



BRETT N. STEENBARGER

Brett N. Steenbarger, Ph.D, Clinical Professor of Psychiatry and Behavioral Sciences and author, helps us understand the stresses faced by traders, their coping styles, and how these affect emotional well-being and trading success

A thick, multi-colored rope with frayed ends, set against a dark purple background. The rope is composed of many strands of different colors, including yellow, orange, red, pink, and blue. The frayed ends are prominent, showing the individual fibers of the rope. The rope is positioned diagonally across the page, from the bottom left towards the top right.

# A Trader's Guide *to* Stress and Coping

**A** trader of the Australian currency market is long versus the dollar, expecting that economic weakness in the U.S. will hold down American interest rates and reward the holding of higher yielding currencies. Suddenly the U.S. government reports a much higher than anticipated inflation number. Short-term yields skyrocket, as traders anticipate monetary tightening by the Federal Reserve. Immediately the dollar rallies versus other major currencies, and the trader's position goes into the red. His heart rate increases, as does his rate of respiration and muscle tension. Thoughts race through his mind: Should I take my losses? Should I stick with my longer-term outlook? The market is gyrating up and down, lurching dozens of pips in a matter of seconds. The trader curses his decision to enter the position in advance of the inflation report. Reluctantly, he takes his losses, wondering if he is selling at the worst possible price.

This scenario, common to traders across all markets, captures the emotional dynamics of trading: an activity fraught with risk and uncertainty. The physical arousal experienced by the trader, and the accompanying cognitive changes are manifestations of stress. Stress is a response to threat: a mobilization of resources that allows organisms the options of flight or fight in the face of perceived danger. Although we sometimes view stress in negative terms, it is clearly adaptive. Without stress responses to rouse us to action, we would be poorly equipped to deal with life's challenges. The ways in which we deal with stress-provoking situations is called coping. Sometimes our coping mechanisms are ineffective as methods of flight or fight, preventing us from constructively handling life's challenges. When coping is inadequate, stress becomes a chronic condition, creating emotional and physical distress. In this article, we will take a look at the stresses faced by traders, their coping styles, and how these affect emotional well-being and trading success.

## Trading and Stress

A large body of psychological research indicates that stress varies with perceived control over threatening situations. For example, a famous set of studies exposed monkeys to electrical shocks. Half of the monkeys could stop the shocks by pressing a lever; the other half did not have a lever. Although the total number and intensity of shocks received by the two groups were equivalent, the group with the lever displayed far less emotional distress, and showed fewer stress-related physical problems than the group that lacked control over the shock.

In trading, it is not difficult to feel like the caged monkey without a lever. We cannot control the markets, and we cannot know their future behavior with certainty. Like the trader in the opening illustration, we jeopardize our money (and sometimes our reputations and careers) when we assume risk in uncertain conditions. Risk and uncer-

tainty are the twin pillars of stress. Without risk, there is no threat. That is why paper trading (simulated trading without the actual investment of funds) is so emotionally different from the actual thing. Similarly, stress can only exist where there is uncertainty. If we knew with 100% certainty that a market was going to rise or fall, trading our privileged information would pose no threat.

As we saw in the opening illustration, time also contributes to stress, as adverse trading events and the need for effective responses can appear within seconds. This time compression interferes with perceived control: we generally feel more control over challenging situations if we can take our time, weigh alternatives, and formulate our best responses. When challenging situations erupt in a moment's time and demand an immediate response, our normal, deliberative coping patterns are no longer useful. Faced with the need to make major decisions **now**, traders experience information and emotional overloads, amplifying their physiological responses. Research by Andrew Lo and Dmitry Repin at the Massachusetts Institute of Technology found this arousal to be particularly acute among inexperienced traders. When hooked up to biofeedback machines during trading sessions, they experienced significant stress-related arousal during episodes of market volatility—the very times when risk is greatest.

One of the least appreciated features of markets that contribute to stress is their ever-changing nature. Markets are not just volatile; they shift in volatility within the day and across days. Sometimes markets trade in slow, narrow ranges. Other times they swing wildly or trend persistently. Just as a trader adapts to one market environment, that environment is likely to shift. How many traders have we all known who made money during the great bull market of the 1990s, only to lose their touch early in the 21st century? In many fields, we can learn skills and remain confident that these will serve us well throughout our career. Trading, however, requires constant adaptation: the skills that worked in one market regime can fail miserably in another. I have met very few professional traders who feel that they have job security. This is profoundly stressful for traders raising families, paying off mortgages, and planning for retirement. When a trader enters a slump, the greatest source of stress is often not the lost capital; it's the nagging fear of having lost one's touch.

During my career as a psychologist, I have worked with dozens of professional traders, watching them trade and helping them with their trading. Some of the traders I have worked with have been phenomenally successful, making millions of dollars a year. Others have struggled to achieve profitability. The one common element across the entire group is that they have been highly competitive and emotionally charged. I honestly cannot say that

the large and successful traders were any less emotionally volatile and stressed than the new and small traders. Reading articles by trading psychologists, one sometimes gets the impression that successful traders achieve a kind of Zen-like control over their minds and feelings. I sincerely doubt that this is the case. As long as there is risk and uncertainty, stress is a normal, expectable human outcome. *Stress is built into trading.* Our job is to ensure that it does not become distress.

## The Cognitive Dimensions of Stress

Our thoughts are as important to stress responses as actual physical threats. Psychological stresses include threats to self-esteem, emotional security, and perceived safety. Cognitive psychologists point out that our reactions to events are mediated by our beliefs and expectations: if we think that we will lose, or if we think that losing makes us losers, we will respond accordingly. This can be seen in the phenomenon of performance anxiety, such as the stress that some people feel before public speaking events, tests, and social occasions. Those who do not experience performance anxiety hold beliefs that make these events non-threatening: they do not judge themselves by their performances. Anxious individuals, on the other hand, hold beliefs that equate performance shortfalls with catastrophes. They gauge themselves by how they are perceived by others. As a result, situations that are not stressful for some people become overwhelming and terrifying for others.

Traders exhibit a variety of cognitive patterns that contribute to stress. Among the more common are:

- **Self-blame** – Traders can become their own worst critics following losses, engaging in a stream of automatic thoughts that depress both mood and adaptive responses;
- **Perfectionism** – Traders can be quick to second-guess themselves, feeling that it's not good enough to take a piece out of a market move and refusing to accept the normal losses that are part of operating in uncertain environments;
- **Worry** – Traders can magnify the immediate situation, becoming panicky over the possibility of missing an opportunity or losing money;
- **Overconfidence** – Traders can become so married to opinions about market direction that they fail to consider alternative scenarios, leaving themselves unprepared to deal with market reversals;
- **Negative Thinking** – After a series of losses, traders can fall into a mindset that expects failure, leading to a

dread of facing the next trade or the next day.

It's worth noting that even very successful traders can experience cognitively mediated stress. If one has internalized a self-blaming, perfectionistic internal dialogue, the profits one achieves will never be enough. We respond not only to actual, physical threats in the environment, but to the threats—real or imagined—that we perceive. Many of the case studies that I described in my book 'The Psychology of Trading' (Wiley, 2003) were descriptions of very high functioning people who nonetheless were burdened by stress and distress. Their suffering was a function of their thinking: they had learned, over time, to process the world in distorted ways.

Unlike the risk and uncertainty that are inherent to trading, psychological threats that result from cognitive distortion do not have to be part of our experience. Ultimately, we can control our thoughts; we cannot control volatile, changing markets. All traders in a particular market and timeframe face the same objective risks. All, at times, will experience stress. *What will determine whether this stress becomes distress and interferes with trading is the degree to which internal, cognitive processes amplify already existing uncertainty and risk.*

## Effective and Ineffective Coping

One of Freud's most important observations was that emotional stresses can trigger coping responses from our past, leading us to deal with challenging situations in ineffective ways. He called this regression. For instance, let's say that we learned to deal with conflict in a previous marriage by swallowing our hurt and going into an emotional shell. Now, during a successful marriage, we no longer have to resort to such coping. During a trade that goes against us, however, we might experience frustration and pain. These trigger the coping from the prior marriage and lead us to withdraw from the markets, preventing us from reversing the trade and/or learning from the experience. Many trader episodes of "I can't pull the trigger" or "I keep overtrading" are the results of past coping patterns intruding into present day trading situations.

Psychologists Susan Folkman and Richard Lazarus suggest that people exhibit three basic coping styles:

- **Emotion-focused coping** – These include strategies to vent emotions, share feelings with others, and process emotional reactions internally;
- **Problem-focused coping** – These are strategies to identify sources of threat and deal with them directly, whether those sources are internal or external;
- **Avoidant coping** – These strategies deal with threats by

avoiding, suppressing, denying, and minimizing them.

All of us utilize each of these coping styles at times, although most of us exhibit preferences toward particular styles. Folkman and Lazarus emphasize that none of the strategies is inherently good or bad: each can be effective or ineffective depending upon how it is used. Avoidant coping, for example, might be disastrous if it prevents us from closing out a losing trade, but could also be adaptive if it allows us to suppress feelings so that we can make rapid decisions.

Before traders attempt to improve their coping, I encourage them to understand how they cope. A journal in which traders identify stresses, how they coped with them, how they felt, and how their trades fared can be very helpful. Over time, such journals reveal patterns to our coping. For instance, we might tend toward problem-focused coping methods on a day-to-day trading basis, but utilize emotion-focused venting during periods of adverse market activity, contributing to strings of losing trades.

Once you know how you cope, it makes sense to ask whether that coping is working for you. I suggest a simple criterion to determine coping effectiveness among traders:

***If your coping enables you to follow your trading plans, including risk management parameters, it is effective.***

***If your coping prevents you from acting upon your trading plans, including your risk management, it is ineffective.***

In other words, effective coping allows you to act in a planful, self-determined way. Ineffective coping prevents you from acting upon your best intentions. Effective coping allows traders to control stress. Ineffective coping leaves traders controlled by their stress.

### **My Favorite Strategy for Improving Coping**

Traders interested in improving their coping have a number of alternatives available to them. On my website ([www.brettsteenbarger.com](http://www.brettsteenbarger.com)), I have archived a number of articles that describe techniques for reducing stress. My book also highlights coping strategies drawn from research and practice in brief therapy. Traders who need more personal assistance with stress management can benefit from work with therapists who specialize in cognitive behavioral therapy, an approach that emphasizes the learning of coping strategies. One immediate strategy that traders can implement to reduce internal, psychological stress is outlined below.

As I mentioned earlier, much of the stress associated with trading is mediated by our beliefs. By changing how we talk to ourselves about trading, we can improve our coping

and minimize distress. One belief in particular has served me well as a framework for effective coping:

***I am a student of the market; my job is to learn.***

A corollary of this belief is something I emphasize to new traders:

***There are two kinds of trades: winning trades and trades you learn from.***

As it happens, I also believe you can learn a great deal from winning trades. The point, however, is that *a student of the market looks at losses as opportunities for learning*. Yes, it is uncomfortable to lose money, and, yes, it can be discouraging. If, however, you lose money on a high probability trade, there is something to learn. Perhaps you've just acquired valuable information about the market: it is not behaving in a usual way. A market that should be trending higher based on historical precedent, but instead is moving lower, is responding to unique situational factors. Identifying these factors can set you up for later, winning trades. On the other hand, a losing trade may teach you something about yourself. Perhaps your execution was poor, or maybe your stop was too close. Your job is to learn: to figure out why the high probability trade failed, so that you can factor that information into your subsequent trading.

The beauty of the learning paradigm is that it not only accepts losses, but actually embraces them. *Your losses are there to teach you something; they contain valuable information*. Losses are only threats to profitability and success if you do not learn from them. I am confident that, if you mentored another trader, you would encourage your student after losing trades. You would not want to destroy that person's confidence and motivation. If that is the case, your challenge is to internalize that process and *treat yourself as your own student*. Arthur Koestler once observed that, "Creative activity could be described as a type of process where teacher and pupil are located in the same person". Such creativity, applied to the trading of markets, is a powerful antidote to distress.

*Brett N. Steenbarger, Ph.D. is Associate Clinical Professor of Psychiatry and Behavioral Sciences at SUNY Upstate Medical University in Syracuse, NY and author of The Psychology of Trading (Wiley, 2003). As Director of Trader Development for Kingtree Trading, LLC in Chicago, he has mentored numerous professional traders and coordinated a training program for traders.*

*An active trader of the stock indexes, Brett utilizes statistically-based pattern recognition for intraday trading. Brett does not offer commercial services to traders, but maintains an archive of articles and a trading blog at [www.brettsteenbarger.com](http://www.brettsteenbarger.com).*

*Brett can be reached via his website [www.brettsteenbarger.com](http://www.brettsteenbarger.com)*