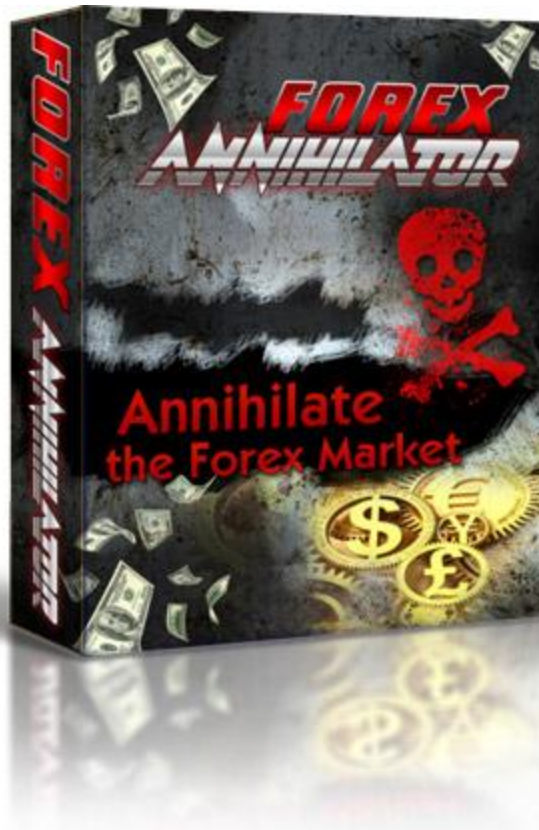


# The Forex Annihilator Advanced Strategy Manual



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FINAL THOUGHT

# DISCLAIMER

The information provided in this eBook are based upon past market results. Because the market is constantly changing, the method presented in this eBook may change, cease or expand with time. We hope that the skills and knowledge acquired from this manual will provide you with the ability to adapt to inevitable market evolution. However, we cannot be held responsible for changes that may affect the results of this method.

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## **MY TRADING STRATEGY 2 DAY TRADING SYSTEM**

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# CHAPTER 1

## INTRODUCTION TO THE FOREX MARKET

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"Give a man a fish and he will eat for the day. Teach a man to fish and he will eat for a lifetime."

Chinese Proverb

# 1.1 FOREX BASICS

## ***What is FOREX?***

The (FX) Foreign Exchange market is the world largest financial market, with a volume of above \$4 trillion a day. Forex trading consists of buying of one currency and simultaneous selling of other. The volume and liquidity provided by the Forex market surpasses aggregated trading volume of all worlds' stock markets including \$25 billion a day volume that New York Stock Exchange trades, this manifest how enormous the Foreign Exchange really is.

## ***What is traded on the Foreign Exchange market?***

Forex trading consists simultaneous buying of one currency and the selling of other. In Forex trading traders open an account with a FX broker or dealer which facilitates the buying and selling of Currencies, and they traded in pairs; for instance the Euro and the US dollar (EUR/USD) or the Great Britain Pound and the US Dollar (GBP/USD).

Assume that buy of a currency as purchasing a share in that respective country. For instance, when we buy Great Britain Pound we are in effect purchasing a share in the Britain economy. The value of currency is an undeviating reflection of what the market believes about the present and upcoming health of the economy.

## ***Which Currencies Are Traded?***

Some of the most admired currencies which are of mainly developed economies are listed below with their symbols:

<b>Symbol</b>	<b>Country</b>	<b>Currency</b>	<b>Nickname</b>
USD	United States	Dollar	Buck
EUR	Euro members	Euro	Fiber
JPY	Japan	Yen	Yen
GBP	Great Britain	Pound	Cable
CHF	Switzerland	Franc	Swissy
CAD	Canada	Dollar	Loonie
AUD	Australia	Dollar	Aussie
NZD	New Zealand	Dollar	Kiwi

### ***When Can Currencies Be Traded?***

The spot FX market is truly dissimilar from all the financial markets around the globe. Different financial centre, banks, individuals and institutions exchange currencies 24 hours a day excluding slight gaps on the weekends.

<b>Time Zone</b>	<b>New York</b>	<b>GMT</b>
Tokyo Open	7:00 pm	0:00
Tokyo Close	4:00 am	9:00
London Open	3:00 am	8:00
London Close	12:00 pm	17:00
New York Open	8:00 am	13:00
New York Close	5:00 pm	22:00

## 1.2 THE STRUCTURE OF FOREX MARKET

### *Exchange Rates*

Generally, exchange rate of currencies are determined by the health of that's country's economy in association to the other countries' economies.

FX Spot market does not have a physical location neither a central exchange. It is considered an Over The Counter (OTC) or Interbank market, because the trades are executed electronically, within a network of banks, constantly over a 24-hour period which is not the case in other financial markets including the New York Stock Exchange.

Numerous firms enable traders like us 'retail trader' to trade Forex market. The pre-requisites of Forex trading are trivial and only require a computer, a high-speed Internet connection, and the information contained within this eBook.

### *The Forex market (OTC)*

In the OTC market orders are cleared or processed on a central exchange but are routed between different participant who they want to trade with depending on the attractiveness of quotes, trading conditions and reputation of the trading counterpart.

The United States dollar is the most actively traded currency, with a share of 89% of all transactions. Whereas, Euro is the second most actively traded currency at around 37% and Japanese Yen at 20%.

### *Why Trade Foreign Currencies?*

There are numerous benefits and advantages of trading Forex. Follow are just a list of few pros of trading Forex and are paramount reason why so many people are choosing this market.

**No commissions.** There are no fees included with trades made on Forex exchange including any of the following clearing fees, exchange fees, government fees, and brokerage fees. However Brokers are remunerated for their services through bid-ask spread which we will discuss later.

**No middlemen.** Spot Forex trading is an OTC market which eliminates the need for middlemen and allows you to trade directly with the market responsible for the pricing on a particular currency pair.

**No fixed lot size.** Spot Forex offers very flexible contract or lots size. You can determine your own contract size and can start trading with a minimum of \$250 and in some cases with even less.

**Low transaction costs.** The transaction cost which is the bid/ask spread is trivial and is typically under 0.1 percent. Larger dealer offers even more attractive transaction cost. However the spread vary from currency pairs, brokers and market conditions.

**A 24-hour market.** Forex market is open 24 hours with different financial centre, banks, individuals and institutions exchanging currencies 24 hours a day excluding slight gaps on the weekends. Forex enables you to choose when you want to trade, either in morning, noon or night.

**No one can corner the market.** Unlike stock exchange and other financial market foreign exchange market has great volume with innumerous participants and there is no single entity including the center banks of developed countries that can control the market price for a elongated period.

**Leverage.** A small amount could be set as margin to control larger contract value. Leverage provides trader the ability to maximize their gains, and at the same time maintain risk capital to a lowest amount. For instance, a broker that offers 400:1 leverage means that \$50 margin funds would enable a trader's control full standard lot that is to buy or sell \$100,000 worth of currencies.

**High Liquidity.** Forex market is enormous and extremely liquid financial market. Your order is instantaneously executed with only a simple click of the mouse under normal market conditions.

**Free "Demo" Accounts, News, Charts, and Analysis.** Most online Forex brokers offer tons of value added services including 'demo' accounts to practice trading as well as real-time market new along with breaking Forex news and charting services.

**"Mini" and "Micro" Trading:** Online Forex brokers offer "mini" and "micro" lot sizes or trading accounts. Accounts can be opened instantly with a minimum deposit of \$200 or even less.

# CHAPTER 2

## THE LOGISTICS OF FOREX TRADING

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"Continuous effort, not strength or intelligence, is the key to unlocking our potential."  
Liane Cordes

## 2.1 HOW TO MAKE MONEY TRADING FOREX

Forex trading consists of simultaneously buying and selling of currencies. It is very simple process to place a trade in Forex market. The logistics and mechanics of Forex trading is very similar to other market (like stock market), therefore if you have prior experience in trading then this should be very simple for you to understand.

Forex trading revolves around exchange of one currency for another. So if you anticipate that the value of one currency might increase so you buy that currency and sell the other.

Following is the example how you make money trading EURO

Trader's Action	EUR	USD
You purchase 10,000 Euros at the EUR/USD exchange rate of 1.18	+10,000	-11,800*
Two weeks later, you exchange your 10,000 Euros back into US dollars at the exchange rate of 1.2500.	-10,000	+12,500**
You earn a <b>profit of \$700.</b>	0	<b>+700</b>

\*EUR \$10,000 x 1.18 = US \$11,800

\*\* EUR \$10,000 x 1.25 = US \$12,500

Ratio of a currency value against another is a simple ratio called exchange rate. For illustration, EUR/USD exchange rate specify how many EURO can purchase one U.S. Dollar. In other words, how many EURO will be required to buy one U.S. Dollar.

### How to Read an FX Quote

Currencies are quoted in pairs, such as EUR/USD, GBP/USD or JPY/USD. As stated earlier every foreign exchange transaction consists of simultaneously buying of one currency and selling of another that is why they are quoted in pairs. Following is an example of a foreign exchange rate and how transaction works for the Great Britain pound versus the United States Dollar:

**GBP/USD = 1.7500**

The first currency stated in known as the base currency (in this example it is GBP for Great British Pound) whereas the one on the right is called the counter or quote currency. (in this example it is USD for United States Dollar).

The exchange rate denotes how many in terms of units of the quote currency should be paid to purchase one unit of the base currency. For this example and the rate shown you would have to pay exactly 1.7500 United States Dollar to buy 1 GBP.

Where as in case of selling the exchange rate denote how many in terms of unit of the quote currency you will get for selling out the base currency. So in this example if you sell 1 GBP you will get 1.7500 USD.

As it name implies the base currency is the “Basis” of the transaction buy or sell. This simply means that you buy the base currency and concurrently sell the quote currency.

If you anticipate that the base currencies will strength against the counter currency you will open a buy trade. In opposite manner you will place a sell trade if you believe that the base currency will weaken against the quote currency.

## 2.2 HOW P/L CALCULATED

This topic will cover trivial mathematics to help you calculate profits and losses. You will also learn what is pip and lots.

### **What is a Pip?**

Pip is the most common unit and the smallest possible increment in the value of currency pair. If the value of EUR/USD changes from 1.2250 to 1.2251, this means a 1 pip appreciation in the value of EUR/USD. The last decimal place of a quotation is called pip. It also helps to indentify your profits or loss.

Each currency has its own value, which makes it is mandatory to compute the value of a pip for that particular currency. In currencies pairs where the USD (United States Dollar) is the base currency (or quoted first) the calculation would be as follows.

Let's assume USD/JPY current rate is at 119.80 (note USD/JPY currency pair only have two decimal places, whereas most of the other pairs have four decimal places)

In the case of USD/JPY, 1 pip would represent 00.01

Therefore,

### **USD/JPY:**

119.80

.01 divided by exchange rate = pip value

$.01 / 119.80 = 0.0000834$

This looks like a very long number but later we will discuss lot size.

### **USD/CHF:**

1.5250

.0001 divided by exchange rate = pip value

$.0001 / 1.5250 = 0.0000655$

### **USD/CAD:**

1.4890

.0001 divided by exchange rate = pip value

$.0001 / 1.4890 = 0.00006715$

In the case where the US Dollar is not quoted first and we want to get the US Dollar value, we have to add one more step.

### **EUR/USD:**

1.2200

.0001 divided by exchange rate = pip value

so

$.0001 / 1.2200 = \text{EUR } 0.00008196$

but we need to get back to US dollars so we add another calculation which is

EUR x Exchange rate

So

$0.00008196 \times 1.2200 = 0.00009999$

When rounded up it would be 0.0001

### **GBP/USD:**

1.7975

.0001 divided by exchange rate = pip value

So

$.0001 / 1.7975 = \text{GBP } 0.0000556$

But we need to get back to US dollars so we add another calculation which is

GBP x Exchange rate

So

$0.0000556 \times 1.7975 = 0.0000998$

When rounded up it would be 0.0001

You might be bit overwhelmed but this is put to only explain how to calculate pip value. Almost all brokers will do all this tedious calculation automatically. However it is good to know how it works.

In the next section, we will discuss how these seemingly insignificant amounts can add up.

### ***What is Lot?***

Spot Forex transaction is in lots. Lots are the number of unit of base currency that you buy or sell. The standard lot size is 100,000; the mini lot size is 10,000 whereas micro lot size is 1,000. As previously explained the smallest increment of that currency that could be measure is known as Pip. Forex trader trade large amounts of any picky currency so that the smallest increment could produce significant profit or loss.

Let's suppose we will be trading standard 100,000 lot size. We will now recalculate some of the above example to check how it influences the pip value.

USD/JPY at an exchange rate of 119.90  
(.01 / 119.80) x \$100,000 = \$8.34 per pip

USD/CHF at an exchange rate of 1.4555  
(.0001 / 1.4555) x \$100,000 = \$6.87 per pip

In cases where the United States Dollar is not base currency (quoted first), the formula will be is slightly different.

EUR/USD at an exchange rate of 1.1930  
(.0001 / 1.1930) X EUR 100,000 = EUR 8.38 x 1.1930 = \$9.99734 rounded up will be \$10 per pip

GBP/USD at an exchange rate or 1.8040  
(.0001 / 1.8040) x GBP 100,000 = 5.54 x 1.8040 = 9.99416 rounded up will be \$10 per pip.

### ***How to calculate Profit And Losses?***

Let take an example in which we buy United States Dollar (USD) and Sell Swiss Francs (CHF).

The rate of the pair will quoted like 1.4525 / 1.4530. As we will be buying United States dollar we will be working on the 1.4530 which in fact is the rate at which other traders are prepared to sell.

Let say, you buy 1 standard of 100,000 lot size at 1.4530.

After some time the price moves from 1.4530 to 1.4550 and then you decide to close the trade.

Therefore the new quote for the USD/CHF will be 1.4550 / 1.455. As now you are closing the trade which means you will now sell in order to close the trade therefore you will take the second 1.4550 price. Which is the price other traders are prepared to buy at.

The difference between 1.4530 and 1.4550 is .0020 or 20 pips.

Using the formula from before, we have (.0001/1.4550) x \$100,000 = \$6.87 per pip x 20 pips = \$137.40

Note, when you place a trade you are subject to spread which is the bid / offer price.

You will open a buy trade based on offer price and when you place sell trade it would be based on bid price.

To summarize when you buy to enter a trade you pay the spread but not when you exit the trade. Same is true with sell, when you sell to enter a trade you pay the spread but not when the sell trade is closed.

### ***What is leverage?***

If you are not familiar with leverage you might be wondering how small investor can contribute such large amounts of money as stated in lot sizes. Assume your broker as a bank who gives you, \$100,000 to buy and sell currencies and requires only a good faith deposit (margin) of \$1,000. This is how leverage works it let you control large contract sizes with small good faith deposit (margin) to amplify your profits.

The amount of leverage provided varies from brokers to brokers.

Once you have funded your account to trade the broker will let you know how much they require per contract traded.

For instance every 1,000 that you put in margin allow you to trade 1 standard lot of 100,000.

As previously stated the leverage which directly affects the minimum security (margin) vary from broker to broker. So a broker that requires 1% margin means that for every \$100,000 traded the broker will put \$1,000 as a security deposit (margin) on the position.

### ***What is margin Call?***

If in case your account equity drops below margin requirement (usable margin) due to loss on open positions your broker will close open positions. This will help prevent your account going into negative balance.

### ***Example #1***

Let's assume you open an online Forex trading with a deposit of \$2,000. You place a trade of 1 standard lot size on EUR/USD, which on this instance requires a \$1,000 in margin. Since you started trading with \$2,000 and \$1,000 was kept aside as a margin requirement for the open trade. Then the remaining usable margin will be \$1,000, this means any losses will be deducted from your usable margin. If your losses exceed your usable margin which in this case is \$1,000 you will automatically get a margin call and all open positions will be closed.

## 2.3 ORDERS TYPE

In simple terms the order type refers how trade will be entered or exited. In this topic we will discuss what different orders types that can be placed are. Some of the broker might not allow additional order type other than the basic buy or sell.

### ***Order Types***

#### ***Basic Order Types***

Following is a list of basic order types which includes market order, limit order and stop-loss order.

#### ***Market order***

A market order is an order type which allows placing buy or sell trade at the present market price. For instance, if EUR/USD is presently trading at 1.2200 and you want to place a buy trade at this price then you will click the buy button on your trading platform to immediately implement a buy trade at that exact price.

#### ***Limit order***

To place limit order you need to set price and duration if the currency price reaches your specified price with the duration then a new buy or sell trade will be placed.

#### ***Stop-loss order***

The stop loss order is a limit order which is specified to an open trade. The purpose of stop loss order is to close a trade is the price goes against you at certain level. Stop loss order is extremely important to limit your risk.

#### ***Additional Order Types***

##### **GTC (Good 'til canceled)**

Once a GTC order is placed it will remain active unless you make a decision to cancel it. The broker will not have privilege to cancel it anytime. Therefore you should remember and monitor the GTC order that you have scheduled.

##### **GFD (Good for the day)**

A GFD order stay active until the end of the current trading day.

##### **OCO (Order cancels other)**

OCO order consists of two interlinked order with price and duration placed above or below the prevailing market price. If one of the orders is carried out then the other order is canceled.

## 2.4 FOREX LINGO

### ***Major and Minor Currencies***

The most highly traded currencies which are G7 currencies and Swiss Francs are called major currencies. USD, EUR, JPY, GBP, CHF, CAD, NZD and AUD are list of major currencies.

All Currencies excluding stated above are referred to as minor currencies.

### ***Base Currency***

The first currency in any currency pair is called the base currency. It denotes the value base currency measured against quote currency (second currency in the pair). For example, if GBP/USD = 1.7500. Then the first currency stated in known as the base currency (in this example it is GBP for Great British Pound) whereas the one on the right is called the counter or quote currency. (In this example it is USD for United States Dollar).

The exchange rate denotes how many in terms of units of the quote currency should be paid to purchase one unit of the base currency. For this example and the rate shown you would have to pay exactly 1.7500 United Stated Dollar to buy 1 GBP.

### ***Quote Currency***

The second currency in any currency pair is called quote currency. It may also be suitable to call it the pip currency as any profit or loss is articulated in this currency.

### ***Pip***

Pip is the most common unit and the smallest possible increment in the value of currency pair. If the value of EUR/USD changes from 1.2250 to 1.2251, this means a 1 pip appreciation in the value of EUR/USD. The last decimal place of a quotation is called pip. It also helps to indentify your profits or loss.

### ***Bid Price***

The bid price is the price at which you open a sell trade (sell the base currency) or in other words market makers are prepared to buy at bid price.

### ***Ask Price***

The ask price is the price at which you open buy trade (Buy the base currency) or in other words market maker are prepared to sell at ask price.

For instance, in the pair EUR/USD 1.2312/17, the **ask price** is 1.2317. This means you can buy one Euro for 1.2817 U.S. dollars. The ask price is also set to be the offer price.

### ***Bid/Ask Spread***

The difference between bid and ask price is called the spread. The broker is compensated for their services via spread.

### ***Quote Convention***

Exchange rates in the Forex market are expressed using the following format:

Base currency / Quote currency    Bid / Ask

### ***Transaction Cost***

The bid and ask spread is also referred as the transaction cost.

Following is the formula for calculating the transaction cost:

Transaction cost = Ask Price – Bid Price

### ***Cross Currency***

A cross currency pair is a pair in which neither base nor counter currency is USD. Such pairs portray irregular price actions since it is same as opening two USD trades. For instance, simultaneous buying of EUR/USD and selling GBP/USD is equivalent to buying EUR/GBP.

### ***Margin***

Whenever you open a new trade a certain percentage of account balance will be set aside, as the initial margin requirement. The margin can be considered as good faith deposit which is refunded when the trade is closed.

Margin requirement vary with leverage which differ from brokers to brokers. If a broker offers a 200:1 leverage this means that the margin requirement is only 0.5 %. Therefore, only \$500 will be set aside as a margin requirement in order to open \$100,000 standard lot.

### ***Leverage***

Leverage could be defined as the ability to control large dollar amounts with a relatively small amount of capital. Leverage provided varies from broker to broker ranging from 2:1 to 500:1.

Increased buying power due to leverage can increase your profits but leverage should be used carefully as the loss also magnifies using leverage.

### ***Margin Call***

If in case your account equity drops below margin requirement (usable margin) due to loss on open positions your broker will close open positions. This will help prevent your account going into negative balance.

# CHAPTER 3

## MAJOR CURRENCIES

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"Life unexamined, is not worth living."  
Democritus

## 3.1 UNITED STATES DOLLAR

United States is the world largest individual economy. It may not be false to say that the US dollar is the king of currencies. The price of major commodities is quoted in United States dollar. More than 60% of the world currency reserves held by central banks of different countries to back their liabilities are in USD. Over 80% of all the currency transactions that take place involve USD. Therefore traders pay utmost importance to current situation of United States Economy. The health of US economy not only has direct affect on the USD but also on the other currencies of the world.

United States dollar is the most actively traded currency pairs. According to BIS (Bank of International Settlements) currency pair' including USD accounts up to 67% of the daily turnover in the currency market.

Central Banks and governments of different countries hold USD as their primary reserve currency, hence USD accounts up to 63% of the world reserves currency. An important fact to note is many countries, especially countries in Asia (including China) maintain large reserves of the USD which they use to peg the value of their currencies against USD. The reason for doing so is to stabilize their currency and to lower the value of their currencies artificially in order to make their export items more competitive overseas.

In addition, many individuals, business and multinational corporations located overseas hold United States dollar for trade purposes and United States dollar is considered more stable than their home country's currency.

Oil, silver, gold and many other commodities are priced in USD, which makes it mandatory to have or exchange to USD first prior purchase of such products.

## 3.2 EURO

Euro is the second most actively traded currency and is the official currency of 16 member nations in the European Union (EU) which consists of total 27 member states. The states which have Euro as their official currency are: Austria, Belgium, Cyprus, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia, and Spain.

The euro is administrated and managed by European Central Bank (ECB) based in Frankfurt and the Euro System which is composed of central banks of Euro zone.

European Central Bank (ECB) works as an independent central Bank and sets monetary policy.

Euro facilitated lowering trade barriers, economic cooperation and integrating the economies of the major countries in Europe.

Another important factor for trader to understand is that each member state that has euro as their official currency are slickly bound to the monetary policy laid down by ECB. Therefore member states can not have extremely different interest rates and inflation. Moreover member states are required to maintain banded peg exchange rate and to allow their currency value fluctuation inside a narrow band.

European Monetary Union (EMU) nations are free to set their fiscal policy.

### 3.3 JAPANESE YEN

Japanese Yen (JPY) is the third most actively traded currency, after United States Dollar and Euro. Apart from this it is also widely used as a reserve currency after the USD, EUR and GBP. Japanese Yen has very low interest rate which makes it suitable for carry trades and borrowing.

Japan economy is the second world largest individual economy and just behind US. It is important to understand economy of Japan to grasp a clear fundament of the Yen. From fundamental standpoint Japanese economy is different from US economy, Japan have extremely few natural resources. After World War II Japan found another way to overtake the world this was not by military force but by economic development.

Japan heavily relies on imported natural resources including oil, gas and other commodities. This is an important factor to understand as Japan imports 100% of its oil from exporting countries thus an increase in the price of oil has direct impact on the value Japanese Yen.

Another important thing to understand is that Japan economy relies on exports of goods such as cars and electronics, as a result a string JPY means Japanese goods and services become more expensive and less attractive for overseas consumers, which might harm Japanese exports.

In order to avoid any harm to Japanese economy Bank Of Japan (BOJ) intervene the Forex market to keep away the Yen from raising.

## 3.4 GREAT BRITAIN POUND

Great Britain Pound (GBP) is the third largest reserve currency and fourth most actively traded currency. UK economy is mostly service based economy with grave importance on financial services. UK earns significant revenue from oil and natural gas exports.

United Kingdom is a member of the EU (European Union) but it has not adopted Euro as its currency therefore not tied with European Monetary Policy (EMU).

Bank of England (BoE) is the central bank of England. The two main functions of bank of England is monetary stability and financial stability.

Pound is very active in the crosses specially EUR/GBP as EU is UK's largest trading partner.

## 3.5 SWISS FRANC

Switzerland is one of the richest countries with world's most stable economy. Switzerland is considered a safe haven for investors and has renowned banking secrecy. It has a service based economy, with low unemployment rate and budget deficit. Swiss practices including economic policies mainly conform to EU standards.

As Switzerland is considered safe haven for investors, money flows into Switzerland at the time of geo-political uncertainty.

It is evident from the chart shown below that Swiss Franc (CHF) strengthens against USD due to its safe haven status 10 days after the September 11<sup>th</sup> 2001 attacks. The pair USD/CHF fall 1251 pips which represent that USD depreciated in value against CHF.



An other example to manifest Swiss Franc safe haven status was at the time of US Invasion of Iraq. Again the Swiss Franc strengthen against USD and the pair USD/CHF fall 1200+ pips in the period of 2 month after the invasion.



The second most important factor to understand regarding Swiss Franc (CHF) is its strong correlation with the Euro. As evident from the graph below USD/CHF and EUR/USD pair have negative correlation. Which means when Euro strengthens CHF also appreciate in value.



As you have noticed in the chart shown above both pairs have 90% of strong negative correlation. This is due to the fact that Switzerland and European Union have strong economic ties.

## 3.6 COMMODITY CURRENCIES

### *Canadian Dollar*

Canada is the ninth largest economy and one of the wealthiest nations in the world. Canada has massive manufacturing sector and net exports of natural resources (especially oil and gold).

The economy of Canada relies heavily on exports which makes closely tied with the international economy especially United States. United States is the leading trading partner and exports flow from Canada to United States of more than 81%.

Canada is the 14<sup>th</sup> largest producer of oil, 5<sup>th</sup> largest producer of gold and chief exporter of oil to the prime consumer of oil (United States). Shift in prices of commodities has a direct affect on the exchange rate of CAD. This means all else being equal; a rise in the price of oil will result into a stronger CAD and weaker USD.

Exports of commodities are key factor to gauge Canadian economy, however in recent years Canadian service sectors has massively expanded. According to Wikipedia service sector accounts up to /3rds of the country's economic output. In other terms it means that a slowdown in United States economy can hurt Canadian Economy and its currency even if the commodities remain high.

## Australian Dollar

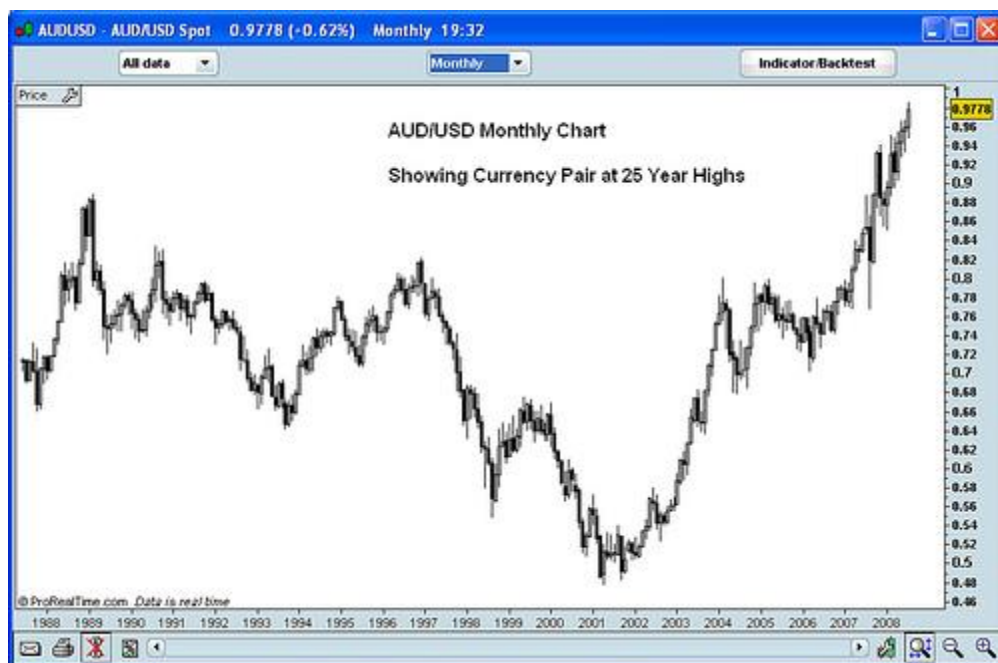
Australia has a prosperous economy and Australian Dollar is the sixth most actively traded currency.

Australia GDP consist of more than 68% of service sector, 4.7% from agriculture and mining which account for 65% of the country's exports. Australia is the 3<sup>rd</sup> largest exporter of gold and the value of its currency has high tendency to move with the price of commodities especially gold.

Australian economy and currency is similar to Canadian Dollar and economy in many ways, however unlike Canada, Australia's largest export market is Asia especially Japan and China.

This gives Australian dollar exposure to Asia. The AUD/USD monthly charts shows remained strong through the current crisis, and the pair has moved 25 Years high.

### AUD/USD Monthly:



## ***New Zealand Dollar***

New Zealand economy greatly depends on international trade, primarily Australia and follows market economy. Other major trade partners of New Zealand are United States, China and Japan. New Zealand population and thus domestic market is very small. It rely heavily on exports of good, therefore a slowdown in their imports economy can directly affect New Zealand Dollar.

Like other commodities exporting countries New Zealand has vast agricultural natural resources like Food, wood, wool, paper and dairy products. New Zealand Dollar (NZD) value is heavily influenced by the commodity prices and health of its importing economies. New Zealand is also strongly focused on tourism.

Until recent time the correlation between New Zealand Dollar and commodities prices have broken down somewhat.

The following chart show NZD/USD and AUD/USD correlation:



# CHAPTER 4

## TECHNICAL ANALYSIS

---

"The gem cannot be polished without friction, nor man perfected without trials."  
Confucius

## 4.1 INTRODUCTION

Study of price movement by analyzing historic price action usually in the form of charts is called technical analysis. Trader usually looks at price action usually in chart form and anticipate future price of the instrument.

A technical indicator is a form of chart plotted using mathematical formula which is derived from the price and/or the traded volume of the financial security. The graphs are usually above or below the instrument price and are helpful in forecasting future price movement of the instrument.

Technical indicators can be classified into two broad categories that is lagging and leading indicators.

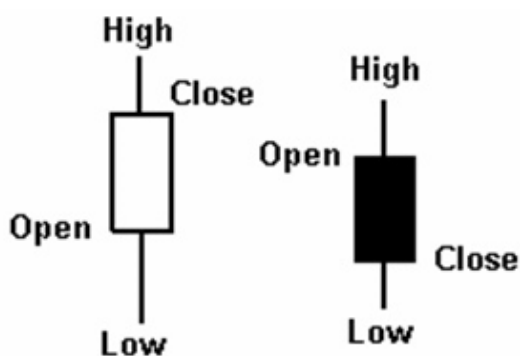
Leading indicators are calculated in an effort to anticipate the future movement of price. As leading indicators try to measure price movement from recent data, these indicator are prone to errant signals and it is usually recommended to use such indicators when there is no clear trend in the market.

Lagging indicator pay emphasis on where the market has been and therefore what will be the future price. Lagging indicator produce least errant signal but at a cost of delayed entry. Lagging indicators are believe to work better in trending markets.

## 4.2 JAPANESE CANDLESTICK

Candlestick charts plots price against time. Each candle represents Open, High, Low and Close (OHLC) of an instrument at a particular time. If the open price is less than the close price this means the for the particular time there was appreciation in the value and the candle is usually un-shaded or green.

If the close price is less than the open price this means for the particular time the value of the instrument is depreciated and the candle is usually represented by shade or red color.



## 4.3 SUPPORT AND RESISTANCE

### Support

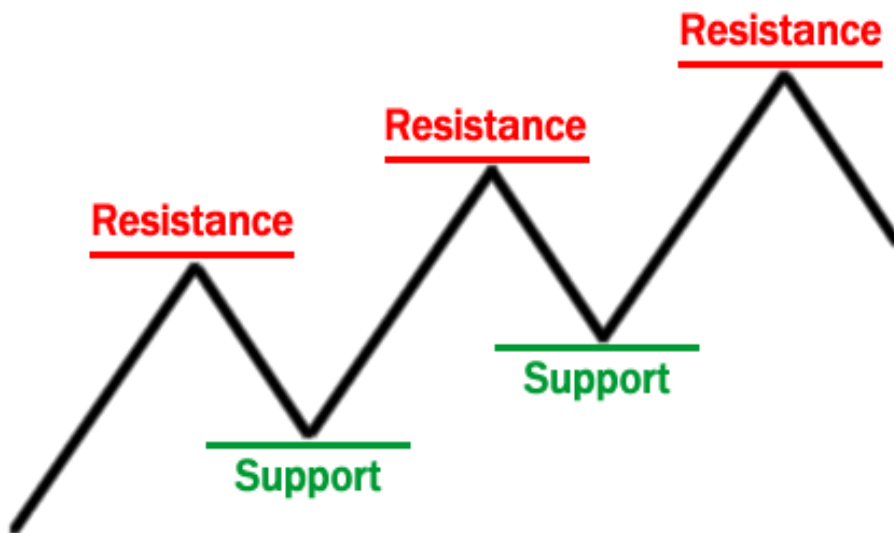
Support is the price level where the price action tends to find a support for falling further. At this level there is enough demand from buyers to keep the price from declining further.

### Resistance

Resistance is opposite of support. It is the price level of a particular instrument where there is not enough demand from the buyer to keep the price to surpass this level.

There are numerous ways to determine support and resistance. One basic way for identifying support and resistance (S&R) is by analyzing the chart to see where the price hit a particular level multiple times without breaking it and retraces back. If the price touches the support or resistance multiple times without breaking it, the more strong the support or resistance becomes.

A very basic strategy that traders use to trade using support and resistance is they buy at support and sell just before the resistance level.



## 4.4 TREND LINES

Trend lines are another most commonly used technical analysis.

In its basic form, traders draw a line below the price in an uptrend (when the prices are moving upward) in order to identify support areas (valleys).

Where as in downtrend (when prices are moving down) trader draw a line above the price to identify peaks (resistance areas).



When you are trying to look out for possible set ups, it is a good point to note that you must also identify the clear trend lines to filter away low probability set ups, even when the indicators are giving you the go-ahead. We know that there are many types of chart pattern formations, but I do not take much consideration into them. What I am looking out for are the ascending (upwards) and descending (downwards) trend lines.

## 4.5 CHANNELS

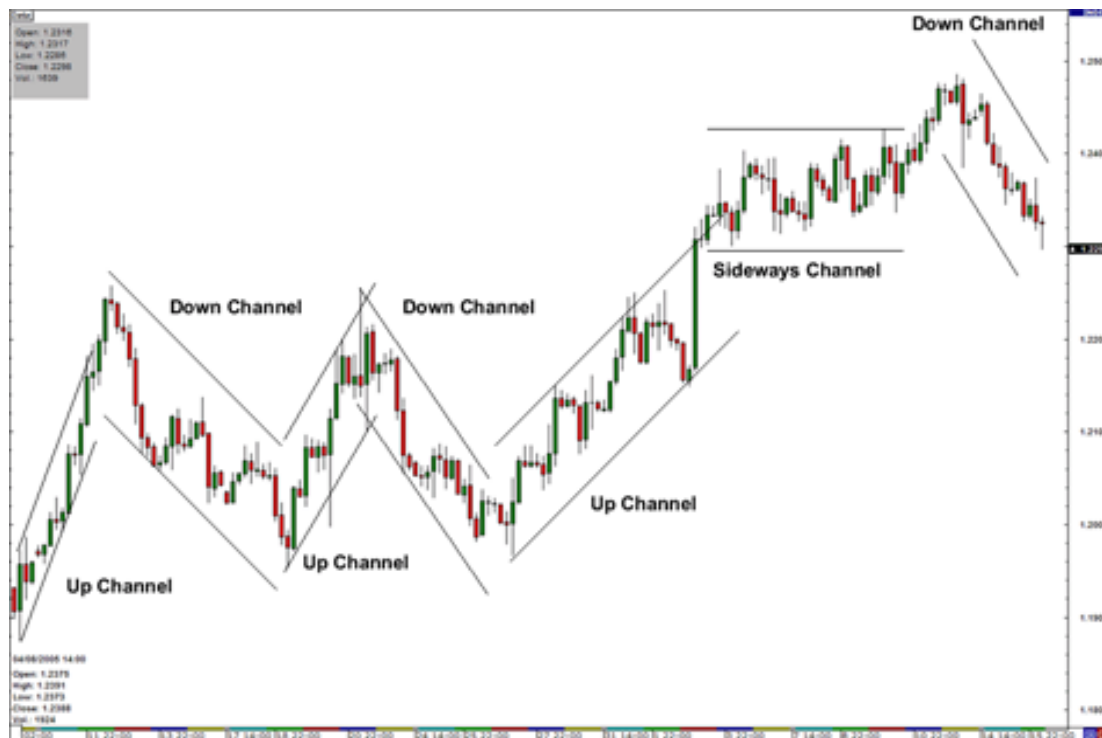
Channels are created by drawing a parallel line at the same angle of the trend line.

To create an ascending channel (when prices are moving upward), we have to simply draw a parallel line above the price at the same angle of the upward trend line.

To create a descending channel (when prices are moving downward), we have to simply draw a parallel line below the price at the same angle of the downward trend line.

The channel also shows the range at which the price fluctuate when in an uptrend or down trend.

Following chart shows how channel are created in an uptrend, downtrend and sideways (when there is no clear trend and the prices are range bounded).



## 4.6 COMMON CHART INDICATORS

### ***THE AVERAGE DIRECTIONAL INDEX (ADX)***

Developed by J. Welles Wilder, this indicator determines the strength of the current trend. I like to call 'strength' as 'momentum' as you can see from my technical analysis at [Me](#). The ADX is measured between the ranges of 0 to 100 and is the calculation is assisted by the two components of ADX; +DI and -DI.

- +DI - When the blue line is moving upwards, it is a signal that the uptrend momentum is getting stronger.
- DI - When the red line is moving upwards, it is a signal that the downtrend momentum is getting stronger.

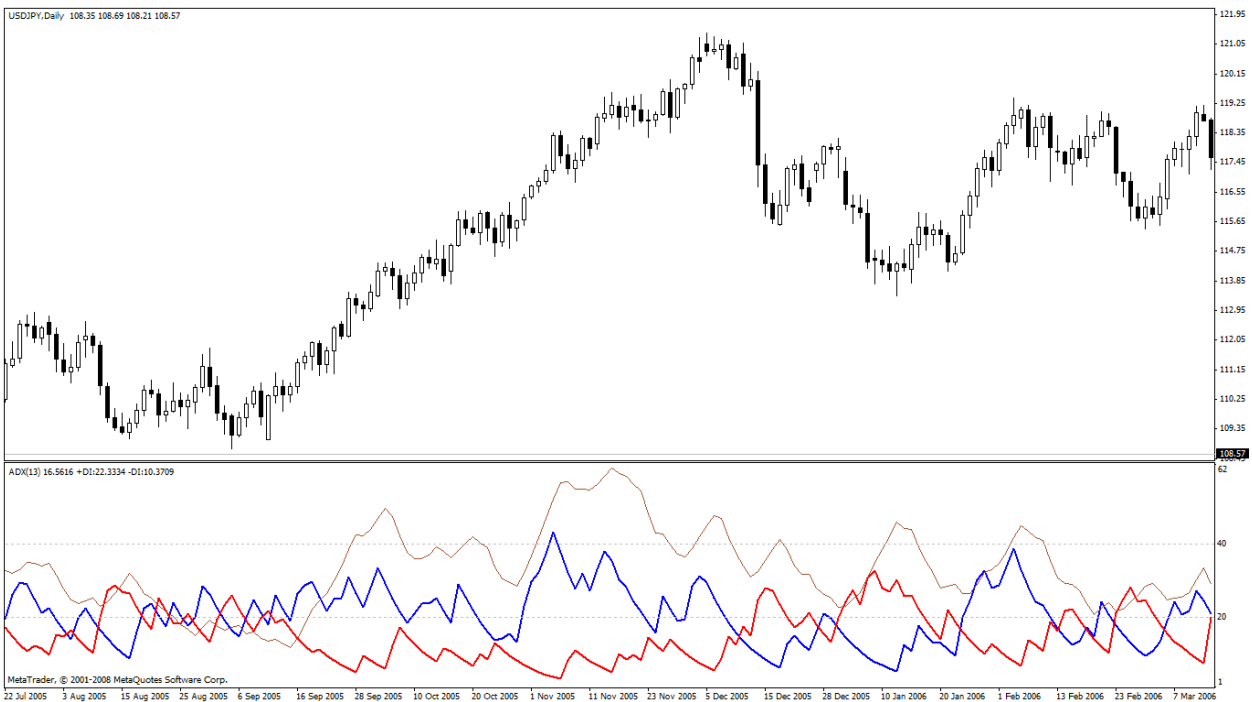


FIGURE 1

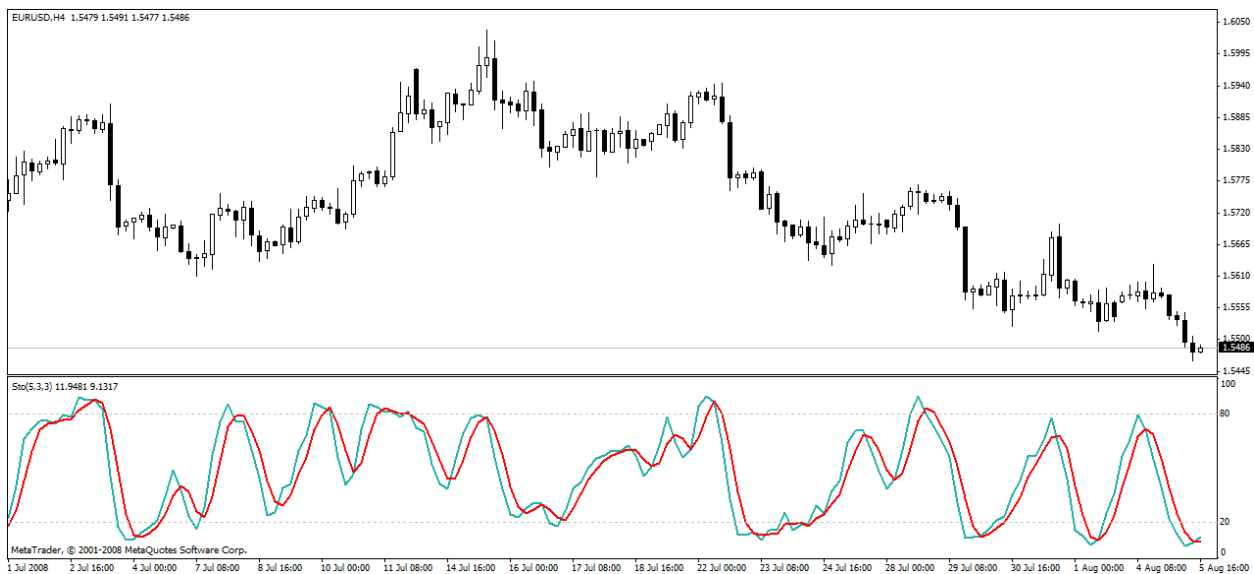
The usual practice is when ADX is below the 20 mark, it indicates that the market is non-trending with low volumes while a cross above the 20 mark signals the start of a possible trend; be it up or down trend. If the ADX is above the 40 mark but falling, it could possibly indicate a retracement from the trend. Please note that ADX itself is not entirely a trend indicator but rather, it calculates the momentum of the prevailing trend.

*How does ADX apply to trading system?*

*This system makes full use of the momentum shift and optimizes the point of entry at the turn of the tide. There is no way (yes I am assertive on this) of catching 100% of the reversal or trend continuation unless you are talking about stocks trading where if you are one of the major shareholders of a company, you can manipulate the price action. Nonetheless, using the method will help you to catch about 65-70% of the market momentum. If you have been checking on the daily technical analysis, you should know by now what I mean by "momentum is weak" and "momentum is strong" etc. The n period for ADX I set for this trading system is 13-period ADX.*

## STOCHASTIC OSCILLATOR

Developed by George C. Lane in the late 1950s, the stochastic oscillator is another momentum indicator that identifies the strength or weakness for a currency pair over a given time period. It is also measured between 0 and 100. When stochastic is below 20, it indicates that the market is considered 'oversold' while above signals the start of a possible bullish movement. If it is above the 80, the currency pair is considered 'overbought'. Between 20 and 80 the momentum is then considered returning to normalcy and healthy. Please note that stochastic might not give an accurate indication if the market is very trendy.



*How does stochastic oscillator apply to trading system?*

*I chose this oscillator because this indicator is a leading indicator, which means that before the price actually turns, Stochastic will reveal a possible shift before it happens. However, there is a downside of this early warning because it could be a fake out or just a minor retracement from the trend. So what is the usefulness of this oscillator with method? This indicator will act as the final confirmation on whether you should enter a trade. I did not change the setting for the stochastic oscillator which is the 5-3-3 setting.*

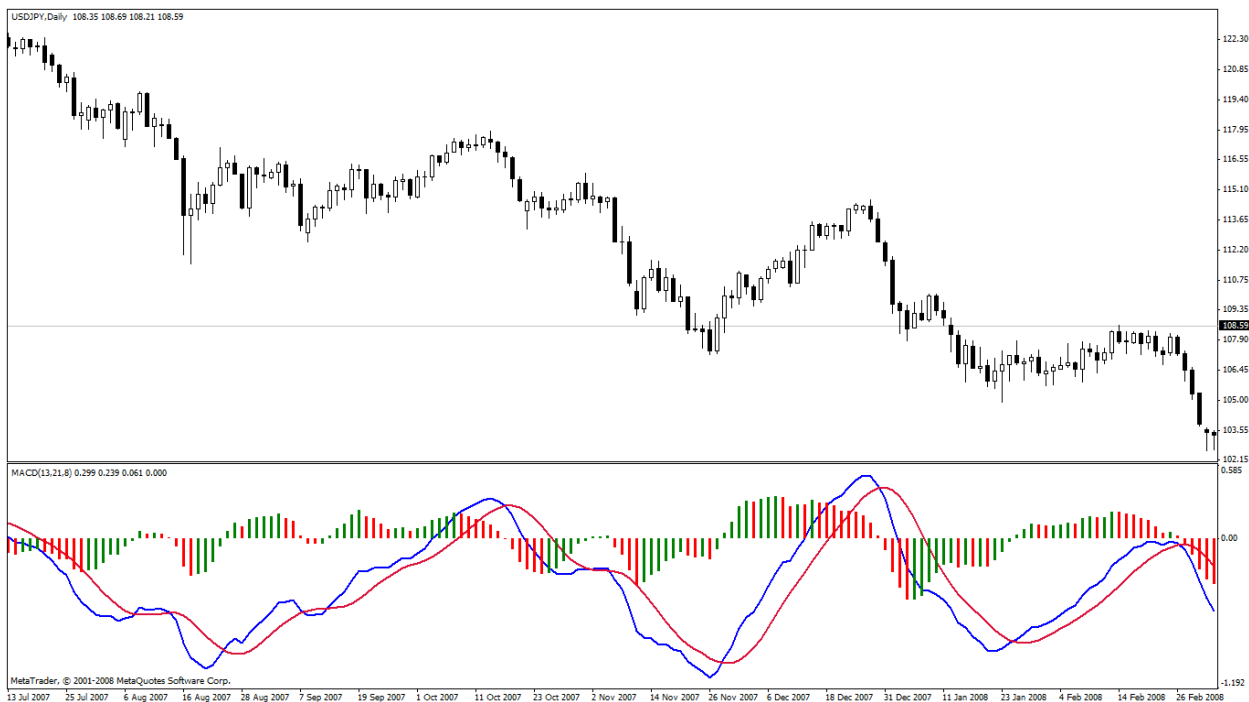
## ***MOVING AVERAGE CONVERGENCE DIVERGENCE (MACD)***

MACD, which is developed by Gerald Appel, is one of the most popular technical indicators to use with. The indicator makes use of moving averages to determine the direction of the price action. The indicator is easy to use because of the histogram display, which is derived from the moving average calculation. Best of all, MACD can both be used as an oscillator and a trend indicator. The original setting by Gerald Appel is 12-period and 26-period exponential moving averages.

*How does MACD histogram apply to this trading system?*

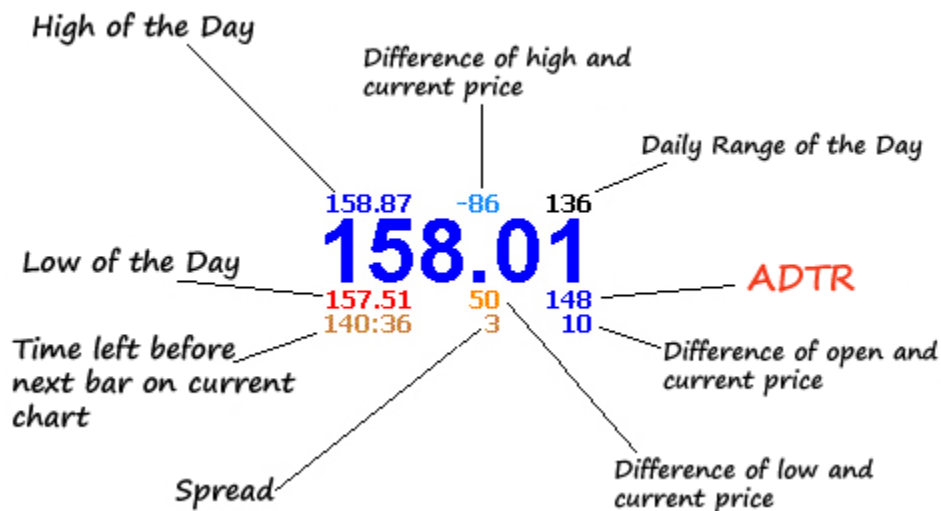
*I have always liked this indicator; it can be used as trend indication or as an oscillator during a ranging market. MACD will act as a double confirmation of the momentum shift together with ADX. However, the setting I used is a 13-period EMA with a 21-period EMA together with an 8-EMA as the signalMA.*

When the 12- period EMA is trading above the 26- period EMA, also denoted by the histogram moving above the centerline (some call it the waterline), it is considered that the momentum is bullish. A bearish MACD means that the 12- period EMA is below the 26- period EMA, denoted by the histogram under the centerline.



## **AVERAGE DAILY TRADING RANGE (ADTR)**

Average Daily Trading Range is the difference between the high and low prices in one trading day. Tracking this range can tell us whether the currency pair is volatile or not. We can also use the ADTR factor to plan our trade within a day. Let's take a look at the illustration below that you will get to see on the MetaTrader4 platform. It is not a must because some other proprietary platforms also provide the daily range information. If your trading platform does not include daily range, you might want to install a demo MT platform just to use it for charting purpose. I recommend FXDD as the calculation of daily range and weekly pivots are derived from their server time, which is GMT+3.

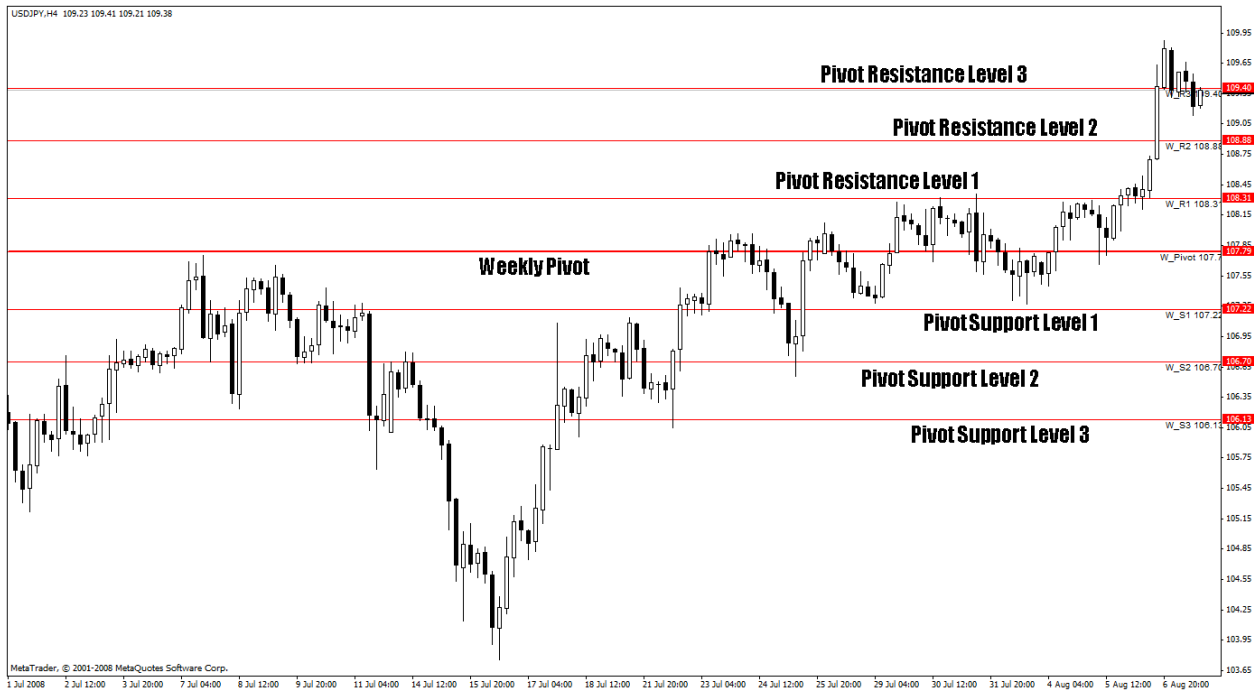


*How does ADTR apply to this trading system?*

*I want to share with you that the average daily trading range is just a guide to whether should you enter a trade if the price action is too near the ADTR. While it is not critical, however, it is a good thing to take note of it so that you can decide not to follow the rules of this system if you are not comfortable with the already formed ADTR late into the day. The method is not affected by the ADTR; it is just an additional precautionary measure for you to consider.*

## ***PIVOT POINTS***

I choose to use weekly pivots is because the calculation on the weekly is not so much difference even if your broker server time is different from the one I used for charting purpose. Using the weekly pivots, we can determine the sensitive areas for the week ahead to plan your trading strategies. I use it in additional to the Fibonacci support and resistance levels -which will be discussed later- to identify multiple confluences of these important lines.



**FIGURE 2**

The calculations of the pivot points are as follow:

Resistance Level 3	=	High + 2*(Pivot-Low)
Resistance Level 2	=	Pivot + (RLv1-SLv1)
Resistance Level 1	=	2 * Pivot - Low
Pivot Point	=	(High of the week + Close of the week + Low of the week) / 3
Support Level 1	=	2 * Pivot - High
Support Level 2	=	Pivot - (RLv1-SLv1)
Support Level 3	=	Low - 2*(High-Pivot)

## ***FIBONACCI RETRACEMENT AND EXTENSION LEVELS***

We have come to Fibonacci support and resistance levels, the last part of the technical tools required for My Trading Strategy 2. This topic is also the most important of all. Before I explain on how to make use of this wonderful numbers, let's take a look at how to calculate the Fibonacci numbers.

The Fibonacci series of numbers are 1 , 1 , 2 , 3 , 5 , 8 , 13 , 21 , 34 , 55 , 89 , 144 and so on to infinite. Now you must be thinking how to derive from 1 to 2, and 2 to 3 then to 5 etc. Did you make the correct guess that the next number is 8? If you don't know, here is the calculation; it is simply by adding two previous numbers and once you get the current number, the next number is then calculated by adding the previous and current number that you have just got. In this example, we got our next number 8 by adding 3 and 5 together. So what is the next number after 8? Right, it is 13 (5+8=13).

*How do pivots and Fibonacci support and resistance lines apply to this trading system?*

*When we decide to enter a trade, we need to see where are the sensitive levels that we need to take note of. The weekly pivots in my opinion are not that critical as compared to Fibonacci support and resistance. However, I want to use the pivots to identify potential confluence of these lines to avoid any additional risks. It proves to be useful*

In the Forex market, Fibonacci numbers are used in terms of percentage ratio. It is by using the numbers we derived above and then dividing those numbers to get the percentage ratio.

Let's look at how the percentage are calculated, for example 8, 13, 21, 34, 55, 89.

Now you use the above and divide them 1 by 1;

$$08/13 = \underline{0.61538461538461538461538461538462}$$

$$13/21 = \underline{0.61904761904761904761904761904762}$$

$$21/34 = \underline{0.61764705882352941176470588235294}$$

$$34/55 = \underline{0.618181818181818181818181818182}$$

$$55/89 = \underline{0.61797752808988764044943820224719}$$

As you can see from the above, all results are near the magical percentage of 61.8%. Now do you see why it is so sensitive and often mentioned in technical analysis and matters to most traders? It is

usually seen as a critical support or resistance line depending on what the trend is. Break of this level would usually see the price action move towards the 100% level to complete the retracement.

For the 38.2% ratio, it is calculated by dividing one number in the Fibonacci series by the number that is found two places to the right.

For example:

$$13/34 = \underline{0.38235294117647058823529411764706}.$$

The 23.6% ratio is calculated by dividing one number in the Fibonacci series by the number that is three places to the right. For example:

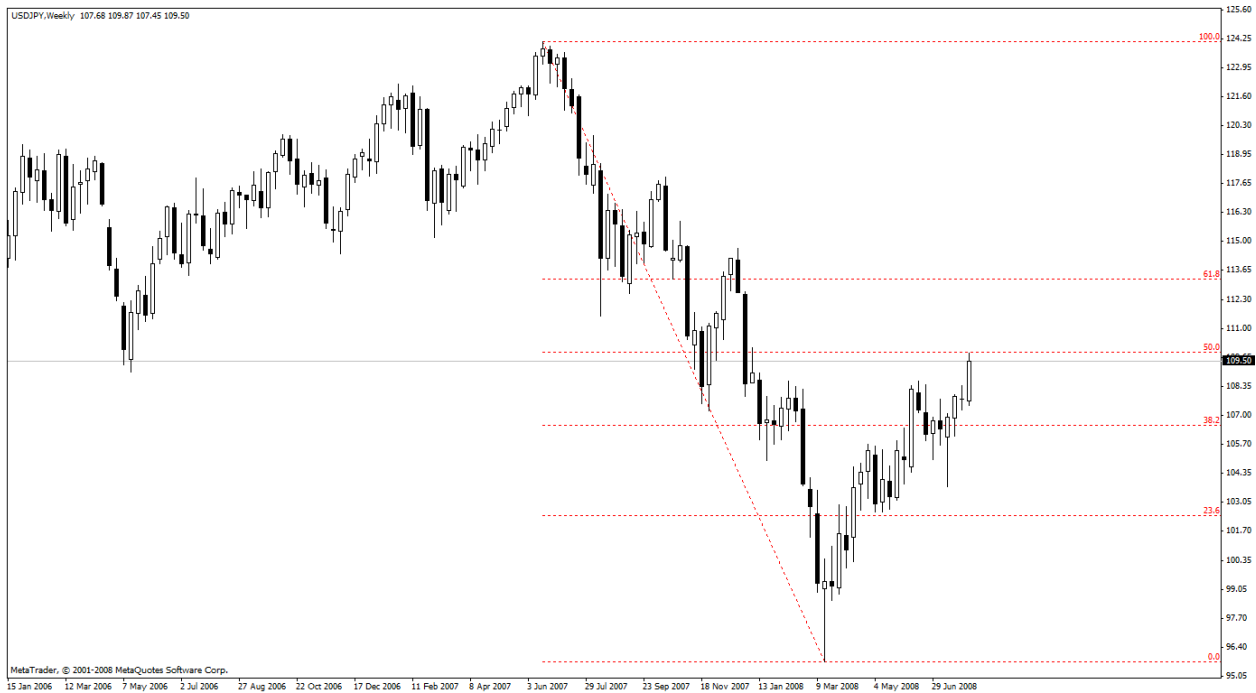
$$21/89 = \underline{0.23595505617977528089887640449438}.$$

*My views on 23.6%, 50% and 78.6% lines:*

*While the 23.6% is considered a Fibonacci level, the 50% and 78.6% are not but it seems the market react to them at times. For myself, I would really consider these lines only if the range is very wide as in calculated on a longer term basis. Then these levels could be seen as more sensitive than shorter time frames.*

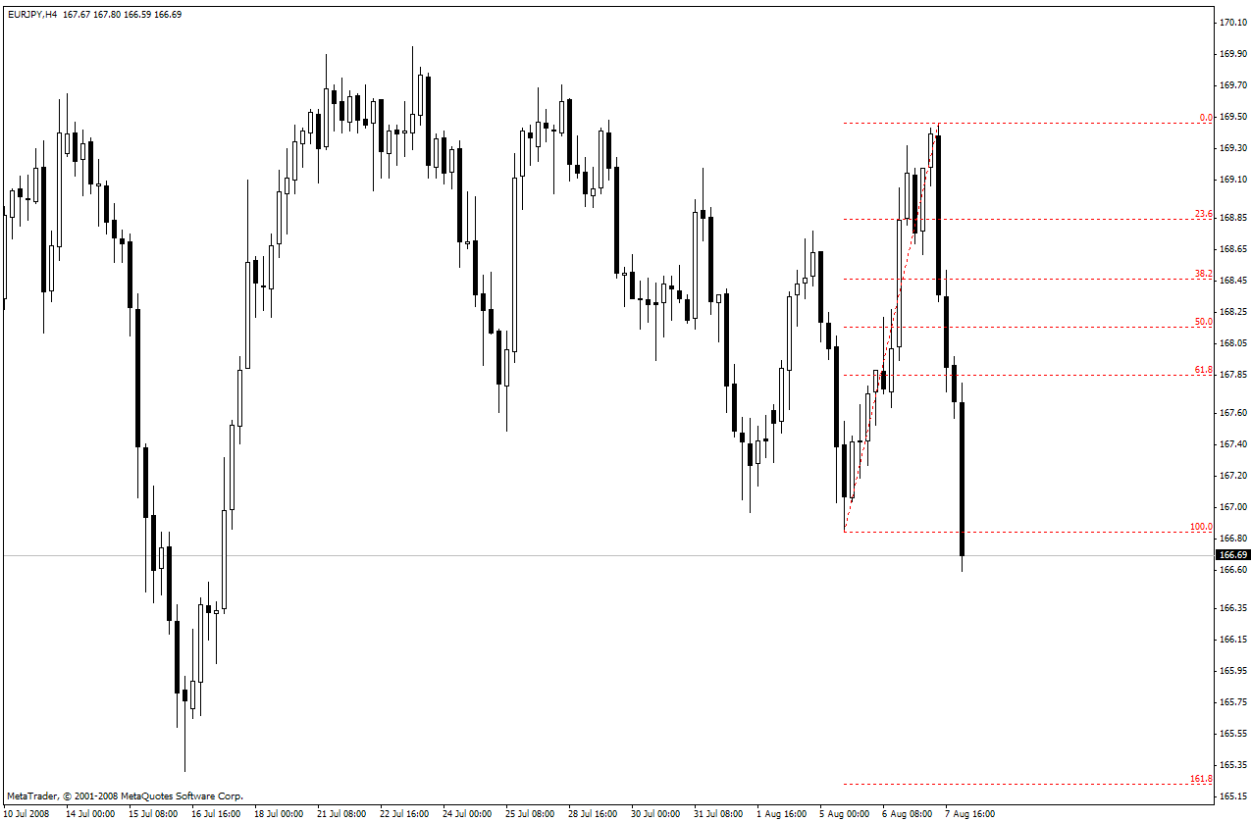
*How to determine if the Fibonacci support and resistance levels have been breached?*

*If you have drawn the lines using the daily chart, then only the daily completion of the candle will give a stronger signal that the level has been breached. If it is drawn on the weekly, you will have to wait till the completion of the weekly candle to confirm the break.*

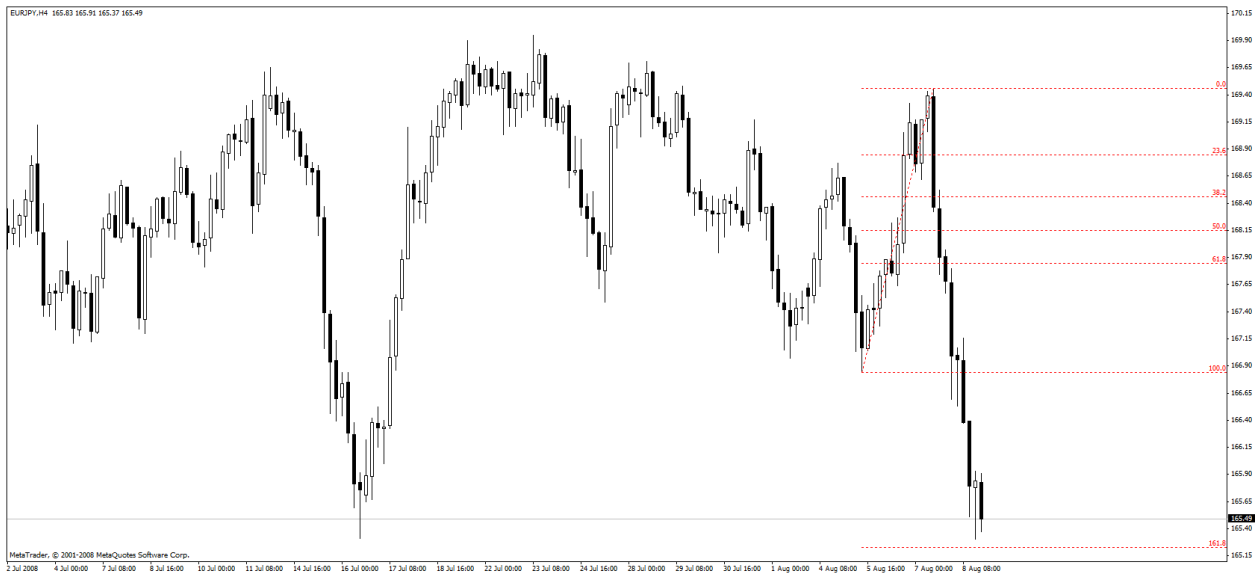


By looking at the last part of this section, you should know that I view it as very important information to share with. Let's go on to how to trade the Fibonacci levels in the Forex market (I will share with you how to combine this method with My Trading Strategy 2 later on).

As we know, Fibonacci levels are usually drawn on the daily, weekly and monthly charts. But do you know that you can also draw the retracement levels on the 4-hour chart if suitable scenario is given? Moreover, these minor Fibonacci levels are worth to consider when you determine your entries and exits. So how do we draw the lines on intraday charts? Let's take a look at this example below:



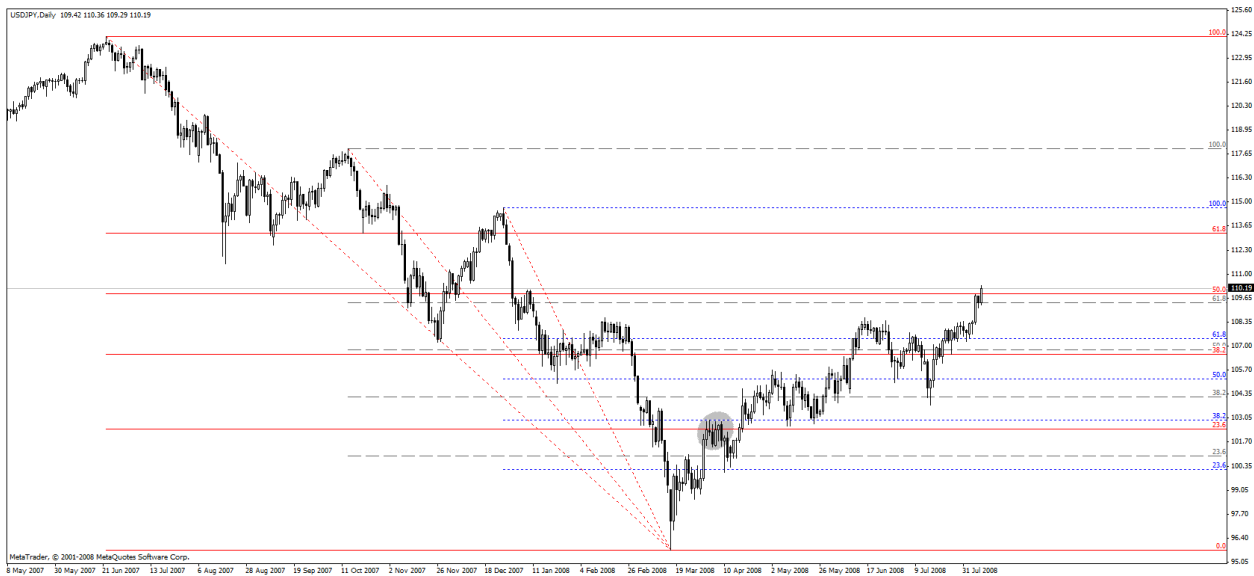
The above illustration is a 4-hour chart of Euro-Yen currency pair. As you can see, this Fibonacci retracement levels would not be able to draw if you switched to the daily chart. However, once you switch to the 1-hour or 4-hour chart, you can plot out the retracement lines and can be seen clearly on the chart. This chart was taken at time of GMT 0035H 8<sup>th</sup> August Friday while writing this amazing My Trading Strategy 2 method. As the momentum has turned to the downside on the 4-hour chart, on the 1-hour chart using the FB2 method, I have already gotten in the trade with a possible target of 165.31 (16 July Low) which is also near the 161.8% extension of this retracement. The break of the 61.8% together with the indicators in FB2 confirmed that the price action is going down and as it did, once it plunged through the 61.8% level, you can see that the sellers are keen to push the price lower towards the 100% retracement.



Several candles later, you can see that the price action has forced down its way lower towards the 161.8% Fibonacci extension level. This proves that Fibonacci lines are proven support and resistance levels to consider with. If you have not been studying on these important lines, now is your time to learn how to plot out those lines to know what is going on clearer.

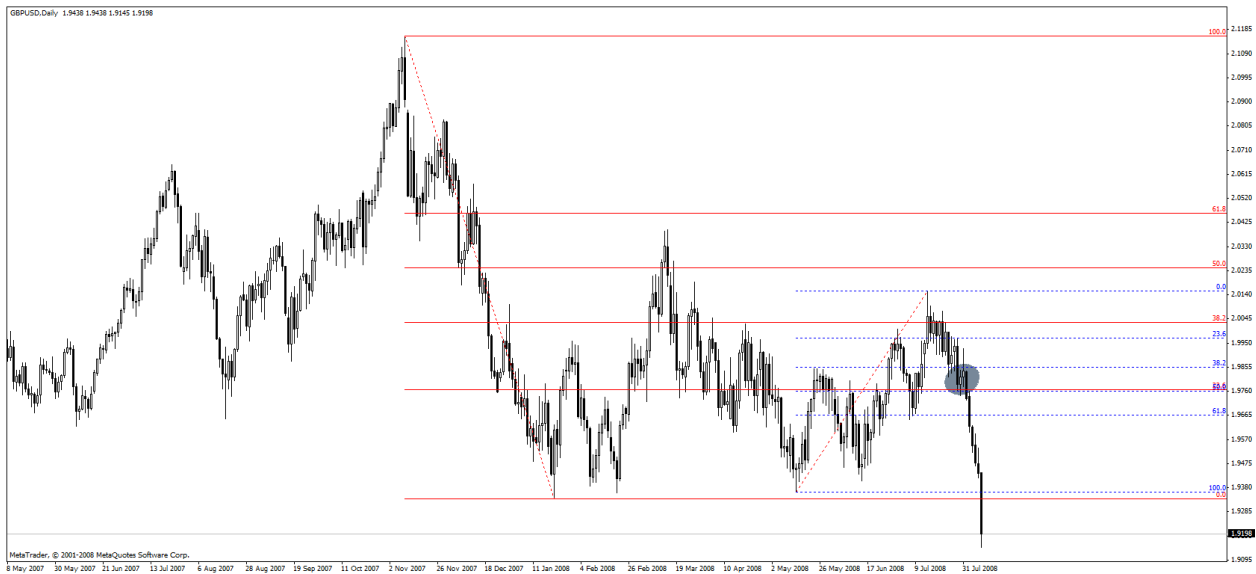
### ***FIBONACCI CONFLUENCE SUPPORT AND RESISTANCE LEVELS***

After we know what are the Fibonacci retracement and extension lines, the advanced stage is to know how to identify the confluences of these lines between smaller and bigger price movements.



As you can see from the above USDJPY chart, there are three possible Fibonacci retracements from the low of 95.73 on 17<sup>th</sup> March 2008. A bigger Fibonacci high (denoted by red lines) was drawn at 124.13 on 22<sup>nd</sup> June 2007; a lower high (denoted by grey dotted lines) was drawn on 117.93 on 15<sup>th</sup> October 2007 with the last one (denoted by blue dotted lines) drawn at 114.65 on 27<sup>th</sup> December 2007.

When the initial retracement started, there were confluences of 38.2% level (blue dotted line) and 23.6% level (red line) near the area between 102.44 and 102.96. The price action was unable to break above this range and retraced back downwards to the 100.00 zone. One of the significant reasons based on technical analysis was that the Fibonacci levels were on confluence mode, the lines of resistance were strongly in agreement at that time of price action. How did I confirm that? I concluded that with the combination of the indicators used by My Trading Strategy 2 system, which I will show you later in details.



Next example I am going to show you are the confluence of Fibonacci retracement lines of two opposite directions. On this GBPUSD chart (my favorite pair to trade), the red lines represent the bigger price retracement from the low of 1.9336 to 2.1160 (if you can remember the important lines without looking at the chart which what I am doing right now, you are in sync with the currency pair and know what is going on inside out) while the dotted blue lines represent the downward retracement from the high of 2.0156 to the low of 1.9363. From this backdated chart, the price movement actually was halted near the 23.6% (red line) and 50% (blue dotted line) confluence of retracements around 1.9758/66 area. This good support level was also confirmed by the My Trading Strategy 2 technical indicators.

## 4.7 MULTIPLE TIMEFRAME

Multiple timeframe analysis means incorporating more than one time frame into your trading strategy. This gives you edge and ensure you do not trade with trend against larger timeframe which might change trend of the shorter time frame.

Once you found entry signal in you preferred timeframe it is recommended to make a strategic decision to go long or short based on the direct of the trend of upper timeframe.

Follow chart shows how to incorporate multi timeframe analysis into your trading.

### 1 Hour



5 MIN



## DAILY



After analyzing these charts we see the pair is in a down trend in 5 minute and the hourly chart however when we move to daily chart it shows not only strong but also an extended uptrend. Therefore it is generally accepted by trader not to trade against large timeframe trend.

# CHAPTER 5

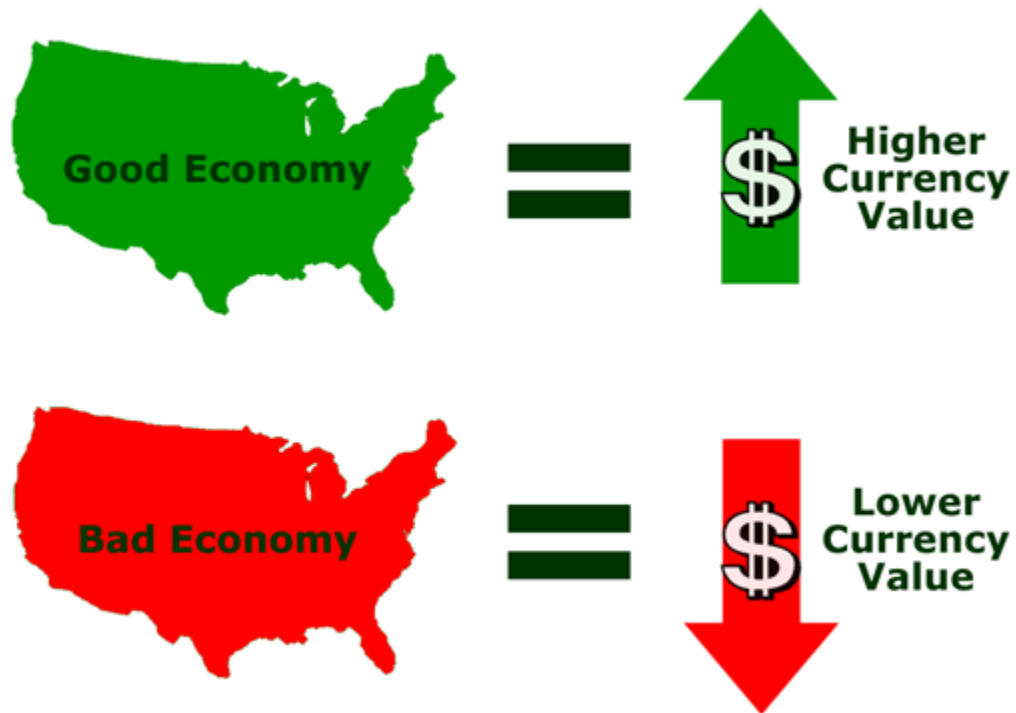
## FUNDAMENTAL ANALYSIS

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"He is foolish to blame the sea who is shipwrecked twice."  
Publilius Syrus

## 5.1 INTRODUCTION

Fundament analysis is a form of analysis in which general economy, and factors that affect supply and demand are analyzed to make trading decisions. In simple terms it means that we study the health of the economy and if the economy seems to be in good state then its currency value will appreciate. The chief reason for this is that other countries and investors will have more trust in that country and additional capital will flow to the economy.



A fundament analyst can focus on everything such as overall health of the economy, economic releases, IR (interest rates), earnings, and production.

## 5.2 OVERVIEW OF US ECONOMY

When studying fundamental analysis it is important to have at least a brief knowledge of how an economy especially United States economy works at USD is major currency.

According to Investopedia.com economy could be defined as the following:

**"The large set of inter-related economic production and consumption activities which aid in determining how scarce resources are allocated. The economy encompasses everything relating to the production and consumption of goods and services in an area."**

United States Economy is the largest economy in the world which is often referred as free market or capitalist economy. In a free market economy businesses are controlled by private sector (non government) including production and distribution of goods as well as services. Moreover in free market economy prices are set by supply and demand. Free market or capitalist economy is opposite if planned or socialist economies in which manufacturing and distributions of goods and services are done as well as prices are set by the government.

Practically United States economy is blended economy as the government does handle some of the tasks which cannot be passed to private sector such as military, road building, education and law enforcement.

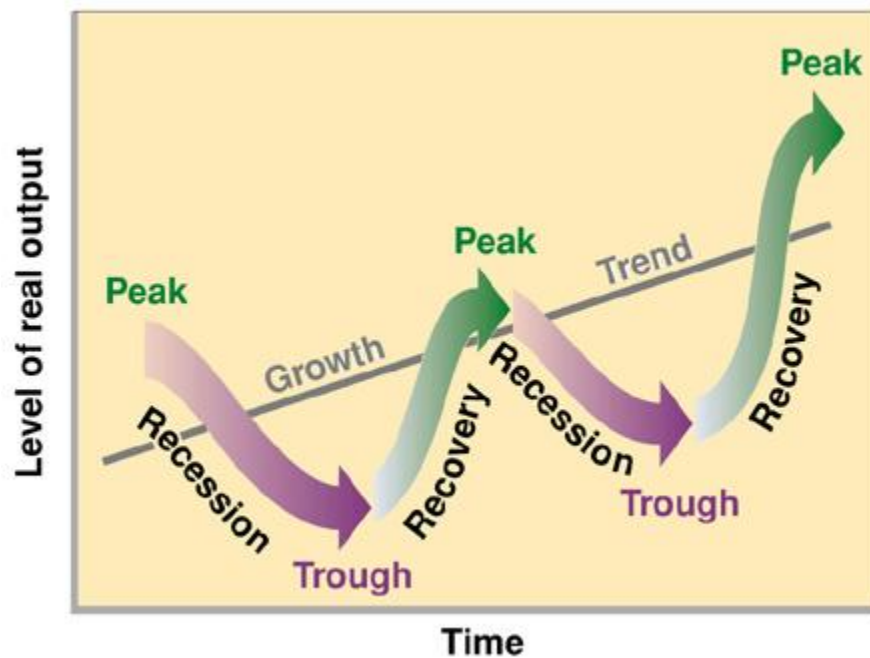
It is important to understand that people usually prefer capitalism and free market economies therefore any move toward capitalism will generally result into market rally whereas move away from capitalism will be sensed by market as anti business and markets generally sell off.

## 5.3 MONETARY POLICY AND FISCAL POLICY

### Fiscal Policy

Fiscal policy is any policy relating to government spending and taxation. Due to different reasons the economy under goes repeated growth and contraction which can be broken down as the following.

- 1) Contraction
- 2) Trough
- 3) Expansion
- 4) Peak



(image source: Wikipedia.org)

Fiscal policy is an effective tool at government disposal in regulating the business cycle. Government spending and taxation must be approved by both congress and the president.

## **Monetary Policy**

Monetary policy is the process by which Federal Reserve in case of United States or monetary authority, central bank, or government of a country controls the following:

- 1) Supply of money
- 2) Availability of money
- 3) Cost of borrowing money (Interest Rate)

These policies are set in order to achieve set of goals which are oriented towards stability and growth of the country's economy.

Interest rate and total supply of money have great impact on economy. Monetary policy is said to be contractionary if it reduces money supply or raises IR (Interest Rate). Whereas, expansionary policy is used to tackle unemployment, this is usually done by lowering the interest rate in inflation.

## 5.4 BALANCE OF PAYMENT

In long term stream of money from international trade, speculation and investment eventually decide the value of a country currency. When there is an increase in demand for export products of a country and/or investment opportunities look attractive to foreigners then all else being equal they currency should appreciate.

### **Trade Flows**

Flow of money in and out of a country due to global trade or commerce is called trade flows. In simple terms it means that money flow from the importing country to exporters' country for the goods and services being delivered.

When a state imports goods this add money of the importing country to the market and generate demand for the currency of the exporting nation. This is due to the fact that goods are usually purchased in the currency of the country where they are manufactured or produced, so the country importing the goods must exchange their currency.

### **Capital Flows**

Flow of capital (money) as a result of investment into and out of countries is called capital flow. As in previous topic we discussed flow of capital as a result of international trade however capital flow results due to money flow due to investments such as stock and bond market, real estate and cross boarder acquisitions and mergers.

### **Current Account**

The formula for calculating the current account for a country is as following

$$\begin{aligned}\text{Current account} &= \text{Balance of trade} \\ &+ \text{Net factor income from abroad} \\ &+ \text{Net unilateral transfers from abroad}\end{aligned}$$

When describing imports and exports you will often hear about current account surplus or a current account deficit. When a value of country exports are more than they are importing is known as current account surplus. Current account deficit is opposite of current account surplus. A country with current account deficit will generally have a weaker currency, this means that the country is importing more than it is exporting and the money flow out of the country.

## **Capital Account**

The general formula for calculating the capital account is as following:

$$\begin{aligned}\text{Capital account} &= \text{Change in foreign ownership of domestic assets} \\ &\quad - \text{Change of domestic ownership of foreign assets} \\ &= \text{Foreign direct investment} \\ &\quad + \text{Portfolio investment} \\ &\quad + \text{Other investment}\end{aligned}$$

Ownership of foreign or domestic assets refers to things such as real estate, foreign and domestic companies' investment and cross border mergers and acquisitions. Portfolio investment refers to investment in stocks and bonds. Whereas, other investments includes investment in loans and bank accounts.

As we discussed in our lesson on capital flows, when a market in a country is outperforming the markets in other areas of the world, money will flow into the country from foreigners seeking to participate in those out sized returns. These capital flows are reflected in the country's capital account. This is the case whether we are talking about a country's stock market, bond market, real estate market etc.

Countries with aggressive inflows or outflows of funds have straight influence on its currency. If other things are kept constant then a country with major inflows create demand for the currency resulting into the appreciation in the value of the currency.

## **Balance of Payment**

In simple terms balance of payment refers to sum of all the transaction by a country with rest of the world. By using balance of payment as an indicator Forex traders can achieve immense imminent into the potential future price action of a country's currency.

## 5.5 ECONOMIC RELEASES

It is important for a trader to understand major economic releases and their impact on trading. There are numerous economic releases that are published every day to cover each economic release will be out of the scope of the book however some basic economic are briefly touched below.

### **Gross Domestic Product**

GDP which is also referred as Gross domestic income (GDI) is a gauge of national income and output of any countries economy. For this reason trader and other market participants closely watch Gross Domestic Product Number (GDP).

High rate of growth is a good indicator for the economy but if markets anticipate that the growth is not sustainable without excess inflation, participant might reach negatively. You can read the analysis from different sources including Bloomberg.com and dailyfx.com are best services available free of cost.

### **Non Farm Payrolls**

Non Farm Payrolls (NFP), economic release is public each month on first Friday at 8:30. NFP is released by the Bureau of Labor Statistics in United States which is meant to show the number of jobs added or vanished in the economy over the period of one month. As the name implies NFP does not include jobs concerning to farming industry.

When business are hiring people this means they are optimist about the future health of the economy. This is expressed in form of NFP.

## 5.5 INTEREST RATES

Interest rate in currency trading is as important as current and future prospect factor that affect the long term earning and direction of stock.

Currencies are highly reactive to economic news that may affect the interest rates of a country.

If the central bank of a country rises the interest rate this makes debt instrument for that country more attractive. This means foreign investors are more likely to invest in the debt of that country as well as domestic investors are less likely to look foreign countries for investment. Therefore, all else being equal the demand for the debt of the country pull the value of its currency.

Conversely, when Interest rates decreases, there will be demand for the debt of the country due to lower earning for investors; usually this will devalue currency and other debt instrument.

# CHAPTER 6

## MONEY MANAGEMENT

---

"Believe it can be done. When you believe something can be done, really believe, your mind will find the ways to do it."

David Schwartz

## 6.1 INTRODUCTION

Money management is one of the most important aspects of trading. It is also the most overlooked part of almost all type of trading. Money management rules not only facilitate us in protecting our capital but also, make us gainful in a long term.

Trading without sensible money management rules is merely playing Russian roulette.

## 6.2 LEARN TO PROTECT CAPITAL FIRST

The primary goal of successful trading is the safeguarding of capital. In order to explain how difficult is to get out of losses there is an example shown below:

Let's assume a trader started with \$10,000 and go down by \$5,000. The percentage of capital he lost is 50%. Now in order to get out of his losses and to breakeven even he need to made 100% return on \$5,000. In other words he has to be twice as successful to cover his draw down.

### **Initial Stop Loss**

It is important to incorporate sensible risk management into trading. This can be achieved by setting stop loss which you can afford to lose on a trade without any substantial affect on the account equity. This greatly vary from strategy that one is trading and from traders to traders.

Dr Alexander Elder stated as following in his renowned book "Trading for a Living".

**"Many studies have shown that trading strategies and traders who risk more than 2% of their overall trading capital on any one trade are rarely successful over the long term. From what I have seen most traders risk way more than this on an individual trade basis, another large contributor to the high failure rate among traders."**

## 6.3 SETTING PROFIT EXPECTATION

In order to build robust money management plan, the key components involved is lucrative trading strategy and setting practical profit probability.

### **Risk to Reward Ratio**

Yet another way to add to your odds of profitability is to always trade with a higher risk to reward ratio. This means you are more likely to make 3 times more than what you are risking per trade. You can significantly increase your chances of ending up profitability if you have 3:1 reward/risk ratio in your trading strategy.

No of Trade	Loss	Win
1	\$1,000	
2		\$ 3, 000
3	\$1,000	
4		\$ 3, 000
5	\$1,000	
6		\$ 3, 000
7	\$1,000	
8		\$ 3, 000
9	\$1,000	
10		\$ 3, 000
Total	\$ 5, 000	\$ 15,000

In the example shown above your percentage of winning trades is only 50% but still you made a profit of \$10,000.

## 6.4 POSITION SIZING

Position sizing is the main topic for money management and vital component for successful trading. Position sizing strategy can be classified into two broad categories martingale and anti martingale.

Martingale is a strategy for position sizing which increases the trade size as the trade suffer draw down or after a losing trade. Anti-martingale strategy is opposite of martingale strategy, which increases position sizing after winning trade or when the trade moves in trader favor.

### **Fixed Position Sizing**

Many traders make the mistake of choosing an arbitrary number such as 1 standard lot per \$5,000 capital or so on when they take first step toward trading. Using fixed position sizing has many disadvantages it does not take into account the dollar value and volatility characteristics of the instrument being traded. Moreover fixed lot sizing does not allow a trader to trade large contract size on trades with high chances of winning and lower the trade size on lower probability of success.

For instance a financial instrument of 100 unit with \$20 value fluctuates 5% a day does not present the risk/reward for a second instrument of 100 unit with \$30 which fluctuate 1% a day.

### **% Risk Model**

The next level of sophistication in determining your position size is by using percentage risk method. In % risk based model contract size is determined by the risk on each trade in provisions of a percentage of your capital. As we looked in our previous topic that traders who risk more than 2% of their capital on any one trade are usually not successful overlong run.

For instance if a trader has \$100,000 in his trading capital and identify from his historic analysis of the strategy that 2% or \$2000 of his trading capital is an appropriate amount to risk per trade.

### **% Volatility Model**

Volatility based position sizing consider how much the price of a financial instrument fluctuates over a given period of time. ATR (Average True Range) is an indicator which shows the volatility of any financial instrument over a period of time. Value obtained from ATR can be used to determine your stop loss level in addition to the position size of the instrument you are trading.

For instance, a trader has \$100,000 in trading capital and he is look to buy EUR/USD which is at 1.3580. After pulling up a chart of EUR/USD currency pair and adding the ATR it shows the value of 0.0084. As you remember from our starting topic that 1 pip represent \$10 when trading standard lot. So taking this into consideration that volatility is dollar per contract for EUR/USD equals to  $\$10 \times 84$  which is \$840.

Therefore if the trader as risk appetite of 2% of his trading capital that he is willing to risk, then on volatility basis this equals to \$2000. This means under this model the trader can put approx. 2.3 standard lot.

# CHAPTER 7

## TRADING SYSTEM

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"The truth of the matter is that you always know the right thing to do. The hard part is doing it"

Norman Schwarzkopf

## 7.1 TRADING SYSTEM I: THE METHODOLOGY

What I have shown you earlier are the technical indicators and tools for My Trading Strategy 2. Now you must be thinking why I chose all these indicators? Frankly, it is more of a personal preference and the fact that these indicators are some of the popular indicators out there that caught my attention.

Basically, ADX has been known to act as a trend strength indicator together with MACD as well. The Stochastic acts as an attacker in the immediate market condition whereby it will tell us whether the momentum indicators are giving us the right signal to go in. Traditional charting analysis such as trend lines support and resistance also must be taken into consideration as well. Also, the Fibonacci retracement and extension levels are seen as the most important areas of support and resistance, with additional pivot lines as pre-empt levels.

My Trading Strategy 2 can be regarded as being a systematic or discretionary trading system depending on how you are going to use it. Of the earlier My Trading Strategy system, this second system supersedes and is considered a much more superior trading strategy. This is why I took a long time to document the whole complete method in this e-Book that you have purchased. I am glad that I did.

My Trading Strategy 2 is a trading system to trade the Forex market. The method is affectionately known as:

- *Momentum Assault* (requires multiple time frames analysis)

### **GUIDE ON HOW TO USE ME MARKET ANALYSIS**

In this section you will learn how to determine whether the momentum is strong, weak or neutral. The support and resistance levels I will update as and when is needed. However, if you are experienced enough, you can plot out the lines yourself although it takes a while to confirm these lines.

I have split to three levels of gauging the momentum. From top down, My Trading Strategy 2 started with the weekly, the daily and then the intra-day 4-hour time frame. The technical analysis will be done on FXDD Meta Trader platform with all the indicators inserted to get the full picture.

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### *Main Time Frames*

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- Long term = weekly
- Medium term = daily
- Short term = 4-hour

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### *Market Analysis - Forex Currency Outlook*

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The color-coded arrows highlight the immediate market momentum and overbought/oversold zones. The overbought and oversold zones are not meant to tell you that the market has reached its bottom or top, but rather, inform you that it is not advisable to enter at the direction of the movement if it is in the zone.

- Up arrows will indicate that the price action could be moving higher, usually signs of higher prices ahead.
- Down arrows usually indicate that lower movements ahead in future.

The colors represent the signal and its current situation of overbought/oversold condition:



Red arrow represents ascending trend with momentum in overbought zone.



Green arrow is the preferred level for opening a new position where the momentum is in healthy zone and not being overbought.



Blue arrow indicates that the ascending trend could be losing its steam as the momentum is moving against the trend. This arrow is not recommended to enter any new positions (existing positions should move your stops to protect your profits).

For example, a Green Down arrow indicates that momentum has recently turned negative from within overbought territory, suggesting lower prices are ahead.



Green arrow shows that momentum is moving in the direction of the arrow, but the signal is within an unconfirmed zone and is neither overbought nor oversold. This indicator is quite common and represents trend continuation or opening a new position.



Red arrow shows that momentum is currently in an oversold zone. Although the trend is progressing in the direction of the arrow, but consideration should be given to exiting positions in the direction of the trend. Therefore, it can be used as a signal to take profit. It is also not advisable to open a new position the market could quickly turn bad if it reverses from oversold zone. Additionally, red arrow should not be considered to open an opposite position because the market can stay in the oversold zone for a very long time if the trend is very strong.



Blue arrow could imply that existing trend could be ending soon and therefore serve as an early indicator to monitor a particular currency pair for a possible reversal in the near future.



*Thoughts on deciding the momentum factor:*

*What I have shown you are entirely based on technical analysis. However, at times to determine the momentum, you will have to look into what is going on with the economic releases and the immediate market momentum. When the GBPUSD technical outlook shows a bearish momentum, a piece of good news for the Dollar would inject further downside. The difficult part is when the data is a bad news, and you have to do your research further to confirm that the momentum should persist*



## 7.2 TRADING SYSTEM I: THE METHOD

I hope you are still with me, if not please take a break and close this file because what I am going to share with you now is the actual method that puts everything together of what I have mentioned.

Before I continue, I want to reiterate that this My Trading Strategy 2 trading system is one of the best systems I have personally developed and used since last year 2007. This system could give you potentially more than 500 pips (you decide the dollar value per pip) on a very good trendy market in a single month. There are many e-Books that sell all sorts of strategies, systems and setups whatever you may call them, but nothing comes close to My Trading Strategy 2 that I am going to share with you, at least in my opinion. When I say it is proprietary, it is the truth. No trader know about this system except for those who have purchased this FB2 manual including the person who is reading now which is YOU. I am as happy as you do that you have picked up this manual, willing to give it a try and rest assured that if you follow what I have shared with you, there is only one way to go in your trading account; which is pips, pips and more pips.

Alright, let's take a deep breath and proceed with the explanation of this My Trading Strategy 2 system.

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## Momentum Assault

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Momentum Assault is a method that requires analysis on two time frames. It is a top-down approach and trade with the primary trend. Below are the time frames you may consider.

Setup	1 <sup>st</sup> time frame	2 <sup>nd</sup> time frame
A	1-hour	4-hour
B	4-hour	Daily
C	Daily	Weekly

TABLE 1

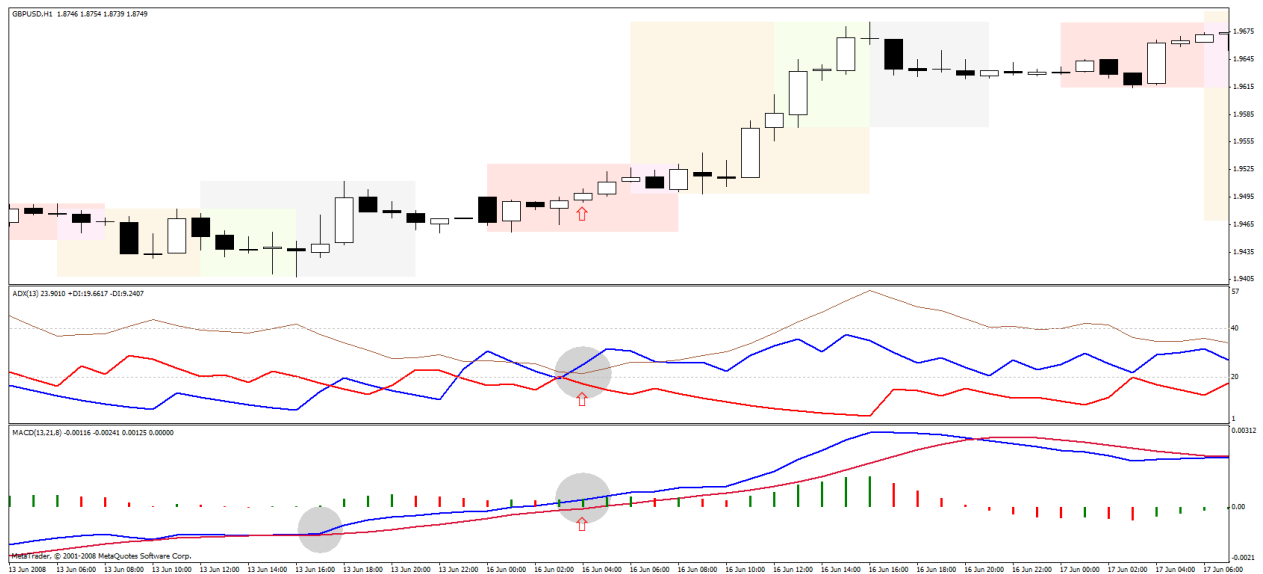
Although I have only indicated these time frames, however, you can also trade the smaller time frames such as the 5-minute, 15-minute or 30-minute time. Personally, I rarely trade those time frames because institutional traders do not trade these time frames and considered as 'noise'.

The indicators needed for this method are ADX and MACD together with stochastic on the 1<sup>st</sup> time frame to determine the strength of the trend or if it is a ranging market, with MACD and stochastic oscillator on the 2<sup>nd</sup> time frame to confirm the entry. Trend lines, Fibonacci and pivot support and resistance levels apply as usual. Now let's look at the rules for buy and sell setups.

- Buy (Long)

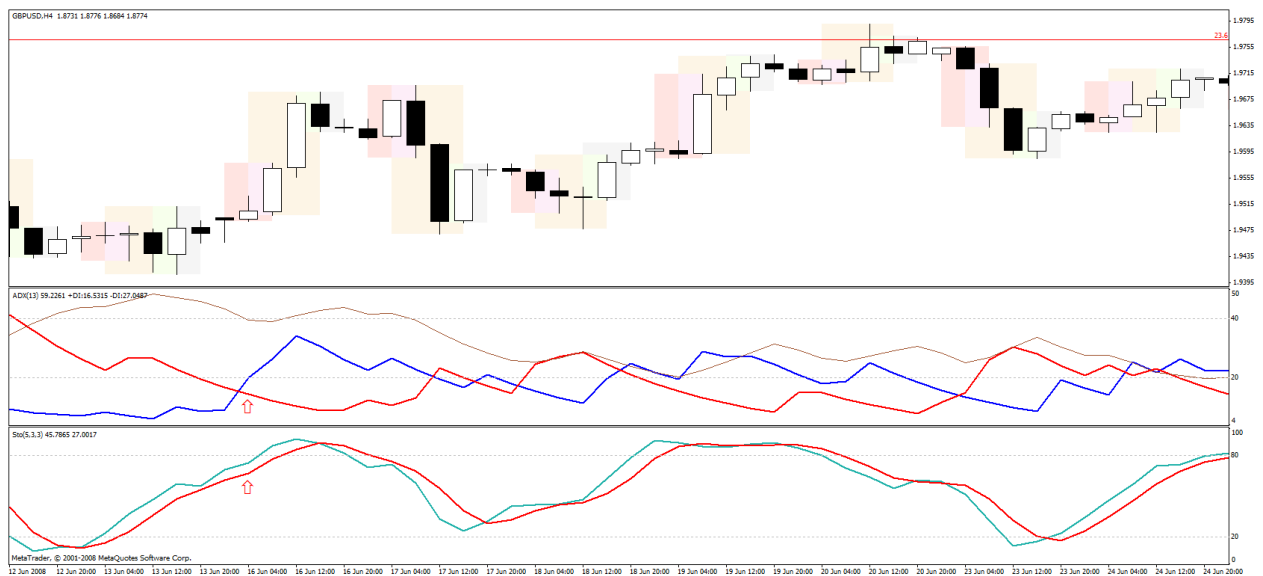
- 1<sup>st</sup> time frame

- ADX +DI Blue Line must cross above the -DI Red Line with MACD histogram above the waterline (or centerline), which also means that the blue line cross above red line; and the histogram bar must be a positive bar (green).



- 2<sup>nd</sup> time frame

- Stochastic and ADX both indicating bullish momentum



- If all of the above conditions above agree,

- Scenario A
  - At the next bar, wait for minor Fibonacci retracement (not more than 61.8%) from the previous candle's high on the chart. Open long position at the retracement and set your stop loss at the recent swing low or near any important support levels.
- Scenario B
  - If the price action does not retrace, open long position at any point of time (the lower the better) after the bullish candle is formed and set stop loss at recent swing low or near any important support levels as long as your percentage risk per trade allows.
- Set a trailing stop equivalent to your stop-loss. Example: if your stop-loss is 30 pips, then your trailing stop will be 30 pips.
- Other than letting your trailing stop stops you out, you can also set your profit target 10-15 pips from any important resistance levels such as Fibonacci, trend lines or weekly pivots (you can get all these support and resistance lines at Me website). You can also exit when the MACD shows a crossover.

*IMPORTANT: It is also advisable to take note of ascending and descending trend lines break. For long signals, break of recent descending line with reversal of indicators provide the best possible scenario to enter a trend. For sell signal, break of recent ascending line is also recommended.*

- Sell (Short)

- 1<sup>st</sup> time frame

- ADX –DI Red Line cross above the +DI Blue Line with MACD histogram must be below the waterline (or centerline) which also means that the Blue Line cross below Red Line; and the histogram bar must be a negative bar (red).

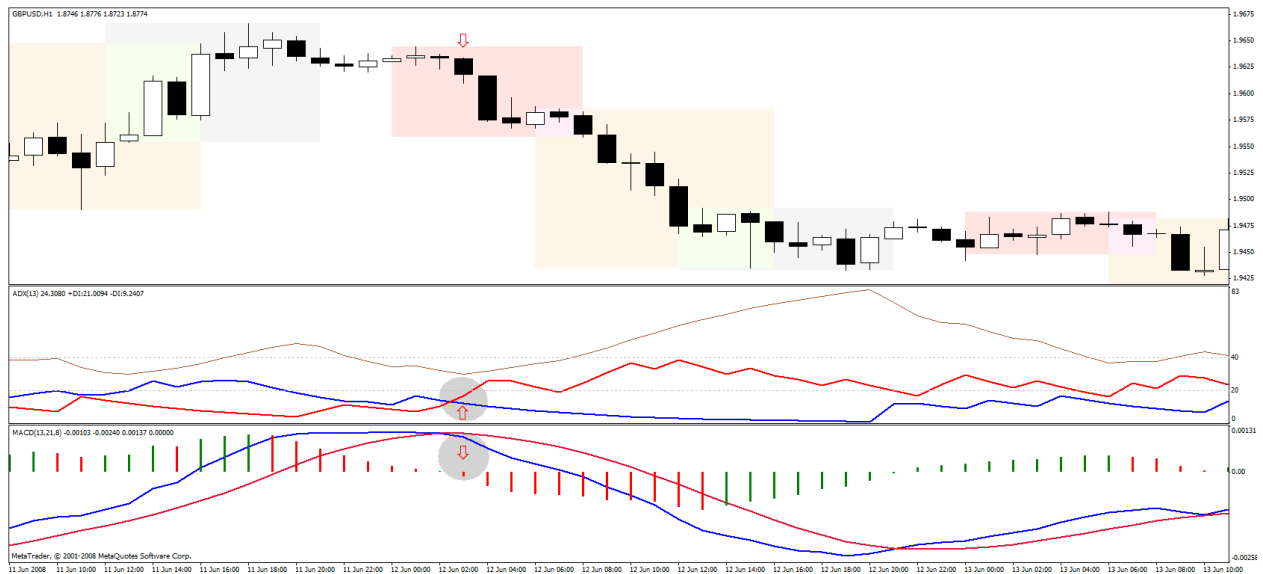


FIGURE 3

- 2<sup>nd</sup> time frame

- Stochastic and MACD both indicating bearish momentum

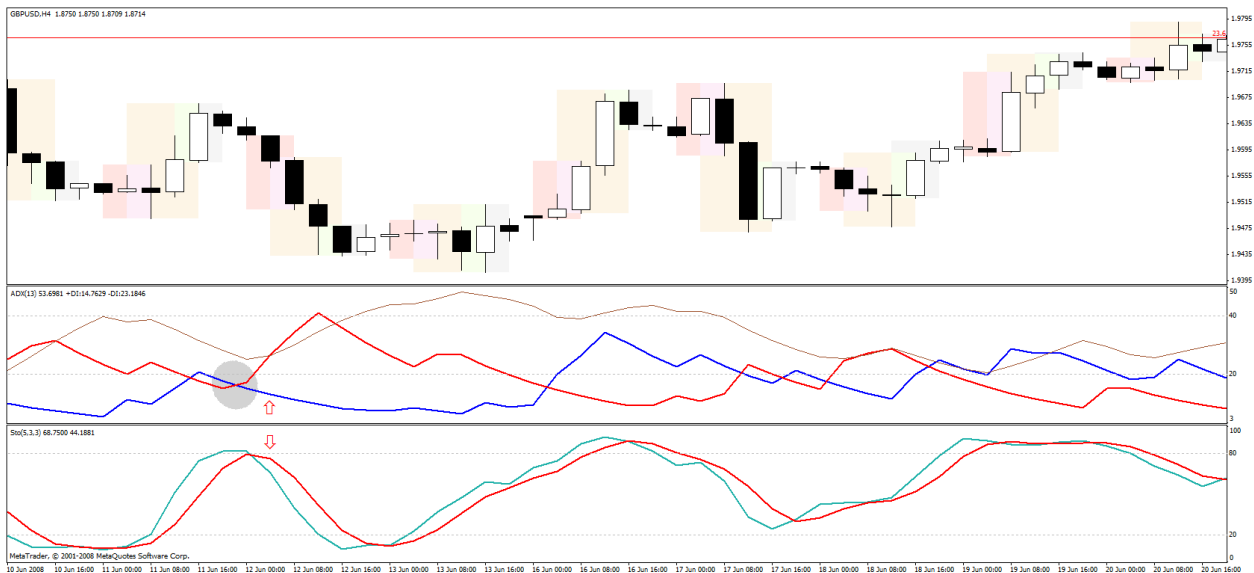


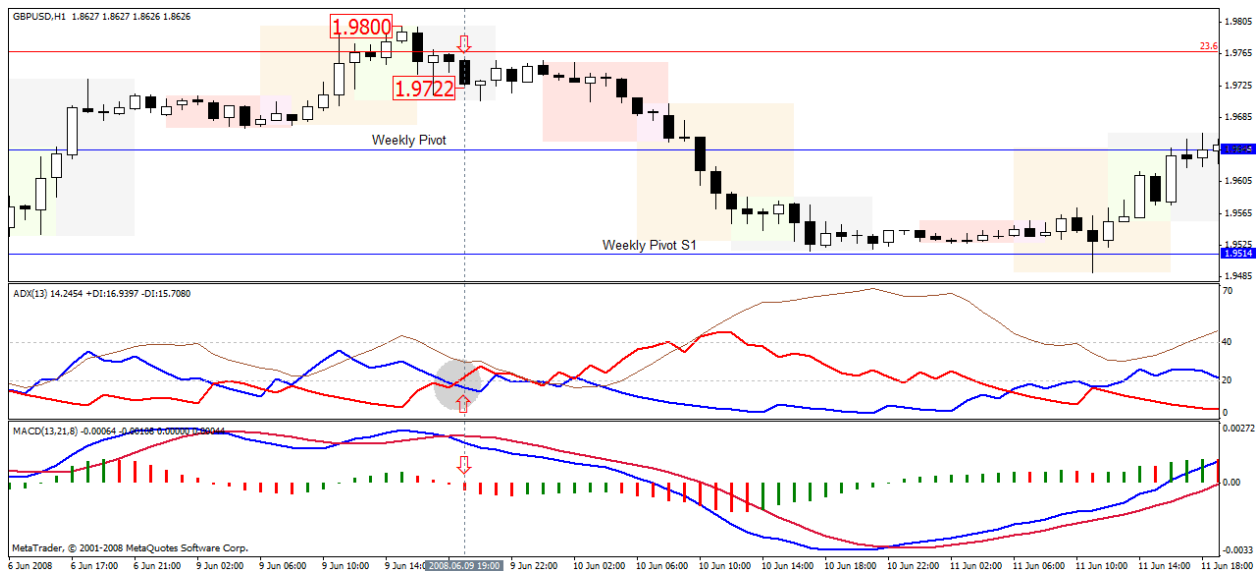
FIGURE 4

- If all of the above conditions above agree,
  - Scenario A
    - At the next bar, look out for minor Fibonacci retracement levels (not greater than 61.8%) from the previous candle's low on the chart. Open short position at the retracement level and set your stop loss at the recent swing high or near any important resistance levels.
  - Scenario B
    - If the price action does not retrace, open short position at any point of time (the higher the better) after the bearish candle is formed and set stop loss at recent swing high or near any important resistance levels as long as your percentage risk per trade allows.
  - Set a trailing stop equivalent to your stop-loss. Example: if your stop-loss is 30 pips, then your trailing stop will be 30 pips.
  - Set your profit target 10-15 pips from any important support levels such as Fibonacci, trend lines or weekly pivots (you can get all these support and resistance lines at the Me website). MACD crossover near the resistance levels ought to take into consideration as well.

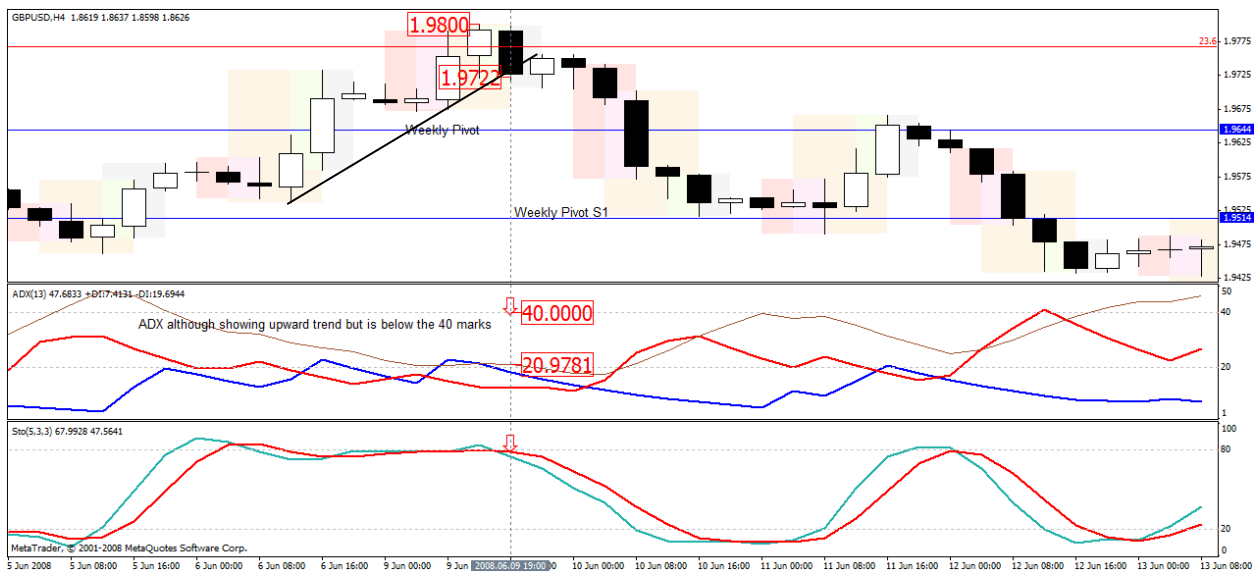
*IMPORTANT: If ADX on the 2<sup>nd</sup> time frame is going opposite direction compared to the 1<sup>st</sup> time frame, then the ADX line on the 2<sup>nd</sup> time frame must show below the 40 marks (not strong) for the setup to be validated, or else no trade even if the stochastic is showing the correct direction. ADX above 40 marks will supersede the stochastic indicator.*

## 7.3 TRADING SYSTEM I: TRADE EXAMPLE

- GBPUSD 09 June 2008 +178 pips



On 09 June 2008 at 1600 GMT, ADX and MACD both indicated that the trend has changed to a downward movement on the hourly chart (Figure 19 - 1<sup>st</sup> time frame). Before entering straight away, I switched to the 4-hour chart (Figure 20 - 2<sup>nd</sup> time frame) to confirm the signal. Indeed, the stochastic has crossed and turned lower and although ADX still indicating that the blue line is above the red line, but it was way below the 40 marks. Hence, this setup was valid.



After confirming the final signal on the 2<sup>nd</sup> time frame, I switched over to hourly and waited for the price to retrace. However, the next bar did not retrace so I entered at the low of the previous bar which was 1.9722 with a stop-loss of 48 pips at 1.9770, 61.80% Fibonacci retracement from 1.9722 to the recent high of 1.9800. The calculator included in this package was used to calculate the Fibonacci levels.

*Please note that I placed the stop-loss at 1.9770 because there was a resistance at 1.9766 which was the 23.6% Fibonacci retracement of 2.1160 to 1.9336. In this case, I felt that the break of this level again should went up further towards 1.9800 area and I was not prepared to lose that amount of pips (setting stop-loss at the recent high) for my risk per trade. I could be wrong, but it turned out to be a good trade after all. Remember to set your trailing stop as well.*

## DOWNTREND - SELL ZONE

Downtrend	Price	Resistance	Price
High	1.9800	23.60%	1.9740
Low	1.9722	38.20%	1.9752
Entry	1.9722	50.00%	1.9761
Stop-Loss	1.9770	61.80%	1.9770
		78.60%	1.9783

TABLE 2

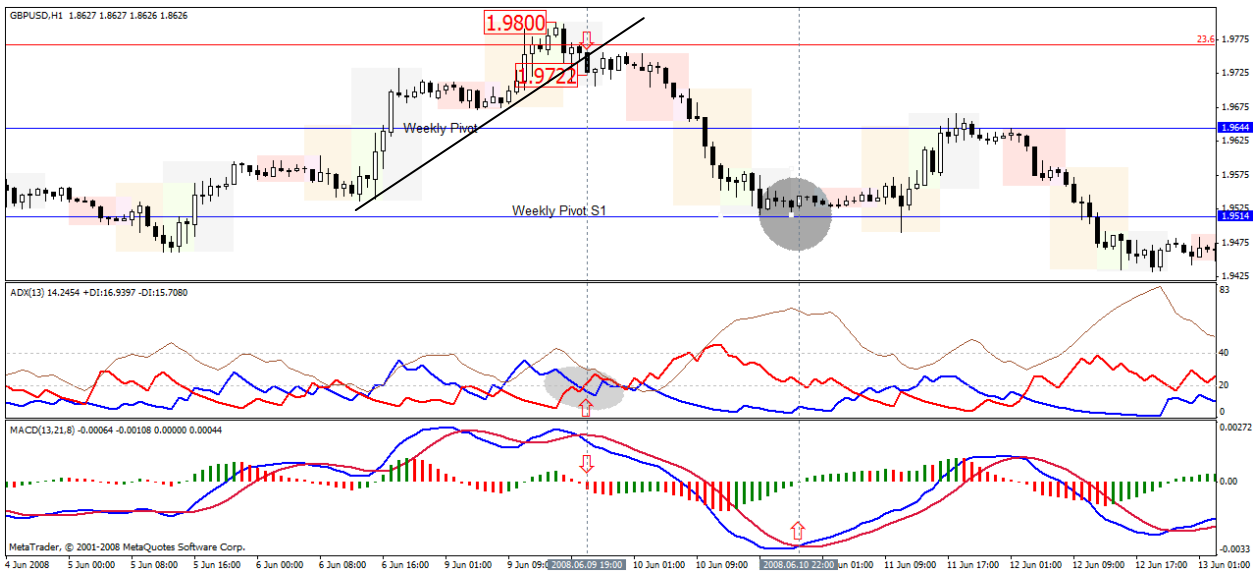


FIGURE 5

As you can see from the chart (Figure 3), the next support was 78 pips away at 1.9644 (weekly pivot blue line) from the entry point at 1.9722, more than what was initial risked (48 pips). As the movement developed, the price was moving in a great downward fashion without triggering the trailing stop of 48 pips. On the 10<sup>th</sup> June, I decided to close the trade at 1.9544 due to MACD crossover, just above the weekly pivot S2 of 1.9514. This trade ended with a gain of 178 pips; about risk to reward ratio of 3.7.

*Note that you could also have been triggered out as the trailing stop would have moved to 1.9578 if I did exit at the MACD crossover, 144 pips away from the entry point of 1.9722. In both cases were winners. Difference is how you exit your*

- GBPUSD 29 April 2008 +189 pips

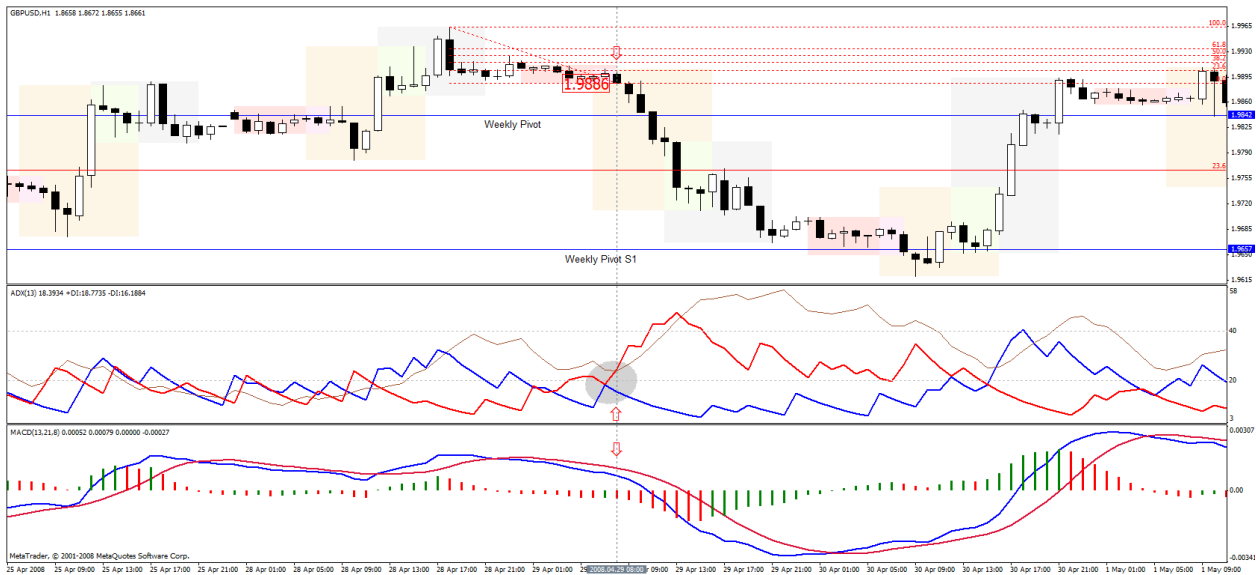


FIGURE 6

On 29 April 2008, GBPUSD pair was on a downtrend, I got a possible setup as both momentum indicators on ADX and MACD all pointed to the same direction on the hourly chart (see above). I then proceed to switch to the 4-hour chart to confirm that the oscillator must show bearish momentum and it did (see below) with break of recent ascending trend line.

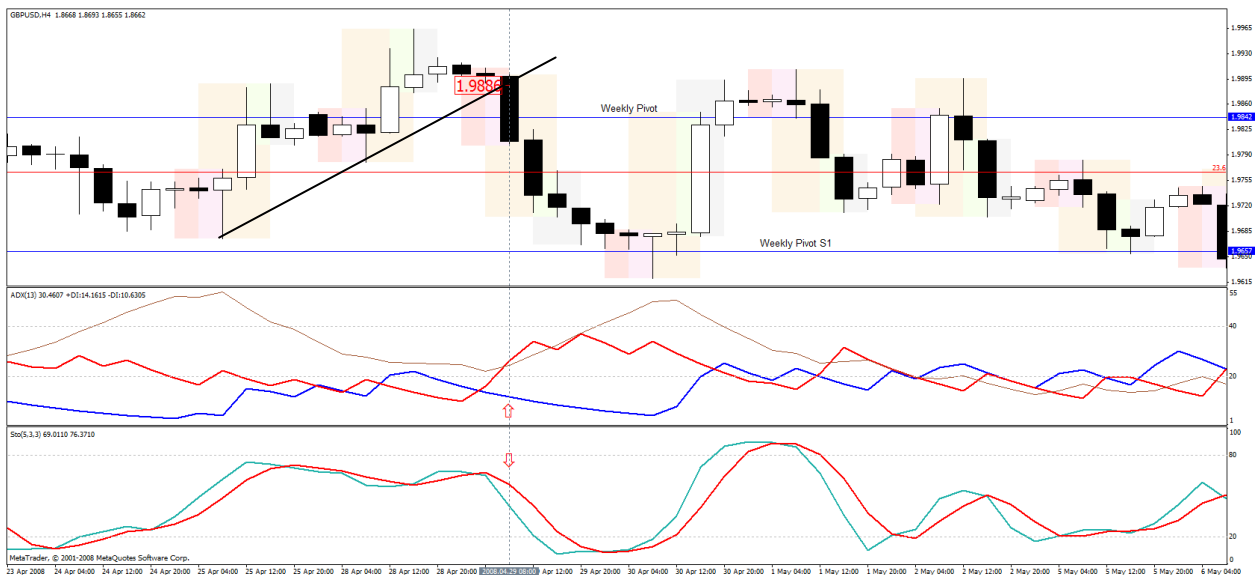


FIGURE 7

Scenario B was formed when the price did not retrace but continued to move lower.

## DOWNTREND - SELL ZONE

Downtrend	Price	Resistance	Price
High	1.9964	23.60%	1.9904
Low	1.9886	38.20%	1.9916
Entry	1.9886	50.00%	1.9925
Stop-Loss	1.9934	61.80%	1.9934
		78.60%	1.9947

TABLE 3

I then set my stop loss at the 61.8% Fibonacci level with a stop-loss of 48 pips because the swing high was too much for my risk per trade. Later the price continued its way down below the 23.6% important support level but I did not close the trade due to the candle was still bearish and MACD shows no sign of crossover yet. As the price continued to drop further, my trailing stop which was equivalent to my stop-loss of 48 pips shifted lower, however, the price later retraced back and eventually hit my protective stop at 1.9697, resulted a total of 189 pips gain with a risk to reward ratio of 3.9.

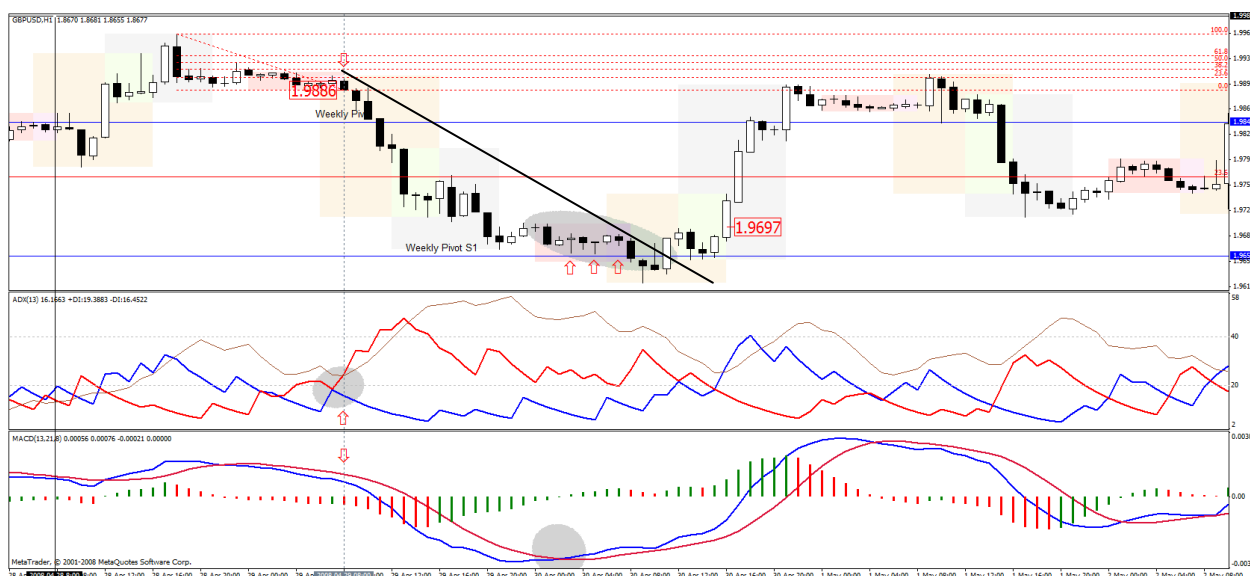
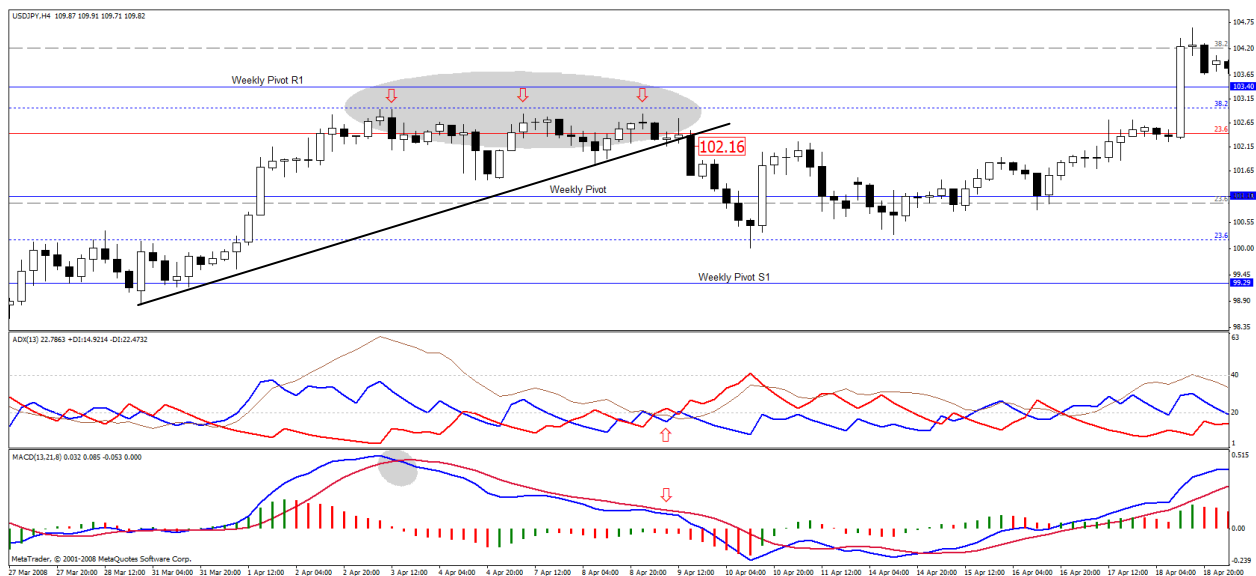


FIGURE 8

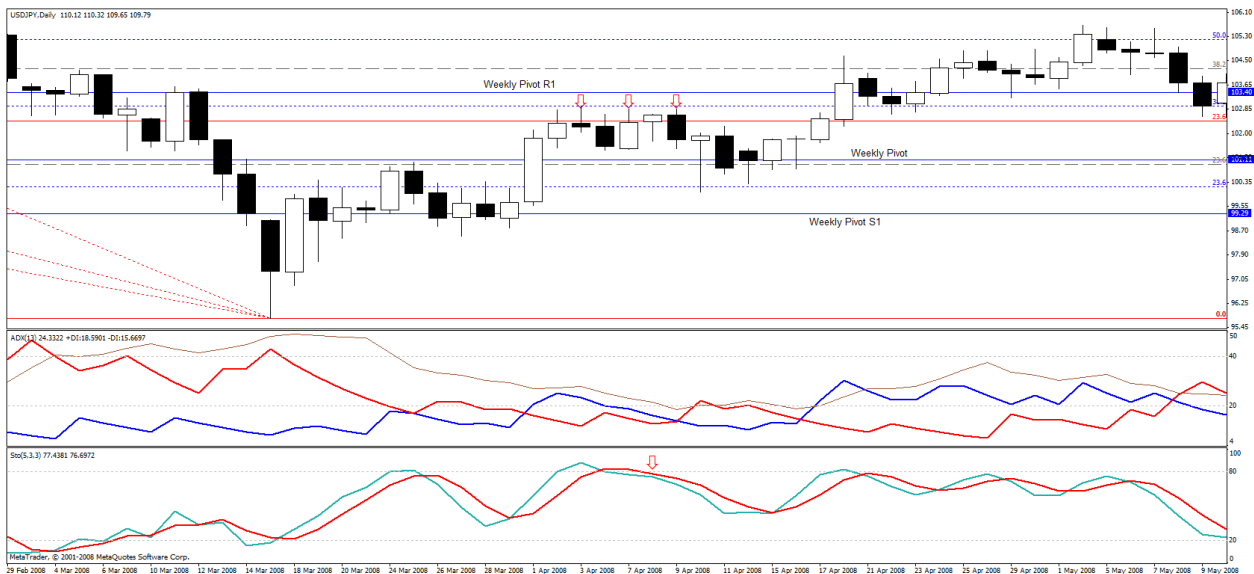
*Although I could have gotten out earlier when I saw there was support at the weekly pivot S2 and MACD has crossed. However, knowing that 100 over pips already in the pocket, I decided to take the additional risk to let it run but it did not turn out better. This trade demonstrated that you can take further risk if you have already made more than 1:1 ratio on the current position.*

- USDJPY 03 April 2008 +164 pips

Earlier you read about the Fibonacci confluence resistance on the USDJPY daily chart (**Error! Reference source not found.**). How do we make use of multiple confluences to confirm that the resistance was strong and if there were any possible trades of opportunity? Let's continue with this example by taking a look at the 4-hour chart which is the 1<sup>st</sup> time frame for this setup.



On the 3<sup>rd</sup> April 2008, we saw that there were confluences of the weekly pivot resistance level 1, the 38.2% level (blue dotted line) and 23.6% level (red line) near the area between 102.44 and 103.40. The first indication of the Bull Run losing its steam was when the MACD crossed (shaded in grey) below the waterline. However, as the ADX was still in the blue and ascending trend line is still intact, no set up was called up. After few days later, the trend line was broken and we got a trade set up with both ADX and MACD signaling a bearish momentum. We then switched over to the daily chart to confirm whether the stochastic oscillator was in agreement with the 4-hour chart.

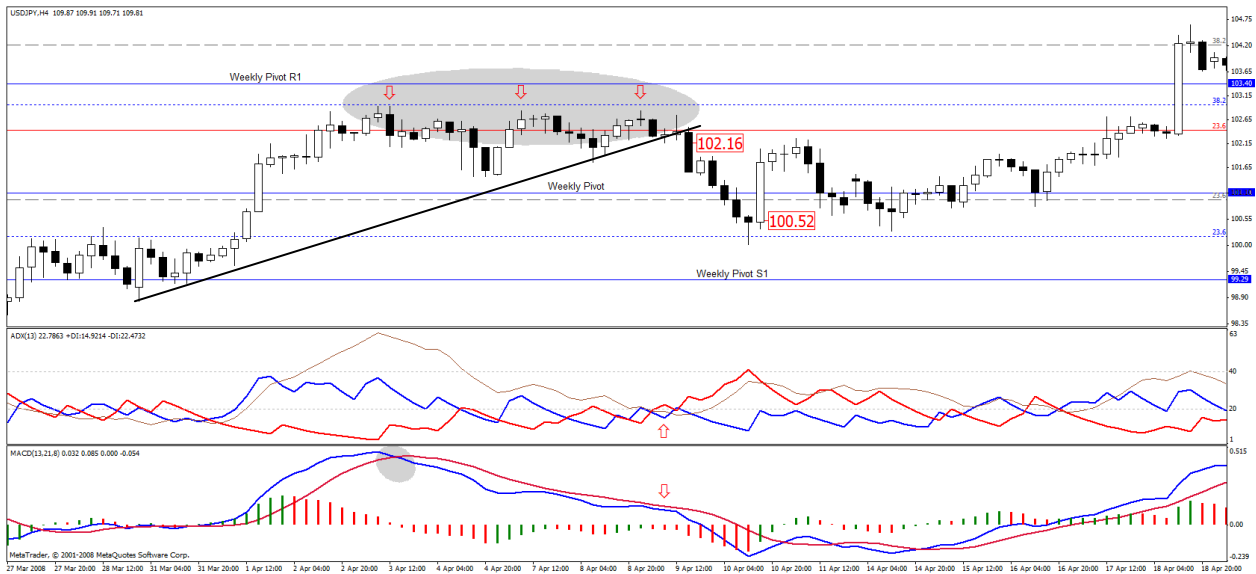


As you can see from the daily chart, the stochastic has already crossed lower and so it confirmed our entry. ADX below the 40 marks also helped to validate the signal. We then look back to the 4-hour chart to enter the trade.

From the 4-hour chart, we knew that there were several bounces off from the confluence resistance which formed a high at 102.83. I entered at the break of the low at 102.16 with a stop-loss at the 61.8% Fibonacci retracement of 102.16 to 102.83 at 102.57, giving me a stop-loss of 41 pips. I also set the trailing stop to 41 pips.

**DOWNTREND - SELL ZONE**

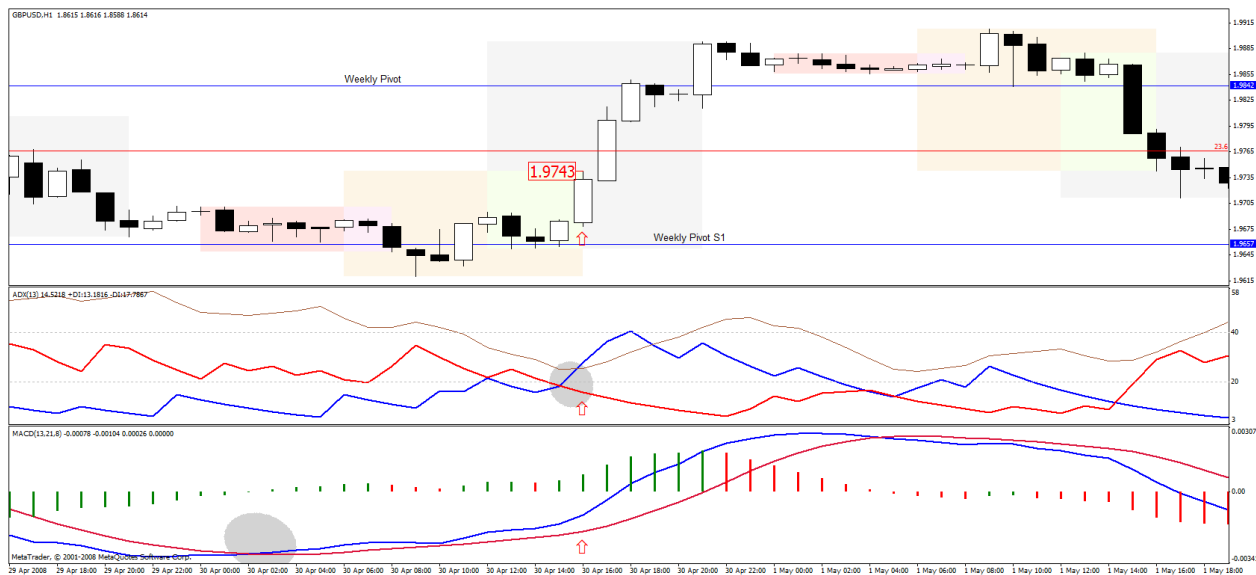
Downtrend	Price	Resistance	Price
High	102.83	23.60%	102.32
Low	102.16	38.20%	102.42
Entry	102.16	50.00%	102.50
Stop-Loss	102.57	61.80%	102.57
		78.60%	102.69



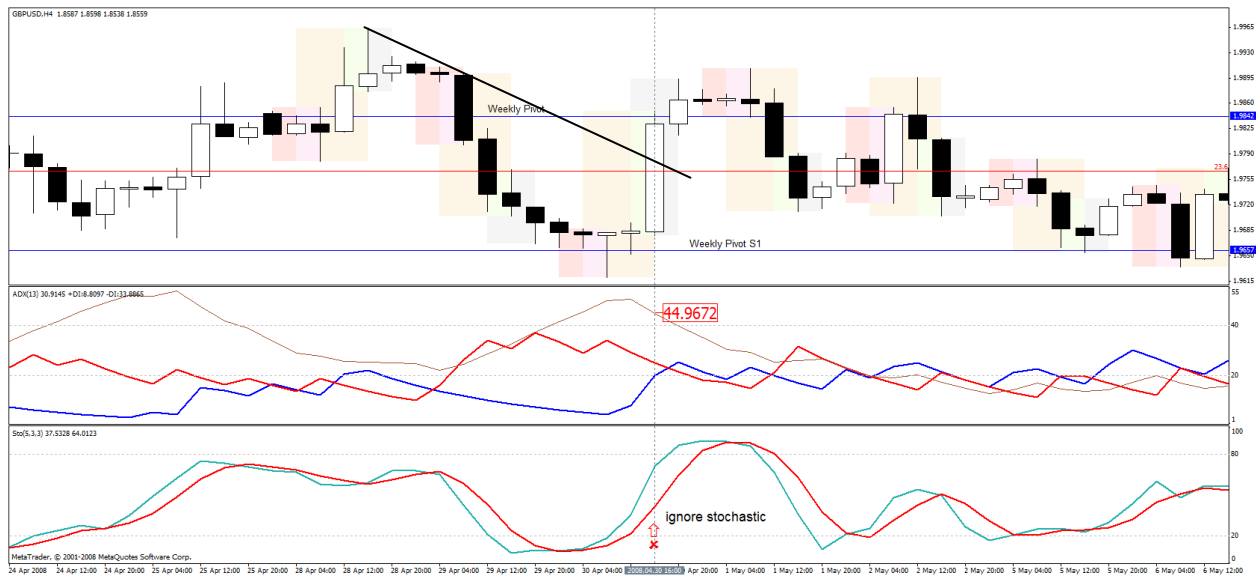
The next day, my trailing stop was triggered and closed at 100.52 with a 164 pips gain. This trade risk to reward ratio was 1:4. Note that I would probably consider closing the trade at the MACD crossover, but the trailing stop was triggered so no action was needed to monitor the market.

- GBPUSD 30 April 2008 – almost a setup

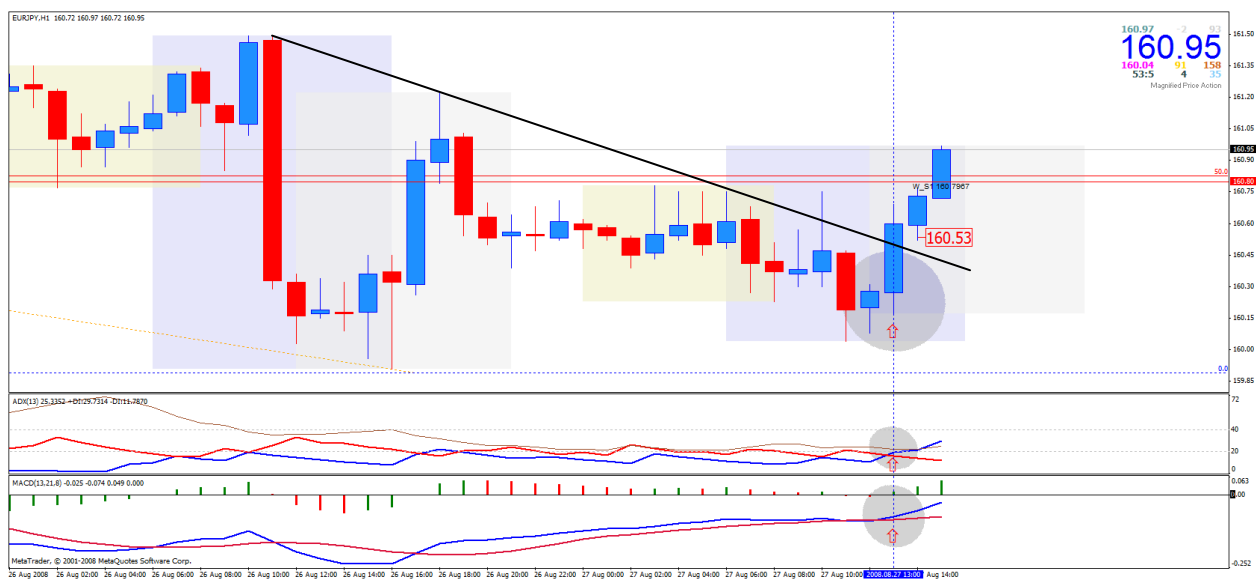
Now this is an example of how a potential trade was denied by the 2<sup>nd</sup> time frame ADX signal. On 30<sup>th</sup> April 2008, the GBPUSD currency pair as we can see from the chart below, the price action has turned to the upside with both ADX and MACD showing bullish momentum together with the bullish candle. With the 1<sup>st</sup> time frame (Figure 28) giving a potential setup, I switched to the 4-hour chart and wanted to confirm if the stochastic has crossed above.



After looking at the 2<sup>nd</sup> time frame, I saw that the stochastic oscillator has indeed crossed. However, as I have mentioned that if ADX indicator is above 40, the setup cannot be validated. Therefore, I did not take the trade. As you can see from Figure 28, in fact, the price actually moved up above the weekly pivot. This trade could have been a winner but I was not prepared to break the rules at that time.

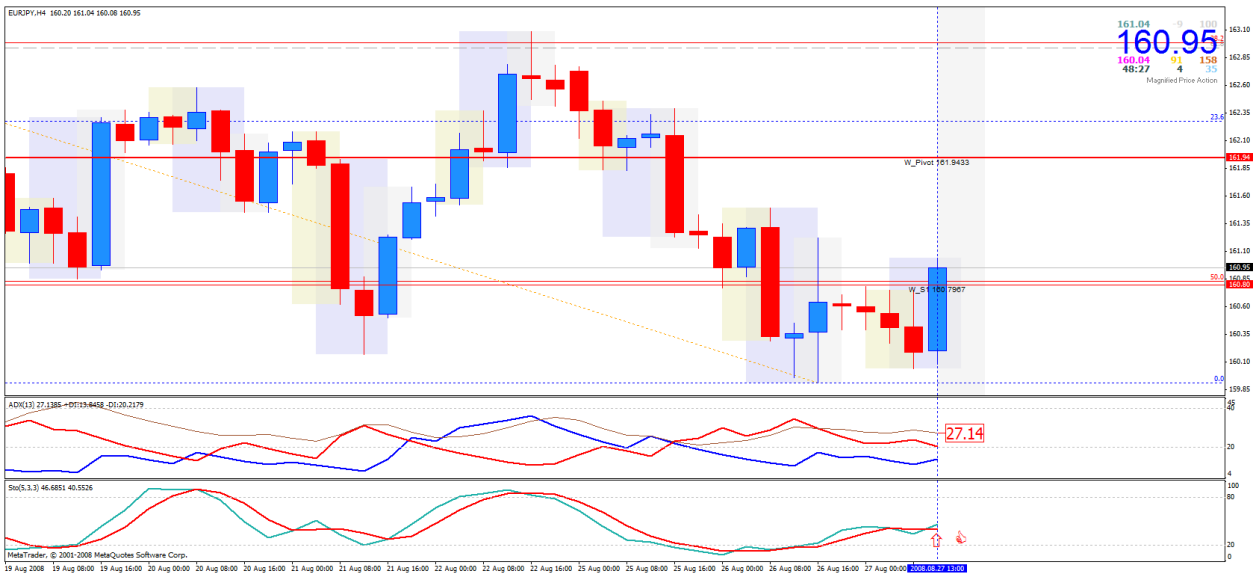


- EURJPY 27 August 2008 +52 pips



THIS EXAMPLE WAS A BUY SET UP WHICH WAS DONE LIVE AT TIME OF WRITING RIGHT NOW AS YOU CAN SEE FROM THE CHART BELOW. I ENTERED AT 160.53 WHICH WAS THE 23.6% OF THE MINOR RETRACEMENT OF THE RECENT SWING LOW AT 160.04 AT THAT TIME. ADDITIONALLY, IF YOU FLIP OVER TO LOOK AT THE 15-MINUTES OR 30-MINUTES, IT SHOWED CONFLUENCES OF UPWARD MOMENTUM SO I FELT IT WAS THE RIGHT MOMENT TO ENTER THE TRADE. THE STOP-LOSS WAS SET AT 160.04 (49 PIPS).

UPTREND - BUY ZONE			
Uptrend	Price	Support	Price
High	160.69	23.60%	160.54
Low	160.04	38.20%	160.44
Entry	160.53	50.00%	160.37
Stop-Loss	160.04	61.80%	160.29
		78.60%	160.18



Apart from that, of course, the 4-hour chart stochastic has crossed and ADX indicating a weak downtrend (below 40) to confirm this setup before I entered the trade.

As time went by, the pair continued to move upwards and the trailing stop of 49 pips was eventually triggered and stopped out at 161.05, yielded a gain of 52 pips. As you can see, the pair later shot up and went as high touching the weekly pivot at 161.94. How I wished if it could have been better!

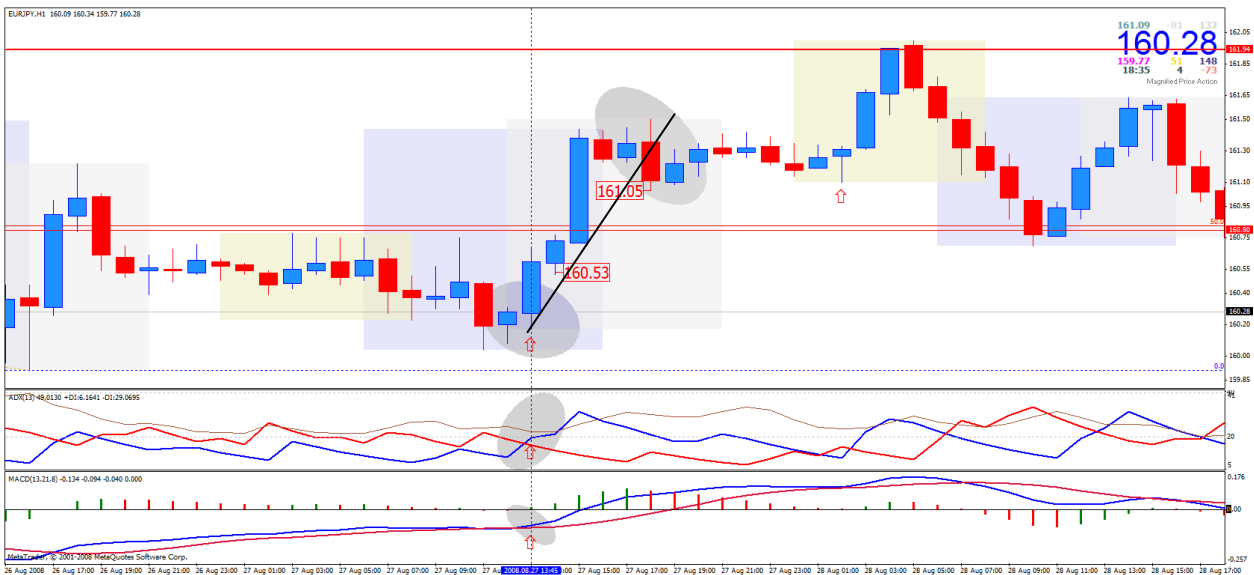


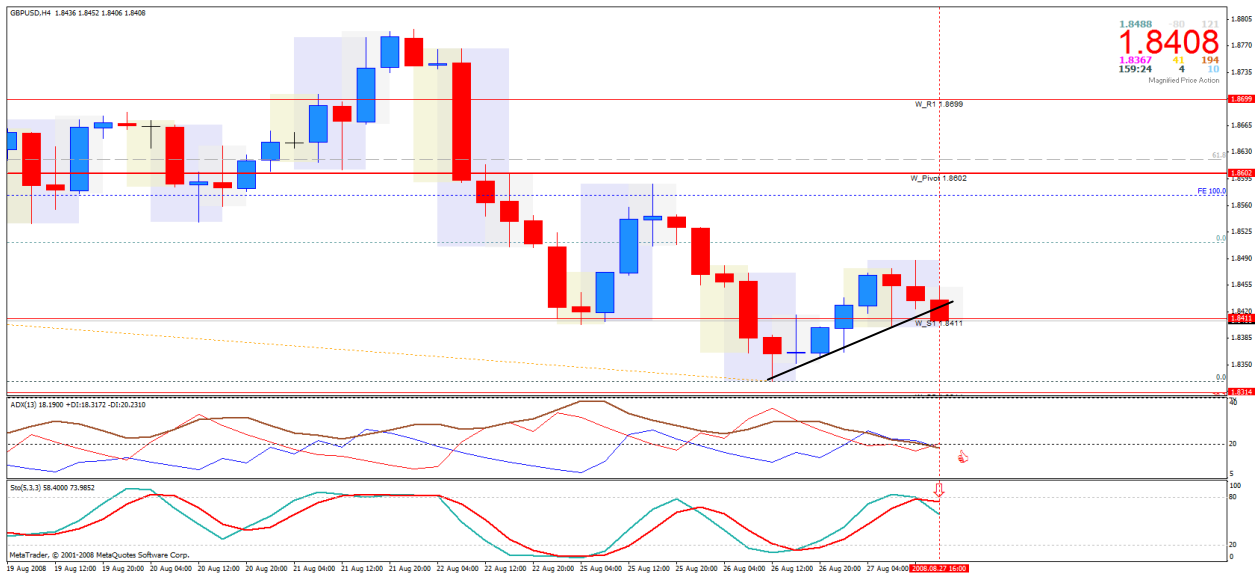
FIGURE 9

- GBPUSD 27 August 2008 +78 pips



FIGURE 10

This was another trade I took on the same day as the EURJPY pair mentioned above. As we know that the recent Dollar rally was a huge run, this trade coincided with the bigger picture and naturally it was an easier set up with vote of confidence knowing that it is aligned with the long term trend. As you can see from Figure 33, MACD has crossed and ADX was flat with bearish tone (-DI above +DI). Therefore, I switched over to the 4-hour chart to confirm if the signal can be taken. Let's take a look at below Figure 34.



On the bigger time frame, we can see that the ADX was flat as well, together with stochastic still fresh from the top of the overbought zone. This confirmed our setup. I then entered it at the break of the weekly pivot S1 at 1.8411 with a stop loss of 48 pips at 1.8459.

**DOWNTREND - SELL ZONE**

Downtrend	Price	Resistance	Price
High	1.8488	23.60%	1.8429
Low	1.8411	38.20%	1.8440
Entry	1.8411	50.00%	1.8450
Stop-Loss	1.8459	61.80%	1.8459
		78.60%	1.8472



Now in Figure 35, the price went further down and eventually I was stopped out with a 78-pip gain at 1.8333. The risk to reward ratio for this trade was 1.625.

## 7.4 MONEY MANAGEMENT

Now you have learned this profitable method and what should you do next? First of all, I want you to try out this method on a demo account and when you are confident and profitable using this trading system, then you decide to trade against the big players in live account. My personal recommendation to open a demo account is what I have mentioned in my first book but I will recap it here again (basically the same).

<b>Capital recommendation</b>	\$10,000
<b>Account Type</b>	Mini account (10,000 per lot)
<b>Maximum risk per month</b>	5%
<b>Maximum risk per trade</b>	1% of capital

- Risk no more than 1% per trade of your capital.
- Let's say you intend to use 10,000 dollars as your starting capital to trade the Forex market. Before deciding how much you want to risk per trade, you should calculate how much you are willing to lose per month so to withstand any possible drawdown. Since we are starting with only 10,000 dollars as capital, I would suggest a maximum cap as high as 5% risk per month, which is 500 dollars.
- So now we know that we can only trade with 500 dollars a month\* even though we have 10,000 dollars as capital. The next step is to determine your risk per trade.

Once we know that we can only afford to risk 500 dollars in a month, and then you will decide how much you prefer to risk per trade. To simplify calculation, let's say we decide to set the risk per trade at 10% of 500 dollars, so that means in a mini account, 50 dollars is equivalent to 50 pips. This risk per trade is also equivalent to 1% of the starting capital. Once you have decided that this would be your money management, the next is to look out for trade setup not risking more than 50 pips, and only if both conditions agree, then you enter the trade.

*This money management means that in order to wipe out the trading account, you have to lose twenty consecutive months of trading to burn that entire 10,000 dollars. Is that possible? Yes, if you don't have the discipline to follow through a profitable trading*

## 7.5 TRADING SYSTEM II: THE METHODOLOGY

The book already cover basic indicators and chart analysis. In addition to My trading Strategy an additional strategy is presented in the topics below. The forth coming strategy can be said as discretionary or systematic trading system. However fundamental analysis can be incorporated into the strategy to gain high probability with huge profit.

The strategy is short term trading strategy and has solid exit rules; to protect profit meanwhile allows riding trend. The strategy hunts for momentum on smaller timeframe. Chart setup includes EMA (Exponential Moving Average) and MACD (Moving Average Convergence Divergence).

## 7.6 TRADING SYSTEM II: THE METHOD

### Strategy Setup

The strategy was developed to work on 15 minute chart. The strategy makes use of two indicators including 20-period exponential moving average. Exponential Moving average is used as trend indicator, which places more stress on recent values. MACD (Moving Average Convergence Divergence) is used in this strategy to measure momentum. Default MACD histogram setting could be used which is 12, 26 and signal EMA = 9.



### Long Trade Rule

- 1) Look for currency Pair with trading price less than 20 period EMA (exponential moving average).
- 2) Ensure MACD is in negative area.
- 3) Wait for the price to cross above 20-period EMA, and MACD to be in process of crossing into or has crossed into the positive area, no longer than 10 bars ago.
- 4) Trigger long trade, 10 pips above 20-period EMA.

### Stoploss Placement

- Place stoploss 50 pips below the 20-period EMA. For aggressive trader stoploss could be placed at swing low.

### Exit Rule

- Close half of the position when profit is equals to amount risked.
- Trail stop at 20-period EMA or by higher breakeven pips.

### **Short Trade Rule**

1. Look for currency pair with trading price above 20-period EMA (exponential moving average).
2. Ensure MACD is in positive region.
3. Wait for the price to cross below 20-period EMA, and MACD to be in process of crossing in the or has crossed into the negative area, no longer than 10 bars ago.
4. Trigger short trade, 10 pips below 20-period EMA.

### **Stoploss Placement**

- Place stoploss 50 pips above the 20-period EMA. For aggressive trader stoploss could be placed at swing high.

### **Exit Rule**

- Close half of the position when profit is equals to amount risked.
- Trail stop at 20-period EMA or by higher breakeven pips.

### **Incorporating Fundamentals**

You can incorporate fundamentals and other multi timeframe analysis into the strategy to increase the predictability and profitability of the trading strategy. Importance of fundamentals factors changes over time, however some of the factor are outlined below which can be used to predict whether the currency pair will be ranging or trending.

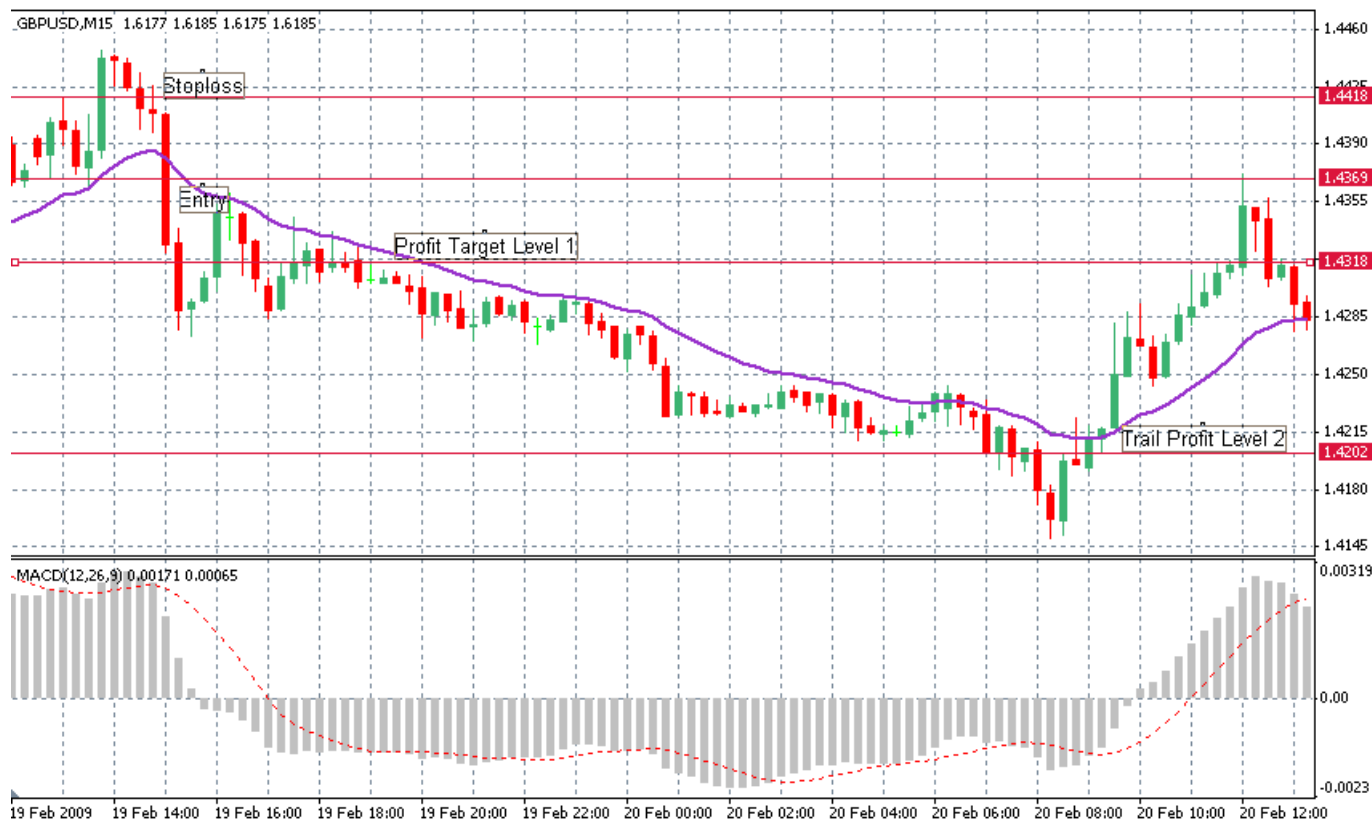
Following are some of the analysis that could be done on major currency pair, once a pair with strong fundament is identified which has clear trend then the above strategy could be applied to it.

Risk reversals near choice or flipping between favoring calls and puts usually depict a ranging pair. Whereas risk reversals strongly bid for puts and call indicating trending market.

Analyze SSI (Speculative sentiment index) to get bias on each pair.



- GBPUSD 20 February 2009 +167 pips



Price crosses 10 pips below 20-period EMA, and MACD histogram shifted from positive to negative area which denote momentum necessary for short trade.

This is one of the trade examples, using the strategy. Indicators gauges momentum and thus pin point entry point. Whereas, money management enables the strategy to lock profit as well as ride the underlying trend.

# CHAPTER 8

## COMMON MISTAKES

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"All I ask is the chance to prove that money can't make me happy."  
Spike Milligan

## 8.1 PSYCHOLOGY OF TRADING

Psychology of trading is yet another important aspect of trading. Many intelligent people lose large capital while trading however in their non trading careers they are very success full and has accumulated large sums of money.

The thing that separate winners from the losers in trading is not how accurately someone picks entry points. But the factors how they will manage the trade after they have taken the trade and how they stick to their money management plan once they are on the trade.

Large majority of the traders do not understand that psychology plays a vital role in money management and they should conduit their emotions correctly while trading.

### **The Effect of Trading Losses**

We are taught by the environment of the importance of always being right. There is always a fear in us of not being wrong and the need to always be right. But this mentality does not go with trading.

Most trading systems that are proved successful takes lots of small losses and then make a big gain on a few winning trades. Unfortunately most of the traders do not have mental toughness lot of losing trades and give up the trading system prematurely, and hurl a profitable trading system without giving it an adequate chance.

### **Destroy Your Trading Account**

A common mistake in virtually all type of trading is holding a trade even the market continues to move against the trade. It was quoted by the renowned economist John Keynes Maynard

*"The markets can remain irrational longer than you can remain solvent"*

Another major factor that differentiate successful trader from the one who is unsuccessful is that a wise trader move to next trade when the market does not act according to his anticipation.

## 8.2 COMMON MISTAKES

### NEVER RISK MORE THAN 2% PER TRADE

One of the cardinal rules which is also the most desecrated rules in trading is that traders lose substantial amount of their account equity in one single trade by taking too much risk. You will find hundred of stories of traders who lose years of profits on a single trade that goes terribly wrong. This is the chief cause why the 2% stop-loss rule should not be violated.

The table below demonstrates that large losses are extremely difficult to overcome

<b>Amount of Equity Loss</b>	<b>Amount of Return Necessary to Re-store to Original</b>
<b>25%</b>	<b>33%</b>
<b>50%</b>	<b>100%</b>
<b>75%</b>	<b>400%</b>
<b>90%</b>	<b>1000%</b>

Let's assume you begin trading with \$10,000 and loss 50% of your capital which in dollar terms is \$5000. So in order to breakeven and overcome the losses you now need 100% gain of on your remaining equity. The best way to avoid this is to have proper risk management and to avoid large losses. For this reason the 2% rule hold utmost importance in trading. If you limit 2% loss per trade this means that you can sustain 10 consecutive losing streaks in a row with a total draw down of 20% of you account equity.

### LOGIC WINS, IMPULSE KILLS

Trader blew up their account more by trading impulsively than by any other mistake. If you ask a beginner trader the reason for taking a long position on a currency pair, you might hear the answer, "Because it has gone down enough – so now it's bound to go positive." This is an example of impulsive trading and wishful thinking; the trade decision is not based on a logical reason.

More money has been lost by trading impulsively than by any other means. Ask a novice why he went long on a currency pair and you will frequently hear the answer, "Cause it's gone down enough - so it's bound to bounce." We always roll our eyes at that type of response because it is not based on reason - it's nothing more than wishful thinking.

Trading impulsively is merely playing the game of Russian roulette. Logical trading is extra precise than impulsive trading.

Trading impulsively is simply gambling. It can be a huge rush when the trader is on a winning streak, but just one bad loss can make the trader give all of the profits and trading capital back to the market. Logical trader will know where to take profit and stop loss if trade goes against him, whereas impulsive traders are only one trade away from bankruptcy.

## ADDING TO A LOSER

Most of the time trader increase their position size and keep on adding to them if trade goes against them. This is a martingale technique in which traders desperately hope that a reversal will occur and their losses will convert to profit. However doing so increases the exposure while the trade goes in loss. In such scenarios a smart trader will typically close the position and head toward next trade.

## NEVER LET A WINNER TURN INTO A LOSER

It is not uncommon to see a trade go up by 30 pips in couple of minute and then it completely reverses to hit your stop loss at 40 pips in a short while.

Traders should learn to protect their profits. There are two easy ways to protect your capital and banking pips. You can add trailing stop to your orders. The second method is to use multiple lots and exit positions on different levels including a trailing stop.

There is nothing worse than watching your trade be up 30 points one minute, only to see it completely reverse a short while later and take out your stop 40 points lower.

# CHAPTER 9

## PUTTING IT ALL TOGETHER

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"The secret to creativity is knowing how to hide your sources."  
Albert Einstein

## 9.1 CREATING A BUSINESS PLAN

Many business fail due to their lack of planning and failure to create a business plan to follow. Creating a business plan give the trader a sense of direction that they are trying to reach. It set goals, and plan to execute. Most successful traders will agree that trading is not different than business and in order to be successful in trading you should have clear and written business plan.

Following are some of the things which should be included into your business plan for trading.

- What are your reasons for which you want to become a trader?
- What do you hope to achieve from trading?  
Be specific here. If the possibility of making a lot of money has drawn you towards trading then list out how much money you want to make from trading and what you plan to do with that money if you make it.
- What are the things that are going to separate you from the large majority of traders who fail?
- What are your biggest weaknesses?
- How do you plan to address your weaknesses and leverage your strengths?
- How much time can you devote towards actively following the market?
- Do you plan to day trade, swing trade, position trade or a combination of the three? Does your choice here reflect the time you have to devote to the markets?
- What market or markets do you plan to trade and why?
- At what times throughout the day are you going to spend actually trading, researching trades, and then learning about the market?
- What are your criteria for entering a trade?
- What are your criteria for exiting a trade?
- What is your money management strategy?
- How will you know if one of the pieces of your strategy stops working?
- After identifying that one of the pieces of your strategy has stopped working what will you do to address it?
- What trading software and equipment you will use to trade and how much is it?
- What Broker/Brokers will you use?
- Do you plan to add money to your account and if so where is that money going to come from?
- If you are profitable do you plan to reinvest profits or withdraw some or all of them?
- If you plan to trade full time how you will support yourself if you aren't profitable right away.
- How much money do you plan to start to trade with? Does the math work out when considering taxes, all costs, living expenses and your initial trading balance?

Those who take time to think about and write down the business plan under these heading generally have a higher chance of success.

## 9.2 MAINTAINING A TRADING JOURNAL

There is an old saying learn from your mistakes, for traders it mean to maintain a trading journal. Successful trader looks at each experience or loss as a chance to learn and grow. Trader openness to leaning from their trades differential profitable and unprofitable trader. A trader should be willing to put effort to prepare a document for recoding his trades and from time to time review each trade.

Trading journals could be used to document trades. You can simply write down details of your trades in a notebook or a word document. However using spread sheet software like (excel) provides you more flexibility and handy analysis options.

Below are 10 things that in my opinion it is important to document about each trade. :

1. What were the market conditions for that day or trade?
2. Why you take the trade, entry date, time and price.
3. Reason for exiting the trade with date, time and price at which you close the trade.
4. Was the trade short terms or long term?
5. Comment on market condition from the time you entered till you close the position.
6. Money management rules that used for the trade.
7. If possible attach a chart with your analysis.
8. Address you weakness for the particular trade or day.
9. Address your strength for that day or trade.
10. You can also add additional comments which you though might be help full.

## FINAL THOUGHT

I hope that you enjoyed reading my latest strategy. I still classified it under My Trading Strategy trading systems because I do not want to confuse you with too many titles and names. That is also to identify in the Forex market that whenever you hear about someone using My Trading Strategy systems, you know that they are talking about Me.

Importantly, I am delighted that you have chosen My Trading Strategy 2 out of so many trading systems out there. It is my pleasure and honor to share you my second strategy which I felt could be your answer to profitable Forex trading. This eBook took quite a while to release because of the complexity and additional effort to explain everything, not forgetting that the tediousness of cut and paste the charts. I am not like some other online traders who hired professional writers to write out their eBooks because I want to be sure of what I am trying to convey to you are what I am thinking actually. In fact, if you have noticed, I actually put the explanation of the trading system on the first part of this eBook because the initial part of reading is usually the most alert and absorb the most.

Lastly, while I did try my best to explain whatever I can put in words, I cannot assure that what you have read here is the complete mind-mapping of what I am thinking. If you think that you need further help on troubleshooting the trades that you have done, you may also want to consider after the completion of reading this trading system, you may subscribe to my personal coaching via emails at a very minimal fee for 6 months. Rest assured that I will answer all questions on the My Trading Strategy systems within 24 hours.