

## The Role of Emotions in Trading

There is a lot of misinformation about the role that emotions play in your trading.

Did you happen to see the Reuters report back in September titled “Wanted: psychopaths to make a killing in markets.” The article outlines research that shows people who have emotional impairment in their brains or who are just unemotional ‘functional psychopaths’ make good financial decisions when handling high risk. Let me quote the article: “In a study of investors’ behaviour 41 people with normal IQs were asked to play a simple investment game. Fifteen of the group had suffered lesions on the brain that affect emotions. The result was those with brain damage outperformed those without.”

While the tone of the article was somewhat tongue in cheek, it reveals a misbelief about emotions in trading and in life in general. The misbelief can be summed up thus: you can only be successful when your emotions are gone.

The truth is that emotions go with you everywhere. You can’t, unless you have brain damage or are psychopathic, not have emotions. Denial of your emotions is unproductive and unhealthy.

Well the question arises, how do I become successful if I do have to acknowledge my emotions?

Successful trading is first and foremost a doing activity. You do things, i.e. manage, to work you winners and cut your losers. Therefore one can acknowledge one’s emotions and still perform correctly. You don’t have to let the emotion distract you from the actions and tasks that are imperative for your success. The metaphor I use is that the emotion is a back seat driver. Better if you take control of the steering wheel and operate sound strategies that will make you very profitable. In other words you have to do things that in the emotional arena don’t feel good. A jumbo jet pilot can’t say: ‘I’m not landing the plane today because I don’t feel like it.’ Professional people detach from their negative emotions to perform well. And guess what? The distracting negative emotions gradually transform into positive ones that are associated with their success.

Because trading involves the management of risk and uncertainty people automatically default to the negative emotions of fear and anxiety. Often rational actions are distorted by the ‘fright and flight’ that these strong negative emotions produce. In this I agree with the sentiments of the Reuters article. Fear and anxiety create poor trading outcomes. One way to deal with your emotions is to replace negative emotions of fear and anxiety with positive ones such as calmness, presence and self belief. The emotional lobotomy that the Reuters article hinted at is not required!

In the Reuters article Professor Baba Shiv of the Stanford Graduate School of Business states that emotions serve an adaptive role in speeding up decision making. Nevertheless he claims the natural yet negative emotions associated with risk inhibit wise decisions. If we can replace uninitiated negative emotions with positive purposeful ones we allow not only better but also faster trading decisions.

The real information about emotions in professional trading is that they exist, don’t have to be negative, but can be transformed into a powerful yet passive ally in your quest secure the outcomes you desire. Furthermore there is a suite of deliberate and purposeful strategies we can employ to stimulate, if you have the will, your emotional transformation into the zone of peak trading performance.