

FOREX TREND LINE TRADING STRATEGY



IT IS HARD TO WIN WITHOUT
KNOWING THE TREND

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Forex Trend line Trading Strategy

(It is hard to win without knowing the trend)

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Disclaimer:

Foreign exchange trading carries a high level of risk and may not be suitable for you, please carefully consider your risk appetite and do not invest money that you cannot afford to lose

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DEDICATION:

To those who are serious in forex trading

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Preface

What do you think when a mobile phone trader still accumulates old model phones while the trend now is smartphone with bigger screen? Yes, the trader will lose money and need to sell them cheap or execute a 'cut loss' action as the trend now is smartphone.

Same in foreign exchange trading, you need to know and monitor the market trend too; you will go against the market if you're still in buying position while the market trend is selling. It is a big mistake if you go against the market with your confidence.

As a trader, understanding the market trend is more important than understanding technical skills. Market trend provides price movement information on macro perspective while technical skills are more on taking advantage on the macro situation. Without knowing the market trend, it is hard to win.

Imagine that you are a soldier with special assignment to free a hostage, what will you do first? First you may learn enemy's macro situation such as: the location, enemy's habits/activities, concentration of soldiers, etc. Once you know the situation you will bring necessary weapons/tools. If you know the macro situation well, you may not need many tools/weapons with you.

Imagine that you are a forex trader with special assignment to make money, what do you do first? First you may learn the forex chart macro situation such as: currency to trade (location), current price position/movement (habits/activities), the trend (concentration of soldiers), etc. Once you know the chart macro situation you will need technical analysis tools such as MACD, RSI, DMI, Stochastic, etc. If you know the forex chart

macro situation well, you may not need many technical analysis tools.

This book will give guidance step by step on how to set up trend lines and how to react when it breaks the trend line. There is no long and boring explanation, and no need special skill to understand it. You only need basic understanding of opening, closing, highest and lowest price in candle stick bar or any other chart bar.

Good luck!

CHAPTER 1

TREND LINE IS ONE OF THE MOST IMPORTANT TOOLS

What is trend line?

Trend line is a tool to guide traders on the macro perspective of price trend which enable traders to know their trading position whether it goes against the market or follows the market. The trend line provides a support and resistance line for the market price.

Trend line can also be explained as follows:

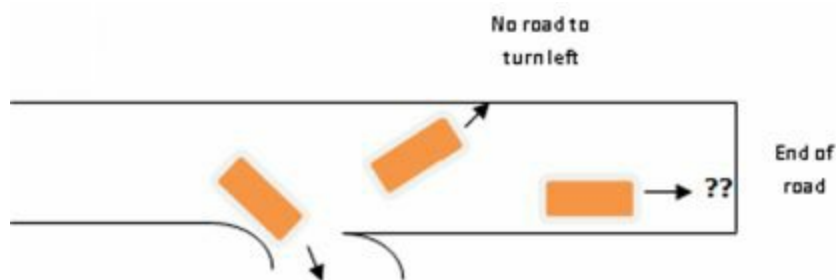
Imagine this is your orange color car:



Question 1: where is the road? Now we draw the road to make it clearer



Question 2: Is your car always in this position? No, your car may have several positions: it may turn right, go straight, or turn left.



Why do we need trend line?

Trend line is like a road structure, it tells people whether there is a road to turn left or right or go straight. Without knowing the road structure, people could have an accident such as they turn left while no road to turn left.

Where can we see the trend line in forex chart?

Trend line can be setup in most technical analysis program. Setting up a trend line seems like an art, depends on the length of period interpretation to find high and low price. Actually, it is not an art, and in the next chapter, this book will show step by step ways to set up trend line in a simple way.

When we should use trend line?

Before trading, we should prepare and update the trend line first to map the market trend and to locate where we are now.

CHAPTER 2

SETTING UP TREND LINE

Most technical analysis programs are enabling you to set up trend line but it is not an automatic program, you should do it manually. Most professional technical traders are using trend line to find potential support and resistance lines for the market price movement.

What do we need?

1. Technical Indicator Parabolic SAR
2. Drawing line tools

1. Technical Indicator Parabolic SAR (SAR)

This indicator is developed by Welles Wilder in his book *New Concepts in Technical Trading* and become very popular tools in technical analysis. SAR stands for “Stop and Reverse”.

The standard parameter for SAR is (0.02, 0.2) means incremental step parameter 0.02 and maximum step 0.2



Chart 1 – Standard Parabolic SAR

How to interpret standard SAR?

If the SAR dot below price, means the trend is up, if the SAR dot above price means the trend is down.

Non standard SAR

Standard SAR parameter is too fluctuating and hard to see the longer trend of the price. To draw a trend line, we need more stable SAR parameter to see clearer picture of longer trend.

The non standard SAR is **(0.02, 0)** means incremental step parameter is still 0.02 but maximum step is 0.



Chart 2- Non Standard SAR gives more stable trend

2. Drawing line tools

Once we know the longer trend with non standard SAR (0.02,0) here are the next steps:

1. Determine two latest up and down trend in SAR group
2. Determine the highest and lowest price among the two uptrend and down trend SAR group
3. Draw lines among the highest and lowest price from those SAR group



Chart 3 – Drawing trend line

A and B are the highest price between the 2 uptrend SAR group and we can draw a line to connect A and B to become a resistance line for future up trend price movement

C and D are the lowest price between the 2 down trend SAR group and we can draw line to connect C and D to become a support line for future down trend price movement.

Another example:



Chart 4 – Drawing trend line

Now you can try to draw trend lines from this chart, remember to use the latest SAR group.



Chart 5- example

Answer:

1. Determine two latest up and down trend in SAR group



Chart 6

2. Determine the highest and lowest price among the two uptrend and down trend SAR group

Within group 1 and 2 - down trend SAR (SAR dot above price), C and D are the lowest price

Within group 3 and 4 - up trend SAR (SAR dot below price), A and B are the

highest price



Chart 7

3. Draw lines among the highest and lowest price from those SAR group. Draw highest and lowest line between A and B to create resistance line, C and D to create support line.

This non standard SAR (0.02,0) can be applied to any currency and it is preferred for **1 hour time frame**.

Other examples:



Chart 8 – Another example

CHAPTER 3

TREND LINE TRADING STRATEGY

1. Price close 2 times in a row above/below trend line (breaks support/resistance line)

Once we know how to setup trend line, the next step is to prepare a strategy. We are looking for price closing above or below trend line (support or resistance line) 2 times in a row. We may use other technical analysis tool such as MACD, RSI, DMI, Stochastic, etc. to confirm this strategy.



Chart 9 – Trading Strategy, Price breaks trend line/resistance



Chart 10 – Price breaks trend line



Chart 11 – Price breaks trend line

What happen if there is a false signal? If it is a false signal, the price tends to touch the existing support/resistance line.



Chart 12 – False signal

2. Price movement between the trend lines

Another strategy is playing with the price swing between the trend lines or support and resistance lines when the closing price cannot break the trend lines 2 times in a row or it is a false signal. This strategy sometimes is not easy to follow due to fast price movement/swing between the trend lines. We need tools to play fast and safe to explore more opportunities in between the trend lines. If you are interested to play with the price swing, you can explore it more in author's book "Forex Secret Trading Model; Tools, Timing, and Forecasting").

CHAPTER 4

TIME FRAME AND MONEY MANAGEMENT

There are plenty of time frame in forex trading such as 5 minutes, 10 minutes, 15 minutes, 30 minutes, 1 hour, 2 hours, 4 hours, 8 hours, 12 hours, daily, weekly, monthly. All the time frames are fine for trading. If you are familiar with 15 minutes or 1 hour time frame, you need to be consistent with it.

Time Frame

The weaknesses of lower timeframe (1 hour or less) are:

1. Smaller profit :Profit is usually taken faster due short term price fluctuation (usually 10-50 pips)
2. More false signal in technical analysis

The benefits of lower time frame are:

- a. Profit may be obtained several time within a day
- b. Faster info on the price trend

The weaknesses of higher time frames (more than 1 hour):

1. Profit may not be obtained several times within a day
2. Slower in knowing the price trend

The Benefits of higher time frame are:

1. Bigger profit potential (more than 50 pips)
2. Less false signal in technical analysis

As a trader, it is preferred to use 1 hour or lower time frames due to uncertainty in market news and other factors. As mentioned above, lower time frame gives faster info on the price trend.

Money Management:

1. Loss : win ratio

In many forex trading books, it is recommended that your loss:win ratio minimum 1:1 means if you have stop loss 1, you need to set potential profit 1. In practice we can say if your stop loss is 30 pips than your potential profit needs to be set 30 pips too. The ideal ratio is 1:3 (lose 1: win 3) but it is not easy to get this ratio in some situations.

Ratio 1:1 is enough in this trend line trading strategy, because you have reduced the risk or increase profit probability. Lets' say you can increase your profit probability to 75%, which means you will have more than 1:1 ratio in long term. It will be 1: 1.33 ratio ($1.33 = 1/75\%$). To make it simple: if you are 100% sure that you are right and you put a stop loss 30 pips as a requirement to get 30 pips gain, do you think your real loss:win ratio is 1:1? I would say your loss:win ratio is 0:1. So 1:1 ratio is not the true ratio because it depends on how you can decrease the loss risk or increase the winning chance.

2. Trading fund ratio

To become a long term trader in forex trading, we need to maintain trading fund ratio maximum 10%, which means if you have fund balance \$ 10,000 than your maximum stop loss position (total) is $10\% \times \$ 10,000 = \$ 1,000$. You can have several trading positions but the total stop loss still maximum \$ 1,000. When you have higher fund balance, you can lower it to 5% ratio or less depends on your risk appetite.

Some online forex trading systems allow you to deposit fund \$ 300, and with this amount of fund, you can calculate the maximum trading fund ratio $10\% \times \$ 300 = \$ 30$, means your stop loss value is \$ 30 or around 1 trading position.

New traders always want to make big money quickly so they may put trading fund ratio 50% or more however this is not recommended for long term trader. The market is not as simple as it is.

Table 1 below will give you an illustration of trading fund and number of position you can place. 30 pips stop loss is just an illustration, you can modify it to 40 or 50 pips.

	(A)	(B= A x 10%)	(C=B)	(D=A+C)	(B/30 pips stop loss)
			Ratio 1:1		
No	balance	stop loss	gain	balance	position
1	300	30	30	330	1
2	330	33	33	363	1
3	363	36	36	399	1
4	399	40	40	439	1
5	439	44	44	483	1
6	483	48	48	531	2
7	531	53	53	585	2
8	585	58	58	643	2
9	643	64	64	707	2
10	707	71	71	778	2
11	778	78	78	856	3
12	856	86	86	942	3
13	942	94	94	1.036	3
14	1.036	104	104	1.139	3
15	1.139	114	114	1.253	4
16	1.253	125	125	1.378	4
17	1.378	138	138	1.516	5
18	1.516	152	152	1.668	5
19	1.668	167	167	1.835	6
20	1.835	183	183	2.018	6

Table 1-Trading fund and numbers of position

CHAPTER 5

CURRENCIES SELECTION

There are many currencies to trade however we do not trade them all. Currencies selection is important in forex trading and try to focus on 2 or 3 currencies first. Some common currencies for trading are:

EUR/USD	EUR/GBP
GBP/USD	USD/JPY
AUD/USD	GBP/JPY
NZD/USD	AUD/JPY
USD/CHF	NZD/JPY
USD/CAD	EUR/JPY
EUR/AUD	CHF/JPY

Table 2 – Common currencies for trading

The criteria to select currencies for trading:

1. The price spreading or differences between buying and selling price are not too wide as this will refer to liquidity and volatility. If you see

EUR/USD price spreading is narrow than GBP/USD, and then it is better to select EUR/USD currency for your trading.

2. Do not put your eggs in one basket. Means, if you already select EUR/USD currency, try not to trade the same base currency such as GBP/USD, AUD/USD, and NZD/USD. If you want to trade EUR currency; for diversification, you can select EUR/USD, EUR/JPY or EUR/AUD or EUR/GBP

Sometimes you may notice that EUR/USD currencies doesn't move but GBP/USD or AUD/USD moves and this creates frustration because you are holding EUR/USD and regret that you does not hold GBP/USD or AUD/USD; but don't forget that most of the time EUR/USD, GBP/USD and AUD/USD are moving to the same way as they are having the same group trading partner, USD. However if you diversification is EUR/AUD or EUR/GBP, no movement in EUR/USD will be covered by movement in EUR/AUD and EUR/GBP.

There is also possible that EUR/USD is going up but AUD/USD going down, if you have these 2 positions, they may be in break even position because one position is up and the other is down. You may also buy EUR/USD and Sell AUD/USD, but it is not an easy decision because the buying and selling position are in the same currency basket (USD). The diversification will be better on EUR/USD and EUR/AUD; you make money from EUR/USD but break even in EUR/AUD.

CHAPTER 6

EXERCISES AND ANSWERS

In this chapter you can do some exercises yourself and then compare them to the

answers. Try not to find the answers before trying them first.

Exercise 1:

Please draw trend lines (support and Resistance) and buying/selling point from this chart.



Answer 1:



Exercise 2:

Please draw trend lines (support and Resistance) and buying/selling point from this chart.



Answer 2:



Exercise 3:

Please draw trend lines (support and Resistance) and buying/selling point from this chart.



Answer 3:



Exercise 4:

Please draw trend lines (support and Resistance) and buying/selling point from this

chart.



Answer 4:

USD/JPY, 1 hour
SAR 0.02;0



Exercise 5:

Please draw trend lines (support and Resistance) and buying/selling point from this chart.



Answer 5:



CHAPTER 7

QUESTIONS AND ANSWERS

1. Do I need forex financial news or announcements?

Not all of us are superman with supersonic ears and laser eyes. The big guys may have these capabilities that enable them to act faster, even before the announcement. They may have their own teams to do research and forecast to get a view before the announcement. The other thing is, when the forex news announced, you will be too late to hear and respond it, so just focus on the forex chart as it reflects the market action before and after the announcements.

If the announcement is negative news and according to theory the price should go down but suddenly it goes up, what are you going to do? Stick to the theory and go against the market or follow the market? There are many interpretation of news and you do not know which parties are going to win or lose in buying and selling action. Remember, it is a market, not a school and in the market, understanding the price trend is more important than proving the theory is right or wrong.

2. Can I use trend line strategy in stock market trading?

In general you can use trend line strategy in stock market trading however it is better not to use it as a main judgment in buying and selling. Stock market and forex market are having different approach in analysis. Fundamental analysis is more important in stock market while in forex market, chart reading is more important.

In forex market, looking at a country currency needs macro approach and there are so many factors affect it such as: inflation, interest rate, unemployment, GDP, industries output, business confident level, politics, central bank intervention and other many factors that sometimes contra each other; so chart is the best way to see all these factors.

In stock market, looking at a company performance needs micro approach and fundamental analysis is the base way to make decision. The fundamental analysis is looking at profit and loss statement, balance sheet, cash flows and potential future earning information. Warren Buffets has proven this without looking at the market chart.

3. Should I update the trend line when the non standard SAR reverses?

Yes, you need to draw a new updated trend line after it reverses, you can still leave several old trend lines (around 3 - 5 support and resistance lines) in the chart as they are still valid support and resistance lines for future price movement.

4. Can I use the non standard SAR for higher time frame i.e. 4 hours, 8 hours, 1 day or even monthly?

Yes, the non standard SAR can be applied to higher time frames or even lower time frames other than 1 hour. For higher time frames, they may require higher stop loss position and longer time to get the break out confirmation. For lower time frames other than 1 hour, they may be more volatility expected.

5. What is the best technical analysis tools to use, MACD? RSI? Stochastic? DMI? Or others?

There is no best technical analysis tool to use in forex trading, each one has its own strength and weaknesses and any of them can be used to make profit. This question is similar to: what weapons is the best to kill an enemy? Or which one is the best among Kungfu, Karate, Aikido, Judo, etc? No answers for it. It is better to master 1 skill deeply

so you know when, where and how to use it at the right moment.