EP139: Trader vs Charts Part 1 of 2

Walter: And I find that I often make really, really poor decisions when I'm watching...

Announcer: Two Traders, Darren and Walter, pull back the curtain on profitable trading systems, consistent money management, and profitable psychological triggers. Welcome to the Two Traders Podcast.

Walter: Welcome to Two Traders Podcast. It's Walter here. Hello, Darren.

Darren: Hello, Walter.

Walter: Today, we are thinking about this idea of if you watch the charts, will it improve your trading? Another way of looking at this is will you learn how to trade by watching the candles unfold in real time? Is that time well-spent? What say you to that? What do you think?

Darren: It's really difficult to tell people that a certain style of trading is not going to help them or is going to help them; or is the right way or wrong way. But, I think what we can learn from -- you know, we've kind of done like a mass social experiment by the explosion in retail trading.

There's been like a big experiment going on and from that we've discovered that people have got certain weaknesses as traders. Certain things are going to trip you up and make it difficult to trade.

What I see really often is that they'll tell me their trading plan and it will all be planned out and back-tested and they'll have an expectation for their trading plan. What you find is that in live trading, their plan performs better than them.

They might have traded for 3 months and broken even or lost money but their trading plan for the last 3 months made really good returns. You see these a lot and I think pretty much everyone suffers this to a certain extent.

What you can learn from that is although it's fairly difficult to develop a decent trading plan, the really difficult thing is executing it. If that's the case, then sitting there staring at the charts when you don't necessarily have to is not a great way to approach it.

Now, someone might turn around and say, "Look, I can tell by the shape and the pattern of the candles what the overriding sentiment is." And that may be true but when you're doing that, you're looking at just a small part of the information. If you'll look at all of the information, what we find is that people make failings when they try to execute their plan. They do that because of human behavior and biases and emotions.

When you're staring at the charts, you're generating emotional reactions because you can't just sit there and think what's going on. Those thoughts are driven by emotions. Being excited, being bored, being anxious, they're all driven by emotions. Although you could trade by watching the charts unfold, you're basically tempting yourself to make human errors so I'd say it's a bad idea.

Walter: Right. I agree with what you've said. Like, I've always kind of said that trading for profit is pretty simple in terms of what the moving parts are. You don't really need that many levers and it's not that complex. Although it becomes kind of a look-at-me sort of thing when you have these groups that have tons of money to burn through and create algorithms and things like that.

I mean that to me is an unnecessary fluff but that aside, I think that it basically comes down to two things. Your trading comes down to your system which is the math side of it. We're talking about statistics, probabilities, odds, all that stuff. And the other side of it is really, "Are you executing?"

Those two things: whether you are executing your strategy and whether your strategy will make money. That's basically what it comes down to. It's not that difficult. To that end, what I would say is, "Yeah, I think you can get a lot out of looking at the charts."

I don't think that if you're in a trade you just necessarily watch it that often - at least for me and the people that I have come across. One of the things that happens there is you typically can talk yourself into a different idea after you have taken the trade.

You take the trade. You've got an idea. You're going to stick with this and then you watch it and then you start thinking, "What about this?" You know you can talk yourself out of it.

I don't think that's necessarily good. But I do think that, in short, looking at the charts concoct a plan and an idea of how you want to interact with the market whether it's a pattern, whether it's the fact that you notice that the particular pair gets relatively volatile at a certain time of the day.

Whatever it is, there's something that you see that you think makes sense to you. You can build a strategy based on that. You can build a strategy that has an edge. But, like you say that's not all of it.

I think the longer you're in this game, the longer you do this, the more years you'd spend doing this, the more obvious the psychology becomes. It's one of those things where yes, you have all these profitable trading strategies that are out there that anyone can literally go into the search engine and pick up off the internet for free. Right now, you can go and do it.

It’s probably going to be difficult for most people to make that work because they don't believe in it for whatever reason. They haven’t convinced themselves that it would work. And more importantly, when they start trading it, when you start trading the system, you find all kinds of reasons to change it or explain why it’s not working in this particular instance or whatever.

In other words, it’s the execution part of it that really gets in the way for a lot of traders. I definitely agree with that. I would just say that I think, my belief is that I think you can look at some charts and come up -- and we’re talking about this from a technical point of view, obviously. People who take a fundamental approach. A pure fundamental approach may even state that you don't need to even look at the chart. You would never even need to see a chart to trade or whatever. Although, maybe those guys are investors on that trader but some of them would be for sure.

I would say yeah, you can get a lot out of the charts. I don't think it’s necessarily very productive while you’re in a trade. Although, if you're trading like really quick little in and out trades, I suppose it’s quite useful. Even then, maybe not. Maybe just lock it in and let it ride. But I think that the real work comes in on the execution side so definitely, I agree with you there.

Darren: Yeah. I think when you look at charts in real time as well, whether you like it or not, your mind is kind of making a narrative about what’s going on. I think with experience that tends to sort of die down. But certainly, initially your mind is sort of generating this narrative, almost like you knew it was going to happen.

Walter: Hindsight bias.

Darren: This hindsight bias. Like, “I knew it was going to reverse there” but that’s after it’s reversed. So you build this confidence in your ability to read what’s going on with the market. I think that’s a bit of an illusion and it’s one really easy to buy into. Especially if you’ve got a trading plan that in the short term is losing.

Say, you’ve started the week and you have taken 3 losses and then you’re watching the charts. You kind of, in your mind start redesigning your trading plan on the fly. It's a really dangerous state to get in.

That’s why I always say that, the exercise you should be doing when you’re looking at charts is, “How accurately can I replicate the plan that I built up over a long time?” So your trading plan that you’ve done a lot of backtesting on and you’ve got all the data. You know exactly how to enter and how to manage your trades.

What you really should be focusing on is not how the candles are evolving. It is, what is the next stage of the plan that I need to execute and how can I do that as precisely as possible. Because that's the only position you really should be aiming for.

It's the precision of your actions and how you execute. Then, if 3 months down the line, you've executed your plan perfectly and your results are very bad. Then, you consider making changes. But you need to get to that point where you've executed with as much precision as you can.

Walter: Yeah, and the questions will come up. Like, "If my plan tells me X, why do I keep doing B?" That's the confronting thing about this. You learn that, "My plan says that I've got to get 4R out of my trades and I keep averaging 3.1R. Why am I doing this? What's going on here?" That's really where the work comes in, doesn't it?

Darren: Yeah. But I think, once you've accepted that, once you've realized that, that's the problem, then we have a kind of, repetition of trying to execute better. You find that you do get better at it and those psychological issues tend to sort them out then. But you need to accept it in your mind first that, that is the problem. I think that's a hard step to make because what you tend to do is to just change your strategy, rather than your behavior.

Walter: Yeah, that's the easy way out. That's definitely the easy way out. And that hindsight bias thing you're talking about, I distinctly remember having these systems. That I would read about in library books or kind of tweaked something that I've or something like that. And I would look at it on the chart and then I would have all the indicators there and everything. I'd say, "Wow this is amazing! It works so well. Look at what it would have done here, and there, there and there."

It was only when I started to scroll back. This was before I even knew about Forex Tester. But it was only when I started to scroll back and look. I would actually pull a spreadsheet out or like a notepad, I would literally, bar by bar scroll the charts forward and create this track record of basically backtesting it. It was only then, when I started doing that, that I realized how much hindsight bias was affecting me.

I mean, it's a really good thing to use a simulator or something like this so you can experience what it's like to actually trade the system. Otherwise, that hindsight bias would color what you see on the charts. You will negate the losers and make up reasons why you wouldn't have taken that trade and it's just crazy.

Darren: I have seen people who do watch each bar unfold. Make their decision. Take their trades, and manage their stops and make it work. At the same time they tend to be following a well tried and tested plan. Although, it looks like they're acting on the fly, there's still a strong plan behind that.

So, I think you can do it if you have a strong plan behind it. But there's a lot of studies as well that suggest that it doesn't improve. It's not good for decision making. You'd be in a much better frame of mind to make good decisions if you did step away from the charts and do different stuff. Distract yourself from it, if you like.

Walter: One of my friends, his best trade, he had it years and years went. He took the trade and forgot about it. And then he came back after the summer and realized he still has the trade on. It was his best winner ever. He decided not to trade in July and August or whatever it was. He came back in September and he said, "Holy crap. I forgot about that trade."

Darren: If you look at the SMP500 every decade, it's kind of doubled or something. You say, "It's simple. You just buy and you hold it for a long time." But then, when you actually look at the changes in prices there then, in 1 decade you were like in drawdown for 8 years. And then in the last 2 years you went into profit. In another, you had massive profits and it re-traced all the way back down to breakeven before finishing. You see what I mean? A simple plan on paper is great but if you don't make the journey and execute it, that's difficult to bear. To live through those drawdowns, etcetera.

Walter: Yeah. I think there was a study done. There was a fund manager that did the study. He was like a smaller fund and he said that the larger funds, made this statement, "It's really good to just remain in the market. Just write it out and stay in the market." This is like the accepted wisdom point. Everyone should just write it out, stay in the market. We've all heard that.

Basically their point was, if you don't stay in the market -- all of these funds would say in their materials -- if you don't stay in the market then you'll miss out on the big days. There's like a handful of days, the days that really move where the majority of the year's move is made only just a few days. What was interesting about what he said was that he looked back, and those days, do you know when they occur? These days where the markets moves really strong and goes up a whole bunch. Do you know when they tend to occur?

Darren: Was it the day before the worst day? Or the day after the worst day?

Walter: Yeah. The day after the worst day, that's exactly right. I thought that was so funny because the funds did not tell their investors this. They have to stay in the market the day after the crash because those are the days when it rebounds so much. They know this, but they are not telling you this. So his whole point was he was trying to figure out a way to stay out of the market when it gets really volatile and when it's likely to crash.

Basically, that was his whole point. But I just thought it was funny because it's like what my Statistics Professor used to say everyday when she walked to the class. Every day she'd start the class the same way. "There are lies. There are damn lies and there are statistics" and it's so true. You can make it look good no matter what sort of hypothesis you're trying to support, you can make it look good. Like this funds do**.** Anyway, I thought that was quite interesting.

Darren: Do you have like a system in your trading where you regulate how you look at the charts? Or you sort of naturally fall into it like a routine with that? Or do you just essentially check it when you feel like it?

Walter: The chart? Do you mean if it's an open trade or looking for a trade?

Darren: Just in general, if you're trading.

Walter: Yeah. What I do, I typically will look at them. Where I live, the D1 candle for the New York 5 P.M. charts, that daily candle starts in the morning for me. So what I typically will do is after that candle prints -- in the winter it prints quite early and in the summer it prints a little bit later. What I'll do is I'll wait until that prints and then I'll scroll through my charts and I'll just have a look. I'll just go through all of the charts.

I have a few that I have on a watch list and I'm kind of waiting for a possible trade. But I'll just scroll through them and then, that's when I record my video and post it in the private forum basically. Then I'll say, "Look, this is what I'm looking at. This is what I like." That sort of thing.

Then what I like to do is later on in the evening, here in Australia which is in the European day time, that's when I like to put my orders in. So that's all I really do. And I don't typically watch them. There's really no reason to. The only thing I might do is see when I could possibly move the risk. So, the risk is off and it goes to breakeven. That's about it, really. That's what I do.

I find that I often make really, really poor decisions when I'm watching. I don't like doing that. What I mean by watching is, if I'm in a daily chart trade and I check it like every 4 hours or every 3 hours, something like that. That's what I'm talking about. It's counterproductive for me, anyway.

Okay, that's it for Episode 139 of Two Traders. This is Part One of Two and in the next Episode in Part Two, you'll see the problem with high win rate trading. Why you need to pay attention to this.

Why most traders lose in forex and how you can use this to your advantage. You'll also see how children can help you find the very best trading setups and why this actually works.

What expert poker players, these are the pros, what they do differently and why is this an advantage for you. This will help you in your trading too and finally, you'll get the weird way to see forex volume in the charts.

All these and more in the next Episode of the Two Traders. We'll see you there.