



Set Yourself Financially Free

Harness the World's Money Mountain

FINANCIAL FREEDOM THROUGH FOREX

By **Greg Secker**
and **Chris Weaver**

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Preface

There are more individual, private Foreign Exchange traders now than there have ever been, and the number is growing daily. There are three main reasons for this. The first is the advancement in technology and, in particular, the Internet. The expansion and popularity of the Internet has made it possible for everyday people to have access to the world's largest and fastest growing marketplace (the Foreign Exchange market) through online brokerages and charting software companies.

The second reason is awareness. In the past, individuals were unlikely to know anything about the Forex market because it was really an exclusive club, only for large banks trading with each other. Nowadays, anyone can trade, and people are talking about it and understanding the profound effects that successful money management and Forex trading can have on their lives.

The third reason for the increase of individual participation in this market is a lack of confidence in the traditional style of investing—that is giving your money to someone you don't know and letting them “have a play with it.” Investors have witnessed their pensions and investments underperform for far too long, and they have now decided to manage their own money and keep 100% of the return (without paying management or performance fees).

At the end of the day, it's your money and you've worked hard for it. After you've lived a little and made some money, the smart move is to find somewhere sensible to grow it. That's why you are reading this book.

There will always be people out there who will happily take your money and do nothing more with it than generate fees, commissions, and income for themselves, leaving you with just a husk of the potential wealth that money could have generated.

I have worked for years, among investment bankers and asset managers. As a young man fresh out of the university, I found the “city” to be a fascinating place—but, after a time, you just have to wonder who is paying for all the flashy cars, expensive lunches, and exorbitant offsite junkets—the answer? You! (Who else?)

We have all watched city bankers (clad in fitted suits and Hermes ties) promise us much—casting their investment outlooks while talking in tongues—but actually deliver little, if anything of value. Recently, we witnessed Goldman Sachs, arguably one of the largest and most successful investment banks, testifying on Capitol Hill for betting against the very products they induced their clients to buy in the latest unravelling of the credit crunch scandal.

How many people did well in the dotcom boom and bust, the oil crisis, and the credit crunch? Did you? No!

It amazes me how quickly we forget the lessons from the past and then, like sheep, we are herded by the next Hermes tie-clad shepherd into his pen, where his well-educated but poorly skilled traders erode our savings with irresponsible money management, poor trading strategy, and just a basic lack of care and responsibility. I remember a certain money manager telling me in a pub in the city one late Friday night, “It’s all about this year’s bonus, after that I’m going to sack this off and do something I really enjoy.”

It was an American psychologist, Robert Cialdini, in the late 1980s who first identified this phenomenon in his groundbreaking book *Influence: The Psychology of Persuasion*. In his book, Cialdini talks about *Captainitis*, and tells us how people need “captains,” because they have such little confidence in their own ability. He cites a specific example:

On the bitterly cold afternoon of January 13, 1982, Air Florida Flight 90 sat on the tarmac of National Airport in Washington, D.C. Following a series of delays, the plane was finally cleared to take

off. As the captain and the first officer were completing their last round of pre-flight checks, the following exchange took place regarding one of the systems:

First officer: God, look at that thing. That don't seem right, does it? Uh, that's not right.

Captain: Yes it is, there's eighty.

First officer: Naw, I don't think that's right. Ah, maybe it is.

Shortly after this conversation transpired, the plane took off. Less than one minute later, Flight 90 crashed into the icy waters of the Potomac River.

This tragedy is an example of a troubling and all-too-pervasive problem in aviation that officials in the airline industry have referred to as “Captainitis.” This occurs when crew members fail to correct an obvious error made by the plane’s captain, resulting in a crash. In this case—and many others like it—the copilot made the calamitous decision to defer to the captain’s authority. This is a clear example of the power of the principle of authority; that is, we tend to defer to the counsel of authority figures and experts to help us decide how to behave, especially when we are feeling ambivalent about a decision or when we are in an ambiguous situation. Experts also have a hand in helping us decide what we should think. For example, one study found that when an acknowledged expert’s opinion on an issue was aired just once on national television, public opinion shifted in the direction of the expert’s view by as much as 4 percent.

Do you think the investment management world runs on this basic principle of authority? You bet it does.

If you are in the Investment Management business, this is important. There is an unending supply of people who are willing to hand over their money to you on the promise that you will do something more useful with it.

Making money in the financial markets requires a personal epiphany. You have to realise that the cultural hypnosis that has been keeping people poor for hundreds of thousands of years works as strongly today as it ever did.

The good news is that you can harness tools and strategies to rapidly affect your psychological and internal beliefs—and this will change your entire world. Simply learning some trading tools and skills is not enough. The old adage, “Scared Money never makes money,” speaks to the importance of mastering your mind and creating confidence within yourself. As Mark Douglas so elegantly puts it in *Trading in the Zone*:

The solution is to change the way that we think to get our minds into a care-free state so that we don’t interpret market information in a threatening way that could cause emotional pain, thereby bypassing the automatic invoking of our hard-wired mechanisms.

Once the psychology exercises are in full flow, we must find a trading strategy that suits our personality and, with that, we are ready to start producing.

Our mission at Learn To Trade is to equip this next generation of up-and-coming, private Forex traders with the skills and confidence required to trade successfully. We understand that 95% of what you read about finance and economics is either useless or incorrect, so we are going to scrap all of the irrelevant information and focus on the 5% that is potent and effective.

To achieve this concentrated approach, we have divided this book into three separate sections. The book should, therefore, be read progressively—especially if you are a complete beginner. Jumping straight to the back of the book and reading only the strategies would minimise the impact that the strategies have on your personal trading account. We have mentored a lot of traders at Learn To Trade, and we know exactly what is required for trading success, including the sequence in which the information should be delivered.

To get the most out of this book, it is vital that you get your hands dirty. Read through it thoroughly and methodically and make sure to complete all the exercises. And, most of all, have fun and enjoy the journey.

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Part 1

Environment—The Right Condition for Trading

The first part of this book is about making sure that your personal environment is right to receive and interpret the strategies correctly. Most people believe that successful trading entails using the “best” strategies only—this is not the case. Successful strategies are certainly a big piece of the trading puzzle, but they are not enough on their own. One way to think about a strategy is as if it were a seed. A strong seed will not germinate without the correct growing environment. Thus, Part 1 deals with the environment.

Chapter 1

The Essentials

Chapter 1 Objectives:

- * Understand the belief cycle and why it is important
- * Discover who you *really* are when it comes to money
- * Understand the difference between learning “how to trade” and how to “make money from trading”

“Everything should be made as simple as possible—and no simpler.”—Albert Einstein

Einstein’s approach perfectly describes how this book will be presented. Trading books generally do a very good job of overcomplicating very simple ideas—not this one!

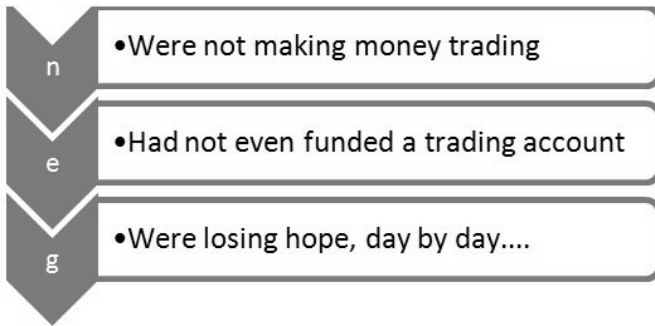
Instead, this book focuses on practical application, with a goal of equipping you with the tools (both mechanical and psychological) to generate life-changing amounts of money through profitable trading. This requires your commitment to **take immediate and massive action** and **lock all the doors behind you**. Most people don’t read much past the first chapter of any book, so given the fact that we can’t be with you in person, I am going to gently nudge you throughout.

At Learn To Trade, we are committed to the success of our traders-in-training. You have certainly made the right choice! We have privately mentored thousands of promising new traders all over the world—from the Americas, Europe, the Middle East, Australia, New Zealand, and Asia. Our family is huge and we are growing; so, despite the fact we haven’t met you in person yet, welcome! Please go to our Web site, www.learntotrade.com.au, to watch some amazing testimonials from our real-life students. These will help to build belief in you in terms of what is possible. Belief is important. Without belief comes little action and, ultimately, little result. Though you can’t replace “real-life” proof as the

ultimate reference point upon which to build your beliefs, taking a look at our graduate's success stories will certainly get you on the right path.

How did all this happen?

Before Learn To Trade came to be what it is today, I was trading from home and inviting friends over to watch me trade and join in. Before long, I had amassed a cult following of some nineteen traders, all camped out at my mews house in Kensington, London, where we would all actively trade the FX markets day in, day out. It wasn't until I was invited to a late-night gathering of keen, recent trading seminar attendees that I learned something very interesting about human psychology and belief. As I got to the party, everyone was excited to finally meet a trader. After a series of questions, I quickly discovered that they



What was going on here? Why had thirty-eight people, who all appeared to be intelligent and well educated, spent over \$5,000 each on a trading program and done nothing with what they had learned? Was this mass apathy at its best? Why did I have nineteen relatively normal people all trading actively at my house? What was I doing differently?

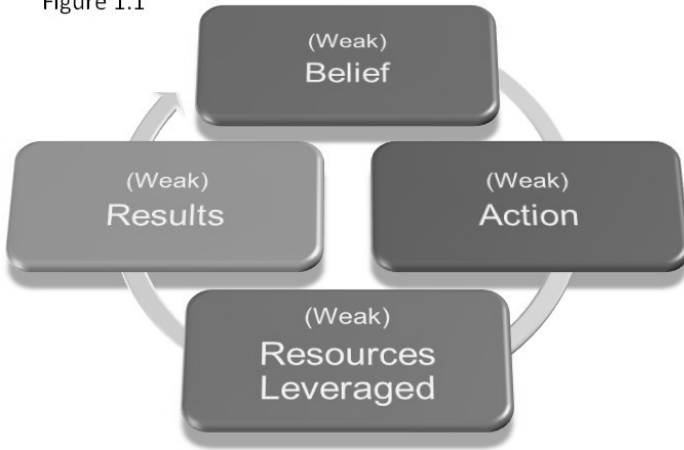
Then it hit me: every person who came to my house watched me trade live before starting to trade themselves! They all witnessed money being protected first and, second, money being made.

So I asked the following question:

Did any of you watch your mentor trade live? Can you guess the answer? Yes, of course, a resounding, “No!”

“The problem you guys have,” I started, “is that you just don’t believe in this stuff.” You haven’t seen it work with your own eyes, which means there’s a little voice inside all of you that is screaming, ‘I’m not convinced this actually works!’” Without real references, there is little belief. Take a look at the diagram below and look at the impact weak belief has on the rest of the cycle.

Figure 1.1



You need to realise that, unless you believe trading is a viable means of making money, you’ll not take the appropriate action. This in turn will result in the limited application of your resources (your time and money) and, ultimately the results will be poor—which will support and confirm the original belief. The spiral will continue, getting more and more powerful with each revolution. The point here is that if it’s positive from the outset, it has a great chance of staying that way; if it’s negative, the same rule applies. We’ll talk about changing beliefs later in this book. For now, concentrate on surrounding yourself with positive examples—our Web site is a good place to start. Look at the belief cycle below to see how strong belief impacts the rest of the belief cycle—this is what you want.

Figure 1.2



Who You *Really* Are and How You *Really* Feel about Making Money

It is critical to establish and discover what trading means to you personally.

The **first** question that you have to answer before reading any further is one of the most important questions of all:

WHY?

Why Forex trading?

You must have a strong “why” or “reason” to trade. This concept has everything to do with your personal moneymaking ability and the understanding that **trading is simply a vehicle**—the most efficient vehicle to get you from where you are, to where you want to be.

This vehicle needs a driver, one who is going in the right direction, and one who has a clearly defined destination. I will be demonstrating the power and significance of a motivated and dedicated driver in great detail later in the chapter.

This *reason why* is your psychological whip to drive you to pursue trading with the enthusiasm and commitment that is required. This is especially true for trading the Foreign Exchange (FX) market. A lot of people like to dabble in this market. This is a sure way to lose money

fast. But if you are willing to be committed, determined, and invested, you can begin a new life of financial freedom and security.

So, what is *your* reason for trading the FX market? Please write it below and refer to it each time you pick up this book. Be as specific as you can.

You must also have an initial target in terms of monthly income. In the box below, please write the amount of money that you would like to draw from your trading account each month. You can think of this as your trading salary.

\$

Now on a **scale** of 1–11 (11 being the most serious, 1 being the least serious), rate your personal level of commitment to your trading experience by circling one of the numbers below. How committed are you?

- 1 2 3 4 5 6 7 8 9 10 11**

We all know that saying we are serious about something is one thing, but **being serious** is completely different. In the next few minutes you will know exactly how serious you are – no more pretending. Most people are desperate to believe that they are serious about increasing their wealth or dramatically changing their financial circumstances. The reality is that most people are NOT. How do I know this? Because most

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people's financial circumstances never experience a dramatic change! The majority of the earning population are exactly happy with their average salaries. That's why it is average. Everyone wants more money, but no one wants to invest the time and money into making it happen. You can't have the product without the process.

For now, let's get back to the "seriousness test." Imagine yourself being financially independent. Imagine the freedom that you have. You don't have to ask anyone if, and when, you can take a holiday. No longer do you have to live your life according to cost, but rather according to benefit. Not only that, you are able to contribute to good causes, events, charities and programs that you believe in. Now you must recognise that all of this starts with you hitting the initial monthly target above.

In the blank box below, write down how much money you are willing to invest into yourself to hit the target that you set yourself. Think of this as a "one off" investment.

\$

At this point you should have:

1. A monthly income target
2. An indication of how serious you are about hitting your monthly target (1–11)
3. The amount you are willing to invest in order to hit your target and begin the journey to a greater level of financial freedom

Great, let's keep moving...

Most people generally want large returns with little investment. Let me show you the results of a student I have done some work with:

Monthly target: \$6,500
Seriousness: 9 out of 11
Amount of investment: \$500

Before we go any further, let me make something very clear. There are no “correct” answers. This is all about discovery. With that in mind, let’s break down this example:

Monthly target: \$6,500—this is a very reasonable initial monthly target to achieve via successful FX trading. The \$6,500 is the joint salary of this man and his partner; therefore, if he were able to achieve this amount, they could both quit their jobs without having to make any financial sacrifices.

Seriousness: On a scale of 1–11 he was a 9. I consider any response that is an 8 or above to be very serious.

Investment: \$500.

This is where it gets interesting. Look at the difference between what he wants to receive and what he wants to give. He would like to receive \$78,000 in the first year alone ($\$6,500 \times 12$ months), with an investment of just \$500 into himself. That equates to a 15,600% return on capital! That is really asking his \$500 to perform! This is not at all uncommon. Most people are trying to find a quick fix, or a “band aid,” for their finances when, in fact, **they need a complete transformation.**

I have a couple questions for you:

- 1) **Would you consider this guy realistic?** _____
- 2) **Would you consider this guy to be serious about hitting his target?** _____

Now look at your answers to the exercise above. How serious do you really believe you are?

Ask yourself these questions and be honest:

Question: Am I approaching this venture looking to gain a lot with only a little effort? If so, have I approached other opportunities in the past that way—what were the results?

Question: Am I looking for a quick fix for my finances or a complete transformation? If I am looking for a complete transformation, what action must I take?

The Good, the Bad, and the Ugly

Let's start with the Bad and the Ugly.

The Bad and the Ugly—The vast majority of people live their entire lives hoping that things will change financially for the better. They will even take small amounts of action to bring about the desired change. Unfortunately, the action they take is normally just information gathering. This is done not to bring about transformation and address core issues, but simply to make them feel better and to convince themselves that they are actually doing something. As a result, a lot of people know what to do but never actually get around to doing it! These people mistake knowing what to do with taking action. That is a devastating mistake.

Here is a quick example:

Most people know that if they want to lose weight, they need to do more exercise and eat better food. But the result is not in the **information**,

the result is in the **implementation** of the **information**. Their knowledge must become action if they want to lose weight—**Learn To Trade!** You can see how strongly we feel about this!

This is why the first paragraph of the introduction makes it clear that you must **lock all of the doors behind you**. If you believe you are going to make money from this, then go for it! I promise you that it is possible. And you are not on your own; we are here to help you.

The Good—So now you know “the Bad and the Ugly,” let’s talk about the **Good!**

The **Good** is that, even if the exercise above revealed that you are looking for a lot and only wanting to give a little, you can still make it as a successful FX trader. I am not saying you don’t have to make an effort, I am saying that trading the FX market is an efficient and effective way to manage and make money. Let me explain.

There are basically two ways to generate money. The first is to work for it. This is the **time equals money** approach. An employee will work for a certain number of hours, or until a certain result is achieved, and will then be paid in exchange for what he or she has done or how much time he or she spent doing it. The second way to generate money is through the efficient use of money itself. This is what we call the **money creates money** approach. With this approach, the more money you have, the more money you make. This is true on a broader scale (because money creates opportunity), and it is also true specifically within the FX market (because money creates trading opportunities). Therefore, the more money that you have, the more money you can make—**money creates money**.

To be a successful trader, it is necessary to shift from the traditional and somewhat dull time equals money mindset to the explosive and transformative money creates money mindset. This transition of thinking takes you from a place of lots of work for relatively little money, to efficient input for a relatively large sum of money. It is the difference between having a salaried approach to your finance and having a money management approach.

Let me summarise this small section with a quote from Edgar Bronfman, former CEO of Seagram. “To turn \$100 into \$110 is work. To turn \$100 million into \$110 million is inevitable.”

Let’s Keep Digging...

At Learn To Trade, we are constantly getting our students to self-analyse and address core issues that are hindering financial progress or success. The reason we do this is because we have seen too many people try to change the fruit of their lives while neglecting the roots of their lives. Let me explain.

Most people constantly look at the fruit, or results, of their financial circumstances and try to change them. This is pointless because the fruit is simply a product of the type of tree that it is growing on. No matter how hard you try, you can never make an apple grow on a pear tree! If you want different fruit you must have a different tree. This is true because the tree is the **source** of the fruit. **If the inflow or source doesn’t change, then the outflow or result will not change—FACT.**

So, what type of financial tree do you have in your life? Is it a tree that allows for constructive self criticism and transparency, or is it a tree full of excuses and reasons why money never comes to you?

Self-transparency is important. If you are unable to assess yourself accurately and honestly, you will not be able to improve the things that need improving. Putting the blame for lack of prosperity anywhere other than yourself is a disempowering activity and never results in positive change or growth. You must be able to assess yourself honestly so that you can move on from where you are to where you want to be.

And that is the key: moving on.

You mustn’t just read this, put yourself in a box, and never begin the pursuit of increasing wealth. The point of this section of the book is for self discovery and the exploration of core financial beliefs and issues. If you believe that things need to change, then you must take action and start the process to change them... and that means now.

Below are important exercises we do with our traders-in-training at Learn To Trade. Please take the time to go through them thoroughly.

Money beliefs – the stories we live

Rate yourself from 1 to 10 with the following (10 = strongly agree, 1= disagree)

- 1) Striving for wealth won't allow much time for anything else in life _____
- 2) Having a lot of money is a big responsibility _____
- 3) I'm not great with money and financial matters _____
- 4) Most of the good opportunities are gone _____
- 5) Striving for wealth can cause stress and health problems _____
- 6) Its not right for me to be rich while others in the world have nothing _____
- 7) I have some resentment towards extremely wealthy people _____
- 8) I can make it on my own. I don't need help from others _____
- 9) The Investing and trading world is complicated and difficult _____
- 10) It's difficult to get rich these days _____

Your total score

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- 10) It's difficult to get rich these days _____

Your total score

The exercise above shows the difference between what you *think* about money and what you *believe* about money.

What has been going on with you?

- Write down how much money you make per month?
- Write down how much money you were making per month last year...
- Write down the percentage growth you have achieved in your income in the last year...
(HINT: Minus the first box from the second and divide the answer by the first box)
- How many additional income streams have you added to your life, in the past twelve months?

The exercise above demonstrates where you have been. Maybe you found that you have done or achieved a lot in the last year, or maybe you realised that you have done very little. Either way, the focus must now be on...

The Future

- Write down how much money you expect to be making per month, this time next year
- How much do all the things cost per month in your dream life?
- Is there a difference between what you expect to earn next year, and what you really want?

This stuff is so powerful! It is up to you to allow these simple and effective exercises to serve their purpose by taking them seriously and referring to them frequently. I also suggest that you show the results to someone else so that you have some accountability. This is important because it puts some **healthy pressure** on you to pursue and achieve.

Private promises we make to ourselves are much easier to break than public declarations of goals. I once had a student who, after one of my heartfelt trading psychology talks, decided to take action and print new business cards, declaring herself a Financial Trader. She then proceeded to hand these out to her family and friends. Needless to say, as a Greek Australian, the pain of not living up to her self-professed new identity and the subsequent ribbing that she would have had to endured from her peer group was worse than not following through. She did indeed become a successful trader and is today regarded as quite an authority on the subject.

Before we move on to the next section, I would like to share with you a little saying that we have at Learn To Trade.

“Your return will always reflect your investment, so invest heavily into yourself!”

I Want to Learn How to “Trade” the FX Market!

Ask yourself this question out loud, and write your answer below.

What is the difference between knowing how to trade and knowing how to make money from trading?

Hopefully, by speaking your answer out loud and also by writing it down, you’ve learned that there is indeed a massive difference between just understanding how to trade and understanding how to actually make money from trading.

The difference between knowing how to trade and knowing how to make money from trading is simple. Think of it like driving: there are normally two different exams you have to pass to obtain your driver’s license. The first test is written and assesses whether or not you know the rules of the road. The second test is actually on the road and assesses whether or not you can implement the rules of the written exam.

Question: Would you rather make a mistake on the written test or on the road test?

The answer is obviously the written test. That is because the potential consequences are so different. If you mess up the written test, you probably just have to take the test again. If you mess up the road test, you may put yourself or others’ lives in danger!

This says a lot about which type of assessment is more critical, and this analogy clearly exhibits the significance of implementation over and above information.

So...

Forget about learning how to trade the FX market! Yes, forget about it! People who know how to trade normally understand a lot of interesting trading topics and can handle themselves in a truly involved trading conversation. This is all fine, but it doesn't produce the desired results: **physical, hard cash mounting up in your personal bank account** and opening doors you once thought were impossible to open! Get this next point into your head now and don't forget it.

I don't need to learn how to trade; I need to know how to make money from trading

This is the foundation of every trading course and personal wealth mentoring session that we offer at Learn To Trade. We believe that the real need is to develop skills for a richer life, not to simply have an academic experience.

Check out this fact:

The likelihood of success when trading the FX market with the dominant trend is not only higher than any other major financial market in the world, it is more probable.

It is a remarkable—yet very true—statement, and to be able to fully appreciate it you must understand something very important:

The FX market is a market that is driven by **buyers** and **sellers**.

Sounds very simple, doesn't it?

Well, this point alone is not unique to the FX market. In reality, every market in the world, essentially, is driven by *buyers* and *sellers*. The difference in the FX market is the number of buyers and sellers and the volume they create. This is called liquidity. The Foreign Exchange market dwarfs all of the other financial markets in the world in terms of

participation and volume. It is by far the fastest growing market in the entire world, and it is currently over three times larger than all of the major stock markets in the world *combined*. A lot of potential traders fear the FX market and use its size as a reason to stay away from it. Some even argue that this is a massive boom, or bubble, which is bound to burst. This would be true if the growth was just merely an inflation of price, but it isn't. It is an increase in participation, making the market even more liquid, which in turn increases the probability of success on a long term basis—bring it on!

Think of it like this: let's say that there are one thousand people who are behind a specific cause. Those people are limited to the strength or influence that they hold as a group. Now let's say that the group grows from one thousand to one-hundred thousand. Their influence and strength has increased, as well as the probability of achieving or realizing what they stand for.

If you relate this concept to trading the FX market it looks like this: If we consider the GBP/USD (also known as "cable") chart, we normally see it trending either up or down (it goes sideways for less than 15% of the time).

For the moment, we will just assume it is trending up. This means that the Sterling is increasing in value relative to, or against, the U.S. Dollar (the next chapter has more on this concept), which means that the buyers are in control of this currency pair and are driving the value of Sterling up against the U.S. Dollar. The buyers want the chart to continue moving up, which is to say that Sterling will continue to strengthen against the U.S. Dollar, so that, eventually, they can sell off the Sterling for a profit. Simply put, the buyers have a "cause" or "agenda" they are fighting or trading for, which is an increase in the value of Sterling against the U.S. Dollar. This upward trend is incredibly strong due to the amount of participation and money that is being invested into this trend consistently.

If you were to trade in the direction of this trend, it would be far more likely that success would occur than if you traded in another trend in

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another market where there is less participation, liquidity, and money behind the move.

Chapter 2

The Basics & The Bounce

Chapter 2 Objectives:

- * Understand the difference between fundamental and technical analysis and how to combine them
- * Understand basic FX terminology and application
- * Understand the principles of the bounce and why amateurs get it wrong because of “social proof”

Two Schools of Thought...

There are two forms of market analysis: fundamental and technical. With each approach comes a set of pros and cons.

Fundamental:

Fundamental analysis is based on economic data. Traders who trade fundamentally wait for specific press releases and attempt to jump into big moves. This is very dangerous because the market is normally very volatile during a news release. If the trader takes the bait and jumps in on a false buy or sell signal and the market moves quickly in the opposite direction, it is very difficult for the trader to get out of the position without taking a hit. With that in mind, there are also huge benefits to trading the news. Large pip scores can be made very quickly, and this type of trading can prove to be very profitable to the seasoned trader.

The reason pure fundamental trading doesn't work for most people, especially beginners, is that it is impossible to define specific entry, stop loss, and take profit prices. This means that trade sizing and reward to risk ratios (I will be explaining each of these ratios in the Risk Management chapter)—become very difficult to determine. This,

combined with the “fast-finger” nature of this style of trading, ultimately results in losses for the vast majority of traders.

Technical:

Technical analysis is based on chart interpretation. Technical traders are looking for the charts to show very clear setups. Once a setup appears, the trader is then able to precisely determine the entry, stop loss, and take profit prices. This is the biggest practical difference between the two styles: fundamental trading is more free flowing; technical trading is more accurate and specific.

The problem with trading only technically is that the market sometimes ignores technical setups on the release of fundamental data. In other words, a trader can see a perfect technical setup and place the entry and exit orders around it, only to see the market react to the data released and completely disregard the technical picture. When this happens, the trade is left to chance. If the news release pushes the market in the desired direction, the result will be profitable; if the news pushes the market in the opposite direction, the result will be negative.

You cannot leave your account open to chance.

You need a solution.

Question: At Learn To Trade, do we trade **fundamentally** or **technically**?

Answer: 100% of both!

Huh? But that’s impossible, isn’t it?

Let me explain. We understand that both styles have their merits. Equally, we understand that both have their limitations. In response to this, we have created a simple combination of the two that provides the best possible environment for success. It works like this:

100% Fundamental—If, fundamentally, there is a lot of news being released on a particular day, we stay **out of** the market. If, on the

other hand, nothing of any significance is happening, then we are fine with sitting down and looking for trading opportunities.

100% Technical—Once we have the “OK” from the fundamental perspective, we trade only technical set ups.

In summary, fundamental information tells us 100% whether or not to sit in front of our computers. Technical information shows us 100% where and when to place our trades.

Basic Terminology

In this chapter we are going to explore the big picture of trading and make concrete distinctions between unsuccessful and successful traders. Before we do that, however, it is important that you have an understanding of the basic terminology.

OHLC Bar

OHLC stands for: Open High Low Close

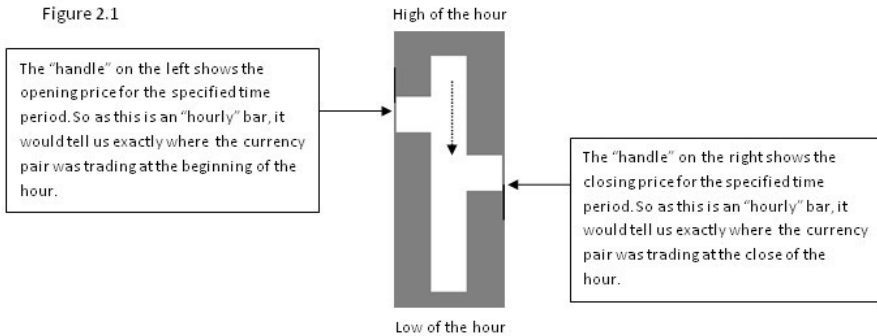
Like any other financial market, the FX market is measured through price movements that are plotted on a chart. A unique aspect of the FX market is that the movement on the chart is measuring one currency relative to another. This is why the “price” on the chart is referred to as the exchange rate.

The OHLC bar shows you where price opens, where it closes and what the extreme highs and lows are over a specific period of time.

Look at the example of an “hourly” bar below:

Financial Freedom through FOREX

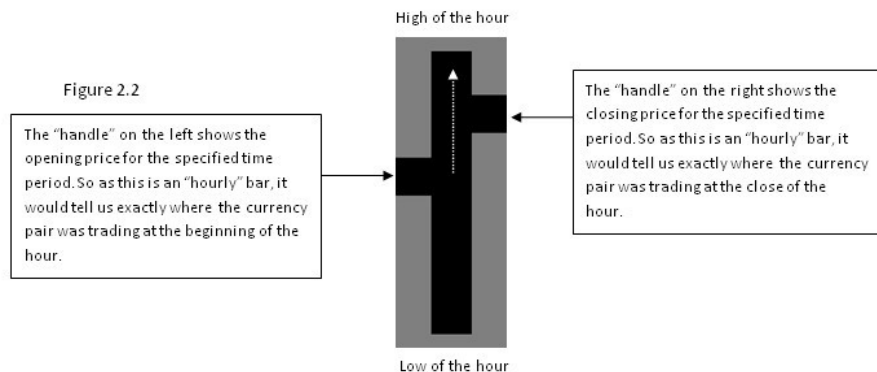
Figure 2.1



Notice that the bar is white. This is because the close of the bar was lower than the open. White bars are also referred to as seller bars. This name comes from the fact that the sellers in the market are the ones who are pushing the price down. That is because they want to sell high and buy back low. In this scenario, the sellers have won this particular hour of trading.

A buyer's bar has exactly the same structure to it but has a higher close than its open. It is referred to as a buyers bar because the buyers were able to push the price up higher than the open during the given period of time. Buyers want to buy low and sell high.

Look at the buyers bar below. Notice that the close is higher than the open.



Although these bars can represent almost any period of time, the most commonly used timeframes to establish long, medium, and short-term

trends, as well as trade entry prices are: Daily, 4-hour, 1-hour, and 5-minute charts.

The longer the time duration of the bar, the greater the value of information it gives. For example, if you had a black OHLC bar on a 1-minute chart, that means that the buyers won the last one minute of trading. One minute, however is very insignificant in the overall scheme of things. Compare that to a weekly OHLC bar. If the buyers were to win that period of time, it would tell us a much clearer story as to where the market is pushing the overall exchange rate. Time is king—always.

Stop Loss and Limit (take profit) Orders:

Stop Loss: You are going to have a few losing trades. That's just life on the "trading floor." For this reason, you need to have a safety net which cuts your losing trades short. The stop loss does exactly that. It is a market order that instructs your broker to close a losing position at a specific price. It is important that you have a stop loss on every single trade, just in case the market shifts very quickly against you.

A major benefit of trading the FX market opposed to traditional stocks and shares is that your stop loss is *almost* always "guaranteed." By "guaranteed," I mean that if a trade moves against you there is very little chance that the price will "gap" or jump over your stop loss order. This is not true in the stock market where "gapping" occurs quite often. There are two notable reasons for this:

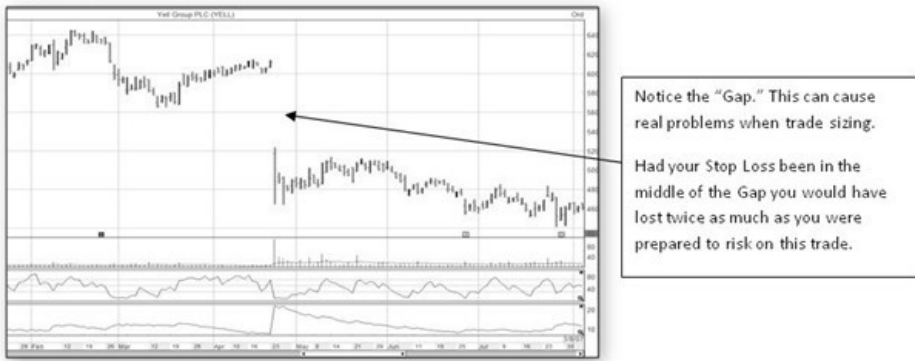
1. Stock markets are less liquid (high liquidity makes it easier to get in and out of a position, low liquidity makes it more difficult) than the FX market, which means the price jumps around much more, or gaps, far more frequently.
2. Stock markets close five times per week (each night, Monday through Friday). The FX market only closes once a week (Friday night). When a market closes, it must also open. But the issue is not *when* it opens; the issue is *where* it opens. The price the market opens at is not only influenced by where it closed, but also by events that occurred between the close and the open. This creates opportunity for gaps in the market.

Financial Freedom through FOREX

Therefore, the more times the market opens and closes the more opportunity there is for your stop loss to be gapped.

The first example below is a picture of the Yell Group Plc chart. This stock experiences a very quick drop in value and you can see how the bars on the chart gap. Imagine if you were in a Long (buy) position (this means you make money when the chart moves up and lose when the chart moves down) and you had your stop loss placed in the middle of the gap. The effect of the gap in price would be that you lose more money than you had originally intended to risk—this is definitely an issue and makes trade sizing and risk management very challenging.

Figure 2.3



The second example is a picture of the 5-min EUR/USD chart. In a very short space of time the Euro strengthens over 150 pips in value against the US Dollar. The point here is that there are no gaps even though the price moved very quickly. Each bar passes off to the following bar with no break or gap in the price action. This makes risk management much easier and far more accurate.



Notice the difference in the FX chart.

Even though the Euro strengthens against the US Dollar very quickly, every price along the way is filled – No Gap. You can risk manage accurately.

Can you see why this is important?

The reason the FX stop loss is only *almost* always guaranteed is because there is a possibility of the market gapping between the Friday night close and the Sunday night open. It is true that the market rarely opens at exactly the same price on Sunday as it closed on the previous Friday, but the gap is normally so small and insignificant that it has no real impact on your trading account.

Limit (take profit) Order: Your limit order is the exit order that you *want* to trigger—it is the opposite of your stop loss. The stop loss stops your losses and the limit order collects your profit at your **predetermined** target. The great thing about the limit order is that it will collect your money for you without you having to be in front of the computer. It is always nice to leave your trading desk with an open trade and come back to banked money. This is only possible because of the limit order.

The limit order is also very useful for controlling the greed in you. Once the order is in place, it collects the money automatically as soon as the price hits the target. No more, “I know that was my target, but let’s just see if I can get some more out of this trade,” rubbish! Later in the book, we are going to talk more about the importance of targeting and taking the money once your target is achieved.

Limit orders and stop losses are both exit orders. The limit order is an exit with a profit; the stop loss is an exit with a loss.

Pip:

Pip stands for “Percentage in point”. In the FX scene, the words “Pip” and “Point” are interchangeable. A pip is measured as the fourth decimal place of the exchange rate. For instance, a currency quote may look like this:

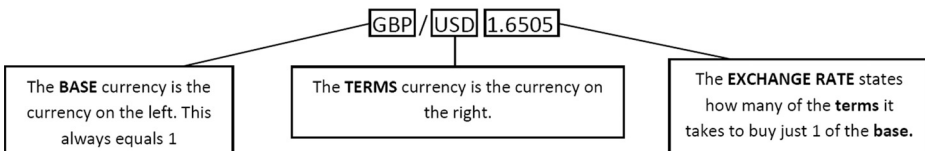
GBP/USD 1.6505

The 5 is the fourth decimal place and the price increment that we are trading. The only exception to this is when there are trading pairs that include the Japanese Yen (JPY). When the JPY is traded the exchange rate will only have two decimal places. It will look like this:

USD/JPY 91.57

Notice that in this exchange rate the second (not the fourth) decimal is the increment that we are trading. This is only because the JPY is involved. All pairs that exclude the JPY trade with the fourth decimal as the point.

What does the exchange rate mean? Here is an illustration:

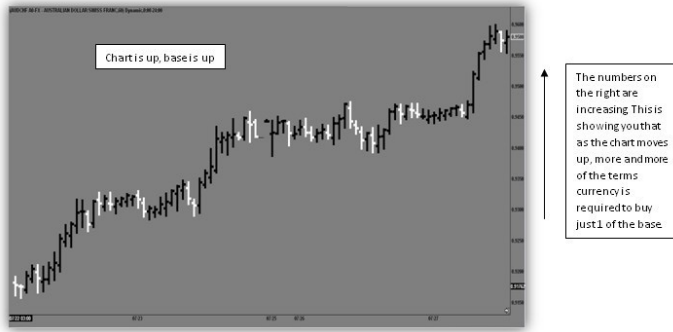


So, in this illustration if you wanted to buy just 1 GBP you would have to sell 1.6505 USD.

Principle: When the chart is up, the base currency is up and the terms currency is down. When the chart is down, the base currency is down and the terms currency is up. Take a look at the example below.

The currency pair in the example is the Australian Dollar with the Swiss Franc (AUD/CHF).

Figure 2.5



Question: According to the trend, is the AUD strengthening or weakening against the CHF?

Answer: Strengthening—remember, when the chart is up the base is up. Or you could say the CHF is weakening against the AUD.

In the next example, you can see the daily chart of the Euro and New Zealand Dollar (EUR/NZD).

Figure 2.6



Question: According to the trend, is the NZD strengthening or weakening against the EUR?

Answer: Strengthening—if the chart is down the base is down, which means the terms currency is up!

Trading the FX market is much different than trading equities. When trading equities you are speculating on the value of an individual share, deciding whether there will be an increase or decrease in value. When trading the FX market, you are trading economies—one economy against

another. For instance, the EUR/NZD chart above indicates that the economy in New Zealand is getting stronger and stronger, in **relation** to the European economy. We know this because investors are selling the Euro in order to buy the New Zealand dollar. When the chart moves down, it indicates that investors are selling the base to buy the terms. When the chart moves up, it indicates that investors are buying the base and using the terms as the “funding” currency.

Trading the FX market is simply trading economies, one against another, and each pair is its own entity.

Pips are important because they hold monetary value. For each pip you collect, you receive money, each pip you give away, you lose money. The process of calculating the value of your pips is called trade sizing. You will learn this ratio in the *Risk Management* chapter.

Buy and Sell (Long and Short)

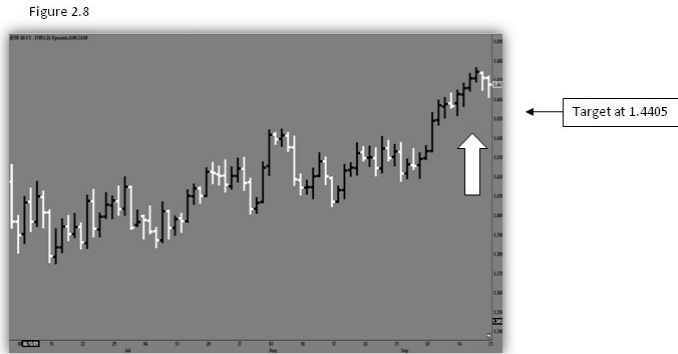
Collecting or losing pips is determined by the relationship between the type of trade you place and the subsequent movement of the market. There are two different positions you can take:

Buying, or “going long,” is an order that you place when you believe the bars on the chart are going to move up (the base will increase, you hope). When you go long, you collect every pip that the exchange rate moves up. Let’s look at the EUR/USD daily chart below, assuming that you are hoping to achieve a 150 point move. Your buy price is 1.4255.



Question: To collect 150 points, what price would the exchange rate need to *rise* to?

Answer: 1.4405 ($1.4255 + .0150$)



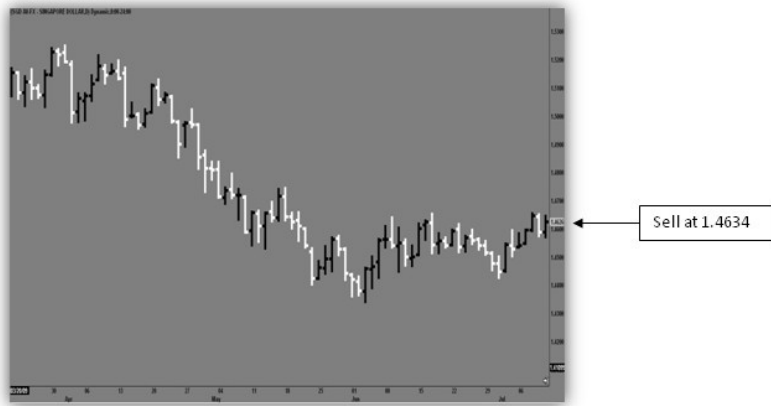
In summary if you have a technical reason to believe that the exchange rate and, therefore, the chart, is going to move up, then you enter a buy position. From there you collect every pip that the exchange rate increases by and you lose every pip that the exchange rate decreases by.

Selling, or “going short,” is an order that you place when you believe that the chart is going to fall down. When you go short you collect every pip that the exchange rate falls. Let’s look at the USD/SGD daily chart below, assuming that you are hoping to achieve a 135 point move. Your sell price is 1.4634.

Note: You do not need to have *bought* to *sell*. If that concept confuses you, then just use *long* and *short*—all you are doing is speculating on a direction, up or down.

Financial Freedom through FOREX

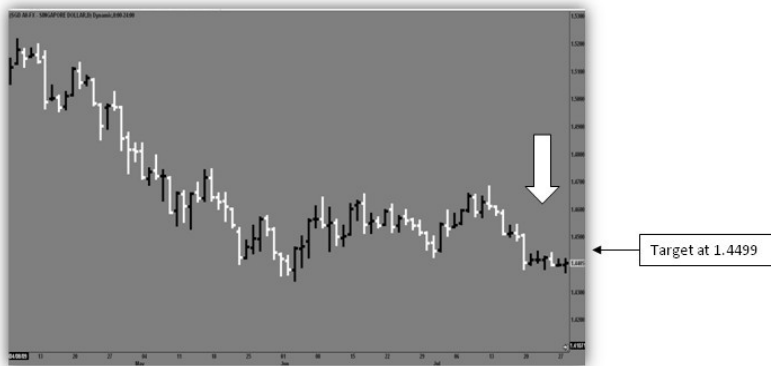
Figure 2.9



Question: To collect your 135 points, what price would the exchange rate need to **fall** to?

Answer: 1.4499 (1.4634 - .0135)

Figure 2.10



In summary, if you have a technical reason to believe that the exchange rate and, therefore, the chart is going to move down, then you enter a sell position. From there you collect every pip that the exchange rate decreases by and you lose every pip that the exchange rate increases by.

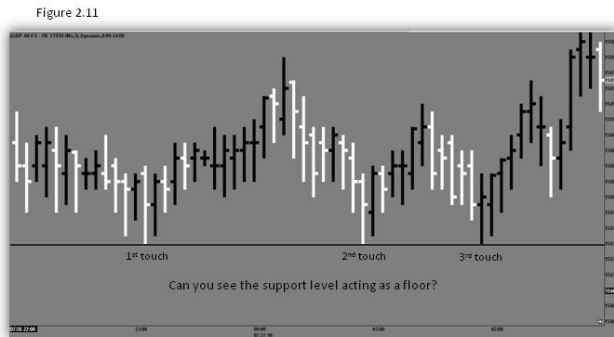
Support and Resistance

Profitable FX traders use support and resistance levels more than any other FX price level. This is because support and resistance levels are

very useful for determining heavy price movements and also provide a road map for the traders to trade within.

Support: A support level is a price that acts as a floor for the price action (black and white bars). That means that when the price falls into a support level, it is held up by it and does not fall below it—it is supported up. Support levels occur naturally in the market when the price of the currency pair becomes too cheap. Remember that a falling exchange rate indicates a sell off of the base currency as described earlier in this chapter (when the chart is down the base is down). When the base currency becomes too cheap, traders begin buying it back, which pushes the price up; buying increases the value of the currency because everyone wants it, whereas selling decreases the value of the currency because no one wants it. A support level is confirmed when this price that is too cheap is recognised by the market at least three times.

Refer to 2.11 below:



In this example, the price action has been supported three separate times at a specific price level. This means that every time the exchange rate hits this price, the market responds by buying back the base currency. This is what causes the price action to bounce off of the support level.

Now that this support level has been established, traders will trade it in one of two ways. They will either go long the very moment that the price action hits the support level in an attempt to get the most efficient entry, or they will wait for the support level to be broken and go short to catch the next move down. Either way, the support level is recognised as being

significant, and it is used to help determine entry and even exit orders for seasoned traders.

Resistance: A resistance level is a price that acts as a ceiling for the price action. That means that when the price rises into a resistance level, it is pushed down by it and does not allow it to go any higher. The price is resisted from going up any further. Resistance levels also occur naturally in the market, but unlike support levels that form when the price of the currency pair becomes too cheap, resistance levels occur when the price of the pair becomes too expensive. Remember that a rising exchange rate indicates buying the base currency, as described earlier in this chapter (when the chart is up the base is up). When the base currency gets too expensive, traders begin selling it back, which, in turn, pushes the price down. A resistance level is confirmed when this price that is “too expensive” is recognised by the market at least three times.

Refer to 2.12 below:



In this example, it is easy to see that the market is treating this specific price level as a resistance. If the price were to break up through this ceiling, it would be a strong indication of strength for the base currency and traders would begin buying (normally after the resistance level has been re-tested—more on that later!), which would contribute to the upward push.

Moving Averages

Moving averages are used to **smooth** out short-term market fluctuations to assist in highlighting longer-term trends.

The moving average will be calculated on either a simple or exponential basis.

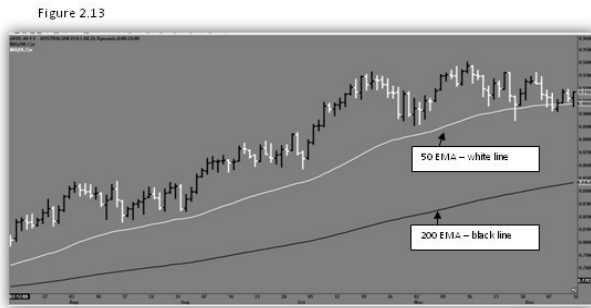
Simple moving averages calculate the average of the prices during a given period with all the periods given the *same weighting*.

Exponential moving averages **apply more weight to the recent prices** relative to the older prices and therefore reduce the lag that is common with simple moving averages.

At Learn To Trade, we always use exponential moving averages.

The **50** exponential moving average (**EMA**) and the **200 EMA** are the moving averages most commonly used to determine the trend.

If the price is above both the 50 EMA and the 200 EMA, then the trend is considered up.



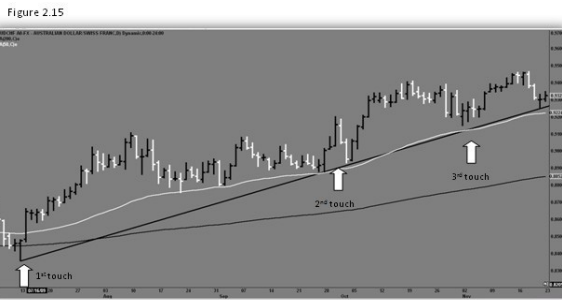
If the price is below both the 50 EMA and the 200 EMA, then the trend is considered down.



To trade using the strategies that I am going to show you, you must understand the relationship between the price and the 50 and 200 EMAs.

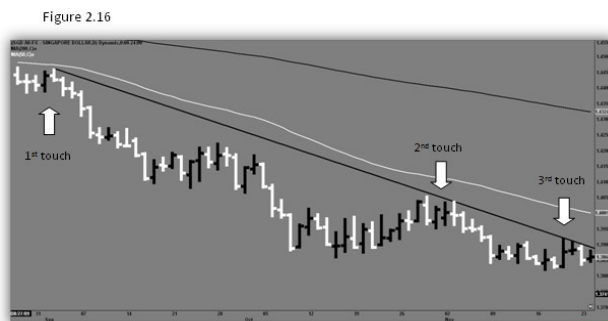
Trend Lines

A trend line allows you to establish the general direction of the price action and provides you with a guideline to trade from. To determine the **trend**, you must first know where the price is trading in relation to the 50 and 200 EMAs—either above or below. Once you have done that, you can then determine if you have a trend line that is in agreement with the moving averages. A trend line must have three touches on the price action to be in agreement. Look at the example below.



Notice the agreement between the trend line and the moving averages. The trend line is up and the price is above the 50 and 200 EMAs. This means that we trade long on this pair.

Here is an example of a downtrend with agreement between the trend line and the moving averages.



Notice the agreement between the trend line and the moving averages. The trend line is down and the price is below the 50 and 200 EMAs. This means that we trade short on this pair.

You must always know which trend is dominant on the daily chart because that is the trend that informs you whether to trade long or short.

Another function of the trend line is to allow you to determine what phase of the current price cycle you are in. This is one of the most important aspects of trading and will be covered in the section entitled Cyclicity.

Bullish and Bearish

Most people who have had some exposure to trading or investing have heard the terms “bullish” and “bearish.” These words are normally used to describe the general direction of a particular market, stock, or currency. I am going to describe both words in the context of foreign exchange.

Bullish: A bullish currency is one that is being bought by traders and investors. When a currency is bought in large quantities, the value of that particular currency increases as the supply decreases. Therefore, if the market is bullish toward the U.S. Dollar, that means traders are buying the U.S. Dollar (which means they are selling other currencies) and the value of the U.S. Dollar is going up.

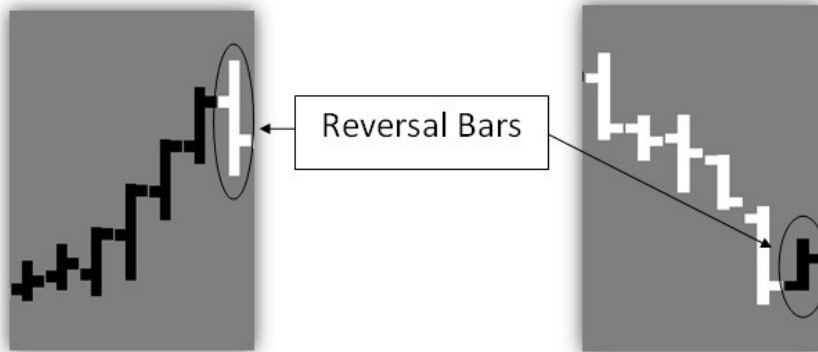
Bearish: A bearish currency is the opposite of a bullish currency. This means that the particular currency is being sold off by traders and investors (which means currencies are being bought) and the value is therefore decreasing as the supply of the bearish currency increases.

Bearish moves are normally very strong as they are fuelled by fear and anxiety in the market. Chapter 5, The Angry Bear, presents a strategy built entirely around the fast-paced movement of a sudden bearish sentiment towards the U.S. Dollar.

Reversal Bars

A reversal bar is an undersized white bar preceded by at least three black bars, or an undersized black bar preceded by at least three white bars.

Figure 2.17



Reversal bars are important because they are the first sign that there is a change of sentiment toward the currencies being traded. It is critical to know what a reversal bar is because you need this knowledge to execute trading strategies and to understand cyclicity.

Cyclicity

It is impossible to trade successfully without an understanding of price ***cyclicity***.

In this section, I am going to take you through the topic of cyclicity and give you some incredible methods to understand the natural flow of the FX market. Here, I'll give you the big picture of what is actually going on—imagine that. Just wait until you combine what you learn about cyclicity with “the bounce,” *and* a specific FX strategy! It is going to blow your mind!

Price is predictable—FACT. Anyone who disagrees with that statement does not understand the smooth rhythms of the FX market.

The moment that the full revelation of the power of cyclicity makes its way onto your trading desk is the moment when things really begin to kick off.

LUNGS, DO YOU HAVE THEM?

If you are holding this book then you must have at least one lung, and if I am writing this book then I must also have at least one lung. Why? Because we are human and humans have lungs – we need them to survive.

Question: Who is trading the FX market, machines or humans?

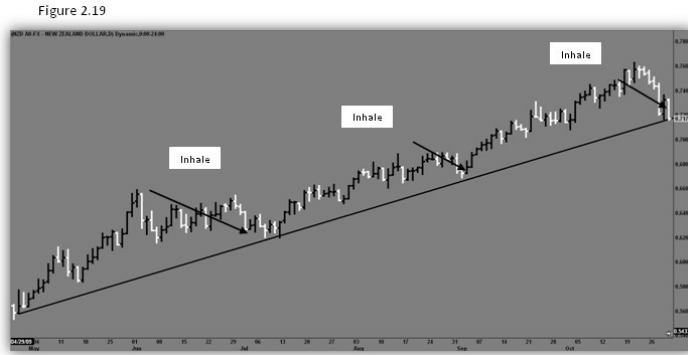
Answer: Humans

Yes, and these humans have lungs! And it is because of this that the FX market also has lungs—rather large lungs, in fact. This is just one of the phenomenal parallels that the FX market has with the individual traders who trade it. The main difference being that the lungs of the FX market do not inhale oxygen and exhale carbon dioxide; rather, they inhale sell orders and exhale buy orders (or vice versa, depending on the trend). In the same way that our bodies could not survive if we could take in oxygen but were unable to release carbon dioxide, the FX market could not survive if it could only take in buy orders without the ability to release the sell orders, and vice versa.

So how does this help you to make money?

Have you ever heard people breathing while they were in a deep sleep? If you have, then you know that it is possible to predict the end of their inhalation and the beginning of their exhalation. You can also predict the end of their exhalation and the beginning of their next inhalation. You can do this because of the natural rhythm of their breathing pattern when they are in a perfectly stable state. It is, however, very difficult to do this when people are running around out of control in a volatile, or directionless, state.

Trending pairs are stable to trade—this is the *deep sleep* breathing that makes price predictable.



In the example above you can see that the exhalation is in line with the dominant trend (the trend is your friend...), and the inhalation goes against the dominant trend (...only half of the time).

You now know that trading with the trend is profitable half of the time and the other half of the time it is not. With this understanding, we have taken a simple truth and refined it to create yet another scenario that provides you with the best environment for trading success. This concept demonstrates very clearly that profitable trading is much more about the quality of your trades and much less about the quantity of your trades.

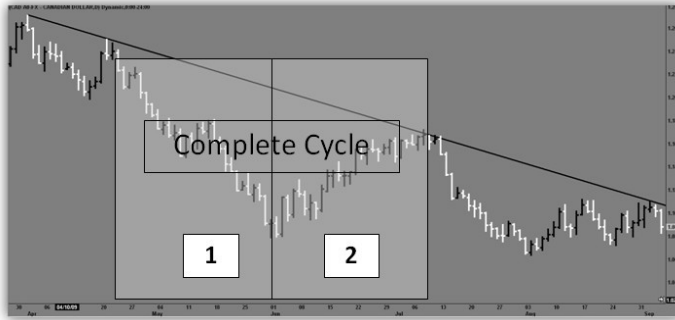
This concept can be simplified even further with our classic 1-2, 1-2 count. Phase 1 represents the exhalation and phase 2 represents the inhalation. When you combine both phases you have a complete cycle. From the examples above, it is clear that if you are going to trade with the **dominant daily trend** (which you are), then it only makes sense to trade during phase 1. Once phase 1 is finished, phase 2 begins. Phase 2 is always countertrend and certainly not your friend.

There are Two Phases in a Cycle: Phase 1 (Exhale; Friend) and Phase 2 (Inhale; Enemy)

Take a look at this example:

Financial Freedom through FOREX

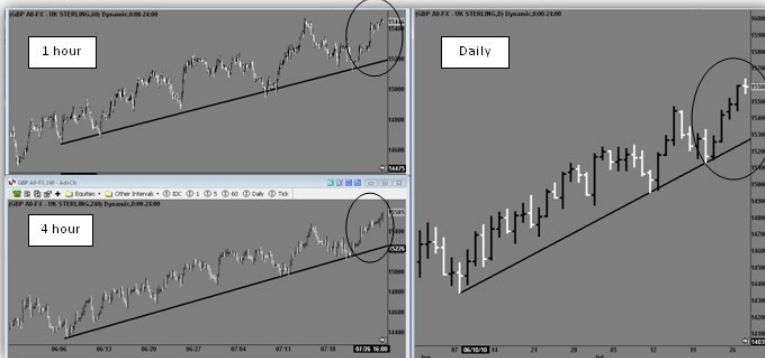
Figure 2.20



To trade successfully you need to know how to read which phase the daily chart is in. The daily chart gives you the clearest understanding of the big picture. From there you can scale down through the 4-hour and 1-hour charts to look for agreement. If all of the timeframes are in phase 1, that is a powerful signal to trade. If all of the time frames are in phase 2, that is a powerful signal not to trade.

Check out this next example of the British Pound against the U.S. Dollar (GBP/USD).

Figure 2.21



Can you see how all of the charts agree on the “push up,” which is the beginning of phase 1? This is certainly the correct phase to trade in.

What next?

By now it should be clear that you trade with the direction of the dominant daily trend. To determine the trend you simply look at the price action in relation to the 50 and 200 EMAs and then establish

whether or not you have a trend line. The next step is to understand which phase of the cycle you are **currently** in. Phase 1 is tradable, Phase 2 is not. Once you have established all of this information, you can begin to look for specific setups to place your orders around.

Question: What is the best time to enter a trade?

Answer: At the very beginning of phase 1, on “the bounce.”

Question: What is the best time to exit a trade?

Answer: At the very beginning of phase 2, on “the pull back.”

Let’s break this down. If phase 1 is the exhalation and the exhalation is in agreement with the trend, then the most suitable time to enter a position is the moment that phase 1 begins. And if phase 2 is the inhalation and the inhalation is in disagreement with the trend, the most suitable time to exit a position is the moment phase 2 begins. It comes down to this: if you can spot the changing of direction in the context of the 1-2 cycle, then you will experience massive trading success.

This all sounds great, but how do you do it? Surely, this is what everyone is trying to do—calling the high and the low. That is exactly correct, which is why we are not interested in calling the high and the low—it’s impossible. That’s why I described the best time to enter a trade as the “moment phase 1 begins,” rather than the “moment phase 2 ends.” It’s also why I described the best time to exit a trade as the “moment phase 2 begins,” rather than the “moment phase 1 ends.” In other words, it is much easier to spot the beginning of a phase than the end of one!

What does all of this mean?

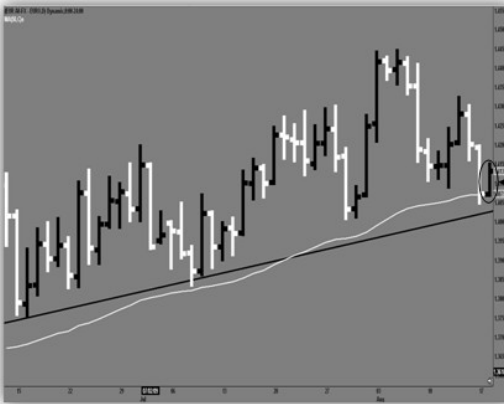
The market does not provide us with the ability to spot the exact moment that a phase or trend ends, instead it provides us with an **indication** of the beginning of a new phase. It does this by showing us a corner, or a “bounce.”

The “Bounce”

The price action will always come back to either a trend line or a moving average (sometimes the trend line is the moving average). The “bounce” is what is likely to happen once it gets there.

The first indication that a bounce is likely is when an undersized reversal bar, which is in *agreement* with the dominant daily trend, forms on the trend line. By *agreement* I mean a black undersized bar in an uptrend, or a white undersized bar in a downtrend. Take a look at the example below:

Figure 2.22



Notice that it is a black (buyers) bar in an uptrend. It is also following two larger white (sellers) bars—the pull back or inhalation. The most important thing, however, is that it is sitting on the trend line and the 50 EMA. A bounce is likely!

Let's see what happens next...

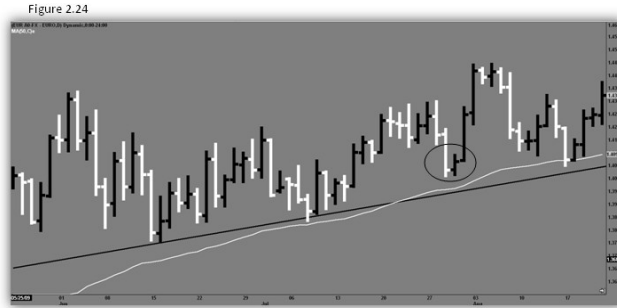
Figure 2.23



Just as expected! The price bounces off of the trend line and 50 EMA right into a buy order.

You can view the small bar as spring. The spring is pushed down very far and the trend line, as well as the moving average, provides the lower support. Once the spring is opened, you get a nice even bounce! This is the beginning of phase 1 or the exhalation—time to trade!

If you look at the same chart, you will notice another potential bounce. There is one thing missing though. Do you know what it is?



Question: Why is this potential bounce not as likely as the previous example?

Answer: Because it has not yet pulled back to the trend line or moving average!

Now, you may look at this chart and point out that there is a nice 350 point move that could have been easily traded at a nice 3:1 reward-to-risk ratio. Maybe so, but when you are trading you must have some rules! The purpose of this book is to show you the trading setups with the highest probability of success. A reversal bar sitting on, or even just below, the support for the spring will be far more successful than one that has not yet reached it! Remember: quality over quantity.

You may have also noticed that the small reversal bars in the above examples followed large white bars. Those white bars represent the market inhalation, which is the profit-taking from the previous long position. Recalling the analogy of the lungs wherein the market inhales to sell orders and exhales to buy orders (in an uptrend), these little reversal bars indicate that the buy orders are beginning and phase 1 is underway. As you can see, this is very easy to spot in a stable, trending market.

Think of it like this:

In an uptrend, the buyers are pushing the market up. At some point, the buyers need to collect profit and exit the buy trades. To exit a buy trade you must sell. So, when the investors who control the market (big money—really, really, big money) begin selling, the market corrects and retraces back to the trend line. Now, people are greedy and investors want more! They will try to duplicate the exact scenario that just generated huge profit. This is why a stable, trending market creates similar-sized cycles—it is an attempt by the market to recreate a profit-making setup. The private trader has the opportunity to see these cycles forming and cash in on the predictability of the movement.

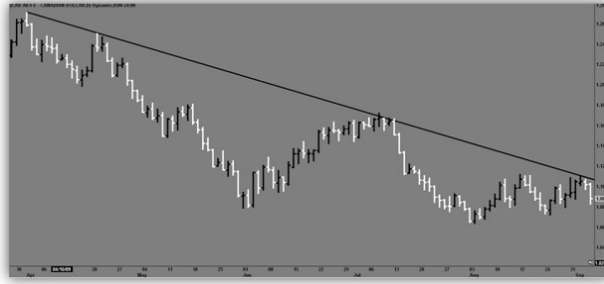
Question: Are you getting really excited yet?

Answer: _____

A downtrend works exactly the same way—just in the opposite direction. The large money is selling, but only until the profit-taking begins and then the buying kicks in. This causes the exchange rate to retrace back to the trend line. At this point, the selling begins again in an attempt to generate more profit and recreate the last successful trading cycle.

Note: when the cycles begin to tighten up, much like we see in the USD/CAD chart below, we learn other very useful information. In this example, the sellers are in control of the pair, so the chart is pushing down. Notice that the phases, and therefore the cycles, are beginning to shrink in depth and length. The message here is that the profit-taking is occurring much faster than normal because of the uncertainty about the future direction of the currency pair. Investors are no longer willing to wait as long before they cash in and take their profits.

Figure 2.25



Cyclicality is what makes the price predictable and predictable price is what provides reliable trading setups. If you can become a master of the cycle, you can make big money in the FX market.

Trading the Small Bars (and Why Amateurs Don't)

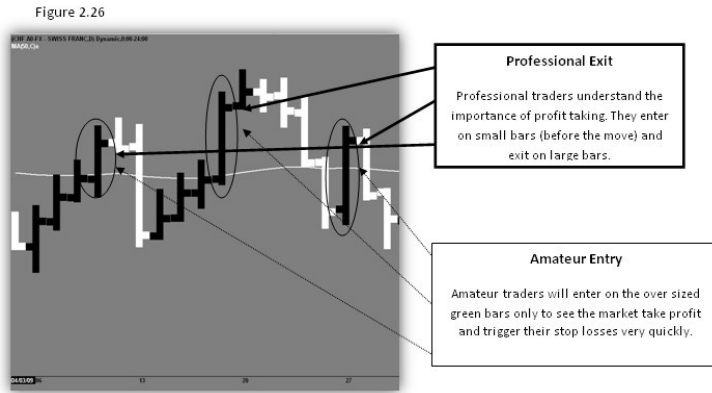
One of the most common mistakes an amateur trader makes is trading off an oversized bar. An oversized bar must be seen as the move itself and not the entry for the move. For instance, amateurs will look at very large up, or black, bars to give them the certainty, or “proof,” they *need* before entering long positions. The problem with this is that, once the bar pushes up a significant amount, the next move is likely to be down—large buying will be ended by quick selling!

Think about this in terms of cyclicality. When buyers push the chart up very quickly, they are planning to take profit at some point, which means at some point they must sell. The selling then pushes the chart back down and triggers all the stop loss orders of the amateur traders who are forced to exit with a loss.

Professionals get richer and amateurs get poorer.

Let me show you an example from the daily chart of the USD/CHF.

Financial Freedom through FOREX



Can you see that the successful traders are leaving the market as the amateurs are entering it? This happens every single day!

Isn't this interesting? The amateurs are exactly wrong!

So why don't the amateurs recognise their error and change their approach? It obviously doesn't make sense to enter into a position after the market has already moved. So why does it happen time and time again? The answer is simple, but it goes far beyond trading and chart interpretation. It invites us to look deep into our very makeup as humans. It's called "social proof."

Social Proof

The definition of social proof explains that, "one means we use to determine what is correct is to find out what other people think is correct" (Cialdini, *The Psychology of Influence and Persuasion*, HarperCollins Publishers)

As humans, social proof influences the majority of our decisions. This is not necessarily a bad thing. Most of the time, social proof assists us in making decisions which might otherwise be very difficult and time consuming. Let me share an example with you.

At Learn To Trade we teach trading, money management, and wealth building programs all over the world. Sometimes we travel as far as New Zealand; other times we stay closer to home. Personally, I get very

confused when I visit a new airport. I never know where to go to get my luggage. I normally stand still for a few moments wondering which direction to walk before I revert to social proof. It is then that I look around me, find out where everyone else is walking, and begin to follow. I don't even know these people, but I believe that if they are *all* walking in a particular direction, then it must be the right way to go—and it is! I follow the crowd and I end up being led directly to my luggage. As I said earlier, social proof is normally a good thing, like in this type of situation. There are, however, times when it is not beneficial to look for social proof, like when it comes to your personal finances. Then relying on social proof can actually be devastating! Let me show you what I mean:

When it comes to investing, trading, or even the handling of personal financial matters, the average person lacks confidence and certainty. Because of this, they naturally look for social proof. This is why the amateur traders wait to see the price move a long way before they enter a position—whether they want to admit it or not, they have no confidence in their ability to accurately predict price movement, instead they wait to see what “everyone else” is doing. By doing this, they exchange efficient and objective entry positions for emotional security and social proof.

It takes a confident trader, who is not concerned with the noise of the crowd, to buy into a sell off or to sell in to a buy off—this is professional trading! And remember, scared money never makes money.

The environment where the need for social proof thrives is one of uncertainty. Think about it like this: if you know the correct thing to do, you do not need to follow what other people are doing. Chances are, you may not even notice what others are doing. If, however, you feel uncertain, you naturally look to the crowds to show you what action to take. It is just like me at the airport. If I were certain about where to go, then I wouldn't look to others for direction; but, because I am uncertain, I follow the crowd.

Studies by psychologists have shown that only 5% of the population are **initiators** whereas the remaining 95% of the population are **imitators**. In other words, only a small percentage of people make things happen,

the rest simply *wait* to see *what* happens. This is why only a small percentage of the population are wealthy and the rest are not.

There is no money in **imitation**; it is all in **initiation**. Initiators are action takers! This is a financial principle that can be seen very clearly in the FX market.

Money is made when you have the confidence to trade the move before it happens, not after it has come and gone. This is how we trade at Learn To Trade—with certainty and confidence. This is possible because our strategies and principles model what professional money is doing. Allow us, through this book, or through one of our programs (www.learntotrade.com.au), to equip you with the confidence and certainty to be an initiator, because that is where all the money is.

Chapter 3

RISK MANAGEMENT

Chapter Objectives:

- * Understand why risk management is essential for professional trading
- * Understand the benefits and risks of leverage
- * Understand how to accurately “trade size” a position and determine your reward-to-risk ratio

The Most Important Facts about Trading

You must have money to trade!

Question: *What happens to your ability to trade if you lose all of your money?*

Answer: *You are no longer able to trade.*

Question: What happens to your ability to **generate a profit** if you lose some of your **money**?

Answer: Your ability to generate profit decreases **in line with what you lose.**

The less money you lose, the more money you can make...

So, given the fact that you must have money to trade, and that your ability to earn decreases when you lose money and increases when you generate money, it's logical to conclude that the more money you have, the more money you can make. From a risk management perspective, you could say it like this: **The less money you lose, the more money you can make.** It is essential that this concept is understood in relation to funding your trading account. Here is a simple way to remember it:

Capital Preservation → Income Generation

Too many people believe that the way to profitable trading is through monster-size winning trades. The problem is that huge winnings generally involve huge risks, and this is not a sustainable form of profit generation or the way a professional trading account should be managed. This type of trading puts you on a rollercoaster that grips your emotions and can leave you feeling deflated with little or no money.

Don't get me wrong, huge returns are great and you can expect to see them in your trading account if you stick to the rules in this book. But you have to keep yourself in the game long enough to seize these extraordinary opportunities when they arise, and that can only be achieved through proper risk management.

Principle: Large amounts of money are only made when small amounts of money are risked.

Let me give you a real life example from one of our students at Learn To Trade:

I'll never forget seeing this man come running over to me, erupting with energy and excitement.

"I have more than doubled my account!" he shouted, "And I have done it in just one week!"

He then went on to explain that not only had he doubled his account in one week, but that this was his first week of trading. You can just imagine his excitement and enthusiasm. He was completely bursting. At the beginning of the week he had \$5,000 in his trading account and he now had over \$12,000. That is a 240% return in one week! That's awesome, right?

My response shocked him.

"That is far too much, you have done something wrong," I said very carefully.

Now, before we go any further, you must understand that at Learn To Trade we embrace enthusiasm and we especially love to hear about huge returns for our graduates. Not only that, these things are common. This level of growth in one week, however, is not sustainable, real growth, and that is what we want. This type of trading is nothing more than gambling on the market.

I went on to explain to him that if he continues to trade like this, he will not only lose the \$7,000 he just made, but he will also lose the \$5,000 that he started with. He did not want this to happen and he graciously took my advice.

The truth is this: within that first week, his account was either going to grow at an outrageous rate or disappear at an alarming speed. It was only a matter of time until his luck, along with his money, would run out. This amount of uncertainty is unnecessary and unproductive. This type of trading just doesn't work.

IMPORTANT POINT: The money in your trading account is what allows you to control or leverage positions in the FX market. Due to the liquidity of this market, you can create large positions through the available leverage. This is good, but it can be deadly.

Side note: Too many FX trading accounts are blown out, or never get a fair chance to get started, due to underfunding and lack of commitment. For instance, a 2% increase on a \$100,000 trading account is \$1,000, whereas a 2% increase on a \$1,000 trading account is only \$10. This is a massive difference and will psychologically impact the individual who is trading. If winning trades equate to only \$10, the likelihood of persevering and sticking to the money management rules decreases. This is because the winning trades do not have the immediate power to enhance your lifestyle, and the losses are all so small that there is a natural tendency to increase risk. The interesting point is that a 2% increase on either trading account is likely to come from the exact same trade setup. The difference, obviously, is the size of the account. This is

not to say that it is impossible to grow a small account into a larger account. You just have to start small in order to finish BIG!

Leverage

Leverage. What is it and how do you use it to *increase* rather than decrease your trading account? Only certain aspects of leverage are really necessary to understand. What is important is that you understand how to utilise it for your benefit. There are plenty of complex definitions of leverage, but the simplest (best) definition is this:

Leverage is the ability to trade as if you have more capital than you actually have.

Leverage gives you the power to control positions in the market that are much greater than your current capital position. You can also think of leverage like a large ship. The ship, in its entirety, is very large, yet the direction that it moves is controlled by a relatively tiny wheel.

The small wheel controls the direction and ***destination*** of the larger ship.

Your capital controls the direction and ***destination*** of the larger market position.

Possibly the most familiar type of leveraged financial contract is a mortgage. When you buy a house you are creating or opening a position in the housing market. Let's assume you pay \$500,000 for a house. You have opened a \$500,000 position in the housing market. Now, unless you bought the house with \$500,000 cash, you probably used a mortgage to leverage your deposit (capital) and to enhance the size of your position in the housing market. The scenario looks like this:

<p>\$500,000 housing market position/cost of house</p> <p>\$50,000 Deposit (10% of purchase price)</p> <p>\$450,000 mortgage required</p> <p>10:1 Leverage</p>

The mortgage finance allows you to complete the transaction by only depositing 10% of the true capital required to buy the home. Therefore, because of the mortgage, you are now controlling a \$500,000 position with a deposit of only \$50,000. In other words, you are controlling 100% of the position with only 10% of the capital—a 10:1 leverage position.

The small wheel is controlling the direction and **destination** of the larger ship.

Your capital controls the direction and **destination** of the larger market position.

All FX brokers offer plenty of leverage to their clients. The usual amount of leverage available is 100:1. (Some brokers will even offer up to 500:1 leverage—this is crazy!) 100:1 leverage means that you can trade as if you have 100 times the amount of capital that you actually hold.

Question: If leverage allows you to trade as if you have 100 times the amount of capital that you actually have, how much faster can you make money?

Answer: 100 times faster! (Is this good or *great*?)

Question: If leverage allows you to trade as if you have 100 times the amount of capital that you actually have, how much faster can you lose money?

Answer: 100 times faster! (Is this bad or *terrible*?)

Think about the effect that leverage has on your profit or loss within the home purchase example from before. You should be able to recognise

very quickly that it only takes small percentage movements in the housing market to dramatically impact the profit or loss on your initial investment of \$50,000.

Let's consider a 10% increase in the value of your property over 12 months. The property is now worth \$550,000.

What is your return on the \$50,000 invested?

100%! Yes! You invested \$50,000 of your own capital and, because of the leverage, you were able to open a position ten times the size of that. Therefore, every 10% movement in the value of your home is multiplied by 10—10:1 leverage. This is great when the market moves in the desired direction. Unfortunately, the market sometimes moves against you. Had the property dropped in value by 10%, it would only be worth \$450,000, resulting in a complete loss of the original investment.

Keep in mind that this example is only leveraged at 10:1. In the FX market we are afforded much greater leverage than that—even 100:1!

Imagine being able to control a \$1,000,000 position with just \$10,000 or a \$10,000,000 position with only \$100,000. This is serious business for serious traders because serious money is at stake. Now imagine all of those traders who have not invested the time or money into learning how to responsibly handle and manage their trading accounts. What results do they achieve? The answer is obvious. Unfortunately, as professional traders and trading coaches, we meet these people all of the time. Some people refuse to get serious and really learn how to trade. They then proceed to blindly jump into the most dynamic financial market the world has ever known and then wonder why they end up bust. To do this just doesn't make sense. The leverage is too great.

New traders will generally accept the implications of leverage in one of two ways: with **love and faith** or with **hate and fear**. The truth is, we need to be far less extreme than that and have a mixture, or balance, of the two.

Love and Faith

Amateur traders who love leverage strongly believe that leverage loves them back. And, not only that, they believe that leverage will always work for them. This is a very romantic way to consider the power of leverage and will result in an empty trading account. With this approach there is no respect or reverence for leverage or the market, only a wish and a hope of getting rich quick. It doesn't work that way.

Hate and Fear

Amateur traders who completely fear leverage are missing out on its benefits. They believe that leverage is there to punish them. There is also a massive lack of confidence and belief in their pursuit of financial independence through trading. It is because of this that they never grow their account. Instead, they live out a completely timid and unproductive trading experience.

BALANCE

The fact is, you need to trade with a healthy balance of ***faith*** and ***fear***. Understand that trading in this market with strategies that work can generate large amounts of cash, but this kind of trading also comes with risks. Getting this type of balance is only possible by adhering to the money management strategies.

GREAT, AND...

This is all very exciting, but with no practical way to implement these principles it will be of no use to you. We need a system of getting the information from this book straight into your trading account. Can you imagine having a tool that automatically gives you the exact balance required to trade and totally transfers the focus from leverage and risk to consistency and sustainability? Would you consider this worth knowing? Yes, of course! The solution is **trade sizing!** This is a practical aspect of trading that will help make your **dreams come true!**

Trade sizing is the most effective way to make it difficult to lose money, yet possible to make big money. It minimises losses and assists in creating real, sustainable income. If you don't trade size accurately you will not be a successful trader. It is as simple as that. However, before we look at the exact method of trade sizing, we need to further explore a remarkable truth about trading. This is a truth that is completely unknown to amateur traders and completely understood by professionals.

The Money You Lose Is Harder to Get Back—FACT!

How can this be? Let's look at an example:

Assume that you are trading with a \$100,000 account. Unfortunately, you place

...The money you lose is harder to get back!

several losing trades that bring your account down to \$90,000. This is a 10% loss on your account ($\$100,000 - 10\% = \$90,000$). It is important to remember that your trading success or failure is always measured in percentage earned or lost—just like any other fund or investment. So you are now 10% down on your original \$100,000 account. No problem, all you need to do is get the 10% back, right? WRONG. 10% of \$90,000 (your new account balance) will *not* restore you to your initial account balance. A 10% increase in your account will only get you back to \$99,000 ($\$90,000 + 10\%$). You must earn 11.1% on your account balance of \$90,000 to bring the account back up to \$100,000 ($\$99,000 + 11.1\% = \$100,000$). The fact is, the more money you lose, the more difficult it becomes to get back to breaking even. This is the negative power of an account compounding in the wrong direction. (We will look at the positive power of compounding our trading accounts in a later chapter, as well as how a successful trading account will grow exponentially).

Question: If you were to lose 50% of your account, what percentage increase would you need to achieve to bring you back to even?

Answer: 100%

Question: If you were to lose 80% of your account, what percentage increase would you need to achieve to bring you back to even?

Answer: 400%

Check it out below!

Initial trading investment \$100,000 – 50% in losses = new balance of \$50,000. To increase your new account balance back to your original balance you must double it (a 100% increase!).

This is not meant to scare you away from trading; this is meant to direct you into professional account management.

As stated above the purpose of this chapter is to create a sound, secure approach to risk managing your account. The information contained in this chapter so far has shown you why risk management is essential: real money is at stake and can be lost quickly.

2% Maximum Account Risk per Trade

The key to exercising proper risk management *consistently* is to use an objective method of determining risk. To do this, you must know the **Golden Rule: 2% Max Risk per Trade.**

You should never risk more than 2% of your trading account on any single trade! If you are trading with a \$100,000 account, your maximum risk on the trade is \$1,000 ($\$100,000 \times 1\%$).

Why 1%?

Question: If you are risking 2% of your account balance per trade, how many consecutive trades must you lose to completely wipe out your account?

Before you answer, have a look at this example:

Let's say that you are trading with a \$100,000 account and you lose on ten consecutive trades (if you finish this book, this is very unlikely to happen to you). With a 2% account risk you may expect your account to be down 10%, but let's look at the true result:

Financial Freedom through FOREX

Trade 1:	$\$100,000 - 2\% = \$98,000$
Trade 2:	$\$99,000 - 2\% = \$97,020$
Trade 3:	$\$98,010 - 2\% = \$96,049.80$
Trade 4:	$\$97,029.90 - 2\% = \$95,148.102$
Trade 5:	$\$96,059.60 - 2\% = \$94,138.408$
Trade 6:	$\$95,099.01 - 2\% = \$93,197.02$
Trade 7:	$\$94,148.01 - 2\% = \$93,206.53$
Trade 8:	$\$93,206.53 - 2\% = \$92,274.47$
Trade 9:	$\$92,274.47 - 2\% = \$90,428.98$
Trade 10:	$\$91,351.72 - 2\% = \$89,524.68$

Now before you give your answer to the question above, consider the trend over the ten losing trades with the 2% risk.

Answer: It never happens!

Exactly right! With a 2% risk, it is physically impossible to lose all of the money in your trading account. This is wonderful because we understand that we must have money to trade, and here we are making sure that we can never lose all of our money. It is also one of the reasons why it is so important to manage your account, wins and losses, in terms of percentages instead of just figures. For instance, I often see amateur traders managing their risk basis on nothing more than a particular amount of money, such as \$2,500 per trade. The problem with this style of risk management comes when the account is trading at around \$25,000. It is utter madness to risk 10% of the total account balance on a single FX trade, especially when there is certainly no guarantee of success. It is mandatory that we create a system in which every time there is a loss the amount of money that is at risk on the following trade diminishes in line with the account balance. This is the basis of our risk management setup. As the account decreases, the risk decreases (remember, Capital Preservation → Income Generation, and large amounts of money are only made when small amounts of money are risked). Conversely, as the account increases, the opportunity and ability to generate profit increase with every single trade—it is literally the best of both worlds, and it puts you in the best possible position for trading success!

Amateur traders get this risk management thing wrong all the time. They ask themselves, “How much money can I make on this trade?” and focus on potential profits, rather than the important question, which is, “How much money can I afford to lose on this trade?”

Successful traders use the power of negative thinking! In other words, we go into every trade *expecting* to lose! And we manage it from there!

That is why the majority of amateur traders lose money—quickly! They turn their trading desk into a gambling den. If you become a gambler, you will come to the natural conclusion rather quickly that the “house always wins.” If you allow yourself, however, to mature into a professional, patient, and successful trader, you will come to the natural conclusion that much is possible and that this trading stuff really works!

There is one rather striking similarity between professional FX traders and professional black jack players—risk management/trade sizing.

Most people don't realise this, but a successful black jack player will only ever risk 2% maximum of his current balance per hand. These players understand the sensational effects of compounding numbers and the consequences of doubling and tripling up, as well as the negative impact of “revenge trading.” Players who are doubling and tripling up, or trading from a mind set or *position* of revenge, are not in control of their situation. Far from it, they are emotionally driven and they create an environment that quashes their ability to think and play objectively. Risking more after a losing hand or trade is the first sign that a player, or trader, is no longer losing only money but is also losing the most important battle of all, the battle of the mind. This is seriously dangerous ground, because there is now a shift from a proactive approach (in control), to a reactive approach (out of control) and a move from order to chaos. The player begins to feel as though the table, or market, **owes** them something. The reality is that it does not—winning or losing is never personal, it is just feedback based on your actions.

Risking more after a losing hand/trade is the first sign that a player is no longer losing only money, but is also losing the most important battle of all, the battle of the mind.

The professional trader understands logically and objectively that the best way to recoup lost money, or just simply make money, is to decrease risk during losing periods and increase earning potential as the account balance grows. This is done by remaining in control and continuing to do the things that have proven to be successful in the past. Does this make sense? The problem is that, when money is on the table, it becomes very difficult to do things that make sense in your head, and much easier to do things that “make sense” in your gut.

Question: Which would you rather do your thinking with? Please circle your answer below.

Head

or

Gut



I am assuming you have chosen to think with your head. Good choice. Now let's look at the practical application of risk management and how we implement our 2% risk rule through *trade sizing*.

Trading Sizing

Trade sizing is the process of determining the value of the pip or basis points you are trading. The ratio itself looks like this:

$$\frac{\text{Account Risk (AR)}}{\text{Trade Risk (TR)}} = \text{Trade Size (Pip/Point Value)}$$

Now that you know how the ratio is arranged, the next step is to understand where to find the account risk and the trade risk so that you can plug them into the ratio. To do this, we are going to go through a couple of practical examples using typical trades. We will do the first example together.

Example number 1: Account Balance of \$100,000

Account Risk

The **account risk** is simply the amount of money from your **account** that you are prepared to **risk** on the trade. You already know that your maximum risk on a single trade is 1%. The easiest way to find the account risk is to take your account and multiply it by 1%.

\$100,000 x 2% = \$2000. This is your **account risk (AR)**.

Once our account risk is determined, we move on to find our **trade risk**.

Trade Risk

The trade risk is the number of points that a particular **trade** has at **risk**. It is worked out like this:

Stop Loss – Entry = Trade Risk

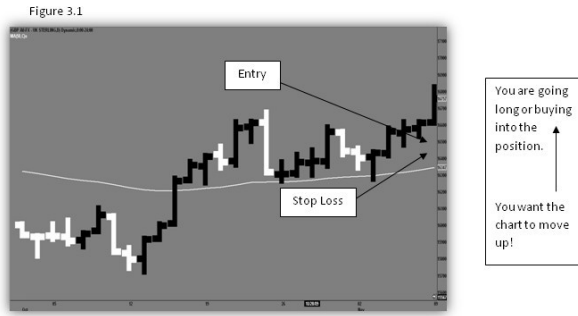
Example 1:

Long Position on GBP/USD (Cable)

Entry: 1.6500

Stop Loss: 1.6450

Financial Freedom through FOREX



The Long position suggests that you want the price to move up from 1.6500 to 1.6501, 1.6502, 1.6503, and so on. The Stop Loss is placed lower than 1.6500 because if the price begins to fall, you begin losing money.

Question: What is the trade risk?

Answer: 50 points (1.6500 Entry – 1.6450 Stop Loss)

Based on the example account size of \$100,000 and the information above, you can now implement the 2% rule and work out the trade sizing ratio.

$$\begin{aligned} \text{Account Risk (AR)} &= \$1000 (\$100,000 \times 1\%) \\ &= \$20 \text{ Per Point} \\ \text{Trade Risk (TR)} &= 50 \text{ points } (1.6500 - 1.6450) \end{aligned}$$

This means that for every point that the exchange rate moves in your favour you receive \$20 and for every point the exchange rate moves against you, you lose \$20.

Question: If the exchange rate moved in your favour 100 points at \$20 per point, what would your profit be?

Answer: \$2000 (100 x \$20 per point)

Question: If the exchange rate moved against you 50 points (which is your total trade risk) how much money would you lose?

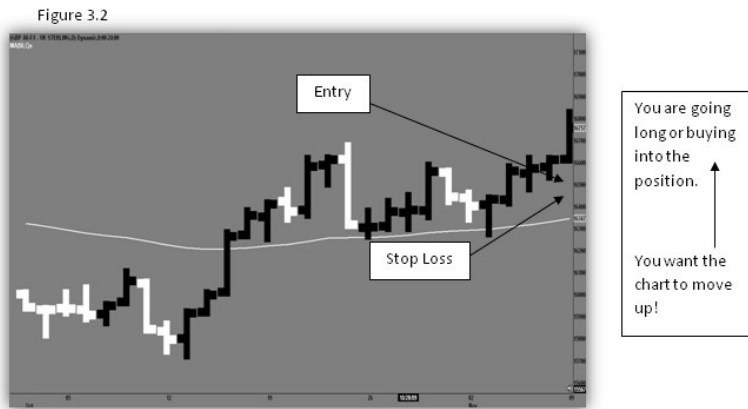
Answer: \$1000 (50 x \$20 per point) and \$2000 is 2% of your total account which is your maximum risk!

Can you see how this works?

What you have actually done is taken the amount of your account that you are comfortable to risk (1%) and broken it up into the number of points that you are prepared to risk. By doing this, you have ensured that if you lose on a trade, which is to lose the points that you risked, you have lost only 2% of your account.

Let's do another example to make sure you can implement the trade sizing ratio. Remember, all you need to do is take your **account risk** (the amount of money you are risking on the trade) and divide it by the **trade risk** (the amount of points you are risking on the trade).

Example 2: Account Balance of \$155,000



Long (Buy) Entry Price: 1.6600

Stop Loss: 1.6575

With this information, you should now be able to trade size your position!

Account Risk =

Trade Risk =

What is your trade size (point value)?

Reward to Risk Ratio

The purpose of the reward-to-risk ratio is to determine whether or not a trade is worthy of you risking your 1%. The minimum reward-to-risk ratio required to enter a position is 1:1.

Reward: Risk Must Be a Minimum of 1:1—Set in Stone.

Never risk 2% of your account unless your target or take-profit limit will provide you with at least a 2% reward.

Ask yourself this question:

“Does it make sense to risk 2% for the possibility of earning less than 2%?”

The answer is *no!* You would be surprised, however, to discover how easy it is to do something so senseless in the heat of the moment. This is why you must plan ahead and have rules **before** you enter a trade, when you have not yet emotionally and financially invested into it.

The reward: risk ratio is also there to protect your account. If you consistently risk more on trades than you expect to achieve, the losing trades will not only wipe out the winning trades, but they will also eat into the original capital invested—this is obviously not the goal! You need to flip that around so that the winning trades are always **at least** as great as the losing trades. By doing this your winning trades will not only wipe out the losing trades, but they will also grow your original capital invested—this obviously is the goal, wouldn't you agree?

In accordance with the reward-to-risk ratio of 1:1, your losing trades decrease your account by a maximum of 2% whereas your winning trades increase your account by a minimum of 1%. This sounds like a recipe for success!

So, how do you work out this reward-to-risk ratio? The easiest way to work it out is to forget about the reward and risk in terms of money and think of them in points instead. By doing this, you simply need to

determine whether a winning trade will add at least as many points to your account as a losing trade would deduct.

$$\frac{\text{Reward (Points)}}{\text{Risk (Points)}} = \text{Reward-to-Risk Ratio}$$

You should also recognise that the **risk** element of this ratio is exactly the same as the trade risk of the ratio used to determine your point value. So, once you have your trade risk for the first ratio, you are already halfway through completing your second ratio.

Reward (Points) = Target – Entry

Risk (Points) = Stop Loss – Entry

Let's look at the first example we used above, only this time we are going to assume a target price as well. It is important to remember that, at this stage, we are just using random prices on the chart to illustrate the process of determining the ratio. In the second portion of the book we will be explaining why and where we are placing our orders.

Figure 3.3



Example:

Long Position on GBP/USD (Cable)

Entry: 1.6500
Stop Loss: 1.6450
Target Limit: 1.6700

$$\frac{\text{Reward (Points)} = 200 \text{ Points } (1.6700 - 1.6500)}{\text{Risk (Points)} = 50 \text{ Points } (1.6450 - 1.6500)}$$

4 : 1

In the example, the reward-to-risk ratio is 4:1.

Question: Is 4:1 better than 1:1?

Answer: Yes! Remember, you need a minimum of 1:1, anything above this is a bonus.

In this example, a winning trade has the potential to increase your account by a huge 4%, whereas a losing trade will only decrease your account by 1%. All things being equal, winning on this trade will pay for your last four losses! The point here is that, although the 1:1 must be achieved before you enter the trade, the more setups you have with a greater than 1:1 reward-to-risk ratio the better.

Check this out!

Assume that you have a \$100,000 trading account and you place ten trades into the market at exactly the same time. Let's also assume that your reward to risk ratio is 3:1 on each of these trades. This means that you lose \$1,000 (1%) on each of the losing trades, and profit \$3000 (3%) on each of the winning trades.

Results:

Trade 1	- 1000
Trade 2	- 1000
Trade 3	- 1000
Trade 4	+ 3000
Trade 5	- 1000

Trade 6	– 1000
Trade 7	+ 3000
Trade 8	– 1000
Trade 9	+ 3000
Trade 10	– 1000
Total Losses	– 7000
Total Wins	+ 9000
Bottom Line	+ 2000

You have only won on 30% of your trades, but you have increased your account size by \$2000, which is 2%. This is tremendous!

Let's give this some context. If you can manage to place ten trades per month at a 3:1 reward-to-risk ratio and achieve even a poor success rate of 30%, the annual simple interest return on your capital would be 24% ($\$100,000 + 24\% = \$124,000$). But there's more. If you allowed the account to grow for a year, the compound interest would provide an even larger return of over 29% ($\$129,360.66$). This is the effect of interest on interest, which we are going to talk about in greater detail later in the book.

This should give you just a tiny glimpse at how the implementation of something which is so simple—yet so effective—can totally revolutionise the results in your trading account! Just wait until we get to the actual strategies....

You may be slightly confused as to why I have suddenly jumped from 1:1 to an example of 3:1. I have done this to dramatically emphasise the point that a reward-to-risk ratio of 1:1 is only the minimum requirement to trade and that, by spotting trading opportunities that provide you with a reward-to-risk ratio of greater than 1:1, your account will grow even faster!

Before your profits can pay you an income, they must pay for your losses.

A Quick Recap of the Two Significant Ratios

Let's summarise how each of the above ratios enhances your trading experience.

Trade sizing: this simply determines the value of your "point." This ratio is based on the two most important things: the trade setup and the size of your account. It is massively important to trade size every time because it eliminates temptations that are common to all traders, and it stops you from doing things like this:

"Man, *I feel good today* and I have won on my last five trades! I am going in at **\$100** a point on this one, baby, yeah!" You do this only to watch the trade go directly against you for a large percentage loss that claims the profits of your last five successful trades—this is gambling.

The other side looks like this:

"Aww, things have not been going my way lately. I have not only had a bad day at work, but the traffic was terrible coming home. I really want this trading thing to work, but I have lost on my last three trades. Maybe I should just go in at **\$1** a point because I am not **feeling very confident right now.**" You do this only to watch the trade move straight into your take-profit order. The only problem is, your point wasn't worth anything, and a trade that should have recovered a large portion of your last three losers hardly impacts your trading account—this is gambling.

Gambling on a trading account can be defined as making **subjective** decisions based only on **emotions created by circumstances**, instead of **objective** decisions based purely on trade **setup and account size**.

Strategic-based trading = objective and consistent

Gambling-based trading = subjective and sporadic

Reward-to-risk ratio: The purpose of this ratio is to make it very clear whether or not the trade is worth entering. It makes it possible for your winning trades to cover your losses and pay you an income.

A common misconception is that you must be a mathematical genius to be a successful trader. This is definitely not true as you can see from these two simple ratios. It is true that there are other aspects of trading that require some basic mathematics, but these can all be computed on a simple spreadsheet. Once you understand how to work out the two ratios above, all of the math is done!

Chapter 4

THE PROFITABLE PROCESS

Chapter Objectives:

- * Understand the principles of trading within the triangle
- * Understand the difference between flexible and chaotic trading
- * Integrate these two trading philosophies into your daily trading routine

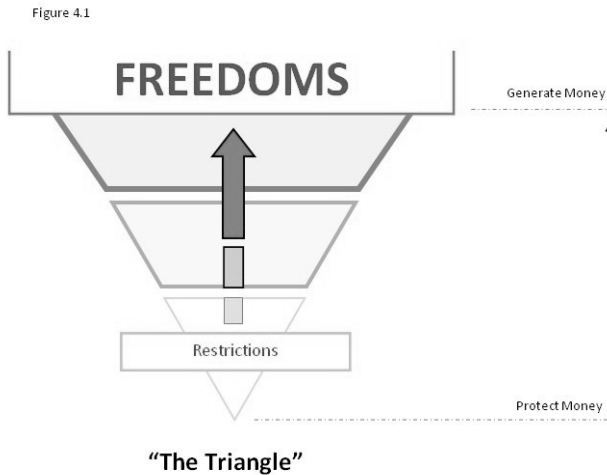
Trading within the Triangle – Creating Real Income and Sustainable Growth

The goal of all successful FX traders is to create real and sustainable profit on a consistent basis. Unfortunately, most traders who begin the journey of trading the FX market never reach this goal. The crazy thing is that most people do not fail because their strategies are bad. Instead, they fail because they lack structure in their approach to trading.

Defining the long term structure of your approach to trading puts you in a secure position and enlarges your probability of success. This is why, at Learn To Trade, we teach our students how to “trade within the triangle.”

Trading within the triangle is the most suitable way to grow your trading seed capital. It minimises frustration and encourages a natural maturity within your long term trading experience. The maturity comes first from a respect for the rules of a strategy, and then through the understanding of the purpose and the principles that the strategy is based upon. Once you understand that, you can introduce discretion to your trading to catch more moves in the market than the basic rules of the strategy would normally allow. The important point, however, is that before there is discretion, there must first be a complete reliance on the rules.

Let me show you an illustration to help demonstrate this point:



As you look at the illustration of the triangle, notice that you are moving from "restrictions" to "freedoms" and not the other way around. This type of structure allows your trading to evolve methodically and naturally. It also removes the burden of trying to "get rich quick" and takes you out of crisis-style trading, which suggests that you need to make a fortune immediately.

Consistency is the key. By trading within the restrictions of the rules consistently, you will begin to develop a very strong understanding of the core principles of the rules. Once you understand why the rules are what they are, you will then, gradually, be able to take certain freedoms and liberties outside of the rules for larger, more professional profits.

A successful journey up through the triangle requires strong consistency in two major areas:

Consistency of Strategy

One of the biggest mistakes that traders make is trying to learn how to trade too many different strategies at the same time. They do this with the belief that more strategies mean more trading opportunities, and that more trading opportunities mean more money. In theory this

sounds somewhat logical, but in practice this approach fails miserably. In fact, this simply creates a chaotic trading experience and leaves you with little success to build upon.

To get started, take the strategies that are given in this book and commit all of your trading time to mastering them. They are sufficient for big money trading. As you trade the strategies consistently, you will develop an instinct to execute the strategies more efficiently and effectively. From the foundation of successful trading within the rules of these strategies, you can begin to move up through the triangle and exercise more freedom and discretion to generate larger profits.

You must get consistent with the strategies in this book and find the value that each brings.

Consistency of Time

Consistency of time is not only the amount of time you spend in front of the trading screen, it is also the allocated timeslot you spend trading. By committing not only a certain amount of time, but also a certain slot of time, you develop the subconscious skills of reading and feeling the market and its shifts in momentum. This is especially true for intraday trading (entering and exiting a position in the same day).

Time in front of the trading screen builds a log of visual experiences that you can call upon in the future to help you execute similar trades for a profit or to stop you from entering trades with a lower probability of success. Remember, though: the key is consistency, not a devotion of 14–18 hours a day! At Learn To Trade, we recommend our students spend a maximum of one to two hours per day in front of the trading screen. Spending too many hours in front of the trading screen normally causes not only anxiety and stress, but also poor trading results.

Trading during the same timeslot each day builds your understanding of “currency characteristics.” Imagine that you have just met someone for the first time and you decide that you are going to spend two hours, between 10:00 A.M. and 12:00 P.M., every day with this person for the next year. On the first day, you know nothing at all about the person. If

you had to guess what they were going to have to eat for lunch on that first day, you would have no idea. You don't even know what time they eat their lunch! You wouldn't know if they were very active during this timeslot or whether they used this time to rest and relax. You are completely in the dark because you have never spent any time with the person.

As time goes on, however, you begin to develop an understanding of the person's characteristics. You could predict with a high level of accuracy what this person would have for lunch on any given day. You would also know the things that cause excitement, frustration, laughter, pain, stress, anger, sympathy, and compassion—the things that “move” this person during this period of time. This is key. Spending the same amount of time, during the same timeslot, with the same person each day gives you the ability to predict what that person is going to do and how that person will react to certain events. That is exactly what you want to achieve in your FX trading: the ability to recognise what moves the currencies and to what extent. This puts you in the best possible position to begin working your way up the triangle. You must be spending the same amount of time, during the same time slot, and you must trade the same currency pair each day. If you do this consistently, you will know exactly when the currency is moving and when it is not. Suddenly, the price action will become predictable and your confidence level will increase. It is with this type of assurance that you can continue working your way up through the triangle.

Amateurs do not understand this concept of time consistency within the triangle and, therefore, normally make the mistake of not designating a timeslot to trade. They may spend a few hours in the early morning, then half an hour in the late afternoon, then maybe a whole day tracking the currency pair followed by a late evening session on a different night. The result of all of that time is just a vague idea of the currency pair they are trading. They end up with nothing that is really tangible or productive. This is the result of having too many freedoms.

Another issue most amateurs have is trying to trade and learn too many different currency pairs at once. This causes problems even if they are trading during a specific timeslot. Remember that, in the triangle, we

move from restrictions to freedoms. This means that you are going to be restricting yourself from learning the movements of every single currency pair in order to focus on just a few so that you can master them—restrictions to freedoms. This is a powerful trading approach and establishes a very strong foundational knowledge of the currency market to build long-term trading success.

Take the example of a musician. A good musician understands exactly how to “break the rules” of music theory, yet still produce a good sound. The only reason he or she is able to do this is because he or she first learned the rules and why they exist. From this point, he or she can go on and create musical opportunities above and beyond what the basic rules of music theory permit. The same is true for a trader. Know the rules and follow them until you have an instinct for them. From there, you can find quality trading opportunities above and beyond the basic rules to generate larger amounts of professional profit.

Trading within the triangle can be summed up as moving from restrictions to freedoms. This is the way to build a reliable income stream from trading. Regrettably, a lot of traders work their way through the triangle in the opposite direction—freedoms to restrictions. This causes tremendous amounts of frustration as it results in low confidence, lack of belief, and, ultimately, the loss of money.

So, whether you are just beginning your FX trading journey or simply continuing it, make sure you remember that it is an ongoing process—know where you are in the triangle.

Every profitable trader has strategies that clearly define the placement of the entry, stop loss, and profit target for each trade. Without a strategy there is no foundation to justify any potential trading opportunity. In Part 2 of this book, you are going to be learning two proven and specific FX trading strategies. You can make a lot of money from these strategies if you are willing to trade responsibly. Initially the rules of the strategies will be restrictive and will allow no room for discretion. You must trade the strategies like this until you build a solid foundation of profit and knowledge. From there, you can then begin to exercise a certain level of discretion or freedom as you trade.

You must remember to trade within the triangle. The bottom of the triangle is very restrictive, but it is also very safe and secure because you are following the rules of the strategy perfectly. The very top of the triangle provides endless amounts of freedom, judgment, and discretion to do what you want, but it is not very safe for the beginner. Here is the principle: the only way to exercise judgment above and beyond the rules at the top of the triangle is by first learning to submit to and obey the rules on your journey up through the triangle. This is the methodical process of becoming a mature, responsible, strategic trader.

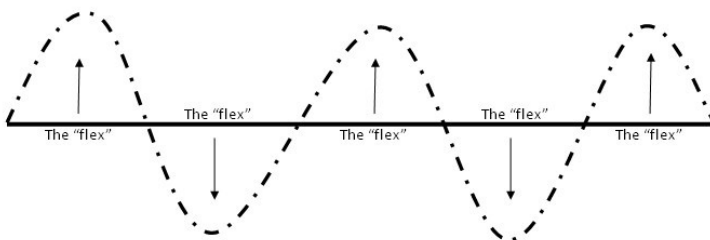
Flexible or Chaotic?

Profitable traders understand the importance of establishing normality within their trading as well as the difference between chaos and flexibility. This concept goes on to emphasise the journey of trading within the triangle. A lot of traders are terrified of becoming robotic within their trading and therefore very quickly forsake the rules of well-established strategies—this is a mistake. As you learn the strategies in this book you must commit to comply with them. Without normality there can be no flexibility, only chaos. Let me demonstrate.

Something can only flex, when it first has an established position. Consider the horizontal line below to be The Norm.

Because we first have The Norm, we can have The Flex. Refer to the example below.

Figure 4.2

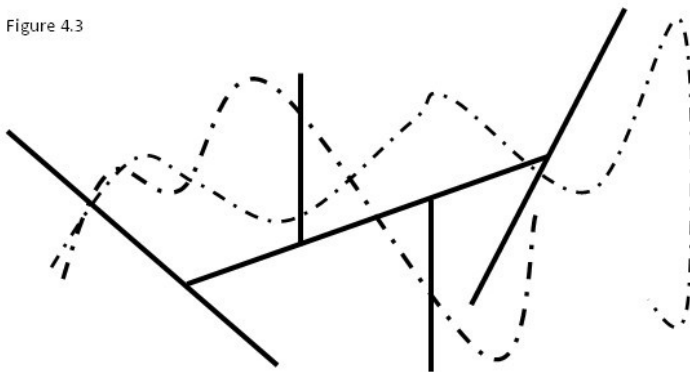


Notice how The Flex is always away from the norm and how it always returns back to it. This is how you use strategies to trade. I am telling

you this now because, if I don't, there is a strong possibility that you will learn the rules of the strategies from the following chapters and, in no time, apply discretion far beyond your familiarity with the strategies. Those "flexes" are your freedoms as you work up through the triangle.

Unfortunately, most people trade chaotically in the name of flexibility. They believe that sticking only to the rules hinders profit. This is a very short-term view, and the results are always the same: early loss of money, followed by lack of belief and frustration. If the trader has the drive to continue pursuing the trading venture, there will be a tightening of policy and an uncomfortable journey from the freedoms to restrictions. That is unnatural and discouraging.

Have a look at the chaotic chart below:



Notice how there is no stability or consistency with this approach. The trader's approach is dynamic in that it is constantly changing. Chaos will never magically result in order. Order must be established.

Successful trading is for the long term. If you are willing to take too many freedoms with the rules of the strategies, you are more likely to take too many freedoms with the risk management and trade sizing rules—this will have a devastating effect on your account. Too many freedoms create chaotic trading, and chaotic trading will wipe your account out fast.

Financial Freedom through FOREX

A consistent and proven FX trading strategy is precious to the trader because, if used properly, it is going to produce profit. Approach each strategy as if it were a new person you are meeting. Take some time to get to know it thoroughly. If you are wise with it, it will become a long-term source of income that will produce profit time and time again.

Part 2

Strategy—The Ultimate Implementation

A good strategy is a trader's best friend. In Part 2 of this book, I am going to introduce you to two of my best friends. If you stick close to them and do what they say, they will make you money; if you ignore them, they will give you nothing.

Chapter 5

THE ANGRY BEAR



Chapter 5

THE ANGRY BEAR

Chapter Objectives:

- * Understand the rules of the strategy
- * Understand how to implement the strategy for consistent profits
- * Make the strategy an integral part of your daily trading plan

There are all kinds of reasons for market crashes, but at the root it's all about herd psychology. In a bull market (that's when the base currency is being purchased), even the smart traders can succumb to what the former chairman of the Fed, Alan Greenspan, famously termed "irrational exuberance."

But when the herd changes direction, sometimes due to nothing more than a change in the wind, its mood can also change from euphoria to gloom. The herd stampedes. A few traders get scared and that fear translates to the whole herd and they all take off. The rest of them don't know why they are scared, they just feel that fear and start dumping currency. Fear overwhelms all rational thinking—until it's over. The buyers turn to sellers, the bulls turn to bears. The point here is that markets are mirrors of the human psyche; like people, they are prone to mood swings. From greed to fear, they suffer from depression and sometimes they can experience complete breakdowns. And when that happens there is an opportunity to make huge profits. Welcome to the Angry Bear.

The Angry Bear strategy is a fantastic intraday strategy that captures the early, negative swing from buyers to fear-driven sellers.

This is Intraday trading at its best, and refers to trades that are opened and closed within the same day. This is, therefore, a short term trading strategy that opens and closes within hours, not days.

Exploring the Strategy

To profit from this FX strategy consistently, you must fully understand each aspect of the strategy. To do this, we are going to ask the questions **who?** **when?** **what?** **where?** and **why?** in relation to the strategy. Understanding each aspect not only provides you with the standard rules for the strategy, but also paints the big picture of what the strategy is all about and why it works. From here, you can build an incredible amount of skill in executing the strategy profitably and consistently as you work your way up through the triangle.

Let's start off with the *who?* part of the strategy and, from there, we can work our way through each of the other questions.

Who Are You Trading?

Trading FX is simply trading one currency's economy against another (refer to Chapter 2, in the "Basic Terminology" section for a reminder of this concept). Therefore, the question of "who are you trading?" refers to the currency pairs that we use to trade the strategy.

There are two particular currency pairs that we trade the Angry Bear strategy with.

The first is the **EUR/USD** (Euro against the U.S. Dollar), and the second is the **GBP/USD** (Great Britain Pound against the U.S. Dollar). These currency pairs are the most liquid and, therefore, most commonly traded currency pairs in the world. The EUR/USD pair accounts for nearly one third of the daily FX volume, whereas the GBP/USD pair accounts for nearly one quarter of the daily FX volume. These currency pairs have several similarities, but it is really only important that you understand the main two, which are:

1. Each pair has a major European currency as its base: Euro and Sterling. In fact, the Euro and Sterling are the currencies of the two largest economies in Europe.
2. Each pair has the U.S. Dollar as it's the terms currency. The U.S. Dollar is the most commonly traded individual currency in the world. Over 80% of *all* foreign exchange transactions include

the U.S. Dollar—there will be more on this in the following chapter.

Similarities in the nature of the pairs means similarities in the character of the pairs—this is important because it tells us that their behaviour is likely to be the same and is therefore the reason why this strategy can be traded with either pair.

You trade this strategy with the EUR/USD and the GBP/USD only—no other pairs permitted.

Trade only EUR/USD and GBP/USD

When Are You Trading?

This particular strategy is traded around the European market open which we are going to define as being between 6:00AM and 10:00AM Greenwich Mean Time (GMT). The reason that this strategy is specific as far as when it is traded is due to the behavioural characteristics of the currency pairs during this period of time. The strategy essentially captures the early rejection of a bullish trading session of either the Euro or Sterling against the U.S. dollar. This rejection during the European market's open, sets the tone until the U.S. market kicks in—that is the move that we want to catch.

Trade between 6 a.m. and 10 a.m., GMT

What Are You Looking For?

A high test bar is what you are looking for because it demonstrates that there was a bullish trading session, immediately followed by a selloff of the Euro and or Sterling against the U.S. Dollar. The visual proof of this shows price that has reached new highs for the session only to be followed by a severe selloff.

Plus, the high test bar is also what you use to define your entry and stop loss on the trade. Remember that this high test bar must be located between 6 A.M. and 10 A.M.

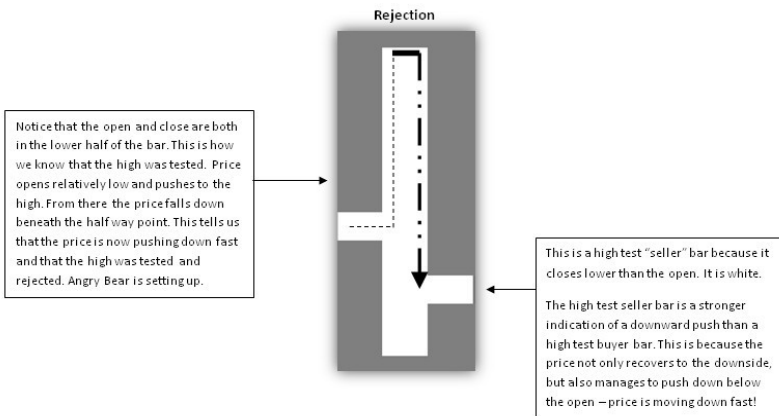
Two specific features are present in a high test bar:

1. The bar must be large relative to the bars that precede it. This shows you that price has overextended to the high—this indicates the bullish move.
2. The open and the close must be in the lower half of the bar. This demonstrates that the price rose and fell very quickly—this shows the rejection of the bullish move and the setup of the Angry Bear.

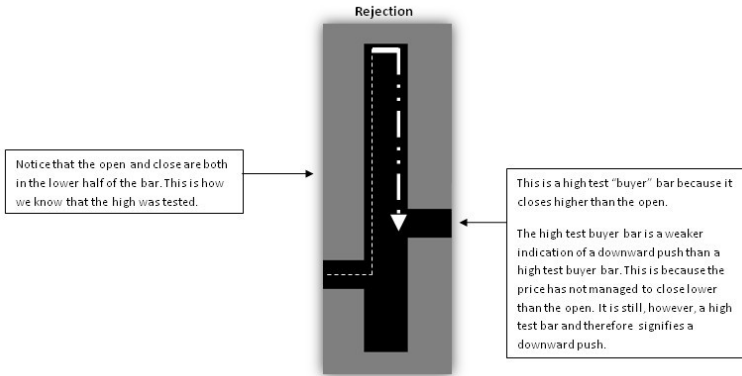
One thing that is **not important** for the high test bar when trading this strategy is the colour of the bar. This means that the high test bar can be a seller (close is lower than the open) or buyer (close is higher than the open) bar—it makes no difference. What you are looking for is a solid test and rejection of the high, not whether or not the close is higher or lower than the open.

The following will demonstrate what a high test bar actually looks like:

High Test Bar (Seller)



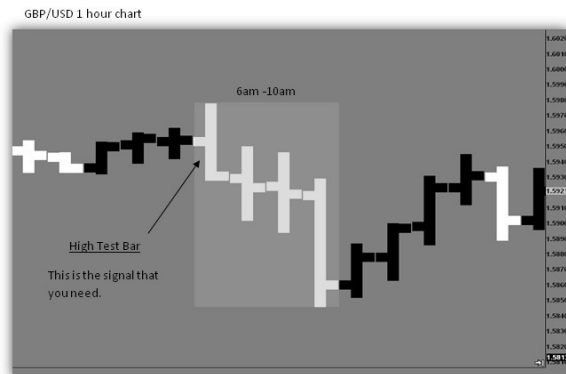
High Test Bar (Buyer)



Never underestimate the power of these bars—especially on the hourly chart. They give you a tremendous insight into what the next few hours of trading hold. This is why the strategy is so effective.

Although we are trading the high test bars on the hourly chart, they are not restricted only to this time frame. You can have a high test on any time chart imaginable. This strategy, however, exploits the power of the high test from the hourly perspective and has proven, time and time again, to generate large profits.

Below is a midway recap of what you have learned so far of this strategy.



The chart above should bring together the rules of the strategy so far. We have a high test bar, between 6 A.M. and 10 A.M. on the GBP/USD hourly chart! Remember that the high test bar is showing you that there was heavy buying activity on the Sterling against the U.S. Dollar, which started at 6 A.M. We know this because the 6 A.M. bar is larger in relation to the bars that precede it. We also know that this buying of Sterling was rejected dramatically within the same hour because the close is in the lower half of the bar. In this example, the close was also the low of the bar—very powerful. You can see the result that this had on the rest of the European morning session: a continued selloff of Sterling against the U.S. Dollar, which was triggered by the high test on the 6 A.M. bar.

Find the high test bar

Let's dig deeper into the strategy by asking the next question, *where?*

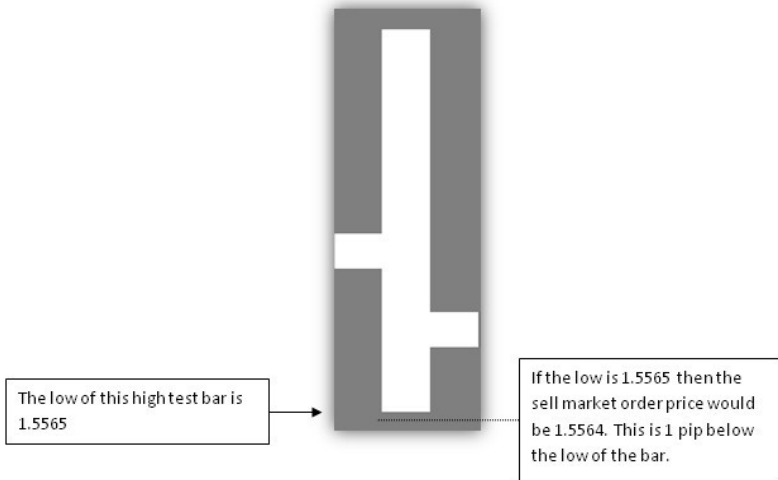
Where Do You Place Your Entry and Exit Orders?

The Entry Price

The entry point on this strategy is done through a market order, as opposed to an instant execution. The difference between a market order and an instant execution trade is that a market order instructs your broker to trigger you into a trade at a certain price, whereas an instant execution entry is placed live at the market touch price.

This strategy is unique in that you will only ever trade it short (sell). There is never a long (buy) scenario, hence the name Angry Bear (there is no happy bull equivalent!).

The location of the sell market order is 1 pip below the low of the high test bar. Refer to the figure that follows:



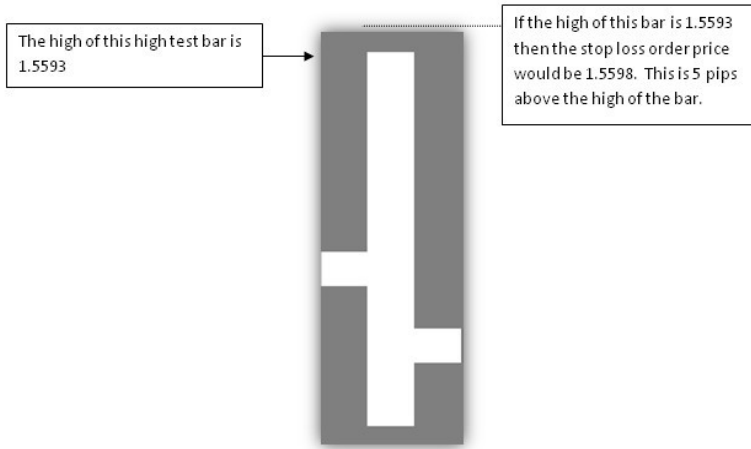
We are treating the low of this high test bar as a support level and, therefore, the very moment it breaks its low (support) is the most efficient time to enter the trade. This break is especially strong given that the price action is pushing down very quickly after a rejection of the upward push. Trading this type of entry with a market order is the best way to hit the exact entry point every time.

The Stop Loss

The stop loss is also done through a market order. This creates an automatic exit and removes the temptation of moving your stop loss further and further away if the position begins to turn against you. That is a common mistake amateurs make. We call it the “dynamic stop loss management system,” and we tell all of our students to stay away from it!

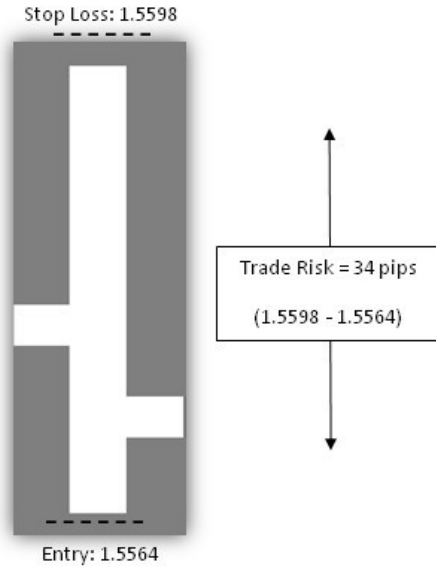
The actual location of the stop loss is 5 pips above the high of the high test bar. Refer to the figure that follows:

Financial Freedom through FOREX



As far as the stop loss is concerned, we are treating the high of the high test bar as a resistance level, and we are allowing a 5 pip buffer. In other words, if the resistance of the high is broken by 5 pips, we are assuming that we are wrong on the direction of the move and need to exit the position. It is important to remember that the difference between the entry price and the stop loss price is your trade risk. This is the number that is plugged into the two ratios that you learned about earlier: trade sizing and reward-to-risk.

The following figure shows the entry, stop loss, and, as a result, the trade risk—all based around the high test bar, which is the key to this strategy.



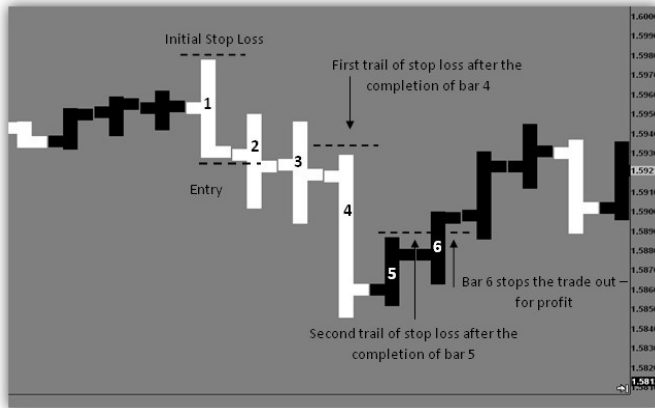
Taking Profit

To take profit is to exit the trade with more money in your account than there was before you entered the trade—this is, obviously, what you want! For this strategy, you do not place a take-profit order to collect your money at a certain level. Instead, you move your stop loss order down to lock in the profit until the position eventually comes back against you and triggers your stop loss—for a profit! This is known as “trailing your stop,” and the major benefit to doing it is that you are locking in profit as you trail without removing yourself from the trade and removing the possibility of generating more profit from the trade.

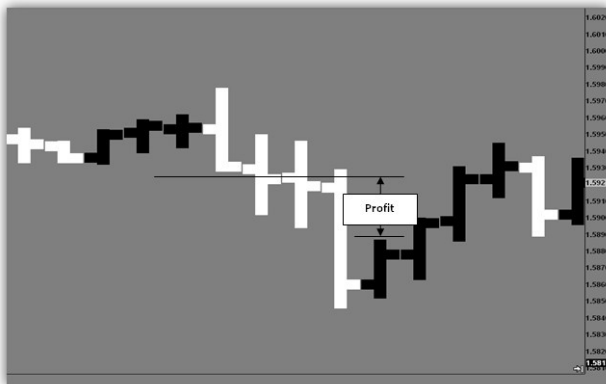
With the Angry Bear strategy, you begin trailing your stop loss order to the high of each bar from the completion of the fourth bar (the bar you enter on is bar one). Remember, bar one can be anywhere between 6 A.M. and 10 A.M.). So, once the fourth bar has formed, move your stop loss from the high of bar 1 plus 5 pips, to the high of bar 4 plus 5 pips. Continue to do this on each bar from this point on until the price triggers your stop loss. The longer it runs the better! The reason we hold the position open for four hours before trailing the stop loss is to allow the Angry Bear to run without interruption before the U.S. session gets involved.

Financial Freedom through FOREX

Look at the following figure for an example of how to trail your stop lost effectively. This example is a zoom in on the same chart that was used in a figure from earlier in this chapter.

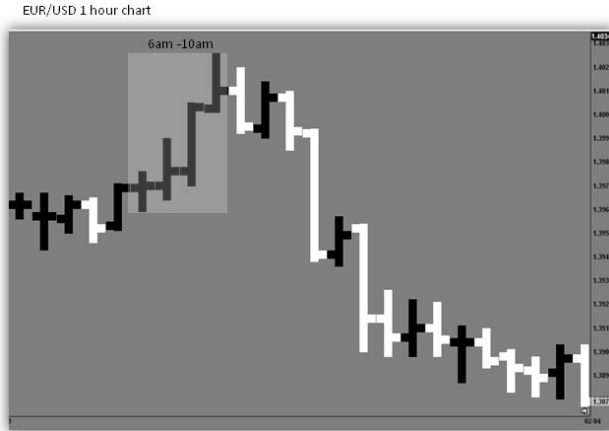


The next figure shows the profit on the trade as the difference between the trigger of the entry and the trigger of the trailed stop loss order.



Notice that you wait until the completion of the fourth bar before you start trailing your stop loss and, from then on, it is after each bar until your stop loss is triggered. So, if bar six would not have hit your stop loss, you would have moved the stop loss to the high of that bar, and so on.

Here is a practical example for you.



1. Circle the key high test bar that triggers the trade.
2. What is the number of the hourly bar that eventually stops you out?

Here are the answers:



The trade is not ended until the 15th bar because that is the first time that an hourly high exceeds the high of a previous bar. Notice also that the 7 A.M. bar was a high test bar that didn't actually trigger in the trade—that's fine. Remember that our key high test bar can be anywhere between 6 A.M. and 10 A.M. On this particular setup, the high test that triggers doesn't occur until the last of the four possible bars, which is the 9 A.M. to 10 A.M. bar. This is also a good example of why you need to wait for the low of the high test bar to be broken before you

go short. Had you not waited for the low of the 7 A.M. high test bar to be broken before entering the trade, you would have lost . However, you can see the benefit of being patient and waiting for the correct entry. This ended up being a profitable trade for over 100 pips!

The *where* of this strategy is all about where to enter and where to exit—regardless of whether your exit is for profit or loss.

Enter 1 pip below the high test, stop loss 5 pips above the high test and trail your stop at the high of every bar beginning with bar number 4

Why Does This Strategy Work?

The strategy works because you are harnessing the power of negativity following an early bullish movement. As the market turns, the high test bar is formed. It is when this bar has closed and the subsequent seller bar trades lower, confirming that move further that we have a trade on. The reason that the four hours is used is because it allows the fear and negativity to persist and build in the same session without the U.S. getting involved (who may have a different perspective on the market and end this selloff by selling a bargain buying opportunity).

This is a strategy that is based on the time-specific behavioural characteristics of the world's two most liquid currency pairs, the EUR/USD and GBP/USD. This strategy acknowledges the importance of liquidity as well as the power of two similar currencies (Euro and Sterling are the major European currencies) both traded against the most active currency in the FX market, which is the U.S. Dollar. Liquidity is important because it provides predictability and reoccurring patterns. Similarity gives us confirmation of normality. For instance, if there is a situation where the EUR/USD chart mirrors the GBP/USD, that informs you straightaway that something specific is either happening to the U.S. Dollar, or something specific is happening in and to Europe that affects both the economy of the Euro-zone as well as the British economy.

When both the EUR/USD and GBP/USD chart are trading in sync, they are said to be correlating. Correlating charts, especially the two charts we are considering, provide you with a great deal of confidence and certainty when opening a position because there are more factors of probability converging together due to the direction and overall flow of money being traded in the market.

Look at the chart that follows. Would you say that the EUR/USD and the GBP/USD are in correlation?



Look at the 8:00 A.M. high test bar that is circled on each chart—same day, same time. That is two profitable trades in the morning session. You can see the result of the correlation as the pairs continue to trade together.

If you see this strategy setting up on both currencies pairs, then make sure you trade them both!

This strategy works because of the common behavior of both currency pairs during the European open

Strategy Summary

The chart below is a quick summary of the strategy.

Question	Answer
Who to trade?	EUR/USD (Euro) & GBP/USD (Cable)
When to trade?	6 A.M. to 10 A.M. GMT hourly chart
What to look for?	High Test Bar (black or white)
Where to enter and exit?	Enter on low minus 1 Stop Loss on high plus 5 Trail Stop from 4th bar plus 5
Why does this strategy work?	Time and Pair-Specific Currency Behaviour

Remember that the key to success with this strategy is consistency. Look for the setup every trading day and trade it 100% according to the rules. It will make you money if you trade it correctly.

Chapter 6

FOREX ECLIPSE



Chapter 6

FOREX ECLIPSE

Chapter Objectives:

- * Understand the rules of the strategy
- * Understand how to implement the strategy for consistent profits
- * Make the strategy an integral part of your daily trading plan

An eclipse is an astronomical event that occurs upon the alignment of three or more celestial bodies in the same gravitational system along a straight line. The Forex Eclipse strategy is a setup that is based off of the alignment or “agreement” of three major timeframes, all of the same currency pair.

To a professional FX trader, a Forex Eclipse is just as beautiful as an astronomical eclipse is to a seasoned astronomer.

Let’s check it out!

Exploring the Strategy

We are going to explore this strategy in the same format as we did for the Angry Bear, which is to ask the questions *who?*, *when?*, *what?*, *where?* and *why?* in relation to the strategy. This will make the learning process much easier for you.

The first question is:

Who Are You Trading?

Remember that trading FX is simply trading one currency's economy against another. Therefore, the question of "who are you trading" is referring to the currency pairs that we use to trade the strategy.

The U.S. Dollar is referred to as the global central currency. This is because more transactions and major global resources are denominated or valued in U.S. Dollars than any other currency. Take for instance the price of oil. Oil is valued at a certain number of U.S. Dollars per barrel.

The global influence of the U.S. Dollar has made it the most liquid individual currency in the world. Liquidity is important because it demonstrates that traders are trading large volumes of the currency. Because of this, specific price patterns form.

You will use the following four currency pairs to trade this strategy:

GBP/USD—Great Britain Pound with the U.S. Dollar, which is also known as "Cable"

EUR/USD—Euro with the U.S. Dollar, which is also known as the "Euro"

USD/CHF—U.S. Dollar with the Swiss Franc, which is also known as the "Swissie"

USD/JPY—U.S. Dollar with the Japanese Yen, which is also known as the "Yen"

These four pairs are often referred to as the "4 Majors" because they are the four most commonly traded pairs on the planet—large participation creates predictable price action. That is what we want.

**Trade only the 4 Major pairs:
GBP/USD EUR/USD USD/CHF USD/JPY**

When Are You Trading?

The Forex Eclipse is similar to an astronomical eclipse in that it can occur at any time. That means that there is no specific time of the day to trade this strategy. This is because the strategy is not based around time but, instead, around a specific setup. This is different from the Angry Bear strategy, which is a setup and time-specific strategy. The FX market is open from Sunday night until Friday night. You can trade this strategy whenever you like within the week.

Trade anytime you see a setup

What Are You Looking For?

The foundation of this strategy is the agreement or alignment of the daily, 4-hour and 1-hour charts. Once we have the agreement of these three timeframes, we look to the 5-min chart to determine our entry.

The “agreement” among these timeframes refers to the location of the price action in relation to the 50 EMA. Is it above it, or is it below it? That is the key. When trading this strategy, we do not consider the 200 EMA, we are only concerned with where the price is in relation the 50 EMA.

Let’s consider a possible Forex Eclipse setup on the GBP/USD. The first chart we need to look at is the daily chart. Remember that the daily trend is the strongest indication of direction for the currency pair. This chart ultimately tells us whether or not we will be going long or short. If the price is below the 50 EMA on the daily chart, we know that we will be going short when we get the setup, and vice versa.

Financial Freedom through FOREX



We notice that the daily chart is in a nice downward trend and that price is below the 50 EMA. This means we are looking for a potential short position. Next, we look at the 4-hour chart to see if the price action is also trending down with price below the 50 EMA.



The price action is below the 50 EMA on the 4-hour chart and there is a clear downward trend. We now have agreement between the daily and 4-hour charts. Now it is time to look at the 1-hour chart.



The price action is also below the 50 EMA on the 1-hour chart. We now have agreement on the three major timeframes. Remember that time is king. The daily chart gives a stronger signal of the overall market view than the 4-hour chart, and the 4-hour chart gives a stronger signal than the 1-hour chart.

Let me ask you a question:

If the daily chart is trading below the 50 EMA, the 4-hour chart is trading below the 50 EMA, and the 1-hour chart is also trading below the 50 EMA, where do you expect the 5-minute chart to be trading—above or below the 50 EMA?

The obvious answer is that you expect the price to be below the 50 EMA. But what if the price on the 5-minute chart is above the 50 EMA and disagrees with the other charts? What would that be showing you?

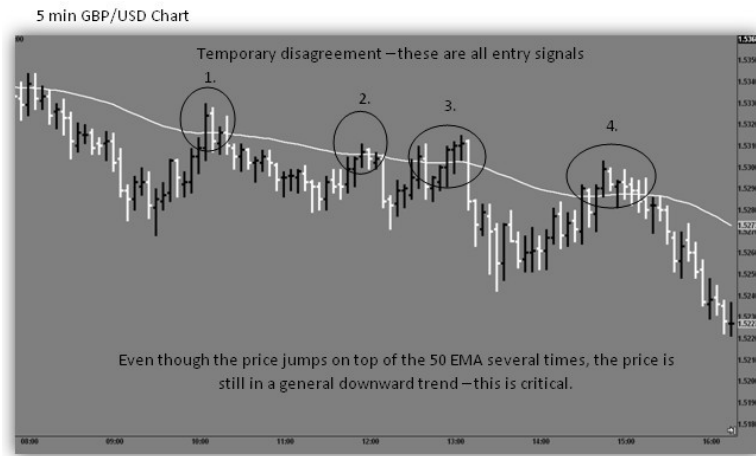
I would like to take this opportunity to introduce you to a little secret. The majority of successful trading strategies are based on identifying the price when it is “out of place.” To be able to do this, you need to understand where the price should be. When you notice that the price is where it should not be, and you know where it should be, you can trade the move or the journey from “out of place” to “in place.”

Coming back to the example, if the price action is below the 50 EMA on all of its major timeframes, but it is above the 50 EMA on the 5-minute

Financial Freedom through FOREX

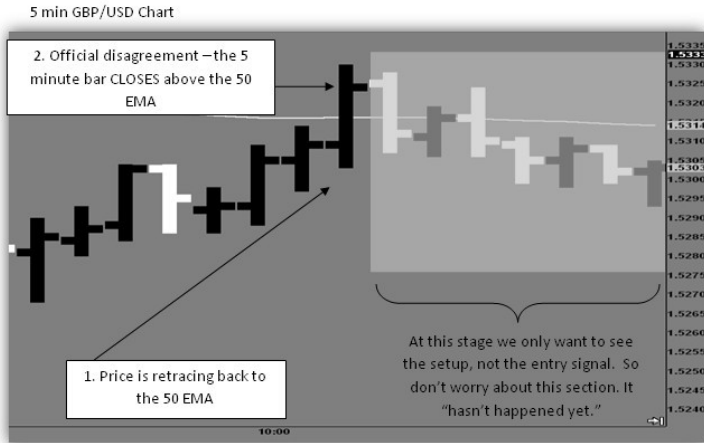
chart, then the price on the 5-minute chart is considered out of place. This strategy captures the 5-minute chart moving back into place. The next section deals specifically with where to enter and exit. For now you just need to know what the setup looks like.

Look at the 5-minute chart that follows:



This picture is a perfect example of exactly what you should be looking for when you are trading this strategy. Although the general push of the price action is downward, there are small areas of temporary disagreement. These are our entry signals. The strategy is traded this way because we know that the strength of the downward pull from the larger and stronger timeframes is likely to pull the 5-minute chart below its 50 EMA.

The figure that follows is the first area of temporary disagreement from the previous figure.



Notice the close of the 5-minute bar on top of the 50 EMA. This is exactly what you need to see. It is not good enough for the price to just trade above the 50 EMA, it needs to close above it.

In summary, you are looking for the daily, 4-hour, and 1-hour chart to all agree on where they are trading in relation to the 50 EMA—above or below. You then need to see the 5-minute chart demonstrating areas of temporary disagreement with the other charts by crossing the 50 EMA to the opposite side and closing. This is the trade setup. Next, we are going to define the actually entry.

Agreement among the 3 major timeframes with a temporary disagreement on the 5-minute chart

Where Do You Enter and Exit?

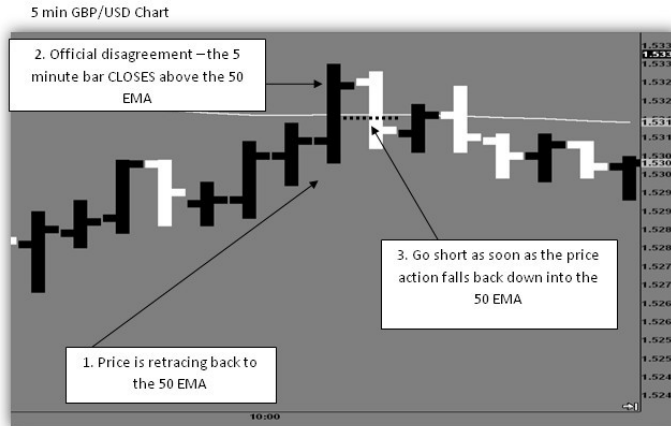
Entry

This strategy is traded with an instant execution style entry. This means that you hit sell or buy, depending on the setup, the moment you want to enter the trade—no entry orders.

Financial Freedom through FOREX

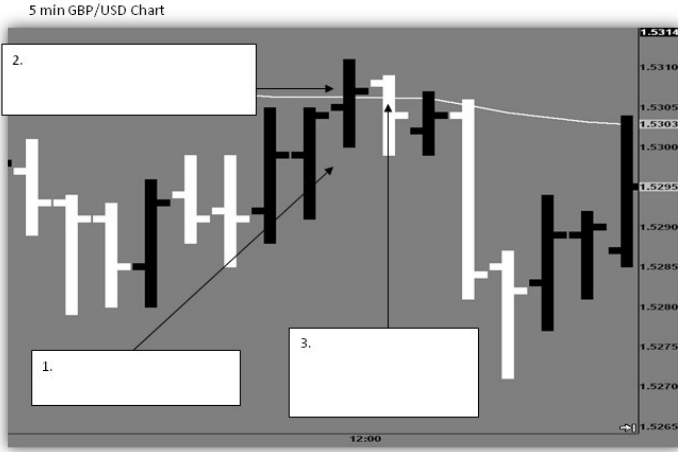
As we are going short in this example, the entry is described as the moment that the price action crosses back down into the 50 EMA from above. This is where the price comes back into agreement with the larger time period charts.

Here is the same picture that we saw earlier, except that it also includes where to enter the trade.



This figure demonstrates the three-step process that takes place on the 5-minute chart. First, the price action retraces back toward the 50 EMA. Second, the price action crosses through the 50 EMA and closes above it—that is the disagreement. Remember that the larger, stronger charts are all trading below the 50 EMA, and now the 5-minute chart is on top of it; the 5-minute chart out of place. Step three is the entry of the trade which happens the moment the price action falls back down into the 50 EMA. This is the beginning of the 5 minute chart coming back into agreement with the other charts. Notice that you are not waiting for the bar that crosses through the 50 EMA to close. That would be too late. You are entering the moment it crosses down through the 50 EMA.

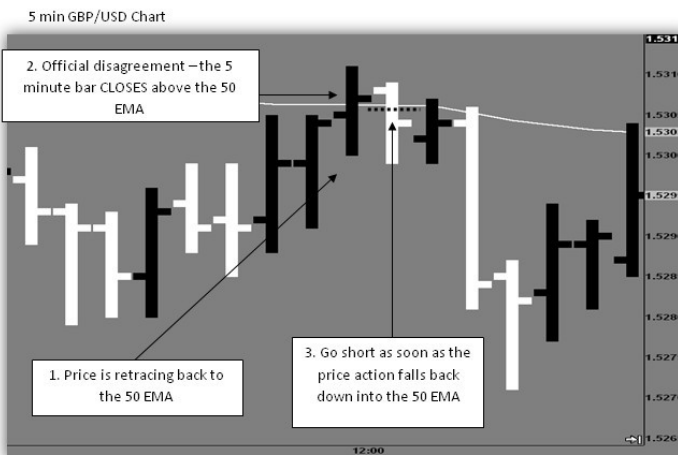
Here is the second entry signal zoomed in from above. Fill in the boxes to describe what is happening and draw a line to show where the entry is.



This shows how the price retraces back up to the 50 EMA, closes on the other side of it (which confirms the disagreement), then breaks back through the 50 EMA to come into line with the stronger time charts. This signals your immediate entry into the trade.

Step one shows the price action retracing back up to the 50 EMA. Step two demonstrates the temporary disagreement through the close of the 5-minute bar on top of the 50 EMA. Step three confirms the entry as the price action crosses back down into the 50 EMA.

Your chart should look like this:

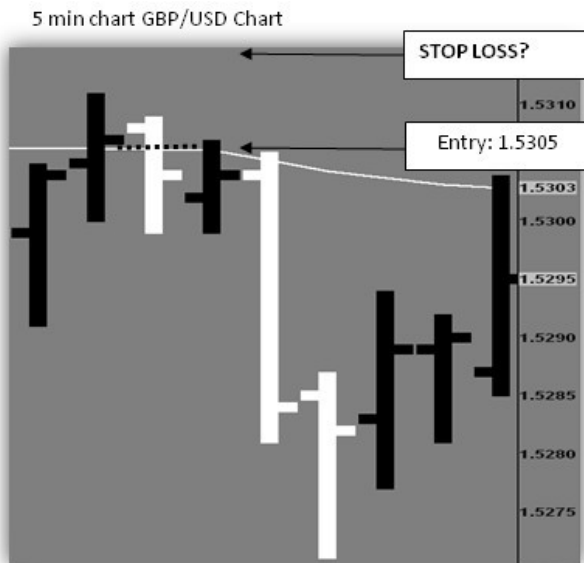


This is the simple, three-step process of entering the trade. Next, we must define our stop loss and target prices.

Stop Loss

The stop loss placement for this strategy is very simple. When you are going short, you place the stop loss 20 pips above your entry. When you are going long, your stop loss is 20 pips below your entry.

This shows an example of a short entry price. Fill in the exact price of your stop loss below.



The stop loss price is 1.5325. This is exactly 20 pips above your entry ($1.5305 + .0020 = 1.5325$). It is as easy as that!

Let's assume that you were going to trade this strategy long and your entry price was 1.5305. What would the exact price of your stop loss be? _____

The answer is 1.5285 ($1.5305 - .0020 = 1.5285$).

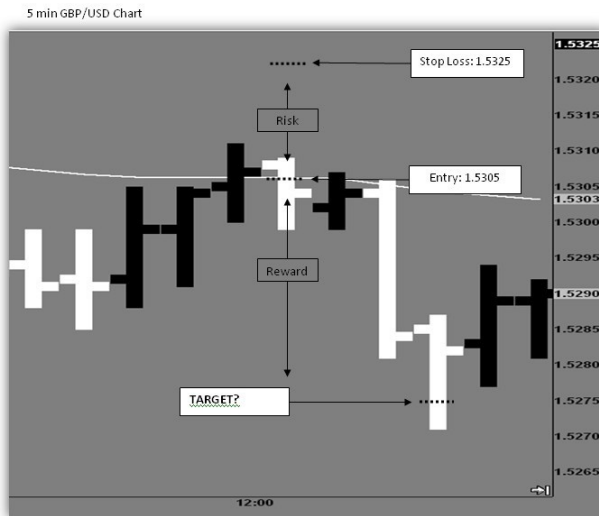
Remember, when you are going short, your stop loss is above your entry, and when you are going long, your stop loss is below your entry.

Let's take a look at how to target this trade for a profit.

Target

The target on this strategy is 30 pips from your entry price. This gives you an automatic 1.5:1 reward-to-risk ratio every time you trade this strategy (30 pips of reward / 20 pips of risk). This strategy is meant to be a quick "in and out," and if your entry is executed correctly you are normally out of the trade with profit in 10–30 minutes. Refer back to the figure above that shows the four entry signals. You will see that each entry signal results in a successful trade, and none of it takes more than 30 minutes to bank. Had you been spending the afternoon trading, you would have collected 120 pips from GBP/USD alone!

The next figure is an expansion of the idea from earlier. You know the entry and the stop loss prices, now see if you can fill in the exact target price.



The target price is 1.5275. This is exactly 30 pips below your entry ($1.5305 - .0030 = 1.5275$). It is as easy as that!

Remember, when you are going short, your target is below your entry, and when you are going long, your target is above your entry.

**Enter when the price action breaks back into the 50 EMA,
20 pip risk and a 30 pip target**

Why Does This Strategy Work?

When a currency pair has a dominant trend that is confirmed by its daily, 4-hour and 1-hour time charts, the probability of the trend continuing is very high. During periods of short-term retracement, the 50 EMA on the 5-minute chart naturally acts as a guideline for the price action to retrace back to before continuing on with the dominant trend. This retracement is the result of short-term profit taking in the market, not a signal of the changing of the trend.

Exploits the power of timeframe and trend agreement

Strategy Summary

The chart below is a quick summary of the strategy.

Question	Answer
Who to trade?	EUR/USD (Euro) & GBP/USD (Cable) USD/CHF (Swissie) & USD/JPY (Yen)
When to trade?	Anytime—this strategy is not time specific
What to look for?	Agreement of daily, 4-hour and 1-hour charts with disagreement on the 5-minute chart
Where to enter and exit?	Enter as price breaks back through the 50 EMA. Stop Loss 20 pips. Target 30 pips
Why does this strategy work?	Catches the natural flow of a trending pair

Although the strategy in this chapter was demonstrated through *short* examples, it can be traded just as successfully going *long*. For a long setup, you would have to have the daily, 4-hour, and 1-hour charts all trading above the 50 EMA, with the 5-minute chart dipping down below the 50 EMA to indicate temporary disagreement with the other charts. You enter the trade as the price action crosses back up through the 50 EMA. Your stop loss is 20 pips below your entry and your target is 30 pips above your entry.

Remember that the key to success with this strategy is consistency. Look for the setup every trading day and trade it 100% according to the rules. It will make you money if you trade it correctly.

Part 3

Purpose—Moving Forward Effectively

Moving forward is not good enough. You must move forward effectively and with purpose. Part 3 of this book equips you with long-term money management and trading concepts that will ensure that you do just that.

Chapter 7

Let's Talk about Money...

Chapter Objectives:

1. Understand the importance of context and objective thinking when considering upfront cost prior to investing
2. Understand that trading success should be measured in percentage increase of account, not just pip accumulation
3. Understand the power of a compounding trading account and working with the percentages

A Life of Cost, A Life of BENEFIT

There are two very clear aspects to any financial transaction: **Cost** and **Benefit**. This is true if the transaction is completely investment oriented, completely entertainment oriented, or even somewhere in between. One thing is for sure, regardless of the nature of the transaction, there will be a giving of money and a reception of a potential financial or non-financial benefit.

The question is: *do you enter the transaction and part with your money or not?*

Contrary to what most people think, the answer to this question is not determined entirely by the amount of cost or investment, or even the potential size of the benefit. It is determined mainly by the focus of the individual and his or her ability to see clearly and make an objective financial decision with limited emotional influence.

This is true because, ultimately, the focus of the individual will destroy either the cost aspect or the benefit aspect of the transaction. This destruction is not intentional. It comes as a result of the focus or exaltation of one aspect over the other—this is a problem area for many investors and spenders because it is normally the benefit that is

destroyed. People believe they are thinking rationally or even objectively when, in fact, they are being swayed by emotions of fear and anxiety. Let me give you an example of benefit destruction in an investment scenario.

The U.K. housing market experienced a massive boom that began in the early 1990s and lasted nearly twenty years. This tells us two things: First, anyone who invested heavily in the early 90s will, twenty years later, have made a considerable amount of money from (or witnessed growth in) their property portfolio (assuming they had managed it relatively well). Second, it tells us that anyone who declined the investment opportunities of the early 90s will be financially worse off than their counterparts (unless they generated large amounts of money elsewhere).

Benefit destruction

I had a conversation once with a man who told me that, in the early 90s, he had a chance to buy a piece of land that would have allowed him to build 10–15 houses on it. He went on to tell me that, had he bought the land, he would now be a multimillionaire—but he didn't and he isn't. Instead, he is still working and paying off the mortgage on the single property he decided to buy in place of the piece of land. He continued by saying, "I knew that I had a great opportunity before me, but I just didn't have the money to get in."

Question: Was his focus on the cost or on the benefit of the transaction?

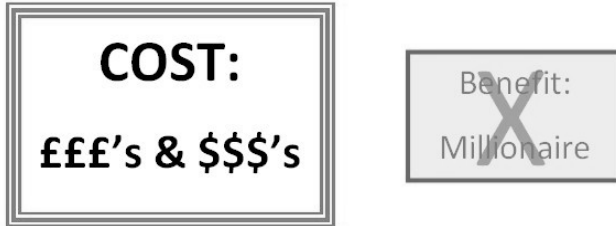
Answer: The cost.

How do we know this?

We know this because his decision about whether or not to part with his money was based on the cost of the transaction. His lack of action was not determined by his belief that the benefit was unreasonable, unobtainable, or even unrealistic, which are certainly things to be considered. He made it very clear that he recognised that he had a great opportunity to make money. Unfortunately, it was his focus on the cost that ultimately destroyed any energy being released into the

benefit. Because of this, he missed out on a shot at becoming a millionaire. What a tragic story... but it happens all of the time.

His focus looked like this:



Now, let's take the same example and look at the alternative mentality, which I call benefit construction.

Benefit construction

It is important to remember that we are considering the same person with the same scenario; i.e., costs and benefits are exactly the same. The only difference is the focus. Now we must be realistic. If the man felt like he didn't have the money in the first example, he will feel the same way in this example, but the feeling or fear should have nothing to do with the action! The deciding factor is whether or not he will allow that feeling of not having the money to stop him from pursuing the investment opportunity. Feelings have to do with emotions, and when you invest, or even trade, you must remove emotions and function objectively. Once you are thinking objectively, you are then able to properly weigh the positives and negatives of the potential transaction. At this point, you are also able to focus on the benefits of the potential transaction and construct a positive result. Had the man taken this approach, he would have come to the conclusion that the benefit outweighed the cost, and he would now be a millionaire.

His focus should have looked like this:



I am not saying that you should neglect the cost and only consider the benefit. I am saying that once the focus is on the benefit, you are able to put the cost in the correct context in relation to the benefit and make objective financial decisions.

So why is this important? There are **two** reasons.

1. **Trading is not the end; it is the beginning.** We tell this to our students all of the time.

One thing I have noticed about many of our new students is that they have a belief that once they make money from trading they will just sit at home and trade for the rest of their lives, not doing a great deal of anything else. This rarely ever happens because, once they begin making money, they realise that with money comes opportunity and with opportunity comes massive excitement and even adventure! This causes their trading to transition from being their ultimate goal to being the springboard to a life of greater excitement and fulfilment.

If you take your trading seriously and leverage your resources efficiently, you will make money. Once you have more money, you will naturally have more investment opportunities—great! With these opportunities comes the process of weighing the costs and the benefits to increase your financial position. To do this effectively, you must be an investor who is able to focus clearly on the potential benefits so that you can place the costs in their appropriate places. The reason I am telling you this now is because I believe you are actually going to make money once you have read this book—be prepared!

2. **Privilege and fulfilment.** Isn't this the reason you are looking for financial increase?

Up until this part of this section, I have focused mainly on the cost and benefit concept in terms of investment or money-generating opportunities, but there is another context to discuss this concept: privilege and fulfilment.

By increasing your wealth you are able to experience life from a more privileged and comfortable perspective because you can do more things that you want to do! This is because an increase in available money allows you to focus more on the benefit, or what you want, and less on the cost, or what you are afraid of and don't have.

Here is a very small and practical example of the point I am making:

At some point in the past you have probably walked into a shop and wanted a particular article of clothing. But after looking at the price tag, you decided that you would have to *settle* for something that *costs less*. This is an example of lack of privilege and fulfilment because of insufficient funds. You were forced to focus on the cost, to the detriment of the benefit, because of a lack of money. And it makes sense to do that here, because you shouldn't spend money you don't have on clothes. If you had more money, however, you would be able to focus more on the benefit and less on the cost, and you would be able to buy the article of clothing. That is an example of privilege and fulfilment—doing and having what you want.

Some people might take this type of talk as materialistic and might argue that doing what you want and having more money doesn't guarantee happiness. And that is true: money doesn't guarantee happiness. But it does remove restrictions and create opportunities for privilege and fulfilment and, if managed properly, also removes financial stress. Remember, a problem that can be solved by writing a cheque isn't a problem anymore—and in my experience, 90% of problems can be solved with a cheque.

It is time to stop living according to cost and start living according to benefit—experience life the way you want to.

The Trader with the Most Pips...

True or False:

The trader who collects the most pips collects the most money.



Most beginner traders answer this question incorrectly. This is due to an incomplete understanding of pips. They understand that a pip is worth money and, therefore, assume that the more pips you have, the more money that you have. On the surface, it sounds alright, but you mustn't forget that you determine the value of the pip before entering the trade. Because of this, it is possible to have fewer pips and more money or more pips and less money.

You will notice that some of our strategies are designed to generate lots of pips, and that the value of the pip is relatively small. This isn't a problem because large quantities of small pips create large amounts of money. You will also notice that we have designed other strategies for the purpose of only collecting smaller quantities of pips that are valued much higher.

Look at the example below and try to answer the following questions. Remember that the trade sizing ratio is found in Chapter 3, Risk Management.

TRADER A	TRADER B
\$100,000 Account	\$100,000 Account
Long trade on USD/CAD	Long trade on AUS/USD
Entry price 1.0510	Entry price .8970
Stop loss 1.0410	Stop loss .8960

Target	1.0610	Target	.8990
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What is the value of each trader's pip?

TRADER A	TRADER B
\$	\$

Assuming both traders are successful, how much do they each profit?

TRADER A	TRADER B
\$	\$

What was the significant difference between the two traders?

Let's go through the answers together.

To answer the first question we must work out the trade sizing ratio:

$$\frac{\text{Account Risk (AR)}}{\text{Trade Risk (TR)}} = \text{Trade Size (Pip/Point Value)}$$

Trader A's account risk is \$1000 (2% of his account balance), and his trade risk is 100 pips (the difference between the entry price and the stop loss price—the number of pips at risk).

Trader A's pip value is **\$10 (\$1000/100)**

Trader B's account risk is also \$1000 (2% of his account balance), and his trade risk is 10 pips (the difference between the entry price and the stop loss price—the number of pips at risk).

Trader B's pip value is **\$100 (\$1000/10)**

TRADER A	TRADER B
\$10	\$100

To answer the second question, we need to multiply the value of pips by the number of pips collected on the winning trade.

Trader A collects 100 pips (the difference between the entry price and the target price) at \$10 per pip, giving a profit of **\$1000**.

Trader B collects 20 pips (the difference between the entry price and the target price) at \$100 per pip, giving a profit of **\$2000**.

TRADER A	TRADER B
\$1000	\$2000

It is interesting to note that both traders have exactly the same amount of money in their accounts. The most significant difference in this scenario is the number of pips at risk (trade risk), which ultimately causes the value of the pips to be different. Notice that Trader A risks ten times the amount of pips that Trader B risks. This means that his pip is ten times smaller than that of Trader B.

Here is the principle:

The fewer pips that you risk on the trade, the more likely you are to lose on the trade. This is because your stop loss order is close to your entry. However, placing the stop loss close to your entry means that you make more money if the trade wins. This is because your 2% is being divided up by fewer pips— $\text{account risk}/\text{trade risk} = \text{pip value}$.

This is a simple—but important—principle regarding stop loss placement and even individual trader psychology. The strategies that are in the following chapters will illustrate exactly where you need to place your stop loss—but, as you mature in your trading, you will begin to spot opportune times to enhance your profit potential by placing your stop loss in a position that is unique to the setup.

Different styles work for different people. If you find losing trades difficult to handle and struggle to keep motivated after two or three losing trades, then you are likely to trade strategies where the stop loss is placed further from the entry point. This gives you a higher probability of success with a smaller pip value—more wins worth less. Or you may be a trader who can stomach a few losses and enjoy the success that comes with trading strategies that collect fewer but larger points—less wins worth more. Either way, you must find which you like and stick with it.

At Learn To Trade, we tell our students constantly to find the strategy and style of trading that resonates with them personally and then run with it as fast as they can.

Stick with what you like, stick with what you enjoy!

A common mistake, which is made by beginner and even intermediate traders, is that of leaving the strategies and setups that are working for them to “practice” and spend time on other strategies and setups that they are struggling to make money on and that they do not enjoy. This should never be done!

Why would you stop trading a strategy that is already profitable to spend time trading a strategy or setup that isn't working for you? It is crazy, but traders do it all the time.

Why?

A lot of traders feel that if they really want to make considerable money from trading, they have to master hundreds of different setups, styles, techniques, and strategies. This is not true. Being a master at a single strategy is far better than just simply being good at four or five strategies. Remember that every aspect of successful trading is quality over quantity—always.

Let me show you an example.

A friend of mine only trades one currency pair with one strategy at just one particular time of the day - GBP/USD between 6:45 A.M. and 8:15

A.M. His target is just three pips per day. Once he has collected his three pips he is done for the day. He never hangs around to see if he can get any more. Not only that, he never places more than one trade on a single day, so if he loses on his trade that day, he will not attempt to reclaim the pips that he has lost. Why would he? **The market doesn't owe him anything.** He has an incredibly disciplined style and it has been working for him for a very long time. Do not be fooled by the fact that he only collects three pips per day. His pips are worth \$1000, and he averages 13 pips per week - \$13,000 a week. This is the power of trading using a style that suits you.

Play around a little

If you are a beginner trader, then make sure you play around a little bit at first. This is how you find out what you love and what you hate.

Imagine if you had to choose a musical instrument that you were going to play for the rest of your life. You would not train for five years on the drums, then five years on the piano, then five years on the saxophone, and then five years on the bass to figure out which instrument you would like to pursue. Instead, you would spend some time having fun and experimenting with each instrument until you found one that “clicked” with who you wanted to be as a musician and the type of music you wanted to create. The great thing about it is that, regardless of which instrument you choose, your purpose is still the same: to make music. The same is true with trading. Regardless of which style you decide sits best with you (whether it is short-term, quick movements in the market for 15–20 pips or longer-term, end-of-day trading) the purpose never changes: making money.

Not only will this concept increase your trading account, it will also amplify your trading experience.

The Powerful Force of Compounding

Albert Einstein described compound interest as “the most powerful force in the universe.” This is a very bold statement from one of the most respected mathematicians of all time.

Successful FX traders understand completely the power of compounding, and they rely heavily on it to assist in growing their accounts. They understand, unlike a lot of so-called traders, that to make money from trading you do not need gigantic wins every single day. Instead, what you need are small percentage gains several times a week that compound into heroic amounts of money on a monthly, quarterly, and annual basis. Let me give you an example.

Let's take a look at a very simple and achievable target of only 1.5% per week growth in your trading account. That means, in a normal four-week month, your target is just 6%. Now, if you remember from the chapter on risk management, you learned that you never enter a trade without having a minimum reward-to-risk ratio of at least 1:1. This means the minimum you will earn per winning trade will normally be *at least* 1%. So hitting a 6% target per month equates to six successful trades per month (net), or just one and a half successful trades a week—logically and mathematically, given the size of the FX market, this is very achievable if you are willing to stick to some rules and be disciplined. The question is, what does 6% a month actually do for you?

6% return on capital per month doubles your capital every single year. That is a 100% gross return on your money. This type of return is completely unheard of as far as traditional financial products (such as savings and pension funds) are concerned, but to the successful FX trader it is a physical reality!

Here is an example of trading accounts that are initially funded with \$25,000, \$50,000, and \$100,000. The example is based on each trader achieving only 1.5% per week (6% a month) over a three year period. Remember that a 6% return on capital per month compounds to double the capital annually.

6% monthly return doubles capital annually—100% gross return			
Seed Capital	\$25,000	\$50,000	\$100,000
End of year 1	\$50,000	\$100,000	\$200,000

End of year 2	\$100,000	\$200,000	\$400,000
End of year 3	\$200,000	\$400,000	\$800,000

The most incredible thing about these numbers is that they are realistic! Remember, this is just 1.5% per week—nothing too extraordinary on its own, but when you combine it with the power of compounding, you get extremely large returns on your capital. This is just one of the reasons why successful trading can be done without spending hours and hours per day in front of the screen. You could hit your first weekly target on Monday morning and be done for the week. This also demonstrates the concept of quality over quantity. Once you fully appreciate the fact that making a lot of money doesn't necessarily consist of placing a lot of trades, you will feel released from chasing down every potential trading opportunity that comes your way. That is proper fund management.

You need to understand that, at this point, you have not drawn any money out of your trading account yet. Instead, you have just allowed the account to grow through consistent profitable trading. Although this is a good thing, if you never take any money out, you obviously never get to enjoy any of the benefits! So, at the moment, we are only halfway there as far as our overall income and growth plan is concerned.

Income and Growth

The goal is to be able to draw a suitable amount of money to enjoy life while leaving enough money in the account to allow it to grow at a compounding rate. Achieving this allows you to continually increase the amount you drawdown without your actions having a negative effect on your trading account. Basically, you do not want your trading account to shrink as you withdraw money from it—that is not sustainable account management.

Here is an example of how to create the income and growth plan. Let's consider the following figure from earlier with the starting capital of \$50,000. We will keep the same target of 6% growth per month. This time, however, we are going to draw half of the profit out each month—3% comes out as income and 3% stays in as growth over the same three year period.

6% Monthly return doubles capital annually – 100% gross return		
Seed Capital	Account After Year 1	Annualized Income
\$50,000	\$75,000	\$25,000

6% Monthly return doubles capital annually—100% gross return		
Capital at Start of Year 2	Account after Year 2	Annualized Income—Year 2
\$75,000	\$112,500	\$37,500

6% Monthly return doubles capital annually – 100% gross return		
Capital at Start of Year 3	Account after Year 3	Annualized Income—Year 3
\$112,500	\$168,750	\$56,250

By now you should be getting a feel for how this thing works. And here is the great news: 6% growth per month is for beginners. We have students achieving up to and beyond 20% growth on their accounts consistently. Just imagine what that would do for the numbers above.

It should also be clear that the more money you have to trade, the more money you can make. Just think of it like this: 2% of \$100,000 is much greater than 2% of \$1,000. Now, that is not meant to put you off the idea of trading if you don't have much to start with. That is meant to encourage you to get started with whatever you have right away—you must start growing your money right now!

Let's take another look at some numbers. If 6% per month doubles your trading capital annually, then 12% quadruples it—400% return per year. This is why Albert Einstein described compounding numbers as the most powerful force in the universe.

Please go to our website and download our “trade your way” spreadsheet. This allows you to plug in figures of growth and income specific to you.

<http://www.learntotrade.com.au/assets-cta/uploads/2015/04/tradeyourway.xls>

The purpose of this spread sheet is to bring clarity to your journey of financial freedom. It allows you to chart the progress of your trading profit and plug it into your personal financial situation. With this spreadsheet, you can plan with accuracy when you will be able to replace your current income and become financially free.

A small percentage of a big pie...

As we draw to a close, there is a very important saying that I would like to leave you with. It goes like this: “A small percentage of a lot of money equals a lot of money.” This is the attitude of traders who achieve sustainable, large amounts of profit consistently on a long-term basis.

The FX market trades several trillion dollars on a daily basis. Your task is to take the tiniest percentages from this market consistently. Imagine you were able to generate just \$5,000 dollars a week in profit from FX trading. Your profit would have no impact at all on the market, but it would have a massive impact on your personal financial position. This is why we can say, “A small percentage of a lot of money equals a lot of money.”

You could also look at it like this: if there are trillions of dollars moving around every single day, there must also be an almost infinite number of pips moving around daily. Imagine if you could grab 250 pips a day out of a market that provides an endless amount of opportunities.

Bring this Book to Life

The biggest mistake you could make would be to read this entire book and then walk away and do nothing with the information. The FX world is full of information gatherers who have read books, paid for courses, and attended introductory seminars but failed to ever get serious, get stuck in, and take action. You cannot afford to be one of those people.

Those people never make it as FX traders because they fail to implement the information they gather. They are full of excuses and self pity. We have a saying at Learn To Trade that goes like this: “Information without implementation is DEAD.” Nature provides us with a clear and powerful demonstration of this point—it’s called the Dead Sea.

The Dead Sea is a body of water that is located in the Middle East between the nations of Israel and Jordan. As the name implies, there is nothing at all living in the Dead Sea—no plants or animals. In fact, the Dead Sea is so dead that, due to the high levels of salt in the water, you can actually float on top of it! The question is, “Why is it so dead?”

Less than 200 miles north of the Dead Sea is a thriving body of water known as the Sea of Galilee. There are small fishing villages and even cities located all around the shores of this lush body of water. The interesting thing about the relationship between these two bodies of water is that the outflow of the Sea of Galilee is the inflow of the Dead Sea—the river Jordan connects the two. So, given that both bodies of water are located relatively close together (fewer than 200 miles) and that the inflow of the Dead Sea is actually the outflow of the Sea of Galilee, you would expect both bodies of water to be similar, but they are not. One is full of life and the other is completely dead. So what is the difference?

The difference is the **OUTFLOW**. The Sea of Galilee has more than just an inflow, it also has an outflow: the river Jordan. The outflow stops the water from becoming stale and dense, and keeps it fresh and full of life. The Dead Sea, however, only has an inflow and, because there is no outflow, everything is dead. The Dead Sea is not useful for creating or sustaining life in any way, shape, or form. It is basically good for nothing.

At the moment, the information you have taken in through reading this book is dead. It hasn’t benefitted you or enhanced your lifestyle at all. It has simply served its purpose in bringing you the required information to begin trading the FX market successfully. It is up to you to bring it to life! You do this by giving it an outflow. So don’t waste any time in getting started. Go do it now!

Success is a habit—It's not what you do once in a while; it's everyday

If I spent a day with you, I would be able to tell how successful you would end up. People often find this a somewhat pompous statement, but I don't mean it to be that. I say it because it's true. The point here is that the secret to your success lies in your daily schedule: what you do consistently, you become.

If you want to change your life, change your daily schedule. It's pretty obvious that good decisions create a better destiny, yet many people don't appear to link up their apparent lack of success to poor decision making. Some people make choices and go on to experience poor results—yet these people wonder why they can't seem to get ahead in life. They never connect the dots. Other people, such as smokers, are aware that their choices may not be good for them, but they carry on regardless—there may, after all, be some secondary gain associated with the smoking, such as the smoker getting a break from the office or getting the chance to connect and have some rapport with other smokers.

The point is, nobody says that good decisions are always simple, but they are necessary for success.

You start to win the game of life by making better decisions. One of those would be to take action now, immediately after reading this book. As you embark upon this exciting journey as a trader, there are also some important things you need to decide to be, in order to have. The well-used phrase, "Be-Do-Have," springs to mind here. We must *be* a certain person, in order to *do* or act in a certain way, to allow us to *have* the things that we want.

To help with this, here is my behavioural checklist, that whilst you may not 'instantly' become, should be your heading - daily.

Attitude: Develop the right attitude and exhibit it daily.

Be responsible: Stop blaming everyone and own your results. Only through this strategy do you give yourself the power to change the results.

Greg Secker & Chris Weaver

Prioritize: Do the important stuff first; read e-mails at the end of the day.

Commitment: Keep your promises; commit to making yourself a success every day.

Faith: Deepen your faith and practice it daily.