

2 TRADERS

[EP22: Being Wrong](#)

Walter: Being wrong shouldn't be a problem, and in fact, if you really look at the math behind it, what you'll notice is that the traders who get paid the most are also wrong the most.

Introduction: Two traders, Darren and Walter, pull back the curtain on profitable trading systems, consistent money management, and profitable psychological triggers. Welcome to the [2 Traders Podcast](#).

Walter: Welcome to the [2 Traders Podcast](#). I'm Walter Peters, and we've got Darren on the line, and Darren and I today, are going to look at this idea of being wrong and whether or not this is something that we should try and avoid, or if there are some hidden side effects to being wrong and what this may do for your trading. Here's the idea. Part of this goes back to what I learned in psychology about children, so Darren, obviously as you know, got a little bit of a background in psychology, and I went to school for a long time to get these psychology pieces of paper and one of the things I learned when I was doing my PhD was about how children, and we'll probably get more into this in the later podcast, but the main thing I learned from studying children was that children are okay at taking a stab at things.

Whereas by the time we get to adults, we sort of have this idea that we don't want to be wrong, and we do a lot to avoid being wrong. What this means is, we often stop ourselves from success and I'll give you an example of something that I heard on a TED talk and I thought it was just brilliant. The guy was talking about children and this idea of how children will just go for it, and this is one thing that I learned when I was doing my dissertation in psychology with little kids, was that they would definitely take a stab at it. In fact, in some ways, children are trained to do so. They'll just blurt out an answer, and if they're wrong, they'll go with another one. Basically, what this guy said was his son was in a play which was the Jesus in the manger sort of situation, so Christmas morning or whatever. His son was playing Joseph, and as you know, the Three Wise Men come to see Baby Jesus, and they bring their gifts. Frankincense, myrrh, and was it gold? Darren? Was that the other one?

Darren: It was gold, yeah.

Walter: It was gold, right. I want to get my story wrong ... I want to get it right, so I don't want to get it wrong. The Three Wise Men show up, with frankincense, myrrh, and gold, and the first wise man comes up and says, "I've come to bring you gold." The second wise man comes up and says, "I've come to bring you frankincense." As the story goes, of course the Three Wise Men come bearing gifts. Now, what happened during the play was the little kids got out of order, so they messed up the order. I think the way that it was supposed to go is one brings myrrh, one brings frankincense, and the final wise man brings gold, but they got it out of script.

What instead happened was, the first wise man showed up and said, "I've come to bring you myrrh," and he gives Joseph and Mary, and Baby Jesus myrrh. The second wise man comes over and says, "I've come to give you gold." Then, finally, the third wise man shows up and says, "Frank sent us." Of course, the kids got it messed up, and forgot that it was "frankincense," and not "Frank sent us," but the idea here is that the kids took a stab at it, and they will go for it, and that's some of the reason behind that is why, as adults, we lose our creativity, and you hear people say things like, "I used to be really good at drawing, and now I'm no good at it." "When I was kid, I was good at this," or whatever. It's not really, I don't think, that we were better at it back then, but back then we didn't care about being wrong.

I think this extends to trading, Darren, and here's why I think this is true. I think that as traders, it's clear that the most profitable systems in trading are mathematically, if you just look at it objectively, are those in the case that you're often wrong. In fact, much more often wrong than not, and yet, as traders, and myself included, we're much more drawn to those strategies that enable us to be right most of the time. In fact, some traders will argue with you, as long as they're right more than they're wrong, they're going to make money. Which, of course, is not really ... It's sort of missing the picture, which is it's all about risk management, it's all about what you're risking and what you're getting, and that interaction with how often you're correct.

I think that this idea of being wrong is something that drives us towards certain trading systems. Again, I'm not immune to this. I do the exact same thing, because I know psychologically, I'd prefer to be right, but my question you for, Darren, is if we were looking at things slightly differently, maybe from a child's point of view, where we're okay with the idea of being wrong, would we make more money? What are the implications of that? Can we change our thinking so that we're okay with being wrong more often? These are the sorts of things that I think about when I think about can traders adopt a different mentality and allow themselves to be wrong.

Darren: I think definitely, it's one of the key problems that traders face, this fear of being wrong and especially losing seems to plague our trade in many aspects. I think it goes back to this mindset thing that we've covered. We've talked about before, where we're solely focused on the outcome of individual events, rather than being able to look at the big picture, and being able to sort of focus on the method we're using. We'll go away and test a system, back test it, for hours, to see that it's profitable, but then, we find it very hard in the moment to stick to that as soon as we start losing. We seem to sort of take a massive knock from losing, even though in our testing, it says that we are going to lose. What's interesting for me is something must happen between that period of being a child and adult where we kind of obtain that fear of being wrong and I think it's about being judged by other people, and being sort of marked down and our own sort of self worth.

Somewhere, we are having that ability to have that sort of growth mindset drilled out of us, and I think a lot of it comes from the way that we're educated, and how we're brought up. I think we're kind of taught it's all about winning, isn't it? It's not about whether you did everything you should, but you came in fifth place or something. It's not about that. It's about winning a medal, being first, second, or third, and nothing else matters. It's about getting an A in math. It's about excelling in something, and it's about success, and not mastery. What we should be focusing on is not about being right, it's about being able to have those near misses and come back every day and persevere until you get it right. I think that is kind of drilled into us as we grow up.

Walter:

I agree. I think you've nailed it. I think what happens is, basically they break us down, don't they? That's what schooling is all about. They teach you what the rules are, how to grow inside a certain box, so you get a little bit of leeway, but you're not really meant to get out of that box, and I think that what you're talking about is sort of also the reason why we lose our creativity. It's interesting to me that I've heard from two traders in the last year, and one trader told me how amazing trading is, because you can be so creative with it and you can pull things together, and snap them together and they're like Lego's and snap them together and create whatever you want, and there's so much creativity available. Then, another trader, just recently contacted me and said, "You know, really trading, there isn't much you can do in trading. It's very restricted. There's only moving averages, and this and that," and so you have two different perspectives, two different traders seeing the exact same thing which is, "How am I going to build this system?," and they approach it so differently.

I strongly believe that the reason why we lose our creativity that most of us have an abundance of, putting things together, creating new ideas, because we're not afraid to be wrong. We're not afraid to be wrong, so we'll go ahead and have a go at it, and then when we get older we learn, "Well, you don't want to do that, because you don't want to be wrong." To me, the real tragedy of schooling is that essentially what it does is it teaches us what not to take a stab at, right? It teaches us where we shouldn't really break out and try something new. If you look back in just even in science, some of the discoveries in science that were made by people. Child psychology was created by a biologist, and you go back and see the major discoveries in science, they're almost always made by somebody from outside of that field. The reason why, of course, is they don't know the rules of that field. I think trading's the same way.

I think what you're talking about, Darren, is true. We need to get to the point where it's okay if we are wrong and it's okay to try and test things. For example, most of the things that I test in Forex Tester, just don't work. They fall by the wayside, and they don't go any further than Forex Tester. Occasionally, things will make it out of there, and into a demo account, and sometimes those don't even work, but I guess the point is, what I'm trying to do is be creative and look at things from a different way. Why use a moving average as a signal for an entry when you could use it as your trailing

exit? Things like this. These are the sorts of things that I would encourage you to do, and certainly if you look at other fields like sales, some of the best sales people on the planet will tell you that one of their secrets to their success is understanding that every time they get a no from somebody, that just means they're closer to a yes, right?

These are the sorts of things that I think traders can take, as well. It may seem like it's a big stretch to go from selling insurance to taking trades on the Euro, but I don't think so. I actually think that they're closely related, and I think that if traders begin to get to the point where we can be okay with being wrong, whether that's being wrong in trying to create a system, or being wrong in a particular trade, I think that we can grow from that, and I think that there's more to be learned from being more creative, and taking a stab at it, than there is being stuck in this box and thinking, "Well, I've got to use moving averages and support resistance because that's what the banks use," or whatever. That sort of thinking, to me, is restrictive, and doesn't allow for you to grow.

Darren: Yeah. I think another problem with trading, as well, is it's never black and white. I think we're always looking for a rational reason for our decisions, and often there's not a clear reason. Is a trailing exit better than a timed exit? Well, it depends on what the market does after you enter. A lot of our decisions are like that in trading. It's not as clear cut as being right and wrong. You weren't right on that occasion. It's how you perform over the long run, and not just that one individual decision. People ask me a lot for definite answers. "Is this time frame better than that time frame?" Well, over certain periods, it may well be, but it's not always going to be. They're always be that level of uncertainty. If you have this expectation where when you're really good at trading, that means you're not going to be wrong, then that's where you're going to come unstuck.

Whereas, if you're realistic, and you're expecting to be wrong a percentage of the time, and you can take that on and go forward with that, then you're much more likely to be able to follow your method, and your system, and trade consistently.

Walter: Yeah, absolutely, and I think that you've spurred another idea when you say uncertainty. I think that's the key to it. I think that, and I'm glad that you said that, because to me, that's really what's going on here with being wrong. When we're older, we've learned the rules, and we know with more certainty, what the right thing to do is, and when we're younger, things are so wide open and we don't know what's going on, there's so much uncertainty, that's why we take a stab at it, and yet, now as traders, infinite uncertainty. Who knows what's going to happen? Is the Euro going to fall 500 pips today? Is your broker going to go broke and you're going to lose your trading account money? Will the central bank step in and change the game, right? All of these things.

Is there going to be war? Is oil going to go up? Whatever. I mean, all of these things that we're thinking about, wondering, "What's going on here?," we have no idea as traders, and that's what we get paid for. We get paid for taking a risk in the face of uncertainty. We've talked about this before, about the idea of we create these little systems and reasons why we're taking a trade, and we support that with our own thinking, and our own patterns or whatever it is that we rely on, but the key here, I think, is uncertainty, and I think that if you can acknowledge that as a trader, you're getting paid for uncertainty, then you should be okay with being wrong.

Being wrong shouldn't be a problem, and in fact, if you really look at the math behind it, what you'll notice is that the traders that get paid the most are also wrong the most. Generally speaking, those traders that have huge, fat accounts, and make much more money per dollar at risk than anyone else, those are the traders that are okay with being wrong. Of course, they also sit on their trades, but that's another podcast, isn't it? I guess, to me, the main point here is this idea of uncertainty, and how being wrong is related to that.

Darren: Yeah, definitely agree, and I read ... I don't know if you know Denise Scholl. She's done a lot on sort of neuroscience and how we make decisions, and in one of her blog posts, she made a really good point about don't be afraid to make mistakes, because the mistakes you make, you learn so much more than when you get everything right, because when you get everything right, then you pat yourself on the back, you get a little bit too cocky, and a bit self sure, and then you tend to make mistakes following that. Whereas, if you can make mistakes, and get things wrong, and still go about things in a methodical way, you'll learn a lot from that, and that will serve you better in the long run, so yeah, don't be afraid of it.

Walter: Absolutely, and the research that I've seen says the same thing about entrepreneurs. The entrepreneurs that just go for it, and don't hold back, and don't wait for everything to be perfect, those are the ones that accelerate their learning curve, and their business along with it, because they're the ones that are just doing it, and then learning, and then re-doing it, and then learning some more. One of the things that struck me about reading some of the market wizards is how those traders often can point back to an early trade where they made a huge mistake, and that was sort of the catalyst for them to change their whole approach to trading. That set them along the right path.

Contrast that to myself where the first night that my friend and I traded Forex, back in, I think it was 2000, we tripled our account the first night, and that was the worst thing that could have happened. It was the absolute worst thing that could have happened, because it set me off on 4 years of failure, but you know, it's just one of those things that, I guess, I had to learn my lesson the slow way. I really wish that we would have lost our account that night instead of tripling it. We did lose our account about a week

later, but that was a different story. Darren, I guess if we're listening to this podcast, and you think, "Okay, that makes sense. I understand. I want to be able brace uncertainty and be okay with being wrong." I don't think that necessarily means that, for a listener here, that you need to change your trading system. I think it just means you need to look at things a little bit differently because you do learn a lot from your losses.

Your losses are going to teach you a lot. Being wrong is going to teach you a lot. Being wrong about developing a system will teach you a lot. For example, when I first started testing systems, I thought that the entry was the most important thing. Now, I've come to believe that psychology, position management, and then exits, probably in that order, are the most important thing, and that the entries can literally be random. The entries, I believe that anyone can take a coin as an entry system, flip it, heads, tails, and make money. I really believe it. In fact, I've gotten to the point now where I've said this enough, and enough students have done it that I need to go ahead and set up an account and just do it, so that people can see this, because it's true. I guess what I'm saying is, if you're listening to this podcast and you think, "Oh, that makes sense to me. I understand this idea, but how do I embrace it?"

What I would suggest to you is perhaps one way of attempting to be wrong more often, is just to give it a go. Even if it's just in Forex Tester, test an idea that seems crazy to you, or like the idea that I just gave you, which is who cares about why you're entering the market, why you're buying or selling, but instead focus all of your energy on the exit, right? Something like that, where the entry literally doesn't matter. You could also do things like instead of using ... Like for example, some people say, "Well, I'm not going to trade when the news comes out," right? Well, what if you actually opened up a demo account, and every time the news was released, you took a trade, just to break out of your mold, just to see what you could do, so every time the CPI or the jobs report, or the interest rate analysis for that particular country is released, just take a trade and see if you can do that.

One thing that I also did once in a webinar was, we had everyone agree. We were looking at, I think, a one minute chart or maybe like a five minute chart and I said to everyone, I said ... I'm pretty sure it was a one minute chart. I said, "Where do we think that the Euro is going?" I waited until we had an agreement, most of the people in the webinar said, "Yeah, the Euro's going to go down. Look at that. It's falling like crazy." Which of course, you can always make a one minute chart look like the GFC. I did that and as soon as everyone said, "Yep, it's falling. It's going. It's going to fall off the cliff," then we bought it, and then we came back to it at the end of the webinar, and it actually made money. There was very little drawdown, maybe like 5 or 6 pips, so these are the sorts of things that I'm talking about when I'm saying, try and just break out of your thinking, and attempt to be wrong, because I think that what you learn from that is invaluable.

What about you, Darren? Do you have any tips for people listening, in terms of what can we do to expand our horizons and get to the point where we're okay being wrong, we're okay being more creative, we're okay learning from our mistakes? What can we do for that?

Darren: I think if you're perhaps one of the traders who's perhaps happy with your system, but you tend to sort of take your losses badly, so when you're sort of wrong, you traded your system, and you take that really badly, and I know how that feels. It feels really bad. When I have a losing day, I hate it, really hate it, but I used to go through a cycle of then taking a long time to recover from that, because I'd then kind of tweak my strategy a little bit, and then have sort of a spree of losing, because I'd change things, and then I'd get completely muddled, before eventually going all the way back to the original strategy I had, and then thinking, "Oh, God. Why didn't I just stay here in the first place?" What I would say is, when you've been wrong, and you've had a losing period, have some sort of blocker before you change anything.

The best one I've ever read about was the one where if you're going to make a change, you have to get a pen and paper, and write down what you're changing, and why. Something weird happens in the brain then, and before you know it, you realize that you weren't actually wrong, you just had a losing day, and actually changing your strategy is wrong, and then it kind of blocks you from making that bad decision. That's a little nugget I take away from it.

Walter: Great. That's an excellent one. Thanks for that, Darren. We will see you in the next podcast. Take care.