

# A personal insight into trading the Forex



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# Forward

This presentation is a combination of my own personal ideas and beliefs as well as a compilation of ideas from books, journals and guest speakers at the ATAA.

Please use the following material for entertainment AND/OR education only. It is not to be considered trading advice.

A specific trading plan must be tailored to suit each individual. This allows them to apply their own unique thumb print to the plan.

# What Market ???

In line with our Trading Plan, a trader must first look at the market they are interested in and perform some analysis as to whether this market is suitable for them. Things to look at are –

- ▶ Time frame i.e. 5min, 1hr, Daily bars etc.
- ▶ Account size.
- ▶ Position sizing.
- ▶ When to trade.
- ▶ Style of trading i.e. Trend following, mean reversals etc.
- ▶ Expected duration of trades i.e. 1 bar, 10 bars, 20 bars.

# Time Frame

To a large degree, the time frame of the bars greatly effects the way I look at the markets and trade the markets.

The account size and position sizes are greatly affected by the time frame of the bars.

The intraday movements can to a large degree be ignored if I was trading on a Daily or Weekly bar period. So what time the Asian markets or European Markets open has no effect on our trading method and style.

Why chose Forex? It allows me to easily get in and out of the market, in either direction and any time frame I choose. In this talk, I will primarily focus on 5min bars.

The general account size required for trading on 5min bars can be much smaller than trading on daily bars.



# Account Size

The size of the trading account greatly determines the time frames and account markets I can trade in.

With an account of \$100,000.00, I could trade virtually any market – Shares, Options, Futures (Index & Commodities, Currencies) etc but most of us here don't have \$100K to trade with.

Why chose Forex? It allows me to easily get in and out of the market, in either direction and trade relatively small position sizes on small accounts.

In this example, I will use a more typical size of an average Forex trader i.e. \$5,000.00. Although the same principals could be applied to larger or smaller size accounts.



# Position sizing – Size

In the Forex world, a standard lot size is typically 100,000. Borrowing from the Futures market, this is normally referred to as 1 contract. Some brokers may also have Mini contracts i.e. 10,000.

**Note** – A 1 Pip move of 1 Contract (100,000) on the EUR/USD pair is \$10.

So a move from 1.0456 to 1.0457 on a position size of 100,000 = \$10



# Position sizing – Margin/Leverage

To determine how big a position I can have based on my account, I need to look at the Margin requirements for my Forex provider. The margins vary from broker to broker but are typically in the 1:1..50:1 region.

To calculate how big a typical position size I can have, I will use IB's (InteractiveBrokers) scheduled size for the EUR/USD pair, this is 40:1.

So to calculate the margin required for a standard lot size of 100,000, I use the following equation :

Currently the EUR/USD cross ~ 1.3000, so I will use this amount.

$$100,000 * 1.3000 = 130,000$$

$$130,000 / 40 = \$3250.00$$

**Therefore for my IB account must have at least \$3250  
This amount falls within my \$5000 account.**



# Position sizing – Margin/Leverage

## Margin calculator from oanda.

**Margin Calculator**

Calculate the margin required when you open a position in a

**Margin Available Calculator**

Account Currency	USD	▼
Currency Pair	EUR/USD	▼
Current Price (EUR/USD)	1.30726	
Margin Ratio	40:1	▼
Number of Units	100000	
<input type="button" value="Calculate"/>		
Margin Used (USD)	3268.15	

<http://fxtrade.oanda.com/analysis/margin-calculator>





# Position sizing – Margin/Leverage

The oanda calculation uses the following formula:  
*({BASE} / {Home Currency}) \* units) / (margin ratio)*

For example, suppose:

*Home Currency = USD*

*Currency Pair = GBP/CHF*

*Base = GBP; Quote = CHF*

*Base / Home Currency = GBP/USD = 1.5819*

*Units = 1000*

*Margin Ratio = 20:1*

Then, margin used:

*= (1.5819 \* 1000) / 20*

*= 79.095 USD*



# Risk

As per the normal touted risk suggestions, I will use a 2% risk model for most of this presentation. New traders may want to use a smaller risk size of 1% or in the 1..2% area.

So on a \$5K account and using 2% risk, this means a risk on any one trade of  $(\$5,000 * 0.02) = \$100.00$ .

2% on a \$1K account = \$20.00.



# When to trade ?

A large portion of people here in Australia that trade the Forex, usually have a fulltime day job and are looking to perform some trading of an evening.

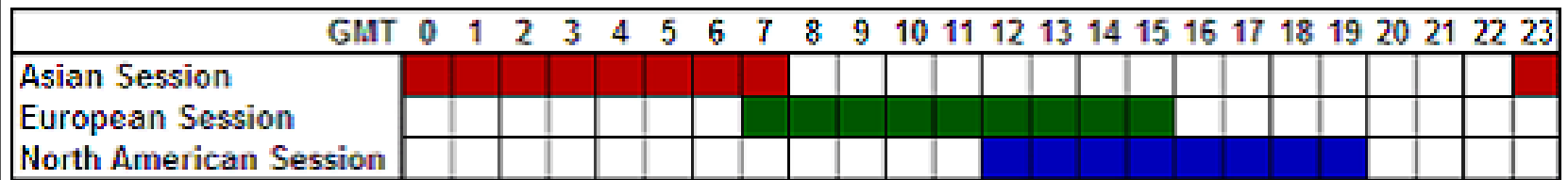
So lets have a look and see when is a good time to trade.



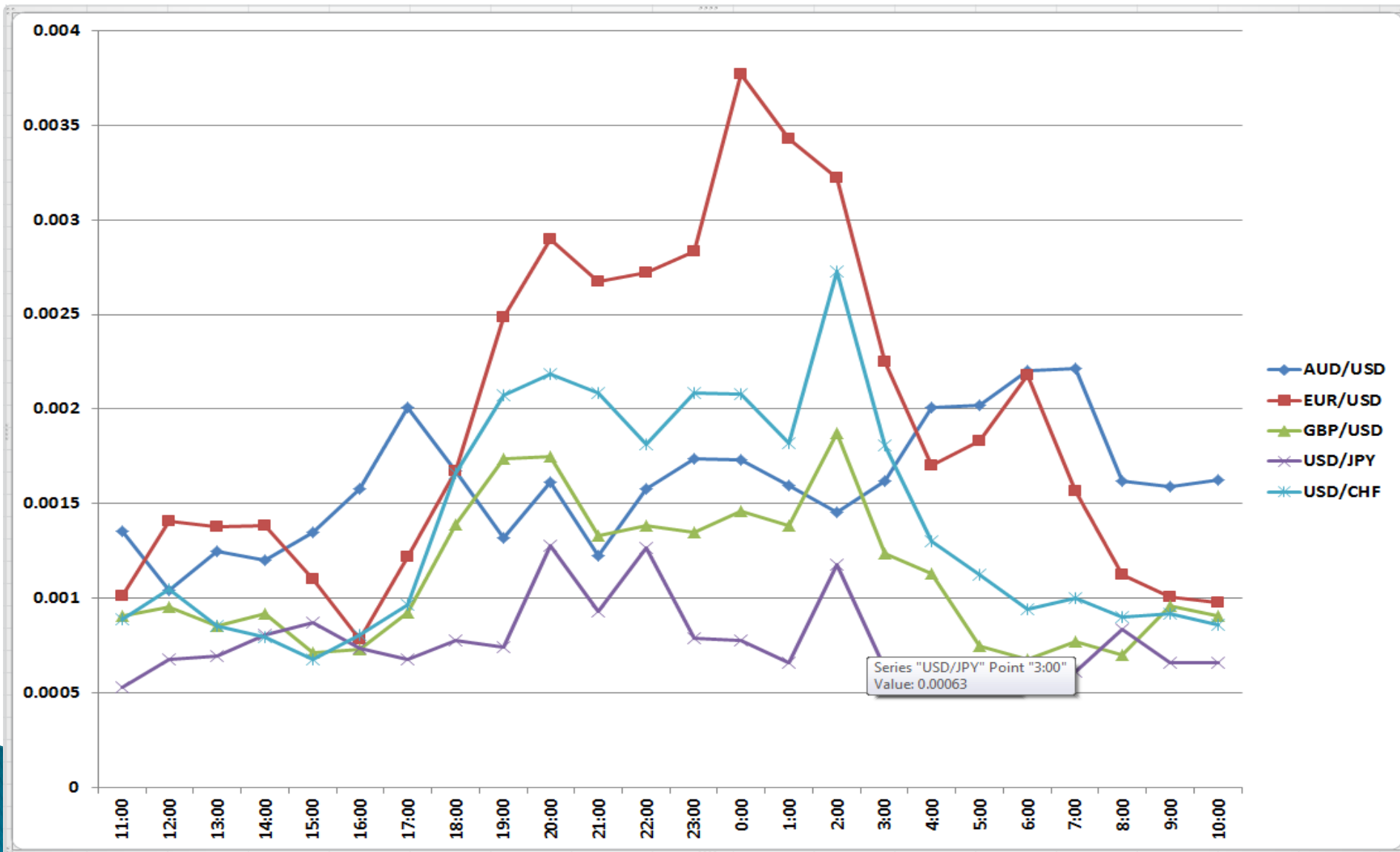
# When to trade ?

Session	Major Market	Hours (GMT)
Asian Session	Tokyo	11 p.m. to 8 a.m.
European Session	London	7 a.m. to 4 p.m.
North American Session	New York	noon to 8 p.m.

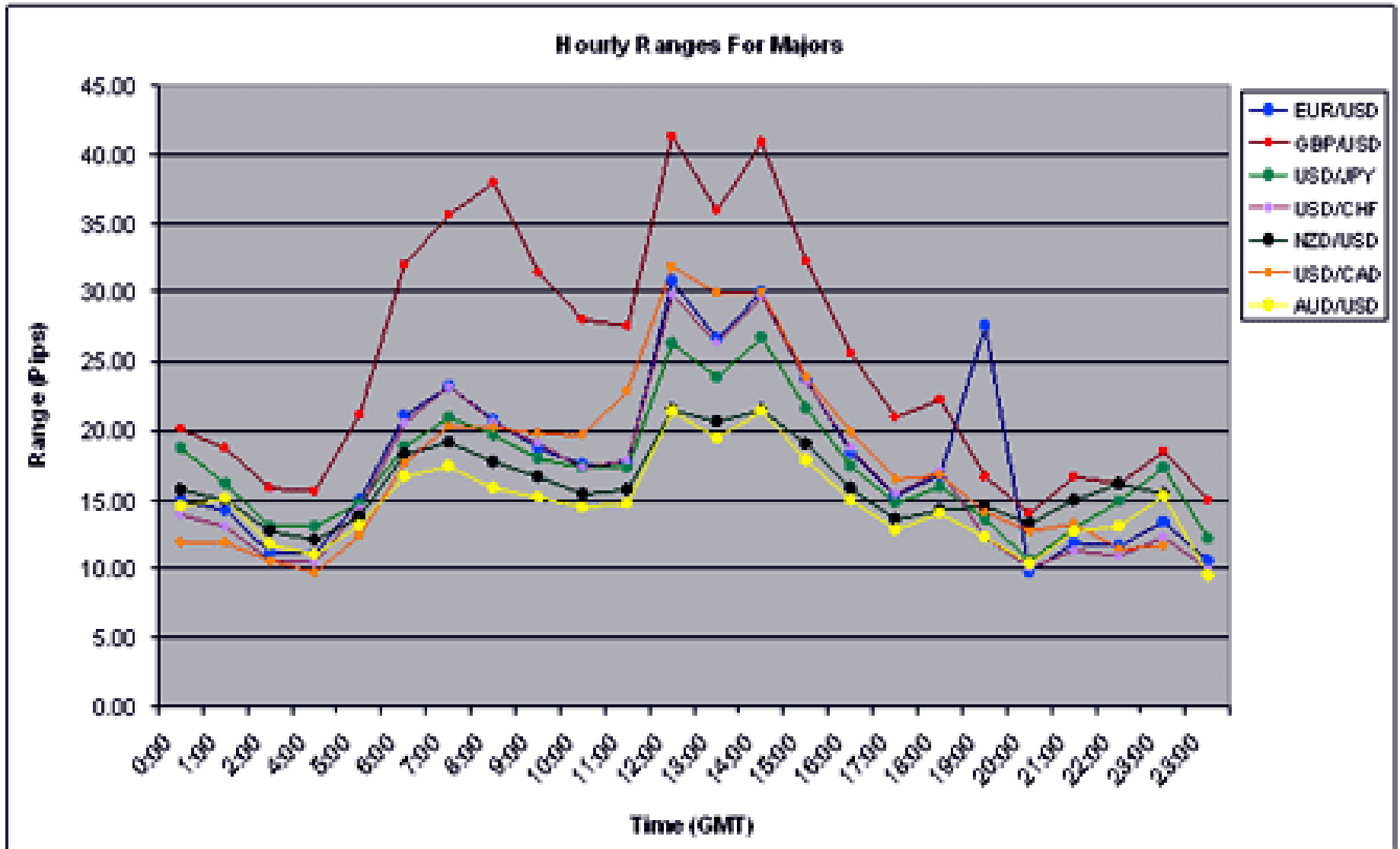
**Figure 1: Major market session hours**



# When to trade ?



# When to trade ?



# Designing the System

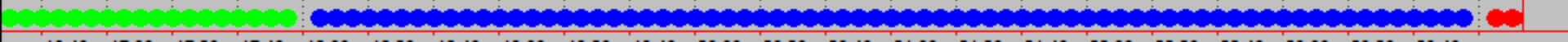
So after determining what time frame and what pairs I'm going to trade, now I need to look at some charts and put together a system.

Remember, a System is –

- 1) Entry.
- 2) Stop Loss / Initial Stop.
- 3) Position Size.
- 4) Exit. (Profit Target, Trailing, discretionary)

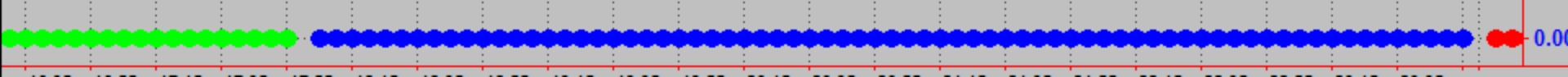


Monday 03-12-2012





Tuesday 04-12-2012



# Sample Chart Review

After examining the charts, I've decided to go with a "With Trend System". Basically, I determine when the market is trending and look to enter on a pullback toward a 20EMA.

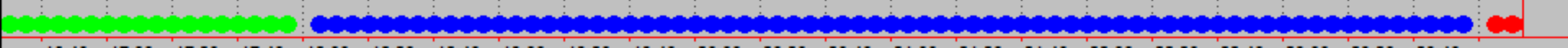
Referring to Van Tharpes work, it is better to make many smaller trades with small profits, then to hope for the 1 in 20 big trade to cover all of the losses.

Therefore, I will use a 10 Pip Profit Target and a 10 Pip Stop Loss.

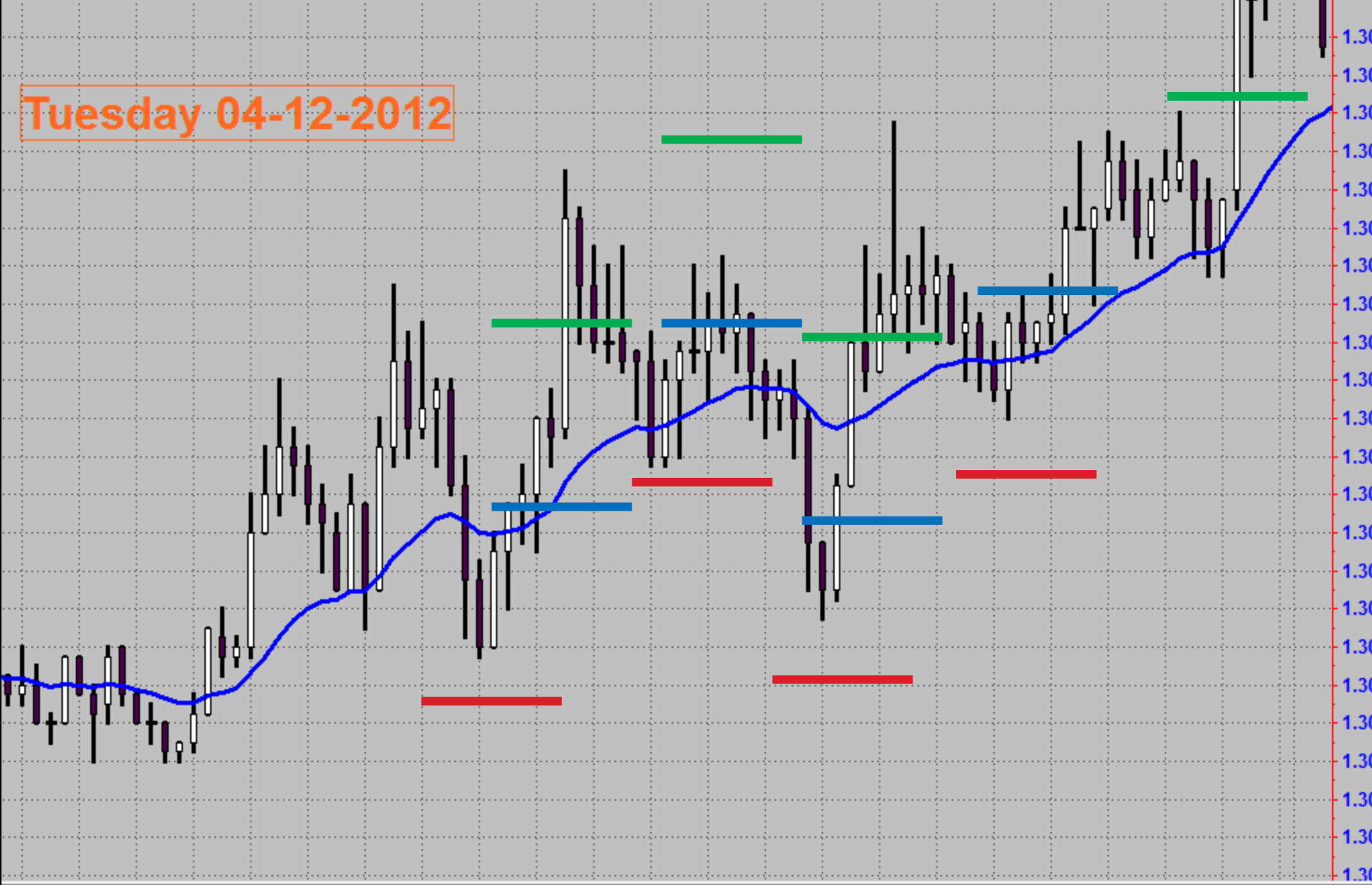
Our maximum risk per trade on our \$5000 account is \$100. \$100 also equals 10Pips when using a 100,000 Lot size.



Monday 03-12-2012



Tuesday 04-12-2012



# Food for thought !

In anyone night, what is a possible average return? 10 Pips? Unreasonable?

How can I improve on these systems?

1. Compounding our position sizes
2. Taking advantage of the Trend
  - a) Bigger Targets?
  - b) Split the trade?



# Compounding our position sizes

So I'm averaging 10 Pips a night (\$100) trading with my 100,000 position size. Over an average year, say 200 trading days, my return would be \$20,000 net.

If I was to not stay with the standard position risk size of 10pips but adjust my position size each day based on my accumulated profits, where would I be?



# Compounding our position sizes

An example -

My starting account is = \$5000.00

1<sup>st</sup> trade I make 10pips = \$100.00.

My account is now = \$5100.00.

What's an easy way to calculate a compounding method?

$5000 * 2 * 10 = 100,000$  units

Where

5000 = Account size

2 = Percentage risked

10 = 100/Risk in Pips ie 10

So at the start of tomorrows session, I change my order size to being  $5100 * 2 * 10 = 102,000$  units



# Compounding our position sizes

Risk (%) =	2	Stop Size (Pips) =	10			Profit Target (Pips)=	5			
Day	Day Start Balance	Units	Profit in Pips	Profit in \$\$\$	Day End Balance	Day Start Balance	Units	Profit in Pips	Profit in \$\$\$	Day End Balance
0	\$ 5,000.00	100,000	5	\$ 50.00	\$ 5,050.00	\$ 5,000.00	100,000	5	\$ 50.00	\$ 5,050.00
1	\$ 5,050.00	100,000	5	\$ 50.00	\$ 5,100.00	\$ 5,050.00	101,000	5	\$ 50.50	\$ 5,100.50
2	\$ 5,100.00	100,000	5	\$ 50.00	\$ 5,150.00	\$ 5,100.50	102,010	5	\$ 51.01	\$ 5,151.51
3	\$ 5,150.00	100,000	5	\$ 50.00	\$ 5,200.00	\$ 5,151.51	103,030	5	\$ 51.52	\$ 5,203.02
4	\$ 5,200.00	100,000	5	\$ 50.00	\$ 5,250.00	\$ 5,203.02	104,060	5	\$ 52.03	\$ 5,255.05
5	\$ 5,250.00	100,000	5	\$ 50.00	\$ 5,300.00	\$ 5,255.05	105,101	5	\$ 52.55	\$ 5,307.60
6	\$ 5,300.00	100,000	5	\$ 50.00	\$ 5,350.00	\$ 5,307.60	106,152	5	\$ 53.08	\$ 5,360.68
7	\$ 5,350.00	100,000	5	\$ 50.00	\$ 5,400.00	\$ 5,360.68	107,214	5	\$ 53.61	\$ 5,414.28
8	\$ 5,400.00	100,000	5	\$ 50.00	\$ 5,450.00	\$ 5,414.28	108,286	5	\$ 54.14	\$ 5,468.43
9	\$ 5,450.00	100,000	5	\$ 50.00	\$ 5,500.00	\$ 5,468.43	109,369	5	\$ 54.68	\$ 5,523.11
10	\$ 5,500.00	100,000	5	\$ 50.00	\$ 5,550.00	\$ 5,523.11	110,462	5	\$ 55.23	\$ 5,578.34
195	\$14,750.00	100,000	5	\$ 50.00	\$14,800.00	\$ 34,804.70	696,094	5	\$ 348.05	\$ 35,152.75
196	\$14,800.00	100,000	5	\$ 50.00	\$14,850.00	\$ 35,152.75	703,055	5	\$ 351.53	\$ 35,504.27
197	\$14,850.00	100,000	5	\$ 50.00	\$14,900.00	\$ 35,504.27	710,085	5	\$ 355.04	\$ 35,859.32
198	\$14,900.00	100,000	5	\$ 50.00	\$14,950.00	\$ 35,859.32	717,186	5	\$ 358.59	\$ 36,217.91
199	\$14,950.00	100,000	5	\$ 50.00	\$15,000.00	\$ 36,217.91	724,358	5	\$ 362.18	\$ 36,580.09
200	\$15,000.00	100,000	5	\$ 50.00	\$15,050.00	\$ 36,580.09	731,602	5	\$ 365.80	\$ 36,945.89
201	\$15,050.00	100,000	-5	-\$ 50.00	\$15,000.00	\$ 36,945.89	738,918	-5	-\$ 369.46	\$ 36,576.43
202	\$15,000.00	100,000	-5	-\$ 50.00	\$14,950.00	\$ 36,576.43	731,529	-5	-\$ 365.76	\$ 36,210.67
203	\$14,950.00	100,000	-5	-\$ 50.00	\$14,900.00	\$ 36,210.67	724,213	-5	-\$ 362.11	\$ 35,848.56
204	\$14,900.00	100,000	-5	-\$ 50.00	\$14,850.00	\$ 35,848.56	716,971	-5	-\$ 358.49	\$ 35,490.07



# Taking advantage of the Trend

My system to this point has been a fixed Stop Loss of 10 Pips and a Profit Target of 10 Pips.

How can I make this better?

What if I was to look at the big trend and somehow incorporate this into my system?



# Taking advantage of the Trend Thought #1

In a major UP trend, the up thrust are larger than the down thrusts, else we wouldn't have an up trend.

So what if I was to define that the Major trend was the relationship of the closing price relative to a 200SMA.

Close price above the 200SMA then Major Up trend, close price below the 200SMA then Major Down trend.



# Taking advantage of the Trend Thought #1

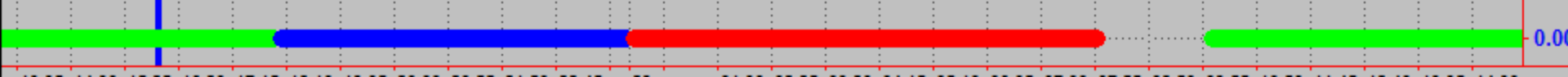
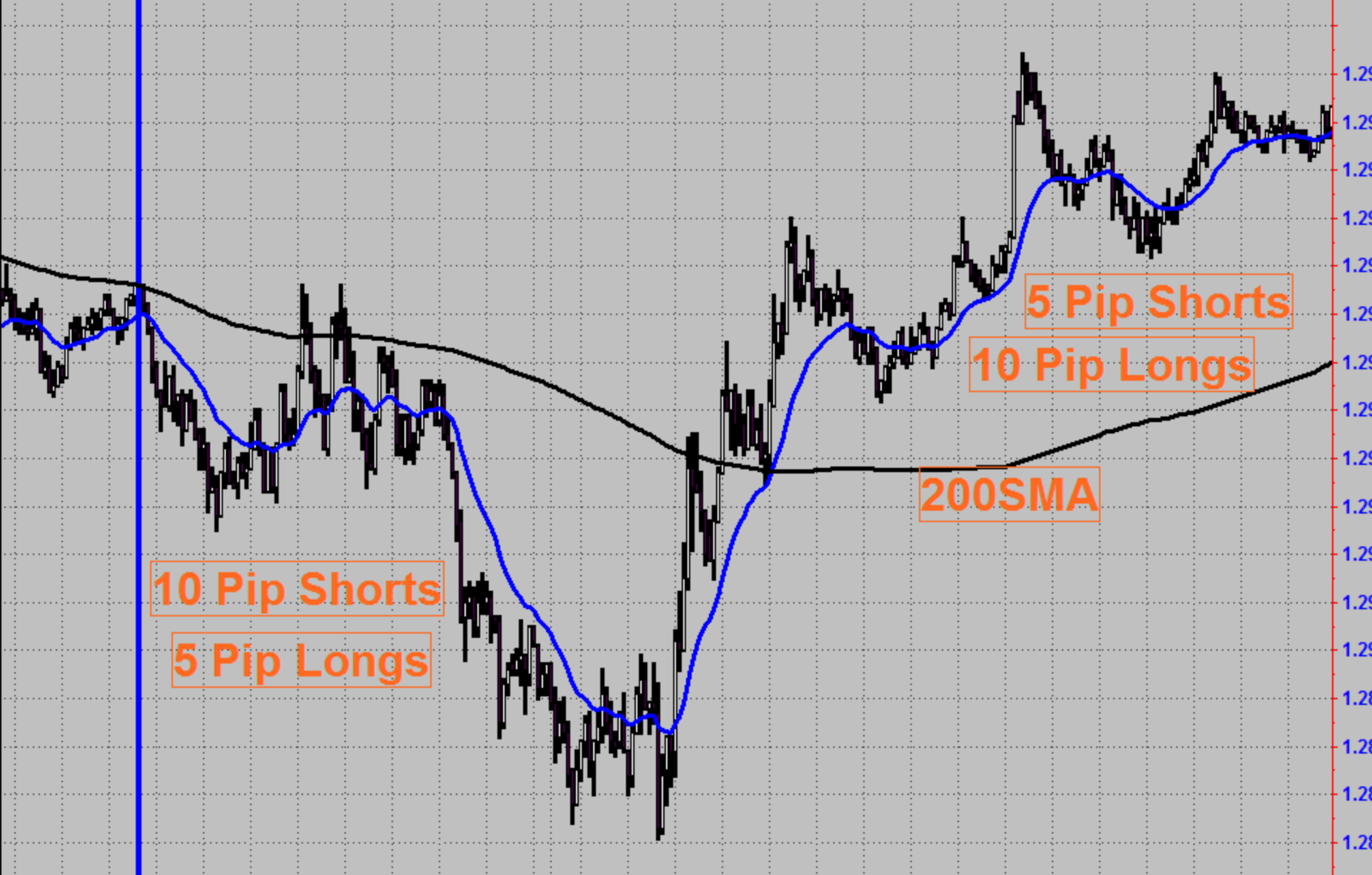
If in a Major Up trend and the price is generally above the 20EMA, then Long target=10 Pips.

If in a Major Up trend and the price is generally below the 20EMA then Short target=5 Pips.

If in a Major Dn trend and the price is generally below the 20EMA, then Short target=10 Pips.

If in a Major Dn trend and the price is generally above the 20EMA then Long target=5 Pips.





# Taking advantage of the Trend Thought #2

If in a Major Up trend and the price is generally above the 20EMA, then Long target=10 Pips for **HALF** the position (50,000) and trail a 5 Pip Stop on the remainder.

If in a Major Up trend and the price is generally below the 20EMA then Short target=5 Pips.

If in a Major Dn trend and the price is generally below the 20EMA, then Short target=10 Pips for **HALF** the position (50,000) and trail a 5 Pip Stop on the remainder.

If in a Major Dn trend and the price is generally above the 20EMA then Long target=5 Pips.



# Taking advantage of the Trend. The Major Trend definition

There are numerous ways of defining a Trend :

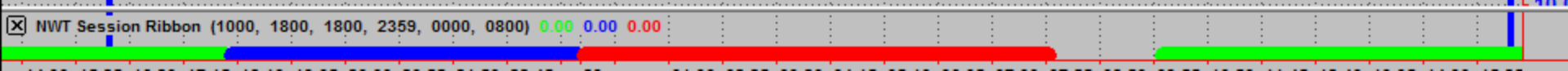
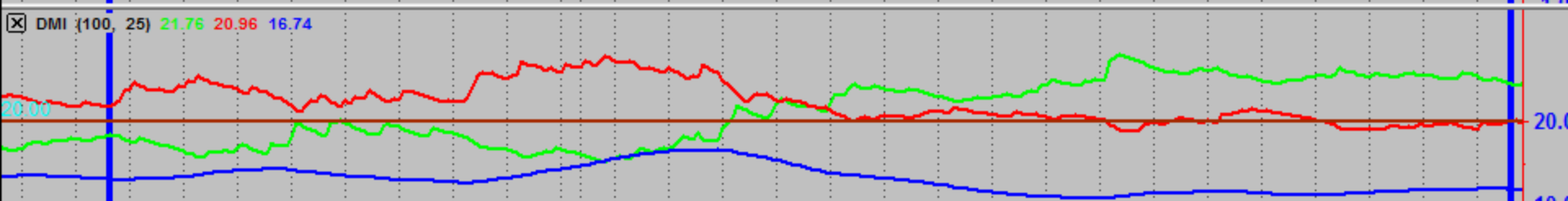
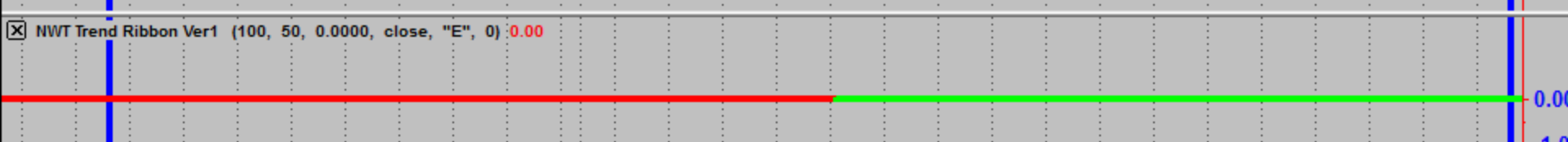
- a) Higher Highs, Higher Lows
- b) Close  $>$  200SMA
- c) ADX  $>$  30
- d) Comparing two MA's
- e) Etc.

Here is an example of a few of these variants.



28/11/2012 2:10:00 PM - 29/11/2012 4:10:00 PM

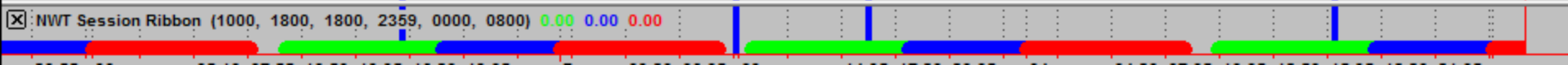
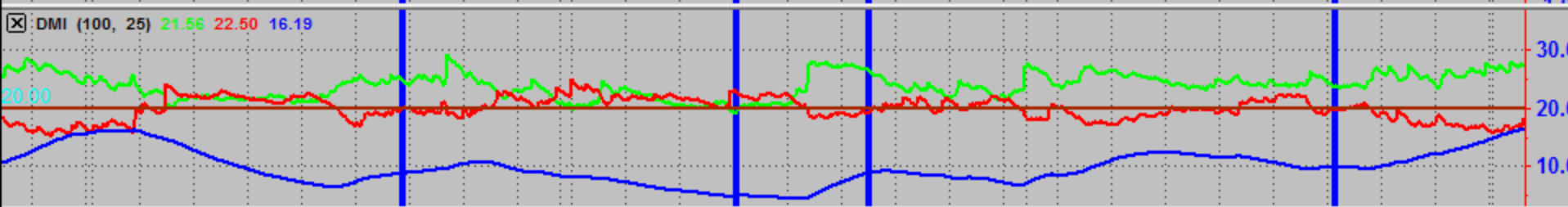
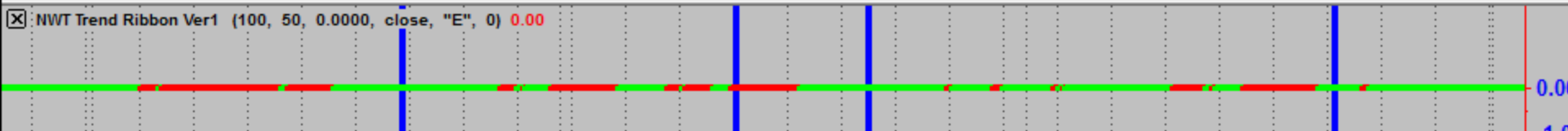
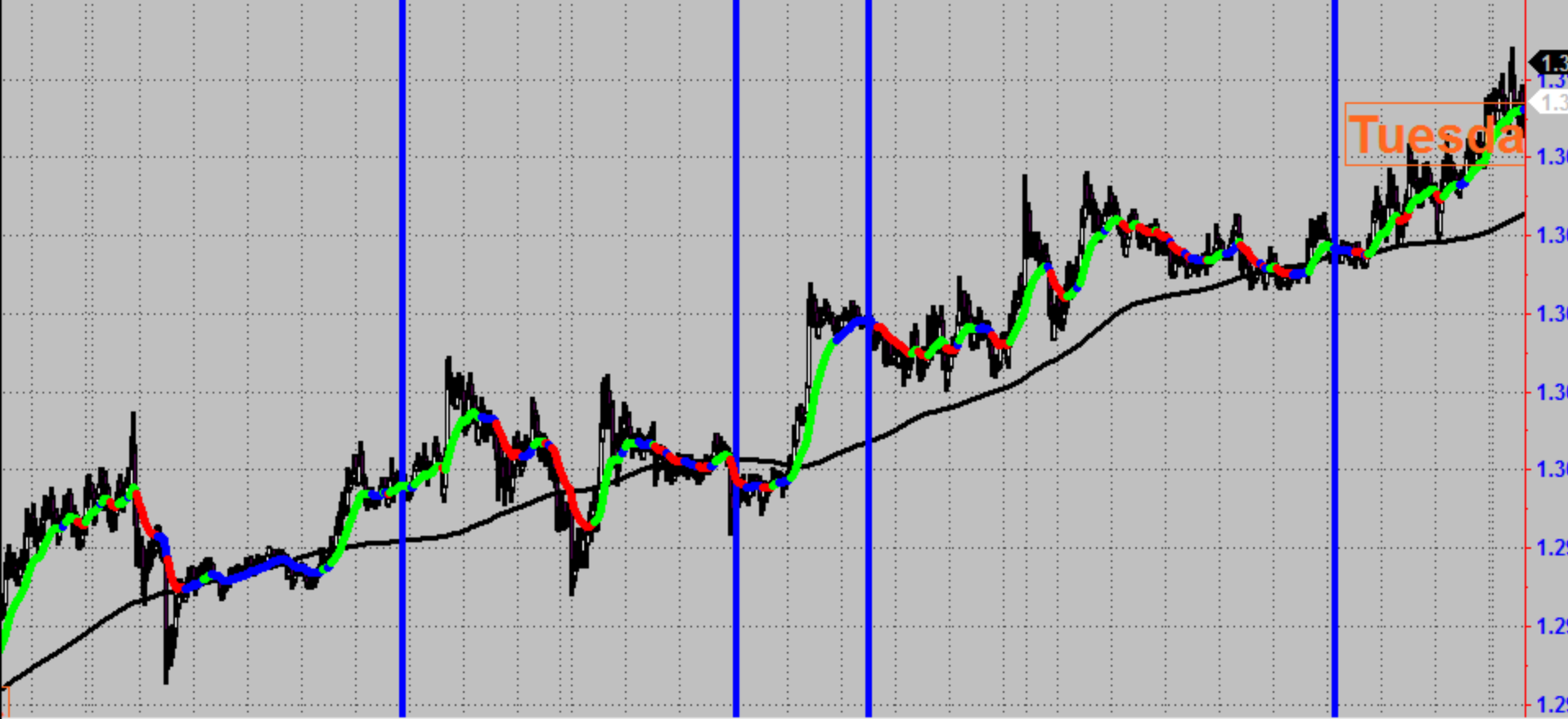
SA EUR.USD USD USD/EUR Cash EUR.USD 5 Minutes Trade IDEALPRO Interactive Brokers Cash 5/12/2012 8:55:46 PM B=1.30955 A=1.30960 H=1.31265 L=1.29885 C=1



29/11/2012 7:25:00 PM - 5/12/2012 1:40:00 AM

MultiC

SA EUR.USD USD USD/EUR Cash EUR.USD 5 Minutes Trade IDEALPRO Interactive Brokers Cash 5/12/2012 9:19:12 PM B=1.30940 A=1.30945 H=1.31265 L=1.29885 C=1





# Trading Strategies - Example



# Wednesdays Price Action

5/12/2012 4:40:00 PM - 6/12/2012 12:20:00 AM

MultiC

SA EUR.USD USD USD/EUR Cash EUR.USD 5 Minutes Trade: IDEALPRO Interactive Brokers Cash 8/12/2012 8:25:44 AM B=1.29260 A=1.29265 H=1.31265 L=1.28760



NWT Trend Ribbon Ver1 (100, 50, 0.0000, close, "E", 0) 0.00

NWT Session Ribbon (1000, 1800, 1800, 2359, 0000, 0800) 0.00 0.00 0.00



# Thursdays Price Action

6/12/2012 4:55:00 PM - 7/12/2012 12:35:00 AM

MultiCharts64

SA EUR.USD USD USD/EUR Cash EUR.USD 5 Minutes Trade IDEALPRO Interactive Brokers Cash 8/12/2012 8:23:31 AM B=1.29255 A=1.29260 H=1.31265 L=1.28760



Legend for trend ribbons:

- NWT Trend Ribbon Ver1 (100, 50, 0.0000, close, "E", 0) 0.00
- NWT Session Ribbon: (1000, 1800, 1800, 2359, 0000, 0800) 0.00 0.00 0.00

# Fridays Price Action

7/12/2012 5:10:00 PM - 8/12/2012 12:50:00 AM

MultiCharts64



# Sample trading video



# In finishing

All though I have focused on the Forex market, I hope you have picked up some insights that you can use on other markets and instruments.

There is an old cliché

**“If you fail to plan, plan to fail”**

*Thank you,  
Neil Wrightson.*

# Bibliography & further reading

- ▶ **Trade your way to financial freedom**

*By VAN K. Tharp*

- ▶ **Street Smarts**

*By Linda Bradford Raschke*