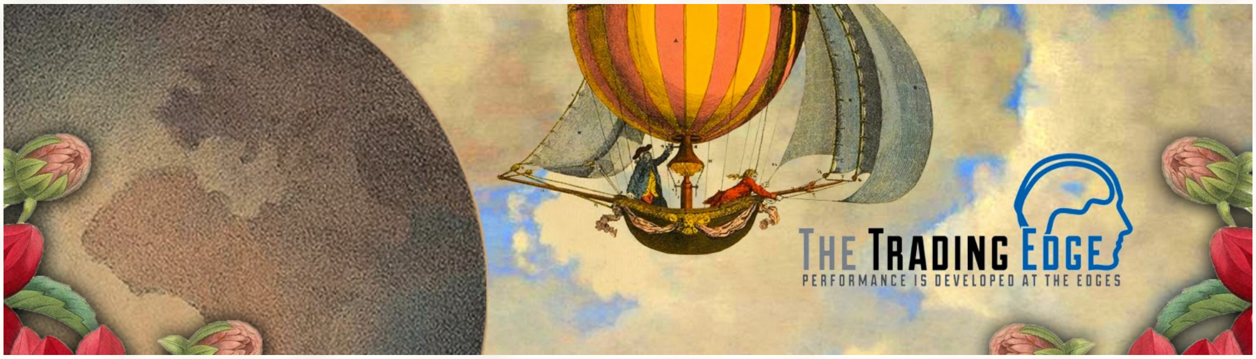

INTERVIEW WITH BRENDAN MOYNIHAN

Lessons from What I Learned Losing A Millions Dollars

00:02Houston: Hi Brendan, welcome to the show

00:04Brendan: Thanks for having me on

00:06Houston: Absolutely, thank you for joining the show, so before we get started today. I just wanna tell everyone that Brendan is the author of numerous books but I brought Brendan on the show because I wanted to talk to him about one of my favorite trading books and it's a book that I often recommend to other traders called What I Learnt Losing A Million Dollars and Brendan I know you probably heard it before but what a great title so what's the story behind the title?

00:30Brendan: The disclaimer is my co-author is actually the one who lost the money, OK. I didn't lose the money, he lost the money and we were just trying to make a fortune off of his misfortune. My take was, that there were, especially in this industry although you can go into real estate and other places as well, because there are so many places and books out there and how to make a million dollars in the market, I just thought it was a paradox why would you write a book and sell it to other people if you know so much about how to make money in the market why wouldn't you just go do it yourself and it's as old as the 1800s; I think the oldest book I found was 1871 called The Beef Bonanza – How to get rich on the plains – it was about making money in livestock and it wasn't stocks but it was livestock. But what really did it for me was I saw and interview in Times about a Time life photographers and they are noted in the industry for being excellent and winning awards for being great photographers. The interview asked what makes a time life photographer and the answer was an example: imagine a murder scene after a domestic violence event where the wife had finally had enough and she kills the husband; the cops come and they're drawing chalk around the dead body and the photographers are taking pictures. The Time life photographer will not take the pictures of the dead body, they take the camera and swing 180 degrees and point to the wife standing in the corner with her head in her hands because it shows the emotions of you know of what she's done but also she had to do it, right. But the fact that they point 180 degrees is just a different perspective and so instead of a book on how I made a million dollars trading commodities last year, I just said well, why don't we take Jim's story and marry it with a sort of clinical dry theory that I have about the mistakes that traders make and investors make. My stuff is too dry to sell by itself and his story is too **(inaudible02:29)**to tell by itself but put them together and we might have a parable that people will identify with; if you get to know him some of the funniest things you have ever heard, he has some of the funniest stories ever and they resonate with people and if you can go back and forth between his stories and if you know him a little bit and kinda weed in some of the dry stuff, it makes it a little bit more palatable so

02:51Houston: Right, and that's so funny that you put it that way because that's definitely what I took out of it, the powerful part for me was the narrative of the story – it really keeps you going and then you wrap up or the second half of the book is like you live the pinnacle but very, very – it gives you that kinda deeper theory that keeps you thinking so the stories draw you in and then you in the deeper insights afterwards that keeps you coming back to the book

03:23Brendan: And then you come back to him saying, do you remember when I did this; well this is an example of it and it just makes it a little bit easier to – it's a shadow between theory and concrete examples – I think it just makes it easier to walk away with it

03:40Houston: Right and I guess the parables are the perfect way to pitch it so, talk to us a little bit more about the book, for the folks who haven't read and it's a great book and we'll get around to when it was published and when it came out in the first place but maybe Brendan you could quickly tell us about Jim Paul's story and kinda how he lost a million dollars or maybe even a little more than that

04:03Brendan: Well, the event took place in 1983, he was a floor trader in Chicago **(inaudible04:10**) he was lumber trader and he had grown up without telling the story in the book – everything he touched turned to gold but he grew up dirt poor in Elsmere, Kentucky and you know was a caddy and, you know, got a taste of the good life and decided that he wanted to do that. He went to college instead of waiting to be at the pledging of the fraternity he just walked in one day and said I just wanna be here and they took him. He had a golden touch, it's like everything he did worked for him we got into the markets and things worked for him. He was a lumber trader but got very excited when a friend of his in a soy bean oil trade and wound up in a limit position did the board trade in soy bean oil (**inaudible05:02**), he had 540; the reason he had a limit on was because he went over the limit and in exchange (inaudible05:11) him but he had to back the position off but in 75 days starting at the beginning of September, he lost 1.6 of the 1.2million dollars that he had, in 75 days. **(05:26Houston:** wow) So, he was down 400 thousand dollars and I gotta say that was 1983. I didn't meet Jim until 1989; I worked for him for about a year and the last day of my employment with him, we went to lunch with an amicable - I was being recruited and I was leaving town and it was all amicable – so he and I went to lunch and he told me a little bit about the story only then. And he said somebody said I should write a book about this and I said you know what I could write that book and so – you waited until I'm leaving town to tell me, right – so (**06:03Houston:** laughs) I had him, he was supposed to tape record the story and tell somebody who had never heard it before so that he would be very animated; he was supposed to tape record it and send it to me. Well, about 6 months goes by and he still hadn't done it and he called me and he mailed me plane tickets and he said "you have to do it, you come up here and record it" (**06:20Houston**: laughs) so I went to his house for about 2 or 3 days and I took about 18 hours, put the tape down and then I took it back and then I was a bond trader, I didn't know how to type but I started to learn and it took about 3 years to transcribe his stuff and then put it in order then gather my ideas, I mean I had a full time job and 2 kids, it wasn't like this was the only thing I was doing and then I had to kinda flesh out my ideas a little bit more. I'd never written a book before so I didn't know what I was doing but that's kind of the nutshell of the back story, to kinda get going

06:54Houston: What a great story, sobefore I get much deeper, why don't you tell a little bit about your background so, it sounds like before you met Jim and you start writing the book you were a trader and then you became an author shortly thereafter. But yeah, tell us a little bit more about your story– how you got started with trading and your background.

07:15Brendan: Yeah, well I, in college I knew what I wanted to do, I knew I wanted to trade and I wanted to trade bonds. And I came out of college and I did get a job in Nashville working on a cash bond desk for about a year but I also knew that I really wanted to be in Chicago or in New York for at least a little while early on in my career. So I was very interested in futures and so I went to Chicago and I worked up there as a research analyst for a couple of years then a went out on my own started trading on my own and I did that a while, then I picked up a job with Jim being an analyst for them in foreign exchange and that's how I got to know them and then like I said the firm that I worked with in Nashville recruited me back and that's when I left and I worked with them and he told me about the story and everything. So I went back down there and I worked with binds for about five years then I went across the street and did currencies for about two and a half and September 17, 1997 I quit and went home, because I wanted to be around to help raise my two boys by then five and eight. And I had about four or five research clients that I had wrote research for in different fields: stock, bonds, currencies, commodities and I just worked out of my house for about fifteen years and I worked in **(inaudible08:36)** the stocks had been going up.

08:40Houston: Yeah that's a great **(inaudible08:42)**

08:43Brendan: And one of the clients was Bloomberg so I'd been publishing for Bloomberg News for a longtime and I'm still a consultant there. I mean that's fifteen years, I started March of 2000 so. Yeah so I mean **(inaudible08:57)** qualified me to write the book in the first place was that I had been the market and have had my series of losses. And when I finished the book and gave it to Jim and he read it. He was very full of himself just in general, but he said "you have to know my story, because how would you know about these losses stuff" and I'd say you're so vain, you're so vain; you think you are the only person who has ever lost money trading. I said look I may not have lost a million dollars in 75 days but you know what it doesn't matter, if I lose five grand or ten grand or fifteen grand in a trade, it's the same process you just choose to be monumental about it. I mean I did it in small proportions you did it in biblical proportions but it's the same thing.

09:37Houston: And it sounds like Jim Paul is a larger than life character is that a fair characterization?

09:40Brendan: Oh yes, he was - big booming voice because he was in a lumber pit so his voice was loud, and his voice sounded like gravel in the bottom of an empty coffee can (**09:49Houston:** laughs) It was, and he'd walk into, we ran out of batteries, the batteries you know wore out in the recorder so we jumped into the car and drove around the corner , pulled over to a place and we walked in and we were looking for batteries. And I'm the thinking I'll go find the isle, no, he just walks in and screams "hello **(in audible10:05)".** I'm saying they are batteries they are on the shelf somewhere, he was probably 6'2" he wasn't a heavy built but just, with that and the voice and, you read the books so you know some of the stories – they are absolutely outrageous. Even he is in South Korea, he's 23 years old he has the purple key to release the nuclear weapon onto the plane you know to take off and he's like "what am I doing? Two years ago I was burning deck chairs on in a bonfire on a beach down in Daytona, Florida. I have no business with this key." Yeah so he was nuts"

10:47Houston: So I think the next step is to have a movie made, I think that's next.

10:52Brendan: Yeah, I've got somebody in mind for that but I own all the rights to it though; I did, I did, I've got a son in Los Angeles and I kind of just got out of college and that's the industry he wants to be in so we might wind up doing that.

11:07Houston: That'll be great I'd definitely buy tickets to that. So let's just quickly shift this for a second talking about the book again. You know as I was telling Brendan before the call, I came across your book when I heard you on Tim Ferriss' podcast last year. Then I received your book as a part of Tim Ferriss' quarterly box and what I was saying is that this book was first published back in 1994 and it kind of blows my mind that we are still talking about it today and it kind of speaks to the timelessness of the subject matter and of your writing. So how does it feel to still be talking about this, this title, this book? Because you have talked about this dozens of times.

11:50Brendan: Well I mean, the two first things, I did kind of get a little more attention from people, but there was a step before that that enabled him to even find out about it because we self-published the book on February 4, 1994 and nobody was self-publishing books back then we did it because we didn't like the economics of the book industry but we sold it out of a post office box in Nashville Tennessee, box 198038. And we were lucky enough to get a bi-line on the cover of Forbes magazine right above Jack Welch's head that says "Biggest mistakes investors make. Are you guilty?" Mark Holmberg that does the mutual fund column there did a full article on it and at the time it was like "1800-BUY-BOOK" and we had a book distributor that they could buy books that way or they could mail it to the P.O box and that's how we got the book up. There was no, well despite what Al Gore said there was Internet but there was no world-wide-web. So the only, it was a very crude way of selling the book, I mean we were the only source, we owned the book and it was not in book stores **(13:04Houston**: yeah) So I know a number of years went by and we put out a number of copies and a number of them sold out then it kind of died down and got quiet and was basically out of print. But when Google announced in the early 2000's that they were going to start scanning out of print books, I was outraged because it took me three years to write this and I'm not just going to sit around and have it them scan it given away for free, I'm sorry. So I was already kind of leading that way in terms of getting things together, when **(inaudible13:38)** book The Black Swan came out and in that book he gave it a nice plug, because he is not known for handing out compliments. (**13:47Houston:** Not at all) But he said the best finance book that I've read is a "How I Lost a Million Dollars". And that kind of gave it a jolt as well, so I, that was April 2007. I republished the book then and it's up on Amazon and we were on Amazon before but the book basically went out of print as well, there's a story there as well which I can explain to you as well if you are interested. But there was a window that I was not in print and used copies were going on Amazon for two, three hundred dollars and so I went and I said I have a couple here do you want one? So it went back on in 2007 but then, in 2007 I was just selling them off Amazon paying my kids to fulfill the orders and they got some money and learned some things about customer service and selling and whatever, whatever. Then Columbia University Press got a hold of it in 2011 and bought the rights so then we published it with a new cover and because they can get into book stores they can draw a bit more attention and the **(inaudible14:51)** about it and that's how you found out about it, so it's really in the last two, three years. In terms of it still being talked about there are two things. One, yeah, I do believe there is timeless lessons we've been making these, traders and investors have been making these mistakes

(inaudible15:05) I think you know since time immortal, nothings gonna change that it's all based on human nature. In terms of how does it feel that you know, well we were talking how things got started, somebody asked Jim and I were talking about this years ago and he said you know do you remember the interview when somebody was interviewing Glen Campbell the country music Western star and he asked how does it feel to be discovered and he said yeah I was discovered after fifteen years of playing in dirty honky-tonks back in the Southwest. Well, so Columbia University press nineteen years after I self-publish the book, they find, they discover it, republish it and then like the next year wins this book award which you know **(inaudible15:44)** book award but they won the award they got a little gold medal and a little certificate and blah and it's like took nineteen years –it's a good thing I can't find a living as an author, I mean

15:59Houston: Did you set out to like try create something timeless? Because you know many of these books you know talk about getting rich quick, they are kind of a flash in the pan right, so those burn quickly then they burn out

16:12Brendan: **(inaudible16:12)** because this is the slip side it is like (**16:19Houston:** yeah) never mind about making money it is like, what do you do wrong? Well, we are human we always going to make mistakes and there is a whole new crop of us coming along every couple of years and it is like they are going to make them too, so I did not sit down and say I wanted my book to go down in the annals of trading book history it was just in my head, I have to get it out and Jim's story seemed to be the vehicle to make that work I had something to say. The other books have basically been yeah, something to say about this and a book seem to be a way to do that again that is not what I do for a living, right. I don't play tennis, I don't play golf, so I don't have a TV so this, is what I do instead

16:57Houston: Yeah, what a great back story, so let us talk about the books, the book is just filled with quotable and great ideas and you have already take about the big one. So the three mistakes that investors make you teased that already, so what are those three mistakes?

17:15Brendan: I am not going to tell anybody they have to go and buy the book. No I am kidding, I am kidding (**17:17Houston: inaudible).** So what happen was I mean I do think, I believe that I have identified the three things that I have done wrong you know, repeatedly and I talk to other traders and you know I kind of dance around it and say hey I am going to research for a book you know but I kind of heard them saying the same thing. So it was sometime into writing the book that I ran across, I don't know what prompted me to do it but I said basically this is a life **(inaudible17:42)** on the psychology of trading, so I look at the definition of Psychology in the Dictionary and it says "it is the study of the mental processes, behaviors, characteristics and emotions of an individual or group, " I'm like those are the three things that I have been writing about, so Chapter Six is about the mental processes, Seven is about the behaviors and characteristics. I have already written it, I just kind of **(inaudible18:05)** the definition and just unpacked it and just labeled the chapters that way because that is exactly what it is, so basically the mental processes or internalizing what should be an external loss. When you lose your keys you know you don't go into a deep funk right, it is an external loss you find them right? An internal loss is the loss of a loved one, a parent, an uncle, a grandmother, dies or whatever. These are internal losses and in that people go through five stages of internal loss, which I have labeled it internal loss the five stages come from a book called On Death and Dying by Elizabeth Kubler-Ross in which she interviewed two hundred patients who were terminally ill to find out if are a common thread and this is where you may have seen in other writings whatever denial, anger, bargaining, depression, acceptance that is right, so the exact same thing happens when you suffer an internal loss whether it is you getting ready to lose your life or you lose a love one to death like denial, then anger, then bargaining, then depression and then you finally accept it. The same thing in the market right. You lose your money, denial (really?), you see and opening quote in the market (really?). I was in **(inaudible19:27)** one time July 23, 1988 the beans opened at $1.9, is this a bad quote? Is something wrong here? I mean, it was like there is something, 1094 which is 109 and a half (**inaudible19:40)** like something is wrong here right, no no.

19:44Houston: (inaudible)

19:45Brendan: So denial and then anger you get mad at the market **(inaudible19:48)** depress, so it is the same process, so what I am saying is when you lose money in the market it is an extra loss but if you start observing yourself that you are going through denial and then anger and then, but you shouldn't internalize what is an external loss that is one of the main, that is one of the things you can outline in terms of what are the mental processes of somebody who is losing, who is a quote, unquote loser or in jeopardy of really losing money because of psychological reasons not because of the technical system that you are using to try to make money (**20:19Houston**:right) so the behavioral characteristics in here I think that people confuse the difference between inherent risk and created risk. So inherent risk is just the risk of everyday life, you walk down the street and get hit by a car you know you get a disease, die, or whatever. Created risk is speculative risk, all the stuff you go on, every game, every roulette wheel spun, no money have to change hands , it has to be no loss unless you go ahead and decide to wager okay. In this chapter I go through and say there are five types of participants in the market. You have investors, traders, speculators, betters and gamblers and investors are parting with their cap full with the expectations of return in the form of interest, dividends or rent-all of those things are paid on a periodic basis, so it is either monthly or quarterly or semiannually whatever right so you plan on been **(inaudible21:16)**. Traders to me are just market makers which are largely gone these days but you know **(inaudible21:25)** flat you are just trying to extract a better spread. Speculators are looking for the difference in price change, they don't intend to commit their capital long enough to get interest, dividend or rent, right they are flipping it right. Betters are interested in been right, you and I can have I mean, what used to be called I don't know if it is politically correct or not to say anymore, you and I can have a gentleman's bet - no money changes hands right, so whoever is right gets bragging right or you have a pinky bet no money, you just want to be right and then there are gamblers which is I admit is a disease I am not qualified to address it, I know the Gamblers Anonymous. I went to a couple of meetings where I was doing research for the book to find out what is going on you know, what this is all about. What happens is that I think people confuse that they don't realize that there are those five and very often people are winding up in that betters camp, okay. A lot of people in investment is a trade that did not work out, I am going to buy this expecting it to go up and if it doesn't work out, I am going to hold on to that that is just you know **(22:35Houston:** alright)and then a lot of times people are more interested in been right you know than making money, so I go through you know the characteristics, the behavioral characteristics of the different types of activities as well as the characteristics that takes place in casinos where with games of chance, the game ends, okay. (**23:03Houston:** right) So in gambling games the game ends, you don't have to do anything, it stops and there is no question who won, who lost, okay. With the markets, they are always open - even on the weekend they are open cause the **(in audible21:19)** down right, and people are going to make decisions base on the news over the weekend so they are get going on Monday and life is what it is, so the problem is that betting is fine in games of chance gambling environment you know, whether you are playing poker with friends **(inaudible23:42)** I am not advocating, I have never done it in my life – I don't understand why people do it - but betting is fine in that environment because it will end by itself but if you are betting, if you are trying to be right in a market which never closes, it will give you more excitement than you can imagine because you can go to through and I'm going to tie in that previous chapter; you can go through denial, anger, bargaining and then have the market rally for you and you are like okay good now it turns back up and roll over and you go denial, anger, bargaining again to a new lower low right **(24:19Houston:** yeah) you can loop back through denial, anger, bargain, depression maybe three are four times before you ever get to acceptance where you know it should not have happened in the first place but because it never ends by itself it is always open and you are betting and trying to do right on something that does not ends by itself, you are leaving yourself open to those two chapters working with each other to create a real problem for yourself

24:41Houston: So it is like a real groundhog there just that just keeps turning over and over again until you **(inaudible24:44)**

24:50Brendan: I think they should release groundhog (**inaudible24:52)** like Groundhog Day Two like a sequel **(24:55Houston:** yeah) and just play the first one over again

25:00Houston: That'll be a clever spin, I like that.

25:04Brendan: They don't have to spend any money

25:08Houston: They get a whole new generation of people watching it too

25:10Brendan: That's right. Did you see the first one? No, I saw the second one

25:16Houston: it's kind of what Disney does every year with their big titles. Like Bambi comes out every twenty five years or what not **(25:21Brendan:** yeah). So back to the mistakes: so number one is internalizing an external loss, number two is kind of confusing what type of participant you are.

25:31Brendan: **(inaudible25:31)** so to deal with emotions, so if you were to ask most people: what are the two driving emotions in the market? They will typically say fear and greed. Well I disagree with that, first of all I'll give you the reasons. First of all emotions are neither good nor bad – they just are. They happen right, your dog dies I guess you'll feel sad; I mean these things just happen - you feel happy you feel sad, whatever. Decision making based on emotions that I can but a value judgement on, that's not good. Experiencing emotions is fine, it's that decision making under that rubric that's the problem. So, I think that rather than like trying to deal with all, you now there are lots of books out there on oh you are this way because your mother didn't kiss you goodnight when you were six years old. I can't do any of that, I'm not qualified to do that, I majored in Finance and that's what I do. But what I can say is that if you really look at it, it's not fear and greed that are the driving emotions on the market. It's hope and fear – our natural responses to the uncertainty in the future - which is the markets and is the topic of the next book that I am currently researching on right now. Our natural responses to that are hope and fear, hope things are going to turn out well and a fear they won't (**27:04Houston:** Right) the paradox is this: we experience both of those simultaneously and whichever one is dominant dictates what your action is going to be. So for example, if you are long and the market is going up you are going to hope it keeps going and you fear it won't. If fear and greed were really the driving emotions, greed means wanting excessive amounts of something so, if you are on the market and things are going up and down, if you were greedy you would get out, get short and make more money so it's not greed otherwise you'd do that. It's hope and fear so if you're long and the market and is going up you are going to hope it keeps going, you fear it won't which ever one is dominant will dictate whether you stay in or get out. So let's say you are fearful, it's not gonna keep going up and you get out now do you know what you feel? You hope it's going to keep going down to make you look right and you fear it's going to go back up. That's just one variation, now you can imagine flipping around and being short same thing or not being in the market watching it go up, hoping it will go up, hoping it will pull back fearing it won't whichever one dominates will dictate what you do. It is a constant tussle back and forth between those two emotions that dictates what we do and making decisions based on that is what I'm saying is a bad thing. **(inaudible28:32)** Making decisions based on that is the problem.

28:43Houston: Yes, a real tug-o-war between hope and fear. And that's a classic example of you trying to get filled on a pullback, you get filled and now you're hoping doesn't go much further down as you've gotten filled already.

29:01Brendan: **(inaudible29:01)** Then you hope it starts going up but you're afraid it won't **(inaudible29:04**) and you turn on a dime, you know, it's like being manic depressive.

29:15Houston: Absolutely, absolutely. So in the book you talk about one way to deal with some of these emotions and I think you called it emotionalism in your trading, I think there are several layers here but is number one you talked about treating trading like a game; So why do you say that?

29:42 Brendan: Well I mean I'm saying you need to have some pre-defined end point to the position, I'm not going to prescribe what methodology you should use there are hundreds of methodologies out there I just think that regardless of what methodology you use, you need sort of this back drop so that not all methodologies are gonna work at the same time, yours might be working and mine might be not be working but I need to at least know about these three mistakes so I get myself out of it, OK. **(30:16 Houston**: right) instead of treating it like a game I only mean there needs to be some end point and you do that by scripting things out ahead of time; what are the circumstances that are gonna get me in and what are those circumstances or conditions or price- whatever it is based on my methodology – that's gonna get me out and if there's a problem with that I address that but not while I have a market position on. If my system isn't working, my methodology isn't working or whatever do the analysis when you're not in the market, don't do it when you're in there because you will succumb to this hope/fear paradox and you'll subject yourself to denial, anger, bargaining, depression and it doesn't change. So to the extent that I say treat it like a game you need to know what the boundaries and the end point are, you have to some set of prescribed circumstances ahead of time to bring resolution to the position

31:05 Houston: Yeah, well said and putting that structure on top of this continuous process that never really ends is gonna basically turn into a discreet process that you can better manage versus just having it run around forever.

31:19 Brendan: Exactly

31:20 Houston: And so how does it layer then into having a trade plan, is that trade plan exactly **(inaudible31:26)** some structure?

31:27 Brendan: Exactly, yeah. Just having it written out ahead of time, objectifying it, getting it out of your head and putting it down on paper. I am a big proponent of and this kinda comes from the title of the book, instead of putting a position on and then outlining or what's to say you're putting in the stop, instead of getting in the market and then putting in the stop or order, this might sound like a little bit of you know like – put your stop in first

32:01 Houston: Yeah

32:03 Brendan: And then you get in the market. It's like, OK, at this level it's either I don't have enough money to go beyond that or I've created enough technical damage or it violates rules three, four and seven of my system or whatever. It happens and I think writing it out and I think literally if you get it, if you objectify it, you're a lot more likely to follow your ideas if you've written it out ahead of time and out it down on paper and just don't deviate from it the moment the position is there; if you get knocked out, you get knocked out four times in a row, if there's something wrong with your system figure it out when you're not in the market but don't try to move or change things in there because the **(inaudible32:47)** takes over and you just make it worse.

32:51 Houston: Right, yeah, so the risk management you speak on there – worry about the risk ahead of your orders is kinda what you're take is

(33:04Both talking together inaudibly)

33:06 Brendan: Don't tell me the good news, I know youre gonna tell me the good news, tell me the bad new first right (**33:10 Houston:** right) like or one of the examples I give in the book is that people say OK this trade has a three to one risk reward ratio and I'm like no it doesn't you're making that up. There is nothing in the odds or probability that says that's – what youre saying is that you're willing to risk one in order to make what you think might be three but there's no probability you can say Oh it's a three to one reward risk ratio, that's nonsense but we kid ourselves into that right, I mean it's one of the weird ways we distort looking at risk. It's like and this one is in the book as well, the odds of you know winning the lottery is like one in a million OK , the odds of getting struck by lightning might be one in a million – you think you're gonna win the lottery but you don't think you're gonna get struck by lightning

34:07Houston: Right (laughs)

34:11 Brendan: So you know it's just some of the ways that we kid ourselves (inaudible34:16) and that's why to me it's timeless, right. It's like people that I talk to read the book but then they read the book again later in the year or they revisit kinda like the second half where the lessons are kinda there, it's like couple times a years they kinda go back and buzz through that as a refresher because we're all just subject to it' it's what goes on in our ears, you know, it's not like we become evolved psychologically mature entities, we tend to make the same kinda mistakes over and over again almost no matter how old we are **(inaudible34:56)**that's one of the things I don't think will go away. Now it's **(inaudible35:01)** bestseller doesn't matter but to the people who have kinda gotten hold of it it's like yeah I can see the benefits of this and it kinda applies to just about everybody

35:11Houston: I have to agree; I'm definitely one of those people who have gone back to the book numerous times. I have my copy right now – it's kind of all dog-eared and underlined but I find myself revisiting the book at least once a quarter. If you want to do something, the story of Jim Paul, you know I guess is a great story around how the self attribution kinda took over and he kind of attributed a lot of his success to his own, his own doing and that kind of magnifies things and, I think most traders fall into that trap especially male traders

35:46 Both talking together

35:47Brendan: I agree ….it is true

35:53Houston: So I find myself I have a hot streak and I think I'm, you know King of the World and then soon after the market will slap me pretty hard so that's when I revisit the book and read some chapters again. So another interesting thing is just around, you know, going back to trade plan for a second, so how do you…the funny thing is we've talked about this before on this podcast but I'm more surprised that a lot of traders even folks who've been trading for a while, they don't have a really defined trade plan and the second part that large traders struggle with is just being compliant around that trade plan- so they may have something written down but they really struggle around maintaining compliance - so how do you…what do you advise them, like yeah I gotta create it in black and white but I just can't follow it; things happen that shouldn't and I just, I go nuts

36:50 Brendan: I think a lot of it is, and this isn't something that I really go to in the book because I really, this is, it's not really one of the mistakes, it's a good point to try to figure out how to implement what I've laid out and hope to be useful advise but it really just comes down to discipline; and the question is are you self disciplined or do you need inflicted discipline. Some people are very self – disciplined they can sit down, they can work in a room by themselves for fifteen years and get stuff done; other people have to be around other people, if that's the case, I would say a few things: one – whatever your normal routine chore it is that you are supposed to be doing around the house, you know one way to build discipline it's like – do it. Anybody who exercises regularly, if you're not and you start anything that you can do to demonstrate that discipline **(inaudible37:47)** whether you exercise four times a week or everyday or whatever it is; I mean take out the garbage every time you're supposed to, wash the car every week whatever it is – anything that comes with some kind of discipline there – if you really don't have that self discipline you need somebody else involved and you write out the trade plan with and objective third party – a broker or a trading partner – and you know you swap plans. It's like look I can get myself into a position, I'm just horrible at getting myself out, you know because **(inaudible38:23)** coming my way, well you know, that's an example of that in the book. Jim's said one of the best trades that he ever made, he got short gold at 300on its way up to you know 800 just because he gave the buy stop to someone else. He wasn't left to try to manage that thing and what it does a little bit is, left to your own devices, you know, you might change the stop or you may stop down and put it back on. We don't like to look foolish, OK we might feel a little bit less inclined to do some stupid thing if you turn the execution of a **(inaudible39:04)**with someone else and make sure its implement OK and it's about as far as I can go. I must say it is not something that I really delve into in the book but just thinking about it now when you're asking me – its discipline and self discipline. If you don't have a lot of self discipline then you need a trusted, you know, other party to assist in the implementation

39:27Houston: Yeah, absolutely. That's a great point and maybe, you know with technology the way it is nowadays folks are really struggling – maybe you can automate some of those strategies and kinda just take the execution out of their hands so they don't rationalise their stops, their stop management. Yeah, I think that's a great piece of advice and you know that kinda ties into as well the inability to make and I guess stay compliant with your trade plan **(inaudible39:53)** link to kind of the random reward structure of the markets, right, so sometimes you feel like you can break the rules because you get rewarded and you know it feels like hey I did the right thing by not following my rules 100% of the time but that ultimately comes back to bite you

40:11Brendan: It does …because that schedule, that random risk and reward schedule for anybody who has looked at (inaudibe40:20) psychology and if you wanna get an activity to increase its frequency whether its an animal looking for food or you know, whatever it is give it a random reward schedule and to the extent that random applies to prices moving in the market, its typical random walk down Wall Street , random prices - to the extent that that is all accepted or whatever, yeah, I mean the market will give you a random reward schedule and if sometimes you break the rules – that's one of the examples that you get in the book like you know is it OK to break the rules or is it not OK to break the rules. It's like, you know, well when you're playing poker it's one thing you know Cincinnati Kid that's one thing but if you're in the market, you're leaving yourself open to again, these three mistakes that feed on each other. I mean I wrote it and then I decided to sequence six, seven and eight in the order of which that definition flows. That's doesn't necessarily mean that's the order, I mean you could start doing hope and fear first and then you start to **(inaudible41:31)** and then into the…it can start in any part of the definition but they feed on each other; it's not like, they're not compartmentalised, they feed on each other

41:42Houston: Yeah, yeah so the sum of the parts are bigger than the individual parts, yeah - makes a lot of sense; and so the random rewards structure schedule is such a powerful idea because like you said you've done the experience and the graphs and you see people how they play the slot machines in Vegas and it's the same way in the markets, yeah. Oftentimes, we've heard the saying "oh rules are meant to be broken but buyer beware or I guess, trader beware when you start doing that, you might get the reward seven out of ten times but the three times will really set you back a long, long way. So that takes us to the next thing though, I love that you talked about it that really powerful idea around tying your self worth to your net worth or your wins and losses, right so we usually tie our self image to our current trading account size or you know or our wins and losses

42:43 Brendan: I think that**,** that's, I mean that in chapter six is connected to how does an external loss becomes an internal loss. What happens that converts a loss of money into denial, anger, bargaining dah, dah, dah? And I think that a lot of it extends from the condition we get in school and we "lose points" for wrong answers. You don't get a test and have to put in, the teacher doesn't say plus two on this, plus three on that, plus nine, no everything is just subtraction. You get the blank test and it's worth a hundred, right?

43:29Houston: Yeah

43:30Brendan: You turn that thing around and there aren't any answers yet, you turn it back in and the teacher is up there knocking points off, so we lose points for wrong answers. When we lose money we think we must be wrong and none of us wants to be wrong (**43:44Houston**: right) we want to be right, so very often we are betters in the market in a continuous process rather than a discreet event, gains where it is okay to do that. And this gets us into trouble; so we don't want to be wrong and this is a confusion between self-worth and net worth. People are more often interested in the gold stars of being right and the gold money of actually making money in trading. So I do think people could use those two and to the end you did it and the upside too, your self-worth is up on a 1.2, 1.3 million dollar trading account **(inaudible44:28)** and lost more than that **(44:45Houston: inaudible).** I mean at the end of the day he was like worth minus four hundred.

44:43Houston: So how do you disconnect that? Do you have any ideas on how do you disconnect that? It seems like it is so tied together naturally.

44:48Brendan: What I hope is happening is that by unpacking it, a lot of people think about it that way, I mean I hadn't read about it presented that way before and again it's almost like an expose, like I'm saying these are some really important things to think about and some things to monitor in your own behaviour and thinking to see if you're succumbing to the psychological mistakes. You need to do something to step back so that when you lose money, you lose because of your methodology not because of your stupidity. You want to try to bullet proof – to the extent you can - your methodology without tainting it with your head; so to find out if you are doing that these are some things to observe in yourself when doing that right: if you find yourself bragging about the size of your trading account ding, ding, ding, ding, ding, ding, hello (**inaudible45:52)** how much money you made it's none of their business; and they may not have even asked you.

46:01Houston: Exactly, you're volunteering the information.

46:04Brendan: Oh hi my name is Brendan; I made five thousand dollars trading commodities yesterday. I mean they don't care and unless you are trying to impress them in which case you need to be doing it in some other way, you know, I mean.

46:17Houston: And this makes stuff like I think, like as you say that why not have a little check list of all the things that **(inaudible46:22)**

46:27Brendan: Yes, you know it's not a bad idea and having that again but like writing it down, and I mean even theoretically just talking about it right now you make your check list you use it each day and then it's like okay, here's what I'm supposed to do and here's what I'm not supposed to do. And like draw a line for the ones I don't know like circle the ones you've failed on and say how, it's discipline if I am I'm sticking to it is that the method for doing it. Type it up on a computer and print out fifty copies of it **(inaudible46:55)**. Did I do this? Did I do that? And if you find yourself calling up your friends and saying "hey I'm making a lot of money." you need to stop doing that, okay.

47:12Both together inaudibly

47:16Houston: I'm guilty of saying, I was reflecting that. My wife knows I'm trading well I'm definitely guilty of saying hey honey **(inaudible47:26)**. That's usually right off the top when the bell rings. It's great, so I know we're getting close to the end of the hour and wanna make sure that I honour your time today Brendan. But is there is a concept that I definitely want to unpack: we talk about how traders often tend to act like the crowd and we find have that we have the crowd mentality.

47:59Brendan: Yes, so that is in chapter eight and it's the emotional and the, the quintessential example of emotional decision making is the crowd. And I went back to Lebons "The Crowd" from 1905 which is you know I'm sure in the traders library. You know we were advertising various books and some of the examples used in there to identify what are the traits of a crowd, but the sort of readers digest version of it is kind of going to pop into it right now is that I believe that if you exhibit, you can exhibit these traits of affirmation, repetition, prestige, and contagion like **(inaudible48:45).** You are in an echo chamber, to call your best friend and say hey what do you think of this and they say yea I think it's looking good you can talk yourself through self talk or you can talk in the isolation of you own trading room - in your den -trading over a computer; you don't have to be around a whole bunch of other people to behave like the crowd does and get that sense of invincibility. You can do it if you exhibit those traits, you can do it in the privacy of your own home as an isolated individual **(49:16Houston:** right) and the crowd is emotional decision making, it is what causes people to you know they win a national championship so they burn police cars, it is because they have protection, things that they would never do on their own they will do under the cover of other people been there with them. I see in the markets you can find yourself what I call making a crowd trade, is that you are held in a rapt state of attention, you may have just lost some money, you looking for the next best opportunity, a tip comes along, you hear this and bam you are off the chair and going to doing it but it is outside the parameters of the trade plan, it is outside the parameters of whatever you know, your system, your methodology is and what is does is. If you marry those kinds of crowd behaviors with our natural response to the uncertain future which is hope and fear, you can create personal manias and panics. A mania grabs a whole group of people and make them go nuts, right; it can be in the market, it can be setting police cars on fire after championship or whatever, it is manic okay, that is hope plus crowd behavior right. And then fear plus crowd behavior is a panic, so I think that you can sit in the privacy of your own room and you can match crowd behavior with hope and have a personal mania and you can marry crowd behavior with fear and have a personal panic and there is nobody sitting the room with you at all your in there by yourself doing this and that is another way that these feed on each other, they are not compartmentalized. It's a dangerous cocktail.

51:08Houston: And that turns into the crowd trade (**51:09Brendan:** yeah) you basically **(inaudible51:10)** you're talking to a crowd trader **(inaudible51:12)**

51:14Brendan: When I use to critique my own (inaudible51:16), it wasn't like I sat down to create my own theory, I was trying to figure out what is going on and in the course of doing it, you know this is the late 80s early 90s when I am doing this I am like this seems to be what I am doing and I just started to categorizing them and then that is when I came up with the three mistakes and then later I found the definition and then I am like okay that works and all goes together, so I called them Crowd Trades I mean that is what I was doing

51:39Houston: Yeah, it's so powerful because it resonates across all time frames whether you know **(inaudible51:48)** of the lowest time frame to you know the investor who is trading years at a time it just resonates across all those time frames yeah

51:55Brendan: yeah, I agree

51:58Houston: Yeah, powerful; so maybe just a couple of quick fire questions and then I will let you share where people can find out more about your work, but I heard you say in other interviews and I just wanted to **(inaudible52:09**) because I thought it was curious. You said that good traders or successful people have a healthy disrespect for money, I love that one (**52:18Brendan:** Yeah). What do you mean by that?

52:19Brendan: I don't know how I came to that or whatever, but you know I found that – going back to that whole self worth, net worth thing right, it is like for me it is you know it, for me money solves problems, okay; and it is not you know flash or trying to make people think that you are better than them or you know, whatever. Look everybody, there is only one person in the world at any given time where nobody has more money than that person, everybody you meet either is going to have more or less money you know what I mean, so why get all wrapped up or caught up in that. It's not like it's a big deal, I mean if it is to you and you are using the market as a way to express that I think it is dangerous. Two of the best traders I know do have a healthy disrespect for it, they are not flashy, they don't have a flashy car or flashy clothes or whatever it is what they do right, they were bond traders in the 1980s and the bond trader in Chicago he did not count money during the day, he counted ticks, it was almost like a game, oh I have thirteen ticks, I got seventy two ticks. It was a number but it was not a power sign in front of it right **(53:34Houston:** yeah) it was not what he was about. I was doing this for about I don't know twenty six, twenty seven years, so that is my observation is that some of the best ones, money is not what it is about

53:46Houston: Yeah, that is a powerful piece of advice and what I see and what I know is that we often as traders as well - any trader comes in the game with the scarcity, they won't be successful because that mind set will only bring more scarcity (**54:00Brendan:** right), so **(inaudible54:03)** call this way I just want tell everyone again that again, pick up Brendan's book it is a great book - if you have never read it – it's a great title and as you said before I heard you talk about the same time is that I think this is a really great book to pair with some of those other books, so the books about how to make money, so you rarely have some of those books about how to make thousands and millions dollars and that is great but this book takes it from the other angle right, so you are inverting that and approaching it from how it is to lose money. So thank you Brendan for your time today. Where can people find out more about you and your work if they want to find out more?

54:41Brendon: I don't know-I mean the books are a hobby, it is like I say it is not what I do for a living, I have written a couple of them I guess, I don't have a website or anything you can Google my name and find the books or articles I have written and stuff like that and but like I say it is just a hobby, it is not my main thing so

55:02Houston: Yeah, l know Brendan has a good page on Amazon that shows the rest of his titles so I would direct people there in case they want see some of your other books as well. Alright, so thank you so much Brendan was a lot of fun today. Hope we get another chance to do it again

55:16Brendon: Great, I appreciate the opportunity

55:18Houston: Yeah, likewise. Thank you

55:19Brendan: Alright, bye-bye

55:20Houston: Have a great day. Bye now