable negative result of starting too quickly. He peered at the closed door as if getting on the other side of it was a secret mission. I wasn't waterboarding the poor kid; I was talking with him. I shared two anecdotes about super-bright past traders who had made the same mistake and were managed out of the firm. Next, I shared my interaction with a large hedge fund that had thought about hiring poker players as their stable of future great traders.

"Mike, what do you think about our fund hiring poker players to trade?" asked the hedge fund member.

"I think it is a terrible idea," I replied, not wanting to waste the busy gentleman's time.

"Why?"

"Because people who are great at poker are great because they love poker. People who are great at trading are great because they love trading."

"How do we know they wouldn't love trading?"

"Because they aren't trading."

"Oh. I guess that is a good point. Well, we are kicking it around internally here."

"It's a horrible idea. I would wish you good luck, but I know how the story will end if you guys try it."

This multibillion-dollar fund never implemented the program.

When I finished, Rudy looked up at Carlton and me and asked, “Is that it?”

“Yes.”

“Oh, I thought you guys were gonna yell at me.”

He was relieved I didn’t yell at him? I wanted to after that comment. Admittedly, I can really rip a trader who underperforms like Rudy had. However, I would have hoped Rudy wasn’t so interested in escaping this session and was instead recognizing what he had to do better.

To expand on the preceding point, poker players who love trading can become good traders. In fact, I was at dinner with a large group of traders on the Upper West Side when a hedge fund manager shared that his best new trader made seven figures in his first year of trading after leaving the world of pro poker playing. But I’ve also seen a number of former poker players at prop firms fail miserably because a love of trading wasn’t there. Worse, it’s the complete lack of an understanding and willingness to be good at our game and build trading skills that concerns me the most. These guys were “shooters” taking outsized chances, addicted to the win and loss of it all, and not making controlled risk/reward trading decisions. There are casinos for those gentlemen (and I hear the Bellagio has an excellent buffet), but not trading floors.

As for Rudy, he’s still with us after achieving a better understanding of what the market expects from him through daily discipline from Carlton. I asked Rudy whether he thought poker players would make for good traders. His response showed growth of mindset and humility, particularly on the importance of being professional:

> Bella, I do believe poker players are more likely to become good traders. What separates good poker players from bad ones is the ability to patiently wait for favorable opportunities and put your money to work when it counts. The blinds (forces bets) in poker will slowly eat at your stack while you wait, but in trading, there is nothing forcing a person to enter a position.
>
> Furthermore, what separates great poker players from good ones is the ability to read the small nuances in subjective information. I have played millions of poker hands online, and I see the same players regularly. After a while, I learned their patterns and would

notice when they deviated from them. It takes a similar ability to read order flow and judge a stock's pattern.

SMB says that you are only as good as the stocks you trade. Ironically enough, table selection is the skill that has the largest effect on poker profits. You are only as good as the players you play against. Once I developed the discipline to no longer allow certain players to sit on my left (giving them the advantage of acting after me), I noticed a huge increase in my poker profits. As you can find table selection near the top of any list by Googling "most important poker skills," this is not simply my personal belief.

However, I've noticed some glaring problems when making a switch from poker to trading. First of all, poker rewards aggression and table control. In almost all situations it is better to be aggressive rather than passive (over the long term). A trader coming from poker must adapt to the fact that he is no longer in control and that his aggression must be *very* selective. This is the major hurdle I have struggled to overcome.

Second, there is speed. Man, if I could slow time down like some sort of superhero, the market would be easy. If a poker player needs more time, he gets it. However, the market waits for no one. You can't just lower the [number] of tables you are playing because you're unfocused that day. Poker allows each player to adjust his own speed from the start. Poker players moving to trading have to know that they will be forced to wait years before they are really comfortable with the speed of the markets.

Lastly, there is routine. [We] poker players enjoy the luxury of being able to play at any time we want and to sleep as long as we want. With sleep being so important for both poker and trading, the poker player must discipline his daily routine a lot more than even the average nine-to-five worker. This sounds relatively simple to the average person, but most poker players have had years and years of this freedom. It does take time to completely adjust.

Poker players do have what it takes to be traders as long as they are willing to take the time to adapt. All good poker players are great at adapting. Trading just takes a lot of time to adapt to.

Okay, so maybe poker players are not a sure bet to succeed, but those who possess a gifted mind must be, right?

Is a Gifted Mind Enough to Become a Great Trader?

During training, there are classroom lecture moments when I ask for an answer from the class. I await the answer, relishing that a tough question causes the trader to struggle and thus learn more. Challenged to answer a question that causes deep thought and struggle are your most productive learning moments. I cringe when a newbie offers an overconfident response. A sick-to-my-stomach feeling manifests if a student gives an answer that's too macro comprehensive. I get faint, in a bad way, if a trainee responds with economic theory supporting his conclusion. When students think they are so smart, I watch them. Closely. It is a red flag of future failure.

It is not that we do not like smart. We love smart. Heck, you cannot get any smarter than my three partners: JK, Spencer, and GMan. JK makes Spencer look slow. And Spencer scored above the 97th percentile on his LSATs the night after I got him drunk at UConn, and the test conditions were 90 degrees with no AC and a loud lawnmower interfering with his thought. What we do not like is those who think that being smart starts them on second base. Those training sessions can tell me all I need to know about the mindset of the new trader. Show me that you think you are smarter than the others in the market and that is determinative of success, and I ride your a$$ till you get that silly thought out of your mind.

Enter VP, a former Wall Street employee licking his chops to trade. I asked him a simple question about why AAPL had gone up when SPY was strong. Three minutes of Europe talk, he made the rounds of all the interested parties in the euro zone, led to his answer. I looked around searching for TV cameras wondering if he was doing a spot on the BBC rather than sitting as a student in my classroom. I was looking instead for this: because the market was strong. I asked him to stay behind after that learning session for a learning session with me.

Guess who overtraded his first day live? Guess who was the first person to piss me off in his class for coming in late to a midday review because he was watching a position? I scolded, “Watching a position? You have been trading five days. What the hell are you watching with 100 shares that is more important that the next 50 minutes of learning?" I was p*****. Your job is to learn, not pretend your 100 shares is important at this stage of your trading career. He thought I was being an a**, truly surprised I was cursing him out. I thought he was acting like a piker. He even asked to talk with me privately in my office after his lateness.

"Bella, can I talk to you in your office?" I forwarded that e-mail to Carlton with "Handle this, please." The kid either gets over his love affair with his brilliant self or we will manage him out of the firm.

The following is a funny exchange at Indiana University (IU) during a trading lecture. The correlation between GPA and CPT came up.

GPA

I was invited to speak at IU Business School, and during my lecture I asked the room full of college students what they thought it took to land a job on a prop trading desk. One uber-confident, preppy Hoosier, standing in the back at this standing-room only lecture, blurted out, "A high GPA." Ah, a perfect moment to make a teaching point.

I grimaced as if in pain and simply replied, "No." This outburst quickly earned the young man the nickname GPA. I couldn't help myself.

Here is our exchange:

Bella: Let's say you actually want to get a job as a trader. How do you do it? Who has a couple ideas? Who actually has a job as a trader? Raise your hand. Who actually wants a job as a trader? Raise your hand. Okay, so throw out some ideas, you want a job as a trader? What do you do to improve your chances? You, sir.

Student: Network.

Bella: Network. Okay, what else? Yes?

GPA: Um, high GPA.

Bella (*chuckles*): No.

(Students laugh.)

Student: Start trading on your own account.

Bella: Yes, very important. Anyone else? Yes?

Student: Keep up with news.

Bella: Okay, keep up with news. (*Points to GPA*) Again? Let me guess: You have to have really good LSAT scores?

(Students laugh.)

GPA: Oh, no, I was going to say to have a mental edge. Stay fresh.

Bella: Okay. Yes?

Student: Marry a trader's daughter?

(Students laugh.)

Bella (*laughing*): That's pretty good. Okay, so trade. I think you should trade. It's so easy to open up a trading account. It doesn't mean you have to open a $50,000 account. But look, anybody can go to Schwab, E*TRADE, wherever you want to go, and you can paper trade and open up a small account, and you can just start trading. I went to an event in New York. It's actually called the 92nd Street Y Lecture Series, and there was an author there named Daniel Pink who wrote this book *Drive*. Best-selling book. He was in law school, and he was at the bottom of his class, and the reason he was at the bottom of his class was because he wasn't going to class. He wasn't reading about the law; he was writing for $15 an article for a magazine that very few people would read or for $25 bucks he was writing an article that was read by even less.

People would ask him after he wrote this very famous book, "What should you do when you graduate?" And what's the most obvious answer? If you ask your parents what you should do when you graduate, what do they say? My dad told me find something you really love and do it. Has anyone ever been told that?

(Most students nod.)

That's pretty common right? I'm pretty sure most of our parents have said that. Dan actually spins it a little differently. "Don't do what you love, do what you do." And for a future trader that means to trade.

So when I talk about being a trader, being a trader is like playing center field for the New York Yankees. Let's not pretend this is something else. This is not a job where you go to and you stay for

> 30 years. This is not a job where they have an end-of-year review, and if you're mediocre, you're staying.
>
> Trade like that and the market is going to eliminate you. You can be good in some years, and the market is going to eliminate you in other years. You can make seven figures from multiple years and never be able to make a dime for the rest of your life. I've seen it.
>
> The guy that I actually learned from was one of the 50 best traders I've ever seen, and he's made so much money that he's retired. But every once in a while he comes back and he tries to trade and he can't make money. He's not into it anymore; he has a lot of money. He just cannot focus on the work that needs to be done to make money. He doesn't need to make money, so I guess the work is not worth it to him.

To my delightful surprise, a year later, GPA reached out to me via Twitter (notice the *Wall Street* reference).

> @Lunchis4whimps
>
> @MikeBellafiore you may remember me from IU a few years back. You referred to me as "GPA." Just got a new account. Thx for the value.

Of course, I remembered him.

There are skills that may translate from gamer, star athlete, math savant, and academic honors to CPT, but they are not as important or as vast as many believe. You are certainly not going to have an easy path to CPT if you won some money online besting DaddyBigBucks in a game of Texas Hold Em. You are not special as defined as starting on second base. What can gamers learn that would help them as traders?

Mental Agility and Concentration Built from Gaming, But...

A number of hedge funds, trading firms, and investment banks have started to look less at exam scores and more at old-school card-playing and board-playing experience when hiring new recruits. Some firms test new recruits with video games to gauge their decision-making abilities. Other firms make playing games a part of the culture to keep traders mentally agile. Susquehanna International Group (SIG) uses a plethora of games such as poker, chess, and bridge. This is done to teach its traders how to manage risk, take advantage of opponents' weaknesses, and stay cool under pressure. Our firm sat for a few years adjacent to a trading entity controlled by a billionaire proprietary trading magnet, where his traders were encouraged to play a myriad of games to improve their trading. For the record, it was well known that these traders severely underperformed our traders to the point where their traders kept pestering Spencer or me or our traders for guidance. David Einhorn, Steve Cohen, and other hedge fund managers are widely known for being successful in the gaming world, and they all agree that these games are excellent tools for training traders.

Whether it has been from a teacher, coach, or parent, we've all been told in one way or another to concentrate. Whether it's working on homework, practicing a new drill, or even just listening in church, all serious endeavors and undertakings of all kinds have a "higher authority" telling us to concentrate. Thing is, concentration isn't taught as a skill. But understanding the need to concentrate, set goals to steadily increase concentration, take steady breaks, and set aside time to think of things that worry or distract us are all essential tasks that we can accomplish every day to increase our skill of concentration. Like all humans beings, professional athletes constantly battle internal and external distractions, but what makes them great at what they do is having the skill to concentrate at the task at hand and nothing else.

Poker and trading require a number of similar skills needed to master each game, with one that is often overlooked: concentration. Each sport requires your full concentration for hours on end, and when an opportunity finally presents itself, you must be able to make a split-second decision. Understanding that not all trades and hands will be winners, professional traders and poker players have the ability to handle several hands and stocks at one time, always clearly understanding the risk they are holding. The skill that few learn to obtain, though, is handling the resiliency from a loss. Most professional traders and poker players lose a majority of the time, but they allow their profitable trades and hands to outweigh the losers. They enjoy taking small losses and understand that it's just part of the game.

While poker and trading do share several themes in common, a few important differences prevent a poker player from becoming a great trader overnight. In a normal poker game, you have a set number of variables, which means that you can relatively easily predict your odds of winning. In trading, however, an infinite number of variables can affect your trade. From the corresponding futures, to the movement of the euro, to a mutual fund furiously buying, there will always be myriad factors that affect the movement of a stock. Therefore, accurately predicting your odds of success on a single trade will be nearly impossible if you do not have the years' worth of necessary screen time under your belt.

Most important, it is the fiery passion of trading that pushes a trader to get out of bed at the break of dawn. It is not the love of betting or the thirst for money. It is the hunger of learning new trading setups, taking in and comprehending enormous amounts of information the market provides, putting on trades and taking calculated risks, and enjoying the comradeship of other traders.

I played the undercard to Jim Rogers, legendary U.S. investor and author, at Shares Investment Conference 2012 in Singapore. Jim was asked for advice on getting into the markets. He slowed the questioner down. "Do what you love. First, it's hard to figure out what you love. But do that first. I had a passion for learning about the world, which I applied to investing. After you find your passion, then execute. Do all the hard work to become good. Maybe your passion is gardening. If so, start gardening. Open up a gardening shop. Then all around Asia will be your gardening shops. Do what you love doing. Then you will never do a day of work. You will wake up excited for the next day. That is my advice."

Let me be very clear so that you do not miss the point of this chapter. Excellence should always be applauded. A high GPA, an 800 SAT math score, athletic prowess, and mastering a game are all outstanding triumphs. You have my complete respect for such achievement. And some skills such as concentration, a history of working hard, and so on will make it easier to succeed at your next passion. You will have skills that make it easier for you to do the daily work required by the market. You have that history of working at a goal and delaying gratification. But no matter how smart or accomplished in another sport, you still have to do that work. You do not stand on second base. You stand at home with a bat in hand with perhaps better hand-eye coordination or better bat speed. But that still means your work task cannot be ignored, and that it is massive. As the legendary Mr. Rogers said, passion is the key. Do not mistake a passion for one game or life challenge for ease of success at another.

From Rudy's trading journey, next we get to explore the importance of execution. Can you execute in real-time? After you have learned all you need to learn, there is still one humongous challenge for the new trader: execution, execution, execution. You must first be ready to succeed as a trader before you can expect to execute consistently in real-time in the market. We will not exhaust all of the reasons why traders fail to execute. We place a few common reasons in front of you so that you recognize that intellectual comprehension of the game is just step one. And there is a huge step two, which you must work on daily. Throughout the rest of this chapter, we address some common issues that relate to execution that came up with Rudy.

You Cannot Execute If You Don't First Settle Your Personal Issues

Trading is not the place to show up and then attempt to work out your significant psychological issues. A trader case study of Rudy highlights this point. We all come to the marketplace with things to work on personally; Rudy had more serious challenges. Carlton and I had been covering for his unprofessional behavior because of some personal issues. In Carlton's words,

> • Rudy comes into the office late on a regular basis. Most of the excuses for his lateness are unacceptable.
>
> • Rudy hasn't complied with SMB risk parameters since he began trading for SMB. For example, Rudy violated his stop by more than 75 percent on numerous occasions.
>
> • Rudy didn't close out his positions when they went against his stop by more than $0.50 on numerous occasions.
>
> • Rudy doesn't have a detailed schedule or consistent system of reviewing his trades and ideas after the close each day.
>
> • Rudy only performs well when he's kept under strict risk settings and constantly policed.
>
> • Rudy has issues on focusing his trading career. [He] seems distracted by his financial situation or issues not related to trading.
>
> • His medical issues have hindered him from staying focused and coming into the office on a regular basis.

Let's be more specific with our challenge coaching Rudy.

"Carlton, where is Rudy?" I asked via e-mail.

"Bella, he's not trading the open. He claims he has to share a bathroom with his roommate. His roommate spent most of the morning in the bathroom," replied Carlton.

Okay, so just when you think you've heard everything in your profession, the old his-roommate-was-in-the-bathroom excuse will enter from stage right.

Trading is not an occupation for you to work on your psychological demons. Look, we all have psychological weaknesses that will hold us back as traders, some more than others. But if, as traders, we have psychological issues that are consuming our thoughts, we need to take a timeout. That crazy girlfriend needs to be attended to (or dumped). That family issue first requires your attention (like my recent loss) before trading should resume. You should not come to the show before sorting out your psychological baggage. You cannot trade well with this mind baggage.

Trader Max

Trader Max is a believer that first you must fix yourself before you can prosper in the marketplace. He wrote me this e-mail below uncovering his recent trading prowess:

Hello Mike,

This is supposed to be a long story but I'll do my best to make it short. Without these changes, I could never take trading as my career.

First, I just started trading like all beginner traders did. I read a couple of books, listened to webinars, joined a guru's chat room, and tweaked my trading software to find out the ultimate optimal indicator.

After a period of time, intellectually, I knew that there was no magic formula or best indicator or ultimate trading system. And I learned the proper actions I should take. I could even teach others what a good trader looked like. However, the biggest obstacle for me was I couldn't walk my talk. I didn't know why I just couldn't do the right thing. I got stuck in that situation for about ten months.

To find out the solution, I started to learn stuff in psychology. I realized that it might have something to do with my mindset. I read the famous book by Mark Douglas, *The Disciplined Trader,* but could not digest it well. It didn't feel right for me. However, I found inspiration in *Seven Habits of Highly Effective People.* It told me that our reality actually depends on our paradigm of the "real world." It's a personalized interpretation.

I sat down and reviewed my paradigm of trading, and found it pretty ugly. A frightened lonely rookie soldier was thrown into a battle field with only a knife in hand. (This is also the image the mass media or lots of trading books paint for us, a dangerous, scary, bloody war zone.) After I realized that I decided to play with it.

I changed the perception of market from a battlefield into an ocean. I changed my self-image from a rookie soldier to a fisherman. To the fisherman, the ocean is a place he respects but also a huge resource he can use. Certainly he knows the ocean is dangerous. So he prepares each trip carefully. But he loves the ocean. He knows what to do when the storm comes. He also knows what to do when the fish come. From then on, trading became an interesting, challenging, and fun game for me. I told the fisherman's story to myself every morning for about two months till I truly believed I was a fisherman. This simple change removed 60 percent of my fear while watching the market.

You might think this idea is quite original. I thought so. When I proudly celebrated this big breakthrough in my trading mindset, a real storm came. My girlfriend left me. This event actually forced me to lift my trading mindset to a higher level.

At that time, I couldn't pay attention to my trading because I loved her so much. All I thought about all day was how to get her back. I tried all methods: I wrote her letters, sent her flowers, talked to her in tears, read tips about "winning your ex back," watched clips "what woman really want" on YouTube, learned tricks from those so called pickup artist (PUA) gurus. But nothing seemed to work. I kept searching till a book saved me. The book is *How to Be an Alpha Male*. (Don't laugh, please.)

I realized the key problem was I was not "alpha" enough. I was showing lots of traits of approval seeking, insecurity in myself, indecisiveness. These are the traits of a beta male. They have no power to direct your own life and build a strong connection with a woman. So I decided to rebuild myself.

Being an alpha male means being dominant and a leader. This actually starts from the inside out. This means to be centered, decisive, and a leader to yourself first. I kept telling myself how to be centered and maintain confidence and strength. I kept reminding myself what my vision was, what I really wanted to be. It had become my habit. I started with changing my body gestures, language, and the way I interacted with people. And then almost everything changed in my life.

As I was removing those beta-male traits, I felt happier about my life, confident about myself. After becoming more centered, I actually became more open, open to others suggestions, tips. I used to reject other's ideas and strongly believed those were noises and distractions that might taint my clear mind.

Because I am centered now, I know what my goal is. I let those "noises" go though me and see them as a resource to use. I won't easily change my mind just because of a piece of advice. I am taking control of my decisions (no matter what the results are; others may call it being responsible for yourself). At the same time, I started appreciating other people's work and help more.

As I felt better, I eventually decided to continue my life and trading.

I hadn't touched my trading station for weeks. I almost forgot it. I had no idea what those changes had done to my trading. I came back to my trading desk as usual and scanned my watch list and drew those support and resistance lines as usual.

The first day back was not a big winning day. It was a choppy day. Little wins and little losses. But I didn't have the heavy and exhausted feeling I used to have after a choppy day. I felt light, relaxed, and full of positive expectations for the next day. It was a bit strange, but a very good feeling. Then in next five trading days I kept this good feeling, and it effortlessly brought me more money than I thought. I realized I had found the missing piece of my trading puzzle.

I love your book *One Good Trade*. For me, it just confirms what I believed. Trading is kind of like playing tennis or badminton. The player has to quickly move to a neutral (centered) position after each strike.

The ideal mindset is, if I could describe it, I would say, bear the goal in mind, be confident about your ability to make the right move (not to pick the direction and time right), and meanwhile focus on the here and now.

Before those changes, I would say only 5 percent to 10 percent of my trading time I had the ideal mindset, and my trading results were just so-so. Well after those changes, I now can keep myself in that state for 75 percent to 80 percent of the time, and my trading results have improved exponentially, a 203 percent gain in 45 days.

So these are the two changes I have made:

1. A new perspective of the market

2. A hardened alpha core

For me these changes were crucial.

Good luck and happy trading!

Michael Martin and I discussed fixing yourself first before trading success in an interview right after the release of *One Good Trade*. Here is our exchange:

Bella: Trading is a reflection of who you are as a person. You need to learn to be patient as a person, not will yourself to be patient when you are trading.

Martin: I've always said to my students that trading doesn't really build your character, it reveals it. So, you've got to do a lot of work, you are always trading.

Bella: And that means spending as much time during the day finding out the best about yourself. Finding the best about your trades, finding the best about your personality, and staying in that zone. And when you do that it really enriches your life, and I'm not talking about monetarily. I'm talking about being a better brother, a better fiancé, being a better son, a better friend. It is something that changes your life, and it really makes the other parts of your life so much easier.... And building persistence, getting yourself up and coming back the next day; these are skills you have to learn.

We All Come to This Game with Flaws

Trading holds a mirror to your human flaws and requires you to fix them or be fixed. If you are an anxious person, you will be an anxious trader who overtrades. If you anger easily, you will be a trader who quickly trades on tilt. If you are scared to take chances in your personal life, you will miss many excellent risk/reward opportunities in the market. If your father never offered you a vote of confidence, you will trade with a lack of conviction. If you come to work late, you will be late to enter a good trade. If you fail to diligently do a trade review after the close, you will fail to search your scanning tools and chat for the best setups in real-time. If you are not willing to do a PlayBook trade after every close, you will not sit in your seat and capture the easy trades. If you anger easily, you will miss an easy flip trade gifted by the market because you are busy cussing the markets. If you are distracted easily, you will be playing on ESPN.com when a stock sets up so perfectly. If you are in a bad relationship, then getting slipped in a stock will start a day of depression, because this is your reality. I will stop here; I hope you get my point. You must address these flaws if you want to be *your best trader* (YBT).

You do not always have to change these flaws so much as recognize them. Understand when they hurt your trading and when they can help. I grew up in a very safe and comfortable environment in a tony part of Long Island. I was trained as a lawyer and drawn to an ideology that things ought to be fair. You can see this in my trading. I fight as hard as I can not to coast when things are going well. I am self-aware of my coasting harming my trading. I easily trade on tilt when I view things are unfair in the market. If I experience slippage in a stock, that will assuredly set me off. The morning of the Knight Capital trading malfunctions is a perfect example. Knight has a series of orders that misfired into a morning session, resulting in an illiquid market on the open and $440 million in trading losses for Knights.

At 9:34 a.m. I tweeted that there was a lack of liquidity in the market and to be careful. I sent an e-mail to those who interact with the front end execution software, wondering whether something was wrong with their platform. If you could hear me on the desk, I was yelling for our floor manager to figure out what the hell was wrong. The news about the KCG trading error that messed up the market came an hour later. My need for fairness had sounded an internal caution alarm that something was not right well before most of the trading world knew. In this case, my emotions protected me and my firm from substantial trading losses.

I also wrote the following note about my emotions, the market's lack of liquidity, and then offered a solution. Here's what I wrote:

> August 2, 2012
>
> SMB Traders,
>
> The last two trading days have had the worst liquidity I have ever seen. Obviously, the huffiness on the desk is high. In my opinion, it should be. I have not been this mad on a desk in three years myself, trading this ridiculous market. The market is broken. And some of these moves are absurd.
>
> Having said that, GMan was still able to post almost $$$ in P&L. And as long as we can hit the bids and pay the offer, then we can make money. [For] traders, there is no right to an orderly market.
>
> The truth is that more movement intraday means more opportunity for us. Let's agree on one thing first: Let's end the complaining and just accept this is the market and that is the way it is. Now, our only concern is this: How do we capture some of the new patterns being created by these low-volume wicks?
>
> Some solutions to consider:
>
> • Trade smaller.
>
> • Scalp.
>
> • If you get stopped out on a low-volume wick, get right back in.
>
> • Set alerts for exits and then manually exit.

- Fade wicks to the upside of stocks clearly in a downtrend and play for a return to the mean.
- If you get pissed, take a mandatory ten-minute timeout.
- Trade significantly less on the open or not at all.
- Limit the number of stocks you are trading.

The market will probably correct soon as algos will be introduced, ending the low-volume liquidity. But if this doesn't happen, then no matter. We then will just have new patterns to exploit.

Thoughts?

Bella

If I cannot get a fill on the bid where it seems I should, I might say, "Why can't I get filled. I am a part of this (expletive deleted) market place as well." I fight being complacent with my trading because of my comfortable upbringing. "I'm up enough on the day, so now it's time to check out ESPN.com." I battle with this harmful mindset every day I am decidedly positive.

I'm a well-adjusted, self-confident, and resilient person. For example, my parents (particularly my mom) instilled in me a belief that there was nothing I could not do. If I ask staff at SMB to solve a problem and they later respond that they couldn't find a solution, my response is this: "I don't ever want to hear you say that we can't do something. It might be too expensive or not worth the effort, but don't ever tell me there is something we cannot do as a firm." SMB was started in my apartment, and it's now a global, trader-training thought leader. It is hard for me to understand how there isn't anything we cannot get done if we work at it.

Think of others with lesser psychological development who play my game. There is nothing wrong with having psychological deficiencies. What is wrong is not working to recognize what they are and not doing the work so that they appear less often and cause fewer disturbances to your trading. I learned from Dr. Katz, a performance coach, who has counseled me and our firm, that there will be perpetual psychological fires. You just want the fires to visit less often, blaze weaker, and burn shorter.

The difference between a nine-to-five job and a career in trading is that trading requires you to rewire your mind. A majority of traders and investors are doomed from the start because they don't understand the preparation it takes to become consistently profitable. Quint Tatro, president and owner of Tatro Capital, LLC, says a majority of those who start trading refuse to let go of their most basic human emotions and tendencies. Most beginners do not live strictly disciplined lives, understand the physical effects of greed, or know how to overcome sudden fear. Thus, years of dedicated effort toward training your mind to embrace the psychological effects the market imposes is a necessity. Even the greatest of traders understand that you have to constantly keep your mind in shape, no matter the years of experience. Charles Kirk, founder of the Kirk Report, recommends smartly that all traders keep track of theirs emotions in a trading journal. We do.

Remember at the outset that Rudy made the mistake of thinking that his past poker betting would give him a head start and advantage with trading? He was quickly reprimanded, as discussed earlier, and you might expect the story got better and faster. Not quite. Two days after his fantasy torture session with Carlton and me, Rudy walked in at 9:28 a.m., sat down, and got stopped out in five minutes. He went 100 percent over his max loss. Conversation two upcoming? I had trained enough traders to wonder if that was even worth my time. Maybe he just wasn't ready to be successful.

Carlton and I had no idea what to say to him about his ridiculousness. Both of us stood in my office with our eyebrows raised and eyes squinting and brains hurting to try to find an explanation for such self-sabotage, rule breaking, and chutzpah right after our first long talk. This absurdity, after two experienced and busy traders who *didn't* ream him out but instead calmly presented an irrefutable case about starting slower? This is why experienced, successful traders never want to coach a trader. Who wants to deal with this nonsense? Aren't there professional, well-trained, state-certified, saint-like kindergarten teachers for stuff like this? This exceeds my patience capacity.

Rudy was the poster child of those who think poker relates to trading and that he can start on second base. He can't. But an incident in my past about myself brought empathy.

I remember when I first went to UConn and how our baseball coach during summer tryouts in no uncertain terms told us that anyone who showed up late to practice would be cut. Sure enough, there was an overnight power outage at my off-campus apartment that killed my alarm clock. By the time I awoke naturally, practice had started. Oh s***. I grabbed my gear and ran to the baseball field. Upon arrival, I was promptly told to go home. I expected to get cut. I came to UConn to play baseball, and it was all about to end before it started.

A list was to be put up the next day for all who would be a part of UConn baseball for the upcoming season. I went to check whether my name was on that list, expecting the worst. Lo and behold, my name was on the list! I went to find Coach and apologize. He looked at me and said, “You know if you weren’t a freshman, I would have cut you. Don’t ever be late again.” That has stuck with me for some time. Rudy didn’t get cut right on the spot partly because he was too new not to make a few mistakes and we felt he would never do it again.

Also, we had learned about some issues that required his serious attention. We had invited him to train with us, and then learned of these personal issues, so we felt he deserved time to work through them. Just not while at the firm. I had Carlton speak with him about a hiatus to gets his stuff in order. He was excused from our trading desk for a few weeks.

When he came back, there was improvement. His work consistency was better. There were no reasons for closed-door meetings. He was doing the work he needed to do to become a successful trader. If you are a trader with distractions, call a timeout and handle your business before you come back into the game. Distracted traders, particularly those with personal issues, will have trouble competing. You have to be ready to be successful before you can be successful.

Rudy’s great mind lets us examine a topic that most non-pros misunderstand. “Trading is not rocket science,” says my partner and Wharton grad Steve Spencer. It ain’t. And the intellectually gifted do not have the edge some think they might.

Overthinking Harms Your Execution

Why do stocks go higher? Answer: supply and demand. Are there going to be more aggressive buyers than sellers at a certain price? Yes. Certain patterns develop that give us an edge in predicting whether a stock will most likely trade higher or lower from its given price. Period. Let’s not pretend we are working for the Council of Economic Advisors.

We are the players of the trading arena. Players perform. I do not have to know how or if the euro zone will stay together—although I was asked this on stage during an international trader panel discussion. For the record, I voiced that I hoped they did but that they probably wouldn't. I have to know how to trade the event. Trading is not an IQ test. The following are some choice quotes from various market veterans of all trading styles:

- Spencer, a graduate from Wharton: "Trading is not rocket science."
- GMan, a graduate of Columbia with a degree in engineering, scolding me in real-time about overthinking a trade we were both in: "Bella, don't make the trade too complicated. It is either going to work or it is not."
- Shark on a KCG trade: "Yeah, I don't know whether they will get funding. I am just going to trade the price action."
- Dr. Steenbarger: "The very short-term trader—the scalper or market maker—can't afford to overthink trades. He or she also can't afford the luxury of a well-laid-out trading plan. Rather, that trader needs to become so familiar with short-term trading patterns that he/she embeds them in perception itself."
- Warren Buffett: "The business schools reward difficult complex behavior more than simple behavior, but simple behavior is more effective."
- Jesse Livermore: "It never was my thinking that made the big money for me. It always was my sitting. Got that? My sitting tight! It is no trick at all to be right on the market."
- "Keeps things very simple and don't overthink your trading methods" said @TraderStewie from http://artoftrading.net/.

And there is more.

The trading community has long been familiar with the story of the "turtles," the result of a bet made between Richard Dennis and William Eckhardt over whether traders are born or can be taught. In wanting to prove to his long-time friend that anyone could learn the game, Dennis was adamant about selecting an extremely diverse group of students to train, regardless of IQ or past experience. As written in Michael Covel's book *The Complete Turtle Trader*, "Dennis was not about to be taken in by a hereditary interpretation of IQ. His aim was to implant his mental software into the brains of his students, and then place them into his controlled environment to see how they would react and perform." While he did select a few college graduates to take part in his experiment, he also included people with much less educational experience. He brought in a security guard, a salesman, an assistant manager, a phone clerk, a bartender, a board game designer, and even a woman, which was rare for the time. “He wanted students who showed a willingness to take calculated risks,” Covel writes.

So how did the newly trained traders perform? In 1989, about four years after the experiment began, 14 of the original 20 turtles had returned an average annual compound rate of return of 80 percent. Just as in the movie *Trading Places,* though not directly related to the turtle experiment, Dennis discovered that IQ and experience are not prerequisites for becoming a great trader. Anyone willing to take risks and who has the patience and open mind to learn a proven method has the potential to be great.

Back to Rudy. First Rudy would execute on too many trades. His superior mind saw more risk/reward setups. Carlton disciplined him into the best of those setups with resistance. Then Rudy wasn’t sizing up in his best opportunities. Carlton would have to push Rudy in real-time to get bigger in these setups.

Let me share a great exercise to help with this. Right after my mom passed, I spent six months standing behind our most promising traders focused solely on them being big in their best trades. I didn’t care if they lost. I was only concerned that they were big when it mattered. Coaching in real-time is one of the most effective ways to make a trader better. Pushing him to get bigger in real-time is a very effective way to get people trading bigger in their best setups. You are forcing them to be bigger and experience that trade. One thing to be careful about as a coach is not to get the trader into trades you would size up in. Get them into trades they want to size up in.

Many traders want to get bigger. Intellectually, they see where they want to add size. But they just cannot execute. And you have to work on this with them just like you do explaining an opportunistic setup. The first step is learning then the next step is executing.

So now the event you have all been waiting for. The review, of a technical analysis trade, where I supposedly rip Rudy follows. First, see Rudy’s trade in PlayBook form.

Midday Ascending Triangle into LT Resistance

Rudy

LVS

Feb. 1, 2012

Big Picture

After its first test of the 130.00 level on Monday, the SPYs gapped above 132.00. Once the premarket high of 132.40 was broken, it was clear we had a high probability of seeing a test of 133.00.

Intraday Fundamentals

Set to report after the close, LVS gapped up and spent the first half-hour testing and rejecting the 49.00 level. After spending most of 10 a.m.–11 a.m. struggling and succeeding to get past 49.75, LVS made its first test of 49.75 at around 11:10 a.m. There appeared to be little selling interest below.

I did not start looking at LVS until around 12:10 p.m., so this information was chart based.

Technical Analysis (Long Term)

Technical Analysis (Medium Term)

Technical Analysis (Intraday)

Reading the Tape

At around noon, I could see 49.90 was resistance, so I set an alert for 49.91. After LVS cleared 49.91 the second time, whenever it pulled back, the volume would completely dry up. There were about 600 lots on the offer at 49.95 that kept LVS between 49.90 and 49.95, but still there was little selling interest. These offers were taken in about a second.

About 600 more lots appeared on the offer at 50.00, but these were again cleared instantly.

Trade Management

Trade Management

I try not to play breakouts midday unless I have a lot of checks in my favor. After [I played] the first breakout at 49.96, LVS didn't move. However, the bids weren't getting slammed, so it felt like one of those slow-to-develop breakouts.

I did not add at the flag between 50.15 and 50.25 because the combination of the SPYs nearing the important 133.00 resistance level and the LVS target level of 50.50 being quite close made the reward not worth the risk.

Trade Review

What did you learn from this trade? How could you have done better? How would you trade this differently for the next trade?

Once I was in the trade and it was working, I forgot to keep close attention to the SPYs (which I told myself would be important). LVS hit its high at the same time the SPYs tested 133.10. If I was less greedy, I could have gotten out of half at around 50.35.

Trade Idea

The 50.40 level provided clear support the next day, allowing several opportunities to get long.

From the Training Room: A Technical Trade Review with Rudy

Rudy: All right, my trade is from the beginning of February, February 1. Midday, ascending triangle into long-term resistance in LVS.

So, with the Big Picture: After the first test of the 130.00 level on Monday, the SPYs gapped above 132.00. Once the premarket high of 132.40 was broken, it was clear we had a high probability of seeing a test of 133.00.

Bella: All right, so that has been a really big level, that 130.00 level, right? On a level of 1 to 10, how important has that level been?

SMB Trader: Eight.

Bella: All right, so we will give it an eight. So, really important level. Okay, good. Good to know that.

> *Make a habit of judging every technical level you view from one to ten. This will help build your charting skill.*

Rudy: So, next slide. The Intraday Fundamentals of LVS: It was set to report after the close. LVS gapped up and spent the first half hour testing, going down, testing, and rejecting the 49.00 level. And, then, after spending most of 10:00 a.m. to 11:00 a.m. struggling and succeeding to get past 49.75, which I will show you on the chart of the last couple of days, LVS made its first test of 49.75 at around 11:10 a.m. And, really based on the tick chart, there was a little selling down there. And, I say "on the tick chart" because I set an alert for LVS and then it popped, and I started looking at it around noon.

So, next chart, please.

> *When you do your PlayBook trades, you want to be complete with your information. Not covering the Intraday Fundamentals is an incomplete PlayBook trade. Perfect practice makes perfect.*

Bella: So, just wait, let's go back. Intraday Fundamentals means what? So, when we are looking at Intraday Fundamentals, what is important for us? Go back. Go back. Go back, Carlton. I'm sorry, Carlton. *(Slide show is placed back on the "Intraday Fundamentals" slide.)*

So when we talk about Intraday Fundamentals, what do we mean?

Rudy: Are you asking me or the classroom at large?

Bella *(snaps)*: Well, since you don't know what it is, I'll ask the classroom.

SMB Trader: Like fresh news.

Bella: Okay, so like fresh news. So, Intraday Fundamentals means... what about LVS? Is there any certain news about LVS on this particular day, right? So, is there any news on LVS?

Rudy: I don't recall. I didn't go into the trade because of the news.

Bella: Could there have been fresh news?

Rudy: There could have been.

Bella: So you are saying that you didn't know whether there was fresh news about a stock before you traded it?

> *Arggh. When you are in a hole, stop digging. What I should have said was this: "How the hell do you consider yourself a pro trader if you aren't prepared to trade this setup, then review it and not even recognize there was essential information you didn't have?"*

Rudy: That is not the reason I got into the stock.

Bella (*looking quite unhappy*): So I will assume that is a no to my question.

Okay, so, Intraday Fundamentals for LVS would be: Is there something specific about the gaming sector? Or is there something about the particular stock that would make it move cleanly in a distinct way that is different from other days?

Okay, so, we want fresh news. Okay? Okay, next. *(Signaling to move into the next piece of PlayBook conversation)*

Rudy: Okay, next slide *(Long-term chart is brought on to the screen; see Figure 8.1.)* So, on the long term, we can see this 50 level being tested numerous times and not being able to get above.

Figure 8.1

Okay, next slide *(Technical Analysis [Medium Term] slide is brought on to the screen; see [Figure 8.2](#).)* So, here we see the couple days beforehand, we have this 49.75 that it was struggling to get above, and then on February 1, that is when it is really going to get above. And, my target was going to be that pivot of 50.5.

Figure 8.2

So, next slide *(Technical Analysis [Intraday chart] is brought on to the screen; see [Figure 8.3](#).)* I like seeing patterns like this where something trends.

Figure 8.3

Bella: Okay, okay, go back to the longer-term charts *(Long-term chart is brought back on to the screen; see* *Figure 8.4**.)* Okay, you drew that red line. Where is that red line going? What price is that?

Figure 8.4

Rudy: [At] 50.20 or so.

Bella: Okay, so, 50.20, you think is a long-term level?

Rudy: Yes.

Bella: Okay, and then show the next slide *(signaling for the Technical Analysis [Medium Term] chart; see [Figure 8.5](#))*. And, if it gets above there, where do you think it can go to?

Figure 8.5

Rudy: Well, my target for this play was 50.50, at least for this day. But I mean on a long-term chart, there could be other days, I did learn.

SMB Trader *(from the back of the room):* Speak up!

Rudy: My target was 50.50, just for this play, but I think if it was able to get above, the target would be much further.

Bella: Okay, so, I guess my question would be what? Who can guess what my question is? Carlton, what do you think my question is going to be?

Carlton: I'm not sure what your question is going to be.

Bella: What do you guys think my question is?

SMB Trader: Why are you trying to make 30 cents?

Bella: Well, I don't even know if I can get that far?

SMB Trader: Why are you getting long in front of resistance?

> *It is not worth your time almost always as a trader to fight for 30 cents. You want to find setups where stocks can trend for multiple points.*

Bella: Yes, so, why are you getting long in front of resistance? So, in the long-term chart, there is resistance, very soon. Right? And, you are showing us an intraday chart where there is resistance at 49.75, though when we look at the longer-term chart, there is resistance, very, very soon.

So, my question is this: **Why are you bothering to get long above there when there is long-term resistance so close?** Right? I will let that be your question. Is that your question, both of you guys, Ryan and Chris? *(Bella directing this question at the SMB traders who just recently spoke, in a joking manner, playing off the obvious fact that he has answered his purposed question for the audience.)*

Chris: Sure.

Ryan: Yes, it is.

(Audience laughs.)

Bella: So, Rudy, Answer?

Rudy: Okay, can you go back to the long-term chart? *(Long-term chart is brought on to the screen; see Figure 8.6.)*

Figure 8.6

I mean, here, especially, I drew the line to the wick. That is why my intraday target was going to be... Oh, I’m sorry. That is 50.50, that line. So, I guess 50 would be... I may have been mistaken in what I said; 50.50 was the level the line is drawn at there. So, my target would be that line.

I made this like a week ago, so I am a little rusty on the details of it.

Bella: All right, so, you think the longer-term resistance is 50.50?

Rudy: That is where the wicks go up to there, there, and pretty good there *(Rudy motions to the wicks on the long-term chart.)*

Bella: Okay, so, you are trying to make an intraday trade on LVS. It gets above 75 cents. Show the intraday chart. *(Intraday chart is brought on to the screen; see Figure 8.7.)* It gets above 75 cents, then goes up to 50.50. That is the trade?

Figure 8.7

Rudy: I mean 75c; I was happy to see that. I didn't start looking at it until it was already above it. So, seeing that it was able to clear that last week of resistance, that was another plus in my favor. I set my alert for 90–91 because I saw LVS having trouble getting above it, and I wanted to take a look at it once that happened, so I will explain my trade to you on the next slide, Reading the Tape.

Okay, so, around noon, I could see 49.90 was resistance, so I set my alert. After it cleared it, I noticed on the tape that the selling interest would just dry up, and there was a pretty big offer there at 49.95 that kept it in a tight range of 5 cents. I will show you again on the chart that after it broke 49.95, another 600 lots appeared at 50, which were cleared much quicker. So, we can go to the next slide.

Bella: So, there was an offer of 600 shares?

Rudy: Yes, and then no one was really taking it, and it just got cleared.

Bella: All right, well, when you see 600 shares getting taking in LVS, what does that tell you?

Rudy: That someone wants the stock.

Audience *(begins to chime in with various responses to the question)*: Nothing.

One trader: So, was it 600 or 60,000?

Another trader: Well, a lot is 100, so....

> *If this trader had taken our training program seriously, he would never say something like this. This is clearly a trader going through the motions, which has caused a very smart person to miss a very basic trading fact about Reading the Tape.*

Bella: Is it 6,000, 600, or 60,000? Is that your question?

Another SMB trader (Prep): Either way, it is really not that relevant with LVS, right? It is a really thick stock. It averages 29 million shares a day.

Bella: So, your question is, Prep, "Why do you think that is significant?"

Prep: Sure.

Bella: Rudy, why do you think that is significant? It's not a lot of volume.

Rudy: To me, I'm adding it into everything else and using it more as a place to get in than anything. It is not the reason for my Trade2Hold trade to hold specifically, but it allows me a good point to start my trade.

Bella: All right, does anyone have a follow-up to that?

(Silence)

All right, well, I don't think that anyone was suggesting that you were only making the trade based on that, but I think that was your "Reading the Tape" clue. And, what we are saying is that in LVS that is not really a clue.

Right? Is that what the consensus is? Because there is so much volume that gets done in LVS, that isn't really an example of something [that] shows more strength on the tape. Right? Did I sum that up correctly? So, what is your response to that?

Rudy: Well, that is exactly what happened, right there *(Rudy points to an area on his Trade Management slide; see Figure 8.8.)* As you can see, this is the most volume of the day *(Rudy circles the area of highest volume with the computer cursor.)* So, relative to everything I was looking at, it was more volume.

Figure 8.8

See, I do not know why Special Projects said I ripped this trader? He is making unacceptable errors. I haven't kicked him out of the training room like I really should have for being so underprepared and unfocused making this trade. I am chanting to myself internally during this trade review, "Keep it together. Keep it together. Keep it together, Bella."

Bella: Okay, that would be much more than the volume you told us about. I'm just telling you what you told me. All I can do is listen. I heard what you told me and asked you a question.

Okay, I think what you are trying to say, Rudy, is that you would like to retract what you said and that there was actually a lot of volume that was done, and it looks like there was about 200,000 shares done, which was a lot for that time period that you saw on the tape. Is that what you want to say?

Rudy: Yes. I'm saying, at the time I got in, that was the biggest volume in a short period of time that was done.

Bella: Okay, so what else do we have?

Rudy: Okay. So, I normally don't try to make a Momentum Trade in the middle of the day, but I liked this setup. I liked how everything was setting up. So, I paid it, wanting to quickly get out, if anything went the other direction. And, you have told us about how, sometimes, things that could be momentum may not appear obvious. They may just slowly work their way in and pick up speed. So, it didn't go against me, and I wanted to keep watching what would happen.

Bella: Okay, so, let me ask you this: Was there anything in the news about the sector, about the gaming sector, when you were trading this stock?

Rudy: No.

Bella: Was there anything unusual about the 49.95 price?

Rudy: Unusual?

Bella: I mean, was it an unusually important level, intraday?

Rudy: At this point, right here *(Rudy points to an area on his trade management slide),* it was. I think so.

Bella: Is that an intraday high?

Rudy: Yes.

Bella: What was the market overall doing when LVS was going above 95 cents? Was the market clearing an important level such that you would want to get long a market stock?

When the market clears important technical levels, we may consider a market play where we get long market stocks.

Rudy: Actually, I'm glad that you mention that. I did forget one of the important parts of this trade for me was how the SPYs were moving, because this wasn't totally In Play, and how LVS is affected a little bit by the SPYs. The SPYs had moved above their range at around this time and were creeping higher toward where they double-topped, which was at about the same time this hit the top. So, the SPYs were acting strong at the time, so that made me more confident in the trade, as well.

Bella: Okay, terrific point there, what do we have next?

Rudy: Well, the thing is I am still working on getting out early. So, I watched this, and as soon as the SPYs started turning, and I saw selling starting to generate on the tape, I just hit out at 23c or 24c.

Bella: Okay, why wouldn't you get out, if it got close to 50.50, the next technical level? It got up to what 50.42?

Rudy: That is one of the problems I have: knowing where to get out if it does not get to your target.

Bella: Okay. You had two lots, you were Tier2. Did you take off any lots as it came up toward 50.50?

Rudy: I did not.

Bella: Okay, **as something starts to get close to your target and you start to see it slow on the tape, that is probably a reason to take off at least one lot.** Right?

> *Develop your trading plan to lighten up on a position as it approaches your target. Do not expect it to always reach your target exactly. You need provisional plans to take risk off the table as the target area is approached.*

So, you want to take off at least one lot. We have talked about this before. So, going up to 50.50, you see selling on the tape, and you get out. That's easy. So, we want to do something like get up close to 50.50, use your judgment based on what you are seeing on the tape, then it is sort of like a Fade Trade. You sell it when it starts to slow on the tape. So, we tick higher, we tick higher, and when it stops ticking higher, we kind of get out and have one left, tier1. And, we see what happens.

And, it's not good there. It's 7 cents from your target, and it is not really that likely it is going to get above 50.50 right away.

Rudy: I think the thing that was keeping me in it was the SPYs were pushing their highs.

Bella: That is fine for tier1. That is a legitimate response, but not for both, tier1 and tier2, because that is why we look at the level. There was a significant level at 50.50, right? When you are making a trade you must respect the next important technical resistance level.

Rudy: Yes.

Bella: Okay, let's go to your Trade Review.

Rudy: What I learned from this trade: Once I was in the trade and it was working, I forgot to keep close attention to the SPYs (which I told myself would be important). LVS hit its high at the same time the SPYs tested 133.10. If I were less greedy, I could have gotten out of half at around 50.35.

Bella: Well, is it greed? I mean, how do you get out of stocks like this? What would be your plan to get out of stocks like LVS, if you had to trade it again? Same setup.

Rudy: So, when the momentum slows close to the target level.

Bella: Okay. And, how do you get flat?

Rudy: I usually set it to what I think is an important support or where it is pulled down to last.

Bella: So, I don't understand what that is. Is that a technical level or...?

Rudy: The next low, maybe.

Bella: What happens if the market had gotten weak all of the sudden?

Rudy: Then I would hit out like I did with both of them.

Bella: What if you saw a lot of selling on the tape?

Rudy: There would be a lot of reasons.

Bella: Okay. Well then, what are they? You need to know that, right? **So, when you say to me, "I have trouble getting out," what you need to do is understand what is going to get you out and then work on that every day. But, first, you need to be very definitive about what gets you out.**

> *This is a common mistake that floods my e-mail inbox from developing traders. Develop your system for exiting. Do not just say you have trouble getting out.*

So, what gets you out of this trade?

Rudy: What did? Or, what ideally would get me out?

Bella: Just in the future, with the same pattern, what would get you out?

Rudy: Tier1 when the momentum slows. And, tier2, probably where I hit out of both once I saw selling on the tape in LVS and the SPYs tested or rejected their high.

So, that is what would have gotten me out, and that is what did get me out.

Bella: Okay. So, what do you think of the trade, overall? Good trade, bad trade? Could you have added size somewhere? Would make it again, wouldn't make it again?

> *Hands down this is the worst trade review in the past two years.*

Rudy: There was a place, when it flagged after the first move, between 50.10 and 50.20 where I could have added, but since my target was 50.50, I wouldn't add that close to my target.

Bella (*interjecting*): You know, I don't want to engage in this. Somebody tell me why this is an awful trade. And what is a trade you really should make?

(Prep raises his hand.)

Bella: Prep.

Prep: I think that this is just a breakout scalp, and if you are going to make the trade, if you just buy the break and that is how you are going to make the scalp, you are looking for a quarter, at the most. It is just taking it off when the stop is going against you. The scalp is for momentum.

I think a better trade would be holding above 20 cents for, at least, 15 minutes. Or, maybe even above 50 cents for 15 minutes. And you are going to play a long-term support-resistance play.

Bella: Okay, so definitely a sort of swing trade above the resistance is a better trade, but let's remember the market, overall. I mean, this trade works for a very specific reason, and you have to understand that. Which was the market broke out of its intraday range, the market got strong, and you found a market stock, and that market stock then pushed higher.

Okay, so if you are playing a sort of market breakout, which is a good trade, you are saying the market breaks to the upside, and I want to get long on market stock. Why is this an awful trade?

And, I want to be clear, this is awful. I don't ever want to see anyone make this trade.

TO: You can pick a lot of stocks to make a market play on, and you want to pick something that is not heading into a hard resistance level.

Bella: Yes. **You want to find something that is above its longer-term resistance matched with the fact that the intraday market is now breaking to the upside.** Okay, so if you are ever going to make this market play, it has to be matched with the intraday market breaking upward. You need to put those two together. And, if you put those two together, then that is a trade that will work.

This trade will absolutely not work.

Rudy: So, you are saying it would be a lot different if that was just a little more.

Bella: If this was above 50.50. Let's say we were looking at an intraday chart and it couldn't get above 50.55, and then the market broke to the upside, and then LVS got above 50.55, that would be a very good trade. And, LVS is a good market stock. This would be a market play with a market stock Trade2Hold, where we would not sell until there was a Reason2Sell.

And, the thing that you really have to do to make that trade is do your research and understand the levels. Maybe you want to trade FCX. People love to trade FCX as a market stock. All right, maybe you want to trade IBM, not as good, but....

TO, what are some good market stocks you like to trade? Although you may not like to trade market stocks.

Prep, what are some market stocks you like to trade?

Prep: Citibank is a primary one.

Bella: Okay, very good. So, Citi is a good market stock.

SMB trader: JPMorgan.

SMB trader: Caterpillar.

Bella: Okay, Caterpillar. Okay, JPMorgan, not so much. I would rather trade Citi, but JPMorgan, we will give it to you. X, I hate that stock, but I will only trade it as a market play. Okay, Exxon.

Okay, so you get the idea. So, there are stocks, and each trader needs to come up with their own list of market stocks that they want to trade when they want to make a market play. These lists of market stocks will shift as the market changes by the way. Some markets APPL, IBM, NFLX, GOOG might be your market stocks. Other markets CMG, CAT, BIDU, LNKD might be your market stocks. And, there are days, particularly when the market gets above or is holding above a significant level, that you may want to do that.

Okay, thanks everyone. Rudy, stay behind please.

Postscript

> A few days after the review, I found Rudy working late in the office. He said, "I was glad you took me to task for my last PlayBook."
>
> I cannot make a good argument that Rudy has any chance to become a CPT with the work above. Objectively, we should have asked him to leave already. But we are slow to give up on traders, in this case too slow perhaps. He either does better work or will be looking for new work.

Rudy Post-Postscript of Class

Literally days before closing the last edits to this book, Rudy sent us this e-mail:

> Everyone,
>
> People come and go from trading all the time without notice, but I'd like to say goodbye to everyone at SMB. Unfortunately, too many external forces are making it near impossible for me to continue to pursue trading at this time.
>
> I really enjoyed the atmosphere at SMB and will *definitely* miss you guys. I can't think of any other place (work or school) that I have felt more a part of. Keep up the hard work!
>
> Also, someone else will have to take over the poker tournaments for me. If you're interested in doing that, go speak with Carlton. Personally, I think one each quarter before earnings season starts works best. :)
>
> Lastly, feel free to e-mail me at [deleted] or add me on Facebook @ [deleted] if you wanna keep in touch.
>
> Best regards,

Rudy

What a class act! When he is ready, I hope to hear about the great things he is doing next. It is amazing how demanding the market is that it humbles such a brilliant mind.

9. Iceman: No Guts, No Glory

Spencer, perturbed, pulled me into my office: "These guys are such a bunch of wusses. Why weren't they loaded in VVUS?" Perturbed now became a rant: "I don't understand. During the AM meeting I told them to watch it at 20. In our SMB Real-Time, I chatted to get big at 20. Look. Here is my chat. I said *I am getting bigger here*. I screamed at the desk to get long. And then I look at the risk monitor. A handful of guys are long 300 and 500 shares. What the f*** is wrong with these guys? You know the only one who was really long?"

Well, I knew, and that is whom this chapter is about.

Iceman (I know, great nickname) is the next trader we will study. His story provides four important lessons of trading:

1. You must have guts to be your best trader and not suffer from "Trader Wuss Syndrome."

2. Find the trading style that works best for your personality.

3. Have some fun while you are at this game, please!

4. Embrace the unavoidable psychological journey to reach the goal of CPT.

As a trader, you must not only construct your PlayBook and execute on your favorite trading patterns but you must also develop the skill to be big, loaded, committed, all-in, add size, or however else you want to say establish a large position. This chapter will help you consider whether you have adapted your trading to your personality; in this case, taking risk suits Iceman. If not, you are holding yourself back as a trader. We will introduce Iceman and share some entertaining vignettes of his time with us. Always add fun and laughter and great people to your learning, please. "We become more successful when we are happier and more positive," teaches Shawn Achor in *The Happiness Advantage*. We will also challenge you to admit that not taking on risk with your best trades is dangerous. Being conservative with your favorite plays is a ticket to trader failuredom. This chapter offers 11 steps to trading bigger, and potential cures for Trader Wuss Syndrome are offered to help you add size to your trading. Finally, take comfort that even successful pro traders must work on psychological issues and learn the best template, Five Steps to Improved Trader Psychology, to fix them.

Now let's have some fun, not take ourselves so seriously, meet a gregarious and charismatic developing trader, and learn from his trading adventure.

Having the Guts to Be Your Best Trader

Iceman was lecturing to our summer trainees in our training room (he runs the SMB College Training Program), their eyes affixed to him as he was walking through a high beta setup that he had just crushed. He looked directly out at the audience of future hopeful star traders and delivered a trading lesson to be written down, highlighted, reviewed, and implemented. He taught, "If you are not taking on enough risk with your trading, then you are taking on too much risk."

Let me explain this further. Trading is a game of math. Your best setups have the choicest combination of win rate and expected reward. *Win rate* is the percentage you profit on a trade. The expected reward is how much you bank when you are right. If you are not biggest in these setups, it follows logically that you are increasing your risk. Let's consider two trades. In Trade A, you have a 60 percent chance of capturing 2 points with 16 cents of downside. In Trade B, you have a 60 percent chance of making 30 cents with 10 cents of downside. If you place equal size with Trade A and B, you are enlarging your risk as a trader. In fact, if you are not willing to do so, unable to psychologically handle the stress of adding risk in Trade A, you are augmenting your risk as a trader. We must strike and strike without mercy when the market gives us our best setup.

It is a long journey to becoming a Consistently Profitable Trader. Anyone who tells you otherwise is a duplicitous huckster or just incorrect. Even if your trading profits are not outsized, it is a huge accomplishment to be consistently pulling money from the markets. Studies show that only 5 percent of *all* who attempt to trade can reach such status. But to go further, more rehearsal needs to be done, and this often requires getting the trader to reach outside of his comfort zone. The great trading psychologist Ari Kiev described this trader state as skiing downhill as fast as you can without losing control. Are you willing to take this risk with your trading?

Let's dive deeper into what we mean by taking on more risk in my game. Taking on more risk means confronting these specific and separate challenges:

- Trading bigger
- Trading stocks that are more expensive
- Trading stocks that have bigger spreads
- Trading stocks that move more intraday (higher volatility)
- Opening drive patterns (plays in the first 15 minutes of the open when the market is more volatile)

These are all separate challenges. For example, some traders can trade bigger with stocks that have a penny spread but are reticent to trade more expensive stocks. Some can trade big but not in highly volatile stocks or right on the open.

If you can demonstrate the ability to become a consistently profitable trader, again, no matter how small your profits, it means that you have the skill and wherewithal to take your trading to the next level and to confront these new challenges successfully. In short, if you are in an A+ setup and you are *not* at your max size, you are losing money. So if you have these skills, and these other challenges offer more trading opportunity, why then do most traders have difficulty taking on more risk? Psychological issues, mostly. A lack of sizing techniques to grow bigger, perhaps. I was on the phone with our partner for our trading *joint venture* (JV) in NYC considering a candidate through statistical analysis of his trading. Our partner said, "This guy is not very good. For whatever reason, he has trouble pulling the trigger. He never uses all of his buying power." We didn't hire that applicant. Yet there are traders who up their game better than others.

Meet Iceman.

Iceman Trades His Personality

Traders often discount finding a trading style that fits their personality. They trade a system that is in front of them instead of first taking a great deal of time to determine which style would best suit them. For example, maybe their buddy is swing trading, so they start swing trading. Maybe they catch a trading TV personality on CNBC and decide to try his trading style. Hey, that guy is on TV, so that trading approach must work for me. Tadas

Viskanta, the founder and editor of the well-trafficked blog *Abnormal Returns*, recently interviewed Jack Schwager, author of the famous *Market Wizard* books, about what it means to have a strategy based on your personality. Mr. Schwager noted in the interview, as well as in all of his books, that the best traders find and implement a strategy that best fit their personality. To be the best trader they can be, he encourages all traders to find a strategy comfortable for them, whether it's long term, short term, technical based, or fundamental based. Further, renowned trading coach Dr. Van Tharp famously advises traders to start with a personality test to determine what type of trader they are. Dr. Steenbarger encourages traders to try multiple products before they turn pro so that they match their trading interests with their talents. At our firm, we created the Rotation Training Program so that traders could learn which product and style of trading made the most sense for them.

In trading terms, if you are cautious in your personal life, trading expensive high-beta stocks with a momentum-based strategy is not a great idea. Your personality will short-circuit this trading strategy. Iceman trades his personality as well as anyone on our desk. Let's discuss how that translates into his trading.

Iceman has no conscience, which we will review in humorous detail, from his personal life to his trading. He has crafted a trading style to fit his personality—trading high beta stocks, stocks with larger spreads, more expensive stocks, Opening Drive Plays, accepting more downside when he is wrong, and emphasizing sizing up in the best opportunities.

A Personality to Trade the High Beta Stocks

One summer day, for some reason I can never remember, we decided on a push-up contest during Iceman's training class. There was a prize (probably free drinks at the next happy hour), and maybe we started this to build morale among the summer trainees. I hope that was the reason. Who was the first to accept the challenge? Iceman, of course. Most of the other trainees slumped in their seats hoping not to be called upon. Just as they would later be gun shy to trade high beta stocks like LNKD, AAPL, AMZN, CMG, GOOG, IBM, and BIDU. Iceman, of course, couldn't get enough of this high beta trading action.

As a former frat boy from a southern school with a deep tradition of frat-centricity, Iceman jumped at this admittedly sophomoric challenge. I couldn't get the challenge out of my mouth before he was volunteering. It was easy to see that this was not the first silly challenge game he had participated in throughout his life. One could easily imagine he had played this game before, but perhaps after six shots and five beer funnels. Instead of "Iceman," he could have earned the nickname "Frat," and we would have left it at that. For example, *Ted,* a 2012 movie saturated with puerile humor, became one of his favorite comedies. In fact, after seeing the movie over a weekend, he insisted that everyone on the desk should run out and see it. He promised to go back again the next week with anyone interested. For Fridays, he started a personal tradition of fasting all day so that he could save room for drinking games after the close.

So who won that push-up contest? Iceman! He won with a fast 100 pushups. Iceman wouldn't lose a competition like that. Just like he wouldn't let a high beta stock (stocks that move the most intraday on average compared to other stocks) get the better of him.

Fast-forward a year later and we're sitting at our trading desk. During a mid-day trash-talking session that traders can lapse into during a trading lull, we mentioned Iceman's conquest as the firm's push-up champion. A new trader with a bit of brass and lots of muscles suggested a challenge to the push-up record. Iceman didn't care for this newb's challenge at all. He scoffed, "Why bother? If you do more than 100, then I will just do more than you." He could have been talking about trading LNKD, a social media high beta stock. "LNKD, why bother taking 50 cents from me on this trade? I will just take $2 from you on the next" is Iceman's trading ontology.

SMBU, our education arm, received an inquiry about doing a webinar on Reading the Tape organized by the social media Russian trading site Hamaha.net for Russian traders. They wanted me to do the webinar because my book *One Good Trade,* translated into Russian, was a sell-out. There were two problems: I do not speak Russian, and most of the audience didn't understand English very well. So in came Iceman. Did I mention that he speaks fluent Russian? In a day, an audience of 700 was attracted for this seminar. Most would get a little nervous before the presentation, right? Iceman? "Bella, this is awesome. Can you believe how many traders they assembled in, like, 24 hours? This is gonna be fun!"

After the huge turnout for this event, Iceman created a mentoring program, led by him, for Russian traders. Ten spots were made available. In two days, the program was full.

One day after lunch with Iceman and a few other important SMBU members, a top female salesperson on Wall Street turned to me and said, “He’s really cute. I am sure that he doesn’t have any problem with the ladies.” I suspect that even if he wasn’t “cute,” he wouldn’t have any “trouble with the ladies.” He is Iceman. With his philosophy, approaching a woman is just a risk/reward exercise. If one shoots you down, you just move on to the next nearest one. One eventually will be interested or eventually you will catch one stock for a huge move.

How *Top Gun* Can Improve Your Trading

Because Iceman is a huge *Top Gun* fan (now you might start to understand his nickname), things discussed on the trading desk are often related to this movie classic, sometimes quite humorously:

> Bella, do you think I would trade better if I watched *Top Gun* while trading? I am gonna give it a try. There are gonna be a lot of bullets fired. I will conduct this social experiment for the desk.

Of course, you will, Iceman. Of course, you will.

Interestingly, Iceman was on to something with his movie-watching idea. Trading psychologist Denise Shull pointed out during a five-course Union Square lunch with me during Restaurant Week that traders who watch movies while in longer-term trading positions make better decisions. She argued that a trader’s subconscious keeps the trader focused on the real trade, which is to say that a good trade is not short-circuited by overvaluing the ticks. While we are on this topic, research also concludes that looking at attractive women before trading helps a trader take on more risk. I encouraged Iceman to try this movie idea while in a Trade2Hold. He loved the idea.

When I arrived back to the desk one trading session with my new Samsung Galaxy S III, the hottest phone on the market in the summer of 2012, many traders were mesmerized by my new toy. After six years as a BlackBerry holder, produced by RIMM, I caved in to Spencer’s advice and purchased an upgraded smartphone. (Please get over the absurdity of my BlackBerry allegiance and keep reading.) Dazzled, Prep asked, “Bella, that is so cool. Can I check it out?” This was the reaction of almost all others on the desk. Iceman? “Bella, do you think Maverick (from *Top Gun*) needed a new cell phone to kick ass?” Well, I hadn’t thought of it that way, Iceman.

A Crisis on Valentine’s Day

My favorite Iceman anecdote concerns the pickle he found himself in with a few young ladies. (Well, actually, my favorite is of him ordering the Friendly’s Happy Ending Sundae, unable to control his laughter in the little town of Danville, Pennsylvania. But we had to drop that story from the book.) He met one girl promptly after moving to the city and began dating her. Then after a combination of cheap beer, shots, and a crowded bar during one of those young professionals nights out in NYC, he met another. How I feel about a big city experience for our young traders reminds me of that Hemingway quote about Paris (admittedly perhaps the most beautiful city in the world):

> If you are lucky enough to have lived in Paris as a young man, then wherever you go for the rest of your life it stays with you, for Paris is a moveable feast.

A young trader should work hard but then make sure he finds time to play and grow individually. Uniquely, NYC offers excitement in all fields: movies, Broadway, sports, law, music, fashion, parks, law, medicine, academia, food, art, advertising, media, new media, fashion, Wall Street, business, private equity, start-ups, and so on. Young, single, and living in NYC is an experience of a lifetime, one in which every drip of knowledge and experience should be consumed. Fulfillment outside of your trading is a key to becoming your best trader.

This being NYC, a young professional lady and young professional man can often meet and start dating without agreeing to dating guidelines. Iceman innocently got himself in a predicament, meeting, liking, and dating two. And he was unclear whether either woman would be concerned to learn there was another. But he never actually took the time to settle this quandary.

Then came Valentine’s Day. Young Iceman now was deeply stressed, like most are holding a 5,000 share AAPL position. He couldn’t take them both out on the same night. He didn’t want to end it with either. Both girls were great. There was never a talk with either. His solution? A night out with GMan and drinks to search for a solution. This would be the equivalent of asking Charlie Sheen for tips on sobriety. GMan bought a new dog for the very purpose of procuring Iceman’s problem. Extending this example further (and having some fun with GMan), you might say GMan bought a dog to be more of a “dog.” Doing some of his best work in this field after a few drinks, GMan devised a solution: a fictitious e-mail. (I would just like to clarify that I had no idea any of this was going on until months later. And I personally apologize to any female readers for these shenanigans.) GMan sent Iceman the following e-mail below to extricate him from his quagmire.

(Warning: Uncontrollable laughter may ensue shortly. Please secure your nearest beverage before continuing.)

> From: GMan
>
> Date: February 10, 2012 6:10:58 PM EST
>
> To: Iceman
>
> Subject: You are gonna hate me
>
> There is a big announcement out of Australia that will affect the Asian market and I'm gonna need your help on Valentine's night. Apologize to your girl in advance. Mine hates me already. Need you to help me manage a few positions. Meet me at the office at 9:30 p.m.
>
> Thanks.
>
> GMan

Iceman then forwarded this GMan-hatched bind-solving e-mail to the unlucky girl (or lucky girl?), and he had his escape. Weeks later, Iceman manned up with the unlucky girl, and then there was one. Of course, that soon led to a first meeting with the parents. "They are not gonna like me. I am not that interesting if I haven't been drinking," Iceman poked fun at himself. The desk roared with laughter and agreed that it was not a good idea. He just got bombed the night before with the summer training program trainees and hopped on the train to a new adventure he knew he would find a way to navigate.

So you might be wondering what these anecdotes have to do with trading. They do: Iceman is not afraid of anything—and this shows up in his trading. And he has found a niche in trading stocks that most do not have the guts to attempt. Also, Iceman enjoys himself on the desk after work, which shows up in his trading. The new field of positive psychology, founded by Dr. Seligman, clearly shows the link between happiness and improved performance. Happiness comes first then followed by success.

No Guts, No Glory

Most traders are uncomfortable when I deliver critical feedback. Not Iceman. “Bella, I want you to yell at me to be bigger when you think I am not big enough.” I used to have a favorite t-shirt from the ski resort at Okemo Mountain that said “No Guts, No Glory.” I should hand those shirts out to our traders. No, I should have Iceman pass them out to our team.

Unfortunately, I can’t say this is true for most of our guys. Let me do my best to re-create a mild scolding I gave in our training room to our desk about, as they say, “growing a pair”:

> You guys have to start taking on more risk. Every trade cannot make perfect sense. Sometimes you just have to play. What exactly are you so scared of? It’s the firm’s money. I am telling you to risk more of our money.
>
> Start looking at these stocks with wider spreads that are trending. Look at CMG, BIDU, IBM, SHW, GWW. Take a controlled chance. I am not saying not to control your risk. I am saying that if these stocks are really trending, you might have to risk more than you are used to. Give them a shot. Try to learn them.
>
> Look, you guys know what you’re doing. But you have to stop being such a bunch of wusses. Let your hands go. Sometimes it’s too risky not to take a shot at a stock with a bigger potential loss because of the potential upside.

Iceman was in the room, and I should have excused him before the meeting began. He has none of the Trader Wuss Syndrome issues that can stifle a young and developing trader. No one on our desk trades The Opening Drive Play better than Iceman. An Opening Drive Play is a strategy in which a trader gets long a stock that gaps up, is In Play, and trades for a momentum move higher right off the open.

An example of Iceman’s prowess trading opening drives can be summarized like this: If LNKD has gapped up and then spiked on the open, I will ask, “Iceman, are you in LNKD?”

“Yep, Bella. I’m just holding.”

The best of the high beta stocks like AAPL might be In Play, and I will notice its opening drive.

“Iceman, did you catch AAPL?”

“Yeah, Bella. I am just holding. Trying to get bigger.”

One day very early in his trading career, Iceman sent a trading review to me after the close that serves as a classic example of his guts to trade:

Analysis:

> What a day. I am really exhausted after this trading day. I probably tried to do too much. That being said, I traded the news well and aggressively. I was down 400 bucks when the news came out because of the crazy market tick, but I stayed poised and made back $1,300 and went up as much as +$880 or $900 at one point before finishing up $760.
>
> I traded WLP with a ton of size and it didn’t work when I had size, so I didn’t make a chop on that and took a really big rip, which set me back, but I kept taking trades with size and saw a really good trade in HCA and used about 2,000 shares on that, and that is when I made $800 in that trade and then another 500 in other healthcare stocks that I was initially down in, and that helped turn my day around. All it takes is one good trade.
>
> **I think today was good because it showed that I have the guts to trade the volatility with size.** I have always had no fear trading these situations, but today I traded them with 1000–2000 shares, which was awesome. Even though I shorted WLP at 67 for 1,800 shares and it stopped me out and then went down without me, I still was in it and I still came back strong with size in other trades. I think HCA is my second-best trade ever.
>
> That being said, VRTX should have been my best trade ever. I need to be open-minded about the pattern and not just the distance traveled. What I mean is when I short 55 and then it goes down to the 52 low, this is still just the first target. It is entirely possible that it could still go down points from there. Also, if a stock is really weak or really strong, I should wait for either a turn on the 15-minute or an exhaustion blow-off bottom or top move to get out of my core. Also, I shorted BIDU the first time through the big level and then lost on that on size and then had no size the next time through. Should have been the other way around.
>
> Also, I should have been bigger in UHS, and I should have been more open-minded about being long UNH into the close. I kept being biased to be short the insurance companies and long the

hospitals, and even though UNH was a long, I didn't want to be long and missed the trade. It is entirely possible that people with this mentality were caught short and there was an intraday long. The same reason that the HCA didn't have follow-through. That being said, I understand my role as a trader is not to be right or wrong, and my job is to manage risk. Being aware of all that allowed me to manage risk well and not give back profits in HCA.

Overall, good job being gutsy. I think this will be a turning point in my trading. I should have been a little less aggressive when the news just came out and focused instead on what the bigger picture short in WLP was and held a wider core. Good job today overall, though.

Iceman revels in added risk taking. If I took him to that Okemo Resort and he was a solid skier, he would be the guy most likely to challenge the group to the bottom on a northeast icy black diamond trail. Of course, then he would be the first to dare anyone not wrapped around a tree to some drinking game at the ski lodge. And the first to approach the nearest attractive female. Iceman has learned that not taking on risk with outsized reward is in fact too much risk for traders.

So a small percentage of traders will not have the personality to trade high beta stocks or opening drives or "man up" with size. But most can and just need to work on how to improve their sizing strategy. The first step is to point out this potential weakness to them. I just did that, I hope. And let them work on solution improvement. That is now your job. I cannot leave this subject without offering some ideas for you to consider if you suffer from Trader Wuss Syndrome.

Eleven Steps to Trade Bigger

My 11-step process to taking on more risk with your trading is as follows:

1. Build your PlayBook.
2. Choose your favorite setups, or A+ trades.
3. Risk 30 percent of your intraday loss limit on your A+ setups.
4. Hold for the real move.
5. Trade a bigger account.

6. Invest in your trading advancement with higher price and bigger spread stocks.

7. Enter stop-limit orders for your biggest positions.

8. Commit to visualization exercises to improve your performance.

9. Trade options for your bigger swing trades.

10. Develop your All-In Trade.

11. Expand your trading time frame.

Build Your PlayBook

The first step in adding more size is building your PlayBook. First you have to know what patterns are best for you.

Choose Your Favorite Setups, or A+ Trades

Next, sort out your A+ trades from this PlayBook. Select the best of the best from your PlayBook.

Risk 30 Percent of Your Intraday Loss on Your A+ Setups

Develop a risk loss rule of placing at least 30 percent of your intraday stop loss with your A+ trades. Or for swing traders, risk 2 percent to 5 percent (up to you) of your account on these A+ trades. So if your intraday loss limit is $1,000, you *must* add size such that if you lose on the trade you risked $300 in P&L. If with your size you could have only lost $200, you were not big enough.

Hold for the Real Move

Also, you must hold your trades for the real move. It doesn't count if you risk 30 percent of your intraday stop but 10 cents into the move you start getting out of your position. Getting big and selling so early is being a piker. Risk 30 percent of your intraday stop loss and hold for the real move, until there is a Reason2Sell for your swing trades.

Trade a Bigger Account

So let's say that now you can risk 30 percent of your intraday stop loss and hold for the real move. Next you want to get even bigger. At this point, most incorrectly focus on adding share size. So if 5,000 was your biggest position, you start to think about trading 8,000 shares. This is a mistake. A better idea is to increase the size of your trading account, increase your intraday loss limit, and continue risking 30 percent of your intraday loss limit. In short, think of your biggest positions in percentage terms and not share size or P&L.

Let me make my point clearer with a story and a blog. SMB hosted a guest lecturer of international trading acclaim. During our Q&A, one SMB trader introduced that he had been consecutively positive every month for over a year but needed to trade bigger. The hedge fund principal instantly offered advice using a trader he had helped. He said, “I had this one trader I was working with who had a similar issue of putting on more risk, though he trades much bigger than you- a book of 250 million. What did we do? We gave him more money. So keep doing what you are doing. Just trade with more money.” Over time, slowly but consistently increase your trading capital and thus your intraday stop loss and how much you are willing to lose on your A+ trades. With this increased capital, keep thinking of your trades in percentage terms. If you can think of trading in percentages, you become scalable. A trader the firm can easily allocate more capital toward because you offer them a clear understanding of their risk and demonstrable evidence that you can handle more capital. If you do not have a methodology to determine your best trades and how you will place risk, then you are not scalable. And if you do not do this, from my seat, you have not done the work to deserve a bigger bank roll.

This visit from that top trading coach and his sizing idea was captured as part of a blog post reprinted here (see bold).

Ten Takeaways From A Top Trading Coach on How To Be A Successful Trader

Jan 10th, 2013 | By Bella |

SMB had an elite trading coach (name cannot be shared for compliance reasons) visit yesterday for an informal presentation with tips on how to improve trader performance. This coach has worked with the top traders in the world, at prop firms, investment banks, and hedge funds. SMB Trader, King of Men, put together a list of ten takeaways from this talk. We thought you might consider them for your trading.

1. Successful traders have meaningful attachments or some other source of motivation and happiness outside of the financial markets.

2. Successful traders are proactive; they know what they need to learn, and they know what they need to do to execute. Being active alone is not sufficient.

3. Successful traders tend to be process driven; they develop and refine routines that turn good trading behaviors into habits and execute these routines habitually.

4. Successful traders have a unique signature; they have an edge that they execute consistently and improve constantly.

5. Successful traders treat every trade as a learning opportunity, especially losing trades.

6. Successful traders identify their A+ setups, best products, and optimal time frames that are most intuitive for them and work to maximize their production in those ideas.

7. Successful traders avoid thinking in dollar terms; they standardize in terms of percentages to measure performance as well as put on risk.

8. Successful traders have a sniper mentality; they are prepared to wait for as long as it takes and ready to pull the trigger when a valuable targets appear in their scope.

9. Successful traders have a comprehensive set of measurable and challenging yet realistic goals; they regularly evaluate their progress and always ask what they need to do to make further progress toward their goals.

10. Successful traders use all their resources to improve, particularly other traders.

Let’s spend even more time clarifying this technique and why it works. Again, most think of trading size as the number of shares you are willing to trade. Do not use this as a measurement. Think of how much you are willing to lose in percentage terms of your bankroll. There may be limits to how much you are willing to lose given the size of your trading account. This might not go away even if you are ready to trade bigger. A rip in that bigger trade with your present-size trading account may bring trauma to your trading brain. The loss may be too much money to you given your account size. That is why you need to increase your bankroll. Get more capital to trade. Then your loss will just be a percentage of this higher bankroll, and you will still have plenty of money left with which to trade.

In summary, increase your trading capital for your trading account. And then keep taking the same percentage risk for your trades. (This assumes your ideas are scalable.) Keep doing what you are doing. Think in percentages of your account as a swing trader and intraday trader. (And, seriously, if you need some more capital, you are consistently profitable, and you need someone to take your added downside risk, give SMB, or a firm like ours, a ring. This is what a true prop firm does.)

It will be an individual and long journey to add size. Do not force this process. You cannot go from being able to lose $300 to $1,000 overnight in your A+ trades. Add incrementally. An extra 20 percent for each 10 days of positive trading data is an effective technique.

Invest in Your Trading Advancement

Next, as mentioned at the beginning of this chapter as we discussed taking on more risk with your trading, you also want to invest in your trading advancement. Dabble with higher-price and bigger-spread stocks. Attempt Opening Drive Plays. Play with stocks that are more volatile. Start with 100 shares. Just try it. Invest in your trading career by taking some growing pains losses in these high beta stocks and bigger-spread stocks. Consider this your investment in your trading education for additional trading strategies. Most likely, you will take some losses before you find setups in these other types of stocks that you can consistently trade. I often have to plan a yell session at my guys, like the “No Guts No Glory” section, to let them know it is permissible for them to lose on these setups. I want to invest in their education for these plays. Go ahead and lose firm capital. In the end, they will add new trading strategies from which we will all profit.

Enter Stop-Limit Orders for Your Biggest Positions

Stop-limit orders (if a stock hits a price, you are automatically executed) can help you take on more risk with your trading. I feel calmer when I place automatic stops for my bigger positions. Recently, I was trading LLY. It had bad news, gapped down, and then popped right on the open. I faded the up move with shorts for a pull in to 49, the discernible support on the chart. I saw that LLY could not trade above 50 (see Figure 9.1), so I started a short position with an automatic stop at the intraday high of above 50, or in this case 50.01. There was a nice battle on the tape at 49.80. The bids dropped out in a way that my intuition signaled a large short position was now the right play. So I shorted some more at 49.74 and 49.70 with stop-limit orders at 49.82 and 49.86. The right play was to get aggressively short. There was nothing to stress out about as my automatic stops were in. I did not have to worry about how and where to exit anymore. I could just sit, gather information, and wait. LLY ended up trading down to 49. Chop! But using stop-limit orders like this is a nice trick to jump start your ability to get bigger in your best positions.

Figure 9.1

On our desk, we discuss one caution about entering stop-limit orders. This is a little insider baseball, but I cannot leave this out of this discussion. *High-*

frequency traders (HFTs) often have access to your stop orders because of their agreements with the exchanges. I will save whether they should for the regulators and policymakers, though it seems intuitive that they shouldn't. Sometimes it can be better to set an alert for where you will exit and then just manually close your position. We do this so that the HFTs do not just run our stops for profit and leave us flat a terrific risk/reward opportunity.

Commit to Visualization Exercises to Improve Your Performance

Visualization is a powerful tool to help you trade bigger. My good friend Bruce Bower, doing some of the best writing on becoming a better trader in the blogosphere, wrote a three-part SMBU blog series on visualization exercises, *Everything You Wanted to Know about Visualization and Trading* (Part I, Part II, Part III). I wrote about this technique in *One Good Trade.* Video lectures from Dr. Andrew Menaker, Dr. Phil Pearlman, and Dr. Steenbarger on this mental exercise are embedded in our training program, the SMB Foundation. Dr. Steenbarger's books and blog, TraderFeed, are wonderful resources for learning how to use visualization to improve trader performance. In short, you will not trade bigger until you spend the time doing visualization exercises to see yourself trading larger. If you are prepared to do this work every day for three months, you will build the mental skill to trade more size. If not, you will be stuck at underperforming trader. It's up to you.

Trade Options for Your Bigger Swing Trades

Some swing and intraday traders have trouble staying big in positions because they see all the ticks in their stocks. Each tick is a temptation to convince yourself to exit. Traders on our desk have found a way to combat this urge. They place their bigger swing trades with options, which makes it much more difficult for them to wuss out. Performance students might cite the 20-second rule as authoritative backup for this technique. Let's say you want to learn how to play guitar. Moving it 20 seconds closer to your couch or wherever you mostly sit in your home makes you more likely to practice. The takeaway is that the easier you make it on yourself to build a habit, like practicing your guitar, the more likely you are to successfully build that habit. Building from this rule, we use options to make it harder for us to fall prey to the temptation of the ticks, by making it easier for us to stay in the position.

Develop Your All-In Trade

I have been thinking about a new trade, the All-In Trade. I have been thinking about this trade for a few years and how it would work. Shark, during his review after the close on a Friday, was working on it. Let's start by reading his review (edited):

> I went for it with an A+ trade. I had 8,000 or 9,000 shares at one point. Now maybe I overtraded it, but I'm working on taking shots when I think a stock is ready, and it just looked three or four times like it was ready to blast off. That is a play where I am gonna pull out five or six grand, at least, if the trade works.

I read this right after he sent it and summoned him to my office. Here, I said the following:

> I love this idea of you getting huge when you *see it.* If you think you really *see it,* I love you just going for it. I mean getting as big as you can while controlling your risk. Determine where you would get out if you were wrong and how much you could get out of within a reasonable price. If you really think you *see it,* then risk your entire stop loss. Just go for it.
>
> The key is you have to really *see it*. You might really *see it* three times a month. Maybe less. But I love you seeing this as a separate pattern. This is a special opportunity. And all I want you thinking about when you see it is how big can you get. How can you get bigger? Am I big enough? As long as you can exit at a reasonable price. Heck, I am even fine with you exceeding your loss limit if you think you really see it, it is ready to go, and this is a special time.

During The PlayBook webinar series, created as a celebration for this book, we discussed with the trading community the concept of A+ trades. To review, first you build a trading PlayBook of setups that make the most sense to you. Then you ferret out the best of those trades, which we call A+ trades. We set risk rules for these A+ trades. For the intraday trader, if you see an A+ setup, you *must* risk 30 percent of your intraday loss. If you are a swing trader, you *must* risk 2 percent to 5 percent of your trading account. This is a powerful exercise to help you trade bigger and make more P&L.

But what about the best of best A+ setups? As a trader, we are sometimes trading when we spot our A+ setups and just *see it*. By "we just see it," I mean that we catch two things: The position has an incredibly high chance of working, and the trade will work *right now*. The ability to Read the Tape helps us see it!

For this setup, perhaps also called the I See It Trade, I propose that you risk your entire day. Risk your entire intraday stop loss. So if your intraday stop loss is $3,000 and you determine that you can get out of 15K shares with an average loss of 20c, you *must* have a position size of 15K shares. You are all-in for this trading session, as they say in poker.

One thing to consider is the psychological risk for this trade. A rip that breeds disappointment is good. A rip that causes trauma is bad. If the rip causes trading trauma, get rid of this trade. Trauma harms your trading, while disappointment is just your journey to getting bigger.

Also, you may only see this trade three times a month. These are special trades. These are the best of best A+ trades and for only when you *really* see it. If you think you see it once a day, we need to work on what this trade really looks like for you.

Finally this trade takes advanced trading skill and discipline. Here's how. After you are All-In the trade should start to work for you immediately. This is why you went All-In. If the trade doesn't work immediately then you MUST start piecing out of the position slowly. Offer some out. Offer some out hidden. Hit a few bids. Offer some more out. Slowly and with trading care, get back to the size of an A+ trade. A skilled pro trader can get in an out of a 10k share position in a liquid name without leaving a foot print.

I love the idea of a few times a month you just deciding you are all-in. And whatever happens, happens. Keep rehearsing your strategy for these special setups.

Expand Your Trading Time Frame

As the intraday and swing trader knows, getting bigger is not just an issue of mindset and capital. Some trades are not scalable. Slippage may interfere with adding extra size to certain setups. One solution is to expand your time frame so that slippage does not change the risk/reward. For example, instead of trading on a 5-minute chart, think of setups you find from the 15-minute chart. In the next chapter, you learn how GMan implemented this with his favorite setup, the Pullback Trade.

Try these 11 Steps to Trade Bigger. I hope it helps your trading!

The Unavoidable Psychological Journey to Success

Let's pivot here to examine another lesson we can learn from Iceman: There is an unavoidable psychological journey to trader success. No one arrives to the show without "issues," "demons," or however else you want to characterize psychological weaknesses. If you struggle with psychological roadblocks, you are like every other trader who has ever existed, including the successful ones. Building the proper psychology and state of mind that a trader requires is a skill. You do not read a book such as *Trading in the Zone* or attend a lecture, perhaps "Become a Millionaire in Six Quick Steps," or talk to a "guru" and then just *get* it. Our traders are exposed to the works of the best trading psychologists. Remember, our training program was generously scrubbed by prominent trading psychologist Dr. Brett Steenbarger. The traders are taught techniques to cure any issue holding them back. But there is still a journey that every trader must endure to learn how to manage himself. Here is the journey that Iceman took, and also the template, Five Steps to Improved Trader Psychology, to rectify any psychological trading issue.

Overcoming Your Psychological Issues as a Trader

Here is a case study of Iceman struggling with his psychology at the start of his trading career. I am sure that many readers have experienced similar conflicts.

Iceman:

> I'm really disappointed. This was bad. Probably the most disappointed I have been in myself in a long time. There is no reason, no excuse, that I'm not up 2K today.
>
> Honestly, I traded the open so well. I was up like 500 bucks by 10 a.m. Then I gave it all back. Then I made it all back and finished up 630. Between 11 a.m. and 1 p.m., I did nothing but lose money. In that time, I could have bought back IBM on that trend line around 194.50/195 twice. I am just so mad at myself for not being bigger in IBM.
>
> In reality, I should have been up like 800 today. I had a $170 error when I accidentally got in IBM instead of MLNX because I entered an order in the wrong market maker box and gave back 170 bucks in IBM. That being said, 800 still is not a good day for

earnings season for me. Anything short of $1,500 is a disappointment. So, either I am trading wrong between 11 and 1, or I need to be less active at this time.

I think if I am up on the open I need to be better at settling down, not being very active, and looking for Trades2Hold with real risk that I actually want to take and potentially hold through mid-day. I need to be better at transitioning from momo *(momentum)* open trading to Trades2Hold. I eventually made this transition and made money from 1 to 4, but I think I did a poor job of this.

The part that makes me angry is that I know this. I even said to myself around 10:30, "Time to settle in, change trading, and wait for setups." Somehow, it all didn't work out for me. Also, the keystroke error really bummed me out. Without that error, I made about $525 in IBM for the day. I didn't buy back the first 194.50 or the second or the third.

Not acceptable. It's fine to not do the second, but the first I must do. And later, when the range is established, I should be bigger buying at support. Also, WCC, I should have 1,000 shares, not 200. This is pathetic.

I am trading way too light. So often I am perfectly correct on a trading idea on no size. I really am selective, and I do have a set playbook, which is why my win rate is high. I need to make the most out of this by actually sizing up. I had almost $2,200 of positive trades today and about $1,500 of losing ones. This is too much to lose. If I cut down how many losing trades I had today, I ended up having one hell of a day. Need to be more selective between 11 and 1.

How best to resolve this? I reminded him of the one key element that intrudes on all traders:

Bella:

You are too emotional while you are trading. You have to work on just making trades and not worrying so much about the result. You are getting in your own way by caring too much and letting disappointment in trades affect finding other trades.

Thoughts?

In other words, always be looking for that One Good Trade, and the money will take care of itself. We miss trades, we fumble on our keys, we are too small at times with our best trades. This is all part of trading. Do not self-interrupt your progress with a trading-in-the-past mindset. Next trade, next trade, next trade.

Iceman:

> You are right. Yeah, I mean I think I just get so mad at myself for not being big in trades that I make chops in. Like I have such a good understanding about what my PlayBook is and how to execute trades, just not big enough. I think if I were performing to my potential, I would be less emotional. Like, I make trades that others find hard to make and consistently make money in them. Why don't I risk more? How do I get past this mental block?
>
> I don't think being emotional prevents me from finding other trades, even when I'm emotional, I am focused. Like today, I still bounced back and made 600 bucks after giving back a lot.
>
> You are right in this situation: I see missed opportunities in stocks I trade, and I feel like because I maybe didn't make enough the first time, I don't buy the pull in, which turns out to be an even better trade, and this is when I get mad at myself.
>
> What do you suggest I do?

Bella:

> Controlling your emotions is a typical problem for the active pro trader. We trade so much that disappointment sits ready for an appearance on every trade. You, like every successful trader before you, suffer from the disease of impossible self-trader expectations. Trading is a game of embracing limitation, often our own. What can you do so you are not so mad at yourself intraday?

Here are some typical disappointment remarks (I call this *trading-in-the-past*) that we hear from many traders:

> I didn't make enough in a trade.
>
> I should have been in another trade.
>
> Why did I make this piece of *s**** trade?
>
> I should have sold this position earlier or later or never.

Iceman has made all of these remarks at one time or another. Denise Shull cleverly frames the context of most trading. She has said that traders are unhappy 75 percent of the time. They are unhappy either because they lost on a position, won and were not big enough, or regret they missed a great trading opportunity. It all comes down to a trader—in this case, Iceman—getting in his own way, self-interrupting. By being so hard on himself for not performing better in real-time, he cannot perform to his ability. It is a vicious cycle of underperformance fueled by personal ambition or, better said, impossible self-trader expectations.

Five Steps to Improved Trader Psychology

So what can we do to break this cycle and get this trader on a path toward improved performance? Here's what:

1. We identify the problem.

2. We allow the trader to develop a plan of correction. First, let the student struggle with a solution. He learns more.

3. We offer a plan of improvement (visualization exercises; and again see Bruce Bower's series on the SMBU blog, Parts I, II, III).

4. The trader does the work, the daily exercises, to improve.

5. If none of this is enough, we call in the psychology coach (sometimes two).

I am sure that thousands of readers suffer from the same trader flaws and feelings as Iceman. I do. I have to work so that they do not infect my trading. Take comfort that solutions exist. It just takes the smart solutions presented here.

I continued this help session with Iceman with the Step 2 approach—allow the trader to develop a plan—and he then responded to my latest e-mail with this:

Bella,

You asked me to discuss being calm. Here is what I have come up with:

1. It is important to understand that this is a marathon, not a sprint. By understanding that this is a continuous game and having confidence in my PlayBook and trading abilities, I can reason that one rip doesn't mean that I am screwed. With the right trading system, I will have more chops, and as long as I am making the right trades, I should make money in the long run.

2. It helps to think of trading as a game. Just play. Don't worry. Just play and keep playing.

3. Think: "Can this trade make my day?" If the answer is yes, and it doesn't work, so be it.

4. I have to be cognizant about the things that make me angry:

- Overtrading In Play stocks, and if they don't offer the best opportunity, losing more than I like on one name
- Getting too top-heavy on longs or bottom-heavy on shorts and chasing stocks
- Not being big enough at the best risk/reward entries
- Overcovering or selling too quickly when I have size
- Sloppy execution because I missed the ideal entry
- Getting slipped really badly

These are the things that bother me the most when I do them. I need to not do these things in order to remain calm. Perhaps I need to understand first and foremost how important it is for me to remain calm. By remaining calm, I perform better and am happier with my job. Being happy and performing well is essentially my main goal. Thus, when I start to do these things that anger me, I need to think of what my goal is (perform well and be happy) and force myself not to do these things for the sake of my goal.

In the end, what makes me money is having a PlayBook and executing my plays crisply. As long as this works for me, I am okay, and all is well, and I need to just chill out and trade.

This was real thought progress. Iceman was finding solutions to improve his trading psychology. He was working his way through Step 2. Psychological issues do not disappear with a single e-mail. PMTC and WLP got the better of his trading emotions soon thereafter.

As the record has shown, Iceman gets upset at missing plays. He got big in WLP the day the Supreme Court ruled on President Obama's healthcare law. Others around him got big as well. He got stopped out. He was pissed:

"OH stopped out of WellPoint. Ripper."

"Why are you pissed?" I asked, sitting behind him.

"I got stopped out."

"It was a good trade. You did the right thing. We all got stopped out. Where would you get back in?"

Then the next day

"[*Expletive deleted*] PMTC," concluded Iceman.

"What?" I asked.

"I got ticked out of PMTC. It just went down 40 cents."

"Well, get back in."

"Yeah."

He got back in, and it continued down.

When he gets so riled up about missing something or not capturing a big move, his angry talk holds back his trading and keeps him from getting into easy trades. Fuming will get a trader nowhere.

Later, there was a knock on my office door, and in strolled Alabama, who claims to be the best hoopster at SMB. No comment.

"Bella, how do I stop trading on tilt?" he asked, as if not understanding he was perhaps the 100th person to have this conversation with me.

Deep sigh. Remember Iceman's earlier e-mail with his list of things that set him on tilt?

"Well, we are not going to fix this in a talk. Go back to your desk and keep a list of all of the things that set you on tilt for the next week. Come back and we will start working one by one on your list."

After you compile that list, you work on each flaw one at a time. Visualization exercises are employed for each mental weakness. One by one, month by month, the trader becomes a stronger mental trader.

As I write, Iceman is at the stage where we are letting him work on his solution on his terms after some guidance from me on his solution plan. If this is not successful, we will call in a professional trading psychologist for further assistance. We are all works in progress, even the fearless Iceman.

Obsessing about His Trading

Iceman cornered me for 15 minutes after the close on the last day of a trading month because he missed making his monthly P&L goal by $30.

“Bella, I am so pissed I didn’t reach my goal. Is that weird? I don’t know why it just bothers me so much.”

I told him several things: He was getting more consistent with his trading, that I was not seeing as many down days as I used to with his trading; he was doing a good job holding on to winners; and he was trading volatile high beta stocks more, which best matched his personality.

The next month was even better for Iceman. His good days found higher P$L. His results continued to be more consistent. He understood his strengths better by concentrating on the opening drive and expensive high beta stock plays. When he learns how to manage his emotions as well as Shark does, he will likely come after Shark for future top trader on the desk. Shark does not scare Iceman. Iceman thinks Shark is just keeping that best young trader seat warm until Iceman’s time comes. And with stocks that offer more risk and more reward, and with Iceman trading the stocks that match his personality more often, you know, perhaps, it is.

Perhaps this chapter has helped you to start thinking about whether you take enough risk with your trading (or even with your life). And if not, start crafting your solution plan to slowly add good risk to your trading and thus improving your P&L. Remember what we learned from Iceman: If you are not taking enough risk with your trading, you are taking on too much risk as a trader.

Let’s take a look at a trade that Iceman made that is a both high beta stock trade and an Opening Drive Play. This is double the uncomfortable risk that most traders are willing to take in one trade. Would you expect anything less from the Iceman?

Opening Drive Play

Iceman

LNKD

August 3, 2012

Big Picture

- The SPY got above important resistance.
- LNKD gapped up in the after-hours.

• Held above the after-hours high in the premarket.

• Extremely bullish setup that needs be played more aggressively.

• Explosive stock that is now more likely to move quickly in our favor.

• A type of Momentum Trade.

Opening Drive Play

• “I cannot make money on the Open,” said by too many traders.

• A pattern that works on the open.

• Excellent risk/reward when you master this trade.

• Can be up big $$ by 9:45 a.m.

• Difficult trade.

• Quick execution skills.

• Gumption.

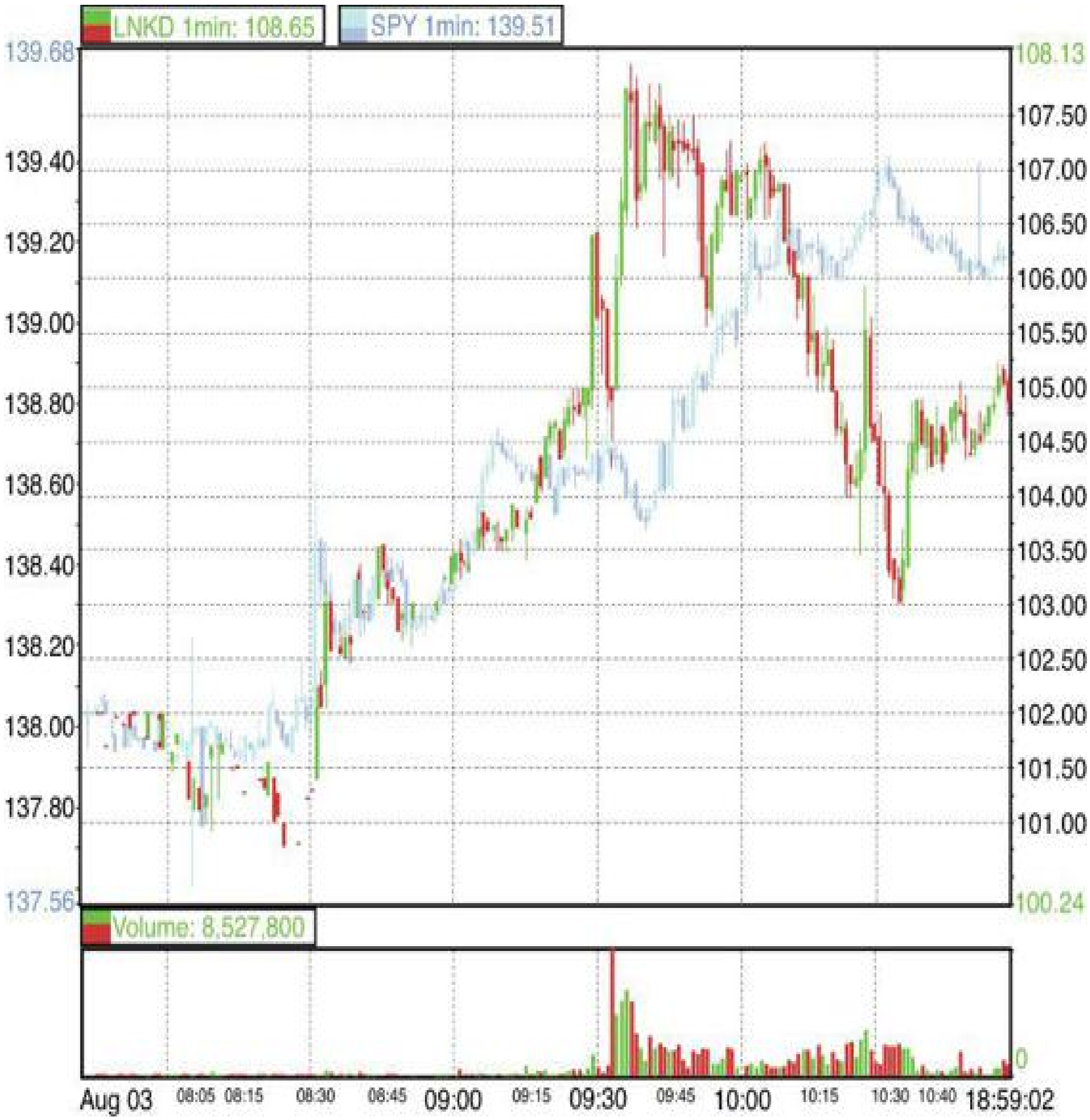
• Capture the big move.

Big Picture

The SPY has been in an ascending range since early June. It finally got above 138.60 on the open, which was the resistance level from the end of July.

SPY Versus LNKD

- LNKD had been in consolidation between 103.50 and 104 at the top of the after-hours and premarket action. It finally got above 104 as the SPY got above the 138.60 level.
- On the open, the SPY traded higher, and LNKD made a push toward 108, which was the next major level. This stock had fresh news, but the bullish premarket price action, coupled with the strength of the SPY, made it a better opening drive trade overall.



Trade Idea

- In the after hours, the stock traded above the prior day high and held above 100. Then in the premarket, the stock drove over 102 and held between 103.50 and 104, above the action from the after hours.
- This shows that not only was the reaction to earnings viewed positively, but also that the buyers clearly had control. This is my

favorite pattern for an opening drive long. Seeing this pattern made me confident that I could take on a bit more risk in a stock that is normally rather thin and risky.

• Probability is very important. There is a difference between risk/reward and probability. Just because a stock has a tight 5c consolidation and one is comfortable taking the trade, especially beginners, doesn’t mean that it is likely to work.

• Having this probability on my side allows me to pay through offers on the opening drive and hold a core until the next level. The opening drive must stop eventually, and therefore we must understand where those sellers that had lost will legitimately think that they have a chance to slow down these powerful buyers that had clearly been winning since the news release.

• Naturally, the first place is at the next big level of 108, and then the next level after that is 110. So, my play was to hold a long on the opening drive as long as it is above the 103.50/104 area and hope for a move close to 108.

• Once the stock approaches the 108 area, my risk/reward doesn’t signal to hold anymore, and I sell when, after having a battle, it fails to get above 107.50.

Intraday Fundamentals

• Third-quarter revenue will be $235 million to $240 million, Mountain View, California-based LinkedIn said in a statement yesterday.

• Full-year sales will be $915 million to $925 million, ahead of the $880 million to $900 million it projected in May.

• Analysts on average were predicting third-quarter sales of $236.3 million and 2012 revenue of $906.3 million, according to data compiled by Bloomberg.

LinkedIn (LNKD)

LinkedIn Corporation (LinkedIn) is a professional network on the Internet with more than 90 million members in over 200 countries and territories. Through the company's platform, members can create, manage, and share their professional identity online, build and engage with their professional network, access shared knowledge and insights, and find business opportunities. Its platform provides members with solutions, including applications and tools, to search, connect, and communicate with business contacts; learn about career opportunities; join industry groups; and research organizations and share information. Its members create profiles that serve as their professional profiles and are accessible by any other member, as well as by anyone with an Internet connection.

Average Volume: 3.5 Million

52-Week Range: 55.98–120.63

Short Float %: 8.0%

Average True Range (ATR): 4.65

Long-Term Technical Analysis

Short-Term Technical Analysis

Reading the Tape

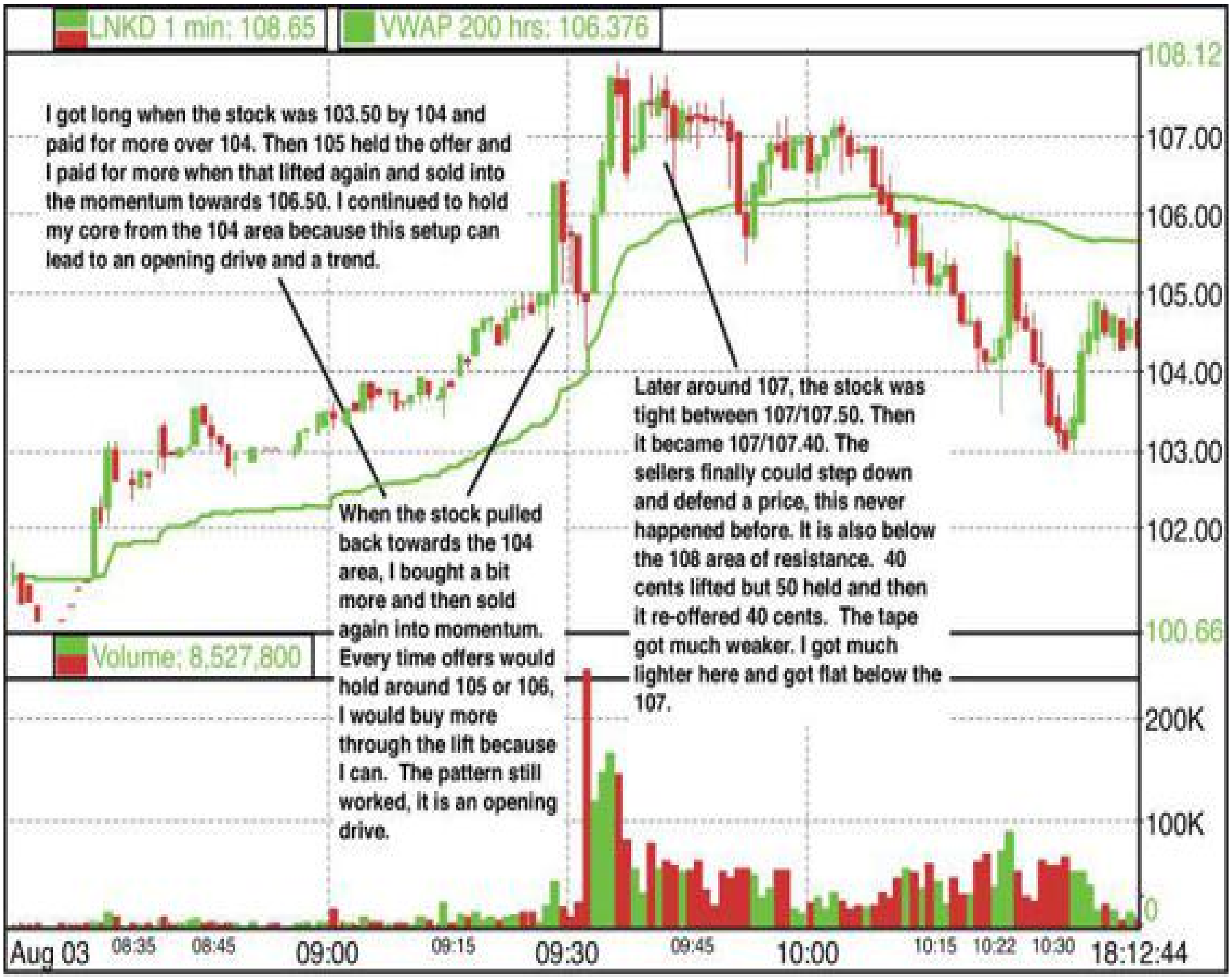
- I noticed the buying in the premarket, and then I noticed how when offers would lift, the stock would just hold higher and not really drop out.
- Once it got above the 104 offer, it never came back. On a move to 106.50 so quickly after lifting the 105 offer, the stock gets really steep, and this is usually a good place to take sales. That being said, the 105 lift and move gives us a place to pay through 105 momentum and lock in some cash flow.

• We still hold our core from 104 for some, but we take sales once it slows for whatever we paid over 105. Similarly, later when it pulls back to 104 and then lifts the 106 offer, we pay and capture the move toward 108. The stock later forms a mini range between 107 and 107.50. It then forms a mini range between 107 and 107.40. This is a sign that the sellers stepped down.

• Finally, a weaker tape and a change in character. Then when it lifts 40, it can't lift 50 cents and gets back below 40 cents. This is a huge change in character. For the first time since 104, the sellers are winning the battle over the buyers. I got much lighter here, and then hit the rest below 107.

• It is very important to get a feel for stock on the open. It is okay to be aggressive early on, but when things change, you must be disciplined enough to understand that this particular trade is over. There may be more in the stock, and it might not be done going up, but this opening drive has ended.

Trade Management



Trade Review

- This was a good trade. As traders, we need to use screen time to our advantage. When we see that certain trades work really well over and over again, we need to take advantage the next time we see it.
- I knew that this was a tough stock, but the *probability* was very important and allowed me to have confidence and get in the stock regardless. I knew that it had potential to drive on the open to the next level, which was several points away.
- However, I think I could have done a few things better. I could have been better at buying it back near 104 and paying for more. If I pay for more through the 105 lifts, I can hold more for the bigger move and take more sales along the way, making more money.

• Sometimes it is tough to gauge a pull in versus a reversal on the open. So, buying in to the 104 area isn't the best place to add a lot, but certainly a place to add some. The place to add a lot is paying through these offers so long as the pattern doesn't chance.

• Everyone tries to get in between 107 and 107.50, but in reality, this is a weak tape; the real place to make money is by having confidence, being aggressive, and capturing this opening drive. Once I already made money on the move premarket, I could have been a bit more aggressive with size once the bell had opened.

Trade Idea

• Long above the resistance at 108.

• Watch 104 as possible support for a pullback play.

• Longer-term resistance is at 110 and 115.

From the Training Room: An Opening Drive Review with Iceman

I counted at least 24 important trading principles discussed in this trade review with Iceman. I highlighted these important trading principles with my comments in the columns so that you wouldn't miss them. Get those highlighters out because this is a trade review of learning.

LNKD

August 3, 2012

Trade the best setups for you!

Iceman: I'm going to talk about my Opening Drive Play, a trade I make a lot. For me, it makes a lot of sense. I think it's a great way to start off the day. It's a great tool to have, if you start the day off with one of your favorite plays. You boost your confidence [if] a winning trade right out of the gate gives you a little risk capital to risk on some of the Trade2Hold later in the session. I think it's a really great trade for you guys to add to your PlayBook as well.

Use after-hours and premarket trading to gain an edge.

Essentially, this trade involves a stock, LinkedIn, which had fresh news and a really bullish setup in the premarket and the after-hours. The advantage of a stock printing in the after-hours and in premarket is that it gives us clues on how it will behave when the market opens. There are certain after-hours and premarket setups that make us more confident that there will be an opening drive.

There is no substitute for screen time.

Trading is all about experience and screen time. When you train your mind and eyes to watch the market a certain way, you start to see patterns. Over time, I've learned that when I see certain premarket action, then more likely there will be an opening drive, and that's exactly what happened in this setup.

Simultaneously, the SPY got over a resistance level, which improved the chances of our long position working. We also have to keep in mind that the characteristic of LNKD is that it has the potential to move a lot. Like on its IPO day, LNKD exploded. Part of the mannerism and characteristic of LNKD is that at times, when it starts going, it gets very loose and the spread opens up, so you don't want to get caught on the wrong side of it because you'll get run over. This stock can move a lot on the open, and if you're caught on the wrong side, you want out because of the potential risk involved.

Bella: Let's just make a couple of points about how we can use premarket and after-hours trading to help us. If there's something in the after-hours where there's a lot of volume done at a particular price and it can't get above that price, we can actually use that level when the trading session opens up. The same thing goes for if the stock can't get below a price but does a lot of volume in the after-hours or in the premarket. We can use this level to trade off of when the market opens.

Iceman: Some of the best setups are if a stock gaps up in the after-hours and then higher in the premarket and holds; that's a sign that we know the news was received positively because the stock gaps up to begin with, but when it actually holds higher the next morning, above where it gapped up, at that point we know that the buyers have control and the people who aren't in are more likely to pile in for an opening drive. The reason things work in trading is because there are certain patterns that lead to certain results, most of the time. Experienced traders know that when a stock holds in the after-hours and holds in the premarket even higher, that might lead to an opening drive. So if a lot of traders are viewing this setup that way, there's more potential for this to happen.

Bella: I'll make a couple of points about an Opening Drive Play overall. I have heard too many traders say they can't make money on the open. So, to me, it's not that they can't make money on the open; it's that they don't have a PlayBook of patterns that works for them on the open. And I think what probably too many traders do is that they look at their results and see that they are not making money on the open and just decide, "Well, I'm not going to trade on the open," as opposed to, "Maybe I should be more selective with the patterns that I'm trading on the open and figure out if after I do that whether I can be profitable." This is one of those trades that definitely works and actually has a higher risk/reward (the good Opening Drive Plays) than even some of our Trades2Hold because there's more volatility on the open. With an Opening Drive Play at 9:45 a.m., you can be sitting at your trading seat up a bunch of money, which is always a good feeling, as Iceman pointed out. But it's an advanced trade. It's something that takes quick execution skills and the gumption to actually trade this setup. You must capture the big move. You can't bank 10 cents and think you're capturing the Opening Drive Plays. You have to try to capture a couple of points when that is possible.

Iceman: Yeah, and when these trades don't work, you take a pretty big rip, and you'll start your day with a pretty big loss....

You can make money on the open.

Bella: Didn't you take one today on the open? What were you trading? RAX?

Iceman *(smiling sheepishly and not thankful Bella has reminded him of this rip)*: Yeah, exactly.

Bella: That's no fun, right?

More downside in a trade doesn't mean you should avoid it.

Iceman: Well, yeah, but it doesn't even bother me anymore because I know when these things do work they more than make up for the times that they don’t work. So the goal is even though you take a rip at times, you have the potential for a big move. The risk/reward is still excellent. And over the long run, you’ll make money on this setup if you trade it correctly.

The Big Picture in this stock is that the SPY got above 138.60, which was a level that was important recently. The SPY got above 138.60 and then kind of got a little bit below this level, and LNKD kind of pulled in at the same time. But all LNKD did was pull into the prices where it was accumulated during premarket. I knew this was a support level and wasn’t a place to panic, but a place to buy more. Then when the SPY got above 138.60 and held above this level, LNKD took off.

That’s the SPY, the Big Picture for this trade. SPY has been in an uptrending channel, as you can see from the chart (see Figure 9.2). It’s a bullish market, which makes it easier to pay up with some of these riskier stocks and anticipate an opening drive.

Figure 9.2

Iceman: The stock moves up; 138.60 put up a little bit of a fight. LNKD exploded in premarket, pulled back in, and then as the SPY made a hold above 138.60, it resumed its uptrend and then also exploded further (see Figure 9.3 with SPY overlaid on LNKD).

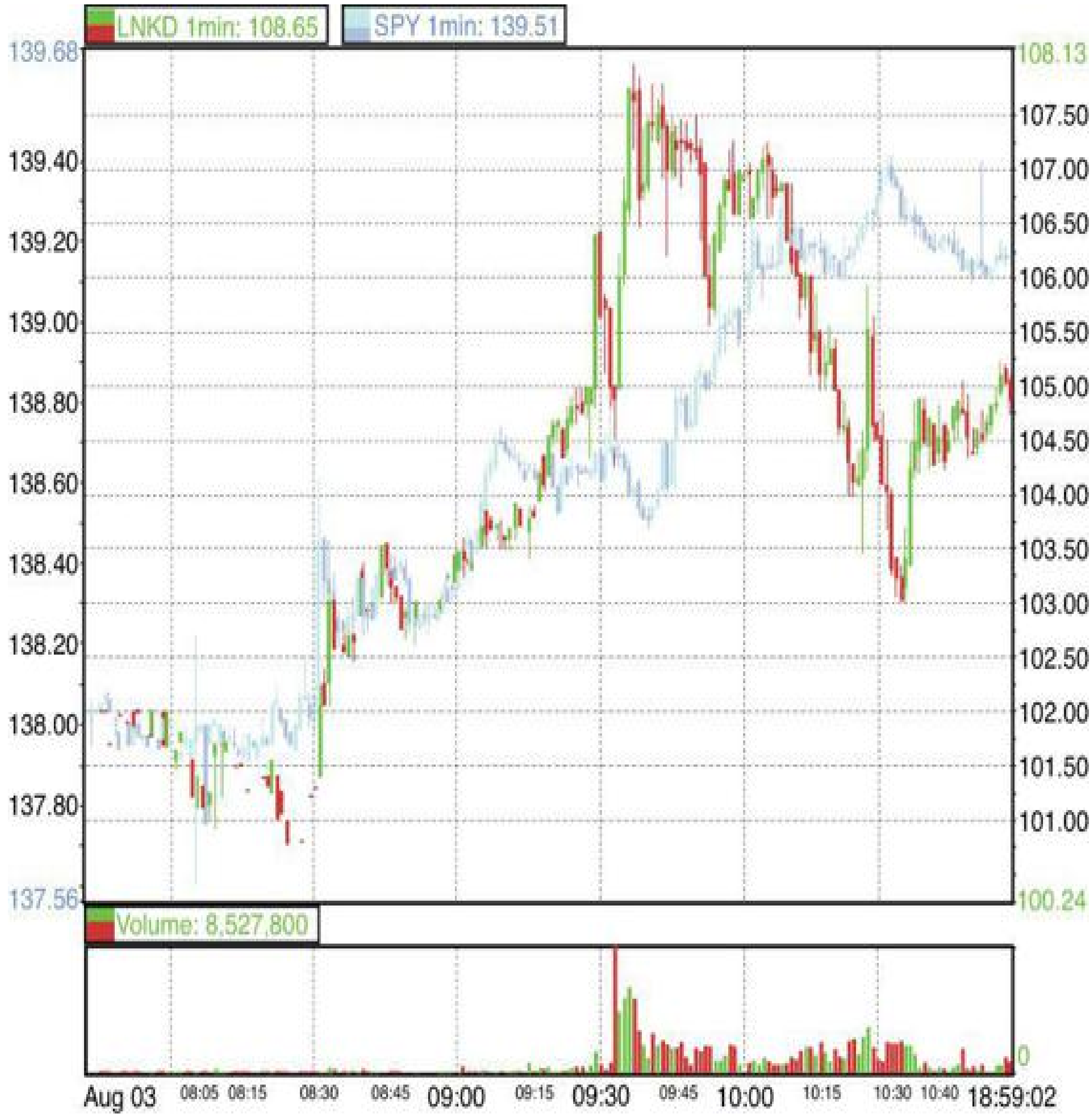


Figure 9.3

Technical levels work better in high beta stocks.

The stock pretty much held higher above 100 *(which is an important level)* in the after-hours. In the premarket, LNKD held 103.50 and 104, so it formed a little range between 103.50 and 104. Here, you have a stock that moved 10 to 14 points, and you're saying, "Wow, this moved a lot; how do I control my risk?" or "It's finally in a 50 cent range." Fifty cents for a stock, by the time is all said and done with 20 points of movement, is actually pretty small, right? So when we see only 50 cents of consolidation in a setup like this, we really have to capitalize on this.

Once LNKD was 103.50 by 104, I was thinking, “If it gets above 104, I know that my risk is below 103.50.” I want to get long if LNKD gets above 104, so that’s pretty much what I did. One thing that is very important in this trade is probability versus risk/reward. Everything is in our favor: a strong market, strong news, and bullish after-hours and premarket activity. All this means is that the probability of the stock trading higher is pretty good. Like I tell you guys all the time, if there’s a 5c consolidation, that’s good risk/reward, but it might not be high probability. You might take that trade ten times and lose on it every time. In the end, you lose 50 cents. Here, you’re risking 50 cents once, and the probability is much higher.

Trading is a marathon, not a sprint. Yes, your P&L resets everyday, but that doesn’t mean that your statistics reset every day. In the long run, you want to be doing things that have the highest probability of success. That’s important. That’s why I love trading these setups. By having this probability on my side, this allows me to comfortably pay through offers once I know that they are lifting and holding higher. And I keep doing that because I know “innocent until proven guilty.” Until that pattern changes, the probability is still on my side.

The next big level is going to be 108 above 104, and the stock is actually going to make a push to 106 and pull in. But eventually, it’s going to find 108. And when it gets there, that’s where for the first time things change.

LNKD actually forms another tight consolidation between 107 and 107.50, just like it did earlier. Every time offers would lift up to 108 from 104, LNKD would lift and hold higher. Once we got to 107.50, LNKD formed this range. Then 107.40 started to hold the offer. So for the first time, sellers were able to get some footing by holding lower. And to make an even stronger case on why I should have sold, 40 cents gets up, it goes up to 50 cents, it gets right below 40 cents, and 40 cents holds the offer again. This is a totally different pattern on the tape than the past 4 points.

> *Great example of how you can tell a stock is done by reading the tape.*

LNKD was lifting the offer, going up, lifting the offer, going up. Finally, it lifted an offer, didn’t go up, and then re-offered lower. That means the sellers finally found their footing. Meaning this was a clear change in character on the tape.

Stocks do not trend on the open.

Now on the open, you don't know whether a stock is going to trend yet. You're simply following the momentum. You are looking for a stock to change its character on the tape, and when you see a stock change its character, you get out. This doesn't mean the stock is done for the rest of the day. In this case, LNKD did try to make another push higher a little later in the day. And over the next couple of days, LNKD made a push to 110. But for an opening drive, we are more than happy with a four-point move and then sale.

Let's get a little more specific. So LNKD beat their sales projections. They beat their number. But essentially it was the solid sales that got people thinking optimistically about the stock. These are our Intraday Fundamentals that we consider.

Nice explanation here of the psychology of a short squeeze.

Let's take a look at the longer-term chart (see Figure 9.4). Many traders were shorting LNKD into the earnings number, thinking that the stock was going to go down. That was in the 90s. When that number comes out, the stock gapped up. You guys are making trades off the intraday charts, but that doesn't mean everyone is. There are plenty of people making trades off the daily chart. Some traders shorted off this level off the daily chart and sat there, out above the next level. These traders were feeling really uncomfortable when the earning came out and the stock gapped up. When that happened, the last place it touched before falling was 108. That 108 is exactly where that stock is going to go to on this opening drive. You can see later that there's a bigger level at 110 and that the stock will get there on the next day, which is why I said the stock didn't have to stop there. But for that day on the opening drive, that is where it stopped, and it makes sense why it stopped there, as we look at the longer-term chart.

Figure 9.4

Between 103.50 and 104, there was a 50c consolidation and an offer that was held. Once it lifted, that's when the stock made the move in the premarket. In the after-hours, it formed this kind of range. So there was a fight between buyers and sellers between $94 and $100. And in the morning, we came in and the stock was above that $100.

> *I love range plays where this a huge battle that ends with a clear winner. Follow the winner and play for the stock to trend.*

The stock is now above that fight range from the after-hours, which means that a winner emerged from the battle. This means that the buyers won. It's simple. If we are trading above the range, the buyers won, and if below the range, the sellers won. In this case, the buyers won. That is huge. When I arrive in the morning, I look for stocks that do that. Those are the stocks that I focus on for an opening drive.

Figure 9.5 shows the hold above after-hours price action in the premarket.

Figure 9.5

Gaining a "position of strength" is very important to hold a core. Fight for the best price and it is easier to hold your core.

Trading around your core for cash flow trades is a wonderful trading technique to learn.

Iceman: Reading the Tape is important with opening drives, because doing so in the first 30 minutes can give you an edge. When the 104 offer lifted, the stock moved all the way up to 106.50. I remember the 104 offer lifted and then the 105 offer lifted. When the 105 lifted, it went all the way up to 106, 106.50. On the open, when you see those offers lifting consistently, you pay them. I pay through 105, and if it doesn't go up quickly, I get out of my additional lots. I still have my core from 103.50, 104 because I don't know if I'll ever be able to get those prices again. I am in a position of strength by being long from there. This is my core. I will Momentum Trade around my core to add cash flow trades. I pay through 105, the stock goes up to 106, it stops, and I get out of the momentum positions. You can make pretty good money trading like that.

Great example of how to momo trade.

LNKD followed a repeatable pattern on this open. It went through 105, it pulled back, it came back toward 104, it held again there *(breakout price, that's another thing we want to look for).* When we see that and 105 holds and lifts again, LNKD goes up. Then 106 held and lifted and moved up toward 108. As long as that pattern continues, we keep following it. I kept paying when these offers lifted and caught the up moves.

Trade the pattern until it stops.

But that all explains how the whole 40, 50c change of character on the tape happened, which I talked about earlier. The offers stopped lifting, and the bids stopped holding above the lifted offers. This was the clear pattern change that I saw.

With setups like this, it's okay to be aggressive on the open and pay through these offers. But once you see that the character of the stock has changed, you have to stop. Take your profits and go trade something else.

Use the tape to spot when the pattern has changed.

I moved away from LNKD and went to trade something else after I spotted the character change on the tape. You will be tempted to buy the pull in and stay with the stock. But the easy money is over. And now you are not making an Opening Drive Play, but more of a Pullback Trade. This is a very difficult trade. This is an especially difficult trade on the open because there is no clear trend so early in the trading session.

Iceman sure does not lack for confidence!

After the character change, it was now 10 a.m., and things trade differently than at the open. You have a different business model for trading the open than the mid-day.

It is dangerous to make the Opening Drive Play your only skill. And if you're going to try to trade like this after 10, you're going to get burnt. So be careful. Once the momentum trading slows down, you have to switch your mentality to trade other setups like Trades2Hold. You have to be able to switch to an intraday swing trading technique after the open. Don't obsess over it. With this trading style, you have to be very disciplined to do it, but it works.

Switch to Trades2Hold, intraday trend swing trades, after the open.

Let's take a look at my Trade Management (see Figure 9.6): 103.50 by 104, the 104 lifts and goes up toward 106, 105 lifts and LNKD goes to 106. It pulls back into the 104 area; that's when we weren't sure if SPY was going to get above resistance. Then the SPY got above that resistance level again. LNKD held at the breakout point as SPY broke above this resistance level and then LNKD all the way up to 108, which is the next technical level. This is where it failed before coming down to the 90s prior to the earnings release. The stock is going up, up, up, and there's the 107.50 change in character on the tape. You can even see that on the chart as it turns down on the chart. When that happens, you really want to be out.

Good traders are self-critical.

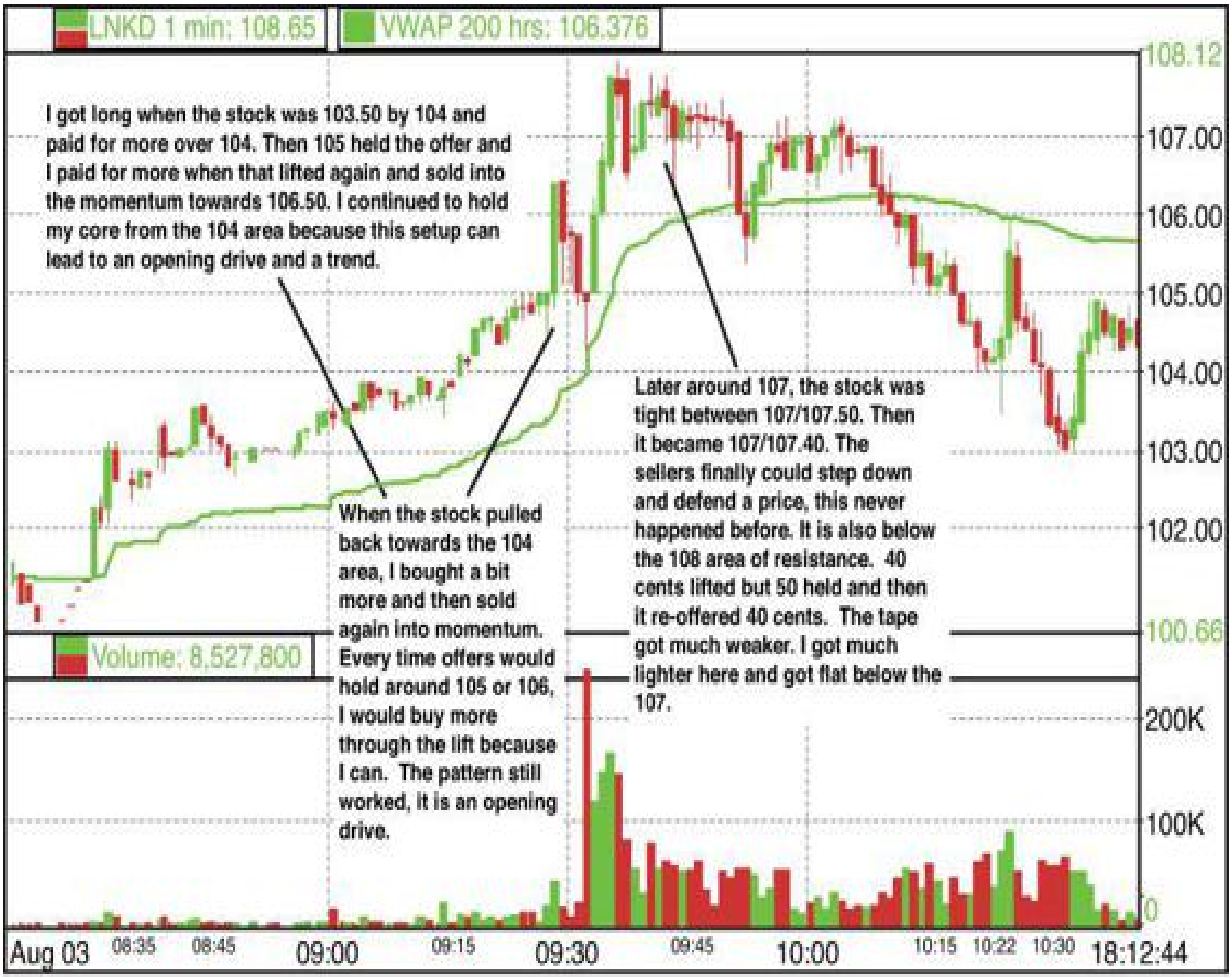


Figure 9.6

Iceman: Let's go over the things that I could have done better. I'm not that good at buying back at 104. When it explodes to 106, I'll make money, but when it comes back to 104, this is where I have trouble. Something that I have to work on is buying those pull-ins. That wasn't the same trade, but that is something I need to work on....

Great intraday technical setup to learn.

Bella: I think one of our better technical analysis trades is when something explodes from a resistance level, has a nice up move away from a resistance level, and then pulls back to that price again quickly. This is a good area to buy. It's a very strong and powerful technical analysis trade. It's one of Spencer's favorite technical trades. Does everyone understand that? So you might not be great at buying things that necessarily pull back, but you might want to make a distinction that when something was at resistance and it moved away from that resistance very strongly [and] then pulls back on light volume to that price, that's a very solid technical trade.

Iceman: Yeah, absolutely. The idea behind that is that the stock is very strong, and if you missed it, where are you most comfortably going to buy it? Where your risk/reward is best, and that's where the move started, so that's certainly a trade you can make.

Another thing I could have done was pay through 105 when I saw the pattern was working because my risk is very small and my reward is very big there. Questions?

SMB Trader: Once it finally opened and pulled back again and broke out, did it ever cross your mind that this is going up too fast? Do I need to take some off?

Lighten up into moves that are too steep.

Iceman: I did take some off along the way. I would add and take off. I had my core that I was holding from 103.50, 104. But whatever I paid through 105 I would sell into 106 or wherever it slowed. Then through 106 I would buy back whatever I sold through 105, so I wasn't just piling on for a mega rip once it turned around. I had my cash flow position, and I had my core position, and I would manage them accordingly.

Measure the moves when trading momo.

Bella: So if you're in a momentum trade and when the stock is going up, you sort of measure the way it's going up. Some people just do that with charts, but if you are actually watching the tape, you should develop a measurement in your head. **It's traveling a certain amount of distance; it's going up a certain amount of cents, in a certain amount of time.** You have an imprint in your brain to what that looks like. Then you actually see a time where it goes up a lot more, a lot quicker than that imprint in your brain. It's too steep compared to other moves; it's perfectly acceptable to take some off, if not get flat.

If you're really paying attention to the tape, you see the overextended move. There's a way it's going up and this patterns continues and then it goes up a lot higher, a lot faster than you have seen. It looks like what a blow-off top might look like such that there’s a risk now for you to be long. This price is not sustainable for the near term, or it could just reverse....

1. If the momo stock does not make as strong an up move, sell.

2. If the momo stock is too steep to the upside, sell.

Iceman: So it’s not like I held my entire position the whole time. I would buy, buy some more, and sell. I would buy back what I sold, sell, buy more, sell, buy more. And, yeah, I probably lost a couple of cents on the way by doing that on those momentum lots, but that’s the way you have to trade these setups because that’s the way you play defense.

Bella: Yeah, but you’re massaging the answer. Junior was just asking, in its purity, how do you sort of tell how to take a Momentum Trade off into a steep move? And your answer is, “Well, I’m doing both; I’m core trading it, and I’m momentum trading it.” His question is if he’s momentum trading it, how would he know whether it’s the top or how to take it off? So there is an answer to that, and it goes back to many years ago when I used to trade Internet stocks. And the way we learned to take things off. You would actually hear things on our desk like this: In a really good stock, you know when it’s done because you can see the difference. One of the most common expressions heard on our desk while we were momentum trading Internet stocks was—and I can still hear the guy behind me in my ear—“That’s no up move I ever saw before!” And then he used much more colorful words, which I can’t repeat. But he was watching the way stocks were going up, and he noticed that they weren’t going up the same way. They were not making as strong of an up move as previously. And then the other way to get out was that the move was so much steeper than we had seen before that there’s too much risk to hold it anymore. So those were some of the ways guys would get out.

Iceman: So your stock went up 20 cents, drops 5 cents, goes up 20 cents, drops 5 cents, goes up 30, 40 cents, and then it goes up 2 points, and then I’m out. Or you can offer some up to get down to a core on the rest.

SMB Trader: You kind of answered my question because I just started with 200 shares. I find that when I get out of my first 100 and take some risk off, I don’t want to overtrade to get back in. I don’t want to be giving away the profit that I’m making on the other 100 shares. Maybe like you said I have to lose a little, but I’d like to make a little more.

Iceman: Just because you took off 100 doesn't mean you have to try to force the other lot back on. You have to wait till the pattern resumes where you added in the first place, and that will give you an opportunity. Because what's the pattern? People try to sell, they lose, they try to sell again, and they lose. Once they start winning, that's a different pattern.

> *At first you are scared. Then you get used to the ride. Then you start having fun.*

Iceman: You guys have to try this, and it has to work for you a couple of times. Then you'll be into it. It's scary a little bit when you first start making these trades, but you have to try it. Live on the wild side. Come in one day where you're like "I just don't care" and then try it. And if it works, the next time you'll care, and you'll know it works. You have to see the potential of these stocks, and if you lose, don't say that it's too much and that you can't handle it. You *can* handle it.

> *Trading is a game of math. If the risk/reward is favorable, take the trade even if your downside is more than you usually allow.*

Bella: Well, you have more guts than the ordinary trader to be able to deal with the rips that are inevitably going to come from trading this strategy.

Iceman: Yeah, but if you think about it mathematically, it's just risk/reward. It's just like any other trade. It's not like you're being reckless by taking it. The difference is that you have to not be reckless by taking it. You can't just be, like, forcing the setup when it's not there because these stocks are thin on the open, less liquid, and if you're wrong, you have to get out. And you have to get out fast, or you will get really hurt. You must have a plan. You're very reactive when trading these setups but that's because you've visualized the way it ought to move. If you see it, you're going to take the trade, but you have to just react because you'll miss it, and then your risk becomes higher than it really is.

> *When you are wrong, exit fast.*

Bella: That's good. That's one of the improvements from last month. Some of the guys were trading the high beta stocks on the open more so and more profitably than previously. You guys showed some more guts, like Iceman.

Iceman: Yeah, Priceline today offered awesome opportunity on the open. I caught a quick 4 points on that one.

Bella: Who’s better than you?

(Traders laugh and leave the training room.)

Postscript

Iceman is one of the most valuable trades on our desk. He runs our College Training Program and our Russian Mentoring Program. He keeps our traders loose, enjoying each trading session. He recognizes that trading and the life of being young in NYC is a privilege we should make the most of. When he sees a setup he just goes for it! He teaches all of us the importance of having fun, taking necessary controlled risk, and adding value to the others around us.

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10. GMan: Trading Is *Not* Easy

GMan is one of the best intraday traders on the Street. I trained him. He became a CPT in the style I taught him. But here's what's fascinating: Although he still incorporates everything important that I taught him, he doesn't trade the way I trained him anymore, which is to say that even though he's retained the crucial elements that all traders need to master, he has found his own completely different style—and what a style it is!

What lessons can we learn from GMan? Well, for starters, trading isn't easy. Even star traders have to adapt and find new ways to consistently pull money from the markets. If you want to win, you better be prepared to fight. Most important, in this chapter we focus on how great coaching turned this recognized trader into the best trader GMan could be.

First, a little more about GMan. If we stepped onto the set of a Colombian soap opera, we could easily find GMan there. The hair of a weatherman, matinee-idol looks, that big smile. But when you watch him trade most days, he is a bundle of stress. GMan attacks trading more with the response system of a professional wrestler (Columbian Chopmaster could be his wrestling stage name) than the engineer he studied to be. We have had to get him outside coaching to work on that.

GMan lives in a world of extremes—between seeking competition and fun. Is GMan competitive? Hah. He would bite the head off a market maker and step all over the remains if that is what it took. I have actually heard him say something similar on our trading desk on numerous occasions.

"Bella if I ever run into the dumb-ass market maker in HAS it's not going to be pretty."

He will fight his market competitors until he wins. And if he loses, he wears around a look of pained misery. I stay away from him on these days. Not even a "Hey, GMan, what's up?" He starts so chill in the a.m., but then can turn into one wound too tight.

GMan's trader speak expresses his competitiveness. Here you go:

1. The boat is loaded. (He is very long a position.)

2. The boat is tilted. (This position better work.)

3. That is a piker trade. (Do not make that trade again.)

4. Get out of there you cockroach. (Stop selling the stock.)

GMan's life is one continual competition. Brian Shannon coaxed GMan into a hike up Mount Whitney, elevation 14,505 feet. To prepare, GMan didn't just go for a few jogs and maybe cut back on the Brooklyn Lagers like most before the big climb. He strapped on a backpack of 30 pounds and walked up and down the 34 flights of stairs at his apartment building for 90 minutes, 5 days a week, sometimes coaxing an SMB trader like Prep to partake.

Previously, when GMan was determined to get in better shape, he didn't go to the gym or hit the weights or maybe take some spin classes for a few months. He did that omnipresent infomercial Insanity Workout, burning about 1,000 calories a workout. Here's another one: GMan took one of our traders to go play racquetball. The guy was a former ranked racquetball player from one of those countries where they really care about the sport. They didn't just go and play for an hour and grab a few Michelob Ultras. It was a two-hour, winner-take-all session with premium scotches paid by the loser. Umm, I didn't see GMan on the desk that next day.

Now, let's be clear: GMan isn't always 100 percent fight. If there's fun or the possibility of fun and any chance for GMan to get to it, he does. Whether that means a 2.5-hour, post-10 p.m. car service to Atlantic City or a cross-country flight out West to catch a college football game with a buddy, GMan finds a way. I have sitting on my trading desk a bottle of Cakebread Cellars Sauvignon Blanc from GMan's last impulsive weekend trip to Napa Valley. He, without fail, leads the Street in e-mails from the airport about last-minute flights to Vegas.

GMan's trading career has not been a clean ascending uptrend to outsized profits. Yes, there was GMan being recognized as a Top Two Trader under 30, as reported by Yahoo! Finance. Yes, he was named a partner at SMB. But his trading journey, now over five years, is one of perseverance, paid outside coaching, and concerted effort to step outside of his comfort zone. As Ray Dalio has said, "When we encounter pain, we are at an important juncture in our decision-making process." The ride to his stature takes work (better called rehearsal ethic), great coaching, improvement of your methodology (trading system), struggle, building from your strengths, self-doubt, firm support, high character, and the inner will of a trading warrior.

Let's study GMan to find out how he re-learned to outperform as a trader. You are going to be surprised at how difficult it all was and how adaptive of his trading system and psychology GMan had to be.

Traders Need Great Coaching

I stood in a packed room in downtown Singapore doing a preview with Phillip Capital for the U.S. equities training program I built for their retail traders. It is custom in Singapore to do a free 90-minute preview, giving a taste of what students could learn before they make a commitment. Fighting punishing jet lag that made me feel like I had been drugged, I stressed the importance of coaching.

"I have a coach. GMan, our head trader, has a coach. In fact, he has recently, after five plus years of trading, made his most progress because we hired a highly paid elite coach to work with him. Our firm works with three coaches presently that help our traders. Moreover, every trader is assigned a mentor. In fact, the trader is paired with the mentor most likely to help them. Why? There is little evidence of elite performers reaching their potential without great coaching. Matthew Syed discusses this in his great book *Bounce*."

Everyone in the room stared at me in disbelief. You could almost hear them thinking. He has a coach? GMan has a *coach?* I thought they were successful traders. Why would a successful trader need a coach?

Let's study some elite performers because traders are, at their most basic, just elite performers, and learn about their coaching so that we can put to rest any feeblemindedness that traders don't need continuous great coaching. I nominate a look at my favorite athlete, Phil Mickelson, perhaps the second-best golfer in the world. He makes more than $40 million a year. He is so rich that he just bid for a stake in the San Diego Padres. He has won multiple majors. He certainly doesn't need a coach, right? No. He employs a team of coaches who help make him better.

Here is a quick summary of the instructors Mickelson employs that help him improve each facet of his game. He employs a putting mentor, Dave Stockton. He hired a short game tutor, Dave Pelz. He has one teacher who works on his long swing, Butch Harmon (famous for building Tiger Woods's first swing). He has a caddie, Bones, whom he consults before every shot, like pilot and co-pilot discussing the best flight path. He pays for a physical trainer, Sean Cochran, who helped him lose 20 pounds. Mickelson's personal regimen consisted of increasing flexibility and power, eating five smaller meals a day, doing aerobic training, and carrying his own golf bag. He works with a mental counselor, Julie Elion, whom he credits with helping him overcome bad weather and rough conditions to finish T2 at the British Open. Mickelson even has been receiving advice from 2011 PGA Championship winner Keegan Bradley on a new putting technique with a belly putter. The guy has a lot of coaches. If an elite performer like Mickelson has so many coaches, then why don't you as a trader?

It's not just Mickelson who employs multiple coaches. "Many players, like Mickelson, now have more than one coach," said Mike Bender, the longtime coach for the 2007 Masters champion, Zach Johnson. Bender likened the support crew around Johnson to something from NASCAR. Bender called himself the "mechanics guy," but noted that Johnson had a mental coach, a putting coach, a fitness coach, and a caddie who has significant say, too.

Top hedge funds and bank traders globally employ personal coaches for their top traders. I have had numerous conversations throughout the years with seven-figure traders whose trading had gone off the tracks and needed a coach to get them back online. I have seen the positive impact coaches have had on my traders even after I trained them. The best practice I found was at multiple hedge funds that offered a list of coaches, specializing in different niches, that any trader can work with. When I visited a top U.S. hedge fund in Greenwich, Connecticut, I couldn't believe there was a gym at the facility with personal trainers available. This place was so much about performance that even in their bathroom hung performance tips: a posted op-ed on the inaccurate calorie listings at fast food joints was right there for reading above a urinal. But, of course, there was. Health and physical condition improve personal performance, so those resources were provided. Elite performers need great coaches—and if you want to become an elite trader, well, you need a coach, too.

I remember the e-mail coming in. I remember where I was. I remember that feeling that overcame me. The worry. The concern. That physical reaction that told me we had to act. In *One Good Trade,* I wrote about GMan trying to quit eight months into his trading career. I didn't let him. The rest became history.

Now I write in this book that GMan tried to quit again maybe two years ago. There were family responsibilities back home. His workload for our education arm, SMBU, was filling his off-trading hours. He wasn't trading very well. He was burnt out. He wrote a very long e-mail explaining a planned move out West and why. A proper and emergency response consumed every minute of my time for the next two weeks. I sequestered myself for hours at a time in my personal war room, my office. I was in full-blown crisis mode.

What was going on here? Was this just a bad moment at a bad time? Was he truly unhappy and ready to move on? What makes GMan great, his competitiveness, also breeds emotional higher highs and lower lows when compared to most other people. Was this just a lower low that I needed to help GMan manage?

Solution-Focused Therapy

Having read most of Dr. Steenbarger's blogs and books and having worked with him, I am schooled in his philosophy of solution-focused therapy. In Dr. Steenbarger's words,

> Solution-focused therapy avoids the pitfalls noted above by redefining the aims of the helping process. When traders seek psychological advice, they typically frame their request as, "Can you help me get rid of X?," where X is a problem pattern in trading. Their aim is to eradicate a conflict, habit, or mood state, which they have interpreted as *their problem*. Solution-focused work does not seek to eliminate such negatives. Rather, it identifies people's goals—the positives they wish to attain—*and the ways in which they are already achieving these*, even in limited fashion. The idea is not to do less of problem X, but to do more of solution Y.

Educated in this mindset, I thought: What could we do to help GMan? I made a list:

1. Stop fading! GMan was fading too much, which caused him too much stress while trading. We could work with his trading coach to trade more of his best setups.

2. Lighten his workload. He had too much on his plate for SMBU.

3. Go home, GMan! He needed to go spend some time with his family.

4. Play! GMan needed an outdoors outlet in NYC. Remember happiness precedes success.

5. SMB, get better. Our desk needed to trade better to add more value to his trading.

6. Emotional checkup. GMan still required help with the higher highs and lower lows as a trader. A plan for improvement with his coach should be discussed.

It Takes a Village

GMan needed help. Even as talented a trader as he is, this is a game that requires support for many of the best. The tricky thing here for a prop desk partner is that you have to trust the coach. Partners can get used to being in control and making things better themselves. The coach cannot tell you what he is working on with GMan or what GMan and coach are dicussing. That is a breach of privacy between coach and player. But you must communicate with the coach about your ideas for improvement (you work with the trader daily and know him best after all) and get those thoughts placed in front of the trader in order for him to recognize them.

So a dance began. Spencer and I would send issues for GMan's trading coach to work on, along with examples of any self-destructive trading. The coach would place these issues on which to work and others in front of GMan, who had no idea we were involved in his coach therapy. GMan would come with his own set of fixes, and the coach would measure those against the feedback he was getting from us. We all had one goal: to help GMan become his best trader.

There were many "Why is GMan still fading?" e-mails that we sent to his coach:

> GMan got crushed today on the open fading the market, SPT and C. He has been trading well. But this is another example of him fading the market against his self-interest. He should be up 3K right now but is down over 4K. These are huge swings that materially affect his P&L.

There were many "GMan is doing better, no?" e-mails back from his coach:

> It appears to me that GMan has settled into a steady, productive trading pattern with decreased emotional volatility. Is that an accurate take on things?

After one such e-mail that elicited a “WTF, doc?” Spencer and I talked about a response. Spencer pointed to GMan’s continual cursing and banging, which basically meant I had to calm down the almost-always-calm Spencer for the price of employing GMan’s coach. And then Spencer would acknowledge improvement in certain areas of GMan’s trading in a return e-mail:

> His fading has decreased. But still seeing the usual banging/cursing on the desk. Not sure if that is just an emotional release and not harmful to his trading.

The Crisis Worsens

Right after GMan had tried to quit the desk again, he had a horrible day. Steve was concerned about how GMan would respond:

> Not sure what is gonna happen with GMan after today. Finished down around 7K with tickets. There was a big cluster**** today with locates, as ABN sent the wrong file to LS, so everything was hard to borrow. Market cracked, but said he couldn’t get short enough stuff. Asked him why he didn’t use options and said the account was locked out....
>
> I responded:
>
> Spend some time talking with him. I am sure he is down. Also talk to the desk about being in the right stocks. All you can do is teach them.

Then the next day with all of us on full alert, GMan rebounded. His coach was following GMan’s progress:

> Sounds like he may be recovering (emotionally and $$) a bit today?

Steve responded:

> He bounced back so far. Up 3K. I spoke to the desk before the open on working with each other more. It was a good talk and then something I said happened exactly as I discussed so that was nice.

I followed up with a short e-mail of encouragement to GMan. (Remember: praise the resilience, not the result.)

> Good turnaround today! Love seeing that. Enjoy the weekend.

GMan hung in there and started to make progress. Let's see how.

How GMan Improved His Trading Methodology

I asked GMan to provide his take on his coaching experience. Here it is:

> **1.** First thing was identifying what I needed/wanted to change to improve my performance. We came up with five things: Eliminating the one big rip a month, eliminating small unnecessary losses forcing my way into stocks that were not ready, getting myself frustrated when things wouldn't trade cleanly or if I was overtrading, eliminating all possible stress in positions not ready, and lastly, building on my strengths to increase the performance of the winners.
>
> **2.** To eliminate the one big rip a month, we worked at identifying triggers that led me to make poor decisions. This one took a ton of work and has made a pretty big difference.
>
> **3.** A lot of the conversations led me to break down all the plays in my PlayBook to analyze which ones were the most profitable with the least amount of stress. Those with the most amount of stress were eliminated altogether from my day-trading account.
>
> **4.** Figured out that those that provide the most stress could be played on a different time frame with different risk settings and trade rules and started trading those via options. That has helped a ton with my numbers.
>
> **5.** Curbing overtrading and reducing all the little losses was a challenge, and these adjustments led me to concentrate in developing the Pullback Trade with a set of rules that worked for my style. It allows me to use the skills I have developed but, more importantly, to trade while I have the momentum on my side so there is no stress in those positions and trade them with conviction.
>
> **6.** While talking about my strengths, I realized that a lot of the overtrading triggered feelings of uncertainty and lack of conviction in my trading. Now I'm much more comfortable just laying out

huge risk, money-wise, but allowing myself to let a stock work its way to my targets.

7. Continuously work on stepping outside my comfort zone size-wise gradually to continue to grow, but doing so in a progressive manner to avoid growing too fast without a solid base for handling the swings in P&L, etc.

GMan and I talked about his assessment, and I asked him if he would expand on his answer. I thirsted for more. Working with a high-level problem at a crucial time in his development is the ultimate learning experience for me (and now you).

Re: Big Rip. I realized one way to improve my numbers was to eliminate the one/two big rips a month. They accounted to about 35–40 percent reduction of monthly P&L. There was a pattern as to how I would put myself in a big hole:

1. Fading the market and trading with a bias.

2. Trading on tilt after missing a play. I spent a ton of time building a position but getting worn out if the play wasn't clean.

3 Going on tilt trying to buy a pullback when the pullback was too extreme.

4. Going on tilt was the easiest thing to fix as I just developed a way to look at the market using hourly charts that made sense to me. Fading market moves has just not been part of my PlayBook since.

5. Still a work in progress, but I have found a way to keep myself on these ideas using the swing account and the options account.

6. This one [buying a pullback] was a trade I really liked and thus took some serious work looking into how to develop a strategy to help me trade those pullbacks.

The process was more or less the following:

1. I went back and studied two years of data looking at Pullback Trades. Serious grunt work that sucked big time.

2. Obviously without the tape for each play, I needed a way to look at those charts and find something to work.

3. After many weekends of looking at the 300+ charts, I started to find the similarities and patterns. The Pullback Trade eventually came from that.

Most might be surprised at how little GMan talked about the work that was done to improve his weaknesses before reading this chapter. It was mostly his coach taking GMan as he was and building from his strengths and trying to minimize the effect his weaknesses had on his trading. GMan continued:

> Well, what was causing anxiety and getting me on tilt was related to plays in which I would start building a position based on the most recent history of the stock (levels on charts, tape, etc.) and then always puking the position, often giving back a ton of money of what I'd already made or just digging myself in a hole. The anxiety would come when the stock would eventually turn its momentum and start doing what I thought it would do.
>
> So, yes, I had to work to identify what was causing stress in my trading, and we thought there would be two approaches to the issue: 1. Working mentally to handle those situations 2. Adjusting the PlayBook so that I could wait until the momentum was back in my favor at the expense of worse prices: lower size but often way less risk and no anxiety. That's how the rules of the Pullback Trade came about.

GMan's Pullback Trade from his PlayBook is presented in detail later in this chapter.

Remember How Tough Trading Is

You may have read the preceding sections and judged GMan as a lesser trader because of his two-times threat to quit and his trading struggles. If so, we need to work on resetting your mindset. Trading is a tough game. A good baseball manager once said that the most important thing to remember when coaching his players was how hard it was to play the game. Even good traders with a track record wake up one day and cannot make another dime. Even the best traders struggle and doubt and need to make improvements to adjust to ever-changing markets. There is a fine line, even for the successful trader, from underperforming to reaching new levels of success.

There is also confusion among traders about the value coaching and mentoring can add to their game. All traders learn mostly from themselves. They review their work, they think about their trading, and they figure out things for themselves. But do not mistakenly conclude from this that a coach and mentor cannot make you better. Yes, you do most of the work to make yourself better. But it's also a fact, borne from what I've experienced and witnessed over the years, that a coach and mentor can help you reach levels of greatness that you could never reach alone.

* * *

I received the following e-mail that encapsulates just how truly difficult this game of trading is when you don't have any direction or guidance. This e-mail is an incredibly insightful sharing of just how brutal this game of trading can be. When I received the e-mail and read it, I just sat at my desk thinking...*Wow*!

Afterward, let's try an exercise together and look at some solutions that could have changed this trader's fate. Are you ready? This is a root canal of trader misery.

> I just incurred my last (big) loss today. Here is my situation:
>
> **1.** Over eight years I have lost, approximately, hmm... $40,000. And it might be more, depending on how much I can eventually sell my worthless penny stocks for. Enough to give my daughter's education a boost. Enough to have money to live on for a few months. Enough to buy a nice car, cash. Enough to pay for the best trader education out there.
>
> **2.** I have shown over eight full years that I have zero skill as a trader. More than that, I have shown an absolutely uncanny ability to lose money in all time frames, in all situations, all instruments. Longer term, swing trading, day trading, long, short, trend, fade. Lose, lose, lose. My estimate is that more than 70 percent of my trades have been losers, maybe more than 80 percent (I didn't always keep statistics), and my dollar loss per losing trade far, FAR overshadows my profit per winning trade. My average loss might be five times the size of my average win. I am possibly one of the worst traders ever, just statistically. The numbers are what they are. But still, there's always tomorrow! I know I can turn it around,

bull****! It’s just amazing how I can fool myself day after day and now year after year, to get up the next day with an optimistic, go-get-‘em-tiger attitude.

Well, no more of that. I can’t let myself lose any more. It’s over. This was a dream for so long, to be able to sit in my house, right here at my computer, and make money. To not be dependent on anyone, not have to answer to anyone. I wanted it so very badly. This hurts like hell. I’ve spent thousands of hours reading, studying, looking at charts, watching webinars. I have over 50 books on trading and investing, and I’ve read all but about 3 of them. (That Neely book on Elliott Wave Theory was tough.)

Now I need to get a second job.

3. Most of my losses have come because I simply can’t implement what I think is a decent strategy. Here’s why:

a. I’m utterly incapable of getting out of losing trades. This has cost me 80 percent of the money I’ve lost. I’m still in about eight penny stocks in which I’m down 90 percent or more. That says something! I’ve called myself an ******* 1,000 times for not getting out of losers immediately, and every day I say I’m gonna do it but I NEVER DO. Just today I did it several times! I mean, for **** sake!! I was screaming at myself just yesterday for this!

Even on the rare occasions when the trade eventually turns my way, I lose because if I would have gotten out of my original losing trade for a small loss, I could have made two winning trades as the market moved away from and then back toward that original position. And, so often I’m so grateful to be breaking even that I get out right at that break-even point; then I watch the market continue on in the desired direction without me.

b. At the same time, I’m just as incapable of letting my winners run. SO MANY TIMES I’ve gotten out with a

$40 or $50 winner, only to see the trade keep going and going in my direction to where I could have had a $500 winner. You can't do a. or b. and be profitable, let alone both. It's just not possible.

c. This is probably a corollary of b., but I have a rule that says if I get into a trade and nothing happens after *x* amount of time, if I have just a small gain or loss, my premise is wrong (I made the trade because I thought it would go my way, right?) and I should get out. I think I might have done this correctly a couple of times, total, over hundreds of trades. Instead I sit waiting to get killed, operating on hope. Just one more minute! Thirty more seconds! ****!

d. This goes along with a. and b. as a classic blunder. When I'm losing I will sometimes ADD to the trade, rather than getting out. Not every time, but not all that infrequently, either. That is (and I can prove it), the very best way OF ALL to become poor.

e. I trade angry, and when I do that I forget the rules and I go big. It hurts to write this one, just like my final $700 loss hurt this afternoon.

f. I trade way too ****ing often! For God's sake! Thirty, forty contracts a day? Are you kidding me? I should have traded maybe five round trips of one contract each per day.

g. Related to e. above, I don't wait for good, high probability setups. I outline what they are in my trading strategy, but I just get caught up in the moment and only use some of the entry criteria.

h. I trade too ****ing big! I should have had a strict rule to trade just a single contract to this point, but once or twice I've traded as many as four, and a couple times a week I trade three. I never mean to, I just let the demons get a hold of me, and suddenly I look up and I'm in two or three contracts. Nuts!

i. I can't handle the heat. I act like a maniac, screaming at the top of my lungs. I get sullen and petulant. I get down on myself. So, when it comes to pulling the trigger on that setup that failed the last two times, I chicken out, and THAT'S when it would have made me money.

j. I need to be right. Deep down, I'd guess my ego would rather be right than profitable, and I often let it drive. Another of the deadly trader sins. I literally have all of them.

k. My execution is at times sloppy. I've bought more when I meant to sell, shorted when I meant to buy, I had my order entry platform set to limit order when I wanted to do a market order, didn't buy the right number of shares, and on and on. I'm strictly in the minor leagues in terms of performance and execution. This, after reading two of Dr. Steenbarger's books and reading tens of thousands of pages of blog posts, studies, strategies, and more.

l. I continue to trade between 11:30 a.m. and 1:30 p.m. (ET), when I know that's the hardest time for me. I usually win in the morning but can't get my bearings when volatility drops off (I keep the statistics).

m. I trade tired. So tired. I work evenings, getting to bed sometimes at 5 a.m. or later eastern time; then I'm up at 9:25 a.m. Not even four and a half hours. I take a nap generally between noon and 2 p.m., but it's still not enough and not the same as sleeping straight through. Plus, I generally stumble to my computer 30 seconds before the bell. I prepared the night before, but still, I really need more time to check out the landscape in the morning. But, I need to sleep more.

So, my intense desire to trade has put me in a situation where I can no longer trade. Good-bye, trading. You taught me quite a lot about myself, and much of that was not so good.

After reading this e-mail, you might think there is no way this guy could have been a profitable trader. Perhaps. But what if we applied some good coaching and mentoring to this allegedly hopeless trader? Look, I get despondent e-mails from traders just like this gentlemen, so I know many of you reading this have had thoughts similar to this former trader. Let's revisit his e-mail, but this time I will plug in some commentary, as if I were mentoring him directly. Consider how much different his mindset (career?) might have been with each typical trading flaw.

Issue 1

Wouldn't it have been better for you to invest in quality training that would have given you a foundation to build from instead of ripping up 40K without direction? Penny stocks? Those are very dangerous, illiquid, often manipulated stocks not for the new trader. What would your career look like today if you had started with a solid educational base? If you had invested in this education, every month, every day, every trade would have been different. At worst a good training program would have kicked you on to a new venture after eight months of learning but clear inability to execute.

Issue 2

You have a resilient personality. Great. This is a wonderful trait for a trader to have, and it could have served you very well with a proper trading base. But ask yourself: What if you had kept statistics consistently? What if you had found a time frame that was best for you and with a type of setup in which you were profitable? If you had, you would have seen that time frame as a way to build on profitable setups while excluding the unprofitable losers.

You clearly have a passion for trading. That is rare, even among many who try to trade. We can do so much with this.

Issue 3a

In my firm, we have a simple rule that all traders must adhere to: If you cannot get out of losing trades, you must trade on the demo until you can. What would your live start have looked like if you had worked on this skill before risking real money?

Issue 3b

Develop a PlayBook. Understand your A+ setups. Develop Reasons2Sell for these best setups. Work on holding your trades until these reasons appear. Judge these trades, win or loss, not by how much money you made but by how you followed your plan of not selling until there was a Reason2Sell.

Issue 3c

I love that you have identified a time stop as a Reason2Exit. This is excellent. Come up with more specific criteria for your time stops. For example, if a stock does not move in 30 minutes for XYZ trade, I will exit.

Issue 3d

Never double down. Paul Tudor Jones never doubles down. If that is good enough for him, it ought to be for you. After all, he trades billions more in products than you. If you are caught doubling down on our desk, our risk manager will put you on demo for three days.

Issue 3e

We all get angry at times. There is nothing wrong with getting upset. Try to recognize when you are irate as a trader. When you recognize you are on tilt, get up and go for a ten-minute walk. Do not return until you have changed your brain chemistry from mad to neutral.

Issue 3f

You should not trade more than five contracts a day until you are profitable trading four contracts a day. You do not increase your trading until you are profitable at a lesser level.

Issue 3g

I would ask that you develop a plan for yourself to rid your trading of the setups that were too stressful and unprofitable (like GMan did with his coach).

Issue 3h

If you violate your sizing rules again, you must be disciplined. If you were to do this at our firm, you would be placed on demo for at least three days. A risk manager would watch you when you traded live. If you did it again, you would be placed on the demo immediately.

It appears that you, like many other traders, would benefit from someone observing your trading so you do not act against your self-interest. This is why pro teams have coaches. When a player is hurting the team, he is pulled from the game. You may need a coach to pull you from the game when you are hurting your team (in this case, your trading account).

Issue 3i

Well, you're not making money. You're not sleeping. I would act that way too. That seems very rational to me. What is not rational is you are not taking the steps necessary to provide more hope.

Issue 3j

You're not the first trader with a need to be right. I can spot these guys on the first day of training, and I have trained bushels of them. It is terrific work that you have identified this as an issue. It would be helpful for you to work with a trading psychologist with some of that $40K to learn why being right is important to you. I spent 2k on a bunch of sessions with a noted psychology coach for one of my traders and turned an unprofitable trader into a profitable one in three months. The first step is to recognize and understand why you are the way you are. A few sessions with a trading psychologist would be invaluable.

Issue 3k

In our training program, The SMB Foundation, we have our traders practice entering orders for ten minutes a day, every day until they are fast. You are an electronic trader. You cannot be slow and error prone. It is like being a concert pianist and thinking it's okay to mess up during a live performance. It's not. Practice entering your orders.

Issue 3l

Set a stop-loss of 30 percent of your intraday loss limit for any time period in which you underperform. We have been doing this on the open consistently and have seen an improvement in firm P&L.

Issue 3m

So much new research shows that college athletes do better with more sleep. Nine hours is better than eight, and eight hours is better than seven. You spent four years never learning how well you could perform because you were not in an optimal cognitive state. Spencer would have simply told you to get a good night's rest each night.

From my seat, I see a very hard-working, passionate, and resilient trader, with some good screen time under his belt. But I also see someone who has eight years of trading data that is irrelevant because he never obtained proper training, didn't have good coaching and mentoring, and could have performed much better with some tweaks.

If this trader were on my desk, I would cool him down. He is burning too hot. TO has sent me similar e-mails without the definitive quitting part. One day as I was leaving the office to grab a fruit salad (for some reason they have the world's best fruit salad on the Street), I overheard two SMB traders doubting their ability and chances of success because of a four-day streak of underperformance. I immediately changed my fructose-overload plans and interjected balance to the negatively charged conversation. One of our better young traders, MQP, sometimes needs a few moments of chilling as I listen to her conclude her trading is the worst when in fact she is just going through predictable growing pains.

I am not guaranteeing that a good coach and mentor could have saved this trader's career. Most traders fail. But you can see quickly there was so much help to give that could have turned around his trader experience. Remember Prep and all he needed to correct? Solutions exist for almost all of your trading issues. Unfortunately, we will never know with this trader. But I can say this: Never be in that position yourself.

Argghh: Insufficient Trader Training

The following e-mail from a trader fired me up (in the bad way). Consider it a sad anecdote of a failed trader. It is such a depressing commentary on the substandard training at trading firms and from trading educators. So many consider themselves to be failed pro traders who ought not to. Instead, the real issue is that they never were professional traders, which means—I can't say this enough—they were traders who did not receive proper training and ongoing coaching. They are part of a trader graveyard reared by the churn-and-burn shops and insufficient trader training.

> Hey Mike,
>
> We talked a while ago about how your book *One Good Trade* has helped me and my five friends on the trading desk at our prop trading firm. I have been trading for about 12 months total and about 6 months live. I have found that your website blogs and tweets during the day have really helped me excel my trading curve. My prop trading firm is more of a "do it yourself" type of firm, and I feel in trading to succeed you need a mentor to guide you through all the ups and downs of the market. Therefore, I came to realize that you, your blog, and SMB Capital have been more of a mentor than my firm in general. I don't think that is right at all. If I want to be successful, I have to find the place, environment, and people that are going to help me achieve that. I would be grateful if you took a look at my attached resume, because I have conviction that your firm has the resources I need to become a successful intraday trader.

I responded:

> Please send me your trading runs for the past four months. Thanks for the interest.

He got back to me. His results? Not good: 1K down days, almost no positive days, and never even a hint of progress in four months' worth of data.

I was reading *Abnormal Returns: Winning Strategies from the Frontlines of the Investment Blogosphere,* in which Tadas Viskanta tackles the issue of the failure rate of a professional trader. Barry Ritholtz, the number one finance blogger in the United States with his blog called The Big Picture and author of the compelling book *Bailout Nation,* compared the difficulty of becoming a professional trader with that of a professional athlete, clarifying that it was easier to be a pro trader but still very challenging. The trader just described should not be considered in the failure statistics. Let me explain why:

> **1.** He was not a professional trader. He was a guy who sat in front of a computer at an arcade offering a rental service. "You rent my

space and my computers for commissions on your trades." It is like a bunch of buddies getting together and renting the basketball floor at Madison Square Garden for a few hours of pick-up ball. That does not make them professional basketball players.

2. How exactly do you lose $1,000 in a trading day when you have not shown an ability to make money? That is irresponsible, unprofessional, and unacceptable. Who the hell was allowing this newbie to rip it up like this? Given his results, this trader's intraday loss limit should have never risen above $150.

3. What was gained from this experience? The gentleman still does not know how to trade. He learned almost nothing from this experience. This is sad.

4. I have read most of the overly negative trading forums complain that training is not worth the cost. Stick this anecdote in those forum posts, please. Forums' poor advice contributed to the useless trading start of this newbie. It's obvious that this person really wanted to be a trader. So what happened? He wasted a year and well over $25,000 failing at his passion while having no chance to succeed.

> There is too much data in the marketplace for a newbie to know where to start without guidance. As I have written before, to become great at anything requires coaching. Don't forget: Phil Mickelson has a team of coaches for his golf game. So in this most challenging market, you have almost no chance without a wonderful support system helping you improve every day.

5. There will be traders who are trained well but still fail. There will, in fact, be a lot. Not everyone can do it. Just like millions play golf, pay for lessons, and never make the PGA tour. Just like hundreds of millions grow up playing soccer and never play for Manchester United.

> But if trading is your passion, why not give yourself the best chance to succeed? Why not really learn how to trade? Why not learn the work you must do daily to improve? Why not learn how good you can be as a trader? Why not surround yourself with other pro traders who can offer mentorship? Do

> you really want to be like this newbie? And if you give your passion your best effort, are trained well, and fail, well, then, that was still an experience worth having.

Some use the objection that they do not have the money for great coaching or mentoring. Unfortunately, as you will see, the market *always* requires tuition.

There Is Always a Market Tuition

Here are two common refrains that I hear repeated from aspiring traders: “I don’t have the money for a good coach” and “good coaching is not worth the money.”

It can cost $120,000 to go to law school. It can cost $100,000 to get an MBA. The best undergraduate degrees may run you even more. Private school on the Upper West Side can run you 40K a year, grades 1–12. There are many different ways to start your trading career. You can go it alone, you can go with a firm that offers quality support, or you can join an arcade that offers the cheapest of the cheap commissions with zero support. Regardless of which you choose, a truth remains: The market will always require tuition.

I have had the pleasure of getting to know Michael Martin over the past few years. Hands down, he is one of my favorite trading educators on the Street. And it is so entertaining when he shares his stories about the other great traders he knows. He is a Wikipedia of trading anecdotes. I will share a line from him that sticks in my head, but first a little more background.

Michael Martin in one off-the-cuff remark to me at *The Other Side of Wall Street* book party for Todd Harrison of Minyanville obliterated this thinking. Michael said, “The market requires tuition from everyone.” Michael, author of *The Inner Voice of Trading*, lost 25 percent of his capital when he started trading on his own, even with guidance from The Trading Tribe, founded by trading legend Ed Seykota. Howard Lindzon, who has taught me more about entrepreneurship by just reading his blog and following his tweets than anyone else on the Web, talks openly about the bumps and bruises every new trader must endure even if he’s receiving superior mentoring (see *The StockTwits Edge*).

I started at a firm that did not offer the trading education that technology, social media, and the explosion of trader education now allows. This set back my learning curve. I did not “pay for training,” but I certainly paid my tuition to the market by struggling for too long to make money and an overly generous split of my trading profits to my trading firm.

I get too many e-mails from those who try to start trading alone, who have needlessly ripped up too much money, and worse yet, have learned very little in eight months of tuition payments/trading losses to the market. You can catch me on Stone Street having lunch with such a person periodically. I also get an upsetting number of e-mails from traders at firms who did not pay for tuition, received insufficient training, and now are looking for mentorship. Sometimes I get the impression that I am teaching some traders at other firms more than their firms, just with a few e-mails, our blog posts, and GChats. (I respond to every e-mail sent to me seeking trading guidance.)

It is the right decision for some to try to learn on their own. Some learn only on their own, some do not have access to quality education, and some are not the formal education type. But if this is your choice, understand that you will still pay tuition to the market. Your trading losses almost certainly will be larger than if you received guidance. And if you start on your own and even do things the right way, you will pay your tuition by taking much longer to become consistently profitable. Further, you will not learn as much or be your best trader.

As a partner, it is my obligation to push myself every day to learn more about the markets. Listening to other traders helps me grow. Befriending other traders makes me more valuable to the trading community and other traders. It is an uncomfortable test of stamina to fly across the world to Asia, but I learn. Adding color to this grind, I did a TV interview on the future of trading and HFTs when I first landed in Asia. I was sent the video. I watched it. I have no recollection of ever doing that interview. I have no idea how any of that happened since the first three days in Asia felt like some sleep-deprivation torture tactic by our partners. It can be lonely to be away from my wife for a few weeks in a faraway land. You know they do not have ESPN or NESN or FOX Sports that plays American sports or YES in these places? But consider the opportunities like sitting at a private dinner overlooking Singapore enjoying a traditional and delicious eight-course Chinese dinner with Jim Rogers discussing the world markets. We now exchange regular e-mails in which I always learn more than I give. That makes me more valuable to my traders.

I work at sending out e-mails to those I don't know. Seth Freudberg kids, "Bella's Rolodex is endless with Wall Street contacts." I work at learning different ways to look at the markets from other market participants. I work at setting up one-on-one lunches to consume trading knowledge. When I am asked to travel to give a presentation on trading, I pack my day with meetings with other traders in the city I am visiting. For my last two-day visit to Chicago I met with 16 separate people. Check my Twitter feed when I travel.

Lessons from Singapore

During my latest teaching assignment in Singapore, I learned an important lesson. I was hungry and it was lunch time so I packed up my iPad and laptop, jammed them into my North Face backpack, and headed for the food court at the Raffles City Mall in downtown Singapore. I wanted some chicken rice, a favorite Singaporean dish (or Malaysian dish favored by Singaporeans, depending on whom you ask).

I picked my chicken rice vendor from a choice of six, grabbed my tray, and started hunting for somewhere to sit and eat. It was quite crowded, so this would take some patience and recon. Finally, I found an empty table. This was my second time to Singapore, but I was still learning.

I looked at my tray, before I sat, noticing that I had no napkins. I have a habit, while on the road, of wiping down my utensils before I eat. New germs make you sick while away from home and I wanted to avoid that. As I perused the table I had unearthed, I noticed four Watson's tissue packets on each corner of the table. This is awesome! Exactly what I was looking for. I opened one pack and wiped down my utensils. I opened another and blew my nose.

If I were in Singapore telling this story to an audience right now, they would be laughing hysterically. In fact, I told this tale in front of 600 at the Suntec Conference Center and watched them laugh hysterically *at me.* You may not have gotten this joke on me yet if in the West. I certainly did not see anything wrong with my actions during the moment. But I had just made an uneducated cultural fax pas.

Shortly after polishing off my soup, which led off the meal, four angry Singaporean women converged on me at my seat. They pointed to the tissue packets. "We saved these seats," the angriest said. "Would you please move?" scolded another. For such a polite culture, obviously I had done something to displease them. You see, apparently those tissue packets were not for me to wipe my utensils or blow my nose. They were placed on that table by these ladies to save those seats. You might say I was learning Singapore but obviously had much more to learn.

One of the trading lessons I will always remember came from a lecture by my good friend Robin Ho, one of the top traders in the Singapore market. I have urged in my writing to master the best setups, often clean trending moves. And also to not spend a great deal of time trying to master the shakeouts. For more supportive evidence, let me share the highlights of a lecture given by Robin.

Robin and I both were key note speakers at a conference for Phillip Capital clients in Singapore. I was flown down to Singapore to talk about the opportunities for the Asian investor in the U.S. markets. I didn't know Robin. but I stood in the back during his presentation because I was suffering from three herniated disks and sitting was the worst option. Tired feet were better than constant pain in my back from the stress on my spine from sitting. Robin was up first to educate the Singapore retail clients on trades for their markets. Like Joe Fahmy, Howard Lindzon, Michael Covel, and other classic trend traders, Robin showed trend trades. The charts were supermodel charts. They were in uptrends with clean channels.

After two decades of trading, Robin had learned that trend trades were most worth his time. This is where he made his money. There was no talk of the shakeouts and getting back in. No one gets rich trading the shakes. Here was a star trader, on the other side of the world, teaching his students what I teach. Build from the easiest patterns and focus on trends.

Every day is an opportunity for continuing education. I paid for my trader education when I first started trading, and I pay for my continuing education with my time, travel expenses, lost income from missed trading days, and lunch tabs. (Why do I always have to pick up the tab?) Not only must you pay tuition to the market to begin as a trader, but there will always be a cost for your continuing education.

The bottom line is that we all need coaches and mentors to perform at our highest level. The idea that you don't need one is not supported by the elite-performance data. Nor from my experience training traders from scratch to becoming the best traders they could possibly be. So, for you as a trader, build your team of coaches who will support you every step of the way!

Party Time

GMan is having fun again, particularly utilizing our new proprietary trading platform Gr8 Trade. He has reached another level with his trading. He is making longer-term plays and trading multiple trading accounts. He is trading multiple products—options, equities, and FX. He just stepped out of my office after briefing me on the eight new algorithmic strategies he was studying with our quant support staff. Some of his strategies are already running live. But he made it to this point only after methodology scrubbing, rehearsal ethic, and good coaching. Make sure that you have the support system in place necessary for you to find out how good you can be as a trader.

Let's end this section of the chapter with an example of GMan back to having fun with Iceman and with the side benefit of you learning some SMB trading lingo. This is a transcript of a Facebook video Iceman and GMan did for the firm:

> Iceman: How's it going? (Iceman) here, trader at SMB Capital. I'm here with our head trader, Gil Mendez. So, here's Gil and he's going to go ahead and break down the SMB trading lingo for us.
>
> GMan: Okay, it's important for you as a trader to have your lingo down. So first and foremost, the hundreds (making in the hundreds of dollars) are called the little bones or the baby bones. As you start getting to the thousands in trader P&L, we call them the G-bones. When you reach the tens of thousands, they're called the big daddy stack bones. And when you start playing with the big daddy guys and you start cruising into the six figgies (figures), they're called the jumbo bones. And then whenever you start getting pretty close to pushing the mils (millions in P&L), you're in a whole different ball game. They're called the mega bones. So, hopefully, along the way, you can join us over here at SMB Capital and join the fun on the desk and understand our little lingo.

SMB created a new training program that's appropriate for the Singapore retail trader. We developed this training program with these challenges in mind:

1. The time difference

2. The inability of most to watch their trading screens ten hours a day

3. The trader who does not have lightning-fast connectivity to the U.S. markets

4. The trader who does not have access to our low commissions structure

I worked for three months putting this program together. I asked GMan to share his favorite trade with Singapore and Asia Pacific. The feedback? GMan's trade that he shared with Singapore was by far the best.

Here is the trade, the Pullback Trade from his PlayBook, that helped improve his trading game and that he presented via GoToMeeting.com to Singapore. It is a trade that you can learn to master on any time frame. It's an awesome trade by an elite trader (and better person) who has fought the fight, adapted, and employed some of the best trader coaches in the country to become his best trader.

GMan's Pullback Trade

In August 2012, I visited Singapore to teach Singapore traders/investors how to trade the U.S. equities markets. This training program was presented with our partner PhillipCapital. The following transcript is from a teaching session in which GMan was piped into our Singapore classroom to teach his favorite trade, the Pullback Trade. This trade can be adapted for all time frames: scalping, intraday, swing, investing.

(For this trade review, I am going to scrap most trading highlights in the columns so as not to take attention from GMan's very detailed description. I will bold important trading principles so you do not miss any and for a better future review.)

Bella: Okay, good morning. So today's session should be shorter than yesterday's Herculean seven-hour session. *(Audience laughter)* We are going to bring in one of my partners today—"GMan," Gilbert Mendez, live from NYC. If you are a good trader, you must have a great nickname like GMan. Does anyone have a trader nickname yet? *(Audience laughter)*

So a couple of things about GMan. One, he has always been someone who makes things better at our firm. I call this being a high-character trader. Instead of complaining about anything the firm does not provide and using that as an excuse for any underperformance, he just keeps adding value. I am not sure you can be a successful trader without first being a high-character trader. He has gone through stretches as a trader where his confidence was very low and then found a way to come back even better. When I asked some of my traders to create a PlayBook trade for this training program, it was not surprising that GMan created the best setup for you to learn. It works well in a whole bunch of different time frames and, yes, for those interested in making swing trades. Investors can even adopt this trade. GMan, as good a trader as he is, has had both ups and downs and has even tried to quit. Twice.

A couple of years ago, GMan was named top two trader under 30. Now he is partner. You might be surprised to learn that GMan has a coach that helps him get better. He works with that coach every week. As good as he is, he always tries to be better. He *must* get better to last as a trader. One of the actual examples of GMan getting better is this Pullback Trade.

GMan is a great tape reader, meaning he can watch the order flow and detect a stock's next direction. But to improve his P&L, GMan had to learn how to trade multiple positions. The other day during an event in Singapore, GMan was piped in to share his trading on the open. He had 21 overnight positions that he was managing while walking Singapore traders and investors through his trades.

(*Audience looks at each other in amazement.*)

To be able to handle that many overnight positions takes an evolution from an emphasis on tape reading to other indicators. On that note, let's bring him in. So, GMan, are you there?

GMan: I am here.

Bella: All right, the stage is yours.

GMan: All right. And good morning Singapore. Let's get the party started.

(*Audience laughs.*)

I wanted to take some time to speak a little about what I call the *Pullback Trade*. Like Bella said, this is my favorite trade. Why? **I can handle a really big portfolio of many different positions and time frames.** And that allows me to manage my risk across intraday, multiday, and even multiweek. So let's just get started.

So about this trade, **I look for what is called the "second leg."** What do I mean by that? Usually, there are institutions that like a stock, and they get in with very heavy volume and create an extreme price. A price that leaves the stock extended. And very often it is very hard to trade the first leg just because you don't know the magnitude of that leg. You don't know how much the buyer has to commit, and it's easy for the buyer to shake you out of the position. It's difficult to manage your risk.

Bella: GMan, can I ask you a quick question?

GMan: Sure.

Bella: So there are two things you can shed some light on for the Singapore trader. The first thing is that a lot of positions that you have been taking recently are overnight positions and a lot of these positions originate from the Pullback Trade. Is that correct?

GMan: That is 100 percent correct.

Bella: The other day we saw you come in with 21 open positions.

Gman: Right.

Bella (*smiling*): There is an objection that Singapore traders make: "I cannot trade the U.S. markets because of the 12-hour time difference. I have to, umm, sleep."

(*Audience laughs.*)

These objections could be made in Australia, China, Japan, other parts of the ASEAN region, like Malaysia, Myanmar, Philippines, Indonesia, Thailand, Vietnam, and so on. Well, GMan is an example of somebody who is sleeping and trading, since he holds so many overnight positions. And the other thing to note is that you really are managing a whole bunch of positions. You are managing 20 to 30 positions on a regular basis. Is that correct?

GMan: That is correct.

Bella: Okay, this is one of those trades that will help you manage a bunch of different stocks **without watching them tick for tick** and creating longer-term trades.

GMan: The beauty of this trade is that you have to be patient with the setup and **wait to get the signal for the trade to work.** After you see the signal and make the trade, then just put your stop-limit order in and you can go on about your day.

Bella: Okay, great.

GMan: All right. You can trade this with any time frame: intraday, micro scalper, trend for the day, trend for the week, and even as an investment trade. One thing about this trade is this might take more than one try to enter and that is something that you have to deal with. **In this type of trade, I would actually prefer to lose some on the first trade because the second trade offers a better risk reward.** I will explain why in more detail later on.

This trade can be used for scalping on a smaller time frame and swing trading. Basically, you can hold the position for 30 seconds, 4 minutes, 90 minutes, and/or 1 to 3 days. Something that is counter-intuitive for most traders is that you are never entering at the bottom of the pullback. **You are always entering when the momentum is on your side**. **And a lot of people think that in trading you have to enter at the lowest entry to make the most amount of money, and that is not necessarily true.** It is very difficult to pick the bottom of a trade without getting stopped out.

Bella: I want to expand upon the point you just made about picking bottoms. So you sit there watching the tape, and you see a stock ticking lower, ticking lower to try and spot when and where you can get long. It is very difficult to forget after you enter a position how bad that stock looked when it was actually going down at the bottom. And if you are actually trying to capture the bottom of the stock, what is the memory that you have in your head? The most recent memory you have is that the stock is weak. It is so hard to shake this memory from your trading head after you enter, such that you have to fight your trading brain to sell this position too early. You have to have a conversation with yourself not to overvalue the memory of how weak that stock just was.

If you buy at the bottom, your recent memory of the stock is it has gone lower and lower and lower, and it looks so bad. Stocks look the worst at the bottom. So that is one of the reasons why you want to see the stock turn. Because now if you see the stock turn, you don’t have that thought in your head that the stock was so bad. And now the thought is the stock is turning up. You can get a lot bigger and hold longer in *that* position. **When you buy that bottom, you inevitably sell too quickly because you cannot forget how bad the stock looked at the bottom.** This is human nature.

Does that make sense? When you try and buy the bottom, you are often wrong and get stopped out. When you buy the bottom and you are correct, you almost always sell too early because of the recent memory about how bad the stock just was. You are like, “Ohmigod, I am in the money.” “Sell! Sell! Sell!” as Jim Cramer says.

(*Audience laughs.*)

This stock was so weak. I should take my money and run. But if you do this, then the math for this play doesn’t work. Good point, GMan.

GMan: Excellent. And one last point about this trade is that **when you can combine the idea with tape reading, then you can *load* the boat with minimal risk.** This really gives you the ability to take a lot more size with minimal risk. I will talk more about this.

The first thing is that you have to use some kind of scanning tool to find stocks that are moving with above-average volume. And this is the key. SMB has developed the SMB Radar and SMB Scanner. Those are my two tools that I use. The second thing is that I assume you know how to draw proper trend lines. With this trade when the momentum is turning back on your side, it’s very easy to tell the trend line has been broken.

Bella: Singapore is the home of technical analysis education. Correct?

(Audience shouts “Yes.”)

GMan: All right, here are some of the requirements. **You need a powerful opening drive with above-average volume for the time frame important to you.** Do you know what an Opening Drive Play is?

Bella: We are going to talk about that in day three, GMan.

GMan: Okay, excellent. First, the key is the opening drive and recognizing the direction of the higher time frame trend. So if you are looking at a 15-minute chart, you make sure that the opening drive is in direction of the trend of, say, your hourly chart. If you are using an hourly chart, make sure it is in the direction of the daily chart. Similarly, if you are in a daily chart, make sure that it is in the direction of the weekly chart.

The next point is that it should be a lower-volume pullback with at least four candlestick bars in the pullback leg. This is the key. A low-volume pullback must occur. Once you have a powerful opening drive with heavy volume *and* a lower-volume pullback, then you have a high-probability trade setup.

The next thing is the bar has to close outside of the trend line to enter the trade. What I mean by *the bar* is the charting bar in the time frame you are using. And we will talk a little more about that. Make the trade when the stock is in the direction of the trend.

Here is the trade (see Figure 10.1). In general, this is what it really looks like. You have an opening drive. You have your pullback. And if the momentum returns in the direction of the trend, you are going to enter where I have circled Entry Area in orange. You are going to have the stop loss just below the swing low, which I indicate with the red line and "Stop right below swing low." The first target is near the previous swing high. The second target is the break of the trend line. Now if you look at it from the downside (see Figure 10.2), you have an opening drive to the downside. Then you have the retracement. When the momentum gets back to the downside, you enter to get short. Place a stop just above the swing high. Your first target is the previous swing low, and the second target is the break of the trend line.

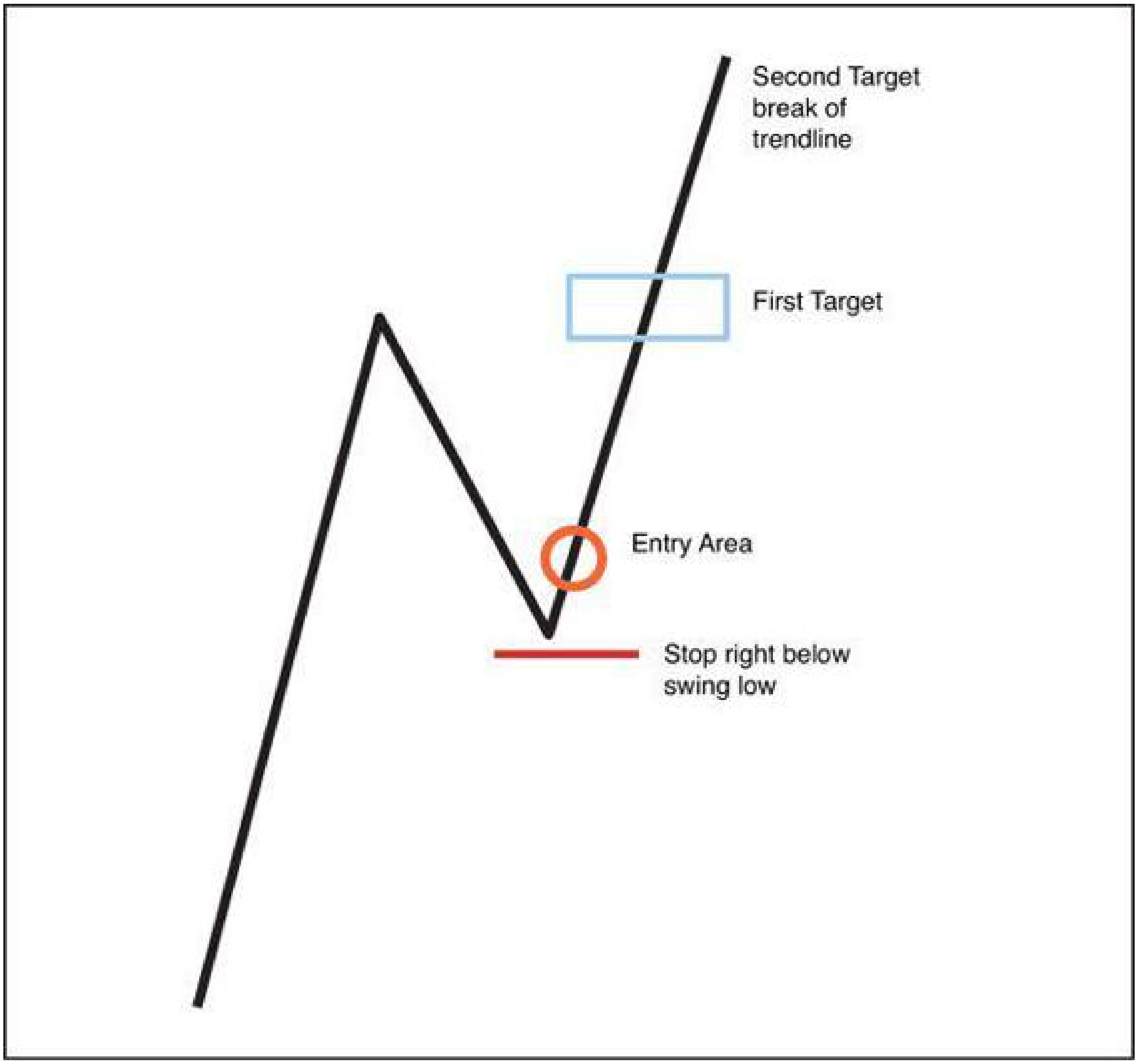

Second Target
break of
trendline
First Target
Entry Area
Stop right below
swing low

Figure 10.1

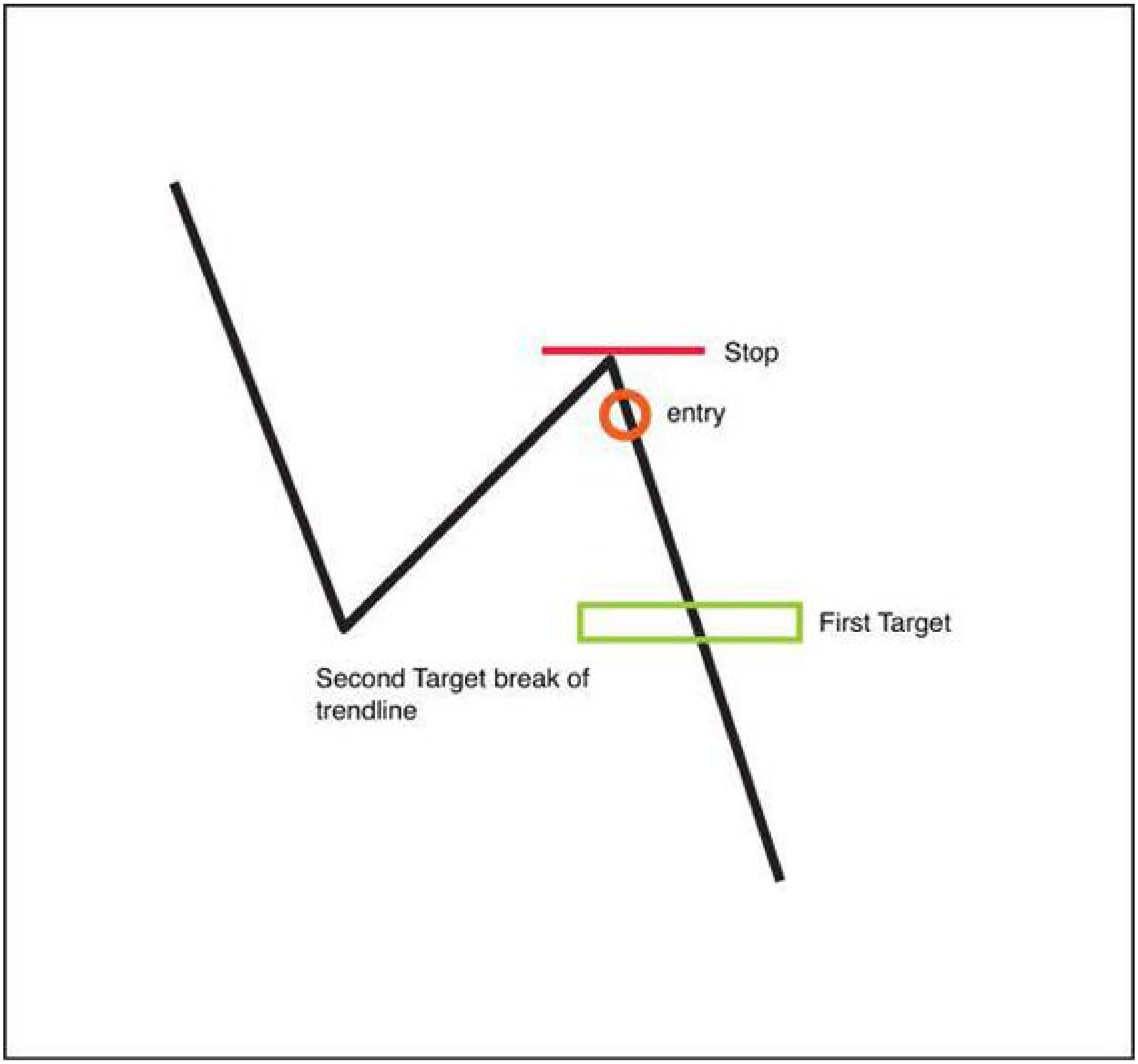


Figure 10.2

All right. Now let's talk about the second entry and what it looks like. Meaning you make this trade and get stopped out. But then you look to enter a second time, which is even a better trade (see Figure 10.3). So you have your opening drive. You have the pullback. And the momentum starts to turn, and probably you enter and take your loss. It breaks your trend line again. The momentum changes back in your direction. You enter your second try, and the same rules apply. Have a stop loss below the previous swing low. Your first target is the first swing high, and the second target is until the break of the trend line.

Figure 10.3

Let's look at it from the other side (see Figure 10.4).

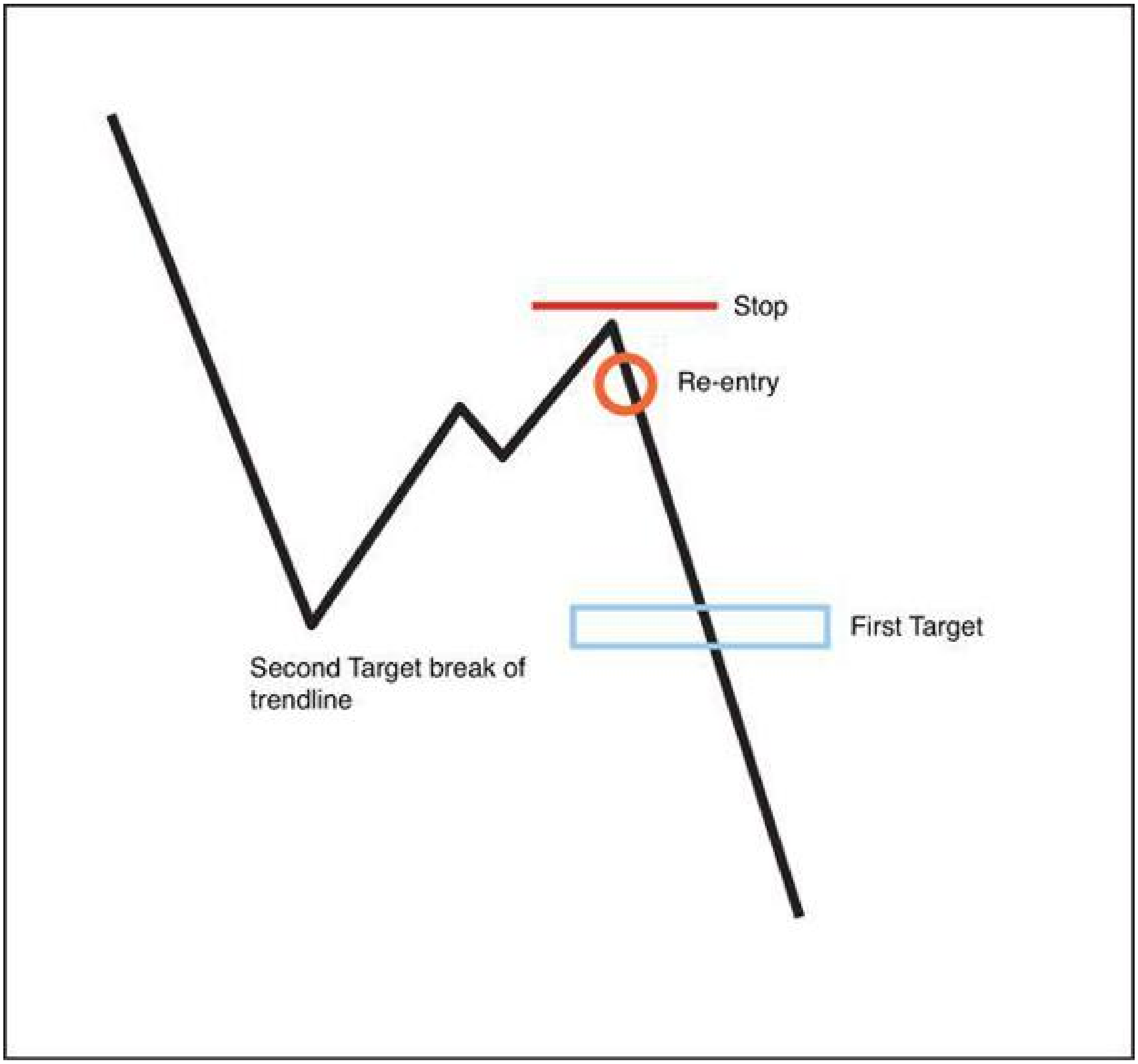


Figure 10.4

On the short side, there is an opening drive and then a retracement. And then you restart the trend to the downside. **There might be too many people shorting the stock perhaps with our first entry.** Take the loss on the first entry. The stock resumes the downtrend, and we re-enter the position for a second try. Your stop is at the previous swing high. You have your first target, and your second target is the violation of the trend line.

Okay, let's talk about the second try, which is pretty important. It tends to be a higher probability trade. Why is that? So let's just think about this for a minute. A lot of people when they see the opening drive, they want to get short. A lot of these people get short too early and get trapped. Buyers come in to establish a new trend, perhaps. That is the psychology of this setup. You have a higher probability in the second try.

Bella: So, GMan, what is interesting about this is that you set up this trade, and spend a lot of time outlining that the first entry might not work. And I think that can be surprising for a lot of new traders to hear. Because most have been taught to enter a trade and how and where to do it. That is the end of the teaching. But in this kind of trade, you are actually saying a lot of the time you are going to be taking the first loss. So what is your mindset after you have taken the first loss in one of your favorite trades?

GMan: Actually, I get pumped. I know **the second try offers a better opportunity, a higher probability risk/reward.** More money can be made with the second try. And very often the first loss is very meaningless compared to the potential of the second trade. So the way I look at it even if it is my favorite trade, it doesn't work all the time. I know there will be losses, and I will cover the losses with a second try. You know for every five losses, there is one winner. I really can make good money in the 20 percent of this trade that works.

> *If you are interested in learning about Fibonacci levels, please read* The Trading Book *written by my friend Anne-Marie Baiynd.*

Bella: You might say you are willing to make an investment in your trading with a first attempt loss. Okay, audience question. GMan, do you use Fibonacci for the retracements in the pullback?

GMan: Great question. I do keep Fibonacci levels in mind, as well as the tape. When the stock starts to turn, I use that information, and I will combine these technical indicators to make a better entry, which helps when putting on a bigger size. For example, if we stop at support for a Fibonacci level and the stock turns, I may decide to enter with more size.

Bella: Question from the audience, GMan. How do you trail your profit? I suspect that that answer is coming.

GMan: Ah, here is the way I look at it. Once I enter a position, I know where my stop is. Once I put the trade on, I don't touch my entry and exit target ever. Once I am in, I am committed to the trade. Once it reaches my first target, I trail my stops using the bigger trend line.

Bella: So let me ask you a question, GMan. So when we are talking about Reasons2Sell, one might be the market hits overall resistance. Another might be the stock actually hits your target price. Another, the stock hits longer-term technical resistance. And on and on and on. The only way you get out of this position for that second target is if it actually breaks the bigger trend line?

GMan: Good question. There is a little bit of leeway to get out of your second target. It is better to make a trade more standard, particularly when first learning a setup. How you make the most profit is you let it break your trend line. With the second target, I use a lot of discretion, and the first target I don't ever mess with it. The biggest part about this trade is you have the highest probability from your entry to the first target, and what happens after that really depends. But I don't touch my position once I have entered the trade and until it touches my first target.

Bella: Okay, thank you. One more audience question. So for your second try, for the second target, is the stop loss all the way above the previous swing high or just below the first target?

GMan: I will set an exit price so I will not lose on the second piece. The beauty of this trade is when it makes a new low or a new high, the stock will tell you how much more momentum or power it has. So if the stock is making a new high with a high volume, it is very likely to work compared to making a new low with low volume. Here, I am skeptical about letting the trade ride. If you look at the pattern, it comes down with heavy volume; and in the second leg, if there is not heavy volume, then my target is the first target, and I will take the second leg if it is just as powerful as the first leg.

Bella: Thank you, GMan. As you get more experience, you will add more rules to the trade as time goes by. But first you've got to understand the basic setup. All right, GMan, back to you.

GMan: All right, so let's get back to the second try. So it's a high probability trade. The psychology on the chart I explained earlier. **I don't ever take a third attempt at this trade.** Well, sometimes I do, but I shouldn't. I am not perfect.

(Audience laughs.)

I never take that third attempt because at this point the new trend is established on the other side. It starts to lose the likelihood it will continue its previous trend. So, for my personal style, I don't take a third attempt. I am only giving a stock two tries. So the retest of the swing high/low tends to take longer than if you caught it on the first attempt. You must have the patience to attempt the second try for the first target. Obviously, this offers you a better risk/reward. **I risk more money on the second try because we have a better probability and a better risk/reward.**

Bella: What is very important about this trade is something very straightforward. How much money are you willing to risk on this trade? And what percentage of that is your intraday loss?

GMan: Good question.

Bella: Thanks, GMan. Maybe I should audition for a TV hosting gig?

(Audience laughs.)

GMan: So, on the first test, I am only willing to risk 10 percent of my intraday loss, and on my second, I will risk 25 percent. Is that clear?

Bella: Thank you.

GMan: Okay. This is the setup and the layout of the rules and what things to do to improve and make the trade your own. We emphasize making trades your own heavily here on our desk. It is not just about learning a trade and executing the trade without any structure. Often what we do is figure out what is the best time frame for you, figure out ways for you to enter with more confidence if using the tape or Fibonacci or whatever works for you. The way I improve this trade is by using the tape to manage my risk better on the entry, and once I get the confirmation, I can get bigger with Tier2 and Tier3 and pull out a lot of money.

> *GMan's reading of the Tape Training Program was inserted into the training program we built for Singapore traders.*

I work based on tiers. So for every tier, I am going to risk 5 percent of my daily stop. Tier1, I am risking 5 percent of my daily stop; 10 percent for Tier2; 15 percent for Tier3; and 20 percent on Tier4.

Bella: What is your daily stop? What is your daily intraday stop?

GMan: Five thousand dollars.

> *GMan trades more than one account and this is just his intraday account.*

So in this case, I am going to risk $250 on my Tier1 for every position. And another thing, if I have 20 positions in Tier1, then I am obviously at 100 percent of my daily risk, but that is very rare.

Bella (*smiling*): Please, then you just ask for more buying power and get it.

(*Audience laughs.*)

GMan: Fair enough Bella. Thinking this way makes it easier to build a lot of consistency with your numbers. And now you can see how the math really helps. If you have a trend day and if you have 20 positions all on the same side, then you can have great day.

You use the previous levels established on the trade to start a feeler position, start your position early without gaining confirmation. Once you get the confirmation with the break of the trend line, you can add to the position.

Use the tape to *add* to the trade while it is working. And next is a favorite trade, *adding* on tight consolidations near previous swing highs/lows (see Figure 10.5).

Figure 10.5

In the above trade, say, for example, you are getting closer to your first target, and near your first target you see a big new seller; then you can get to Tier5 or Tier4 with very little risk. So there are a lot of very different ways to add to your positions while it is working. This is all about how you make the trade on your own.

Okay, now let's get into more of the time frames. So I like to trade on an hourly chart. It could take two to three days; sometimes it really takes four days to capture the first target. If you are in a really super strong or super weak stock, it can take a day. **The positions that get to the first target quickly are usually the ones that have a good follow-through.** And this is ideal for short-term swing trades. With this trade, you can put them on and check at the end of the day or check on them every two or three days. This is the ideal setup. Entries can be better timed with a 15-minute chart. Once you have big positions, watch them a little closer so that you are managing your capital.

Next is the 15-minute chart. I am watching some trades that are moving intraday. And these are mostly two- to four-hour setups. Twenty to 30 percent of the time you can take the positions overnight. This is an excellent setup for overnights. And it is very ideal for intraday swing trading. Your entry here is better with a five-minute or one-minute chart.

The next is the one- to three-minute intraday charts. These are ideal for scalping volatile stocks. If you are really trying to scalp in the market and you are more a micro-trader, this can be an ideal setup for you. Twenty percent of my trades are with these time frames. I can generate $500 to $1,000 a day with this technique, and it is easy to take money out of the market.

Now let's look at some real chart examples (see Figure 10.6). You are looking at a chart from August 2nd. So this is an hourly chart. On the opening of the 2nd, there is really nice volume, 10 million shares. It is much higher than the previous days. You see the pullback on the 2nd, and the trend seems to be back again on the 3rd with a big candle. You may enter at $18, but you get stopped out, as it was a fake break into the trend.

Figure 10.6

Now let's see what happens the following day. You redraw your trend line. And on the next day, it is right at 17. The following day, it breaks the trend line and comes out with good volume, and I add to my position at 17.25, and in the next five hours, it gets to the first target. I draw my trend line. And in the next three or four days, it goes up to 21 from 17.25. Any questions about this trade?

Bella: Yes, there is a question, GMan. Do you have to change the trend line as the chart is changing?

GMan: You do. And this is why initially I drew my trend line with the first three candles on the pullback. **You always want to have at least four candles on the pullback.** In the fifth one, I was out of the trend line, and obviously now the stock breaks the initial trend line, and we are stopped out.

The rule with trend lines is you redraw the trend line at the swing high through the high of the move where it makes a swing low.

Bella: Do you add when the stock was trading higher after the first target?

GMan: I made an entry at 17 and added some near 17.25. And I didn't add to my position after the first target. This stock I didn't trade aggressively. It was not a clean tape.

Bella: When we add, we have to be responsible and always add a stop loss. So if the tape is not clean enough for you, do not add and add and add. GMan was trading ADSK live in front of 700+ people the other night and was getting bigger and bigger and bigger. ADSK was very clean. SMB made a huge chop in ADSK that the audience saw live. GMan made 8 points in that ADSK play, all for the audience to see in real-time. It was awesome! All right, GMan, back to you.

GMan: Okay, let's look at another example (see Figure 10.7). In the same day, GMCR makes a very powerful drive on really nice volume. I was not interested on the first day, and the trade really started at the entry point *(green circle)*. I have the bars; I have my trend line and my entry at 22.25 and a stop loss at 21. Using a smaller time frame can be helpful here. At this point, I am getting only a 1:1 risk/reward ratio. So I started out smaller than normal. I obviously got stopped out. So I draw another trend line and enter at 20.80, which also gave me a better risk reward.

Figure 10.7

The momentum picks up in the direction of the trend line, on the 7th. The first entry was on the 3rd. My second entry was at 21 with a stop at 20. Now you have a better risk/reward, and it is a better trade compared to the first leg. It got to the first target, and I made $3 in the position.

Bella: If you have fixed the stop loss at $20.80 and it gets below there on light volume, do you exit or not?

GMan: Ninety percent of the time, I will exit. If it is a one-minute or a five-minute chart, I try to give the stock more room. Since this is a much bigger time frame, many more people are involved.

Bella: Are you holding on to 10 percent of your position after you get stopped out? That helps to track if this was just a shakeout.

GMan: Well, that is more a personal thing. If it is my first entry, I keep 10 percent so that I can keep track of the position just in case I get caught up in other positions.

Bella: **A lot of times we hold on to positions we are very confident about, even if it is a small position, because when you actually own something, you track it better than when you don't.**

Could the Singapore traders skip the first entry and wait for the second entry?

GMan: I have thought a lot about that. If you are trading a 60-minute chart, you are better off waiting for the second try. If you are trading the 15-minute, it is more like a coin flip. I think for the 60-minute chart, the probability is more like 70/30 that you get a second try. For the shorter time frames, you have to take the first entry.

Bella: GMan is a professional trader. He takes many of the first trades because he does not want to miss out on this trade. Even though the second try might have better odds, that does not mean taking the first try isn't also a profitable setup. Do not worry about losses as a trader. Your job is to do the right thing. And if you have an edge, you have to take the trade. Losing money is part of trading.

GMan, what do you mean by Tier1, Tier2, Tier3, Tier4, Tier5?

GMan: I always think about how to make my numbers consistent every day. So, for example, if you have 100 shares of GMCR, and you are risking 60 cents... if you have 100 shares of Apple, a $670 stock, with 100 shares with your minimal risk of three or four points. So in this case you are risking $60 with GMCR, and in Apple you are risking $450. This will throw off your numbers because it's the same setup, but you are risking more capital. On my Tier1, I am risking 5 percent of my daily loss ($250). So if I'm risking 50 cents, I can trade 500 shares. So in APPL if I'm risking 2.5 points, I am going to have 100 shares. So using Tier1, I am risking the same amount of capital. Meaning my risk/reward is the same for both stocks. Most traders, believe it or not, do not do this, and this messes up the consistency of their trading. Does that make sense?

Bella: Thank you, GMan.

GMan: Okay! Let's look at a couple of more examples (see Figure 10.8).

Figure 10.8

Here, we have VVUS from August. You have a good volume opening drive over three or four days and then a continuous pullback. Actually, on the tape, you can see a lot of accumulation at the 21.30 and 21.40 area. Actually, I bought my Tier1 at 21.50, 21.60, and had to deal with it for the next two days. But you can see the break of trend line, you then can see your entry around here, and the pattern repeats itself. There is good volume at 21.30, and then again it breaks the trend line and then you add to your position with Tier2 over here and Tier3 and Tier4 until 22.60. And as you can see, the previous swing high is 23.40. So I had $250 at risk for a $6,000 profit. All right, let's look at another one (see Figure 10.9).

Figure 10.9

This is a trade in Facebook. This is a 15-minute chart, and you have the opening drive intraday setup. This shows you something that works intraday. There are 5 million shares traded with the downside move. FB breaks the trend line, and you enter again at 20.85 with a stop at 20.95. Your first target is 20.70. So you are risking 15 cents for 15 cents in this case. You have an entry at the dotted line, which didn’t work. You take the second entry here, and with this second leg, you have a very profitable trade.

All right, that is all the examples I have, and obviously one of the challenges is you have to go home and look at charts, and find the time frames that work best for you. This really is a powerful trade.

Bella: Question from the audience: Did you take any profits in the Facebook trade in this setup?

GMan: Actually I shorted FB at 21.60 and added to it at 21.50 and took profits before this setup. I have a swing account and an intraday account, and I definitely made profits in the intraday account in this setup. Do you have a comment, Bella?

Bella: When you were putting this play into your PlayBook, how long did it take for you to get confident with it?

GMan: I have been using this trade for a couple of years. But I wasn't making good money with the trade. **Only after spending time looking at my numbers carefully for a month, I realized that the key was the second entry.** I was very happy with the results when I took big positions in the second entry, and the profits were much bigger than the original loss on the first try. And this has changed my play.

Bella: So, this is your favorite setup?

GMan: Yes, correct, for multiple day trades.

This trader is now affectionately called "Mr. Lunch."

Bella: Question from the audience, GMan. If the entry comes near lunchtime, will you wait for after the lunch?

GMan: I eat lunch at my desk. So I will execute even during that time.

Bella: Question from the audience, GMan. Will you hold this trade over the weekends?

GMan: Yes. There is obviously risk involved in that. I take risk overnight. What I try to do is look at the overall short-term momentum in the market. And potentially if the market seems to be going up the next day and if I have a lot of shorts, then I will go long with the SPYs to help hedge my shorts. I might remove some longs to lessen some potential risk.

Overall, you have to identify the time that works for you. If you can't do anything overnight, then the 60-minute chart is not good for you. The 15-minute is the best for you.

Audience: Can you go to the second-to-last chart please (VVUS 60-minute chart)? Here, the pullback is very substantial. So how do you see this as a pullback and trade confidently?

GMan: Good question. You see my chart here (see Figure 10.10).

Figure 10.10

And the play in question was this leg over here. I want to enter at 21.40 and take out 23. You see it in a longer time frame, and you can see support at 20. I am playing the pullback over here and wanted it to go higher, but obviously it reversed. So you can see how powerful it is if you are making the trade for the first target. It is likely that it will reach the target, but over the next couple of days it reversed. So I always say if the target is too far away that you take profit early and don't get too greedy. Does that answer your question?

Bella: Yes. Any other questions? GMan, what is the split between your intraday trades and position trades and are you noticing that you are taking more position trades recently?

GMan: In terms of volume, I will say 10 percent of my volume is in position trades, and pretty much a lot of my trades are intraday. I will give you guys a good example. I am still doing 60 percent to 90 percent of my volume intraday because I will take the longer-term swing trades to make really good money on the trades I like. I trade over 200,000 shares daily.

So that was a detailed description of the Pullback Trade. Now start making it your own. And shoot GMan an email on your progress, gmendez@smbcap.com. Trade well!

11. South Africa

I was in my hotel room overlooking the Atlantic Ocean in gorgeous Cape Town, South Africa. Dressed in tan slacks, a white Paul Stuart dress shirt, and shined Ferragamo black loafers, I happened to be taking in the ocean when the phone rang. I answered it.

“Mr. Bellafiore, your driver is here.”

Grinning, I thought to myself: I have a *driver*? Life is good!

I went down and met a gentleman who was indeed my driver, a former competitive basketball player from Malawi named Geoff. He escorted me in a souped-up Range Rover to one of the coolest trading offices I have ever seen. I was in Cape Town to work with our partners African Gateway and their prop arm, Storm Securities, to help their successful South African market traders add U.S. equities to their trading quiver and, of course, to take a look at their South African trading. We reached our destination—this prop desk was a suburban oasis.

I walked through the front door of a mansion that houses these South African traders, passed two maids in the kitchen preparing braai (South African barbeque), specifically marinated steaks, and avocado and feta cheese salad. I soon learned that a lot of these guys eat healthy—and look like they could be found inside the pages of a *Men’s Health* magazine. Walking further inside, I saw a pool outside to my left, which was open and ready for some action. There was a bar to my right, fully stocked, and I mean seriously fully stocked with anything you could want. Eventually, I would favor too many of the local Cape Town flavor, Castle Lights. Still further ahead I spotted the gym. Come on! What trading firm doesn’t have a built-in gym—and one that comes with a shower installed? Trainers meet traders here early in the morning to help them work on their fitness. During lunch, many of the traders hit the gym to blow off steam. Some, such as traders No Carbs and Carpe Diem, even work out in teams and push each other during lifting sessions.

Oh, wait. I almost forgot. There was a pool table on the way in and huge, flat screens for viewing cricket, rugby, and soccer. During my stay here, I would come to miss American sports, any American sport, even a bad NBA game. I began to understand the soccer and the rugby, but not the cricket, where two teams can play for six days and the match can end in a tie. And people say baseball is slow?

I headed upstairs to the second floor. This was the trading floor. Forty or so “mates” were sitting next to each other gaming the South African and London markets. My NYC trader attire to their shorts, flip-flops and t-shirts clashed. I was here to teach these pro traders how to tackle the U.S. equities markets. I didn’t know what to expect. Here’s what I was about to learn:

1. The PlayBook will help South African traders with their markets,

2. The PlayBook will help the desk capture trend plays that they are not making, and

3. The PlayBook will reinforce their trading fundamentals, which have slipped of late.

The No Trend Pledge

The first rule about teaching—or just being a gracious guest for that matter—is that you must make a connection with your students. It’s hard to get through to people if you do not get to know them, find out what makes them tick, and show them that you care. This is coaching, teaching, mentoring 101. But I had just walked in. I’m the person, the author, some “Bella” guy from NYC staying for ten days, who they do not know. The only thing pro traders are more skeptical about than their positions is a trading author. I would have to quickly show them that I’m a trader first, a trader who also teaches.

I walked around the room and shook hands and met the traders. They seemed happy to meet me, like they had been waiting for my arrival. Well this was a nice start. Even considering I was a bit beat, as I had just flown from Singapore to Johannesburg and then to Cape Town and it was really 2 a.m. back home.

The good news for my teaching assignment was that I had been working with some of these traders before my arrival. I did a series of webinars with about a dozen Storm traders on U.S. equity trading. Technology, as it is, one webinar was conducted via a smartphone and wireless headset as I drove four hours from my family condo in Tampa to the Westin Diplomat Resort & Spa in Hollywood, Florida, for a trading presentation. I also had developed and shared a special training program for experienced South African traders.

This was a much more active trading training program than the one I would later devise for Singapore retail traders, as these guys were active pro traders with impressive track records. They trade at the largest prop firm in South Africa, which might do 10 percent of that market's daily volume. My visit was the end of the training program that I had built. That end was to get these traders to start developing their PlayBook of U.S. equity setups that made the most sense to them.

As I walked around and talked with these pro traders, a common theme repeated: their markets do not trend. This was restated often and as the gospel from multiple different traders. After the tenth trader rehashed this mantra, I started to feel as though I was at some political convention where all the politicians had signed a No Trend Pledge. So I started to remember my trading in 2003, 2004, 2005, and 2006—markets where I had to fade most moves trading U.S. equities. Quickly, I learned which stocks they were mostly trading: the three biggest South African banks (FirstRand, Absa Bank, Standard Bank), gold miners, and oil.

The South African market is not as volatile intraday as the U.S. markets. There aren't as many opportunities as in the U.S. markets because there are mostly 20 names that a majority of traders closely follow. If you talk to some of the best South African traders, they might expand that list to 50 names. But this isn't the U.S. equity markets with 5,000 plus stocks to trade and almost every day a dozen of stocks In Play.

All of this felt like when I first started trading and we could trade only NASDAQ stocks. And we could only trade NASDAQ stocks on the long side, as mandated by our firm. "We are a long-only firm," promulgated management. Basically, we traded the same stocks every day: the semiconductors, the chipmakers, and the technology companies. It was a year of DELL, CSCO, MSFT, INTC, AMAT, KLAC, and NVLS. Yes, INTC used to be a great trading stock in the '90s. And CSCO used to be a bellwether that kept growing. In fact, John Chambers, CEO of CSCO, was once idolized like Steve Jobs (whereas today some squawk for his departure).

During our first training session, I introduced the concept of The PlayBook and how the Storm team should think about their trades. I didn't care which trades were in their PlayBook, just that the trades made sense to them and that they archived a best trade daily. But on Day One, Stormers were sure to let me know that their markets did not trend, so they could not make Trend Plays like we encouraged to traders on our desk.

Okay, I thought. I was not an expert in their markets and had heard their message...*repeatedly*. I have to admit, in my notes I circled this thought and surrounded it with a huge question mark. It didn't make sense to me that Stocks In Play wouldn't trend in their markets. But they were so wedded to this doctrine that I accepted their observations and prepared to help make them get better with patterns that worked best in their markets. That's *my* job!

A Trading Desk of Tennis Players

After our first day of work, it was time for dinner, drinks, socializing, and learning more about these traders personally. The first trader I chatted with had played professional tennis. At one point, he recounted he had been ranked as the seventieth best player in the world. Wow!

I asked him his favorite city.

“We really just went from the hotel to the courts and then to the airport, so I didn't get to spend much time in each city.”

Twenty minutes in, group shots were proposed and ratified. I had not had a shot since perhaps law school. But this didn't strike me as a crowd where a no thank you would have been acceptable. Shot one.

The next trader I talked to had beaten tennis legend Pete Sampras when he was 16. He smiled and relived that athletic feat stroke by stroke. More shots were ordered. Shot two.

The next trader had won the Silver Medal at the Atlanta games with Tim Henman.

The next trader had been ranked twentieth in the world at his peak.

Another trader had won four doubles Major Championships.

There were two college FSU tennis players.

The founder of the firm was storied as the number-one South African tennis player when he was a teen and built his firm around the principles of transforming high-level tennis players into traders. He also garnered the reputation as one of the best South African traders. His theory was that former high-level tennis players could better fight all day to pull profits from the markets. This idea made me think of GMan, our ultimate all-ticks battler.

There was never a stock created that could stop GMan from fighting. As a former high-level athlete, I felt comfortable with this team of traders. These were guys I could understand and respect. I liked them immediately.

Shot five.

Was It True That Stocks In Play Didn't Trend in South Africa?

The next day I came back to learn more about the South African markets and this team, our team. I felt I needed to understand how they were trading their markets so I could best apply the principles of the PlayBook to their trading. Entering stage right was FirstRand with fresh news, making it a Stock In Play.

FirstRand was one of their top three bank stocks:

1. Standard Bank of South Africa Limited, traded as JSE: SBK
2. Absa Group, ASA: SJ
3. FirstRand, FSR: Johannesburg

FSR had had trouble clearing longer-term resistance I was told. It did on this day during the open session. Hmmm. In our markets when a stock clears long-term resistance, we get long and probably make a Trend Trend Trade. A *Trend Trend Trade* means a stock in a trend on the long term and intraday charts. We follow this trend. We hold this position **with the direction of the trend** until there is a Reason2Sell. This is one of our most powerful trade setups, an A+ opportunity.

During the midday, we met to discuss their open and apply the principles of the PlayBook to their trading. Was there a trade that made the most sense to them that they could archive for their PlayBook?

In fact, I wrote a blog post from South Africa, discussing the importance of seeing the markets as patterns that make sense to the trader.

See the Markets as Patterns

Trade, control your risk, breathe (VVUS)

Feb 28th, 2012 | By Bella

I'm in Cape Town, South Africa, training former elite athletes.

Sifting through the daily trading reviews from yesterday it was clear that many traded VVUS. I want to make one point. See your trades as patterns. Trade the setup and then accept the result. Trading is not about being right. It is about controlling your risk. And finding patterns where your risk/reward for you is exceptional. Match Play winner Hunter Mahan teaches us the importance of this mindset for elite performers (traders):

> "If I wanted to be the player that I felt like I could be, I was going to have to change," Mahan said after capturing the WGC-Accenture Match Play in a two-and-one win over Rory McIlroy. "I had to take it easy on myself and basically not try so hard. I didn't want to have my identity stuck with my golf score. They needed to be separated, and I needed to play golf because I enjoyed it and accepted the result and moved on and not get attached to it."

One of our SMB Traders sent a "proper" (as we say in South Africa) review of his VVUS trading. He summarized his trading precisely with this thinking:

I traded 22 tickets on VVUS and there were about seven distinct trades I made:

1. Pre-market scalp,

2. Opening drive at 23,

3. Fade the ticks to buy a pullback during an opening drive, move from 23.80 down to 23.30,

4. Buying into a pullback after 10 a.m., after it puts a top at 24.83,

5. Intraday resistance breakout at 23.50,

6. One last try for the big move to the long side: taking a feeler and scalping the range from 24.40–24.80, and

7. Getting short when the range fails and confirms a lower high for the afternoon sell-off.

Perhaps thinking of your trading like this will help your trading.

During this first in-person trader review session in Cape Town, we reviewed FirstRand. One trader chimed in that he shorted FirstRand just above resistance. I asked what type of a trade he would call that. Silence.

"We call that a Fade Trade. So what is the trade?" I asked.

The trader looked confused but said he was betting that FirstRand would fail and return to the mean. A Fade Trade is a perfectly acceptable trading strategy to master. Just not with this set up. This is a setup to be removed from your Fading strategy.

"Why?"

"Because there is no follow-through in our markets."

(And on Christmas, Santa Claus slides down the chimney and leaves presents for all the boys who were good.)

"Look, you guys know your markets better than me. But FirstRand had fresh news and just broke out above resistance? If you were on my desk, I wouldn't let you short that. That is a long and a Trade2Hold to see if it will trend for the next few days. But hey, maybe your markets are different.

"Anyway, what is most important is that you start to archive patterns that make the most sense to you. A great part of the process is to write down all the characteristics of a familiar setup, brand these patterns in your brain, and then develop the intuition to trade them live.

"But getting back to FirstRand. If you want to make a fade trade with the first pop above an important resistance level, that's fine. But if it holds above resistance and doesn't go down, then you have to cover and get long. You should develop the plays that make the most sense to you. But you don't get to make up your own trading fundamentals."

Trader individuality within longstanding market fundamentals is good, but you do not get to make up plays. Fading a stock holding above long-term resistance is bad fundamental trading. I call this making up a play. This play doesn't work for the intraday trader and worse yet causes the trader to miss an A+ setup.

Later in the day I walked by the desk of a few traders and watched and listened to what they were doing. Some were still shorting this FirstRand, and it was clearly above resistance, had held above resistance, and had moved away from resistance. There were no important technical resistance levels near. Clearly, this shorting was a problem. Adhering to the proper fundamentals of your sport is important no matter what your game or who the player. I wondered if it was really true that their chosen In Play stocks could not trend. Maybe they were trading the same names every day and it was only true that on most days these stocks didn't follow through, but on the day there was fresh news that these names probably would trend.

Here's what happened: FirstRand not only traded higher above that important resistance level, but it trended nicely for the rest of the day. In the States, we would have just gotten long and held. Chop! *That* is how you make $3K plus with just one trade. Shark works hours before and after the close to spot setups like that. Pippen dreams in Mandarin for setups like this. Iceman would be at max buying power, chillin' and ignoring all young lady chats and calls.

We met in their conference room after the close. The founder of the firm sat in. Jules, another partner, was there and looking very focused and serious for a guy who's perpetually happy-go-lucky. All the partners sat in. I asked for the chart of FirstRand to be brought up.

"Okay, so does anymore have a play, a pattern, that they see in FirstRand?"

Silence.

What the hell? These guys had just missed a layup trade in FSR; they could at least spot it as an awesome long.

"Who was shorting First Rand?"

Some hands went up.

"Okay. Thank you. I'm curious. Why?"

There were sheepish attempts at "I thought it would reverse."

With my peripheral vision, I could see the founder of the firm and market veteran squirming in his seat, clearly uncomfortable and looking up at me, politely waiting to see my reaction. He was like one of those kids overloaded on sugar who you knew just was about to explode. I knew what he wanted to say. He knew what I was going to say. We had both said what I'd convey a hundred times: whether it was me in NYC or him to Stormers in Cape Town. Markets are markets. Trading psychology is trading psychology. Yes, our markets were on other sides of the world but A+ trades are universal. They exist in any market.

These guys could convince themselves all they wanted that stocks with fresh news don’t trend in their markets, and yet here was a glaring example sitting right in front of them, one that we had discussed hours before about how to attack above resistance. And most of them had traded it, ignoring one of the most fundamental rules of trading.

I started calmly, “You cannot short that stock. It had fresh news. There are no technical resistance levels for points. It held cleanly *above* the resistance level. There is no trade here but *long*.”

Stares and silence.

The founder was now pissed. My calm was not appropriate for a mistake that too many traders had made. But I was a visitor in their trading home, without the hours of personal sacrifice required to rip them as they deserved. Owners don’t mind paying the bills in a tough market. They have deeper pockets and that is their contribution. But they hate it when their guys miss layups.

He most appropriately blasted, “Guys, you have to learn to trade with the trend. This was a MASSIVE opportunity, and you didn’t take advantage of it. That is inexcusable. I am so glad to have Mike here to point this out because I was thinking the same thing. And it is important to hear it from a different point of view. You have to take these opportunities more seriously.”

So much for Stocks In Play don’t trend in South Africa.

Like a father scolding a child, this firm head had made his point. And like a master coach, he did so without putting his traders down, without harming their confidence, while pointing to the future opportunities that together they would capture. Teach; do not demean.

After the founder ceded the floor back to me, I continued. “Okay, guys, there’s a trade tomorrow that we must make. What is it?”

“The pullback to 26,” offered one “Joburg” trader who was visiting for my instruction.

“Yes, if FirstRand holds above there on the open, you have to get long. We call this a Second Day Play. This is a very powerful intraday trade. We use the most important prices from Day One of fresh news and trade off those prices. You have to start thinking about getting long right now. If it holds above there on heavy volume, what will you do? If it gaps above, what will you do? If it comes back to this price on light volume, what will you do? How you do tomorrow depends on the work you do tonight, the mental preparation you do to crush that opportunity tomorrow."

And that, I hoped, took care of that.

The American Version of SMB Traders Off the Tracks

What happened in Cape Town has happened to my desk in the States and legions of good desks worldwide. Let me share one such incident just shy of one year later. One trading day right before the December holidays on our desk, I frustratingly noticed our guys missing easy setups. I had had enough. At the top of my lungs, I screamed, "Why the **** is there only one other trader besides me short PAY and ADBE. PAY formed a Bullish Flag Pattern, Shark called it out, yet only one other and me are in it? ADBE brought the Opening Range and was In Play and no one is in that? That is completely unacceptable! Get in the easier set ups! Stop *making up* trades!"

An hour later after I still had not cooled down, I sent an email:

> There will be a mandatory meeting after the close at 4:15. I recommend that you do not sit in the front row.
>
> Here is how I remember that meeting:
>
> You guys are not expecting enough from yourselves. (*long pause*)
>
> You guys do not see how good you can be. (*long pause*)
>
> You are not taking advantage of the intraday patterns that work best. (*long pause*)
>
> You are making up some plays.

I stood with a notebook in my hand making sure I hit all the points I had furiously scribbled to highlight before the meeting. I was using a great deal of mental energy to keep from throwing it at a few of them. I emphasized that traders must first learn and make their own the best intraday setups. Trend Trend Plays. Second Day Plays. Bullish and Bearish Flag patterns for Stocks In Play.

I continued:

> Are you covering all of those opportunities? Are you as big as you can be in all of those setups?

> Are you working to make sure you do not miss any of those opportunities? Build from these trades and then add plays to your PlayBook! And *stop* trading AAPL everyday. That is great that you guys learned how to trade a high beta stock but trading it everyday is not well thought out. Trade it off of very important technical levels and when it is really In Play. Adapt the skills you developed for trading high beta to other opportunities like recently in NFLX. Don't miss the NFLX trade because you are obsessed with trading AAPL everyday. "

There was more cussing and loud talking. GMan spoke. Carlton spoke.

"Bella, anything else?" asked Carlton.

After another long pause, I ended this trading priorities reboot with, "Yeah one more thing. I do not want anyone in this firm thinking you cannot make at least 200k a year."

Just like Storm had perhaps gotten off track, my firm does. As traders you will and do. And it takes a firm leader to get traders to reprioritize the firm's trading. News flash: Sometimes we really have to get after our guys to get them back on track. Some call that Tough Love.

Some "Proper" Traders

After the meeting, Monti, one of the partners, inquired about my interests for the weekend. He's an ex-banker who has South African trading connections like President George Herbert Walker Bush has political connections. The guy is a walking Rolodex of South African trading.

In the short time I was there, we met a billion-dollar allocator for Citadel who grew up with one of Monti's traders. We tossed ideas around with the brains behind a hundred million dollars of algorithmic trading profits at one of the local big banks. We listened to a South African hedge funder looking to cut a deal. We sat with a local firm visiting to talk about a merger or a JV with Monti. We chatted with Maria Ramos, the head of Absa Bank and the second most powerful person in the country. (Okay, so I was responsible for that.)

Most everything that comes out of Monti's mouth starts with "I have a mate who..." or "We have a close friend that...." If you were starting a management team for a trading firm, you would select him. You just want to be around him, help him, and see him to succeed. They call it Charisma.

“Bella, the guys were thinking of a golf weekend if you are up for it.” And here it comes...: “One of our buddies has a house at a club up the coast.” Of course, he does, Monti. Of course, he does.

Before my visit, I was diagnosed with three herniated disks and had been making it through the day with oxycodone, ten Coke Zeros, and a rolled-up towel to support my back while sitting. Golf? I couldn’t even ride the cart for a round, let alone swing some metal around my body for 18 holes. And remember, these guys were mostly pro athletes, so imagine how they must play golf.

“I hear there are some decent wine farms here. How about that?”

“I think the boys can manage that, Bella.”

Stormers Stevie, Phillie, and Carpe Diem quickly expanded that to a weekend of wine tasting, cheetah petting, a professional rugby match (my first), and a climb up Table Mountain (my last).

Now how can I best describe these three? They are traders with some wonderful characteristics to aquire for your trading.

Phillie: Some Call It Perspective

> “Do not spoil what you have by desiring what you have not; remember that what you now have was once among the things you only hoped for.”
>
> —Epicurus

I often remind U.S. traders like TO not to be so hard on themselves. They can often wallow over their trading errors and miss the big picture. If I had a couch in my office, I might be able to get some graduate degree Psychology credits given my hours of trader counseling. They are young, living in an amazing city, playing a game they love, embracing a life-shaping challenge, with great teammates. This might be the best time of their life. Some call it Perspective.

I was having the “best brunch in NYC” with Mai, a Thailand trainee, at Sarabeth’s. I made this point. Being young and single and living in NYC is an experience of a lifetime. And then you get all that other stuff. Wow! Interestingly, I didn’t see this among the South African traders, as they possessed a markedly more positive outlook—a better perspective on trading and life. There was no better example of this than Phillie.

The boys and I had lunch at the first winery, dining on springbok, a local meat. I did not find the meat to my liking as it was too gamey for my taste. Ask Phillie and you got, “We had a very nice serving.” Before hitting the wine farm, we went to pet some cheetahs. The guys were clearly bored and only partaking in this tourist activity for my sake. Phillie’s take? Here you go, and this is about as negative as he would ever get: “It was quite average.”

Next, after we hit the winery, we headed to a Stormers match, the local pro rugby team, but we needed cups to finish the bottles of wine we had bought. The courtesy shop had none, so the guys bought jam jars to polish off the remains. I wondered if in NYC we would have griped to the courtesy shop that they should start stocking plastic cups for future clients. Instead, we sipped carefully from our jam jars, laughing in our van at the absurdity of it—and after the 320-rand jam jars rip. There is almost no complaining allowed in South Africa. You carry on.

On a crowded subway, reading a NYC tabloid, I stumbled upon a wonderful exercise that has helped me be more positive. Before bed, I write down three things for which I am grateful. Then I replay one positive experience from the day. You might write:

> I am grateful
>
> I trade with great guys.
>
> I am grateful I am doing what I love.
>
> I am grateful that I got better today.

Each day your list will be different. You might then replay a terrific trade you made or meeting a lovely potential significant other—whatever you wish. This is an exercise that has helped me. Try it.

Phillie has the sense of humor of Hugh Grant with boyish fluffy hair and piercing blue eyes. But he is a shy one, or plays that part. Again, like the others, he is an annoyingly good athlete. I think perhaps a scratch golfer. At least he wasn’t a former tennis pro. With every sentence uttered by Phillie, I feel as though I’m watching The Australian Open. Phillie sounds just like tennis analyst Cliff Drysdale—so much so that now when I watch a tennis match, I wonder why the heck Phillie is calling the game. All told, it's hard to spend ten minutes around Phillie without him making you laugh.

Spending time with Phillie reminds me of what I always try and remind my traders: trading is just a game to be enjoyed with your mates. Bad trade? No worries. Carry on.

Stevie: There Is No Option But to Succeed

Stevie? Oh boy, Stevie. So we went to the first wine farm and got served our first tasting. The hostess poured and explained the wine. Phillie was ready to propose to the server and said as much after she left. The charming and easy-on-the-eyes hostess brought Phillie to joke, "We need to plan more firm wine farm outings. You guys free Wednesday?" We all laughed, spitting up our white wine. Then the second tasting arrived but, shucks for Phillie, it was from a fellow.

"Hey, Stevie. How have you been? We haven't seen each other since that last shoot years ago," said the male.

What the hell was this dude talking about? What is a shoot? Are they hunting buddies? Stevie looks like he hunts about as much as Phillie looks stressed.

But what was more interesting is that the pour was light all around and this new server kind of had an attitude.

"Stevie, who is that guy?"

"I don't know."

"Well, he knows you."

"Yeah, I don't know."

The punter kept coming back with the pours, and each time it seemed to me and the boys that the interaction got worse and worse. This gentleman was holding something against us because of our Stevie.

Fast-forward to later that night and we were all at a bar in downtown Cape Town. Winter months in the States and Europe are warm weather months for Cape Town, which attracts many of the world's top and wannabe top models during this season. It was about time to close at Chin Chin, a local hotspot crawling with these wannabe models, and I was wondering how we were going to get home, seeing that we were all bombed. And it was past 2 a.m., so too late to call our driver.

One girl walked right up to Stevie. Too close if you ask me. I swear, not ten minutes later she was driving us all home, and between us clearly had no intention of making it back to her place.

So that shoot? Apparently, it was a model shoot, and the young ladies apparently *looove* Stevie, which causes awkward moments when we run into guys he has obviously pissed off. A stolen girlfriend? A stolen would-be-girlfriend?

Stevie may be a lady-killer, but he's also extremely focused as a trader. In fact, Stevie was the first to send me a PlayBook trade from the South African markets. He keeps a detailed trading journal. He asked the most questions. Rumor on the trading floor is he swore off going to a local gentleman's club in Cape Town for the entire year in order to improve his trading. Some call that dedication. He is a worker.

You learn to spot the workers as you train more traders. Alabama is one of those on my desk. He was disappointed in his results so I gave him extra practice in an email:

> I would try this to get better at determining good probability trades from the bad.
> This will take some work.
> It's up to you whether to do it.
> Do **two** playbook trades a day.
> Before each open review all of the trades you have added to your PlayBook.
> And review the PlayBook trades of the others shared on the desk.
> Do this for three months.
>
> This will get you some serious reps looking at patterns that make sense to you and others.
>
> Stevie would have done this work.

But there's something more about him. He has what I would call an I-will-not-fail attitude about him. I love that about him, just this visible refusal not to win. But there is something more. This goes unsaid by many pro traders. There might also be a fear to fail like any other job would be a prison term. Trading to him, the rest of the Stormers, and most traders globally is the best job in the world. Giving up this amazingly cool title of trader, every day is new and often in-the-moment job and life would be hard. And judging from my interactions with him and his eagerness to get better as a trader, I doubt he will have to.

Let's take a look at how The PlayBook can be applied to South African markets with an Important Technical Level Trade in FSR, FirstRand archived by Stevie.

Important Technical Level Trade

Stevie

FSR

February 23, 2012

Big Picture

The FTSE/JSE All Share Index has been consolidating above the 34,000 level with the breakout level of 34,400 well within reach. On this particular day, we were holding strong at 34,100. Our market was also very well supported by the performance in the U.S. market with the S&P Future (ES Mini) trading at a 2012 high of 1366.

The banking shares in particular had rallied very nicely over the past month (February) and were consolidating at the upper end of their ranges with little in the form of pullbacks, which would suggest that a break to the upside was a more likely scenario.

Intraday Fundamentals

FSR released a trading statement prior to the market open stating that earnings would increase by between 24 percent and 28 percent. The increase, although due to a non-recurring item, may lead to speculation in the market of the declaration of a special dividend and should therefore be taken as a very bullish sign moving forward.

Technical Analysis

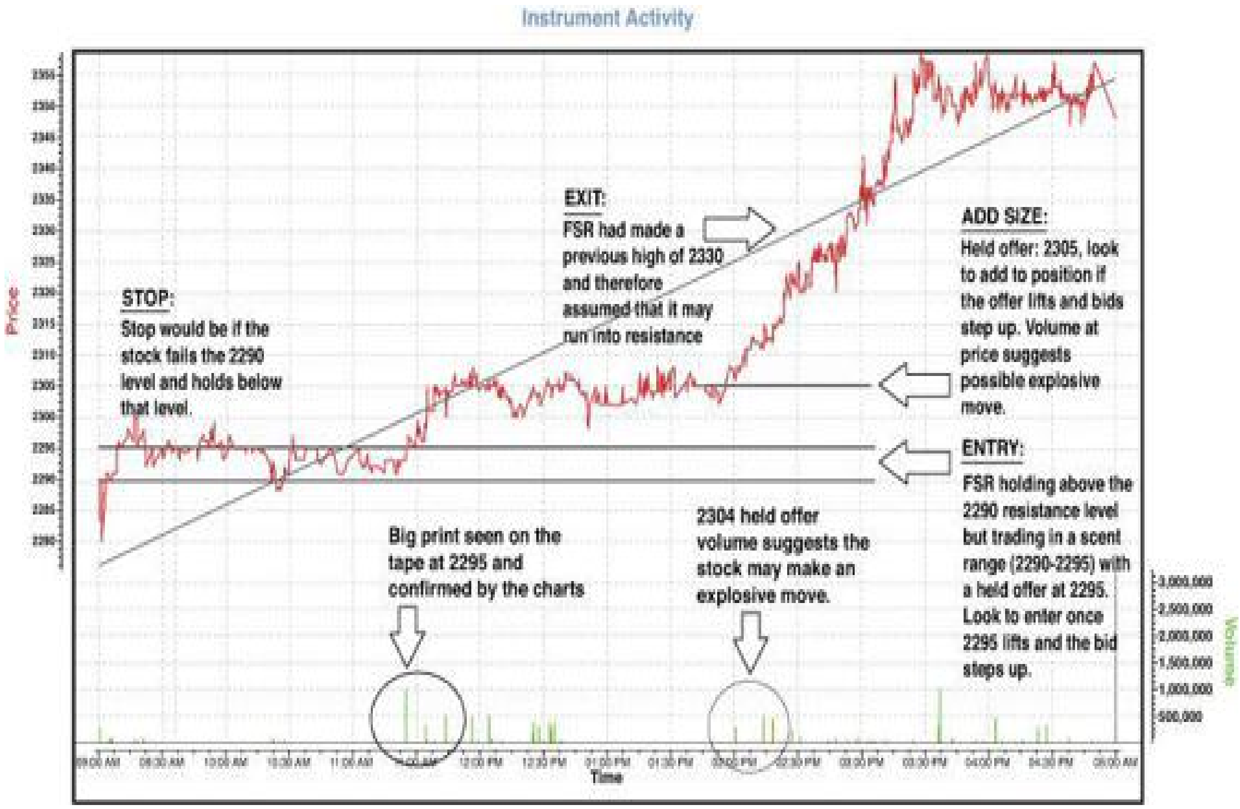
FSR had recently closed above a key short-term resistance level (2290, actual close: 2294) and had therefore triggered a technical buy signal. Further assumed resistance would be at 2330, its most recent high with short-term support at the 2250 level.

Reading the Tape

FSR opened at the 2290 level, traded down initially to 2280, but snapped back quickly and held above that level for the rest of the morning. The stock then traded in a 5-cent range between 2290 and 2295 with a held offer at 2295. A particular big print went through of 1.5m shares at 2295 and the bid stepped up to 2300 immediately, which was a very bullish sign. The offer once again held at 2305 with the stock only really printing on the offer, suggesting the buyers were willing to pay the offer price. Once 2305 lifted, the stock made an immediate 2 percent move to 2350 and held.

FSR has an average volume between 8m and 12m shares, and by midday on the particular day had already accumulated a volume of 15m shares by 12 p.m., suggesting that there was strong buying in the stock and that it had the potential to move higher.

Trade Management



Trade Review

FSR had released positive news on the day prior to market open; it had also recently closed above a key resistance level and on the day had confirmed this by holding above there. There should be no excuse that it wasn't a long as all the necessary bullish signals had been triggered.

Adding more (significant) size to the trade once 2305 lifted given how much volume was being done, there was something to learn from and apply going forward. Volume at price suggests a lot about the possible move a stock can make, and in this case it made a very sharp 2 percent move after lifting.

Presented with the same situation in the future, I would be comfortable playing in greater size in my initial lot (40,000/50,000 shares vs. 15,000/20,000 shares), as in terms of risk/reward, it was a great trade.

Carpe Diem: A Comfort for Action

> "It is impossible to live without failing at something, unless you live so cautiously that you might as well not have lived at all."
>
> —J.K. Rowling

Carpe Diem lives each day to the fullest. His core life philosophy can be summed as: If you can have fun, then you MUST have fun. On my last day in Cape Town, Monti and the boys and I hit the town. We were standing at a swank bar that felt like NYC. A bachelorette party was sitting down adjacent to us. Traders, alcohol, women: Something was going to happen next.

We had been there ten minutes and were now on our third round of smoothie shots concocted and ordered by Carpe Diem, who was growing annoyed by this bachelorette party.

"These girls are the worst. They are not having any fun. This is the worst bachelorette party I have ever seen."

Carpe Diem sent over shots, as he was personally offended by the idea of someone not having out-of-control, end-of-days fun at a bachelorette party. I got the sense he might react this way if it was just a Tuesday night book club for a group of female friends. The ladies sent back tequila shots. We drank them. Ouch.

Carpe Diem found Richie, a young, carefree, and rising Joberg trader, and ordered him to do...something to entertain the girls. (OK, let's not disclose the full story here, but let's just say without hesitation, in fact without even thinking of hesitating, Richie stumbled over and did what was ordered). Mission accomplished: The girls were now having a good time and Carpe Diem could go back to enjoying this night out with the boys.

Then there's the time Carpe Diem got us last-minute reservations at a local hot spot for 20 people. How? He called up and impersonated a local celebrity.

"What do you mean you don't see my reservation. Do you know who I am?" (as he proceeded to impersonate a local celebrity).

I am so sorry (Mr. Local Celebrity). You can come down anytime.

Table obtained.

After Stormers got over their insistence their stocks do not trend, they started spotting trend trades. One was in NPN. At a 52-week high, it took some guts to find a way into this trade and hold. It can be difficult to exit JSE stocks if you are on the wrong side of a trade. But this trader, like Iceman, has no fear. He partied with this Trend Trend Trade in NPN all day long as we present below.

A Trend Trend Trade is one of the first trades you should learn in any time frame. See this trade in NPN below.

Trend Trend Trade

Storm

NPN

February 29, 2012

Big Picture

The FTSE/JSE All Share Index was up 100 points (+.3%), and the S&P futures were also up 5 points (+.4%). On this day, all sectors were trading well, and most markets across the globe were positive.

Tencent, the Hong Kong subsidiary of NPN, was up about 2 percent in Hong Kong, and all technology shares had traded very well the previous night in U.S. trading.

The Trend Trend Trade

A Trend-Trend Trade is a trade in which the stock is trending intraday as well as long term. When these two technical trends are in alignment, the trade made in the direction of these trends becomes one with a high probability for success.

Trend-Trend Trades work well when a stock releases major news that confirms the direction of the trend. For example, if the stock has been trending down for the last two years and then releases highly negative earnings, a great Trend-Trend Trade can be made off this information.

Levels that are shared on the intra-day and long-term charts are very powerful to trade off of. Big moves may be made here, so set alerts at these levels.

Technical Analysis

The previous day NPN broke through its recent consolidation, its all-time-high, and important resistance going back 13 months.

Technical Analysis

Technical Analysis

Reading the Tape

NPN broke through extremely important resistance the previous day in decent volume, so my goal in the morning was to enter on the open for a trade to hold as long as world markets were reasonably stable. I took my first lot at 410, which was a bit of a pivot level from the previous day. The stock struggled to break through 410 for the first hour, but when it did, I added to the position. Because of the size of my position and the relative illiquidity of NPN, I didn't trade in and out too much. I exited the position on the mid-afternoon push to 415 when I felt the stock was running out of steam.

Let's meet some more Stormers.

Brody: A Pursuit to YBT

> I would sooner fail than not be among the greatest.
>
> —Keats

I walked onto the Stormers trading floor and saw that Brody was trading FSR. Brody had joined us the previous weekend at the local rugby match and we had talked some trading. In the States, when you go to a ballgame, there are concession stands everywhere with a plethora of heart attack food choices. In South Africa, locals walk around selling things like freshly made donuts and boxed cappuccino. Phillie made a huge mistake of choosing the cappuccino option. It felt like a bad trade to me as soon as he made it. Ultra-positive Phillie concurred. Standing about 6'3'' and weighing 240 pounds by my eye, Brody looks like he played some rugby and could still play. As it happens, he actually was a Silver Medal doubles tennis champion.

"Bella, what do you think of this position?"

Brody was short 25K FSR 20c from significant support.

"Get out of that position. It makes no sense. Why are you so big right in front of significant support? Save that size for when it gets below that significant support."

"You are right."

He covered.

Brody is one of the firm's top producers who likes to trade big-boy size. This is a guy who has a feel for the markets and has no fear to size up in a trade, even the tougher trades. This trader has no hesitation to pull the trigger on an All-In Trade, from our Iceman chapter. What if we took those superior trading skills on this pro's pro and got him into plays that were a little easier to handle and with way more upside? I saw it happen with GMan. GMan transitioned out of stressful trades into easier ones—and these changes have dramatically improved his performance.

For example, difficult fade trades can be exchanged for trading stocks that are moving in the direction of the market. Now, I understand the appeal of fade trades: this type of trade is based on the idea that no stock moves up in a straight line, so it's fun to try to call the tops and bottoms of mispriced moves. Spencer has written early and extensively about what he calls *the #newnormal*, a lower volatility trading market, that makes fade trading intellectually more appealing as well. Some fade trades are well worth placing risk into the marketplace. But they have to be the right setups. Too often, these fade trades are hard and stressful and often not worth an experienced trader's intellectual and mental trading capital.

The central issue here is that superior tape reading as well as entry and exit skills can be applied to better risk/reward trades and lead to a heftier P&L. Often, traders who are making money mistake their making money for finding a style that is best for them. Maybe. Maybe not. They must be cognizant of their advanced feel for the markets and superior trading skill. The question is always the same—"How good can I be as a trader?"—and not "Am I making good money as a trader?"

It was surprising to me how open Brody was to change. I would guess this is partly why he was such an accomplished tennis player. You don't reach Olympic medal status without a lifetime of pushing for daily improvement. It's also a great lesson for the new and developing trader. I should also point out that Brody (is it possible to say "Brody" these days and not think of the captivating *Homeland* character?) was always front and center during review sessions, where I would eventually hear "Hey, Bella, what do you think of this position?" before the session was over.

Brody reminded me of SMB friend Bruss, a professional futures trader in Phoenix. Bruss took the SMB Foundation because he wanted to add equities to his quiver. At lunch with Bruss and Freudberg in Phoenix, Bruss complimented our comprehensive training program, particularly finding his newfound Reading the Tape skills additive to his trading. Bruss fits our culture perfectly as he was a former elite athlete—a star baseball player, reaching AA with the Orioles. There is an important lesson here. Bruss was a successful futures trader who wanted to learn more, was willing to invest in his trading future and sought SMB out to improve his trading game. Here Brody was one of the top traders in South Africa seeking me out to improve his trading game and willing to invest more in his trading future. Remember Seth met us the same way- willing to invest in his trading future. Now he runs the options division of SMBU. Like Seth, like GMan, like Bruss, like Brody, keep investing in your trading future. Let there never be an end to your trading education.

The takeaway here is that Brody was and is still a top-performing trader with a long history of success and yet he *still* wanted to improve his game. That's the mark of a great trader: never take anything granted, never relax into routine, always be open to hearing new ideas and, most important of all, accept criticism. That, in a nutshell, is how you become a YBT: you have an unquenchable thirst to improve; you have the willingness to do the work—which includes considering new ideas and possibly abandoning old ones—and to take necessary instruction to elevate your game.

Rudders: Ultra Calm and Giving

There was this unassuming and humble guy who kept asking questions. His calm stood out on the desk. I felt like if I dumped him in the middle of Times Square, he would just slow everything down and find a path to the sidewalk. Meet Rudders, a top South African trader.

Ask Rudders why he is so calm and he answers, "I suppose years of competing in tennis week in and week out helps you deal with winning and losing." I didn't hear any stories about his athletic prowess from him. Nor did I hear from him that he consistently took money from the markets. Let's get back to this point later.

On a Sunday, Rudders, Phillie, Carpe Diem, and I climbed Table Mountain, one of the New Seven Wonders of Nature, at my request. A Sunday morning getting in some physical exercise at one of the world's treasures felt like a great start to the day. Then there would be lunch and drinks with Jules and the boys after, taking in views of the ocean at his private club. With my messed-up back and with what I can only diagnose as "elevation asthma," it took me forever to climb the mountain. Every few hundred feet I had to stop and catch my breath. I felt as though my heart was going to explode out of my body.

With his family waiting for him back home to spend the rest of the day, I was clearly holding up Rudders. In the States, this probably would have drawn a look of "Come on, Bella; let's hurry it up" from another trader. Spencer for sure would have left me by now. But Rudders and the guys couldn't care less. We got to the top when we got to the top. Carpe Diem and

Rudders looked as if they could have run to the top of the mountain, but they were fine waiting for me.

Toward the end of my trip, I learned from another trader that Rudders was actually probably the best trader at the firm. Where did that come from? Rudders would never tell you this himself. I would learn he also was a very high-level tennis player after one of his buddies who had just played in the Olympics came by for a visit. Seriously, didn’t any of these guys have friends who worked at the local Walmart?

And that NPN trade? Take a look again at the chart provided previously. Rudders crushed it. He was big and holding and completely calm about his size and open profit. During this trade, I walked the desk, giving input and watching traders handle this prosperity. There was no thought of “Bella, where do I sell?” from Rudders or “Bella, where do I lighten up?” No. This was a Trade2Hold, and with his ultra calm, the only thing Rudders was thinking was “Now, where should I add to my position?” Brilliant!

Some say that those naturally calm make for the best traders. Rudders would on a prop trader’s Mount Rushmore of calm.

One more quick observation about Rudders that is also so true of Shark. I shot Rudders a few emails for help on this chapter, and he responded promptly. I have been known to circumvent Shark’s normal review process and ask him for something special and specific that I can then share with the desk. For example a LULU options trade special request from me or an example of an All-In trade. I am not sure what it is. GMan is this way as well. In fact, this is true of all of the top traders in this book. If you ask them for help, they help. They enjoy the process of work. If as a trader you ask them a question after the close, they sit and are generous. Good traders are givers. In this giving, they are learning, working on their game, internalizing the best of their trading. Give like Rudders, and you will become a better trader, with the added benefit of being a better person.

JoeBoy: The Natural

Months after my visit to South Africa, our wives, JoeBoy, and I sat at Abe & Arthur’s, the hottest restaurant in the meat-packing district of NYC, letting our wives talk about things interesting to them while we talked about —you guessed it—trading. JoeBoy briefed me about his recent in-the-money AAPL position. I briefed him about a recent-out-of-the-money trader we were backing. In my writings, I have discussed how I am not impressed by natural talent, as trading is a skill developed through concentrated practice. But I have to say that JoeBoy might just be an outlier.

While I was in Cape Town, there was a buzz during an after-market cocktail hour that JoeBoy was seriously in-the-money in some gold buy right after the market close. This news could not be confirmed, and traders were asking other traders for confirmation, like CNN reporters. It was. JoeBoy made $22K on gold and silver contracts in about 15 minutes on the day right after we had a non-farm payroll number. Apparently, this happens often.

JoeBoy archived this play in SMB PlayBook form here.

Precious Metals Fundamental Play

JoeBoy

February 29, 2012

Big Picture

At 9:00 a.m. on Wednesday morning February 29, 2012, Ben Bernanke was due to report the Feds' semiannual monetary policy report to Congress. This was a day that the market had been waiting on for some time. U.S. economic and jobs data had taken a turn for the worse at the end of 2011 and the beginning of 2012. Because of this, markets were really starting to price in the chance of the Fed coming to the table with some sort of stimulus, potentially in the form of quantitative easing.

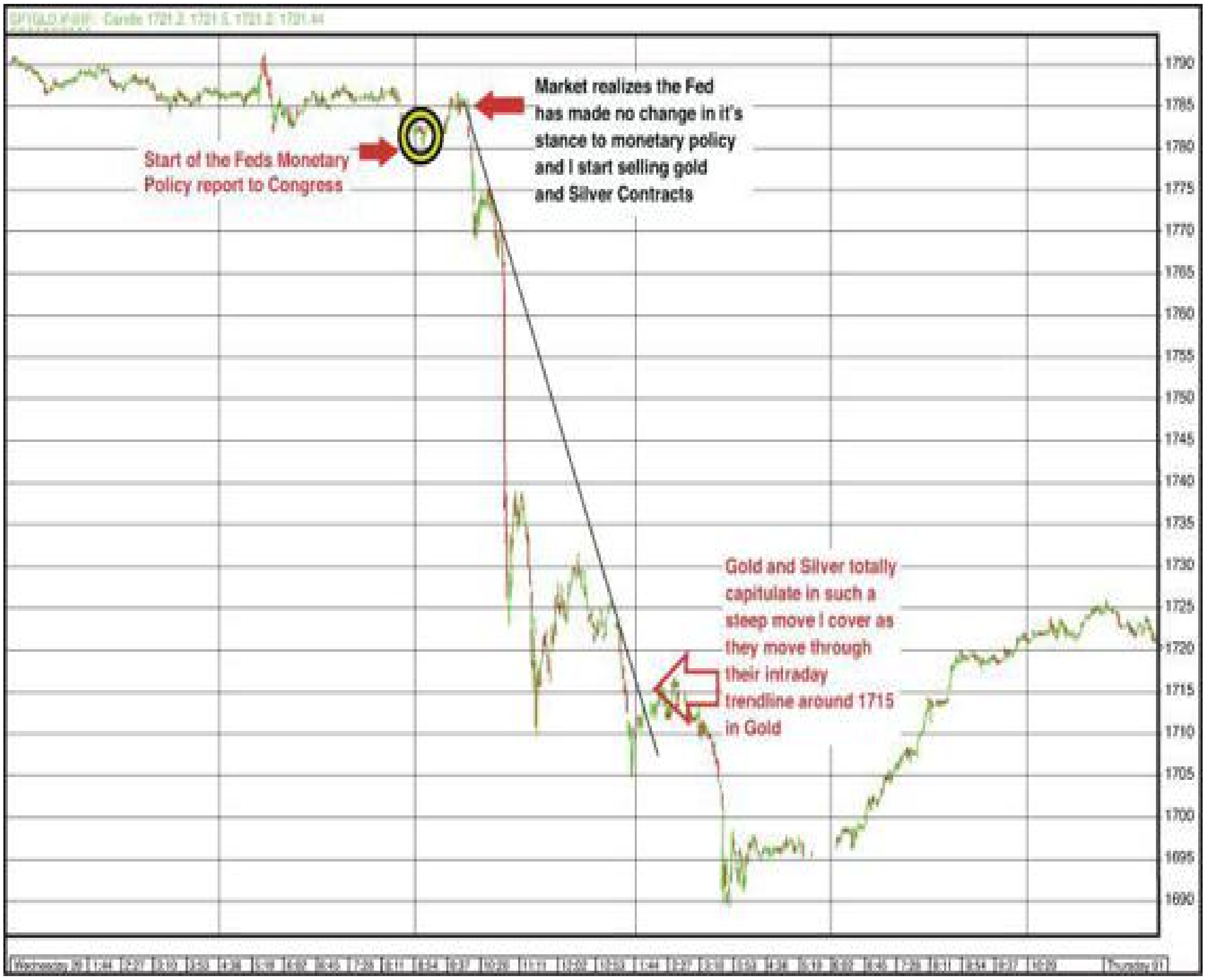
Over the previous couple of months, price action had been very bullish in the precious metals space because of the potential of quantitative easing lingering. Therefore, there was great expectation on Bernanke changing policy to something more stimulant.

Intraday Fundamentals—Nothing particular was happening in the precious metals markets early on. They all seemed to be in a sort of wait-and-see mode. If anything, gold seemed to be struggling to break above 1787.

Trade Idea

Due to all of the recently poor economic and jobs data in the U.S., the market had built in the expectation of some sort of Fed stimulus. This was the contributing factor for the gold price running over the previous two to three months. I knew there was very large speculative interest open in the precious metals futures markets, and if the Fed didn't make a change to their stance, that most likely it was going to force the specs out.

If the Fed doesn't give the market what it's looking for, I'll use that opportunity to sell short the precious metals market. Typically, it takes the precious metals market longer to react than will the S&P future. This allows precious additional time to put my trade on.



Trade Review

I sold short two contracts of both gold and silver within seconds of the announcement. I had this plan in my head hours before the meeting. If the Fed didn't make an adjustment to their previous stance, I was going to short several precious metals contracts.

I entered this trade on a fundamental basis, knowing that the fundamentals of the trade should drive it lower if the market didn't get the result it was looking for out of the Fed.

After entering the trade, I waited for trade action to confirm my theory that gold and silver should sell off.

Gold and silver capitulated so quickly, it made it difficult to add to my trade at levels where I felt comfortable selling.

My next decision would be on where to cover. This decision was made on a technical basis and not a fundamental one. So I entered the trade because of fundamental reasons, and I exited my trade because of technical reasons.

As you can see by the previous chart, we entered a very steep sell-off. I used the gold price moving through its intraday trendline to exit the trade.

JoeBoy reminds me of my old friend Mr. Boo, whom I traded with “back in the day.” Mr. Boo was notorious for getting amazing fills and was well in-the-money before you even saw the stock as strong. JoeBoy was Storm’s best-trader-turned-partner who began to trade less in order to grow the business. Nevertheless, he was always checking his positions for American stocks on his iPhone. His attentiveness toward the American playing field led him to see how the firm was giving away money by not capturing the big trending plays. He wanted this to stop.

After Rudders and Carpe Diem caught the NPN for serious profit, JoeBoy expressed his gratitude that I had been around. He caught on quickly that not only had these two traders made more by holding and being big in the position, but they didn’t fade the move as they usually did (well more accurately as Carpe Diem usually did). Instead of a memorable gain for these traders, it could have been a huge rip fighting the continuing trend. This is the danger of fading very strong stocks. And it can be demoralizing for traders to see a missed opportunity to go long. The muttering under their breath starts. A banging of the desk can follow. Perhaps even a slamming of the firm door and a loud cuss trailing the exit. A few traders who get down like this can drown a firm in regret and negativity. Worse yet, better traders, regretful of a missed opportunity, can actually demoralize an entire firm if their regret spreads to all the other traders.

As for me, my trip in South Africa was a wonderful learning experience, and as is always the case with me, I was happy to help!

During my last day with Storm, the founder toasted me for my contribution over after the close spirits. I thanked him for his kind words and spoke from my heart, “This experience with you exceeded my highest expectations. I consider you my friends and hope you do as well. Trade well!” Then we joked about a future trip to Vegas as male traders do. The biggest compliment and reward I received are the emails that come in from time to time from my guys at Storm.

So what's the larger takeaway here? Easy: The PlayBook can be applied to all markets. No matter how tempted you might be to think otherwise, markets are markets. There's a universal trading psychology that applies to all of them. The temptation of a bad trader—perhaps I should be fair and say the unseasoned or untrained trader—to short when you should go long exists everywhere. By the same token, great traders are all alike in the sense that their passion, willingness to invest in their trading future and relentless dedication to learn more and to become better than they currently are is universal. Whether you are a trader in Singapore, London, Russia, Brazil, Australia, or Hong Kong, you can be sure the mindset of your market's great traders is the same: They find the setups that make the most sense to them, then internalize this knowledge, get bigger in their best setups and then act—trade—on it. This is your path to becoming a "proper" trader.

Conclusion. The Future of Trading

> I am not bound to win, but I am bound to be true. I am not bound to succeed, but I am bound to live by the light that I have.
>
> —Abraham Lincoln

Remember where we started? My dad had a stroke and we lost my mom, her brilliant presence. Some of our better traders were poached. The SEC requested hundreds of pages of documentation about us while investigating another firm, a capital and brain drain. Admittedly, SMB was, for the first time in our history, heading in the wrong direction at best and much worse at worst. I couldn't trade or go to the office full time. With the addition of time and perspective, Keats provides us comfort during such peril:

> Do you not see how necessary a world of pains and troubles is to school an intelligence and make it a soul?

Those were some difficult and disheartening times. While I miss my mom terribly each day and that will never go away, things are getting better, and we are making progress again.

Buster Olney, author of *How Lucky Can You Be*, ends each of his aggregator baseball blog posts with

> And tomorrow will be better than today.

Professor Seligman taught us that optimism is a learned skill with opportunity often right in front of us after dishevel. Each offers wisdom to inspire our trading work and life.

Remember that meeting in the Southwest with a potential strategic trading partner, with me grabbing at that undersized dress shirt not an hour old? After 18 months of negotiation, we completed a deal. Today SMB sits in a joint venture (JV) with a deeper-pocketed, proprietary trading technology leader. SMB is responsible for training all of its new and developing traders (and thus ensuring continual and profitable new blood into our venture), coaching and managing bigger NYC traders and SMB traders, and finding trading models to back for our NYC office. During that perfect storm where we were not at our best, we rebuilt from our strength, and we showed we could build profitable traders during a period when others couldn't. Our prop desk sits in a JV exactly where we want it:

1. We back discretionary, experienced traders, taking all downside risk.

2. We back automated trading models.

3. We teach, coach, and mentor traders from scratch and fully back them after sending them through the right starting process—our college training program.

4. Our discretionary traders are bionic with state-of-the-art proprietary scanning software and quant support that ensures they are alerted to all of their favorite custom setups. And they have management tools to exit more positions.

5. The JV possesses technology that enables our discretionary traders to create automated trading strategies without the need to code and with the support of quants.

6. Equities, options, FX, and futures strategies are welcome.

7. Absolutely no commission markups apply to the traders. We are their trading partners and only split profits.

Our trader education arm is booming. SMBU continues to grow; we now have or are very close to having partners in South Africa, China, Singapore, London, Russia, Israel, Canada, Spain, Argentina, Colombia, Dubai, Brazil, Nigeria, Poland, and Mexico. We have added The SMB Options Tribe, a growing community, which by the end of 2013 will be the premier options education provider. We have added FX. SMB Systems, our newest enterprise, teaches those with an interest in how to build auto-trading strategies and happily backs those with promise.

In my personal life, my wife and I are expecting our first child. I walk around repeating the line from classy winner Payne Stewart to Phil Mickelson after he beat him at the U.S. Open: "You are about to be a dad!" My wife and I moved into a newly renovated apartment on the Upper West Side, seeking more space, safety, and amenities in anticipation of our first child. We are having a boy. My dad, with the heart of a lion, keeps improving. Today *is* better than yesterday.

All of this has been a long, difficult slog made possible only because of great partners like Spencer and GMan and the good fortune to team with high-character, elite peerformers like Shark, TO, Pippen, Prep, Iceman, and yes, even Rudy. I share these stories so that you know we all get knocked down in this game and must get back up. Firms don't have all the answers. Traders struggle, even those who become CPTs. Trading is not easy. CPTs struggle to be YBTs. So now you know the truth about the path to trading success. We all have to keep working at it. Trader Disneyland, where the uber-bright become millionaires because they are smart and where trading is only about clairvoyant market calls, does not exist. We all will have some very difficult periods that test our commitment and perseverance. It is okay to fail. Remember what Dalio taught us, "Weakness doesn't matter if you find solutions." Just be mindful of the next pivot you might have to make. Keep after it.

How You Can Become a Profitable Trader

If you are a new trader, follow the Path of Pippen to give yourself the best chance of success. Better yet, be even smarter and start learning early like our former intern, Special Projects. If you land a chance on a pro trading desk, work like TO and Shark. If you are a CPT but want more, consider whether you are taking on enough risk with your best setups, like Iceman does. If you are underperforming as a trader, remember Prep; there is a solution to all of your flaws and focusing on your strengths is always the best way forward. Or perhaps you need to take a time out like Rudy, *like me*, and work on yourself first before you can succeed. Or perhaps you just need a refresher in your trading fundamentals like our friends in South Africa, and SMB at times, so start building a PlayBook of your best setups. If you are really good and want to be a YBT, remember GMan and Brody, the importance of great coaches, and remember that you will have to keep working to improve and adapt your trading methodology. For all the above, build a PlayBook that makes the most sense to you; after all, this is your business.

Discretionary trading skills are being undervalued and just might be at the bottom. Allocators overvalue anything quantitative. Discretionary traders can better tap into their skills and exponentially monetize them by embracing new technology and opportunity. The good news is the future will be better.

Doing research for a speaking engagement in Canada, where I was the chairman and responsible for the opening remarks, I was surprised to learn how badly most HFT firms are struggling. I differentiate HFTs from auto-trading because I consider HFTs those implementing high-speed scalping strategies. Lower volatility, increased costs, threat of regulation, and lower volumes have forced many HFT firms to cut back as they struggle to survive or even to close shop. The world is becoming more connected such that traders with skill will have more opportunities. Trading education is expanding such that other products can be learned virtually or in-house. Software has been developed so that discretionary traders can build automated trading strategies without the necessity to code. Tools are available for discretionary traders to be more bionic and dramatically improve their P&L.

There is an exciting path for the new and developing trader. It is different. It is not just "become an intraday trader and get bigger." It is not "learn one product and get bigger." The future is to learn how to trade. Take two years (where are you going?) and really learn how to trade. Develop your PlayBook. Get big in your A+ setups. Then slowly work on adding plays to your PlayBook with small size, while you are sure not to miss your A+ setups. Then dabble, expressing your best trading setups with others products. Then test your strategies in other markets (coming soon). Next build auto strategies to add another revenue line to your trader P&L. Develop a goal of never missing any one of your A+ setups by building these auto strategies. Become a multiproduct, multimarket, bionic discretionary quant trader. The perfect path is to start young and build skill before you ever turn pro. This is the future path to becoming YBT.

Trading is about building from your strengths, doing more of what you do best. For the abstract thinker and *Les Miserables* fans: "A river's just a river." Well, how do you know what you do best? You start building a PlayBook of the setups that make the most sense to you. You do not do this just by replaying your trading day in your head or just banter with your trading mates and call it a day. You sit down and document in substantial detail the trades that made the most sense to you each trading session. You start to compile *your PlayBook.* If you haven't started doing this before reading this book, start now.

From your PlayBook, ferret out the A+ setups. Take these setups, place them in a binder, laminate them, and review them before each open. This is your business. You are in the commerce of extracting as much as you can from the market for these setups. Actually, the words of Steve Jobs are appropriate here:

> Your time is limited, so don't waste it living someone else's life. Don't be trapped by dogma—which is living with the results of other people's thinking. Don't let the noise of other's opinions drown out your own inner voice. And most important, have the courage to follow your heart and intuition. They somehow already know what you truly want to become.

How can you trade more setups like this? Should you invest in filters/alerts software to find more opportunities? Should you join a prop desk where ideas are shared through call-outs or proprietary technology yields more of your best ideas? You develop your system to cover as many of these trading opportunities as you can handle. And then you get bigger with these setups. Slowly and patiently, seek to raise your risk in these trades. We discussed risking 30 percent of your intraday stop as an intraday trader or 2 percent to 5 percent per A+ trade if you are a swing trader. These rules are up to you. My suggestions are guidelines. But you must develop hard and firm rules to get the most out of your trading and be scalable.

Let me add emphasis to one idea mentioned previously: You have to stop missing the opportunities in your best setups. With the advance of technology, you have no excuse to miss your best trading opportunities. This is a performance game. Either you maximize your take from the setups that make the most sense to you or at best you underperform and at worst are eliminated by Mother Market. I was on a phone call with a top U.S. equities trader and Spencer, whose trading we back. He has traded for 15+ years. He summed up this point absolutely for today's trader, "In these markets with computers and everything, you cannot miss the easy setups. You cannot leave that money on the table." Amen.

For the new trader, hear the market truth: Trading is a journey that will require many years to become competent. First, learn if you love trading. Spend some time at this discipline, whether working as an intern, doing simulation or demo trading, getting trader education, or so on. The first question you must answer is this: Do you love trading?

Next comes choosing the right markets and products. Expose yourself to different trading vehicles and markets while trying to determine your best instrument and time frame. You do best when your talents blend with your passion. If you do not have the mind to momentum trade, then don't.

After you sort this out, start to attack your best product and time frame with the commitment of a pro. We do the best we can at our passion because what else is there? Develop a basket of setups, through live trading and error, review, mentorship, coaching, and self-reflection that make sense to you with the creation and upkeep of your PlayBook. Co-opt the trading strategies of others, but do not copy. Charlie Munger, vice chairman of Berkshire Hathaway, said, "I believe in the discipline of mastering the best that other people have ever figured out." Learn from those others, but make their trades your own. Keep adding profitable setups to your PlayBook. Never stop.

One of my favorite e-mails from a prop trader went like this:

> The day you quit working on your game both mentally and physically is the day your career comes to an end.
>
> I have suggested a way for you to structure your trades with The PlayBook:
>
> The Big Picture
>
> Intraday Fundamentals
>
> Technical analysis
>
> Reading the Tape
>
> Intuition
>
> Trade Strategy
>
> Trade Management
>
> Trade Review

If you believe this template will work for you, please use it. I hope that you have learned valuable trading lessons from exposure to how we archive our best trading setups and our review of them. How you think through trades is most important. Understand that some trades will work, but then not. However, the art of thinking through your trades and the acceptance that you will have to pivot to new strategies during your trading career will allow you to sustain as a trader. There is no destination for the trader; there is only the perpetual challenge to learn and improve.

You Are a Multiproduct, Multimarket, Bionic Discretionary Quant Trader

Hurricane Sandy ravaged NYC and KO'd our office for three weeks in late 2012. SMB had to move three times to temporary offices during this outage. As a result, a diner near my new apartment became my new office. Across the booth from me, sipping bad coffee, was a prop firm head from Dubai who funds a small desk of mostly seven-figure bond, equities, and derivative traders. I was his first appointment after his flight halfway around the world and crazed taxi driver ride into NYC. He was frustrated.

"One of our better traders banks about $500k with one strategy. Here is how he does it. He finds a U.K. stock that reports bad news. Then he finds a corresponding stock. When that stock spikes during the day, he shorts it big. I keep telling him to try this technique on U.S. equities because it has so much more opportunity, but he will not listen."

One of my good friends who runs a very successful prop firm explains this old trader attitude succinctly: "It can be very difficult to get older traders to change." This keeps the experienced pro trader from YBT status.

If you ask a successful trader what he trades, he might respond as follows:

> I trade U.S. equities.
>
> Or
>
> I trade Australian treasuries.
>
> Or
>
> I trade municipal bonds.
>
> This response is too small.

Instead, consider this:

> You are a momentum trader.
>
> You are a mean reversion trader.
>
> You are a relative strength trader.

You can be, and that trader described earlier should be, a Global Bionic Pattern Trader. That $500,000 can become seven figures.

Bionic trading tools can arm you with more opportunities and the ability to manage more positions.

You can learn to better express your best trading ideas with different products, such as options.

You can express those ideas with auto strategies and expand your game to discretionary/auto-trader. Seven figures can be mid-seven figures.

You Can Be Better Tomorrow Than You Are Today

Please remember during this jaunt that trading is a game. Trading is a privilege.

Do not think of trading as success or failure, but rather as you finding out how good you can be as a trader. What a worthy pursuit if this is your passion. Remember these words from Abraham Lincoln:

> I am not bound to win, but I am bound to be true. I am not bound to succeed, but I am bound to live by the light that I have.

Your light is your passion. Be grateful to have found it, water it every tick of your trading life, and let your trading reflect your best you.

Keep rehearsing your trading game! The words of Bill Bowerman, founder of Nike and legendary track coach memorialized in the brilliant film *Outer Limits*, may help you understand what you are really doing while training to be your best trader:

> Running, one might say, is basically an absurd pastime upon which to be exhausting ourselves. But if you can find meaning, in the kind of running you have to do to stay on this team, chances are you will be able to find meaning in another absurd pastime: Life.

I sincerely hope that you find meaning in the pursuit of striving to become your best trader—and along the way learn trading's and this book's true lesson: You *can* be better tomorrow than you are today!

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