# Master Your Trading Psychology

## *Control expectations and risks to become a better trader*

June 2014 ï Interview with Glenn Neely

Interviewer: Hello, listeners. This is Bud Fox from GreedAndMoney.com. Today I have the privilege to have Glenn Neely, the expert in NEoWave, as well as Neely River Technology. Glenn, how are you doing today?

Glenn Neely: Iôm doing well. It has been a while.

Interviewer: Iôd like to discuss trading. Iôve been trading since 2009, and Iôve had several paradigm shifts in trading and trading psychology. I find quite a bit of similarity between how you shifted from being a pure forecaster for NEoWave and then discovered the Neely River Technology that you utilize in your trading service now. Can we talk about something in that direction?

Glenn Neely: Yes. It sounds like youôre starting to make some realizations on your own that forecasting sometimes can be problematic for good trading. When youôre focused on a forecast, you tend to only look at the ñrainbowò and the great ending to your trade that you hope will happen. Itôs more of an idealistic perspective on trading than the real-world dangers involved with trading.

Itôs something that took me over 15 years to realize and begin to make that transition. It sounds like youôre getting there a lot quicker than I did.

Interviewer: My trading journey in the beginning was to try to learn all the mechanics, terminology and various indicators. Of course, in the beginning of trading, you try to be on a Holy Grail quest for that wonderful indicator thatôs never going to be wrong.

Glenn Neely: Everybody wants that when they start.

Interviewer: I went through that ï I thought somehow I could miraculously forecast the market. Obviously, that Holy Grail quest was a failure. I realized that market conditions change all the time.

My next quest was to try to really be very good at market analysis. Every day, during and after market, I study the market. I study the charts and analyze all kinds of internal indicators such as graphs and all kinds of things to try to find that edge to tell me what the market would do tomorrow before I trade.

I spend tons of time doing that. Of course, once in a while Iõd get it right and feel great. Sometimes I would lose quite a bit because I was fairly certain thatõs what the market was going to do.

Then I realized thatõs not what trading is all about. Trading is about risk management. Then I went into another shift of trying to really manage my risk, understanding that the market can do just about anything. Thatõs when I finally started working on my trading psychology.

Itõs interesting when I reflect upon my entire journey as a trader. The first thing that a trader should work on is the psychology, but usually traders tend to get hurt a lot or have a few accounts blown. Then they realize that quite a bit is mental and the importance of managing yourself ï your trading psychology.

Interviewer: Trading the markets is like a microcosm of life. Most people want all the problems they experience in life to be something elseõs fault and not their own. The reality is that your life is pretty much the result of the decisions you make as you go through your life.

There are things that can happen out of anyoneõs control, such as tornadoes, hurricanes, and earthquakes, but generally it goes in the direction based on the decisions you make over a lifetime.

Trading is the same way. It goes based on the decisions you make. Itõs not the market causing the problem. Itõs not other people. Itõs not the Federal Reserve. Itõs not ñthemò who are controlling the markets, even though we donõt know who they are. It mostly boils down to managing risks properly and not letting your expectations influence too much about what youõre doing.

Your focus is mostly on limiting risk initially on entry, getting risk to zero as quickly as possible, letting the world take the market wherever it's going to go, and then making sure you're trying to capture as many profits as possible in an unemotional and objective way. As you said earlier, that's what the whole Neely River concept is about.

It's about trying to objectify and automate the process of trading, so it gets it out of the realm of opinions, emotions, and psychology. The focus is on logical and non-forecasting-based technology for entering and placing stops, moving stops, identifying targets, and having what I call aggressive stops to make more money, more profit.

That's really what has made all the difference for me. My trading in the last 10 years, and especially the last five years, is dramatically better than it was in the first 5, 10, 15 years of my career. It's all the result of this shift in focus away from forecasting as much as possible and more toward technology, style, strategy and risk management. It's not about what I think the market is going to do.

Interviewer: I've been utilizing your service since 2009 or 2010. I'm not sure of the exact year you started the Neely River Technology.

Glenn Neely: I was doing it in the background in a fuzzy, mixed River Theory/Wave Theory way, but it became much more dominant in probably 2008 or 2009. Then around 2010 or 2011, I began to incorporate it a great deal into my NEoWave Trading service. It became an integral part of the service. Now it's probably the dominant part of my service.

Wave theory gives me the direction, but it doesn't give me any of the specifics of the trade. It's almost exclusively River Theory now that dictates how we're going to get in, where we're going to place the stops, and which timeframes we're going to trade. All that is much more mechanically and logically determined, not emotionally or forecasting-determined.

Interviewer: I see a major shift in your service in the articles and information you provide to your customers. Being a customer of yours for many years, I realize that as well.

In the beginning, you very much focused on forecasting. Sometimes it's really dead on. Of course, when it's wrong, it's wrong.

Now the forecasting is more used as a way of saying, "Perhaps the market is going to do this," but you would not recommend your customers enter a trade unless they get some kind of confirmation in your Neely River Technology to say this is how you're supposed to enter the market.

Glenn Neely: Right. For example, several people wrote to me recently saying, "You sank those B waves, and then you go back up toward the high." (This was a few weeks ago.) "Why don't we trade the B wave rally?"

This wasn't a public announcement. This was a private email. I said, "B Waves are very unpredictable. You don't know how long they're going to last or how big they're going to get. I don't know whether it's going to make a new all-time high or not, which it could. It makes it very dangerous to trade B Waves, so I'd skip the whole B Wave."

Then they started saying, "If we're not going to exceed the high or if it's only a 50/50 chance it might break the all-time high," which it did today and yesterday, "why don't we go short now because the risk is really low?"

I said, "The chances are pretty good that it's going to break the high. I don't want to put a stop there and go short before and make a pretty good chance we're going to be stopped out." If I'd taken that trade, we'd have been stopped out.

When it comes to Wave theory, the way I incorporate it with River Theory is I'm only interested in trading the impulsive or trending waves. I'm only interested in trading Waves 1, 3, 5, A, C or E.

I'm not interested in trading Wave 2, 4, B, D or X. They're just too dangerous. They're all countertrends. You don't know exactly when they're going to finish. You don't know how long they're going to take a lot of times. You don't know what structure they're going to take on.

They don't give you a lot of potential because they're going against a bigger trend in the other direction. You might go up 100, and the downtrend will only be half or a quarter of that. It’s sort of stupid because you’re not going where the big potential is. I always avoid trading B Waves, Z Waves, X Waves, 2 Waves and 4 Waves. I’m only interested in trading 1, 3, 5, A or C as a general rule.

Now that we’re potentially getting close to the C Wave starting of what I think is this current ABC correction, I might consider going short. Still, I think it’s risky because the downside isn’t that great. The really good trade is probably going to be the next buy signal after the psychology gets pretty scary and negative during the next decline.

You have to weigh what’s the risk to reward based on Wave theory? How much potential is there compared to the risk? Then I look at River Theory to give me the criteria of how to enter, where to place the stops specifically and how to move the stops. It’s really in the stop movement and the targeting, which is objective with River Theory. It’s extremely difficult with Wave Theory to know how to raise your stops while the market is trending and where to target your exit, because there’s almost no way to know a trend is coming to the end until after it’s over. There’s no way to know which lows are the right corrective lows to put stops, because you don’t know if it’s the first phase of an ABC or the end of an ABC. There are a lot of things that can’t be known until after the fact, so I find it very difficult to manage a trade once you’re in with Wave theory.

I only use Wave Theory to give me the direction. Everything else is determined much more scientifically and objectively with River Theory. I assume that’s the direction you’re heading also.

Interviewer: Yes. I’m trying to become as mechanical as possible.

Glenn Neely: How are you doing with that?

Interviewer: It’s great. Basically I spend two or three hours in the morning day trading. Since I’m a day trader, my timeframe is a little different than the service you provide, but I use that as more of a guideline. If I get a 1 move for the day, I’m basically done for the day.

Previously how I’d do it is literally watch the regular hours and the after-market hours and read all kinds of articles about market analysis and how things are supposed to go. Iôd hear all kinds of opinions about what people were saying. It was so stressful!

Right now my life has been simplified. Itôs really relaxing. I get hit by my daily stop limit, which I have a certain percentage Iôm willing to lose. When I lose that, Iôm done for the day. And the next day is a brand-new day. Some days I donôt even trade if it is really choppy.

Itôs been quite a journey to get to this point. Someone whoôs just getting started or is still struggling with that really has to take that paradigm shift to get to the point where they realize itôs not that complicated. You shouldnôt make it so complicated.

Trading is not easy, but itôs fairly simple if you have a certain type of rule on how youôre supposed to get into the market and how youôre supposed to get out. If you follow that to a T, over the long run itôs similar to playing poker.

Glenn Neely: As long as you manage risk.

Interviewer: Thatôs right. You have some kind of odds that you manage.

Glenn Neely: Thatôs been my experience too. I thought Wave theory was the magic answer to everything and that as long as I could predict the market, Iôd make a lot of money. It took me about 15 years to realize that wasnôt true.

Once I got past that and started to let the market do more of the dictating to tell me when the move stopped, I became more of a reactionary trader and not a forecasting trader. I didnôt worry as much about what I thought was going to happen as what I could prove had already happened.

When I trade now, itôs ñwhat has happened today that allows me to do something different about my current position?ò

Right now weôre in long T-notes. According to River Theory, if we have an up day tomorrow, Iôm going to be able to raise our stop well above breakeven. Iôm not anticipating that Iôm going to be able to raise the stop there. Iôm waiting for the market to do something that then tells me it’s okay to do what I was waiting to do. I wasn’t predicting it to happen. I was waiting for it to happen.

That’s a completely different approach from what most people do. They spend all this time trying to think what’s going to happen, and they take action on what has not proven to be reality.

Interviewer: That’s how I think my trading style has changed. Before, I had been very much of a top and bottom picker.

Glenn Neely: Yes, anticipating.

Interviewer: That’s right. Of course, sometimes I’d get to a good trade. It’s phenomenal because you hit on the spot.

Glenn Neely: That doesn’t happen too often.

Interviewer: Exactly. The probability of that is not high. Now I tend to be a trend trader where I try to get in. I will never make the most money and get the beginning few ticks or the last few ticks, but I try to get the middle, the meat.

That has also changed my life in terms of stress level as well. Before that, the multiple stops. It does some kind of psychological hindrance to your ability to feel good about your trading. Now it’s different.

Glenn Neely: Most people when they’re new to the business are so into the forecasting and so desperately want to make money that they think every day is the day the market is going to have a massive move, and that’s going to be the day they’re going to make a killing. They spend all their time planning for and trading for an event that’s extremely rare. Most of the time, not much happens.

It reminds me of a cohort of mine. I guarantee you for almost 10 continuous years, every week, every day, every month he was saying, “This is going to be the day the market is going to crash and the whole world is going to hell.” It was his relentless assumption.

We talk by email on a pretty regular basis, and I keep telling him, “You can’t get massive market moves no matter what you think, no matter how bad the statistical analysis is, no matter how lopsided the banking system gets or the credit margin ratios get ï no matter or whatôs going on. Until the public is obviously involved in the market, no major top or bottom can ever happen, not that Iôve ever seen in my lifetime. You always need extreme fear or optimism. The public is talking about it. Itôs on the news. People are involved. Itôs in the newspapers and on local television. It's either good or bad.ò

Right now, none of my friends are talking about the stock market at all. Iôm talking about outside of the realm of people in the business. If you go out to parties, nobody talks about the stock market. If you watch the local news, thereôs virtually no mention of the stock market, so we canôt be at the end of anything serious yet.

The only way the big traders can get out of their positions is if the unprofessional amateurs get into long positions. A necessary part of that phenomenon is that you have to create buzz and interest, which is sort of like advertising. That advertising is free, but it catches on with the public. As some people in the public start making more money and tell their friends. Those friends might get involved and make money. Then they tell their friends. It eventually creates this momentum of action and involvement that then is picked up by the news media and paper because theyôre feeding them the information they want to hear.

If the market is a very popular thing among a lot of people, then the media is going to start talking about it. The papers and magazines will start talking about it because they know people want to hear about it.

Until theyôre all involved and participating, you canôt have a major stock market top or bottom. Iôve told him for years, ñItôs just not there yet. Thereôs not enough involvement.ò

Once in a while there might be a juncture where it might be happening. Then Iôd take a short-term chance, but then it goes away for months or a year or more. Then we get to another juncture where it might be happening.

At this juncture right now, there clearly is not enough excitement. Even though he keeps quoting me all these statistics about how over bar we are and how thereôs so much margin debt in the market, I say, ñAll that is fine, but the final missing part which always has to be in place is this psychology of the market. There has to be a lot of excitement for a major top. There has to be a lot of fear and depression for a major bottom. And we are not there yet.ò

Interviewer: Yes. The major top I personally experienced was 1999/2000, the NASDAQ stock. Thatôs the time where everybody was talking about it. The news was always talking about some dot-com that had negative earnings and was still trading at a crazy price. I suspect thatôs the level of excitement youôre talking about for a potential market top.

Glenn Neely: Yes. My experience was that until the local media stations and local newspapers start talking about the market, youôre not at the up end. It almost always will involve low-level, non-financially oriented publications and news shows to finally mention the stock market on a relatively regular basis with some level of excitement. ñItôs been making new highs every month for the last year.ò

Thereôs some giddiness, excitement or optimism at the local newspaper and local television level. Thatôs when you create enough involvement by the unexperienced, amateur public investor to create a top or bottom in the market. We donôt have that yet. The minute you start seeing that is generally when the beginning of the end is near.

These are all the trends that Iôve experienced in my life. You mentioned 1999. The 1966 through 1972 through 1982 period where there was the peak in ô66, I was alive but just a kid. I experienced the 1980/ô82 pessimism period very clearly. There was the ô87 top, the ô88/ô89 bottom, the ô95 period of pessimism, and obviously the dot-com peak in 2000, the 2002 low, the 2007 high, the 2009 low, and now the current period. I think some time in the next three to six months weôre going to create another major market top.

Iôve experienced eight major tops and bottoms total in my career. From all those experiences, I can say we just donôt have the kind of broad-based interest we need in the market to create a top yet. I think itôs going to happen later this year. Weôre just not there yet.

Interviewer: Sure.

Glenn Neely: Do you want to call it a day? We've had some nice general conversation.

Interviewer: Some of these conversations might be more useful to most traders than some kind of analysis about goal or stock market. At the end of the day, everybody who gets involved tries to be successful. How they get successful is to be a better trader.

Glenn Neely: Hopefully we can lead them away from wasting five or 10 years trying to find the Holy Grail.

Interviewer: Exactly. I think you and I, as well as many other traders, have already gone through that. Perhaps some of those new traders can realize maybe they are in the wrong pass and eventually work on something in terms of psychology or risk management.

Glenn Neely: Right, and speed up their learning process.

Interviewer: That's right. Glenn, I really appreciate it. I'm looking forward to chatting with you next time.

Glenn Neely: I appreciate it. I'll talk to you soon.

Interviewer: Thank you

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