

# *Swing Trading With Heiken Ashi And Stochs*

## *The Final Version*

*June 2012*

This document represents the culmination of nearly a years worth of trial and error, blood, sweat and tears. With the help of others on the forum I have taken an original idea and improved it until we have arrived at a consistently profitable system.

The rules can be summed up very easily and I have strived to keep the simple approach of the original system in the final version. Although I am calling this the final version I understand that different traders will have different beliefs about the market and will want to change elements of the system to suit themselves. That is absolutely fine with me, it's what trading is all about.

If you are relatively new to trading then try just following the rules to start with and see how it feels for you. The system is definitely profitable if followed correctly but it takes some discipline to continue to follow the rules after you have suffered a series of losses and break evens and it feels like you are going nowhere. I have been through many of these periods and the one thing I can say is that they never last forever. If you stick to the money management and trade management rules you will get through the slow patches and see your account grow in time. Just be patient and keep following the rules. Any idiot can strike lucky with one or two overleveraged trades but in the long run it is only the patient and consistent systematic trader that will be in the game long term.

### *The game plan*

Before I set out the system let's just talk about what it is we are trying to do. I like Greg Michaelowski's mission statement and game plan. Our mission statement is to make as much money as possible with the least risk possible. We will control fear by always using stop losses and only taking trades that allow us to enter the market with a relatively small stop loss.

Our game plan is to trade the impulse moves of the daily trend by trading the hourly trend that follows a daily system signal. I have tried trading countertrend moves as well but I find them less reliable and more choppy moves and so I am now sticking to only those daily signals that move in the direction of a daily trend. This will reduce the number of trades available but remember that when you find a good trend you will be banking very large gains so they are worth waiting for.

### *The original system*

The original system consists of heiken ashi candles, a 100 sma and stochastics with the settings 8,3,3, low/high. There are examples of valid signals at the start of the thread. I recommend you read the first few pages of the thread where the system is set out. Basically you are looking for a sloping moving average, the price above or below depending on the trend and a smooth pullback. Once the price has pulled back towards the moving average, the stochs have crossed in the direction of the trend and the heiken ashi candle has changed in the direction of the trend then that is a valid signal. Again, there are examples on the thread.

### *The final version*

The final version of the system is a dual time frame system. I prefer to trade daily and hourly charts but any two timeframes with a similar distance from each other will work. For position trading use monthly and daily, for scalping use 15 or 30 min charts and 1 min.

The system is still relatively simple. The indicators are the same. First wait for a valid signal on the daily chart. In theory you could just trade the original system and take the trade with a 200 pip stop loss and close the trade when the heiken ashi candles change back. That is fine but by using the hourly chart we can trade into the trend using smaller stop losses and also adding more trades as the trend develops.

Once you have a valid signal on the daily chart (the daily candle must have closed as a valid signal so you start trading the next day) then move to the hourly chart. If you have waited for the daily candle to close then the price should already have closed and be trading above or below the 100 sma in the direction of the daily trend. It often takes an hourly impulse move to create a turn on the daily chart so we do not want to enter straight away as after a big hourly push you will often get a pullback.

### *News and when to trade*

At this point it is important to watch for any major news announcements out for the pairs you are considering trading that day. I prefer to take trades in the morning UK time as then you have the rest of the day to move your trade in your favour. Aud and Jpy pairs can be traded in the UK evening as they have more liquidity in the Sydney and Asian sessions. If there is major news in a few hours time I will take a trade but I will try to get to break even if I think the news could cause a large spike. Avoid NFP morning altogether. Once the noise has calmed down you can trade in the nfp day afternoon.

### *The initial trade*

Our first trade will be the first valid system signal on the hourly chart. Remember, a valid signal is a smooth pullback, stoch cross and heiken ashi change away from the 100 sma. Quite often after a cross of the 100 sma you will see the price come back and actually bounce from the 100 sma. This is usually an excellent trade opportunity.

### *Trade management*

Once a trade has been entered put the stop loss 20 pips behind the 100 sma with the trailing stop ea (available on the thread) trailing behind the 100 sma by 20 pips but also with the option to 'close by ma' set to true. This means that if the price closes the other side of the moving average but doesn't hit the stop loss it will still be closed as the trade/trend has been invalidated. This prevents you from being stopped out by spikes that go 5 or 10 pips past the moving average but the price closes the right side of the moving average. The 100 sma is watched by a lot of traders and the battle between buyers and sellers can be intense around that level causing spikes before the trend continues.

Now you have a trade and a stop loss in place the only thing to do is wait. If the trend continues then eventually your trade will be at break even. In the meantime if you do get a pullback towards the 100 sma and a smooth heiken ashi change and stoch cross then you can only add on if the stop losses on the two trades combined do not add up to more than 50 pips. You will often get a second signal just below the first and it is fine to take that second signal if the two stop losses combined are not more than 50 pips. If the price is too close to your first entry then let it go and give your first trade more time to work out.

Continue to add trades all the time the price stays the right side of the 100 sma but keep in mind the 50 pip max risk rule. On a long trend you should be able to add 3, 4, 5 or even sometimes more trades per position.

The exit signal for all trades is when the 100 sma is breached. Either the price goes a long way past it and hits your stop losses or the price closes the wrong side of the moving average and the ea closes out the trades.

This often means that you will lose at least one of your trades for a small loss. On the occasions that you catch a good trend you will be banking between 400 and 1000 pips on all trades combined so a small loss won't matter.

With a trend following system like this you will find that you get a lot of small losses and break evens before you catch a good trend but by using the higher timeframe trend to start looking for trades you should increase your probability immensely.

### *Money/Risk management*

I recommend risking no more than 3% on your first trade and each subsequent trade. There is an indicator on the thread that will calculate the lot size you should use to risk X% over X pips. I have this set to 50 pips at 3%. In time as your bank grows you should reduce your risk on each initial trade, ideally down to 0.5%. You may find that you only catch one or two really good trades a month but they will pay for all of your losses and more.

### *Summary*

- 1) Wait for a valid signal on the daily chart
- 2) Move to the hourly and wait for a valid signal on the hourly
- 3) Enter the trade with the stop 20 pips behind the 100 sma, use the ea
- 4) Take every valid signal provided the combined risk on all trades is not more than 50 pips
- 5) Exit all trades when the 100 sma is breached.

### *Pairs to trade and correlations*

I will trade any pair. As I am only trading signals in the direction of the daily trend I will trade every pair that sets up but I will not trade positively or negatively correlated pairs together such as eurUSD and usdCHF or usdJPY and cadJPY. I will trade eurUSD and gbpUSD or audUSD together as they are not always completely correlated but one further rule is to only expose yourself to the same currency pair twice so if I have two trades featuring USD then I cannot take any more. If I have two trades involving the euro then I will not take any more.

### Daily routine

- 1) Review current trades. Is there a chance of an add on today?
- 2) Review daily charts for any new pairs setting up.
- 3) Set up charts for any possible new trades.
- 4) Check news for the day.
- 5) Check rules concerning correlated pairs and the two trade per currency rule.
- 6) Monitor the charts for possible trades. The stoch crossing indicator is useful.
- 7) Take any valid trades and ensure ea is set up properly and stop loss is in place.

### Some extra rules

- 1) Always wait for a candle to close before you open a trade. If you miss the end of the candle but the price hasn't moved far then it's still ok to enter but don't chase a trade for the sake of it, you'll just increase your risk needlessly.
- 2) Only ever use your predetermined position size. Never increase your position size after a loss.
- 3) Never add to a losing position, only add on when your previous trades are in profit.
- 4) Never take profit manually because you "think" the price will pull back. It probably will pull back but to catch the big trends you have to stay in through the pullbacks.
- 5) If there are no trades setting up on the daily then don't try to guess a trend on the hourly.
- 6) Stick to one system in one account, keep your systems separate. Most brokers will allow you to open multiple accounts to trade different systems.

The above is my exact trading plan. I will be trading this on an ongoing basis and I will be on the thread to discuss trade setups. Thanks for

reading this far and if you can see any errors or omissions or anything else you would like me to discuss then please let me know via the thread or PM. Good luck with your trading.

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