Secrets of Forex Trading-First published by Forex Journal-December 2008

Among the pantheon of markets available to traders in this time of internet, broadband and supposedly 24 hour markets, Forex occupies a special position on the highest podium, but that's not to say it is without it's special traps and difficulties and most are of the "shhh it's a secret" variety that you won't know about until you fall into the trap that the manipulators have laid for you. Then it's roughly akin to being hit by a large, angry freight train..

A much easier option is to work with others who have a larger range of experiences in the hope that lessons can be learned once and shared, without each having to undergo the exquisite pain of a "gottcha" moment as you fall into one of the many traps laid for the unwary. In truth, there are fewer of these in forex than in other markets (equity indices are the all time champion joker) which is why I constantly advise my clients that forex is the easiest and safest market to trade, and equities the worst. Today we will examine a special forex trading project that we have been running at the Danielcode to see what lessons I can impart to you. Almost nothing in this model complies with popular trading lore which is why it works so well!

The Danielcode Forex Experiment

In order to create some meaningful data on forex trading I have been running an experiment at the Danielcode website www.thedanielcode.com since 1st July of this year with the DC forex Model Account. This summary sheet appears on the front page of the DC website.

Danielcode T.03 Model Forex Account*	
Updated:	2008-11-14
Account Starts:	2008-07-01
Capital:	$50,000
Trades Fin YTD:	$51,311
Return Fin YTD:	102.62%
Average Win:	$782
Average Loss:	$902
Win %:	89.41%
Average Risk:	1-4%
Days YTD:	136
(account history / *explanatory note)	

To give the program veracity, we laid out and published the rules and assumptions that the model account makes and I arranged for an independent third party to verify and post the trading results. The explanatory note lists the assumptions made by the model account and the account history sets out every single trade made in the account. Please take a moment to read the explanatory note so that you are familiar with the assumptions made. In particular, note that there is no allowance for slippage or brokerage in the account.

The first thing you will have noticed is the phenomenal return of 102.62% in just 136 calendar days and the high strike rate at 89.41% of winning trades. Less obvious is the degree of risk undertaken and what that actually means. Let's examine these issues now so that you can appreciate not only the tremendous profit potential of systematic forex trading and the opportunities that forex offers but also the building blocks of what I believe to be one of the most successful trading system in the world at present.

The aim was to collate a consistent output from the Danielcode program with a trading methodology that was simple and available to part time traders. You will find this program pretty cool! Eventually most professional traders adopt a trading system. This does not imply a black box solution but merely that at some stage you need to codify your trade selection and risk management rules to avoid the "will I, won't I" mental and emotional conflict that an ad hoc process inevitably brings.

Follow the ad hoc route long enough and you will destroy yourself emotionally and probably financially as well. You will jump into the easy trades that everyone sees and avoid the more subtle trades that surprise and usually produce the big winners. You bet too big or too small and eventually you don't bet at all as your plans lie in tatters and your self worth lies bleeding in the waste paper basket along with all those wonderful plans. The world is full of spruikers anxious to recruit you to the forex trading world. Systems abound and enticements like "It's Easy" advertised prominently on a well known trading platform are the come on.

Nothing could be further from the truth. It's not easy. The smartest minds and the best funded and researched trade strategies are on the other side of your trade. The trading platforms are stacked against you. All have a huge mathematical advantage (that's why they are in the business) and some are plain thieves that change the rules of the game as they go. And not to your benefit. Thousands of man hours and diagnostic computer programs are run to determine optimum trade strategies. Millions of dollars in research and resources are arrayed against you in the trading game. You have to be very good indeed to overcome these odds and in my thirty years of trading nobody has ever offered me a helping hand as I offer you, so read carefully. There is much to learn.

Trade Selection

Basic entry signals are created by the proprietary DC T.03 trading signals. The Danielcode is an ancient numeric model derived from the Book of Daniel that creates ratios that rule the universe. Trees, plants and animals including humans all grow and develop in accordance with Danielcode ratios. It is the universal definer.

Markets too are ruled by the Danielcode and it is a source of continuing wonder to see something as heterogeneous and conflicted as modern markets turning at the Daniel sequence numbers within a few ticks or pips. There are a large number of articles and videos available free at the DC website which highlight some of the more notable calls made by the Danielcode in markets as diverse as Forex, Gold and Silver, Equities, Oil and US Dollar index this year. Some were truly historic.

I create T.03 entry signals daily for over 30 forex pairs as well as other markets. Half are posted for members on the DC website and the balance are reserved for private clients. How those signals are created is not germane to this article but what is important is that they are created completely mechanically from spreadsheets that list the qualifying factors that make up the algorithm. You are welcome to see every entry in the model account, available to all at the DC website, so that is the first step in building a successful trading system. Of course the signal needs to have a high initial strike rate but that is only one of the building blocks that we require.

Risk

We have a number of risk factors in trading forex as we do in any market. Trading is all about risk. Traders love and embrace risk; it's what the game is about. Successful traders control risk to a high degree. Your approach to risk will depend on your trading stance and personality but risk management must be a cornerstone of your trading plan.

In the DC model account we use a very unsophisticated approach to risk. We maintain the total risk at no more than 4% of our trading bank and distribute that risk over all possible fills. The nature of forex trading is that a significant move in one currency will trigger trade entry signals in associated pairs so it is usual to have a number of possible trades with a high degree of correlation. To deal with this we simply calculate the number of all possible fills on the day and pro rata the number of contracts or mini contracts.

Importantly in any sequence of trades, some will be good and some bad. Some will be monster payoffs and others disasters. We never know in advance what the result of the next sequence will be so it is vital that we make the entry risk on each trade as nearly as practicable equal. Otherwise we will introduce an inadvertent bias into the model. For a more sophisticated approach you should calculate the difference between your entry point and the initial stop loss and express that in dollars. Then divide the allowable risk in your trading plan expressed in dollars by the initial risk on entry. That tells you how many contracts or mini contracts you can take to comply with your trading plan. If there is more than one possible trade that can be filled you pro rata the number of contracts across all eventualities. More simply, if there are three orders that may be filled today, take only a third of the calculated risk management compliant number of contracts for each order.

Further sophistication is achieved by using correlation tables available from your broker or on the internet. Personally I have not found these tables of value and prefer the simpler pro rata approach

Diversification

Almost all forex markets are correlated to some degree so we do not get diversification within the asset class but we can get a degree of helpful risk diversification by trading a wide group of forex pairs. The single greatest barrier to success that I see in my clients is their adoption of one, or just a few favourite forex pairs to trade almost as if they were old friends or household pets. All forex markets trade the same, so you will do much better by trading a wide selection of pairs. I trade over 30 forex pairs. The best results come from simply taking each signal as it comes without fear or favour.

Did you know that the Australian Reserve Bank spent a record $3.5 billion buying Aussie dollars last week? How could you. Central banks don’t wave a red flag as they are intervening in currency markets. That’s the whole point. This is just one of many unknown risks that will affect your trading and the way to minimise this risk is to trade a large number of crosses. They are most unlikely to all be undergoing intervention simultaneously.

Trading Platforms

There is no central exchange for forex and as such a number of trading platforms have sprung up with no central regulator. That means that you have few options if you have a dispute with your platform owner. Many are backed by banks who profess high standards of propriety and honesty. Recent banking events in US, UK and elsewhere should have opened your eyes to the fact that banks and financial service companies have led the bad actors in the credit implosion. They didn’t know what their assets were, couldn’t manage risk as they were totally unaware of what the risks were, and when push came to shove they looked after themselves first and clients a distant second. Be very cautious who is holding your money and if it is a bank backed platform ask for a letter from the supporting bank on its letterhead setting out what guarantees it is giving you in plain language.

Don’t be fooled by assertions of millions of dollars in capital backing or “interactive risk management”. The millions in assets are meaningless if there are more millions in debt and guarantees and the rest is mere advertising puff. With trading platforms like all institutions these days you need to know who is holding your funds and who is guaranteeing payment to you.

Trading platforms supposedly get their prices from the back end of banks. Some do and some don’t. The spread between the bid and ask is basically the platform’s profit and risk percentage. From the spread introducing and trading brokers are paid and many traders with substantial accounts under management get an introductory fee by the platform's owners also. The essential point here is to ensure not only that the spread is as small as possible but that it stays within reasonable limits. Spreads can change quite dramatically during the trading day and if that spread opens too far, even the best crafted trading system will be defeated.

I recently had this report from an Australian forex trading client of undoubted veracity using a platform that was recommended by one of my US brokers

> Oct 3, 8:09am Gold Coast time, AUDNZD spread = 22 ticks
> Nov 6, 8:40am Gold Coast time, EURAUD spread = 30 ticks, at times over 100 ticks.
> Nov 6, 9:05am Gold Coast time, CADCHF spread = 14 ticks
> Nov 7, 2:58pm Gold Coast time, CADCHF spread = 94 ticks
>
> CADCHF spread has been consistently 12 ticks. We were out to 75 odd ticks profit. Spreads have just been skyrocketing on that cross, (45 ticks, settled at 17 now). We got stopped out on a spread widening, and stopped out at 9899 for a 20 tick loss. Very frustrating. I'm seeing spreads of 94 ticks at the moment.

This particular platform is a US invention that as you can see are large on spreads and short on customer satisfaction. They are a market leader with huge advertising and marketing programs. You will likely have seen them. They profess to being reputable. This is as close as it gets to highway robbery. You start the trade effectively with 2 zeros on the roulette wheel and some time during the day the casino adds another 5 zeros to their take. This allows anyone with a level III screen to hit all the stops in that spread and that's exactly what these guys do. For those who assert that it doesn't happen and that spread widening merely reflects banks pulling back from the trade, come on down to Sydney. I have a nice Harbour Bridge that I can sell you. Honest!

Watch the spreads. They are the life blood of forex trading. Shop around. If you see something akin to the above experience happening to you, close your trade and find another platform.

Be careful of the prices provided by trading platforms and free web sites. It is essential that the OHLC of your daily bars is correct and that they come from a program that is properly set for time. Forex bars begin at 2200 GMT and end at 2159 GMT. Most US platforms are not correctly set and tend to close their day at 1630 US CST. I know it is a pain to work through these details but if your daily bar is closing on US time your daily price bar will be wrong. I use data from Genesis Financial Technologies and have for many years. Their forex bars are correctly configured and their data is precise.

Forex is the only true 24 hour trading market and that is one of its attractions. Anecdotally we notice that almost 80% of out T.03 system fills come in the European trading session so an American centric view of this world just doesn't work.

Because the daily data bars from different platforms are all different you need to allow a 5-7 tick buffer on your entry if trading off daily bars, to ensure that if you think you are buying a daily bar plus a few ticks, that in fact is where your order is.

Stop Management

You need to be proactive on moving your stops. On the T.03 trading model we move the stops to break even early and aggressively. On stop management the key is to be actively reducing risk while not shuttering the trade unnecessarily. There are a number of trading systems based on taking a very small profit as a method to enhancing the strike rate. That approach is not even statistically true. Profitability is a function not only of strike rate but also of the average winning and losing trades. It's the few super trades that make the winning average strong. Have another look at the DC model forex account. There are lots of small winning trades in there but it's the few 600lb gorillas that make the average. You must be able to harvest these occasional gifts as they occur.

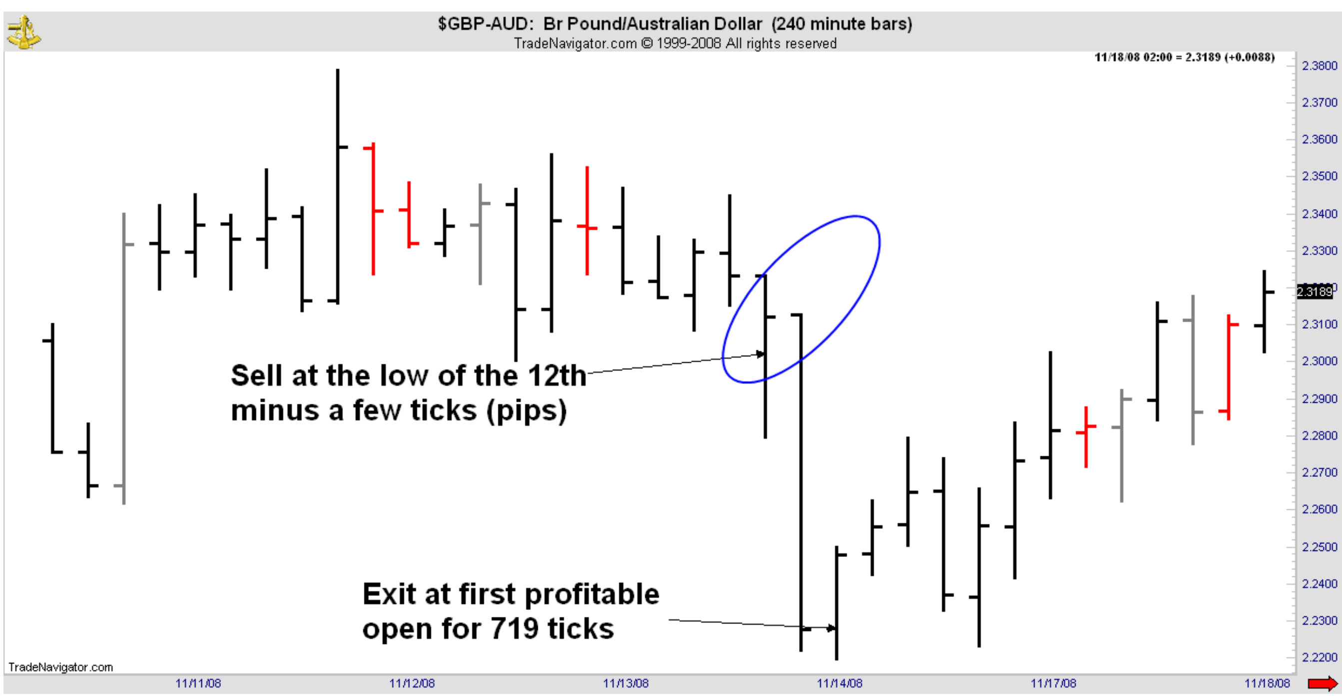
For the model account we move the stops to break even quite early and then use Larry Williams' first profitable opening on the daily bars to exit. There are many other exit strategies but this one is simple and understood by all.

Stop and Limit Entries

I am a momentum trader. I need to see the market moving my way. If we have timed the entry right and it is supported by the obvious indicators (stochastics etc) then we can expect an initial surge of momentum often sufficient to push the trade far enough from entry that we can move the stops to break even. That for me is the definition of a winning trade. I have now got rid of the risk on entry and have a risk free ride to my exit point which is FPO or the stop. Such an aggressive stop management policy means that we are stopped out of a lot of good trades but as I told you earlier, I am creating entry signals on over 30 forex pairs so entries and trades are just like the fish in beautiful Lake Taupo where I spend much of the year. The Trout are famous and there is always another one swimming by!

Most pro traders are derisive if not scornful of "on stop" momentum entries. They prefer to see the entry signal triggered and then hope for a retracement so they can buy their contracts on limit. This way they have a much smaller stop. The trade off, is that the trade may not retrace to their designated buying spot and they are unlikely to get that first momentum push that accompanies a well timed stoch entry.

Below is a recent T.03 trade that made 719 ticks (pips) with an entry simply off the daily bars. There was no significant retracement and the high of the entry bar was never breached.



Talking about Money

Gentlemen never discuss money, but in this business it is how we measure success. Our job as traders is not to be right but merely to make money. That of course implies being right for at least the time we are in the trade but given that the future can never be known by mere humans, the shorter the time we are in the trade the better our chance of being right just for those few moments (sometimes a few days) in time. Typically the T.03 trades run from 1-3 days. This I have found to be optimum, as most countertrends on daily charts are 1-3 days so even if you are trading a countertrend the probabilities are in your favour.

In the Danielcode model account we have executed 85 trades in 136 days from 1st July, about 4.7 trades a week from 31 pairs. 76 of those trades were winners and 9 were losers. Some of the winners were just 1 tick reflecting our break even plus 1, stop being hit. That reduces the average winning trade but increases the strike rate.

Note that the account is calculated on a level stake basis, that means the risk is always 1-4% of $50,000 the starting account. If you used a progressive staking method of adding winnings to the bank progressively and therefore increasing your bets as the progression advanced the results would be several degrees better. You can do the math. For assessment purposes though, you should always look at a flat stake summary. Progressive staking is dependant on where in the sequence the account starts. My experience is that if the program doesn't stack up on a flat stake basis nothing will save it.

Summary

The T.03 model account that I have shown you today is simply one output of the Danielcode price sequences that I have written about previously, collated in a consistent and verifiable manner. There are an infinite number of alternates and adjustments that we could have used, but I wanted to answer the question "Can I make money trading forex" and by implication "how much?"

The answers are Yes, you can make money and if you become good at it you can make a lot of money. If you take the model account return of 102% in 136 days and amortise that over a year you will see a staggering return off a 4% risk model.

Like anything worthwhile you need to work at understanding the markets and the trading platforms. At the Danielcode we have a large range of free resources to get you on your way as a forex trader. There is a DC Trading manual in document and video form, a series of "Learn to Trade" videos and a T.03 execution video as well as articles and videos on other markets. There is a free forex practice account.

We have pro and prop traders of the highest level from some of the biggest names in the world as clients and we have members who have never traded before who come to the Danielcode to learn. All are catered for with the proprietary T.03 signals that I provide as my gift to members, and my hope is that you will be able to make some money while you are learning. Most do. The T.03 signals have specifically been designed for the lazy (like me) or part time trader. Entering near the previous day's high/low is simplicity itself. Of course a dedicated trader will anticipate the signals on shorter term charts although I never go below a 240 minute chart. They will have smaller stops and bigger relative positions. They will also get more false signals but they know how to deal with that.

The purpose of this article is to show you how well a daily signal, executed off daily bars can perform. The Daniel sequence numbers give us true support and resistance in "price" and the T.03 signals give us an approximation of cycles or "time". As WD Gann said so presciently "When time and price are squared (equal), a turn will occur". Mr Gann didn't know about the Daniel sequence because Sepharial didn't know. But Sepharial knew a great deal about time cycles.

I invite you to visit the Danielcode Online to begin or further your journey in the wonderful world of Forex trading.

***Joh 4:48* Then said Jesus unto him, Except ye see signs and wonders, ye will not believe.**

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"The fox knows many things, but the hedgehog knows one big thing. A Hedgehog Concept is not a goal, intention or strategy to be the best. It is an understanding of what you can be best at. The distinction is absolutely crucial".
Isaiah Berlin, The Hedgehog and the Fox