The Training Wheels Forex Trading Manual

v1.1, November 2011

1. Introduction

My path to becoming a forex trader was as follows:- first, due to the high Australian dollar, my employer was having trouble selling products overseas and needed to cut back on its expenses, as a result of which I was one of several who were laid off.

Being a computer programmer in his 40s, seeing few jobs advertised and feeling pretty deflated from losing my job, I decided it was time to work for myself by trading the stockmarket, which I'd done part-time for several years. That all went well until the markets went seriously pear shaped in August 2011. I needed something where I could short the market and profit from moves in either direction, so I turned to Forex.

I quickly discovered that all my methods for trading shares were of little use in Forex. There was no concept of accumulation or distribution, which is what I was used to working with, and after blowing a couple of demo accounts I knew I needed to find a method that would consistently get me into successful trades while keeping me out of bad ones. So I did what all n00bs do, I searched online forums, reading dozens of trading method threads. I downloaded and tested bucketloads of indicators, even wrote some of my own.

Eventually I developed a trend-following method that seemed to be working ok, and went live with it. Then I joined a forex chatroom, where several experienced traders derided the whole idea of using indicators, and were trading reversals, so thinking they were smarter than I, I discarded my system and tried to adopt their methods instead. As a direct result, within 3 weeks I had lost 60% of my account. It wasn't the good people of the chatroom who were to blame, it was my own fault for abandoning what worked for me and trying something that takes years to master.

See the problem with Forex is that there are no rules. In every other career, there are rules you must follow to do your job well, but there's probably as many ways to trade Forex as there are traders. That freedom can kill your account. If you trade without rules, your emotions and "gut instinct" take over your decision making, and for most people that will bring out all their worst character flaws. You'll be afraid to take opportunities that are staring you in the face, thinking "what if it goes against me". You'll pre-empt trend changes, going against the momentum of the markets thinking that surely this is the top (or bottom), and at the end of the day you'll look back and think if only you'd traded with the trend instead. You'll snatch at profits instead of letting winners run, you'll let winners run when they're clearly turning against you, and you'll shift your stop losses (or not use them at all!!) thinking its ok, the market will turn back your way, no need to take a loss.

So I realised that I needed a fixed set of rules to follow that worked for me. It needed to get me in good movements, and prevent my bad habits from taking over. In particular, I wanted to follow trends and enter on pullbacks, and to avoid trading any reversals, and after a lot of research and experimentation this is what I came up with. Trading this method is netting me steady consistent profits, and I'm gradually earning back the money I so quickly and easily lost when trading without a system.

I've called this method Training Wheels, because its written not for experienced traders who know what they're doing, but for new traders who are grasping at straws, wondering how on earth they can possibly make a go at this taking losses day after day, and losing all confidence in their trading. I've also called it that because quite a few of the indicators in the method can be dropped, I hope, once the trader has gained confidence in what they're doing and are finding the indicators redundant. Yes that includes me too.

If you're in that position and realise you need to stop trading from the hip and start following rules that work, perhaps this will be of use to you. If, however, you don't want to restrict yourself to a set of rules governing when and how you trade, then please don't read any further.

If you want to trade reversals and pick tops & bottoms, please look elsewhere as well as this won't fit you either.

It does not guarantee any amount of pips per day, as the market sets that. Some days it runs, but others it grinds sideways or chops around with no direction. What the Training Wheels will do is provide sound entry and exit points to try and make the most of what is on offer.

It is not a system that can be turned into a successful EA, at least I'd be incredibly surprised if it could. And that would defeat the purpose, which is to help you (and me) learn to become a good trader, which can only be done by manual trading.

If you want to capture every market movement, and have an array of dozens of entry and exit setups to choose from, this isn't your system. I looked for just a few that worked, occurred regularly, that I could trade consistently and make a profit from, and that's what I'm offering here.

One last word – you may come across veteran forex traders who tell you that indicators are all rubbish, designed to make you lose, and that pure price action is the way to go. They are almost certainly right that price action is the best way to trade, but that does not help the newcomer who lacks the skills to understand what the price is doing and how to trade it. Some indicators serve specific purposes and do it very well, and its really about how you use them. Like any tool they can be used properly, or for tasks they weren't designed for with predictable results. The indicators in this method have been carefully selected and tuned to help you understand the price action, and assist you in quickly making trade decisions.

2. Legal Disclaimer

Trading foreign currencies is and extremely risky activity but is potentially a profitable opportunity for educated and experienced investors. Before deciding to participate in the Forex market, you should carefully consider your investment objectives, level of experience and risk appetite. Most importantly, do not invest money you cannot afford to lose. There is considerable exposure to risk in any foreign exchange transaction. Any transaction involving currencies involves risks including, but not limited to, the potential for changing political and/or economic conditions that may substantially affect the price or liquidity of a currency, the risk of settlement discrepancies, broker errors and malfeasance, outright fraud and many others.

Moreover, the leveraged nature of FX trading means that any market movement will have an equally proportional effect on your deposited funds. This may work against you as well as for you. The possibility exists that you could sustain a total loss of all initially deposited margin funds and be required to deposit additional funds to maintain your position with any given broker. If you fail to meet any margin calls within the time prescribed, your trading position may be liquidated and you may be responsible for any resulting losses, including amounts potentially more than your deposit. The content provided herein is put forward in good faith and believed to be accurate and effective, however, there are no explicit or implicit warranties of any kind made in connection with this information. Should you choose to use this strategy, you will be trading exclusively at your own risk of your own free will.

By using this method, the reader (thats you!) agrees not to hold the author of this information, or any of his or hers affiliates, assigns, or heirs liable for and to explicitly hold harmless from any decisions that you make based on information contained in this document, or any information found on any electronic forum or from any email discussing this strategy, no matter where it is or where this method was put forward.

3. The Secrets of Trading

I've copied this largely verbatim from "The Simple Dance" trading manual by Clay Ferrell - I hope he doesn't mind. It is an absolutely brilliant introduction on what to expect from Forex trading, what your goals should be and how to go about becoming a successful trader. I saw no point in re-inventing the wheel in my own words, so here goes:-

Everyone wants to know the secrets of trading. They are pretty simple really and the true secrets have absolutely NOTHING to do with a particular strategy. They ARE about YOU personally and how YOU operate in life. That is the main reason no one wants to believe them and why they remain "secret." These secrets are hidden in plain sight for all to see and learn freely. It is other people who want to make money trying to sell you some great system or strategy that supposedly they alone have been able to figure out that cause all the confusion in trading. Supposedly their "system" allows them to unlock the "secrets" of trading consistently and profitably.

So, in this first part of the manual, I'm going to list the most profitable secrets there are anywhere of trading successfully. The secrets are as follows.

Secret #1: Stick to ONE strategy.
Find a strategy that makes sense to you and stick to it and it alone like a faithful wife and master it. This is probably the single greatest secret in all of trading. Master ONE strategy. There are no "systems" only strategies that work if you master them. If you jump around from one to another you will never master anything and be forever locked in the sucker's dream of "the system" or the "Holy Grail" of trading. The truth is, all strategies work for the ones using them if they will learn to master them.

Secret #2: YOU are the main secret in trading.
You are the greatest secret in trading. You have been gifted with the fastest computer known to man at your birth and you have the ability to learn, adapt and modify everything you see and come into contact with. The way you "see" things is very different than the way other's "see" things. If you can master "you" and your emotions about trading (talked about in another of the "secrets), you WILL become successful. And that leads us to secret #3.

Secret #3: Simpler is better.
Simpler is always better. The more complex a strategy is, the harder to learn it will be and the easier it will be to make mistakes that will shake your confidence, slow you down and cost you, possibly, years in mastering trading. Anyone who says differently probably has a "system" to sell you.

Secret #4: Accept the "numbers game" view of it.
Mastering trading is not hard. It's just an issue of accepting the "numbers game" of it all. All things have a "probability" ratio or a "numbers game" that creates the success of the effort. Whether it's sports, industry, sales or trading, there is a "numbers game" behind it all. The more you can find an "edge" something you can exploit, the faster you will become will become consistent at your effort and that consistency leads to success.

Secret #5: Master yourself, master your trading.
Your own emotions are the only real "enemy" in all of trading. Brokers who manipulate price feeds cannot defeat you. Market makers who charge large spreads cannot defeat you. The news cannot defeat you. Changing markets cannot defeat you.

Greed is extremely deceptive. It's not wanting to have large accounts, it's not wanting to be wealthy. In trading, greed is none of the normal things you are taught it is. In trading, it's wanting to get that next point when the strategy says your done. It's wanting 30 points when the strategy's rules say 15 is enough. It's wanting to swing for the fences on every single trade. Greed is not being willing to take it slow and allow it to grow. It's not allowing compounding to work and wanting to have it "now."

Fear will kill your trading and add years to your effort of being successful. The rules of any strategy are designed to take the emotions out of your trading. Allowing yourself to "second guess" the rules is fear. Not taking a trade instantly on the signal is fear. Exiting a trade before the rules call for is fear. Anything that keeps you from following your rules is fear and it short circuits all of your efforts and all of your training and adds years to your trading and robs you of success. You must eliminate it from your trading.

Revenge will destroy you as well. You are not the target of any great conspiracy and the market couldn't care less about your trade or your position. The brokers may want you to be a victim, but trading out of a desire for revenge will skew your thought and twist what you "see" on the charts. It will defeat you as will greed and fear.

Arrogance will destroy you just as fast as either of these others. Trading from the perspective of any emotion will kill your trading. Arrogance will do it just as fast as greed, fear or revenge. You are NOT mistake proof. Even IF you believe you have mastered a strategy, any strategy you will still make mistakes. Arrogance will lead you to even bigger mistakes, then to revenge to try to make up for it, then to greed to try to get "just a little more" so you can earn back what you lost.

Complacency threatens to bite you after a few good trades. Suddenly you feel bulletproof, and the next thing you know you've made lazy mistakes, abandoned the rules that got you in those good trades, and you're handing back the money you earned. Each trade has nothing to do with the one before and needs just as much attention, caution and care.

Secret #6: There are no makeup trades.
Trade each trade and each session as if it were the only one. Yesterday is gone and does not deserve to be remembered in trading. The only thing that exists in successful, consistent trading is the trade you are about to place. Make it the best on possible and forget the past so your emotions don't have a place to take hold on you.

Secret #7: Persistence and attitude will overcome everything.
If you believe you can do this, you can. If you do not believe that, quit now. Nothing can stop or defeat you but you. That is true of

everything in life, not just trading. It does however apply specifically to trading. Never ever listen to anyone who says you can't trade.

Secret #8: If it's not boring, you are NOT trading correctly.
People love excitement and things that are interesting. SOLID trading is exceptionally boring. One of the hardest battles you will fight is to just trade and not try to "fix it" or "improve it." or worse, get impatient and "wing it".

Secret #9: Some days you just have bad days !
Every single athlete of any sport in any age has faced the "gremlins" of a bad day when for no apparent reason, someone whose skill and physical prowess are not even close simply trashes them. There are no reasons, to rationales, no analysis that can stop it. It will happen, but you can limit it! Trading is no different.

This is the reason for rules. They are to supersede your mind, instincts, emotions and all of your efforts to overcome it, which runs counter to everything we have ever been taught in life. STOP! Walk away when you start violating ANY rules, ESPECIALLY the 6 winning trades and STOP or the THREE LOSS and STOP rules!

If you're ever, ever, tempted to not set stop losses as you're sure the market's going your way, STOP TRADING AND WALK AWAY. If you have positions that are open without stops, close them immediately, even at a loss, and shutdown your computer. If you keep trading you will undo days, weeks of hard work in one session.

LEARN to limit your arrogance and pride of how good you have become, or how good your strategy is. LEARN to limit your losses! Follow the RULES!

4. The Basic Rules

Time frame: Whatever you choose, from 1 minute to monthly. The indicators automatically adjust their parameters for different timeframes, and the method works the same way for all of them. So pick a timeframe that suits your personality, the amount of time you can devote to trading and the length of time you prefer to hold.

My preference is to enter and exit on either the 5 minute or 15 minute charts, based on the inherent noise level in the pair I'm trading – the more random noise, the higher a timeframe is required. It works perfectly well on the 1 hour chart or higher. It also works on 1 minute charts if you are so inclined.

You'd trade exactly the same way on each timeframe. The quicker the timeframe, the more frequent your entries and exits, and the tighter your stops and profits. If you trade really well you'll make a lot of profit, but you have to be super-disciplined and know what you're doing. The longer the timeframe, the fewer the entry and exit points, but the greater the moves between them. Its your call which you use.

Indicators: Use only those provided on the list in the next section. Don't add to them, as it'll just confuse things. If you find that some in the list aren't helping you, then remove them - the simpler the better, and the less cluttered your screen the better you'll trade. That said they're there to help you and each plays a specific role.

Do Not Chase The Market! If you've missed an entry, so be it. There'll be plenty more, and you're taking huge risks in chasing the price. Don't do it.

Maximum Trades per Day: 6 successful ones, 3 failures. It will be galling to have to sit out if your first three trades hit their stops, particularly if you come back later and see highly tradable movements. The reason for this is that once you lose a few trades it **will** affect your mental and emotional state. You'll be tempted to start ignoring the rules and you'll do stupid things. Its for your own good - prevent loss, and walk away. By the same token, a run of successful trades feels great, and you'll be tempted to repeat it by ignoring the rules and thinking you're superman. Don't do it - prevent loss, keep your profit, and walk away. Tomorrow's a new day, you can start again then.

Respect your Stop Loss: If you fail to set stops, or move them away, you're courting disaster. We all get trades wrong, and even the best setups can turn to mud. Accept it, its nothing personal, cut it short and don't take a bigger loss than you need to.

One trade/pair at a time: Especially when you're starting. Trades need your full attention. Its your money on the line, don't be reckless by opening trades left right and centre. You won't do better by trying to catch every movement on every market - it'll bite you. Stick to one at a time and manage them well, and be content with that.

Risk Sizes: Risk no more than 2% of your capital at one time. This is not based on the margin committed to your entry, but how much you'll lose if your stops are hit. Consider adding to an existing profitable trade only at valid entry points, and where your stops from both the new entry and previous ones will protect you to at least breakeven level.

Entries and Exits: Use only the entries described in this manual. Using anything else is trading some other strategy, not this one. Take profit when the rules say to do so. Don't get greedy, don't hang out for more than the market is offering and in so doing lose your profit.

Trust the Indicators: They actually are correct most of the time. Don't trade counter to them. Don't pre-empt them. If they say the trend has changed, believe them and trade accordingly.

Fundamentals Analysis and News: Some people will tell you that you absolutely must be well informed and know about news releases as soon as they occur. I'm here to say that the markets have a mind of their own. They will rally hard in the face of disastrous news, and drop through the floor when all looks rosy, and if your thinking is influenced by "the news" then you will mistrust the signals this strategy provides, or even worse you'll trade against it, and you **will** miss major moves.

You do not want a fixed mindset of where the markets are going to go. You need to be relaxed and happy to change direction when the strategy says its changed, even if it means closing contrary orders at at loss – especially if it means that, because to hold them is to invite ruin into your account balance.

So don't stress about trying to understand why the market is doing what its doing. You don't need to know, really you don't. All you want to do is profit from its movements, whatever direction they may be in, and steadily add to your account. That's your mission here, not to become an economist.

Forums and Chatrooms: Trading forex on your own, day in day out, is a lonely business. Its natural to want company of like-minded people and to make friends. But there is a huge danger here. Enter a chatroom full of good (and bad, there's always a mix) traders and you'll be exposed to many different strategies and ideas. There'll be some people who'll set themselves up as experts and deride any trading calls that conflict with their views. You'll be tempted to doubt yourself and your methods and follow them, and it'll be so compelling, especially when everyone in the room agrees on a trade entry, that on occasion you'll do just that. How do you think I lost 60% of my account?

Stay away – I know its hard – but while you're trading stay out of forums and chatrooms. Concentrate on nothing but the strategy and its rules and trade accordingly. Do not allow distractions like this to ruin your profitability and destroy your confidence. Take it from someone who's been there. On the other hand if you can find other traders online who are trading the same strategy as you, take the opportunity to discuss trade setups with them as that's far better than struggling along on your own.

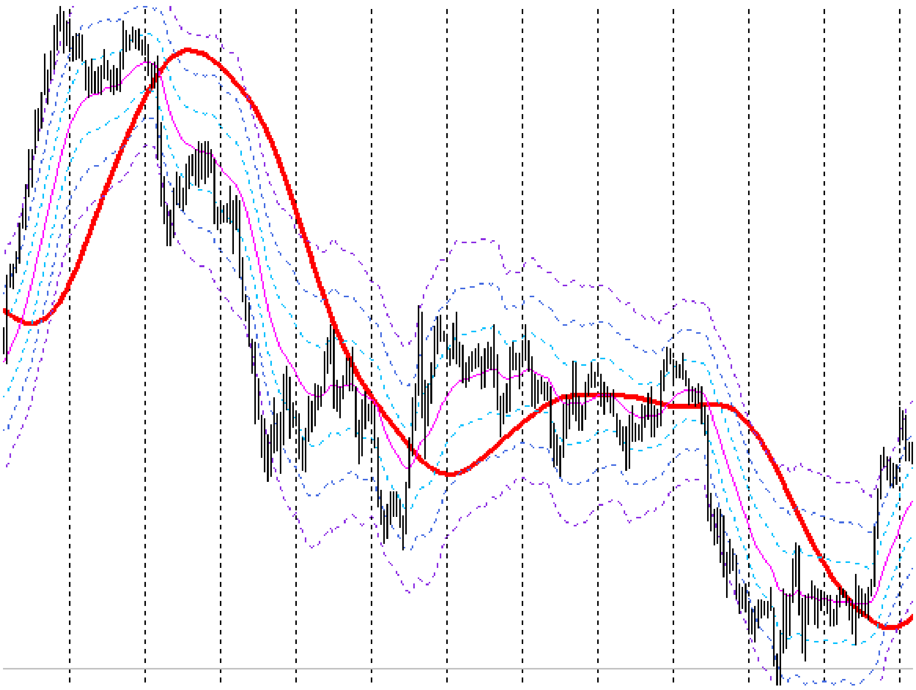
5. Indicators

As I mentioned previously, each of these indicators has been modified where necessary to make them automatically adjust to different timeframes. There should never be any need to go fiddling in the input parameters – they do what they're designed to do out of the box...

ATR Channels: Like a moving average, they clearly show whether the price is strongly trending or not, but unlike an MA they provide multiple lines for support and resistance. When the price moves to extremes in the channels you know that a retrace or reversal is becoming likely, remembering that the price will always want to return to the middle even in a trending market.

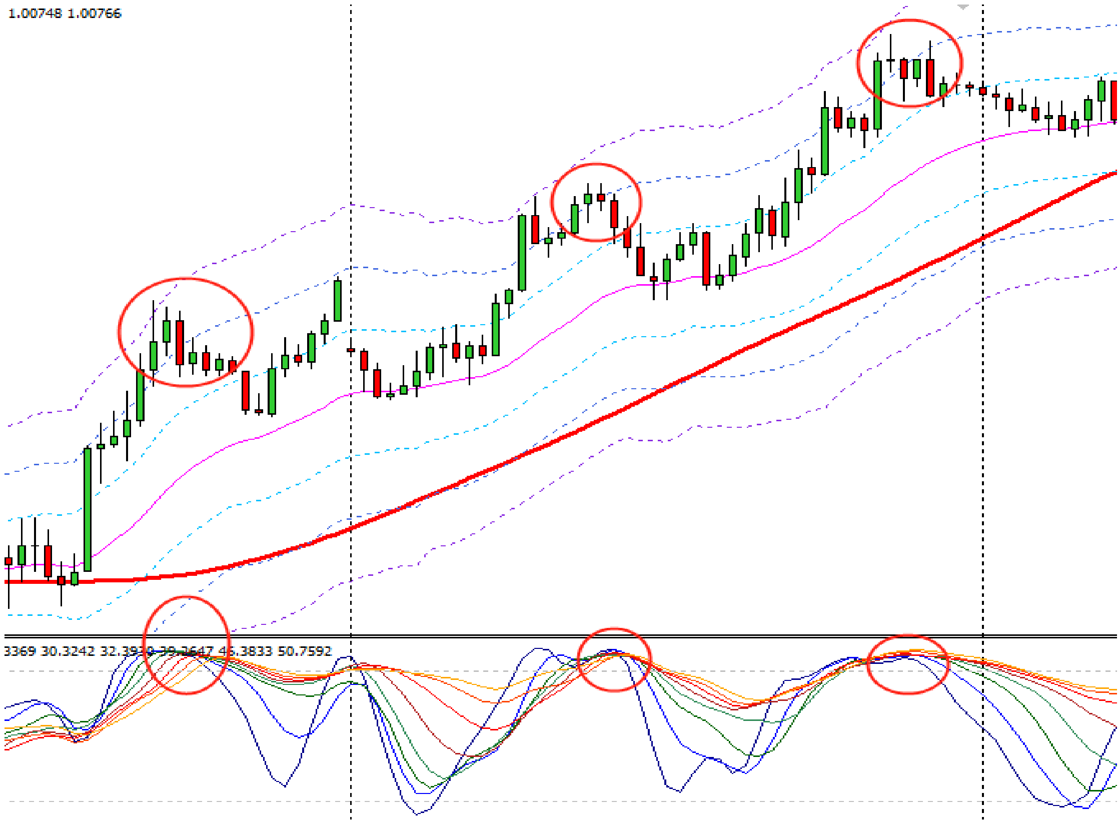
Trend Signal: This is a T3 moving average, configured so that overtakes trends when they become overheated and in need of a rest (or perhaps a reversal), letting you know when to take extra care on continuation trades, and when to consider the possibility that the trend has changed.   Note how in the following image, the Signal will overtake the price, and when it does it nearly always heralds either a consolidation or a reversal.

This is one of the key elements we use in deciding which direction to trade, and how long to keep trading.



End of Bar: This little gem is essential in my view, whatever strategy you follow. Simply its a countdown until the current candle ends. I prefer to enter close to the end of the current candle, rather than taking a risk early in its life or mid-stream.

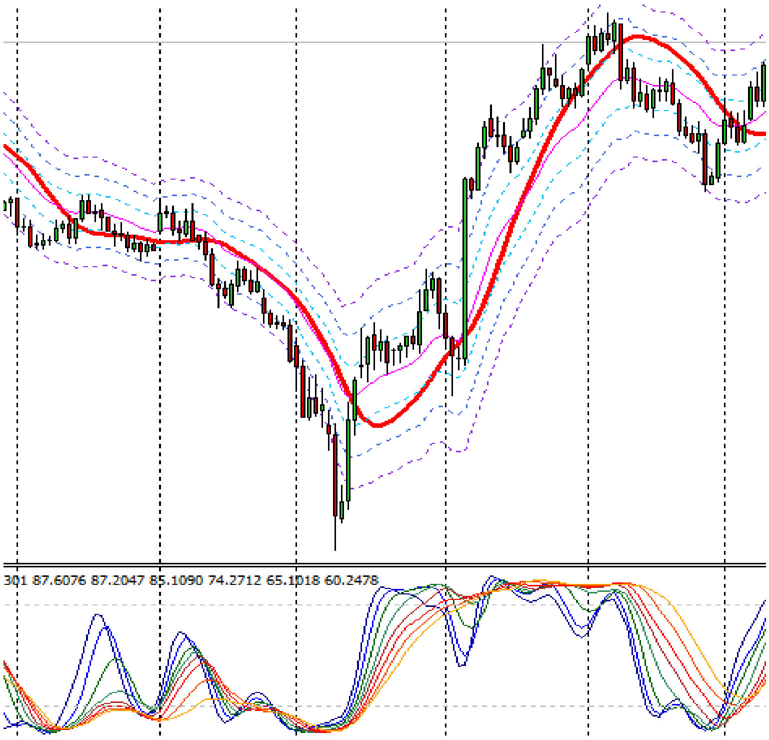
Stochastic Rainbow: In conjunction with the ATR channels, this is used to identify points at which to take profit, as illustrated on the following image. Its also used to help determine entry points on pullbacks.



6. Trading Step 1 – Determine the trend

This is the first thing to do every day before looking at any trades, as it decides the type of entries to look for and the methods to use.

You should do this by considering different timeframes, for instance:-



The Daily chart shows us that USDCHF is in an uptrend, having just finished a consolidation and started on what may be the next upleg. Its approaching the extreme ATR channels, so a pullback is possible – but as you can see when it likes to run it can stay in the extreme channel for quite some time.

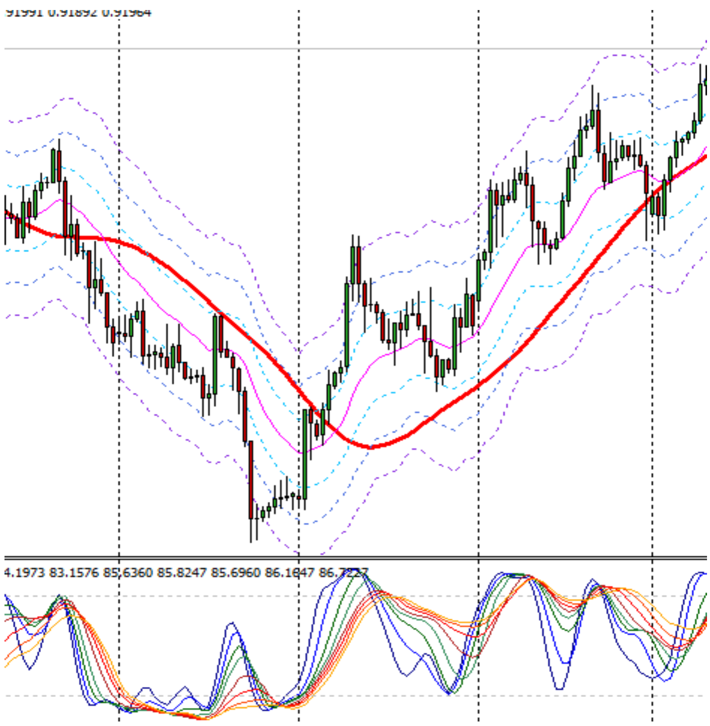
Stochastic is not overbought, The Trend Signal is under the price action, so other than the ATR Channel position you'd be looking for long entries.

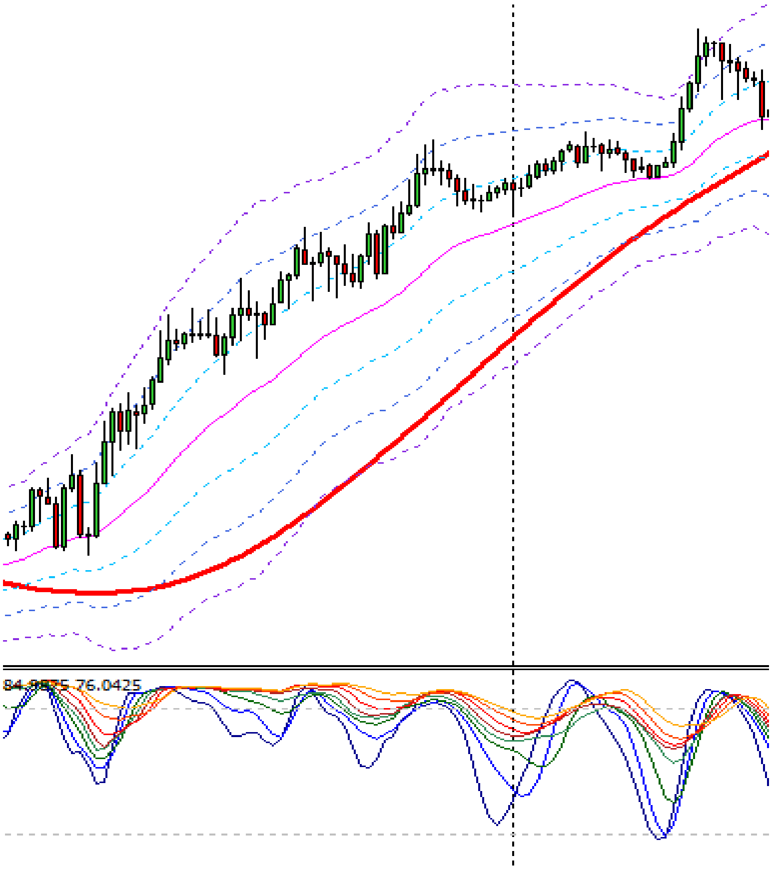
The Four Hour chart:-

We can see that the price is rising in a series of stairsteps, coming back to the middle of the ATR channels after each move.

Right now its in the extreme channel, and the Stochastic Rainbow is approaching overbought.

This is not a level we'd consider buying at, rather we'd want to take profit if we were long, and wait for a new entry.





Finally the 15 minute chart.

Here we can see that its had a great run, and recently consolidated to the midline of the ATR channel before shooting up again.

Now its again approaching the midline after retracing from an oversold (Stochastic) and extreme ATR position.

The Trend Signal is still under the price, though getting a little closer.

Keeping in mind the 4 hourly and 1 hourly picture, we do expect this to have a significant retrace at some point soon.

Right now though the 15 minute chart is still pointing to upside, and the retrace to the midline is a potential long entry point.

If, however, the price fails to bounce firmly and is reluctant to move to a new high, I'd be very very wary of any more long entries given the need for a retrace highlighted on the longer timeframe charts.

Of course, if the price does not stop at the ATR Mid Channel or just below, I'd be reluctant to enter long at all just now and may even consider a short-term short entry.

Even if you trade off 15 or 5 minute charts, always look and see what the longer term charts are telling you, otherwise you can be caught out by movements that you didn't (and should have) see coming.

Remember that the longer term charts trump the shorter term charts. That is, if a longterm chart like a 4 hourly says to look for long entries, and a short-term like 5 minutes says go short, listen to the longterm. Basically when you have a conflict like that, you usually would not trade at all.

Occasionally, as in the above example, you can see a pattern where in a longterm chart it is clearly in need of a retrace, and looking at the price movements you can see that the retraces are often steep and cover a good pricerange. In that case, if the short-term chart gave a contrary signal, you might choose to trade it knowing that the potential gain is worthwhile.

I've used Daily, 4 hour and 15 minutes as an example, but you can choose whichever you like. Make sure though that, unless you're trading off the weekly or monthly charts (!!) you look at at least two longer timeframes than the one you're trading before entering trades.

7. Entries

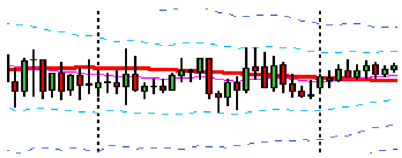
Our aim is to latch onto an existing trend at the safest possible entry point - also at the point that offers the greatest possible gains once the trend has become obvious. Our aim here is not to enter at the top or bottom, as nine times out of ten any method that tries to do that will get it wrong.

So what we want to do most of the time is enter on pullbacks, waiting until they turn in the direction of the trend as well as obeying a few other rules. We can also enter on breakouts, which are a little different and occur less often (and have greater risk), and on the initial change of trend. Each of these are described in detail later, but first ...

7.1 Is it safe to trade?

We must be able to answer YES to this question, otherwise we stay out of the market. So how do we tell? While our training wheels are on, the Trend Signal is the key.

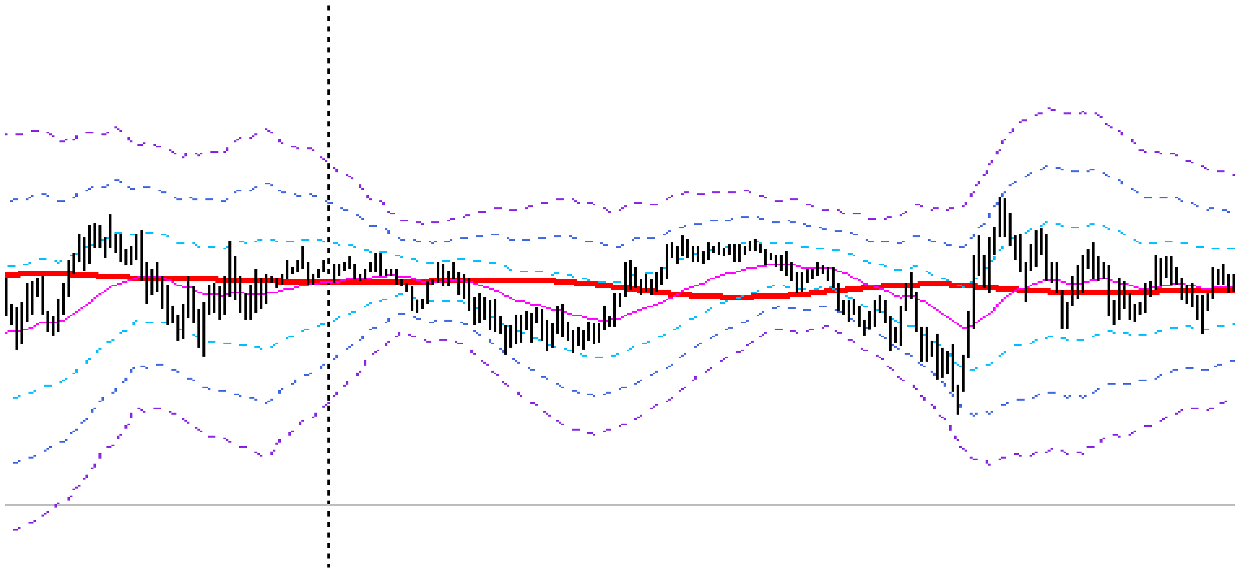
Look at the price action on the shortest timeframe you prefer to trade.



If it looks like this, with the price ranging between the inner lines of the ATR channels & the Trend Signal mixed in as well, stay out! There is only pain trading something like that.

Nothing to see here folks, move along.

Want another example, ok here's a beauty:-



After a few thrilling roller-coaster rides on the preceding days, suddenly for nearly 24 hours AUDUSD decided to grind sideways in a tight range. See how the price becomes constrained in the inner ATR Channels, and whenever it does start moving somewhere, it corrects back again. The Trend Signal is horizontal right through the middle.

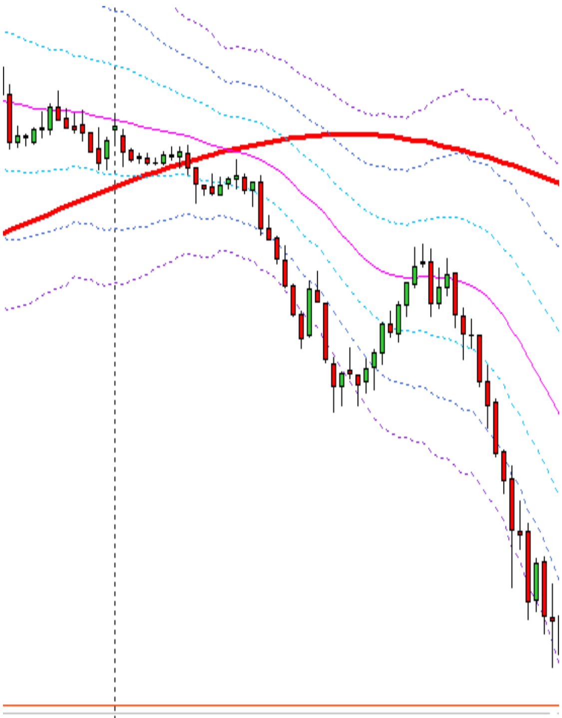
I can't stress enough – you **cannot** trade using trend-following methods in a market like this. It <u>will</u> burn you. There's no point getting angry at the Trend Signal line, saying why can't it move aside so I can trade, as its telling you the truth.

You have only two options in a market like this – if you can stomach the quicker action of shorter timeframes and if the above range is enough to make decent profit, you can drop to the shorter timeframe and trade the smaller trends that present themselves according to the rules in this Manual. If even on 1 minute the Trend Signal is piercing through the middle, for heaven's sake stick with the other option – STAY OUT OF THE MARKET. Take a well-earned break! You deserve it!

7.2 The Trend Change Entry

Often when the trend changes, you'll be given a pullback or breakout entry, described in the following sections.

Sometimes though the price just rolls over into a new trend, without any fuss or ado, as if there's been a change of shift in the trading room. Buyers have left for lunch, sellers have taken over – you get the picture. Here's an example:-



I could see the Trend Signal approaching, and as price was slowly drifting down without support I expected a change of trend was possible, particularly as it was overbought on higher timeframes.

When it hit the Trend Signal, it pushed through, hesitated, then started a strong move down with the ATR midline providing strong resistance.

So what to do? Enter on the move through the Trend Signal.

Here's the rules for the Trend Change entry:-

1. Like a breakout trade, aggressively cover your entry point with a stoploss. There well may be a pullback a little later, and doing this will give you a chance to make profit, or at least avoid loss, and then enter when the time is right.

2. You want the difference between the angle of the price movement and the angle of the Trend Signal to be fairly large. The more sharply diverging they are the better.

3. Only enter if the preceding trend is obviously played out and the longer term charts show a good movement range for a trend change … or if the preceding trend was just a consolidation from a stronger movement, and the crossing of the Trend Signal signifies that the main movement will continue.

4. Do not enter long if the price is already in extreme high ATR channels, or short if its in the extreme lows.

5. Do not enter if the price has been chopping around sideways, with the Trend Signal wandering around the middle.

Its important to understand various patterns that can occur when the Trend Signal passes through the price. Preferably the Signal should be high in the ATR Channels for a change to a downtrend, or low for a change to an uptrend. If it pierces through in the middle, watch hard for the price to be firmly constrained on one side or other of the ATR Channels before risking an entry.

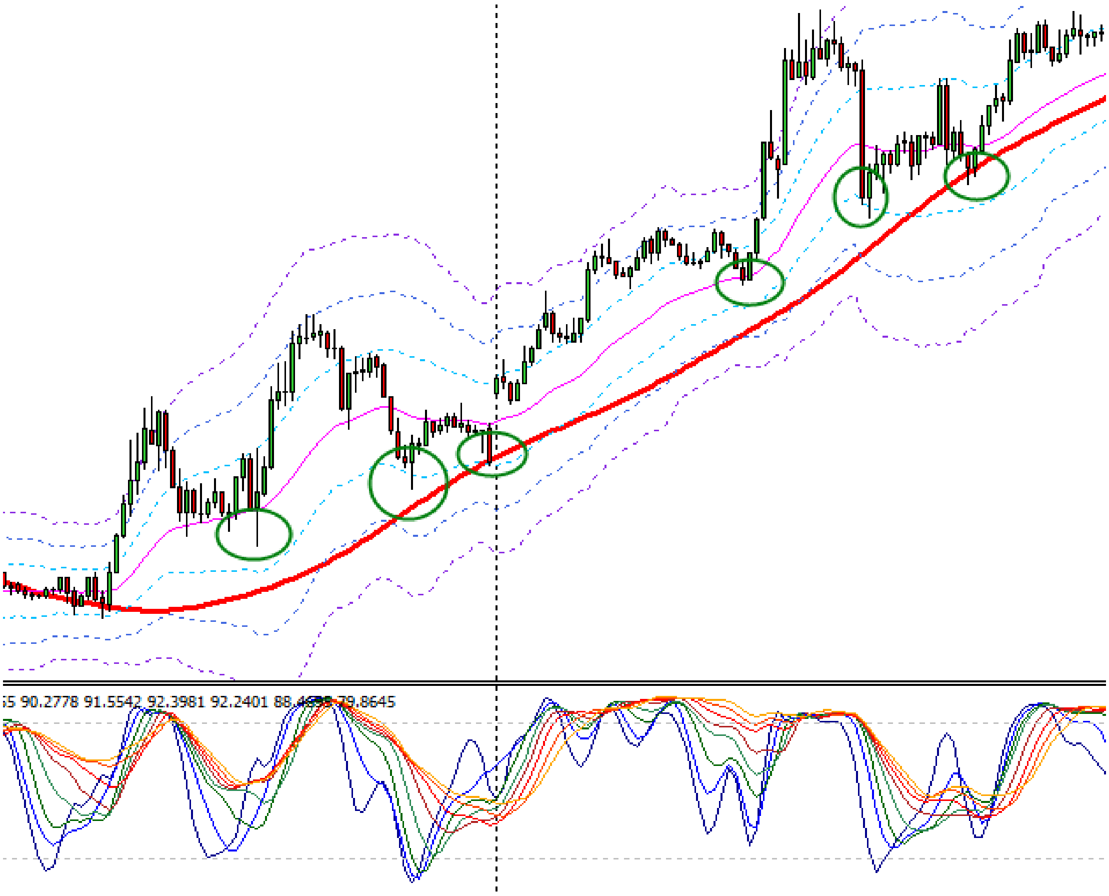
Sometimes the price will make one last doomed attempt to keep the old trend going and catch the Signal line after its past. This can be a great entry for the new trend when that attempt fails and rolls over, but its something to definitely be aware of.

7.3 The Pullback Entry

Firstly, we are trading only in the direction as indicated by the Trend Signal – if below main body of price action we look for Longs, if above we're looking for Shorts. We have a few choices for entries here, but what we want is the lowest possible entry price in an uptrend, and the highest possible price in a downtrend.

Here's where the ATR channels are vital. Remember that the basic principle of the ATR channels is that the price will always want to return to the middle, so with a pullback entry that's exactly what we're waiting for. Sometimes it'll overshoot a bit and touch on the next line past the middle, but that's fine as well provided it doesn't hang around there too long. Any further and we don't enter. Sometimes in a really steep trend a pullback only hits the line prior to the middle, which is also tradeable under certain circumstances.

Here's an example of several great entries in an uptrend:-



Note the multiple entries as it visited either the ATR midline or the line beyond. All were great entry points.

So here are the rules for pullback entries:-

- The Trend Signal must be under the price, preferably under its lows, for long entries, and over the price for short entries.

- The Stochastic Rainbow must not be concentrated in overbought territory if you're entering long, or oversold if you're shorting. For 15 min and less timeframes, what you're looking for is the line fanning out from a previous overbought/sold state and the fastest lines curving back in the direction of the trend. Study the above examples and see what the Stochastic was doing at the best entry points. Also note that the faster lines dropped a long way, often to oversold, before the entry presented itself. Longer timeframes usually don't provide enough candles for this pattern to present itself.

- This is most important – **the price itself must show some sign of turning in your direction before you enter**. Sometimes this can be very quick, so you have to have your order ready to go, and yes sometimes you'll be faked out. But what you don't do is have a pending order sitting there to be hit as the price retraces, as who knows where it will stop? Every reversal begins as an apparent retrace, and every pullback has that possibility attached to it. So play it safe, watch for a convincing turn, and only then enter.

- The price must ideally be at or near the mid ATR channel line, or the next line (below in an uptrend, above in a down). If the price retraces further, other than a quick poke through & back, do not enter. You <u>can</u> enter on the line preceding the ATR midline only if a pullback in this trend has bounced from there previously, but be very careful.

If <u>any</u> of the above fail, <u>do not enter</u>. If you do, you are following some other strategy, not this one.

Once you've entered, a higher swing low will have formed (uptrend) or lower swing high (downtrend), so you can place your stop a little below/above this point – your stop can be logically close, and once the price safely moves on and the trend continues you have the choice to move it up to cover breakeven.

Now I mentioned that the price must show some sign of turning in your direction before you enter, and this is the most difficult thing to master with this type of entry. If you don't wait for it and pre-empt an entry, you might be lucky but you'll likely get burned. If you wait too long the price might suddenly run away and you've missed the chance. So how can you tell when its safe to put your toe in the water and enter a trade on the pullback? There's two methods I'm using to help with this:-

Firstly the Stochastic Rainbow.

Notice how on this trend, the quicker lines on the indicator reach quite low, sometimes to oversold, before turning up. That's a pretty good signal to look out for.

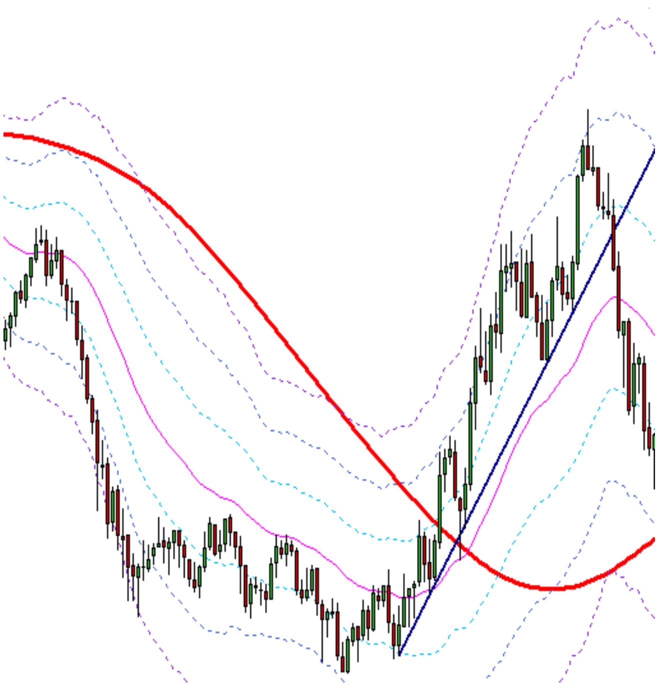
If pullbacks in a trend have shown stochastics reaching this far previously, it makes sense to give them time to do so again on the next pullback.

Here is the other method – drawing a trendline on the retrace at a lower timeframe, and watching for it to break.

This is AUDUSD with a sharp pullback during a longer downtrend. It was sharper than normal, so on the timeframe I was trading (1 hour chart) there was no time for the Stochastics to create the pattern they had in previous pullbacks.

What you can do on sharp pullbacks like this is draw a trendline as I've done here. For upward movements the line must be under the price, for downward it must be over, and it should have as many touches as possible without too many penetrations of the line.

What I'm looking for here is a clear break that tells me sellers are back in control and its safe to jump back in short in accordance with the longer trend.



Multiple Entry Sizes, and Scaling In

When you're learning the method, its good to keep things simple. Enter one lot for each trade, exit it when you take profit or are stopped, and enter again when you get another signal.

When you're comfortable with this you might want to consider the following strategy:-

On the first entry into a new trend, enter three lots, not one. Make them a little smaller than what you'd usually trade to avoid over-committing yourself.

One of these is a "scalp entry", meant to capture short-term movements in the trend.

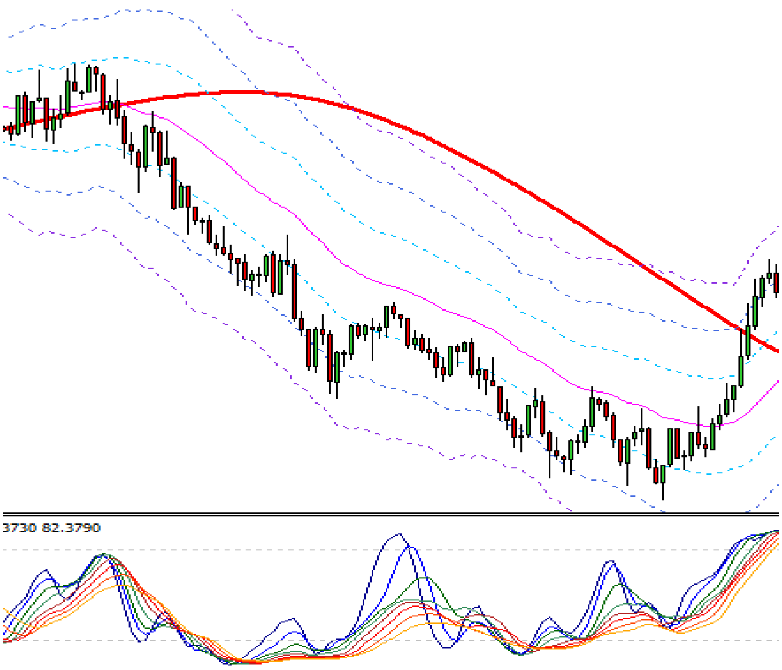
The second is the "swing entry", which you want to hold for the life of the trend.

The third is the "position entry", which you cover at break-even only. Sometimes these will survive subsequent price movements as a major trend develops, and you'll be able to hold these entries for days or weeks at a time, continually gaining profit until you're sure the much larger movement has ended.

As the trend progresses, when you get a signal to take profit do so with just the scalp entry, and on a re-entry signal you're adding a single scalp entry again. If you want, you can add an extra swing entry if you feel the trend is a strong one.

More on the management of these entries in the Managing Stops section.

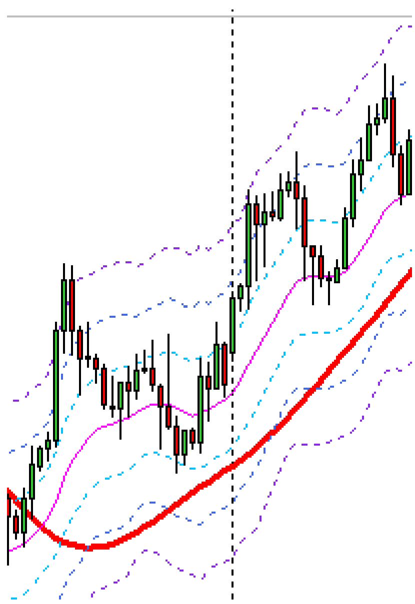
Multiple Chart Timeframes are not only useful at the start of the day when doing your initial analysis. You should have them open as the day unfolds too, which is why its important to concentrate on one pair. Here's an example of why …



USDCHF bounced strongly out of a retracement pullback and looked like it was about to resume the overall uptrend.

I can't enter on the 5 minute as a Trend Change Entry as its already in extreme ATR levels and overbought on the Stochastic Rainbow, so I'm waiting now for a pullback opportunity.

All good except lets look at the 4 hour chart...



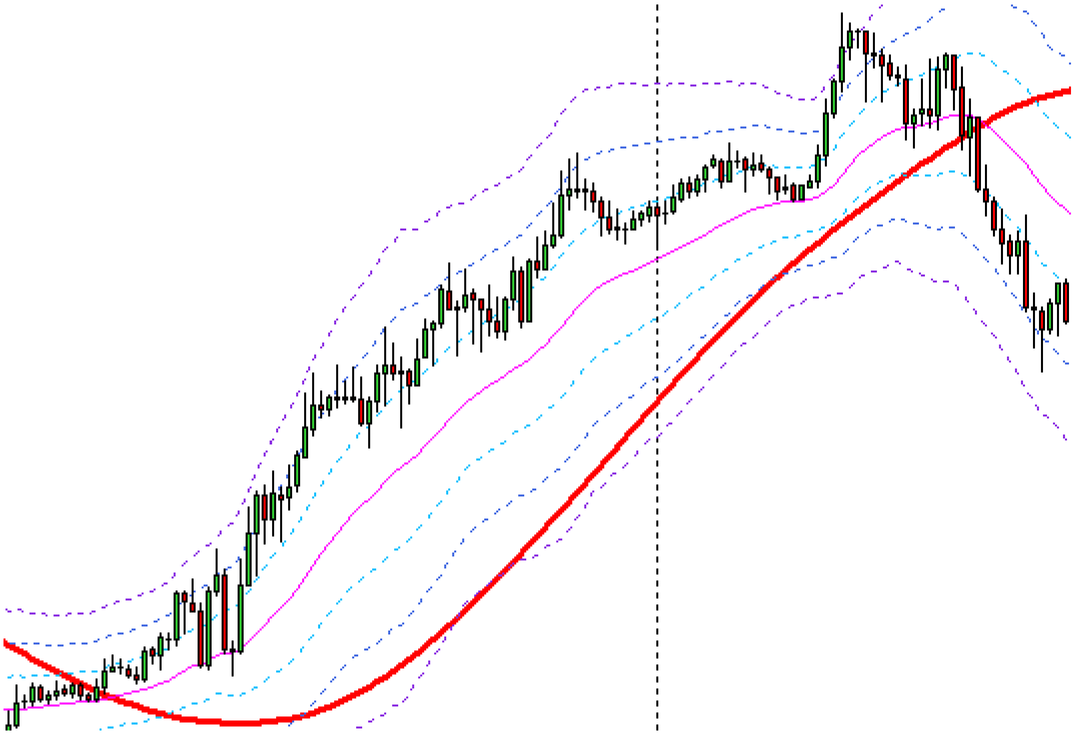
What an opportunity we missed! We could have been in right at the bottom of a bounce!

Who said fast timeframes always give you the best entries?

It always pays to know whats happening on longer timeframes.

Finally a note of caution on pullback entries. Pullbacks work best on trends that take healthy breaks at regular intervals.

If you see a trend running hard and not providing much in the way of pullbacks, then it finally decides to take a rest and come back to the midstream of the ATR channels, be wary. It may be an excellent entry point, but as the trend hasn't bothered with pullbacks until now, it could also be a sign that the trend is exhausted.



Here is USDCHF running hard, barely pausing for breath and not approaching the ATR midline for support for a long time.

Finally it does, then shoots off for another last run to extreme territory.

But that's the last gasp of the trend. It makes one last attempt to bounce again before plummeting through the Trend Signal into a downward move.

So if a trend isn't regularly pulling back, then suddenly it starts to, be wary. It doesn't mean the trend is over, but it just might be.

7.4 The Breakout Entry

Unfortunately, sometimes the market doesn't play fair and give you pullbacks to enter on. Sometimes it starts in a direction and keeps going, and going, and going for hours on end, the pips churning away, while you sit on the sidelines awaiting a pullback that never comes.

So how, under this strategy, can you trade these movements? They can be some of the strongest movements on the market, and it would be a crying shame to miss them. Here are the rules by which I look for breakouts:-

Firstly we are not considering the trend here at all. Sometimes breakouts will be in the direction of the dominant trend, sometimes they'll go violently in the other direction. Sometimes there won't be a trend, with the price consolidating and the range of movement getting smaller and smaller, then with a huge bang the starter's pistol is fired and the candles start racing.

So what we're looking for is hard to predict. A breakout can come out of nowhere. So to trade these you need three things:-

1. To be present, trading the market when they happen.
2. To have quick reflexes, and the ability to discard your idea of what the market is doing and react.
3. To know the rules of the breakout entry like the back of your hand.

And here are the rules:-

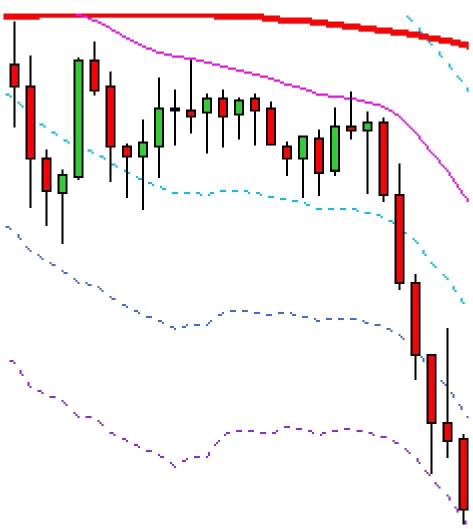
1. The candles forming the breakout must be unusually large, and have very little retrace in them (ie no long tails implying resistance to the move). We do not trade breakouts formed by smallish candles, as the chances are we'll get a pullback entry.

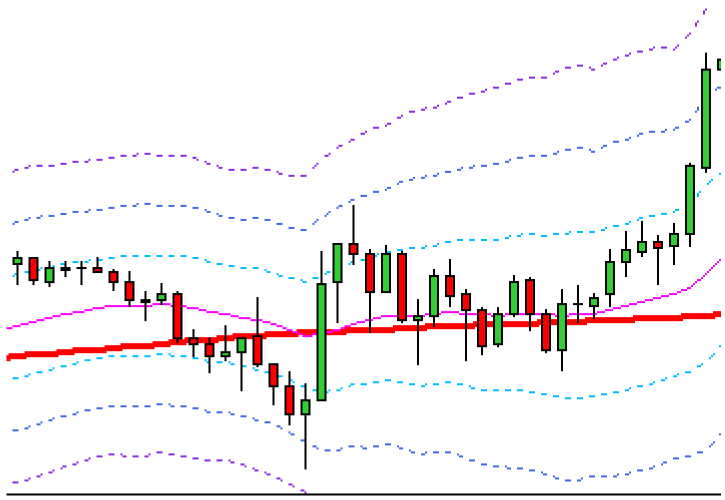
2. If the breakout is upwards, it must quickly move past recent highs with no hesitation. If its down, it must blow past recent lows. This shows that the move is strong enough to overcome opposition.

3. When you see the above, enter immediately, and aggressively protect your entry with a stop as soon as possible. If it turns against you, and some breakouts will, you don't want to be holding the bag while it races in the other direction in a classic "fake-out" move. You want to be out on the sidelines, your account safe, watching and waiting for your next entry.

That's it. Quite simple really.

Here's some examples. See if you can spot where you'd enter based on the above rules:-





Lastly, unlike Pullback entries, I do not like entering multiple positions in a breakout. I simply enter one lot, due to the volatility inherent in the movement and the possibility that it could quickly reverse. If the price keeps going without pullback and I cover Break Even with my stop, I could carefully feed in another entry, also with a tight stop and cover it as soon as possible.

The hard part with breakouts is that it feels like you're chasing the price. In this case however you're not. Big candles, explosion out of the current range usually means the market has made up its mind and is intent on going somewhere, so you need to be on board.

7.5 Taking Profits and Exiting Trades

When a trend is running, you know when to take profits using a combination of the Rainbow Stochastic and the ATR Channels.

What we're looking for are:-

1. The price entering the extreme ATR Channel, usually after a succession of candles in the direction of the trend. If it pokes beyond the extreme ATR Channel, all the better.

2. A roll-over in the Rainbow Stochastic, preferably with a concentration of lines at an extreme level.

For example:-

Here is a strong uptrend, and I've circled the take-profit areas in Red.

At each, the price had pierced into the outer ATR Channel or beyond, and the Stochastic Rainbow was concentrated in oversold territory.

When you see this, do not hesitate. Do not hang out for more. Take your profit.

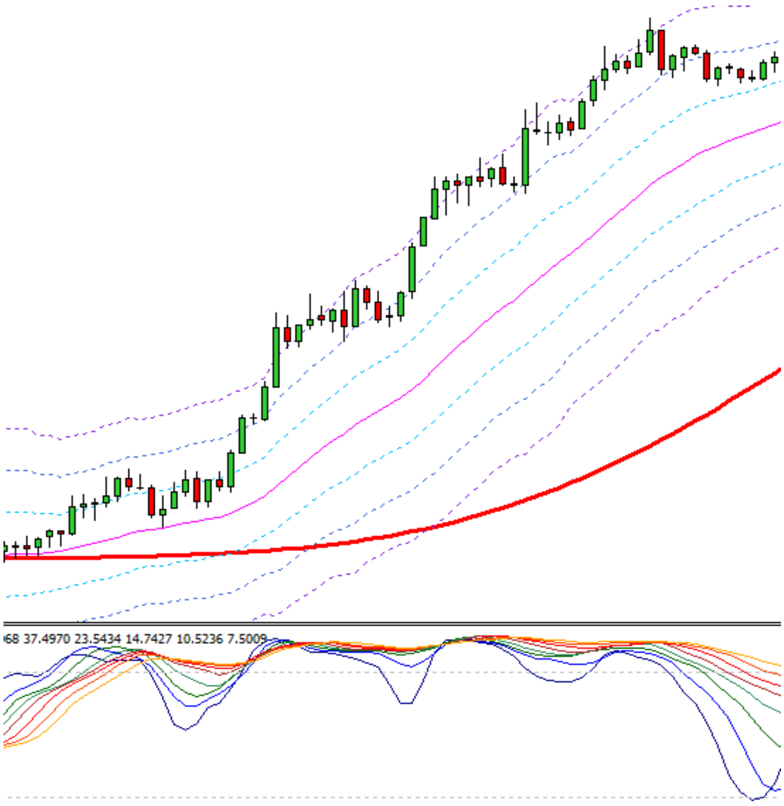
Note though that sometimes the trend doesn't play ball and stop for a retrace. Sometimes it just keeps on going, but the majority of times it doesn't, and if you don't bank your earnings you'll end up regretting it.

This is where multiple entries come into their own. You can take profit on a scalp entry and rest easy if you're still holding swing and position entries. But if you have just one entry, you exit and the price keeps moving, you're left hanging waiting for a pullback that may not come for a while.

Sometimes, of course, the price can reverse without being in extreme ATR territory or with the Stochastics far from oversold.   You can, if you feel the price action is unsustainable or weak, take profits when the price reaches a higher ATR channel and loses momentum, or if the Stochastics are diverging in the opposite direction of the price action.

There are some times though when the market wants to run and run and run in one direction. No pullbacks, no hesitations.

Here's AUDUSD during a manic surge on Friday 11/11/2011:-



Had you taken profit at the first combination of overbought and extreme ATR Channels, you would have been left hanging for a pullback entry that never came.

Sometimes then in the early stages of a new trend, I don't take profits immediately on the first signal to do so, but rather (on the scalp entry) keep the stop nice and tight just underneath.

If the retrace happens, my stop's hit and my profit is still very good. I can look to re-enter on the pullback if the trend wants to continue.

If however, the price just crunches sideways for a little while then continues up, I still hold my entry and my profit is maximised. Using this method on this particular rise, I'd still be holding my scalp entry now, with the stop just under the price.

7.6 Managing Stops

The period immediately after you've entered a trade is the most dangerous. The market will do one of three things – move decisively in your favour, go sideways, or move against you.

This can happen no matter how strong the trend you're trying to catch, no matter how well-placed and timed your entry point is.

Obviously having a good entry point helps. If you've entered an uptrend on a pullback, you have a logical swing low below which to place your stop. The closer the better, provided that for the stop to be hit you're sure that the market is indeed moving against you, and its not just a random downspike before it moves up again.

When though do you cover breakeven? If I'm sure the entry is well placed and I see the price moving confidently away in the right direction, I still wait until its at least one ATR channel distant from my entry point. That should usually be enough to save it from random noise. Bear in mind if you're shorting to allow extra for the spread distance.

If I'm not confident of my entry or I see the price having trouble resuming the trend, I move to BE aggressively. Better to have it taken without loss and have to re-enter than to have the market move against you and take losses you could have avoided.

By the same token, if the market moves sideways and does not want to resume the trend after a few candles, I'd suggest closing the trade. Better that, and having to re-enter, than having a reversal suddenly break out and take your stop.

Once the trade is underway its a lot easier, as you're in profit.

The key here is to give the price room to move and be patient. With the "scalp entry" I usually try to keep the stop an ATR channel's distance from the price, and of course I'm looking to take profit when the rules indicate.

The "swing entry" stop I move once another pullback has occurred and the trend resumed – it goes to where the new swing low or high is. If no pullbacks occur, I keep it 3 ATR channels width from the price.

The "position entry" stop stays at Break Even. It only moves once a counter-trend or consolidation has occurred, and presuming the trade is still alive, it moves to the low (uptrend) or high (downtrend) of that consolidation.

8. Beyond the Training Wheels

Ok, if this system is working for you, as it is for me, keeping you trading in the right direction and making profits, then what next?

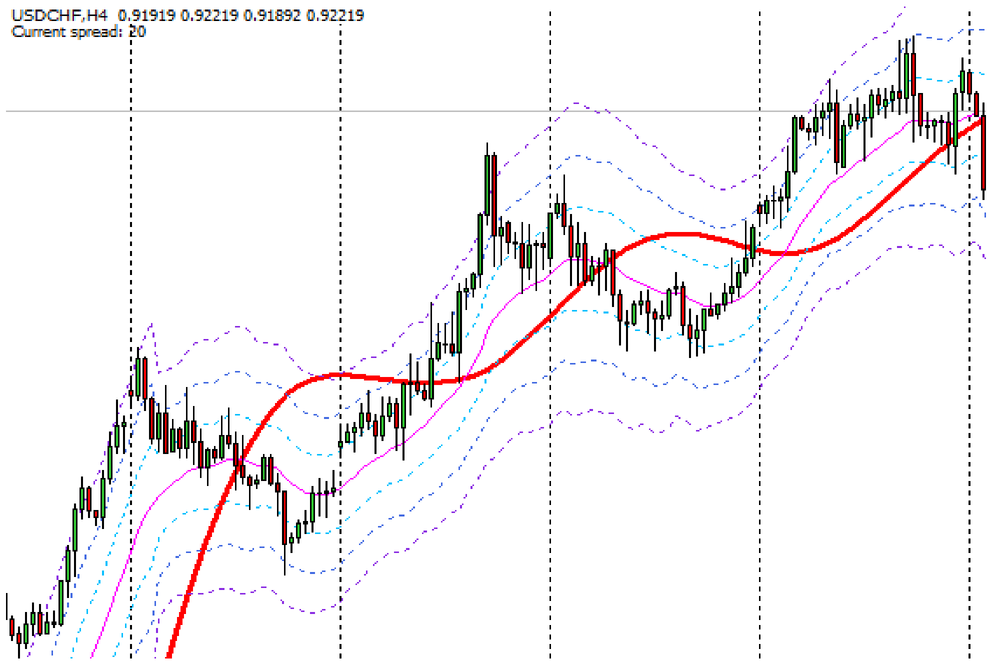
Obviously you can stick with this strategy as it is – if its working, why change it right?

However, the idea of this system is to help new traders find their feet and trade in the direction of the trend. There's always more to learn though, more arrows you can put in your quiver to improve your trading.

For me, one of the first things to add is a knowledge of Dow Theory. You can read all about it here: http://stockcharts.com/school/doku.php?id=chart_school:market_analysis:dow_theory but this is it in a nutshell:

An uptrend is defined by prices that form a series of rising peaks and rising troughs (higher highs and higher lows). In contrast, a downtrend is defined by prices that form a series of declining peaks and declining troughs (lower highs and lower lows).

Sounds simple enough, and you can see it in action on your charts, for example...



We can clearly see a series of higher highs and lows.

If we knew this was an uptrend, each time it retreated from the high, we'd be looking to see if it held support at a higher low than it did before. If it does, the trend is still intact and better still, we have a new entry point. In fact, with this knowledge we could even ignore the meanderings of the Trend Signal, as we can see a clear pattern here. Its finding support in the lower part of the ATR Channels, perhaps a little lower than we'd normally look for a pullback entry, then moving into the next upleg.

Now lets look over on the right of the chart. The last pullback entry looks good, however the price does not raise very far, failing to set a new higher high, before it suddenly drops to a LOWER low. This alone doesn't mean the trend is over – it could just be a temporary blip - but its a major warning sign. Perhaps sellers have signified an intention to start offloading here.

So what do we look for next? You guessed it, a lower high. If the price cannot, when it rebounds, get above the previous highs but instead rolls over at a lower one, then you're justified in assuming that the trend is turning down and using that high as a pullback entry point for a short trade.

Of course, sometimes the market doesn't oblige us by setting nice orderly highs and lows in a progression like a set of signposts. Sometimes it'll move dramatically in one direction for hours on end without pause for breath. Sometimes it'll roll over slowly, without setting any apparent peaks, and then gradually accelerate into an exponential rise or fall. But the vast majority of the time you'll have peaks and troughs to judge by.

By the way, when looking for evidence of a trend change, make sure the peaks & troughs you're measuring are of the same size the price has been setting. If its falling away in much smaller peaks & troughs, like the retrace in the middle of the above chart, chances are its not a trend change & is just a pullback. Look also at where it is in relation to the ATR Channels, which are an incredibly useful guide, and in which channel it found support previously.

Dow Theory is not the only weapon you can use. There are two more that I am gradually applying to my trading – gradually because I do not want them distracting me from the principles of this strategy, which keep me trading with the trend.

One is application of **chart patterns**. You can read a comprehensive summary of them at Tom Bulkowski's site: http://thepatternsite.com, so I won't go into them here. I use them now, I used them as a share trader as well, but like anything else I've found that they always, always come second to trading in the direction of the trend.

If a pattern calls for a reversal, maybe be wary of trading at all until its clear a reversal is happening or has failed. If you're following the Training Wheels strategy, don't take a reversal trade thinking to pick a top or bottom, as it will burn you, and it is something other than this strategy. If you think a reversal or large retrace might happen, and the trend has shown that retraces are of a tradeable distance, consider dropping down to a lower timeframe to enter using the Training Wheels methods rather than risking a counter-trend entry without any rules to back you up.

Another tool you can learn to use is **volume spread analysis**. The theory behind it is that if volume increases and a price movement stalls, it means sellers or buyers (depending on the direction of the movement) are coming in to block further progress. Its a sign of potential reversal. By the same token, early in a trend if you see strong volume on the candles that start the trend in progress its an excellent sign that the trend has legs.

Again, its not something that you'll base trades off on its own, definitely not a tool to use to pre-empt trend changes and go in thinking you've picked a top – I can't stress that enough, don't don't do it. What VSA will do though is give you that bit more understanding of what's going on, and help you interpret the price action as it happens.

Add the Volumes indicator to your chart, and just watch when volume spikes & what the price does. See if you can draw correlations. Bear in mind though that volume in the Asian session is usually light, and it gets especially heavy when both Europe and the USA are running together. Its the strength or weakness of volume for a candle relative to its neighbouring candles that counts.

Also, if you think, say, that sellers are arriving in force to stop an uptrend, by a sudden surge of volume with either a small candle or a candle with a long bearish tail, wait until the next candle or two. If they continue up, then yes there was a fight but the buyers won. If it keeps hesitating, it might consolidate until one side or the other takes control. If it starts on down, and accelerates, the trend might be over or at least in for a good retrace.

Finally, you can research and start to apply horizontal **Support and Resistance** areas and **Fibonacci** retracements & extensions. These are powerful tools, but I believe they're dangerous for new traders before they've found their feet.

Get used to seeing the price in the context of the ATR Channels and Trend Signal first, get used to trading with the trend. Get consistently profitable with this simple method and then you can start adding extra tools to complement how you trade.

9. Frequently Asked Questions

Ok, actually these questions aren't asked frequently at all, as I haven't even finished writing this manual let alone shown it to anyone.

These are what I think people might ask though …

Q. Why don't you use support and resistance areas?

The method does not need them. Yes its great to know where they are, but for a newcomer who doesn't know how to trade them – when they're likely to hold, when to bounce, when to be broken, they can just be confusing. Follow the trend exits and entries, and by & large you'll do ok, and you can add to your knowledge as you go.

Q. Why don't you use Fibonacci levels for targets? Or Pivot lines?

Again, I didn't feel they were necessary for new traders adopting this method. The price will do what it will do. If it wants to go up for 300 pips, ignoring fib levels and pivots on the way, then that's what it'll do, and having the idea in your head that it'll stop at those levels can harm your trading.

Q. Why not suggest counter-trend trades on the pullbacks?

Because often pullbacks are sidewards, and sometimes they look like occurring but don't. Its playing with fire fading the market against the trend. I've learned the hard way not to do it, and its suicide for new traders to make a practice of it.

There is an exception – the USDCHF charts I posted in the Beyond the Training Wheels section. There's a clear stair-stepping trend on the 4 hour chart, with large drops between the (even larger) rises. If you trade on the 5 and 15 minute charts, those drops of 70 pips or so are not something you'd want to miss out on. If, however, it was only falling back 20 pips on average and in a sideways bumpy fashion, I'd be sitting out waiting for the next signal to resume the trend.

Q. Why are you, a learner, suggesting a new method?

Because I think it works, and might help other newbies. I also hope to improve it based on people's feedback. And we should all be constantly learning. In addition, an experienced trader may well have forgotten what it was like to be a newcomer all those years ago, and not realise how the methods that seem simple and obvious to them are daunting to someone who is just starting out.

Q. How well are you doing with this method really?

I've actually turned $2500 into $200,000 in six months. Actually, no. I'm at the stage where I fully trust my method, and when I trade it I have not yet had a losing day. My problem is still that I'm still liable to have brainfades and forget the rules, and trade what my gut says instead, and that's when I get into trouble.

Gaining the victory over your own impulses and becoming disciplined enough to follow the rules all the time without emotion – that's the biggest battle I've faced and am still fighting every day. This system has kept me profitable when I've followed it, and each day its a matter of practise following the rules, trusting them and not my thoughts or feelings.

I'm learning especially to NOT follow news, and to remain uninformed about what's happening in the world at large. I am now avoiding a chatroom populated by many experienced and helpful traders while I trade, simply because its so easy to follow "groupthink" and trade against your method.

Q. This system is costing me money! I hate you and all who sail in you!

If Training Wheels does not work out for you I'm sorry, perhaps another system would suit you better – there's plenty out there to choose from. I only know it fits me, it saved my Forex career so far, and I wanted to share.

I also suggest to people trying this strategy that they do so in Demo mode first. Do not rush into live trading with this, but get yourself used to making the entries and exits in the strategy until you can do it consistently. Once that's happening, and you're confident in the method and your ability to stick to it, only then should you progress to live trading.