

Chapter Nine

5/13/62

She was the first girl I thought I liked, or loved, or whatever. She sat next to me in a 7th grade class. I don't remember much about the class, mostly because I was spending so much time concentrating on Carrie. Most of the time, she was my friend. Except when we were outside of class.

Outside of class, she paid no attention to me. She ignored me. If she ever talked to me, she made fun of me, refused to spend time with me (or even admit I existed). Of course this only made matters worse. All of this only made me want her more. Carrie moved away after the 7th grade.

5 years later I found myself standing behind her at the market.

Every feeling I'd ever had for her returned instantly.

I was so entranced that I watched her as she left the drugstore, got into her car, and pulled out of the parking lot. Just when I thought that she neither remembered me, or even noticed me, she turned

around, rolled down her window, and blew me a kiss. My heart jumped into my throat and I felt weak.

I never saw Carrie again.

You know what a pip is already. Do you know that most forex traders spend their careers chasing after pips in the same way I chased after Carrie's attention? She never gave it to me, unless (at the end) it was to blow me a teasing goodbye kiss. She had received all the benefit from my attention and never gave anything back except a blow to my self-esteem. Gosh, that sounds a lot like when I first traded currency – and the pips teased me until they simply moved away in the end, with a good-bye kiss.

Have you ever watched the market and wondered why the harder you tried, the more quickly the pips distanced themselves from you? I remember when I first started trading that the market would move away from me and I would begin to think: it's moving. Why is it moving away from me? Couldn't it just as easily move in my direction?

For a while, I made money on gut decisions. I'd make some progress, a few pips or more a day, but never really understand the signals. For instance, I'd make a profit just barely, and watch in horror / relief as the market swung the opposite way right after I exited the trade.

Or I'd enter a trade, lose a bunch of pips, and then exit the position at a loss – only to watch the market swing back in my favor. Only, of course, the position was closed and all I could do was sit there and watch, just like I had stood in the parking lot of the drugstore, watching Carrie blow that goodbye kiss.

What I learned

Until you're no longer impressed with pips – no longer frightened by them, nor infatuated by them, not in love with them, no longer simply hating them – they won't give you the time of day. The acquisition of pips is

your only goal in the currency market. But pips are fickle and if you pursue them full of emotion, you're going to get burned.

I learned in the drugstore that day 20 years ago that Carrie would have paid attention to me if I had simply ignored her every once in a while. If I had been able to get my feelings under control. If I'd been able to act cool instead of like a freak. If I'd been able to calmly make a plan, stick to it. But I could do none of those things. My emotions took hold of me and turned me into an idiot.

It's the same for pips. We all want them. We all want as many of them as we can get. But some of us are willing to risk everything for just a few of them. We'll chase after them like a 12-year old boy. And you know what? They don't give a damn about you and me.

This chapter will present a plan for learning about pips, where they're going, what they're about to do, and then arm you with a strategy that once implemented, can take a lot of the emotion out of trading.

Your goal will be to:

1. Enter positions as soon as a particular signal is given.
2. Exit the position as soon as a particular signal is given.

The payoff will be:

1. The emotion should be gone from the trading.
2. You will enter and exit trades with discipline and focus.
3. You will get about 25 pips on the good trades. Maybe 30 and maybe even 50. There will be more winning trades than losing trades. The average loss will be about 25 pips.

Attitude is 99% of Trading

Developing the right attitude about your trading is most of the work. Once you get your attitude (your discipline) under control, you're going to have more pips than you know what to do with. So much has been written about this that you'd think that you've already heard enough about it. I've written about it elsewhere, too¹, but I've got to stress that no technique or strategy is worth more than the discipline you have to implement it.

The 5/13/62 strategy requires discipline. This is the most powerful personal characteristic you can acquire. Period. It will earn you more money and success than any other attitude or personality trait. If you're low on discipline, please take the time to consider what I'm saying:

In trading, discipline simply means two things:

1. Enter a position as soon as your system triggers an entry signal.
2. Exit the position when your system triggers an exit.

If you do not acquire discipline, this system will not work for you.

No trading system will work for you. But this isn't a book about discipline. In fact, this book assumes that you have discipline, or you're willing to acquire in order to implement a profitable trading system.

So, for the purpose of this discussion, and for the testing of this strategy, please be disciplined – even as you practice.

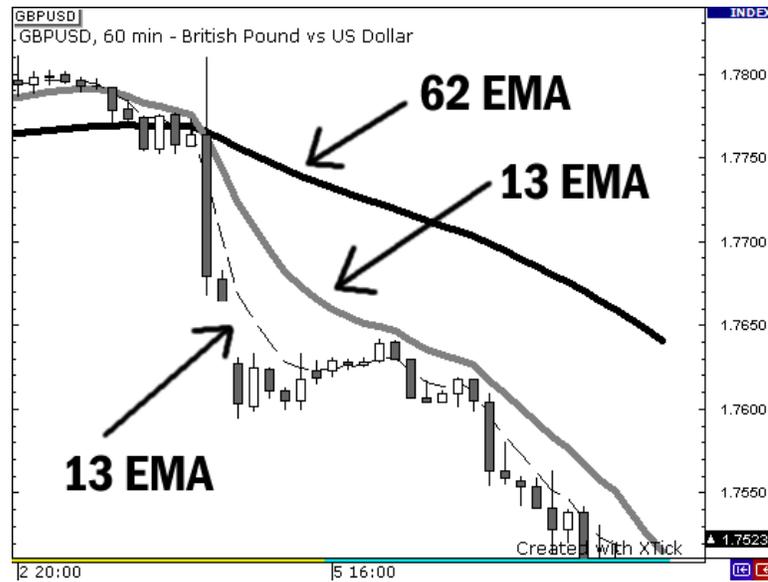
Exponential Moving Averages are the Key.

They are the core element of this strategy. From the beginning you should understand that I didn't invent the 5/13/62 strategy. At least I don't think I did. There are some extras that I add in, but essentially, all of this information is available elsewhere. That said, I believe

that most of the people that write about forex have a way of putting you and I to sleep.

So maybe this is the first time you've heard about it, but in any event, I'll try to keep it interesting.

Here's where we start. With a chart:



On the chart above, there are three moving averages that I identify with snazzy arrows. If you are having problems sorting out which moving average is which, I advise you to poke your eyeballs out with a pen.

If you have not poked out your eyeballs, you can easily see that when the 13 crosses below the 62, it seems like we are in a downward trending situation.

The inverse is also true (although we cannot see it in the chart above): if the 13 crosses above the 62, it seems like we are in an upward moving trend.

That's not quite everything, so we need to move on and do some more investigation.

Can We Just Trade Crossovers?

The question arises: if those statements about upward and downward trends are true, then why not just sell a currency pair every time that the 13 crosses below the 62?

The answer is a that I have backtested (mechanically, by programming trading software) the system of simply buying when the signals cross above and selling when the signals cross below. There are even companies that build trading robots that will automatically buy and sell when these signals are given. But, as much as I'd like to say differently, it's not that easy.

There are all types of false signals (crosses that happen but that don't turn profitable). Here are some other principles of this strategy, divided in three sections: entering the trade, staying in the trade, exiting the trade. The principles of each section will help you maximize your gains and minimize your losses.

But first, a quick look at the tools you'll need.

Charting Software. You are going to need to be able to view candlestick charts, as well as moving averages. Charting programs are plentiful and free these days, so this is not a problem. Here are some charting programs I have used in the past. Some are free and others are not:

- Metatrader
- Xtick (what I use now)
- eSignal
- Oanda

The 30 Minute or 60 Minute Chart. I have used the 15 min, the 2 Hour, the 4 Hour, and even the daily charts with this system. I recommend that you study this system with the shorter time frame charts, like the 15 or 30 or 60 minute, so that you can see lots of examples of this system in action.

Moving Averages. Your charting software will automatically calculate the moving averages for you. But to get set up, you need to plot (as I did above) the 5, 13, and 62 EMAs on your 30 minute chart.

Part I: Making the Trade

Below you'll find the principles behind making good trades. And avoiding the bad ones. These are guidelines. Good trades based on these guidelines are the result of applying them enough times that you begin to get a feel for the market. I want to emphasize that you can change these rules. You can manipulate them. You will be most successful when you make this "your own," by adjusting so that you feel most comfortable.

Holidays and other bad days. Try not to trade on holidays, especially U.S. holidays. It's best to stay out of the market on those days and catch up on time with your family, see a movie, adjust the metal rod that was placed in your back, insert a metal rod in your back, or fire up the barbie-q and roast some weenies. Or you can back test your strategies. It's also best to never, ever, ever, enter a trade past 14:00 GMT on a Friday.

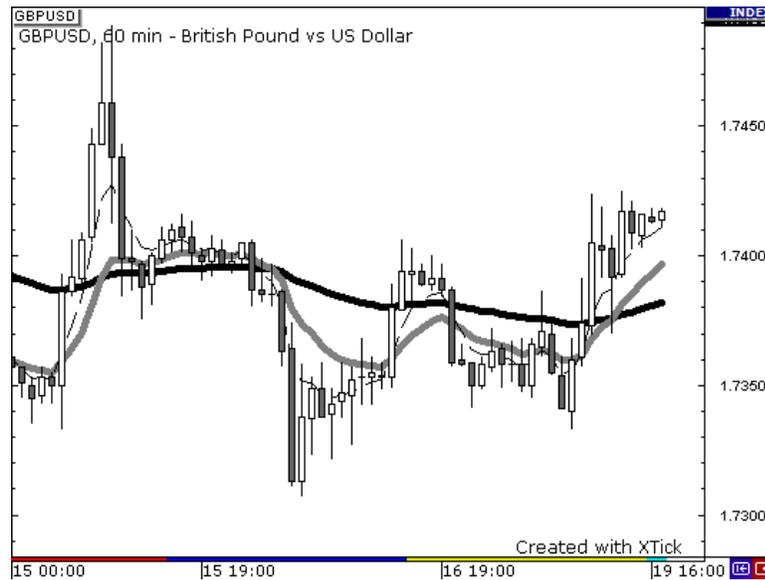
On holidays and late on Fridays, the market is unpredictable and might not move enough to give you any profit. Or it might move 50 points in one direction just for the heck of it, and then move back. Of course it might move a zillion pips, but that's the exception rather than the rule. Then you're stuck in what might become a losing position, but meanwhile, you're losing money to premiums/interest paid to your broker. This is a good time to shove a metal rod into your spine.

After 13:00 Eastern US Time. This is when the market slows down, and there can be a lot of false breakouts. Avoid trading during these times, especially on the shorter time frame charts.

Please take my advice and just stay out of the market, with this system, at these times. You may lose some opportunities, but you will lose (also) the chance of getting trapped in a motionless or unpredictable market.

Other systems, long term systems in particular, can work okay late on Fridays and on holidays. Those are systems that I teach in the live seminars and in the web-based training.

DNA Spirals. Often, a currency pair will find itself in a dorfwad, go-nowhere pattern that I call the “DNA Spiral.” This is an apt name for the pair because the candles can spin back and forth around the EMAs, seemingly tangling them up into a twisting pattern. These are times that you do not want to trade. Here is an example below.

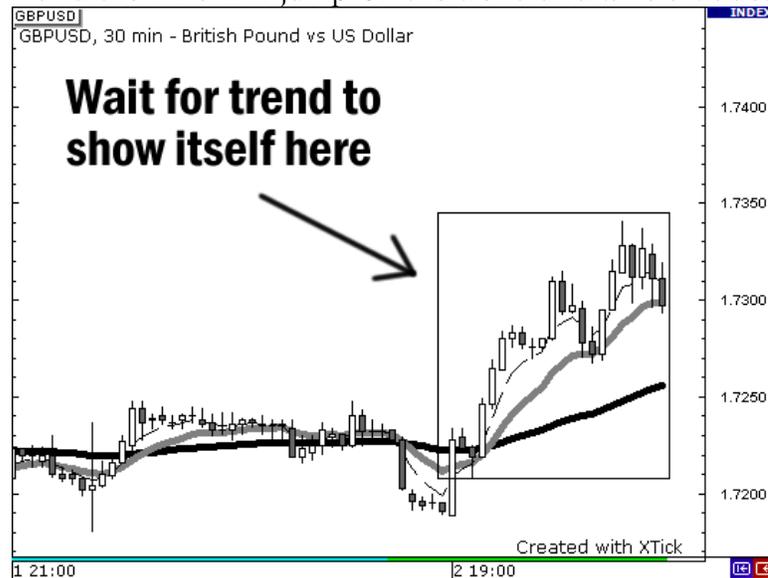


If I just told you when NOT to trade, we would only have a lame chapter, fit for burning or toilet paper.

But now I am going to share with you when you need to become really excited about taking the trade.

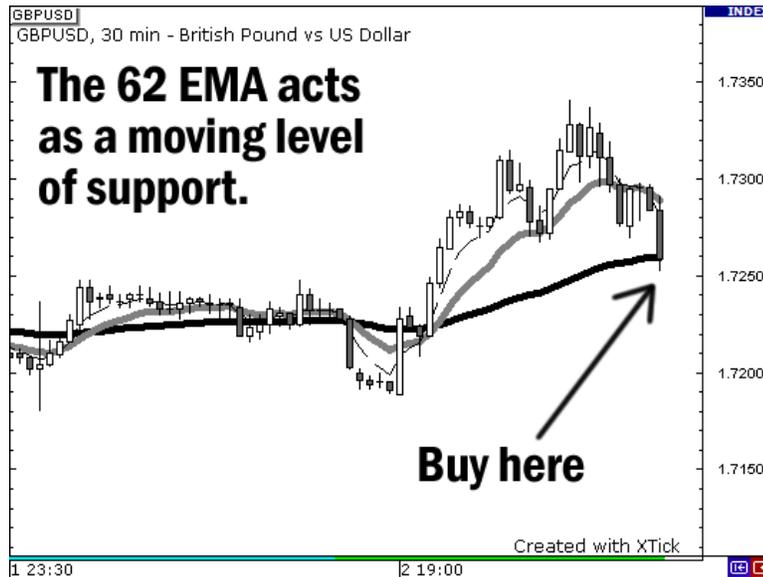
When the 5 crosses the 13, and the 13 crosses the 62, and the 13 is at least 30-40 pips away from the 62, we are ready to trade. When this happens, we know that there is a higher probability that a trend has developed and we will have a chance to get in on the trend. Let's spend a moment and talk about this.

There is no reason why you can't just take every single crossover as soon as it happens. Meaning, you can avoid the bad hours and just wait, during the active market hours of 02:00 am – 11:00 am Eastern US, for the 5 to cross the 13 and the 13 to cross the 62. This actually does work. It can be a profitable trading system. But what I am asking you to do here is to actually consider waiting until a trend has shown itself – and then we will jump on the trend and take a trade.



Once we see the trend, we are ready to start thinking about a trade. And here is what we wait for: *We wait for the candles to fall back down and touch the 62*

EMA. Then we buy.



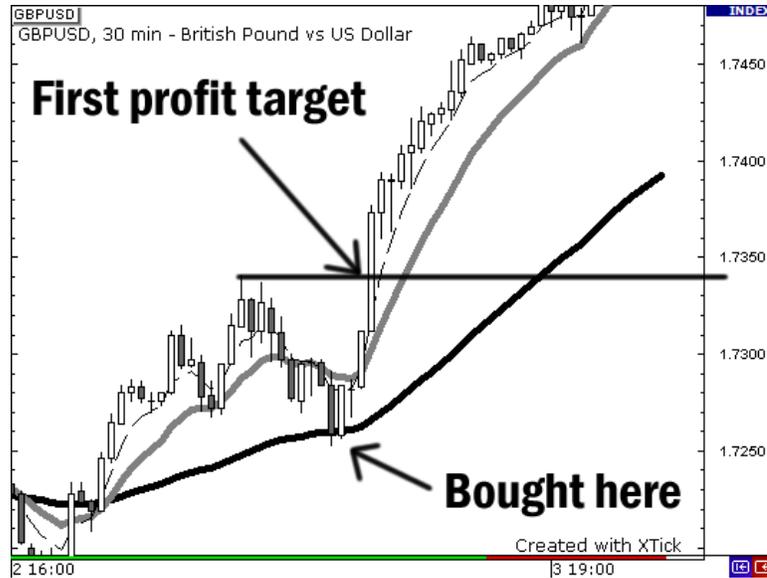
What about stops and limits? It's quite easy, really.

To contain our risk, we place a stop loss 25 pips below our entry price. The maximum stop I am willing to accept on a trade like this, on the 30 or 60 minute charts, is 40 pips. I won't show where we place the stop because I

We have more options on our profit target.

Set a profit target at the previous high that the pair made, before the candles fell back down to touch the 62 EMA. This will usually give us a profit target of at least 30 pips. On the example in the chart above, we have a profit target of approximately 80 pips. That's a very reasonable risk-to-reward setup.

Set a trailing stop of 20 pips and just let the trade run. This allows for the greatest amount of profit in fast moves in your favor.



Part II: During the Trade.

So now what? You have a great trade going. Do you set it and forget it?

I believe that anyone who tells you to “set it and forget it” is appealing to your greedy desire for quick, easy profits without any work.

And right now, I would like to spend a few moments appealing to your desire for quick, easy profits without doing any work.

After the trade is open, and you have your stop loss and profit target set, it is a perfect time to go do something else. Have you ever noticed that if you stare at the charts, the candles never move? But if you go walk the dog, eat breakfast, start a rock band. I could play drums and this guy with really long hair at lead vocals, who smokes so his voice can be really raspy, but has family and drug problems and sometimes has to spend the night in jail, which eventually breaks up the band and leaves us 10 years later on VH1’s “Where are They Now?”

If this disappoints you, or if you don't know whether a rock band is right for you, then feel free to watch the trade while it is open. That's perfectly ok, but just remember that many traders have experienced problems with peeing in their pants while their short term trades are open.

Part III: Where to Go From Here.

I have worked with hundreds of traders, all over the world, and many of them have altered the 5/13/62 system to work for them. They get in earlier, or later, with different stops and limits. Or they trade on special days.

The point is that you can adjust and test this system to make it your own. And when you make it your own, that is when you start making some serious pips.