

Why Can't Most People Buy the All Time High?

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Supported by the
Incline Village Trading Tribe

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Dedication

I dedicate the paper to my wife, Jessica, and my parents, Drs. Elizabeth and Thomas Vician Sr.

Acknowledgements

I send special thanks to my wife who supported me through rough patches and helped keep me on task. Her encouragement provided wind in my sails.

I thank the Incline Village Trading Tribe for helping clarify my thoughts and review my work. The collective critique process challenges, frustrates, and inspires. Members include Ed Seykota, Easan Katir, Todd Hurlbut, Matt Johnson, Sven Hemmert, Jason Dekker, JoAnn Hankin, Jake Carriker, and Jason Russell.

Finally, I thank Gordon Corbett and Edward Kim of the Toronto and San Jose Trading Tribes, respectively.

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Introduction

Trend following makes sense and money. Yet most traders, investors, and portfolio managers cannot do it. People fail to implement many important components of trend following systems. One such component is the historical price breakout. Most avoid it. Many decry it. Successful trend followers buy it. Why can't most people buy the all time high?

Hypothesis

The difficulty is emotional. People who are unwilling to fully experience uncomfortable feelings inhibit themselves from buying historical breakouts.

Explanation of Hypothesis

The historical breakout is one of trend following's important entry signals. However, this event triggers very uncomfortable feelings by its very nature. Most persons avoid historical breakouts to sidestep having to experience untenable emotions. People do not like, or negatively judge, these feelings that arise. With this negative judgment present, people become unwilling to fully experience their uncomfortable feelings. This seems to agree with a common heuristic: Avoid doing things that feel bad (like fully experiencing uncomfortable feelings); do things that feel good instead.

One quick, effective, and common way to avoid experiencing uncomfortable feelings is to rationalize. People make all sorts of excuses to avoid entering markets at historical breakouts. Rationalizations are excuses and justifications to avoid experiencing untenable feelings. Indeed, they sound quite reasonable when compared to the loathsome option of fully feeling very uncomfortable emotions.

Most people are unaware of this dynamic. Ironically, they become aware when they fully experience their untenable emotions. Willingness may require the removal of negative judgment about uncomfortable feelings. Even negative judgment has a feeling associated with it. Removing this feeling behind a negative judgment requires its full experience as well. Only then do people become willing to fully experience and reintegrate their original, uncomfortable feelings about historical breakouts. This process dissolves seemingly intransigent emotional difficulties or inhibitions associated with buying the all time high.

How can people learn to do this? A robust method is the Trading Tribe Process (TTP). Ed Seykota, featured in the book *Market Wizards*, is the creator and guiding force behind TTP (www.tradingtribe.com).

Anecdotal Example

The following example offers a demonstration of this hypothesis. It describes the story of Jeff and a trade. Jeff's experience is an anecdotal amalgam. It includes the author's eleven year

experience as a successful trend follower, his study of other peoples' difficulties with historical breakouts, and his advanced work with TTP since 2003.

Chart 1 – October 26

Jeff's system highlights a stock due to very strong price action. He places it on his watch-list to monitor it as a potential trade. He marvels at the strength of DIGL as it surges from \$10 to nearly \$20 in just eight days. He notes its historical high at \$23.75. "Wow! This stock really moves," he thinks to himself. Yet, an uncomfortable feeling of apprehension begins to grow as he ponders buying the historical breakout. His somatic experiences of apprehension are mildly clenched teeth and a light pressure in his chest. Almost immediately, Jeff does not quite like the way he feels about buying DIGL. He is uncomfortable and not at ease. "I'll keep watching the stock. Moving so fast from \$10 means it needs to take a rest before it goes much further." Thinking about a needed consolidation makes Jeff feel a little better. His apprehension eases somewhat, but he still has some light levels of residual teeth clenching and chest pressure.

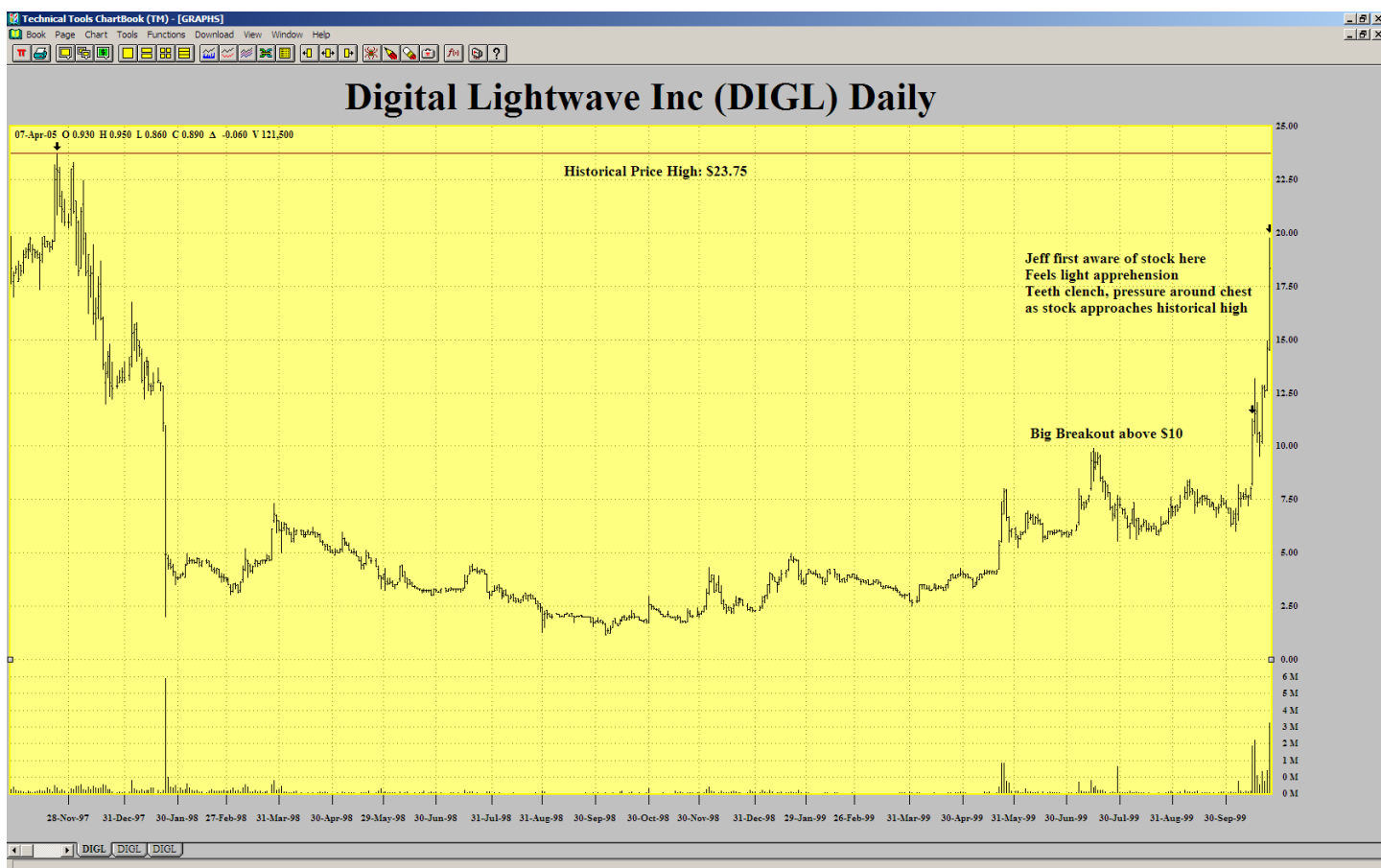


Chart 2 – November 2nd & 3rd

Despite Jeff's need for the stock to pause to make him feel better, DIGL continues to rise. Jeff's smoldering apprehension greatly intensifies as the stock consolidates only four days before surging to just under its historical high at \$23.75. His molars clench hard. His jaw hurts and feels tired. The pressure in his chest tightens like a constricting band. The stock hits its historical high. Jeff's apprehension reaches the intensity where it tips over into fear. He feels scared to buy the stock, and he really dislikes this feeling. In lockstep, a flood of reasons to cancel his order enter

his mind. He thinks, “This stock can fall so far and fast from this height. Where’s the pause to refresh? You’ll end up buying the top of the move if you enter now. Look, you missed the majority of the run from \$10 already. It’s almost done. You know you can easily get whipsawed on this one without a consolidation. Did you really do enough research on this company?” With this seemingly encouraging and supportive self-talk, Jeff does not follow his system and avoids buying DIGL. Immediately his jaw pressure decreases, and his constricting chest band loosens. His self-talk soothes him. Jeff doesn’t have a position, but he feels much better. Feeling better is good.

All of Jeff’s common rationalizations are excuses. They are a justification against buying the historical breakout and fully experiencing his concomitant uncomfortable feelings. More importantly and mostly overlooked, the act of rationalizing is a tool Jeff uses to generate enjoyable feelings. Like most people, he feels better when he rationalizes. Somatically, it gives Jeff a subtle, comfortable sensation of warmth and calm through his body. He displaces and alleviates his untenable feelings of intense apprehension and fear with these enjoyable feelings. While Jeff feels much better, he second-guesses his trend following entry signal and lacks a position in a strong stock.

Jeff sees DIGL reverse direction sharply and close well under its historical high. His decision to cancel his order seems to be the right one. He thinks, “Ah! Finally, here comes the pullback! Nice call to avoid the whipsaw. I made the right move!” The market validates his rationalizations. Jeff feels great. He decides to stop watching the stock intraday and check on it after the close. He reasons that the reversal is large and comes after a big move already, which portends a likely, upcoming consolidation.

Jeff calls a good trading friend who, not surprisingly, has a similar difficulty buying historical breakouts. Greg also validates Jeff’s decision. He tells Jeff that his reasons make a lot of sense. “Look, you didn’t get whipsawed like everyone else. That’s the worst!” he says. Somatically, Jeff’s jaw feels relaxed, and his chest expands freely. He feels calm and warm from his rationalizations that turn out to be correct. This is by far the best Jeff feels since discovering the stock. He figures to buy shares of DIGL between \$17 and \$20 on the impending pullback. He splits the difference with a buy limit order at \$18.50.

On a deep level Jeff gets what he wants. He makes an emotional trade. He avoids fully experiencing feelings he really dislikes. For that benefit, Jeff must skip buying a very strong stock at its historical breakout that may continue a forceful up-trend. It is far more important to avoid his uncomfortable feelings than it is to follow his system and potentially profit. For now, Jeff feels great and waits for DIGL to trigger his order to catch the dip.

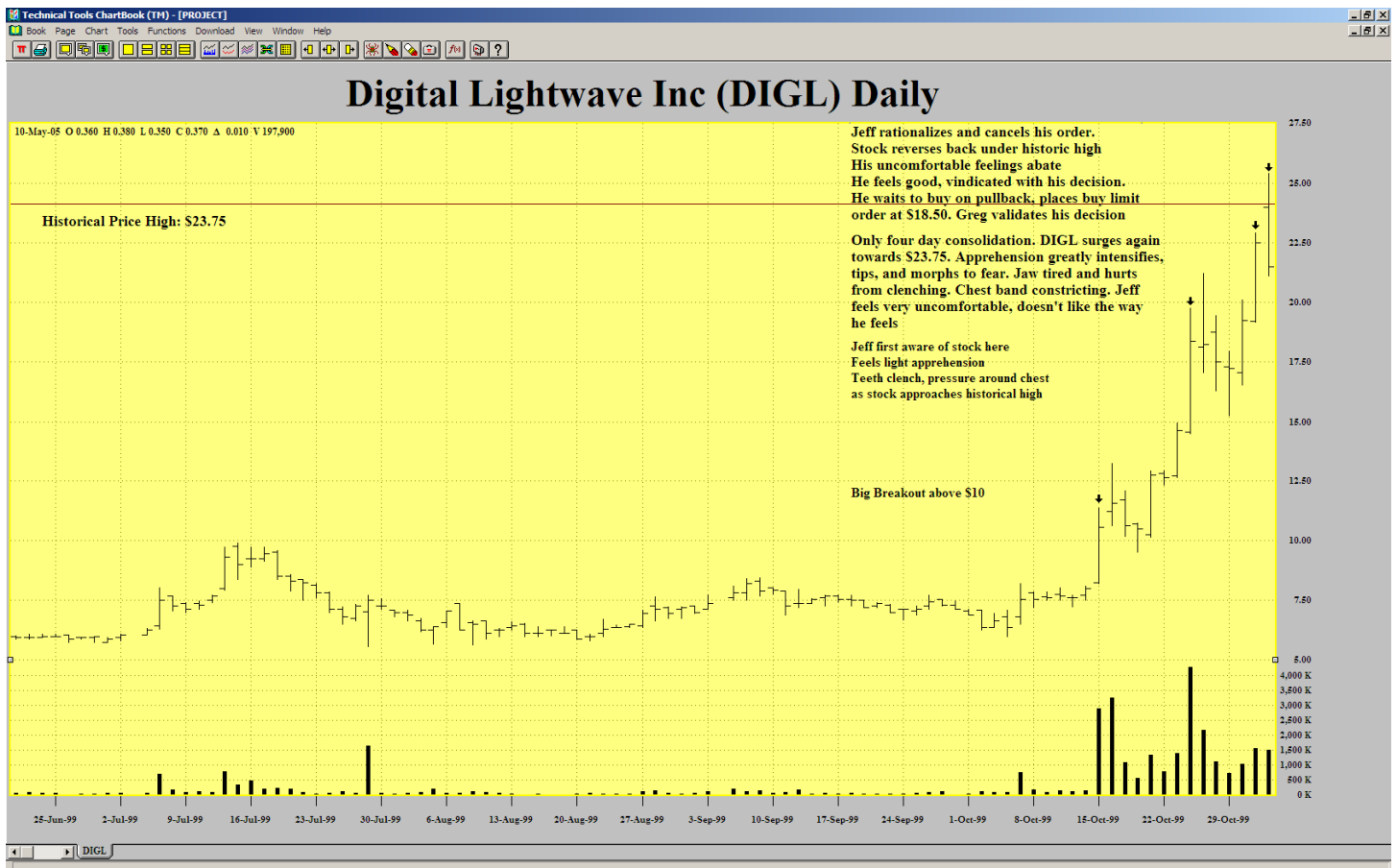


Chart 3 – November 5th

Despite all Jeff’s rationalizations, two days later the stock skyrockets higher by more than 50% in a day. It never comes close to his buy limit order at \$18.50. Checking his watch-list after the close, Jeff stares at his screen in disbelief. Very strong somatic feelings of apprehension and fear immediately reappear. His jaw clamps shut to its tensest level thus far. His chest band constricts so tightly that he momentarily loses his breath. However, these feelings quickly dissolve and morph into a new one that suddenly appears. It is frustration.

Jeff’s frustration is a familiar emotion which has five somatic parts or forms. First, he feels a cool, numbing feeling shooting down through him. It feels like liquid dumped over his head which cascades down his body. Second, he shakes his head and clenches his fist. Third, his lips purse and tighten. Fourth, he mumbles to himself, “Another one got away. Trend following is just so hard. How was I supposed to buy *that* stock? Can I really do this?” Fifth, he feels a hole or pit in his stomach. Feeling intensely frustrated, Jeff removes the DIGL from his watch-list as well as his system’s stock universe. His feelings of frustration lessen immediately. As they decrease a bit more over the next day, an idea flashes in Jeff’s mind to do some research to create a new set of system parameters to help him buy these “crazy” historical breakouts. This makes Jeff feel much better as he gets to work. His uncomfortable feelings of frustration disappear.

Jeff’s search for a new, different, or better set of trading system parameters is a typical response. Most people cannot handle the emotions that associate with executing simple parts of a robust trend following system like buying historical breakouts. Indeed, many people institutionalize their unwillingness to experience untenable emotions. They remove historical breakouts

altogether as an entry trigger from their system. It is just so much easier to change or abandon a robust parameter than it is to work on oneself, especially when it comes to feelings that people hate experiencing.

Indeed, the very robustness of some simple trend following parameters derives from their very ability to elicit extremely untenable emotions. People are adamantly unwilling to follow them. They cannot handle the intense emotional discomfort to which these parameters give rise. Few people can embrace deeply untenable feelings as normal and ok. Few can choose to fully experience them. Instead, people find themselves in perpetual pursuit of the next “best” (read: most emotionally comfortable) indicator, software product, or trading system for a solution. People search futilely outside themselves for the root emotional cause that lies within, which is their unwillingness to fully experience uncomfortable feelings. Few win in the financial markets, most lose.

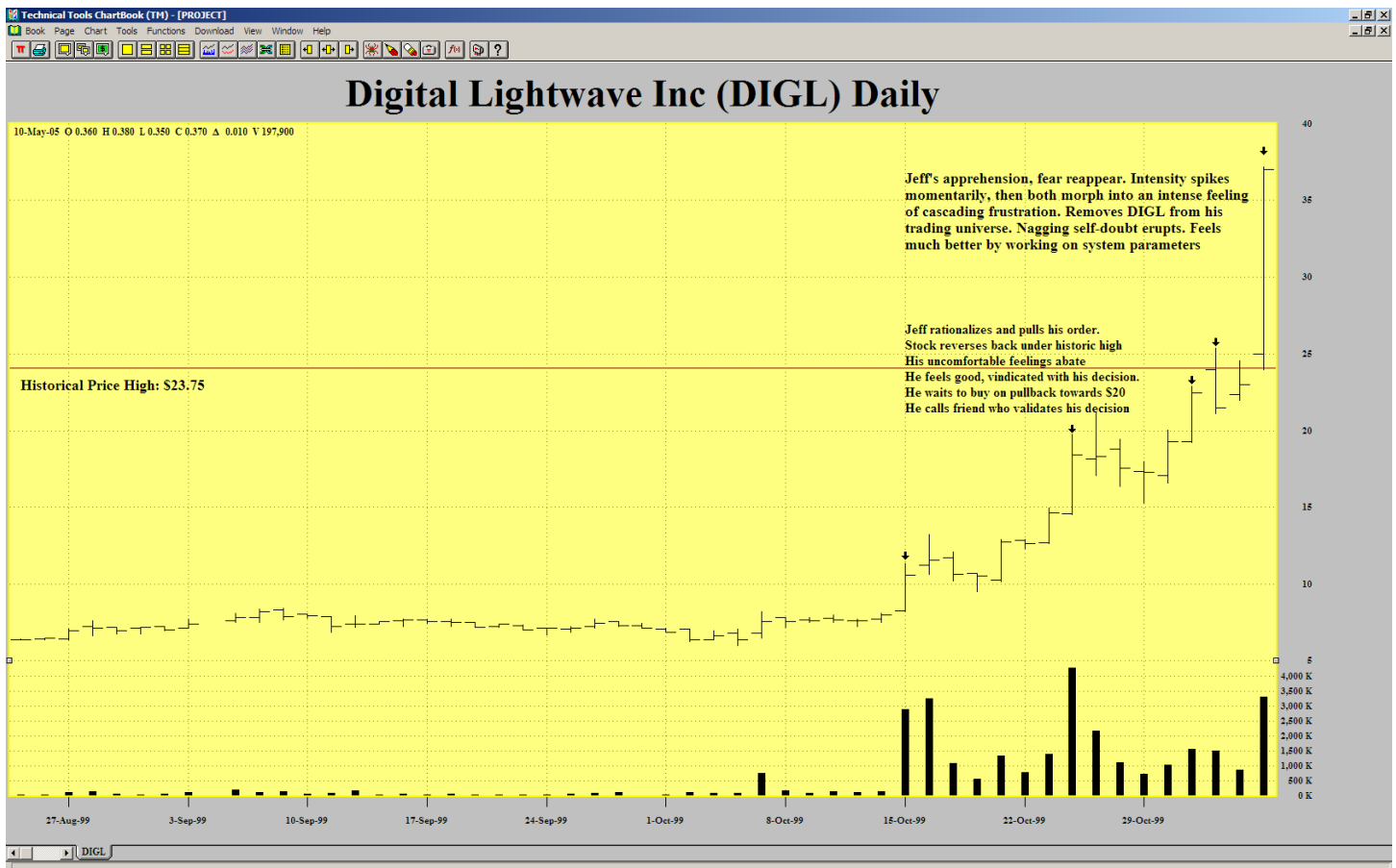


Chart 4 – February 23rd

DIGL trends much higher while Jeff stays focused on trading system development. In his case parameter changes are just another form of rationalization that masks, complicates, and obfuscates. What is really going on?

Jeff feels really bad about jumping his trend following entry signal. Along with his somatic feelings of frustration, he has another arise: a nagging, negative thought of self-doubt about his ability to win in the market and be a trader. It questions his identity. Self-doubt feels terrible.

Jeff wants these feelings to stop, so he turns to system development to bail him out emotionally. Indeed, system development makes him feel great. He gets to feel productive, goal-oriented, and hard working. Jeff uses the enjoyable feelings he creates by being productive, hitting goals, and working hard to dislodge and replace his nagging self-doubt and frustration. It is effective. He feels much better. At the same time, he “proves” to himself that he really is a trader by diligently working on his system. Unfortunately, Jeff is no closer to being able to buy historical breakouts despite all his hard work and productivity. In fact, Jeff actually degrades the robustness of his trend following method by tinkering with it under the false pretense that his difficulty is only mathematical and not emotional.

Jeff is unwilling to embrace another especially critical feeling for trend followers. It is the feeling of missing a major move or *regret*. Jeff cannot stand to keep DIGL’s symbol on his watch-list or part of his trading universe. Along with fanning his self-doubt and frustration, DIGL’s presence gives him a headache and throbbing heartache. These are his untenable somatic feelings of regret. Jeff cannot stand it.

Jeff squelches the growing intensity of these feelings immediately. Eliminate the source to stop the feelings. Jeff removes DIGL from his watch list and his system’s stock universe. In turn, his somatic feelings of regret quickly ebb. He intends to have no clue about how high it may trend. DIGL’s up-move remains out of sight and out of mind. Knowing anything about it gives rise to regret, which gives rise to the feelings he is unwilling to experience. Unfortunately, Jeff is unaware of any further historical breakout buy signals his trend following system may generate for DIGL. He carefully protects himself from experiencing regret.

The intensity of a people’s regret seems to run in proportion to how far a move extends from where they avoid entering. The bigger the move, the higher the intensity of regret and the more unwilling people become to experience it. With some trends, both regret and the unwillingness to experience it can become severe. With severe unwillingness to experience regret, people easily avoid participating in major trends. Jeff’s unwillingness to experience painful feelings of missing a major move makes it easy for him to miss DIGL’s major run.

Moreover, Jeff overlooks the positive intentions of his uncomfortable feelings. All have an underlying positive purpose. Regret’s positive intention is to remind Jeff what it feels like to miss a big opportunity. It feels so intensely bad that he wants no part of it. Yet, by being *willing* to fully experience it, his feelings of regret transform from enemy to ally. They become commanding motivation to stick to his simple, trend following system. Look what Jeff must feel if he fails to execute his system and let a big winning position get away. Suddenly it becomes much easier for him to stick to his rules. Regret supports only if he is willing to fully feel it.

Self-doubt about winning and being a trader has positive intentions. It keeps Jeff honest with himself. It injects a helpful dose of cold reality and personal responsibility if he becomes willing to fully experience it. Self-doubt raises tough and pointed questions. Does he really want to win? Is he really a trader? Jumping his system signals is surely not the way to answer a confident “yes” to either of these questions. If he does not think he can win or be a trader, self-doubt leads him to another critical question: what stands in his way and inhibits him? It may lead him to look inward if he becomes willing to fully experience it. Conversely, it may lead him away from trading and to his real right livelihood if his honest answer is “no.”

The positive intention of Jeff’s frustration is to motivate him to change his system jumping behavior at historical breakouts. Jeff’s system says to do one thing while he does another. If Jeff

becomes willing to fully feel his frustration, it powers him to find answers to the hard-hitting questions created by his own self-doubt. His intense frustration gives him the emotional energy and persistence to do whatever it may take to transform his behavior.

Risk control is the positive intention of Jeff's fear. Fear serves as a protective warning. It can emotionally support a trader to cut losses short and manage risk wisely. It is a good feeling to experience. Fear keeps people safe physically, emotionally, and financially. Being unwilling to feel frightened allows people to ride losing positions down and accept huge losses. What do they have to fear? Nothing! They are unwilling to experience it.

Note the last bar of Chart 4 below. It is another historical breakout from a 34 day consolidation after the stock more than triples in price over three months. Jeff continues to work on his system. Unfortunately, he is oblivious to another all time new high buy signal his system would generate. His unwillingness to experience uncomfortable feelings keeps his inhibition towards buying historical breakouts active. It continues to sabotage his ability to follow trends.

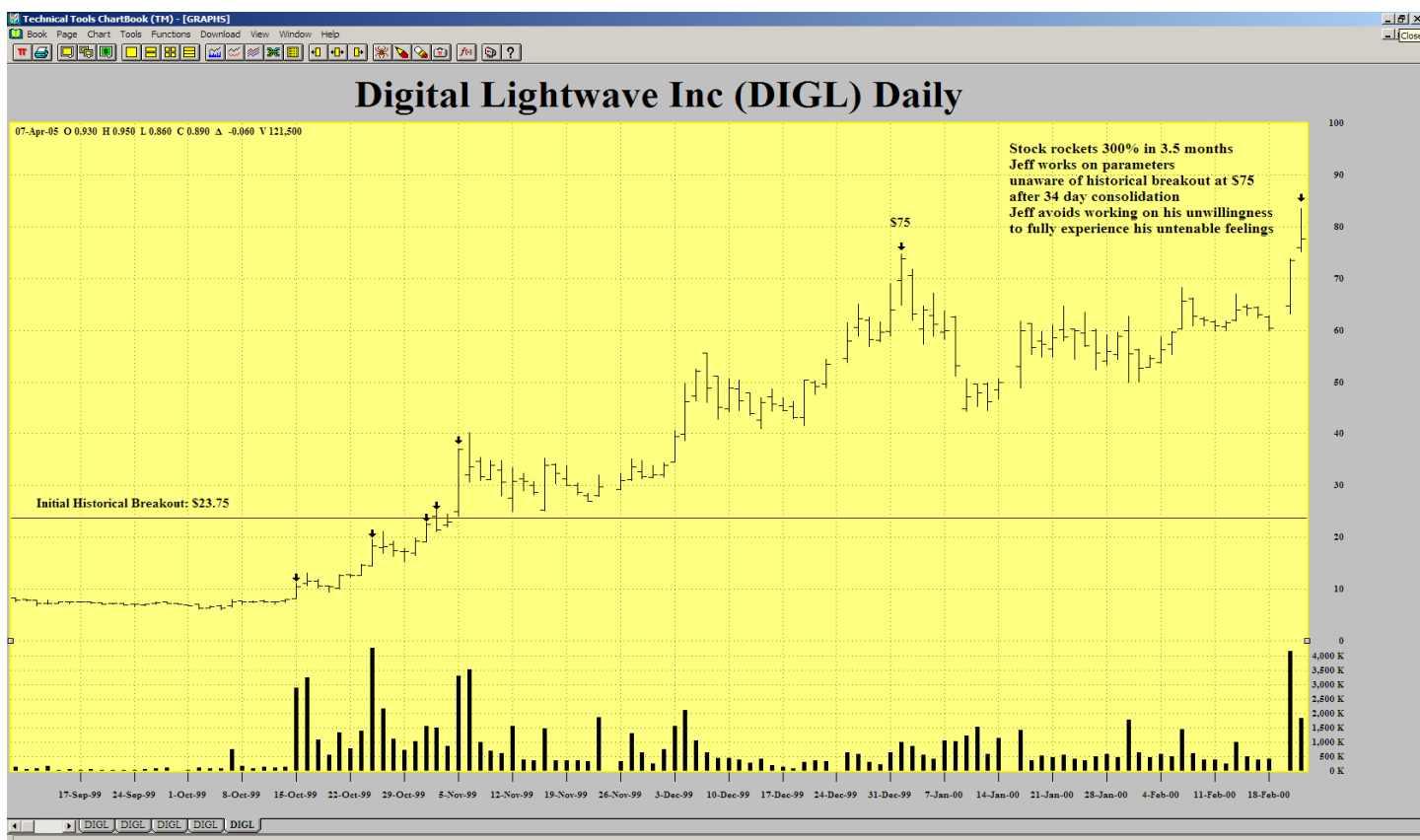
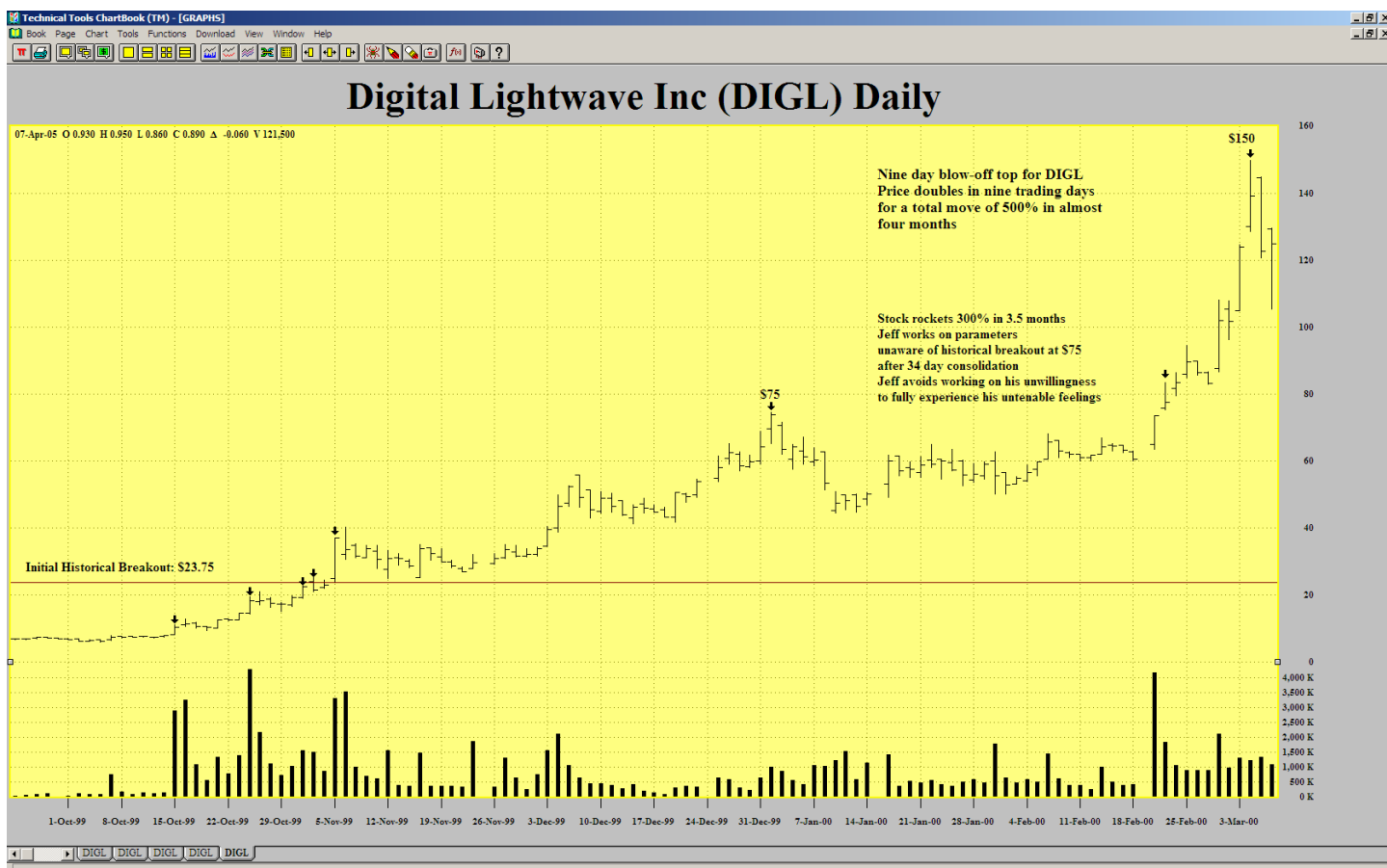


Chart 5 – March 6th

DIGL doubles from \$75 to \$150 during a final, blow-off move that occurs in less than ten trading days. Jeff misses a gigantic run of over 500% in roughly four months. His unwillingness to experience his uncomfortable feelings is an expensive habit. In late March Jeff pulls up a chart of the stock. He becomes very frustrated about missing another big, winning trade. Regret and nagging self-doubt seep up. Yet, something changes. Through an act of seeming grace, he does not push these feelings away. Through the pain, Jeff gains a little insight. It motivates him to turn inward for a solution. While Jeff remains unaware of the dynamic that inhibits him, he accepts

some personal responsibility for his frustrating results. Jeff begins to think that trading system development may not be the answer. “Where do I go from here?” he mumbles.

When the student is ready, the teacher appears.



A Note on the DIGL Chart

For trend followers, a majority of profits come from a minority of trades. Finding and riding strong, persistent trends are critical factors for success. Historical breakouts provide a fertile field to find stocks beginning strong and persistent up-trends. While DIGL’s rocket up-move occurs during the NASDAQ’s “once-in-a-generation” blow-off of 1999-2000, similar moves occurred before and after this period. For example, a very *small* sample of historical breakouts from 2003-2004 with large rallies of similar or greater magnitude include AVO, HRT, INCX, PHRM, SHLD, TASR, TZOO, TONS and WYNN.

Fully Experiencing Our Feelings

Jeff’s difficulty buying historical breakouts stems from his unwillingness to fully experience uncomfortable feelings. When it comes to an uncomfortable feeling or emotion, what does it mean to fully feel or fully experience it? How can someone learn to remove negative judgment about his feelings and learn to enjoy or at least accept them?

The Trading Tribe Process (TTP) is a robust method. It is new and transformative psychological technology. It is the focus of the book by Ed Seykota called *The Trading Tribe*. It can be found

at: www.tradingtribe.com/book. This author directs readers to the book for a full and comprehensive presentation of what it means (and does not mean) to fully experience uncomfortable feelings through TTP. An accurate description is well beyond the scope of this paper. Readers can find a small article on TTP at www.seykota.com/tribe/TT_Process/index.htm along with a large frequently asked question (FAQ) section. Ultimately, the best way to learn TTP is through firsthand experience as an active participant in a tribe or workshop with skilled members and a trained project manager. Only this can give a true “gut” understanding of TTP.

Fully experiencing uncomfortable, untenable, and strongly disliked feelings is a radical departure from the way people normally handle their emotions. TTP swims against a cultural current that encourages us to mask, escape, divert or hide from them. People have years of entrenched and engrained defense mechanisms protecting themselves from fully experiencing untenable emotions. These defense mechanisms are second nature and essentially impossible to overcome alone or through more traditional means.

TTP applies a trend following model to experience emotions. It embraces all feelings that present in people. It creates a judgment-free, tribal environment. It fosters group pressure and unyielding encouragement. This supports people to remove negative judgment to fully feel their untenable emotions. Only through full experience can people reintegrate them. This reintegration process dissolves seemingly intransigent and incorrigible emotional issues.

In Jeff’s case, his difficulty buying historical breakouts dissolves. Jeff’s apprehension, fear, frustration, self-doubt, and regret no longer hold the same power over him. He removes his negative judgment or dislike of them. Jeff becomes willing to fully experience his uncomfortable feelings. Next, he goes through another process to fully feel them. Finally, Jeff reintegrates them in a final step. He loses his inhibition and feels emotionally free to buy historical breakouts. Jeff experiences insight as an “aha.” He gains wisdom and clarity into how he inhibits himself, where he formerly had no idea. He understands that his difficulty buying historical breakouts is emotional. He realizes that his system parameter search is another form of rationalization and means to escape his uncomfortable feelings.

TTP helps Jeff:

1. Fully experience his feelings of dislike or negative judgment about his untenable feelings.
2. Reframe negative judgments to neutral or positive ones.
3. Fully experience his untenable feelings that inhibit him from buying historical breakouts.
4. Reintegrate his untenable feelings to gain insight, find their positive intention, and dissolve his inhibition towards buying historical breakouts.

Conclusion

The historical price breakout offers an important entry point for trend followers. Yet the moment it occurs, most people find it too emotionally difficult to buy it. They cannot handle the feelings that arise. Instead, people commonly use rationalization as a tool to avoid experiencing their feelings. Rationalization is a by-product of the unwillingness to fully experience untenable emotions. Unwillingness to fully experience uncomfortable feelings inhibits people from buying historical breakouts. Removing negative judgment about untenable emotions fosters the willingness to fully embrace and experience them. Fully experiencing and reintegrating uncomfortable feelings clears inhibition. This creates emotional freedom to buy historical breakouts.

Most people have an antagonistic relationship with feelings they dislike. They believe these emotions can only damage, disrupt or interfere with their trading. Through TTP, people realize that their own unwillingness to fully experience uncomfortable feelings sabotages their trading. People learn to reframe untenable feelings as natural and helpful emotional allies – even while trading. Learn to celebrate and embrace your own uncomfortable feelings through the Trading Tribe Process!

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About the Author

Tom is a fund manager and partner at Choice Alternative Investments. He is a trend follower with a successful track record over the past eleven years. Since 2003, Tom practices and attends workshops on TTP. He is a member of Ed Seykota’s Incline Village Trading Tribe. Tom acquired the following NASD licenses: Series 3,7,55, 63 and 65. He graduated from Claremont McKenna College with a degree in Psychology.

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