During my time

Inevitably, I will always get a similar derivative of a common question; which is great, that's why we're here. The questions generally fall into five common categories:

1. How to become a trader on Wall Street
2. How to become a trader in an investment bank
3. How to become a trader without a degree
4. How to become a trader from home
5. How to become a successful FX trader

I trust you're beginning to see a theme. After speaking with these people, it's apparent that the real underlying question is: "How do I, as a retail investor, with no connections or experience, evolve my education, thinking, risk management, and business practices to that of the professionals?"

To start, let's get rid of the first two questions. Becoming a trader at a nationally known investment bank or on Wall Street itself is a straightforward and easy process, provided you're male, between 22 and 25 years old, have a degree from a top tier school, previously established connections in the industry, and know enough high net worth people so that you can bring at least $10m in new money to the firm.

From there, it's the simple matter of becoming an analyst for a few years until you can network your way onto an established prop desk at the firm. Then you're a glorified gofer/apprentice for a year or so until the guys at the desk trust you not to screw up too badly and you're given some trades to make.

If you survive what is essentially a gladiatorial arena, you'll be given larger trades to make, occasionally allowed to develop your own ideas, and then somewhere down the road you'll be allowed to manage a portfolio. So, as we said, it's a straightforward and easy process.

For the rest of us, becoming a professional trader is an evolution rather than a defining event, which, when you stop to think about it, makes sense. No professional trader has ever appeared on the earth in a bolt of lightning, fully formed, clad in a hand-tailored suit, and ready to manage money. We have always said at Paragon Trading that traders aren't born, traders are forged. Something that is forged goes through fire and pressure and comes out harder and improved in the end. There is no college degree that spits out a professional trader at the end of four years. Even given the accomplishments and pedigrees that Wall Street firms seek in their hiring practices, the process to become a professional trader is arbitrary, rife with nepotism, and the training inconsistent and haphazard.

When we look at the path a professional trader has taken, we see that key events mimic the evolutionary process, in that some can be referred to as genetic (learning and trying something new without really knowing what the result will be) and epigenetic (as in how a trader reacts to his environment, i.e., how an unexpected event in the markets will affect the trader). Furthering the analogy, we find that the process is messy, prone to dead ends, sometimes produces wholly unexpected results, and for those people that can find the Golden Path, we see avenues that allow for tremendous evolutionary leaps that ensure not only survival but success.

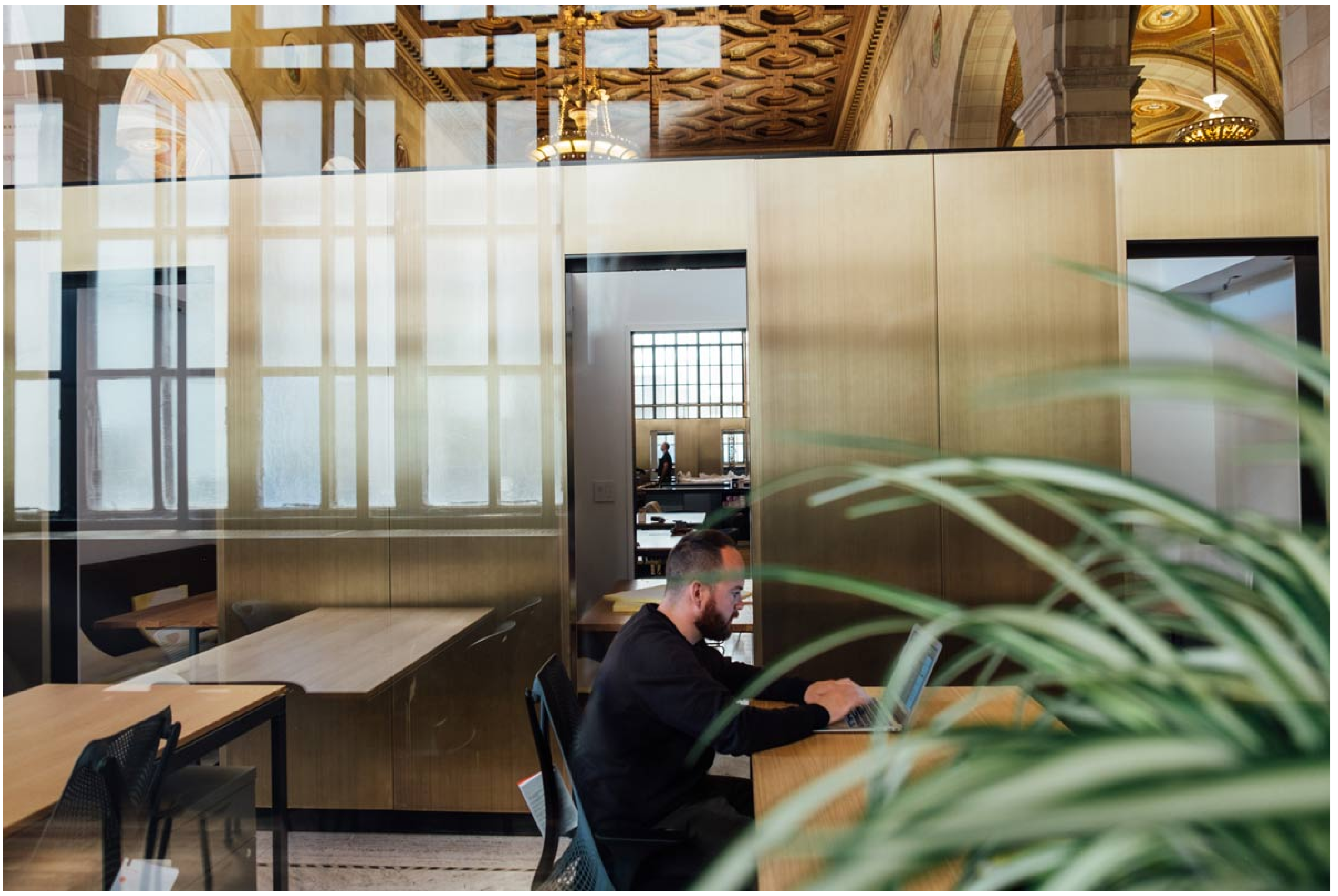
So, without further pontification, let's delve into the evolution of a trader.

Phase Zero: Paycheck to Paycheck

We've all been there at some point in our lives. It's that uncomfortable existence where income is balanced with expenses on a razor thin edge. A path to survival is on one side and an abyss on the other. It is the evolutionary equivalent of a microbial morass where you're just happy to survive at the end of the day. Sometimes happiness doesn't even enter into the equation and you just meet the rising sun with grim determination.

One thing that is clear is that you want to get out of this soul-sucking tide pool as quickly as possible. This stage is best endured in one's late teens and early twenties when you still have a modicum of faith that things will get better, when you can sing Monty Python's *Always Look on the Bright Side of Life* without bitterness or irony.

Unfortunately, the Great Recession was the equivalent of a financial Chicxulub meteor impact, sending many people further along in their evolution back down into the Paycheck-to-Paycheck tide pool. The moral of that story is to advance as far as possible as fast as possible so that you can continue to grow during the next financial meteor impact instead of being knocked flat.



Phase One: Saver

How to save is usually something we learn as children. We toddle to the bank, hand in hand with Mom or Dad to open our first savings account, often protesting loudly because a child has no way to process the concept of delayed gratification.

As parents, we often view this as an exasperating exercise in futility with a 20-year duration. If your kid gets a job in high school, he still has you to fall back on, so his income is 100 percent disposable. Even when he moves out, initially, he still reverts to Paycheck-to-Paycheck with you as a lifeline. But, at the very least this exercise plants the seed that saving is necessary. Your child won't appreciate it for a long time, but it's probably still a good idea.

From an evolutionary standpoint, saving is the equivalent of swimming to the side of the tide pool and developing the ability to walk on land for short periods of time.

Saving as an investing practice is pretty awful, simply because your interest is taxed at the marginal rate and what interest you get will not keep up with inflation. Over the long run, you will actually lose money because the value of what you saved will go down. That said, it's a step in the right direction and a precursor to much more lucrative activities.

People seeking to evolve further save for two reasons: 1) to have a liquid asset to cover emergencies; and 2) as a parking mechanism to gather assets for follow-on investments.

Phase Two: Fund Investor

Becoming an investor in a mutual fund is one of those large leaps that, strangely, didn't require any exceptional effort on the part of the investor. Most people are introduced the mutual funds as one of the benefits of their employment.

You and your colleagues are stuck in a room, coffee and doughnuts are provided, usually by the asset management company hosting the event, and you're subjected to an hour-long presentation of the company's benefits, including the 401(k) plan.

You get introduced to new, sexy terms, like "dollar-cost averaging," "diversified portfolio," and "life-cycle investment model."

The first time you sit through one of these presentations, it's actually a little exciting. You're thinking, "I'm actually an adult now. I'm investing for the long term. I'm planning for the future." Your company is probably matching a portion of what you're setting aside, so in your mind that is essentially free money.

The pack of papers lands in front of you. You check boxes, choosing from the list of funds you're given as options for what you want your contributions invested in (which at this point are guesses on par with picking numbers on a Keno card), you sign your name, and you get back to work.

Congratulations are in order at this point because you actually took the major step to become an investor. You pulled yourself out of the tide pool with the Paycheck-to-Paycheck people and the Savers. You're now walking on the savannah…with the herd.

Whether you know it or not at the time, by being in the herd, while you are better off than you were in the tide pool, you are now viewed as a prey animal by the people running the money.

The thing to remember is that the fund managers get paid before you do. You later learn the difference between "load" and "no-load" funds. You get end-of-year statements and you learn what 12(b)(1) Fees are. You begin to watch a little financial news and get introduced to the concept of "window-dressing," and "tax-loss selling."

Sooner or later, you learn that wolves don't concern themselves with the opinions of the sheep. Some people are happy to be the sheep. There's safety in the herd, after all.

But if you're reading this article, you're not one of the people content to be part of the herd. You're one of the people looking to break out of the herd and make the next evolutionary step.

Phase Three: Stock Picker

Typically, making the move from Fund Investor to Stock Picker is the financial equivalent of an epigenetic event. Most often, it's predicated on opening an end-of-year statement and realizing, mouth agape, that your fund manager performed the extraordinary feat of actually losing money in a bull market.

The next fateful words out of your mouth are along the lines of "What *@#$%^& idiots! How hard can it be to make money? A trained monkey could do a better job than these morons!"

Following this bout of righteous and rightful indignation, you do what any self-respecting alpha personality does and go out and open your own brokerage account. You're going to show them what's what.

If you're honest with yourself, your first couple of orders to your broker are probably in the mode of ready, fire, aim. It happens to everyone and it's understandable. You've got a new toy (your brokerage account) and you want to play with it (put in orders). Very quickly, though, you begin to realize that this is harder than it looks.

You must remember that you went from being part of the herd to the first ranks of a predator. You eat what you kill now. The problem is that you're now a lone hunter because there's no one else to help you. In the wild, the success rate of a tiger is less than 20 percent. A good portion of your waking moments are now dedicated to seeing how you can increase your success rate.

Within the phase of Stock Picker, there are six identifiable stages of evolution:

Stage One: Blind Faith Guru Follower

After the first couple of picks you make that immediately lose money, you begin looking in earnest for some edge, any edge, to help you out. Immediately, the light bulb goes on and you think, "TV! I'll watch TV! There are entire cable channels dedicated to helping ME make money. If they're on TV, they must know what they're talking about. After all, they're gurus."

The next thing that happens is that you begin to religiously watch a favorite guru or a favorite financial channel in the hope that you'll get some actionable trades but you're really watching for the entertainment value (you just haven't realized or admitted it yet).

The worst thing that you can do, but we've all done it before, is to take the recommendations the guru is talking about and put money behind them, blindly. "Well, I heard it from [Insert Name of Favorite Guru Here]. He's a guru. He must be right." No due diligence, no risk management analysis, just enter the trade online and click the Buy button.

All those gurus on TV, if they're even still trading, are trading under some draconian restrictions. For example, many of them cannot short the market; they must be long only. If they report a trade on TV, they may have to hold the trade for at least 30 days. Thirty days is a long time to hold on to a position that's going against you, whether it's an investment or a trade.

You must remember that these gurus may have initially gotten on TV because of their trading acumen, but the reason they stay on TV is for their ability to entertain.

The last thing to remember is that when one of these gurus talks about a position on TV, the smart money's already gotten into the position. Whether you make money on a trade is secondary to whatever network on which these gurus appear. The only thing network management cares about is the fact that you ***are*** watching that they can count your eyeballs, report them to their advertisers, and justify their advertising rates.

Stage Two: Chat Room/Tweet Slave

I have, for years, held the position that stock chat rooms on the major (and minor) financial sites have cost investors more money than Larry King's and Donald Trump's divorce settlements combined. From my experience they are staffed with three types of people: overly enthusiastic cheerleaders, trolls with the maturity of a 13-year-old, and the totally clueless who are just happy to have someplace to type in mindless questions and statements.

The great thing about the internet is the anonymity allowing you to say whatever you want. The bad thing about the internet is that you have no idea who is posting what garbage for what reason.

The cheerleaders have already gotten into positions and they want the affirmation of having other people praise their self-supposed intellect and to know that other people will invest alongside them because of the "advice" that the cheerleader gives on the chat board.

As far as the trolls go, who knows what motivates them beyond a mean streak that most socially apt people outgrow in their late teens and early twenties. I mean, really, if I'm short a stock, I don't care if you're long, or if you're short alongside me.

The takeaway here is that with chat rooms, and their newer cousins, stock tweets, you have absolutely no idea of the experience, ability, or reputation behind the post or tweet.

Stage Three: Break-Even Chanter

Lack of an exit strategy, whether to book a profit or cap a loss, is the bane of the evolving investor.

As humans, we have a psychological need to be right about a decision. It's what feeds our ego. At this stage in their development, aspiring stock pickers spend an incredible amount of time analyzing each investment or each trade. They invest this time to the point that they are emotionally invested in the positive outcome of the investment or trade.

We've all been in this position before, and it's not fun. Usually, what starts out as a short-term trade that was researched in eye-bleeding detail is executed, and almost immediately, it begins to show a loss.

Here's how the internal monologue plays out.

"Man, this was a good trade. The fundamentals are great. I even checked the technicals on that fancy new website I found last week. Well, that's OK. I'll give it some room to run."

"Shoot! It's coming up to that stop-loss point that I said I would get out at. You know, this is still a good trade. I know it's going to bounce back. I'll just give it some more room. It'll bounce back, I know it."

"What the hell just happened? Out of the entire S&P 500, 499 of them are up and I'm in the only one that's down! Calm down, this is all part of the gain. Whoa, it's really past that stop-loss. I should have gotten out then. I don't want to get out now. It's got to bounce sometime soon. I'll feel like an idiot if I get out and it comes back and runs. I'll just give it one more day."

"By all that is holy, what is wrong with this stock?! If I book the loss now, this one position will wipe out the rest of my gains for the year. Just get back to break even, that's all I ask. I'll get out when I'm at break even."

"Please, please, just get back to break even and I swear I'll get out."

And the conversation with yourself goes on in that vein. What should have been a short-term trade with a defined exit becomes a "investment for the long-term," all because you listened to your ego rather than followed a plan.

We can talk about this situation with some levity because we've all done it. It's important to recognize that ego plays a role in investing and trading, and it's not a good role. The sooner an evolving investor faces this and puts procedures in place to mitigate it, the sooner he can move on to activities that are actually money-making rather than time destroying.

Stage Four: Penny Stock Dupe

Years ago, I gave an interview. The topic was penny stocks. Boiling down the essence of my interview, the takeaway I gave was thus: If you have a pathological need to lose money, by all means, invest in penny stocks.

The road to exploring penny stocks is understandable. Generally, you've found that it's hard to make money investing or trading in the stocks listed on the established markets, so you want to try something else, really anything else. At this point, you're in a suggestive state of mind.

By this time in your evolution, you've probably clicked on enough links or submitted your contact information to some form and ended up on some list. Via the magic of modern marketing, you end up finding out that there is an entire world out there that is "hidden" from the "common" investor. It's the magical world of penny stocks.

The hook really does a good job at playing to greed. It always involves an historic "case study."

"Can you imagine (yes I can) if you had invested in [insert pink sheet ticker symbol of really obscure penny stock] (what the hell is this?) when it was only $0.001 per share (a thousand shares per dollar? Is that possible?)? [ticker symbol] is an up-and-coming player in the [insert name of obscure esoteric sector that has gotten some recent press coverage] industry (that's an industry?) and it's now trading at $1.05. If you had invested when [ticker symbol] was at $0.001 per share and sold today, you would have made 1000 times your initial investment (*ding*, tell me more)."

From a marketing standpoint, it's beautiful. From a wealth building standpoint, it's a vampire. It will suck your time, energy, faith in your abilities, and your capital with odds of success that are far worse than the lottery.

In 16 years, I have seen one model that has consistently made money in penny stocks and it wasn't a signal service or a newsletter; it was a PIPES (Private Investment in Public Equity) fund. This type of fund is limited to accredited investors, actually invests in about one to two percent of the deals they see, negotiate really lucrative deals involving convertible preferred shares with a healthy dividend, warrants for more shares, and most importantly, a good percentage of the board seats.

The fund has positioned itself so that it knows exactly what is going on in the company it's investing in and is in a position to take the helm if management goes off course. This is a far cry from a retail investor typing in obscure ticker symbols from some signal service of dubious reputation in the hopes of getting a lottery ticket.

Stage Five: Newsletter Addict

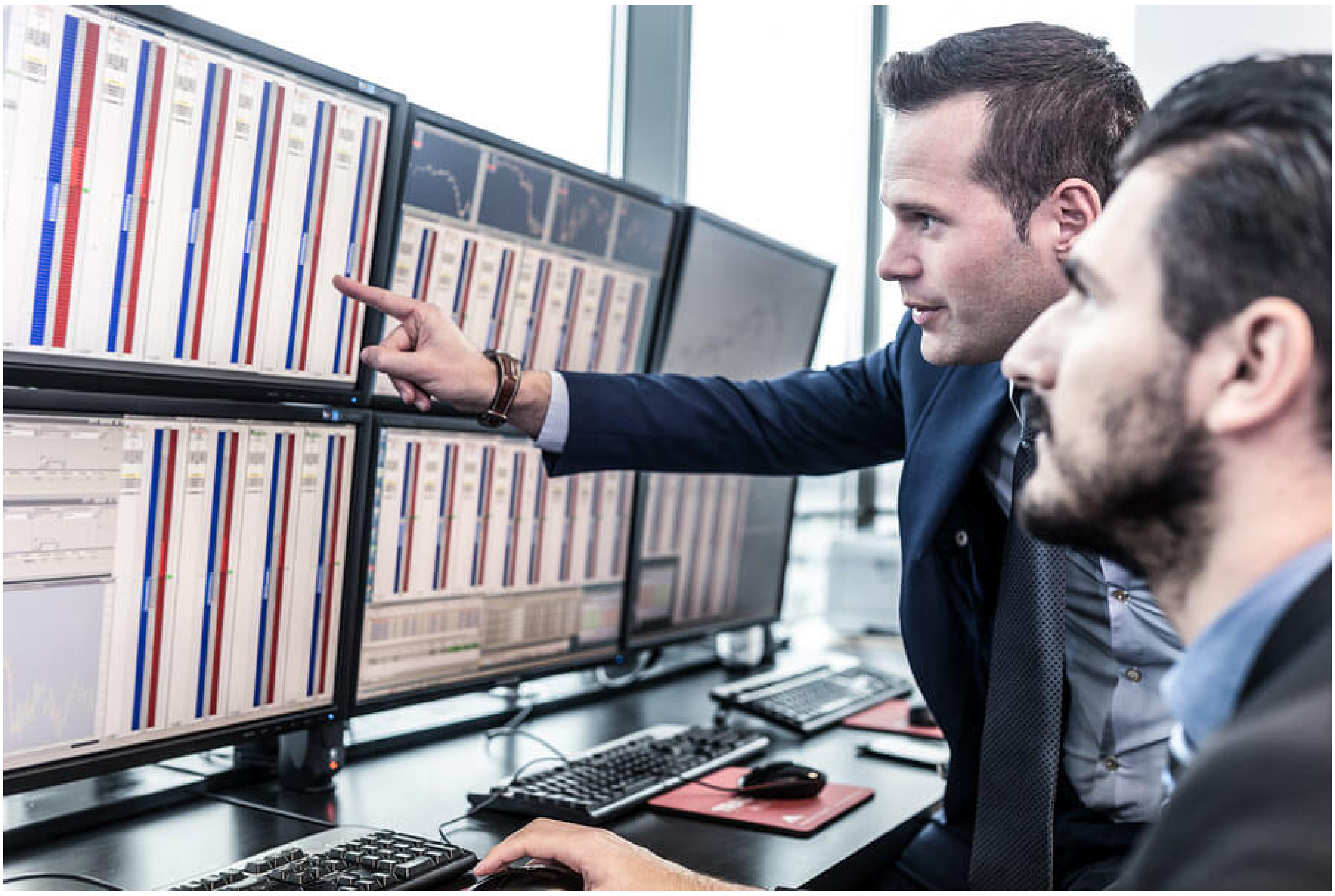
I have mixed feelings on newsletters. First, you have to take a look at where the newsletter publishers' motivations are - they are motivated to sell subscriptions. Second, you get what you pay for. Third, they have nothing at risk if their newsletter recommendations turn out to be dogs. Sure, they may have to gain another subscriber after you cancel your subscription, but they aren't on the hook for any of your losses.

That said, some newsletters out there have some interesting ideas and insights. Evaluating their views judiciously, inserting your own analysis, and applying risk management consistent with your personality, and you can glean some genuine value from a few of them.

The problems arise when an investor gets some success with a newsletter and does one of the following:

1. Follow the recommendations of the newsletter religiously without critical thought;
2. Begin to believe that if one newsletter is good, two, three, four or more newsletters is bound to be better; or,
3. Don't get immediate gratification from one newsletter and begin to bounce from newsletter to newsletter trying to find the magic one that is going to make them rich.

The underlying theme of all this is that you can't outsource your analysis and your risk management and expect to do well. All the major investment banks did this in the sub-prime mortgage boom and ratings agencies prior to the Great Recession. That didn't work out well for them or us.



Phase Four: Seeker

Winston Churchill once said, “You can always count on the Americans to do the right thing after they have tried everything else.” The same is true in an investor’s evolution in becoming a trader; after trying all the get rich quick shortcuts that invariably lost them money, an aspiring trader will experience an epiphany and realize that trading requires three things:

1. Comprehensive training from someone who actually knows what they’re doing. This includes not only the trading methodology, but exploring and understanding what your personality is, determining where you fall on a risk spectrum, and multi-level risk management.

2. Ongoing support to answer questions in a timely manner, to keep you engaged, and to provide advice and over the shoulder risk management.

3. Meaningful capital. While this is actually the least important, trading while undercapitalized is a millstone around many traders’ necks. The time and effort you will put in for a 50-share trade is the same time and effort that you will invest for a 5,000-share trade. The only difference is the amount of capital behind the trade.

That’s it. Three things: training, support, and capital. Simple in theory but much more difficult to find.

This is the point where you need to take stock of your personality and make an honest assessment of what timeframes you want to trade. On the face of it, you may not see that it makes much of a difference, but it does.

You may find that your personality and your lifestyle dictate that you remain an investor. We define that as someone with a holding period of six months or longer, generally looking to play the markets on the long side, possibly with the occasional short-term hedge, but really looking for long-term appreciation. You may find that you’re best suited to become an active investor but will never seek to become an active trader.

Investors look at different things than traders. Investors should learn to conduct fundamental analysis and care about the long-term operations and prospects of a company. Those things mean nothing to a trader. In reality, someone who tries to trade on fundamentals often loses. Warren Buffett sums it best: In the short-term, the market is a voting machine; in the long-term the market is a weighing machine.

On the other end of the spectrum is the day trader. You may find that your personality likes rapid fire decisions, and you can sit in front of the computer from 9:30am to 4pm every day. You would then actively seek out how to become a day trader, learning about charting on multiple time frames, seeking out other day trading groups or day trading firms, and learning the risk management techniques required to become a day trader.

Finally, you might look at becoming a swing and position trader, holding positions from a few days to a few months. I’ve found personally, our firm, Paragon Elite Trading, has made a lot of money, and studies have shown that swing and position trading is probably the best way to take advantage of meaningful moves, up or down, and holds the least amount of risk for someone seeking to become and active trader. This timeframe is technically focused as on day trading, capitalizes on the substantial moves that investors look for, but doesn't tie up capital for the time that an investment does, nor does it offer the risk that day trading does.

Once you find which timeframe fits your personality and your lifestyle, the next choice is to determine what instruments you want to trade.

The vast majority of people start with stocks and many people stick with them. That's fine, but it is capital intensive. I used to manage an All-Cap Growth Fund with over $1b invested. In that case, capital intensive is not a problem. But for those of us that did not inherit a country, we may want to consider alternative investment vehicles. You may discover options and be attracted to the limited capital required and the leverage options provide, but then you'll need to learn about how options are priced and the effects of the movement of the underlying stock as well as the effects of time decay and overall market volatility.

Alternatively, you may find that you like the freedom of being able to trade all hours of the day, enjoy researching the interactions of global banks, and have the intestinal fortitude to manage high leverage. My guess would be that you might want to research successful forex strategies and/or take a professional forex trading course.

You're probably going to have to test out a few different timeframes and a few different instruments to find what fits your personality, but that's fine. You'll be fitting the square peg in the square hole rather than the round hole. Trust me, you'll be much happier seeking out the information, testing it out, and finding a fit than the person who tries to be something he isn't.

Evolutionary Leaps: The Golden Path

There are a select group of people that short-circuit the evolutionary path to becoming a trader. They are the ones who make the jump from Phase One: Saver to Phase Four: Seeker in a single leap. The people that find the Golden Path can step off the road they're on at any time and make the conscious decision to skip to Phase Four: Seeker at any time. We've found it's never too late.

It's simply realization that trading is a team sport and then an affirmative decision to seek out the three requirements to become a successful trader: training, support, and capital.

As Paragon Trading's CEO, I often conduct a thought experiment and ask those who wish to trade with us what the ocean's apex predator is.

Most people would say "Great White Shark."

They were wrong. The ocean's apex predator is a pod of orcas; Killer Whales. They're known as the wolves of the sea. Orcas will take on a Great White…and win.

To complete the evolutionary journey and become a successful trader requires commitment and some courage. Trading systems can be learned, risk management can be learned, discipline can be learned, or systems set in place to enforce discipline, but learning requires commitment.

Taking the next step in your evolution or making the leap to the Golden Path requires courage. You're overcoming the fear of the unknown. You're taking the path less traveled. You have questions and you're afraid you won't find the answers or won't like the answers. You're afraid of failing.

That's fine. The thing about courage is that it compounds. The first step is always the hardest. After that, each step builds on the one before it.

As courage and knowledge builds, it can act as a bank account, allowing you to face the fear of the unknown.

We're not afraid of the pullback, the correction, the downturn, the bear market, or the next financial meteor to enter the atmosphere. We've built our base of knowledge, sought training, sought and accepted support, and have the capital to back our plays.

Even though all the firm's traders have evolved along their own paths, we don't stop. We are constantly evolving as market conditions evolve.

We don't fear the next market meltdown because we have the knowledge and experience to recognize the signs, position ourselves, protect our capital and actually thrive during the next cataclysm.

We don't do this as individual traders; we do this as a firm made up of individual traders working toward a common goal.

We are the pack.

We invite you to learn more about our pack and if we are not a good fit, we will happily point you to another pack that might suit you better. It's not important that our pack be the biggest, but that our pack at Paragon teach, support, and back our traders to the best of our abilities so that they may, in turn teach and mentor the next generation of traders that join the pack.

The more people that take the perilous track that is the evolution of a trader, the more control people have over their lives, both financial and otherwise, and the better off we are as a society.