

Transcript

THE ARTFUL TRADER

Episode 2: Lose, Lose, Lose... Win! The 7 Year Itch with Ray Barros

Michael McCarthy: The 7 Year Itch. How seven years of straight losses taught this trader one of the toughest lessons in the business.

Ray Barros: There's no such thing as quick, easy money. Trading is the hardest profession in the world. But it can be taught, you can learn it, and if you are willing to put in the effort you will be successful.

Michael McCarthy: Ray Barros managed to turn seven years of losses into remarkable wins, and now he wants to give something back. He set up a training program, and is teaching newer traders the skills he learned the hard way.

Hi, and welcome to The Artful Trader. I'm Michael McCarthy, the Chief Market Strategist at CMC Markets, Asia Pacific. In each episode we unlock the secrets behind the highs and lows of the industry's experts, and discover their journey to mastering the art of the financial markets. In his over 30 years of trading Ray Barros has seen many traders, both beginners and experts, mistake luck for skill. He was one of them. He has made all the mistakes in the trader's manual, and then some. But after carefully studying his losses, he developed an approach that gives him a winning edge. Ray retired from managing a private hedge fund 2010, and is now teaching and mentoring others. His biggest piece of advice, let's find out. From Hong Kong, welcome Ray Barros to The Artful Trader.

Ray, you're a brilliant student at Sydney University's School of Law. As a lawyer you were hugely successful, and then you turned to trading. Seven years of straight losses. That must have hurt.

Ray Barros: Oh absolutely. I mean I sold the legal practice, and in 18 months I gave it all back. Then my wife supported me for the next five and a half years or so. It was difficult, I've got to tell you. Because I like to say when I'm doing a lecture sometimes that Chrissy used to bring money in through the windows, and I was tossing it out the front door at almost twice the speed that she brought it in. She was supporting the family. In that seven years I dropped about 750,000 Aussie dollars. It was a long, hard journey.

Michael McCarthy: So what was it like in those early days? I mean it must have put pressure on your relationship with your partner.

Ray Barros: We've been married for 50 years.

Michael McCarthy: Congratulations!

Ray Barros: Thank you. I was going to say I've been married for 50 years because she has been such a wonderful kid. I was trading, and I kept losing money. I blew my account for the umpteenth time. I said to her, darling please, I've learned my lesson. Just fund me once more, just this last time, I promise you. I promise you I'm going to be different. So she gave me 25 grand, and were trading the S&P minis, which in those days was full. We have \$500, we didn't have the mini. Sorry, the previous S&P is \$500 a point. We were doing about a seven point range on a Friday night. By the end of trading on Friday night I bought every high, and sold every low, and I had blown the 25 grand.

Michael McCarthy: Wow.

Ray Barros: Honestly she never said a word. Many years later when I was successful it was a different story. She let me have it then. But in those years when I was struggling, she never said a word. I was so lucky to find her.

Michael McCarthy: Losing like that for a long period of time can take its toll on even the strongest traders. What are your thoughts around building and maintaining that resilience?

Ray Barros: Part of it is I got into transcendental meditation when I was in university, and that helped a lot. Now the modern research shows that mindfulness meditation, or any type of meditation, but especially mindfulness will help you settle your doubts about yourself, if I could put it that way. Also I was very lucky, I came from a family background that basically said you can do anything you want, as long as you set your mind to it and don't give up. So it was difficult. I won't say it wasn't difficult. There were times when you just wanted to chuck the whole thing away and say, what's going on here? Am I really suited? So all those things helped. Chrissy being supportive, my family background, transcendental meditation. All those things came together and just gave me the resilience to keep on working.

Michael McCarthy: So it sounds like confidence and self belief are key characteristics of traders?

Ray Barros: I think they're absolutely critical. Trading is the only game in the world where our hardwiring is against us. We move away from pain and into pleasure. In trading we tend to look at losses as painful, and yet it's part of the game, it's a necessary cost of doing business. If you can keep your losses small, which means you've got to accept them, and take them as early as possible without fear, the market will then go your way. So confidence and self belief are absolutely critical.

Michael McCarthy: Do you think there are other qualities that constitute natural talent in a trader?

Ray Barros: I'm not a big believer in natural talent. I think the good thing about trading is the fact that you don't have to be the best in the world, you just have to be confident, because 90 percent of the population is giving you money. I think probably one of the things that I've found more than talent, there's a new therapy out there called acceptance and commitment training, or acceptance and commitment therapy by Russell Harris. I think he's from Australia. That has helped a lot. I think applying that, and those ideas are much more helpful to a trader than natural talent.

Michael McCarthy: So you can work your way up to being a good trader.

Ray Barros: Absolutely. This is I think one of the things, that the traders coming up nowadays don't appreciate just how lucky they are. They have some very, very good trainers around the world who are genuinely trying to help you. When I first started all we had in Australia was get rich quick, buy my system and you're going to be rich tomorrow type thing. We didn't have any of the basic psychology, money management. None of those things were available to us. I had to fly to the States to do Pete Steidlmayer's market profile to get introduced to these ideas. So I think that you can certainly work up to it. As I said, I think the generation of traders today are very, very lucky.

Michael McCarthy: I'd acknowledge that as well. So who taught you?

Ray Barros: Well Pete Steidlmayer. I said, I don't know whether the audience would be familiar with him. He was around in the late 70s, early 80s. He brought the market profile into prominence. I flew across the States. I remember that very well. Because I said to Chrissy, can you afford to send me? She said, okay, but I'm going to be on \$5 a day living expenses. We only got our own flat, thank goodness. Off I went to the States. Peter turned me around.

Michael McCarthy: Peter Steidlmayer, isn't he a co-author of one of the best little books on the markets, Market Logic?

Ray Barros: Yeah. Markets and Market Logic. Peter has written about four books. He wasn't the easiest person in the world to understand. If you read Markets and Market Logic you'll see what I mean. But his ideas were fantastic. For example, you and market understanding equals success is one of his famous statements, and that's certainly true.

Michael McCarthy: What were some of his other ideas that really resonated with you?

Ray Barros: Well to me he focused on managing the trade. He said your entry is important, because if you can enter it in a nice spot, then you have less angst about the market going against you. But you're never going to buy at the exact low, and you're never going to buy at the exact high. What you can control is managing the

trade once you're in it. He said the best trades are where you're wrong, and you have given yourself enough time to exit without loss. That really resonated with me.

I won't say I went to a seminar and became an instant trader. I think it took me 9 to 12 months before I turned the corner. But at least he gave me the ideas to work with. That has always been the focus of my trading. If I want to improve on looking at how can I exit a little bit earlier, how can I tell when my trades aren't going to go the way that I want them to go. Putting aside the fear that the moment I exit, it's going to go my way. That's what Pete taught me. He said, look if you exit early, and you're wrong about the exit, you can always get back in. Don't worry about exiting early. You look at the structure of the market rather than price to determine your exits, and I thought that was fantastic.

Michael McCarthy: So one of the keys is living to trade another day.

Ray Barros: Yeah. Really managing your losses. So the more you can reduce your losses. I don't think you can control your winners that much. In the sense that you get into a trade and the market will do what it will do, and you do the best you can to manage it. If it's a choppy market, you're probably going to be in and out many times looking for the right spot to get back in. If you take those losses as being really tiny, then you can have ten losses in a row. If you're losing maybe 0.01 percent each time then it doesn't hurt. But if each time you lose it's going to cost you three or four percent, that's a whole different ballgame.

Michael McCarthy: Your father was a trader as well. I imagine some of his lessons and values were passed onto you. What did he teach you about riding the wins and losses in the market?

Ray Barros: Dad was a wonderful investor/trader, and he didn't want any of his children involved in the markets I'm afraid. He came from the classical, their background was very much the children are going to be professionals. Become a lawyer, become a doctor, become an accountant, become a teacher. So all of my brothers and sisters got university degrees, and there are eight kids in the family. So I didn't really get into trading until he passed away. But what he taught me was self belief, perseverance. If something is not working, don't keep repeating the same mistake over and over again, go find out what you're doing wrong. Success comes from making errors. Usually you're going to learn more from your errors. If you can accept those, you can fail 10,000 times, but that's only one step towards your journey of success. That's I think what he gave all of us. All of the children have that same attitude.

Michael McCarthy: You served a very long apprenticeship. You've been a very successful trader for many years. Now the wheel has turned, and the student has become the teacher.

Ray Barros: Yes. Absolutely. Fortunately from my point of view, Chrissy always comes to my presentations when we're trying to fill the class. I'm not as successful a teacher as I am a trader, simply because she says I sell hard work. I'm not an actual salesman, so I pick up those skills. Whenever I do a talk about people wanting to be traders I'll say, look, it's the hardest profession in the world, tell them what it's like, and tell them how difficult it's going to be. It's no wonder I guess that people don't sign up, I make it sound too difficult. It is a difficult profession.

Michael McCarthy: Well you're telling the truth, right?

Ray Barros: Well yes. I mean people come to these things, and the question is I've got \$2,000, and I want to make \$100,000 a year. You've got to tell them, that's not going to happen. If you can make 15 to 20 percent per year you're doing extremely well, you're doing very well. In fact the first year, if you haven't made any money the first year if you can break even, you've done well, and then incrementally go from there. But I've been very lucky. I've got some great students that have come through the classes. Really they've become friends. They've taught me so much, simply from their questions. Things that I take for granted they will ask. Suddenly I think, why didn't I think of that? Seeing it from that perspective. That opens up my perspective, and it makes me a much better trader.

Michael McCarthy: So do you get together with your former students socially?

Ray Barros: I meet them socially. We talk on the net. We've got a small trading group on the net. I'm always trying to improve my trading. So whenever I come across something that I like, or I've taken a course that I like, I will pass the ideas on. They do the same. So it's on an ongoing trading group. One of the things that has come out of recent research that has been quite useful for trading is that you're better off in a group. They hold you accountable. If you organize the group properly, it's called flip the classroom. This new mode of teaching includes group learning. This group learning structured properly is a very, very big help to a trader I think, because essentially trading is a lonely profession. If you can have a group behind you, it just makes life so much easier. You've got support. Sometimes spouses don't understand, and the group there helps both you and the spouse. We've got a good group going.

Michael McCarthy: I'm sure many of our listeners would love to be in that room one time. What's it like to be in the room? How does the conversation go? What's the feel?

Ray Barros: We try and have one once a week. Not everybody turns up, but we start off. Each one will say how they're seeing a particular market. So we try to allot markets to certain people, to certain groups. Say Mike, next week you're going to be on the [? decay], or Ray, next week you're going to be on a couple of currencies, or whatever it might be. We then give the views, and we tell the group what we're

planning to do. Then the following week when we do the follow up what happens in the group is you tell them whether or not you've followed your plan. If you didn't, why you didn't.

Telling others what you're going to do makes it more difficult to trade impulsively. Then if you do trade impulsively, the group knows about it, then they're going to ask you why, what happened, what are the circumstances. They offer their two bits. Out of that interaction you might dismiss 90 percent of what is said. But this ten percent that you retain, you use to make yourself a better trader. What happens here is that if you keep hearing yourself say the same mistake over and over again, you're more likely to do something about it, than if you just sat alone with your own thoughts, because you're not accountable to anybody then. But now if you're talking to someone, it's a public shame, whatever you want to call it. Especially in the east Mike, you know what face is like.

Michael McCarthy: Yes.

Ray Barros: It makes a difference.

Michael McCarthy: It's a very powerful pressure. We all have to struggle with that temptation to trade off our impulse. That sounds like a very powerful way to overcome it. Ray, you've been quoted many times as saying, listen to the trader talking about his losses, not the one talking about his wins. Because the one studying and learning from his losses is likely to be the better trader.

Ray Barros: Yes. The thing is when you make a mistake, you've got to distinguish between mistakes and losses. So I don't worry too much about the outcome of a trade. You have no control in a sense about the outcome. What you have control over is the process. The mistake is not following the process. So if you find that you're making the same mistake over and over again. You might not follow your plan. Recently we had a talk in Singapore. A chap got up and said, look, I've been to many courses, I've spent a lot of money, but I don't seem to follow whatever they've taught me. We sat to talk a little bit afterwards. We found there were certain social environments, certain events would happen in his life that would almost invariably lead him to breaking his rules, if I can put it that way. That's what I mean by learning from your losses. If you identify, what is it I'm doing?

There's a good quote someone once gave me a long time ago. He was a psychiatrist I got friendly with. He said, if you have an outcome that you want, and you have a series of behaviors that lead away from that outcome, and each of those behaviors have what appears to be a really good reason, forget the reasons. They're excuses. Look at what you're doing. Look at the behavior, look at the result, and find out the reason for the behavior. That's what's going to put you on your way. I think that's the best summation of my approach to losses. I'm doing something, it's resulting in

something I don't want. What are the conditions under which that behavior is being executed? How do I change that behavior? That's what I think is really important.

Michael McCarthy: I can understand why your method has been so successful. It sounds like you're constantly honing it. Generally when traders get together, we hear a lot about the successes. But losing trades can be just as memorable. Is there any trade that you recall particularly that really taught you something?

Ray Barros: In terms of losses or profits?

Michael McCarthy: Well we might do both if you don't mind.

Ray Barros: Let's do the losses first. We had a situation once where about 18 months ago I had a particular view I think on the dollar CAD. Because I do what I call an 18 day swing trader, a monthly trend trader. But I execute say on the 60 minutes of when I'm getting ready to take a trade, I'm relaxed, and I'm focused. I'm letting it set up. As soon as I see the setup and trigger, I pounce, right? That's the theoretical, the way I should approach it. I also know that if I get very tired, I should not be trading. That night we had a number of social engagements, blah blah blah, and I was pretty exhausted. I just wanted to go long I think, or go short, I can't remember now. Let's say I wanted to go long. For some reason I went short. It cost me 200 pips to reverse the position from where I got in. You look back on that and say, I ought to know better. I know I'm going to trade poorly if I'm tired, and yet I did it.

Michael McCarthy: I'm sure we've all been in a similar situation. How did you feel the next day, after you had had a chance to recover?

Ray Barros: Not good. But there is a thing that Russell Harris said, you have to accept it. Blaming yourself, and being down on yourself doesn't do anything. Just work out the why, the circumstances. So in this case I was tired. Likely it's 18 months ago, and I haven't traded when I'm tired since. That was a reminder that no matter how good I think I am, certain rules apply, and you've got to keep to them. But on the profit side let's talk about a story which is verifiable. This is actually on the blog. I have a particular strategy, which I now call the Brexit strategy. Essentially it's a situation where if you look at it objectively, it's a 50/50 chance of that event occurring. So with Brexit if you looked at all the polls, and you looked at where the polls were being taken, you could say, well in the educated areas like London and so on there was a very strong consensus that Britain would stay in the European community. If you went out to the working class, lower middle class areas, there's a strong consensus that would not be in their favor. If you followed this polls, this was very clear. Yet prior to Brexit the market rallied, the sterling rallied very, very strongly.

So I was recommending in the blog that people cut their position size down, because if you were wrong, and people didn't move outside of Brexit, and you did go short for sterling, you could be down 300 or 400 pips very quickly. But if you were right it was

going to make a big move in your favor, and the risk/reward was really, really good. I call that the Brexit strategy. The idea is to enter just before the result comes out, if you can. So I entered after New York closed. The market rallied a little bit more, sold at high, and then the results started coming in. That was probably one of my best trades I think in the recent past.

A guy from my thoughts on the blog wrote to me thanking me. He said he made over a million bucks. He said, you don't have the courage of your convictions, because I only put a 25 percent position size on. Because I figured, as I said it's very important you pick your position size down, because you're going to make up in volatility what you'd normally make up with your position size. I thanked him of course. I said, I'm glad you made a million bucks. Thank you for your comment about me not having the courage of my convictions. Imagine if I had been wrong, he'd be writing to me to you know. [Laughs].

Michael McCarthy: [Laughs]. Well off the top of my head Ray, there's something like 1,200 pips available in that hour or two after the result was clear.

Ray Barros: There was.

Michael McCarthy: Sorry, did you shut the trade down almost immediately, or did you swing with it?

Ray Barros: With this kind of trading you cut it off when you think the low is in place. That's not hard to tell, because part of my approach to markets is wipe off the year, and you've got a selling climax. So there are some very objective rules about when a low is likely to be formed. It has to spike down. You have that X with people, and access low and so on.

Michael McCarthy: To the moments after you had closed the position, you've exited. What was going through your mind?

Ray Barros: Just strategy works. I try not to get too depressed when I'm in a draw down mode. We all get them. In those times whatever you do, whatever has worked in the past just refuses to work. So you reduce position size, you get out earlier, and so on. Similarly on the big profits where you think, wow, that was a really good trade. Fantastic. You try not to get too carried away. But I felt good. Obviously you're going to feel good. You take a good profit, and the trading works out the way it does. It more of a kick out of the replies. Not so much the outcome of the trade, but the emails I got, and the comments I got on the blog. About people taking the trade and not following instructions, and getting stomped out, and them not getting back in. That sort of thing was instructive.

Michael McCarthy: You've seen a lot of the markets. You've been in them a long time. Clearly there are trends in markets, and approaches markets. How has trading changed over the course of your career?

Ray Barros: I think we're seeing less trending moves. Although if you look at the ES for example, that has been a very strong up trend, which looks as though it might continue, but we'll see what happens. I think the fact that we've got instant news now has affected the way traders react to markets. In the old days we used to say, markets get a little bit [? 23:34]. They tend to tell you what the economy is going to do further down the track, and I don't think that's true anymore. Traders nowadays react off the news, and are just as impulsive, if you will, as the retail trader. I'm talking about the institutions, because they move the market. They're reacting off the news. A new bunch of kids that are in the market nowadays react off the news, and Brexit is a classic example. I don't think that would have happened as much in the old days.

So we're seeing less trending moves, especially in the currencies. We're seeing more [? whip] source. So you need to be a little bit more nimble, if you will, about exiting your poor trades. If something is not working, you've got to exit it earlier rather than later so that you can go back in. Because the market has changed so much that much more quickly. The indices are a bit different. Because of QE we've taken the floor away from shorts, if I can put it that way. We've got a floor for the support of the up trend. Although the federal reserve has said it's going to stop, has stopped QE.

There is still a lingering belief, talking to the people, friends of mine that are in the game as hedge fund managers and so on. There is still a lingering belief that if this market dies tomorrow, if we have a huge crash of the stock market tomorrow, the fed will come back in and pump the prime again. There won't every be a way from the market. You won't return to the normal status, as far as the stock indices are concerned. I'm a little bit concerned about that, simply because as some point pump priming, if it continues the way they've been doing it for the amount of money they've been putting into the system, at some point that's going to stop working.

Once that starts to reverse, when we start going back to normal, interest rates have to start going back up again. I belong to the Austrian school of economics. I believe that really does forecast what the economies are going to do. I think we're going to be in for a very, very deep recession, depression type situation, simply because we've had years of pump priming. It's just going to be very interesting to see what happens between now and say the next four or five years. Whether or not we're going to get a top in these equity markets.

Michael McCarthy: Right. Often as traders, and particularly equity market traders, we make our biggest wins when our market falls. Do you think that that introduces a bias into the way we think about markets?

Ray Barros: I don't think that that's true for traders in general. I think in general each trader has a bias. I know for example, one trader who trades the Aussie dollar always looks to the short side, never looks to the long. I think there is a bias at the

moment for the long side. You're sure you're going to get people who want to short the markets from going too high, they're going to sell it. That's there, right. I probably fall into that camp more than I would the long side. But I think the majority of people at the moment, as far as the equity indices are concerned, is that they do favor the buying dips. They think, if I buy a dip I'm safe.

The problem with people like myself who remember the '87 crash is that this market looks to me to be running out of steam. In the old days we could look at volume and range to give us some idea of whether we were talking [? 26:53]. But again, QE has distorted the signal, so that's not available. So I'm not sure that that's true Michael. I think it's true perhaps for me, and maybe people of my generation. Where we went through '87, we went through the 60s and 70s where the market was going sideways to down. Because I started trading when I was at university, and lost money obviously, then gave it away.

Then again '87, that was my first profitable year. The only reason I was profitable that year is because I was short Black Friday. I went short on the close on Friday. I remember walking into the broker and Monday. In those days of course we didn't have terminals where we could sit there and watch the Reuters green screen and chart by hand. My broker, the guy who denied this guy, was pale. I walked in and said, what's the matter with you? He said, it's down 100 points. I said, okay, so the Dow is down 100 points. He said, no, the Dow is not down 100 points, the S&P is down 100 points. I thought, okay, how much is that in dollars and cents?

Michael McCarthy: So what's really coming through here Ray is that you're always learning, and you're always adapting to changes.

Ray Barros: Oh absolutely. Michael, markets continually change. Learning behavior changes. So yeah, I'm always learning. I never stop learning. One of Chrissy's pet peeves is that we need to keep giving away my books, because otherwise I just wouldn't have space for it in the library. The Hong Kong library said to me, any time there's a [? 28:36] of books that are immaculate, you can give it to us anytime. Every 18 months or so if I don't send them some books they write to me now and say, have you taken us off your list?

Michael McCarthy: I see. You're clearly in demand. So Ray, listening to you it's clear that you have a real affection for markets and trading. Why do you love it?

Ray Barros: Mike, just think of it this way. There is nothing else in the world out there, as far as I'm concerned, that puts the management of my enterprise, whatever I'm doing to make a living, totally within my control. I fall or I succeed based on my judgment alone. That's it. There's no external. You don't owe anything to anybody else. Even if when you're teaching you might think you can help X,Y,Z students. But if they don't want to be taught, if they can't see the value, if you can't. You can show them all the reasons in the world, emotional and rational reasons why they should do

X,Y,Z, and if they don't want to do it there's nothing you can do about it. That doesn't happen with other markets. If I want to make a profit, I have to do X,Y,Z process. If I follow that process over a large sample, I will make money. That I know just from the results of the trading. If I break X,Y,Z process I might make money on this straight, but over a large sample size I'm going to lose money. So that's one thing that's totally within my control. Success or failure is in my hands. So that's something I really love. I value that independence. The second thing is it's the only profession in the world where 90 percent of the people who are your competitors are giving you money. I mean where else are you going to get that?

Michael McCarthy: Very true. And very attractive.

Ray Barros: Yes it is. I only like to say to traders, or people who are listening to this broadcast, there's no such thing as quick, easy money. Trading is the hardest profession in the world. But it can be taught, you can learn it. If you are willing to put in the effort, you will be successful. It doesn't need any talent. You only have to be [? competent/confident]. You don't have to be the best to make a very, very good living. You can become really wealthy out of trading. But you need to do the right thing. You need to follow the right processes. So forget about making 20 million dollars on a \$1,000 account next year, just do it slowly step by step. The younger you are when you start, the easier it will be over time, because compounding is such a great tool. You certainly get emails from people, and emails from the spouses saying, thank you so much for helping. If it hadn't been for your help, I don't know where we would be. That sort of thing. That makes my day. I have to say that's worth a million bucks.

Michael McCarthy: Right. It has been fascinating, and a lot of fun. Thank you very much for your time and your generosity today.

Ray Barros: Thank you sir.

Michael McCarthy: That was Ray Barros. You can find Ray's best advice for newer traders in an exclusive Artful Trader blog post. Read it now at theartfultraderpodcast.com, where our podcast listeners can also access some limited time offers. The Artful Trader is an original podcast series by CMC Markets, a global leader in online trading. The information in this podcast is general in nature, and does not speak to your personal financial situation. To stay up to date with the new episodes, subscribe now on Apple Podcasts, or wherever you get your favorite podcasts from. Make sure you share it with your friends, and leave us a rating. I'm Michael McCarthy, and this is The Artful Trader.