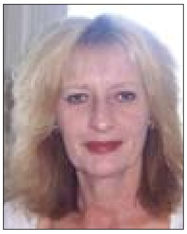

JADE GATE

Forex Success – Top Ten Tips (Part 2)

The moment of greatest possible exposure to risk in the Forex markets occurs in the first few minutes after opening a trade. Jade Gate provides a series of trading tips to help a trader increase his chances for trading success.

You have opened a position at what you believe is the right moment, now what? How do you manage your trade in the best way possible?

The moment of greatest possible exposure to risk in Forex occurs in the first few minutes after opening a trade. Account erosion (the leading cause of blown accounts) occurs due to being stopped out repeatedly. How do you select your entry point and protect your investment at this critical moment?

Unlike other market instruments, such as the stock market, the margin for error in the Forex markets is extremely tight. Gaining mastery of the Forex instrument requires a high level of precision. If a trader lacks knowledge or skill in a particular area, this market will be anything but gracious about it.

In preparing this article, it has been necessary to assume that most readers are across the technical analysis basics. The focus is on tips to help with trade management and to extend a trader's existing knowledge of technical analysis tools that work consistently well in Forex (with some allowance made for bringing new traders up to speed).

There is no universally right or wrong way to approach technical analysis or for that matter, trading style (swing trading, intra-day trading or scalping). Every trader has his own style and preference.

That said, scalpers bear the highest possible level of risk since the moment of entry (and frequent entry) is the time of greatest exposure to potential trade failure. Nevertheless, some traders become very proficient scalpers, trading within the body of moves already in progress and prefer this method of trading over swing or intra-day trading.

What can traders do to maximise their chances of success?

1. Select Your Precise Moment of Entry Carefully

Getting on board the Forex freight train while it is still moving is no simple task. Precision in execution at this critical juncture is extremely important.

Wait until there is solid evidence that price momentum has expired or peaked

- Look for evidence that sellers or buyers are coming into the market at that level.
- Look for bullish engulfing or bearish engulfing candles in the 1-minute charts, 5-minute charts and 15-minute charts and hammers/inverted hammers in the 5-minute or 15-minute charts. The larger the timeframe (e.g. 15-minute upwards), the more reliable the candles (or bars) become.
- Wait for price to test

Do not rush into a trade just because it reaches your entry point. Wait for price to test. Wait for evidence confirming your trade choice. Price may overshoot before recovering. Keep your finger off the trigger until you see visible evidence that it is about to change direction. Price may arrive at your entry point, but that does not mean other traders believe similarly and are going to buy or sell at that point – you need to see hard evidence that selling/buying is occurring in sufficient volume and with sufficient consistency to generate a reverse move (or further extend an existing directional move).

At entry, you are looking for immediate results as soon as the trade is opened. That is, at the time of greatest risk, you are looking for the trade to quickly move into profit. Unless buyer/seller support has been established (it has legs that hold), getting your trade into profit quickly will not happen. The objective is to capture the right "shoulder" of a price move at the exact moment it begins to gather steam and accelerate.

Successful traders recognize that price will grind on support or resistance levels more than once before changing direction. They wait for evidence of buyer or seller support coming in and for that support to be tested before getting on board. They seek to time their moment of entry with precision in order to capture an immediate positive result for the trade.

2. Cover Your Investment Immediately

As soon as your trade moves into profit and you have 10 to 20 pips clearance (or more, depending on the pair you are trading) move your stop up or down to immediately lock in protection of your investment. Practice this until you have a pip clearance formula you are comfortable with. Never leave a trade that has moved into profit, flapping in the breeze. Despite appearances, the testing of support or resistance levels may not yet be complete – momentum that looks expired or peaked can be re-energised to test again one or more times. Cover your position immediately at the breakeven entry point, since this is the time of maximum possible exposure to risk.

The benefit of this approach – the worst thing that can happen is:

- the trade is stopped out at breakeven or in very small profit. If this occurs, step back and reassess. The market is telling you your entry point is (possibly) not correct, do not argue. The market is always right. Wait for the re-test to complete before entering again.

The best thing that can happen with this approach

- the trade will continue to run in the direction of your trade.

Either way, you win.

Employing this technique to manage a trade at the critical high risk juncture helps to reduce your error rate, prevent erosion of your account and preserve your capital funds, provided you have met the criteria in #1 and chosen the moment of entry carefully to begin with.

Successful traders guard their trading capital closely and insure their investment against loss at the first available opportunity.

3. Quarantine Your Trade Against Retracements

Take profit off the table when a threat looms. No trader ever goes broke taking profit.

If you need to re-enter at a later stage, you can. Be clinical and ruthless about taking profit. The objective is to extract as much money out of the market as you possibly can. When the market gives you money, take it, bank it and wait for the next opportunity. Move your trade protection stops up or down as the trade progresses (with an appropriate degree of allowance for zig zag price movement along the way and your preferred style of trading).

Develop a set of trading rules that give clear guidelines for when you need to act to lock in profit. Do not cling to hope when contrary evidence is building. Learn to recognize the most reliable signs for when your trade "goose is cooked" early (e.g. for intra-day traders, hammers/inverted hammers in 5-minute or 15-minute charts, higher timeframes for swing traders, indicating reversal).

When a profitable trade reaches your target, price begins to test a support/resistance level or you become concerned about the trades' potential to keep running, close it out immediately to lock in your profit. There are no guarantee that price will continue to run in the direction you expect. If it continues to run once the level is tested, you can always make the choice to get back on board safely. Closing out does two things. It locks in profit and it provides opportunity to trade the counter trend move (or you may prefer to wait for trend resumption).

Some trend and swing traders use an approach that takes half of the profit off the table while leaving the balance in play. These traders move their protective stops up or down to just above/below the threshold of the 50% retracement mark. This is a judgement call for you as the trader. (More on swing trades at Tip # 8.)

Successful traders recognise and respect the threat of risk to a profitable position in progress, and exit. They lock in profits from the moment of entry until the trade target completes or the threat of retracement reaches their threshold to exit.

4. Understand and Monitor Price Action Drivers Closely

A main issue that is often overlooked in Forex education is detailing the inter-relationships of various currencies to each other and the inter-relationship of the currency market to other markets. What actually causes price to move?

The primary drivers of price movement are:

1. Risk aversion climate. This can be tracked by watching price on the USD/CHF and USD/JPY charts (which, for the benefit of new traders, is why these two charts are always two of the default templates in any trading platform.) When risk aversion kicks in, traders buy the USD/CHF and sell the USD/JPY (usually). This has a flow-on effect to all other currencies. Traffic on these two charts, but especially the Dollar/Swiss (USD/CHF) tends to control all other price action.

2. Economic news releases. Expected bad (or good) news can be factored into the market during the hours prior to release. This explains why news, once released, does not always move the market in the direction you might expect. It may have already been factored into the market. News release data may also occasionally simply be ignored.

   Print off the weekly calendar and keep it next to your trading station. Know when news items are in the queue, research the historical data on that issue (e.g. via the links in the FF calendar page and other news sources). Look for anything in the news that might move the market in either direction in the period of time prior to release (e.g. speculation on good /bad data can drive price up or down to resistance/support thresholds before the event).

3. Gold and oil prices, and the commodity currencies they relate most strongly to (gold – AUD/USD and oil – USD/CAD.)

4. Price action on the stock market – the Dow Jones, NASDAQ and the S & P in particular. Currency markets are especially sensitive to movement in the futures market for these indices (as a measure of economic confidence/ risk aversion dynamics).

5. Profit taking occurs particularly around whole numbers and Fibonacci levels or pivot point levels. When the market becomes concerned about the capacity of a market to break through psychological barriers or support/ resistance levels, profits can be taken out and locked in while the issue tests.

6. Stops domino effect and stop hunts. Since many traders

utilize similar stop levels, a move that "clips" these can trigger an extended domino effect. This may or may not reflect a bona-fide move. This may also occur in reverse when new highs are being tested. Buy orders are in the market immediately above the threshold of resistance. If price clears resistance, this can "clip" the buy orders into action.

7. Random spikes, also known as 'whip saws.' Protecting your trade against this alone is one reason why traders need to lock in profits at every step along the way and use stops religiously.

8. Greed – the market can move simply because the opportunity exists to make money. It does not always need a "fundamental" reason.

9. Sudden unexpected news – this may include public health threats (like swine flu), terrorism acts, geological or climate events or the sudden escalation of a war threat.

10. Carry trade price action, particularly ahead of the weekend when institutional traders are looking to park funds in a place with the best short-term interest rate.

11. Price action on the EUR/GBP cross controls price action on the EUR/USD or GBP/USD and the yen crosses (GBP/JPY, EUR/JPY).

12. Watch the time of day. Before the U.S. session starts, Europe controls the trading floor. During this time, momentum tends to support the Euro and GBP heading north (proviso risk aversion is not on the agenda that day, monitor the economic news data, U.S. futures, FTSE and DAX for further clues on this).

    When the U.S. session starts (around 7.00am ET), it is time for "Game On." If the U.S. dollar is going to find or extend its support, it will likely happen at the beginning of the U.S. session (though not always, Europe can also buy up the dollar and short everything else, subject to risk climate).

    Each global trading zone is prone to support its own currencies, particularly at the times when the market opens times for that region. (Make your own observations/draw your own conclusions on this). The EUR/GBP cross can influence prices while Europe controls the trading floor. New traders needing a desktop international time-clock can obtain a good free one from here http://qlock.com/download/ (scroll down to the lower part of the screen for the free download version).

    Successful traders monitor the key drivers of price action closely. They keep their finger on the pulse of the market for any potential change to trade circumstances.

5. Support and Resistance

The importance of support and resistance and the role it plays in the Forex market cannot be emphasized enough. Different traders approach monitoring support and resistance levels can vary. These are some of the most common ways of plotting and tracking support and resistance.

- Trend Lines
- Fibonacci retracement levels (weekly, daily, hourly)
- Pivot Points
- Elliott Waves
- Forks

For traders who prefer Fibonacci (include me in this group), you may wish to add the 76.4 setting to your default program. This level is often omitted in default Fibonacci retracement indicators but it is a key level that many advanced traders know and use.

Successful traders know the value of support and resistance. Their preparation includes plotting these levels on their charts and they often use these levels as triggers for trade entry and exit.

6. Technical Analysis That Works in Forex

Successful traders have put in the time and effort to identify a technical analysis system that works consistently for them in the dynamic Forex market. Technical analysis that works in other markets may not apply in Forex. Successful traders know that there are circumstances where a standard technical analysis approach may not hold true. Getting acquainted with the "exceptions" is part of the apprenticeship.

Every trader has his or her preferred set of technical analysis tools. However, a common theme is to "Keep It Simple." Charts that are too "busy" or overloaded with "noise" can complicate rather than streamline the trader's job.

An important skill to develop is identifying the potential direction outcomes (both long and short) in any given chart and assigning a proper weight to each scenario. Quality analysts always give both sides of the equation and for good reason. Look for and examine any contrary evidence

Chart 1

Chart 2

in the technical analysis (because news tends to follow the analysis, not the other way around – the signs (usually) appear first in technical analysis.) When clarity is absent, stay out.

Some additional knowledge you may find useful for trading Forex is outlined in the next sections. (Please keep in mind that this information is not intended to be definitive. This is a tips guide in condensed form.)

Successful traders use a technical analysis system that works consistently for them in the Forex market. They know the

Chart 3

circumstances (via experience) when their analysis can be relied upon and when it cannot.

7. Chart Timeframes and Candles

Although shorter timeframes are used for selecting a precise entry point, short timeframes can be unreliable for candlestick purposes. Reliability is most evident in the 15-minute timeframe and upward. Hammer and inverted hammer candles are important, having a high degree of reliability that increases with larger timeframes (hourly and daily). Other candles with a good degree of reliability are: piercing line, gravestone doji, dragonfly doji, bullish engulfing and bearish engulfing.) Keep in mind that there are no 100% bulletproof strategies – you are looking for candle formations with the highest degree of reliability (80% or more).

Some lesser known but highly reliable candle formations are outlined below.

Candle Wicks. Pay attention to the wicks of candles as well as the body of the candle. A collection of 3 or more wicks on a 15-minute chart or higher (the higher the timeframe, the more reliable candles become) can mean solid price rejection with an imminent reversal. These are called tri-tips (3 wicks), quad-tips (4 wicks) or quin-tips (5). If you can draw a horizontal line across the top (or bottom) edge of the body of the candles, horizontally intersecting a collection of 3 (preferably more, sometimes up to 6) wicks, you have a very reliable signal of price reversal. Price tends to move in the opposite direction of the wick(s). Long wicks are especially interesting since they indicate price is being driven with force in the opposite direction (this is what generates hammers/inverted hammers).

Tweezers. One bearish, one bullish, side by side, both with good (equivalent length) wick extension to the downside (bear candle first, bull candle second, for bullish reversal) or wick extension to the upside (bull candle first, bear candle second, for bearish reversal). Tweezers are especially useful on daily charts as an indicator of major trend reversal. They also have application on the 15-minute timeframe and higher. Chart 2 shows a good example of classic bullish Tweezer candles (and what they can do to price) can be seen on the USD/CHF chart on July 15/16 in 2008 . They are called "Tweezers" because (other than looking like a pair of tweezers) they "pinch" price and propel it with force in the direction of the last candle in the tweezer.

Always review the daily and hourly timeframes before entering a trade. It is important to step back and look at the bigger picture before launching into the microscopic detail and hitting the trade trigger (because higher timeframes usually hold precedence over lower timeframes.)

Successful traders keep the big picture in view. They have ascertained the most reliable timeframes to suit their trading style and know which candles (or bars) with the highest degree of reliability.

8. Swing Trades and Knowledge of Chart Patterns

Since the market repeats itself, chart patterns are a useful trading tool. Recognizing a chart pattern with an attendant trade set-up forming, and recognizing it early, helps.

Chart patterns are particularly important for swing traders. Having the confidence to leave a trade on the table when the retracement of the initial move begins (and being able to sleep at night!) requires experience and close familiarity with the pattern a trader is seeing. Swing trades that run successfully for several days or longer are the most profitable form of trading in Forex. Many traders cite the "let your profits run, cut your losses" mantra (which holds truth), however, doing this with confidence is an acquired skill and contingent upon your knowledge of chart patterns.

There are times when letting your profits run is the perfect strategy, and other times when letting your profits run can be a recipe for disaster. Knowing the difference, the time when it is appropriate to do this, and at what point to close out a swing trade, forms part of the trader's skill and sound judgement.

Some of the most common chart patterns traders should be familiar with are:

> Head and Shoulders, Inverse (or Reverse) Head and Shoulders, Flags, Wedges, Triangles, Breakouts, Double Bottoms, Double Tops, M shapes and W shapes, Continuation patterns.

For new traders, additional information on the chart patterns can be found at

http://www.investopedia.com/search/searchresults.aspx?q=chart+patterns&submit=Search

or

http://www.babypips.com/school/pattern_schmatterns.html

(or any other good quality site that provides education on chart patterns).

Successful traders recognise chart patterns as they form. They understand the implications of the pattern for a trade in progress or as a potential entry set-up and they know when the pattern has reached its limitation to warrant an exit (or partial profit taking while allowing the balance to run).

9. Moving Averages

Exponential (EMA) and simple (SMA) moving averages are widely used in the Forex market as guides to trend direction. In some instances, they are used for generating of trade signals. Typically, moving averages have most impact on daily charts, however some traders also use moving averages across multiple timeframes.

EMAs that are used to plot and pay attention to are the 21, 55 and 200. (As shown in the chart #2, 200 = hot pink, 55 = violet, 21 = light pink). The 200 EMA is particularly important since it has the characteristic of behaving either like a gorilla (bearish) or a trampoline (bullish) in terms of its impact on price. Looking at the USD/CHF tweezer chart at tip # 7 – note what happened to price after the 21 crossed the 55, and especially note what happened when price touched the 200 in two places (the trampoline kicked in). Review of where price is in relation to your moving averages (either SMA or EMA) should be part of your daily preparation routine.

When moving averages converge, their effect is compounded. Price can become "stuck" between two moving averages. Once it clears the hurdle, it may take off with speed. When moving averages cross over, price is likely to continue moving in the direction of the line crossing over. Daily moving averages can also act to support price or act to suppress price when there is no other apparent support/resistance level in play. This is one reason why referring back to the daily timeframe during the trade session is important (if a key moving average is near the price action).

Successful traders plot and pay attention to the moving averages of most proven value to their trading system.

10. Oscillators and Momentum Indicators

An oscillator that works well in Forex is the full stochastic with parameters set on 20, 2, 2. (Shown in chart #3). This gives a very clear signal since it glues itself to the ceiling or floor when momentum has expired or peaked. This indicator has application across all timeframes. The lower 1-minute, 5-minute and 15-minute timeframes are especially useful for selecting the precise moment of entry. Using the 15-minute timeframe as the base, look for the signal to be sitting in the same place on the floor or ceiling across all shorter timeframes (as well as the 15-minute) and for evidence of the signal beginning to turn up or down in the opposite direction to where it has just been. Look also for confirmation in the candles.

This gold chart shows the value of the 15-minute timeframe for this oscillator.

The caveat with oscillators (of all varieties) is that they can be close to useless when the market is trending strongly. Overbought or oversold conditions can remain the status quo for a very long time. This is why you need to see supporting evidence in the candles to warrant acting on a signal. It is also why referring to higher timeframes matters. When the market is running strongly, the base reference point for this oscillator needs to shift from the 15-minute to the 1 hour timeframe. Look for the oscillator hitting the floor or ceiling in unison on all timeframes – 1-hour, 30-minute, 15-minute, 5-minute and 1-minute. Also, look for confirmation in the candles.

Oscillators and other technical analysis tools have value but only up to a point. Interpreting their value, when they apply, when they do not apply, is a skill learned through the experience of trial and error. This is one factor that contributes to a trader's sound judgement.

Successful traders understand the limitations of their technical analysis indicators. They may use oscillator and momentum indicator tools as a second opinion to their own judgement and other market signals in combination.

Summary

Choose your moment of entry carefully, wait for price to test. Time your entry with precision. The objective is to get your trade into profit as quickly as possible to contain the high level of exposure to risk at this critical juncture.

Cover your investment at break-even as soon as practically possible. As price moves in the direction you anticipate, move your stops up or down to protect your earnings. Decide on an adequate level of risk to hold once a trade is profitable and lock in profits whenever a threat reaches an unacceptable level. Learn to recognise the most reliable signs of retracement. Do not cling to hope or stretch your protective stops. Be clinical and ruthless about taking money out of the market and putting it in your own pocket.

Closely monitor all key drivers of price for the currencies you trade. Research thoroughly, do your own due diligence and look for potential sources of threat to trend direction. Critically appraise any and all information you read, including opinions of analysts.

Find a technical analysis system that works consistently well for you in the Forex market and refine it until you reach a level of precision in its use. Prepare your charts ahead of the market week and update them daily, include the key support and resistance areas and plan your trades around these levels (unless scalping).

Successful traders possess sound judgement, borne out of two things –

- Knowledge of technical analysis tools that work in Forex, the rules and exceptions that come with market experience.

- The skill of the trader, in particular -

  - the capacity to recognise safe and potentially profitable entry points;

  - precision of execution at the moment of entry;

  - keeping the error rate low;

  - quarantining trades against retracement / knowing when to exit;

  - accumulation of consistently successful "winning" trades;

  - competence in trade management.

Jade Gate is a professional in the management and education sectors (managing education facilities) and has been trading stocks, options and futures for 5 years. She began trading Forex one year ago. She thought Forex trading would be fairly straightforward given her background, but found it much more complex than she had anticipated. She has recently come through the "apprenticeship" phase and is now trading Forex successfully. These tips are 'fresh from the trenches,' so to speak.

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