THE NETPICKS INFORMER

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LETTER FROM THE DEVELOPER

Could it quite possibly be Fall already? It wasn't long ago that I was "enjoying" something like 60 days straight of 100 degree plus summer weather and just like that fall and cooler weather has arrived.

Historically, this is always a time of great volatility in the markets. You all know some of the biggest crashes have happened around this time – and some amazing rallies. As far as I'm concerned, the more volatility the merrier. I would certainly not expect this to be quiet times.

We'll have some holidays coming up here in the U.S. and globally that will of course put the brakes on the market volatility but it's likely to be very temporary. This should be a great time to be an active trader.

With that in mind, we continue to put 100% of our focus on how we can help you become better active traders. You'll be hearing quite a bit about our new Seven Summits Trader "PRO" version (SST Pro) coming out just a few weeks from when I'm writing this to you. If you think what the SST can do in its current format is impressive, wait to you see what our team has been busily working the long days and nights on for the Pro version. We're bringing you advanced tools and automated trade plan development, the ability to track the advanced trades that the SST so capably produces and even teaching it live in person if you choose.

Now, we simply would not stop there. We're also about to release the first of our new podcast series called "The Day Trading Authority" that is going to be hosted by myself and Brian Short. This free podcast/MP3 is going to be released regularly, and we'll be cover topics of great interest to you as active traders. In addition, we'll have guests such as our trading coaches for interviews and we're planning to interview NetPicks clients as well.

Which reminds me, do yourself a favor and get over to the Trading Tips Blog at the NetPicks website. http://www.netpicks.com/trading-tips gets you there. Why? We've got interviews from successful NetPicks clients, as well as a broad range of articles, videos, tutorials and webinar replays from our esteemed Coaching team. Highly educational, and trading talk not based on theory, but based on actual, daily experience live in the markets. Is there a better way to learn? It's the only way to learn – from people doing it each and every day. And yes, this is all free as a service to you the active trader.

Remember, active traders do not fear the news. We embrace the news and we can definitely profit from the news. While everyone else might be out there despondent over so much doom and gloom we can use our skills and navigate through these times of volatility with success. Just arm yourself with the latest knowledge and skills. That's why NetPicks exists and what we're here for – to help you. It starts in the pages that follow. Enjoy this issue and as always, I wish you much success in your trading.

Mark Soberman

Mark Soberman

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WHAT'S NEW AT NETPICKS

As usual, new and exciting developments are afoot at NetPicks HQ!

The Day Trading Authority Podcast

As Mark mentioned in his 'Letter from the Developer' article, we've just started our first NetPicks podcast, called the Day Trading Authority (pretty cool name, right?).

What is a podcast? Basically, it's a radio show recorded on a regular basis (for us, every couple of weeks) that you can download from iTunes (or our website) and listen to at your convenience. Each podcast will be downloaded in an mp3 format so you can upload your NetPicks podcast to your iPod or other mp3 player. Listen in the car, on your way home from work, at the gym – anywhere!

From trading success stories, to our biggest obstacles, what the market is doing (and hey, what the market ISN'T doing) – nothing's off limits here. It's funny, it's informative – and it's all education. So make your way over to our NetPicks podcast website and download the first episode now:

http://www.netpicks.com/podcast

Author Series Interviews

We're also building awesome relationships with experts and other industry top-dogs to bring our continuing series of educational webinars to a whole new level.

From Michael Martin who wrote *The Inner Voice of Trading* to Anne-Marie Baiynd that penned *The Trading Book: A Complete Solution to Mastering Technical Systems and Trading Psychology*, we're partnering with them to share their exceptional expertise with you.

To be invited to the next Author Series, click on the link below:

http://www.netpicks.com/authorseries

Seven Summits Trader Pro Version

Our workhorse trading system, the Seven Summits Trader is getting a professional grade makeover with the SST Pro Version coming out in November of this year!

Boasting solid results week after week, month after month – owners were coming to us wanting MORE tools for serious trading careers. We're not talking about the occasional hobbyist here… these traders are bent on making a living day and swing trading with the SST. And with the SST awesome track record, we couldn't see a reason to NOT come up with a 'professional-grade' SST package with developer-level tools and advanced tactics for the serious trader.

Make no mistake, when we say 'serious trader', we don't mean 'advanced-level trader.' Even new traders can be serious – they just need to have the drive, commitment and understanding of what it takes to trade on a serious level (not just 'here and there' whenever it's convenient).

If you think you fit this criteria, put down this newsletter and visit the SST blog below to get on the Updates List for the SST Pro and we'll send you more info:

http://sevensummitstrader.com

ARE THE HARD AND FAST RULES... ...REALLY THAT HARD AND FAST?

Shane Daly

After my recent webinar held with NetPicks, I have and continue to receive quite a few emails. The questions are all over the map but two show up in just about every single email:

- What is the risk/reward ratio?
- How much to risk per trade?

Those are fair questions. After all, every single trader has had those two items pounded into their heads time and time again. While it is easy to rattle off the usual answers, it is really too simplistic. After all, positive R/R ratios are not the grail to a successful strategy, nor is risking 2% per trade.

So what is the correct answer to each of these questions?

Let's look at risk to reward

If I take a trade where the risk is $100 and the reward is $300, what is the ratio? I am sure you said the risk to reward is 1-3. Is it? Out of those two-dollar amounts, what is the only true definite? The risk amount. The reward amount is potential, what you will shoot for. It is not a definite amount. So if the only definite is my risk, what good is that number? On the surface it makes sense. Make sure your wins are multiples of risk. In actuality, it really doesn't show the effectiveness of

your strategy. Well, what does? While you may not want to totally discard risk/reward ratios for the sake of having a rule set, there is something else you may want to keep your eye on. (Having a high reward to risk based on market structure can increase the probability of making money but is beyond the scope of this article)

The key for me and has been for years is keeping your eye on the average profit made over a series of trades. In no way did I invent this. I was first exposed to it years ago by Van Tharp. Here is the calculation:

Average Profit/Trade =

(Probability of Win * Average Win) – (Probability of Loss * Average Loss)

Let's assume you have a strategy that wins 70% of the time. Assume your average win is $400 and your average loss is $800. Most would discount a 1-2 reward to risk strategy.

Plug in some numbers:

(70% * 400) – (30% * 800) =$40.00

Even with a negative R/R, this strategy will still make money. Play around with that calculation and you may be shocked at how a low winning rate can still make you money.

Risk per trade

Since we are talking about risk as well, what is the amount you should risk per trade? 1%? 2%? Sorry, once again there is no straight answer. There are many factors that go into your decision including your comfort level AND your strategy. There are some setups that I play where I have risked in the low double digits simply because the probability of making money on it, are great. It may be prudent for those new to trading to stick with the often-touted percentages. When to increase your risk percentage is a pretty advanced approach

to trading. If not done properly, you will hand your broker your account faster than you actually funded it.

Check back to Trading Tips for my next video where I go into detail on what moves the markets and how you can learn to cut your trading learning curve in half.

- Shane Daly: Forex Expert Extraordinaire from the Great White North

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WHAT IS A FOREX TRADE COPIER? *Ron Weiland*

What is a Forex Trade Copier? Until about a month or so ago, I did not have any idea. The good news is I found someone who has been researching them for several years and has given me the inside scoop that I want to pass this experience along to all of you. So, what is a trade copier? The easiest way to explain it is a trader enters his Forex trades and they are then sent to all of the others accounts to copy or mirror his trading. Unfortunately, like with trading in general almost nobody has been profitable longer term with acceptable risk. Far too many trade dangerous systems that using martingale or averaging that adds to losing positions.

There are really 2 types of "copiers" for clients to consider. There are manual software copiers popular mostly for MT4, and Forex like I am using which allow for intimate personal control of how you want to execute the trades the Master Trader is sending over: things like trade size or risk management. Then there are mirroring technologies offered by popular websites (e.g. Tradency.com, Zulutrade.com, Collective2.com, Rentasignal.com, and Metatrader247.com). These usually want you to open an account with a specific broker or a group of brokers, so that the signals will go to your broker account. They also mark up the spread to pay the trader!

Copiers and/or Trade duplication in all their forms are VERY popular. The desire for people to leverage already successful traders is huge. The statistics for profitable traders is low and most everyone knows this. So any trader who has a profitable system with good risk management and who offers their services through some kind of trade duplication technology will be very attractive to potential clients.

Copiers do have latency, though, so they aren't always successful for every type of system. Scalping systems of 8 or 10 pips won't work well if you don't have the same broker. Only "BLOCK trading" with the same broker would be guaranteed to work for that kind of scalping system. On the other hand any system that has larger targets/stops than scalping (like the UST or One Day Swing Trades or Keltner Bells) works very well using an Internet copier.

The manual copiers like I am using which run locally on the clients MT4 require the system to be running 24/5. So this often means it is best to get a VPS so you know that your MT4 will always be connected to the internet to receive the trader's trades. With some services like Zulutrade, this is all handled

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on their website backend and you don't need to worry about running anything locally or on a VPS. The biggest downside with services like Zulutrade, is often you have limited choices in broker and they markup spreads.

Finally, another great thing about trade copiers is that your results can be published and verified for the world to see. There is a site mt4i.com that posts trade results from other traders using trade copiers. The trader can delay the posting of the trades, by 12 or 24 hours.

This way, people who are not paying for the signals can't see them in real time and follow them.

So, we will continue to test out trade copiers and very soon you might see us release a trade copier type of service. As many of you know, I have been calling live VIP trades using our Ultimate Swing Trader system for the past year and a half. Soon, all my trades can be sent out live and posted on a 3rd party website for verification. Pretty neat huh? We will keep you posted and remember, if you want to play with a trade copier and follow another traders signals, make sure you Demo Trade it for a while to be safe!

TRADING PLAN METRICS *Bob Malinowski*

I recently ran into a neighbor at the local grocery store who knows that I have been trading full time for a number of years now. He has a full time job at the Pentagon, but like a lot of people, also has a stock portfolio that he manages for himself. He often asks me what I think about particular stocks, or what direction I think the market is going, but this time the first question he asked me was "what is your win rate"? Now, I usually tell him that my opinion about particular stocks or the direction of the market is of little importance (even to me), and that no one should be taking stock trading advice or tips from anyone without first having their own solid back tested trading plan. But this time his question seemed even more irrelevant. At first I was not sure how I should answer him. To place the answer in the correct context would require more time to explain than I cared to spend while shopping for vegetables. So I decided to toss out a number, 65%, and see how he would react. To my surprise, he was satisfied. No follow-up questions about average win rate or any other relevant details that would actually tell him anything about how well my trading was going. Wasn't he aware that there is more to trading success than win rate?

In this article, I am going to cover some of the minimum basic trade plan metrics that are required to adequately assess your back tested trade plan and track your progress as you trade it. As we shall see, win rate is important, but there are other factors that are equally important. The following metrics and relationships between metrics will be covered:

Win rate
Loss rate
Average win
Average loss
Total number of trades
Number of winning trades
Number of losing trades
Profit factor
Statistical Expectancy (average profitability per trade)
Expectation (mathematical outcome)

Win rate is usually the metric that is first considered by new traders and often pitched by trading system or service sellers in aggressive advertising. Win rate is calculated by dividing the number of winning trades by the total number of all trades, and is often represented as a percentage. Conversely, loss rate is simply the number of losing trades divided by the total number of all trades, or 1 – win rate. We often hear of systems that have high win rates (or even systems that "never lose"), but in trading there are always tradeoffs. The most important metric to be linked with win rate is average win and average loss. Average win is calculated by taking the sum of all winning trades and dividing it by the number of winning trades. It is the expected value of an average winning trade. Average loss is calculated by taking the sum of all losing trades and dividing it by the number of losing trades. It is the expected value of an average losing trade. A system with a high winning rate can still be a losing system if the average loss is much greater than the average win. This important detail is often left out by promoters of high win-rate systems.

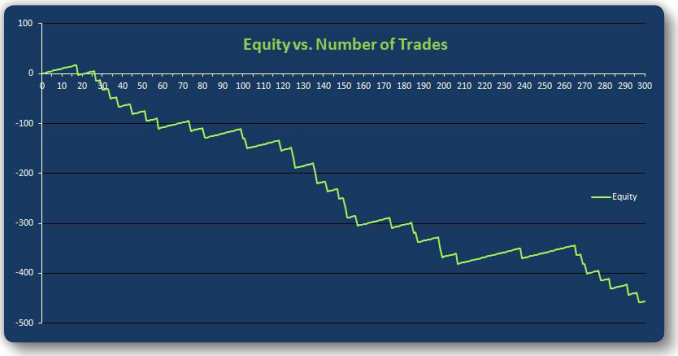


Figure 1: Trade Plan 1 with 90% win rate, Average win/loss ratio 1:20, PF 0.45

For the purpose of the following examples, I will refer to the gains and losses using dollars, however gains and losses can be expressed in dollars, points, ticks, pips or whatever. Figure 1 shows an example an equity curve resulting from 300 trades taken using a system with a high win rate of 90%, but with average losses that are 20 times greater than average wins. These types of systems can be seductive because the high win rate is alluring for a while, and can often appear to be paying off, but then the inevitable losses occur, wiping out all gains. An example of a strategy capable of this type of behavior would an option spread selling strategy. The premiums collected are small and predictable, but when the market suddenly moves against you, the losses can be significant. Notice that the first 15 or so trades were winners, but the next trade wiped out the gains and returned to break even. Also notice that there was a period starting around trade 205 that went for over 50 trades where results were positive, but again, subsequent trades wiped out all the gains, and then some. When the win/loss ratio is this unfavorable, even a high winning rate is not enough to make up for the losses, and the statistics associated with these types of systems make them losers in the long run.

Figure 2 shows a trade plan with only a 10% win rate, but unlike the first trade plan, the average trade win is much higher than the average trade loss (18 to 1), resulting in a winning

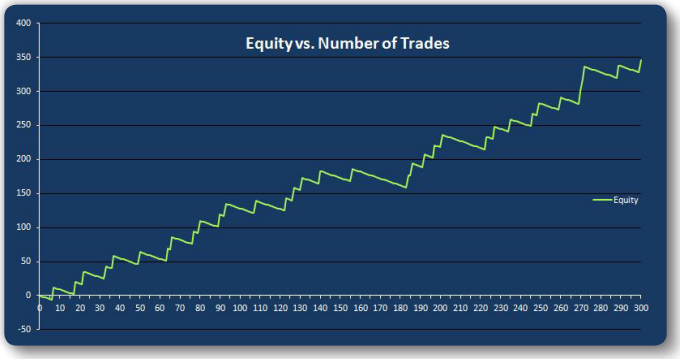


Figure 2: Trade Plan 2 with 10% win rate, Average win/loss ratio 18:1, PF 2.0

trade plan. An example of a plan capable of this behavior is one where each trade risks a small amount of capital with the small expectation of hitting a home run. There are lots of small losers, but when the trade is successful, the gain is large. This example starts with a number of losing trades, followed by a win that more than makes up for the losses. Notice that the overall equity curve is positive, but there is a section in the middle where a string of over 50 trades is in drawdown. Although these types of plans can be profitable, many traders find it difficult to handle the trade psychology, and the stress associated with long stretches of losing trades causes them to abandon the plan.

Figure 3 shows a trade plan with a 50/50 win rate. Each trade is just as likely to be a winner as a loser, but since the average

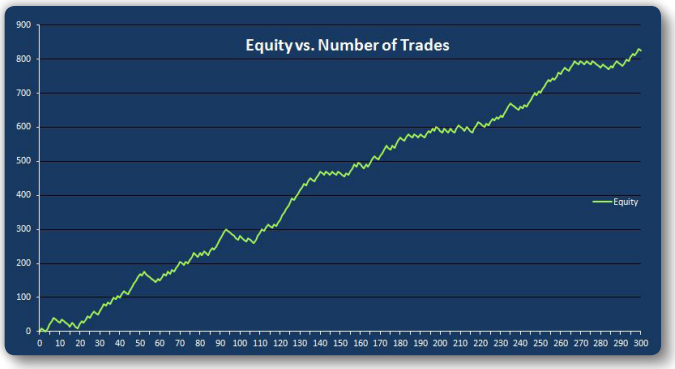


Figure 3: Trade Plan 3 with 50% win rate, Average win/loss ratio 10:5, PF 2.0

winner is twice as high as the average loser, the overall equity curve is positive. Notice that there are periods of drawdown just like the second example, but they tend to be shorter in duration because the overall equity curve is smoother. Since the number of winners is approximately equal to the number of losers, we don't have long periods of either winners or losers.

So, how do we determine whether or not a trade plan has the potential to be profitable? The answer is Profit factor. Profit factor is calculated as the ratio of the sum of all winning trades to the sum of all losing trades.

Profit factor = (gross winning trades) / (gross losing trades)

or

= (Win rate x average win) / (Loss rate x average loss)

Profit factor needs to be greater than 1.0 to have a winning plan. That makes sense; it simply means you need more total winnings than total losses. The second formula above shows how profit factor can be calculated using the win rate, loss rate, the average win amount, and the average loss amount. It is easy to see now why the first trade plan was a loser:

Trade Plan 1 Profit Factor = (0.90 x 1) / (0.10 * 20) = 0.45

Since the profit factor was less than 1.0, this plan was doomed from the start. Here are the profit factors for the second two trade plans:

Trade Plan 2 Profit Factor = (0.10 x 18) / (0.90 * 1) = 2.0

Trade Plan 3 Profit Factor = (0.50 x 10) / (0.50 * 5) = 2.0

Both of these trade plans had profit factors greater than 1.0, and therefore were profitable. All else being equal, the higher the profit factor the more profitable the trade plan.

Another important performance metric that makes use of the win rate, loss rate, average gain, and average loss is statistical expectancy. This metric is calculated as:

continued on next page

Expectancy = Net of all trades / Total number of trades

or

(Win rate x Average win) - (Loss rate x average loss)

This metric is also known as the average profitability per trade because it gives us the expected profit, on average, for each trade made. Here are the expectancies for the three trade plans above:

Trade Plan 1 Expectancy = (0.90 x 1) - (0.10 * 20) = -$1.10

Trade Plan 2 Expectancy = (0.10 x 18) - (0.90 * 1) = $0.90

Trade Plan 3 Expectancy = (0.50 x 10) - (0.50 * 5) = $2.50

Notice that, on average, the first trade plan is expected to lose $1.10 per trade, another indication that it is a losing plan. After 300 trades, we can expect to lose on average about $330, and the chart shows this loss to be a little over $400. The next two trade plans have the same profit factor, so you might be inclined to conclude that they are equally profitable, but notice that the trade plan 3 has a greater expectancy per trade. After 300 trades, we would expect that trade plans 2 and 3 would have net gains of $270 and $750 respectively. The equity charts above confirm this. Notice that like trade plan 1, they are close to their expected values, but not exact, because again we are dealing with statistical expectancies.

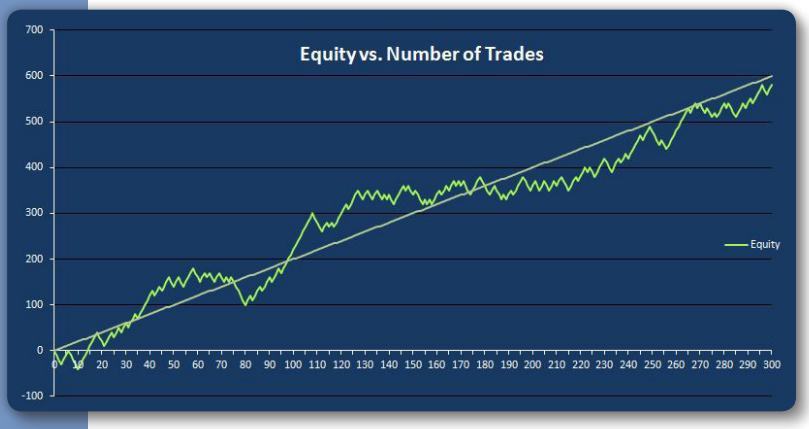


Figure 4: Trade Plan with 60% win rate, Average win/loss ratio 10:10, PF 1.5

A final example of expectancy is shown in Figure 4 which is a trade plan with a 60% win rate, with average win of 10 equal to the average loss of 10. Using the above formulas, the profit factor is 1.5, and the expectancy is 2. Even though the average win equals the average loss, this trade plan is profitable because the win rate is greater than 50%. Figure 4 shows that with an expectancy of $2.00 per trade, we can plot the expectancy along with the actual trades to verify that the plan continues to be valid. If we see over time that the actual trade equity diverges from this line, then we know that the market has changed, and we will need to re-evaluate our plan.

This is useful because in order to analyze our trade plans, we need to include not only win rate, average wins and losses, and profit factor (to determine that we have a winning plan), but we need to add expectancy and number of trades in order to determine exactly *how* profitable we expect the plan to be over time.

Finally, there is another statistic that is useful for determining how robust a plan is. It is called Expectation, or mathematical outcome, and is calculated as:

Expectation = Expectancy / Average loss

This metric reflects a more subtle concept, but an important one. Expectation reflects how robust a trading plan is by measuring how sensitive it is to changes in average loss. The greater the ratio of expectancy to average loss, the higher the expectation. With high expectation, small changes in average loss will have little effect on our net profits. As this ratio gets smaller, however, small changes in average loss will have a greater impact on net gains. Some good rules of thumb for expectation are: If expectation is less than 0, then the expectancy (gain per trade) must be less than 0 and it is a losing plan that should not be traded. If expectation is between 0 and 0.5, then the plan is OK, but we should monitor our losses to make sure the average does not significantly change (get greater). If expectation is greater than 0.5, then we have a robust trading plan. Using the formula above, expectation for the four example trade plans are:

Trade Plan 1 Expectation = -1.10 / 20 = -0.055

Trade Plan 2 Expectation = 0.90 / 1 = 0.9

Trade Plan 3 Expectation = 2.50 / 5 = 0.5

Trade Plan 4 Expectation = 2.00 / 10 = 0.2

It should be no surprise that the expectation for trade plan 1 is below 0, since it is a losing plan. Of the remaining three plans, trade plan 2 is the most robust with an expectation of 0.9. Expectation for trade plan 3 is right at 0.5, which means it is moderately robust, but should still be monitored. Finally, trade plan 4 is the least robust, and although it is profitable, it should be monitored more closely for changes in conditions that might cause it to become a losing plan.

There are also a number of other trade plan metrics that are useful for other purposes, such as fine tuning risk per trade, but the metrics presented here will at least ensure that the plan has the potential to be profitable in the long run. So, the next time your neighbor asks for your win rate, give him some other statistics. For example, tell him instead that last year you had 875 total trades, 350 losses with an average loss of $200, and a profit factor of 2.25. See if he can determine your win rate and net gain for the year (answer: 60%, $87,500).

TRADING THE CRUDE OIL INVENTORY REPORT *Brian Short*

One of my favorite times to trade each week is on Wednesday and specifically the Crude Oil Inventory Release. My goal for this article is not to give you a specific trade plan for this event, but to give you some general guidelines and share some observations I have noticed in trading the release of this report.

The crude oil inventories are released every Wednesday at 10:30AM EST (14:30 GMT) by the Energy Information Administration (EIA). If there is a holiday on Monday, Tuesday or Wednesday, the release time will be moved to Thursday at 11:00AM EST (15:00GMT). The crude oil inventory report represents the weekly change in the number of barrels held by commercial firms, including domestic and customs-cleared foreign crude oil in transit to refineries. This release generally brings a lot of volatility into the market.

Leading up to the oil inventories release, market analysts will give their view on what the change in inventories figure will be. The average expectation of all these different market analysts becomes the market consensus figure and this expectation gets built into the price of oil. So let's say that analysts expect that inventories will fall by four million from the previous week. In this case, all else equal, the price of oil should go up leading up to the release. When the actual change in inventories number is released, it is the deviation from the expected number that is really important. If the actual inventories figure shows a two million decline when a four million decline was expected, then that is actually negative for the price of oil. All else equal, oil's price should fall after the release.

What's really great about this event is that the analysts are rarely correct in predicting the exact number. It's just like a weatherman with hit-and-miss, mostly miss and sometimes a big one. It's this discrepancy that can create some very active price movements after the release of this report.

As traders, there are two ways we can approach trading the crude oil release. The first way would be to trade the release deviation. For instance, if the expectation was for crude to come out at plus four million barrels and the actual release was negative two million barrels, that is a deviation of six million barrels and we would expect this to be very bullish for crude and the price should head higher. In this scenario we would go long on crude futures at the market and try to ride the uptrend as long as possible. There are, however, a few issues that you should be aware of with this type of trading. First, the price action right at the release is very volatile most of the time, with spikes in both directions and very likely not executable. Slippage is also an issue right at the release, so beware of this on your entries and exits.

The second way would be a systematic approach and my preferred way to trade this event. When using a systematic approach, we let price action and our system tell us what trades to take. Next, I would like to review my general trade plan for trading the crude oil inventory release. Notice that rule number three has us sitting out the first two minutes after the release. This helps us avoid the choppy price action that can occur right after the announcement.

1. I use the *Seven Summits Trader* method as my core strategy.
2. I use the *SST* on a 377 CL futures front month tick chart.
3. I begin trading after the first 2 min have passed so at 10:32 am EST I have the potential for my first trade. I will get in sync with the system if a trade has triggered before the 10:32 am start time, but the price action must be at or below my entry point.
4. I use what we call Power of Quitting (2 wins and done.) That means if I have 2 wins on the session and I am positive, trading stops.
5. All trading stops at 11:30 am EST. If a trade is in progress at that time it will be managed to its target or stop.

If you would like to see a video review of a Crude Oil Release you can go to the link below.

http://www.netpicks.com/trading-tips/trading-the-crude-oil-inventory-release/

So, if you're a trader who is time challenged and cannot intraday trade each day, I would encourage you to look at trading just this one day a week. Most of the time we will get very active price movement after the release and on some days I am done trading as quickly as 10 minutes. Finally, take the points in this article and develop your own trading plan and approach to trading the Crude Oil Inventory Release.

Good trading to you.

FLEXIBILITY IS YOUR KEY TO SURVIVAL *Guest Contributer, James Kessick*

Having a plan for what we think the market may do can be an important tool for a trader to succeed. But human emotions can at times get in the way and make us hold onto an idea by stopping us from seeing deviations in the market which change the prospects of the plan. Sometimes it's purely that in the moment of the trade it's difficult to work out whether changes have occurred in the market or it's just the theatre of the trading day playing out in its sometimes confusing and disorienting manner.

I have seen and heard of many a trader who has a good run then is wiped out. Why? Because they find something which seems to work for them really well but when that ends, they aren't flexible enough to change the plan or at least have an alternative to turn to. My belief is that we should always be flexible in our trading to give ourselves the best chance to survive and prosper.

Here are some simple yet important ideas to help you maintain your flexibility:

- Don't trade when you haven't prepared thoroughly. If you haven't prepared and you don't know what to expect, you are less likely to be able to adapt your view of the market quickly and appropriately.
- Don't trade when you are tired or emotional. This is probably my biggest source for being stubborn in my trading. It is a trigger for a less aware and more emotional state which is often blinding of reality.
- Be aware of the big picture as well as the small. Having an adaptable plan is often about looking beyond just what and how you trade. Understanding the market from different types of participants' perspectives can give you a variety of ideas to study.
- Plan for alternatives so that if you see deviation, you still have solid reasoning for what the market may do. Decide that the market has shown a different agenda and trade it without a careful plan and you may be asking for trouble.
- Try to have a 'break clause' for your plan. Know the elements of the market which are telling you its story. Understand where these elements may appear to help confirm your plan and things which may persuade you to switch to a different plan. Watch the market for these tells through your trading timeframe and you'll see the plot unfold before you.
- Don't be behind the curve. If you are chasing an entry or an exit, you are far less likely to be able to see what is going on. The real cost of missing an entry is often not about missed profits, but how it changes your emotional balance.
- Monitor your strategy over time. If you don't, you'll be less aware of mistakes and how much they cost you. You'll also be less aware of changing market conditions. Traders who don't fully observe their strategy's performance often complain about the market being poor rather than looking to see if there's a better way to trade the current conditions.

Here is a simple example from Thursday 13th October 2011. Quite near the top of its recent bracket, the E-mini S&P 500 clearly sold off into the 4:15pm EST close. One of my scenarios was a possible selloff. The plan was if I could get a test of the prior day's late selloff and gauge strength, I might go short to position myself for a further move down. Weakness on open and I'd be waiting for a move back up of some sort to see whether or not the selling could persist. So what happened was there was selling early on, but not to the same extent as I had thought. This was the first sign to me that a bigger selloff wasn't about to happen. The next sign was when price had got into the Monday/Tuesday range, price action was suggesting buying. All this was happening while the trend was still down. The 3 min chart to the right was where I switched my view and started looking for long entry points for a test back into Thursday's range.

The market does what it does regardless of what you expect. Get it right and you might profit, get it wrong and you will lose. So whenever you trade you have to think in probabilities. Not the probability of what the market may do, but the probability of your judgment of the market being correct. Take each and every action of the market as piece of information. When you lose on a trade, if you have thought it out well and you have a sound strategy, that information is golden. It's probably cost you a lot too, so make sure you use it well! When you start doing this, you'll see that there are many different ways a market can behave and you'll be much better positioned to profit even when situations arise which you felt were less likely to occur.

Trade well.

BIG VISION – BIG PROFITS

Navigating the Rough Waters of the Sea of Russell *Troy "TJ" Noonan*

Everyone has heard the analogy that the market moves like the ocean. Major macro trends are like big tidal water flows producing powerful energy moves. As you work down to smaller timeframes you find smaller waves inside of the big tidal movements. Keep working down and the moves in the market are like the ripples on the surface of the water. Much of it is just a reaction to short term market noise just how the ripples in the water are often due to a number of small creatures swimming around or in some cases, thrashing around. A wounded fish or sea creature might be the source of a feeding frenzy in shark-infested waters, for example. The sharks thrash around causing choppy surface water but the major currents are unaffected.

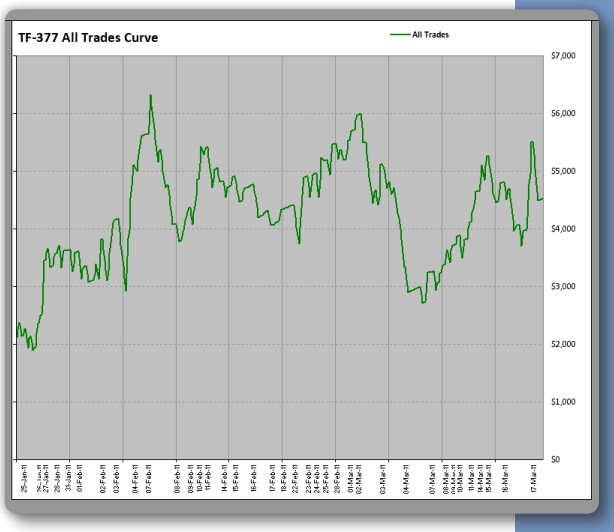
This is analogous to what occurs in the markets. Major moves occur and then the markets retrace, and consolidate. The 'sharks' thrash around pushing the price up and down, while all the dying 'meat' gets consumed. If you think about, it is pure Darwinism. The strong consume the weak. The strongest survive. The important thing to make sure of is that you do not find yourself overboard, swimming around with the predators. You need to stay in the boat!

Trading is a lot like fishing if you think about it. You float along with the major currents and ride on top of the ripples and choppy waters. You bait your hook and cast it in the water. You get nibbles. You get bites. Sometimes you catch your fish, big or small. Other times you lose your bait and maybe even your hook. Heck, you could even lose your entire fishing pole. Just don't get pulled overboard! A small but significant percentage of the time, you hit a bounty that you could scoop up with your net. Those are the best of times and are the experiences that help you achieve your reason for being in those waters in the first place. Your catch ebbs and flows like the tides you are riding on. It's all about odds and probabilities really. You have to have your line in the water though or you'll never catch anything. As long as you remain well established in your boat, on top of the water, and you don't run out of bait (amongst other things) you can keep casting your hook in the water, and the odds will work in your favor over time.

As we post our trades and build our win/loss column, we can rise to an even larger point of view and look at a different type of wave. We can begin to see the waves that our equity curve creates. The equity curve is a powerful way to measure where you are at with your trading. Moreover, IF you are executing your tradeplan correctly (and it is a good tradeplan), you can discern what is happening in the market as it relates to your overall performance. What do I mean by that? The best way to describe what I am saying is to look at some examples.

Let's take a look at some fishing expedition examples on the Sea of the Russell eMini. These are waters stocked full of rich bounty. But, along with the rich bounty are hungry dangerous predators. Back in January, stretching through until midway through March of 2011, we found ourselves in very dangerous waters. If you saw an equity curve like this, would you venture into the Sea of Russell?

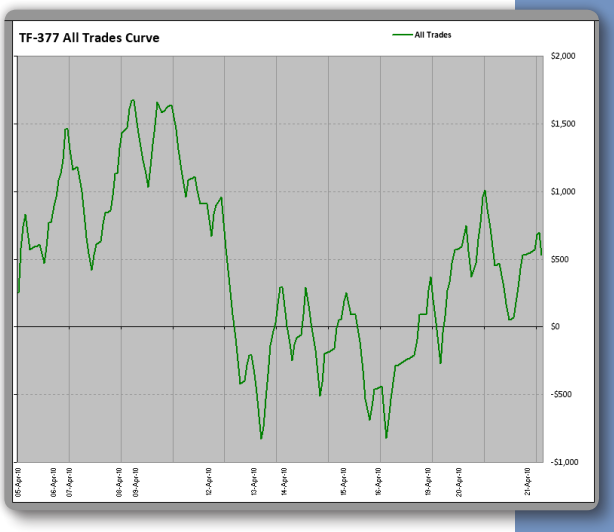
These were very choppy waters of course and boats were getting crashed against the rocks and the weakest adventurers were getting thrown overboard with wanton destruction.



Some traders however, having been through these waters before, were much better equipped to handle these dangers. In fact, they had navigated similar seas back in April of 2010 and the memories of that past journey and the ultimate outcome played a major role in surviving it a second time around.

See the similarity?

There's no substitute for experience. Experienced fishermen (traders) were able to navigate through these waters and those that survived were soon richly rewarded. Both times, the fishermen



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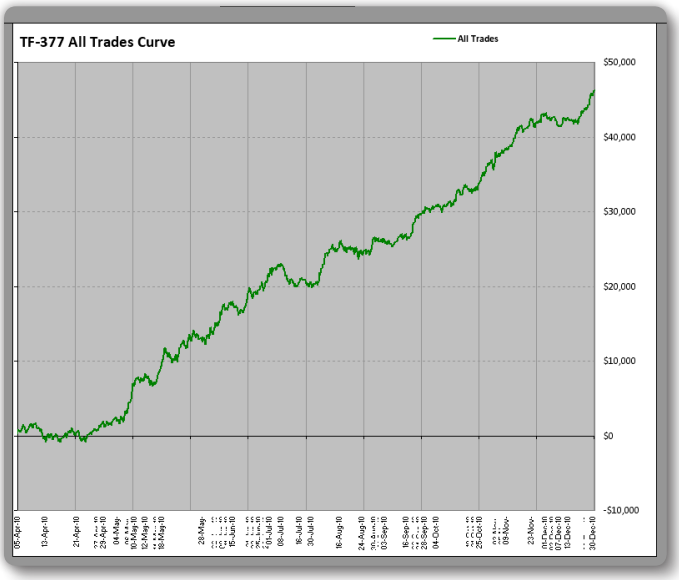
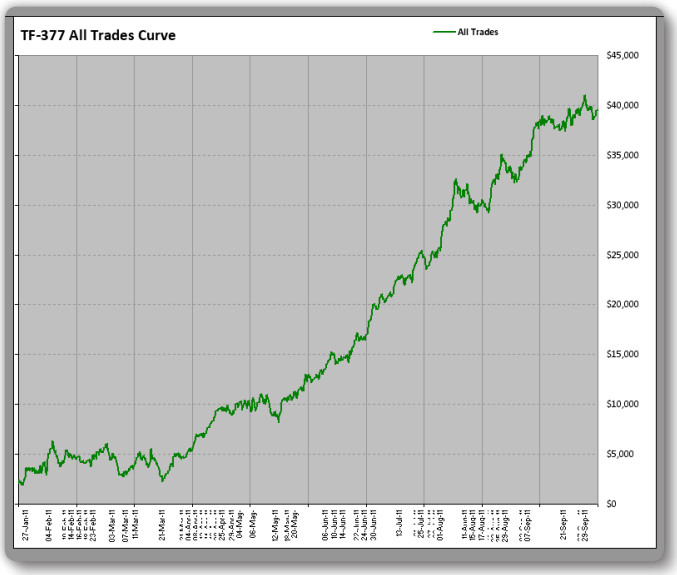
that actually climbed up the mast to get the higher 'bird's eye view' found a way to navigate through the hazards and were able to take full advantage of the huge tsunami sized waves that followed.

After passing through and surviving these same waters in 2010, check out the waves that traders were able to catch.



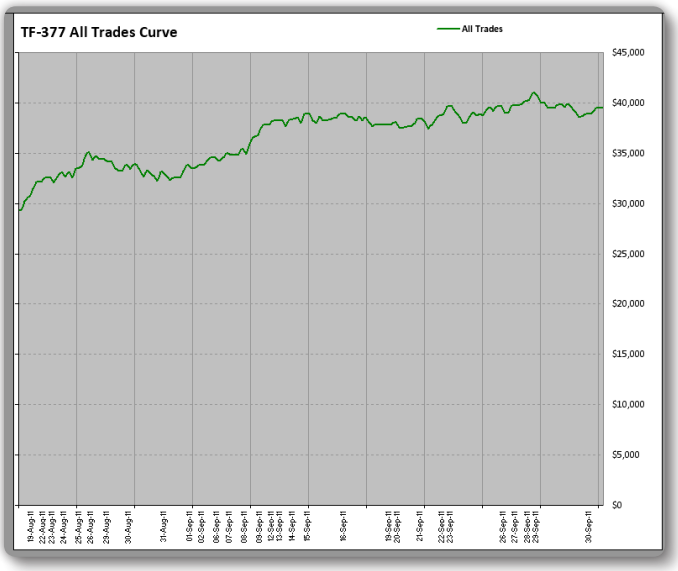
Those who were better equipped and had the broader vision were able to ride the tides as they swelled to higher and higher levels, reaping rich bounty every step of the way.

Then, after hitting the rough waters again in early 2011, (requiring the same broad vision and adequate equipment) Russell eMini Sea Farers rode a new tidal wave to even richer bounty.



Sure, there were some harrowing moments and perilous hazards along the way, especially for the unprepared and inexperienced. But the pattern is clear as day if you could lift yourself to the top of the mast and see beyond the feeding frenzy that occurs in the choppy waters immediately below.

Could we be entering a new hazard zone? We've definitely seen a lot of choppy waves. Check out the last few weeks (as of this writing, Oct 2011).



The last 100 Russell points (fish) have been hard fought. The current has been low and the waters treacherous. But if we look at where we've been and how we have handled similar waters in the past, our odds of surviving this part of the equity cycle and then being richly rewarded for our efforts, yet again, are very high indeed.

No one can ever know the future. Gaining a bigger insight and broader vision will make you a better trader. Your decision-making will be based on the bigger tidal movements in the market and not based on overreacting to choppy waters. You will be able to stay on course and follow your bounty. For sure, along the way, you will hit areas with a low catch and may even take on some water and have to throw some overboard, but if you just continue onward, you will catch your bounty again and ride the crest of your success. Best of all, it will show up in your equity curve as a tsunami of profit heading eastward and ever rising.

CUTTING THE MUSTARD *Troy "TJ" Noonan*

There are some distinct differences between the SST and the SST Simple. One of the obvious and immediate differences is the way the initial stop is determined and placed. As you may or may not know, the SST begins each trade giving the setup a lenient amount of space to develop. As the trade progresses, it seeks to cut risk and ultimately put us into a risk free position. Part of its overall effectiveness is the dynamic method it uses to place the stop far enough away from the setup bar to avoid initial chop and churn. We don't want to get stopped out due to short-term market noise, only to then watch our initial trade theory turn out to be correct, but with us already stopped out and on the sidelines.

The SST Simple is a lot different. It wants to put its stop just on the opposite side of the setup bar. This results in a much tighter stop, which a lot of traders prefer. To compensate, we have slowed down the trigger line, amongst other things. And while it has been an excellent performer on many markets and timeframes, sometimes it is prone to get caught up in the chop and churn that could occur when price range contracts.

What if you could apply a filter that would help you determine whether or not your SSTS trade 'cuts the mustard,' or not? This handy little technique comes to us from one of our members, Mr. Everett Kelly. Everett hit the jackpot several months ago when he won a free version of the SST during one of our promotions. We're very impressed with him, not only because of his unusual good luck, but also because he was astute enough to not squander the SST or devalue it, just because he won it at no charge.

Quite the contrary, in fact, Everett actually took the time to fully learn the SST, following the training and ultimately taking full ownership and making the SST (and SSTS) his own. He was gracious enough to share his experience with our membership during an interview, which you can easily check out for yourself at: http://www.netpicks.com/trading-tips/secrets-from-successful-traders-everett-kelley/

One of the things he discovered, (and as soon as he shared it with me I knew that it was going to be a great idea since we had used a similar technique with excellent success on a prior trade strategy) was the use of a simple filter to help mitigate some positions that might not have as good of odds as other setups. Everett suggested putting a 50 exponential moving average (ema) on the chart, giving it a mustard color and then using it to help filter out some bad setups. He called it, the 'mustard line.'

His idea being that many traders use the 50 ema and that it would identify short-term support and resistance. If the 50 ema came between the entry and the target, it would create an additional hurdle to have to 'fight' through and thus, logically would imply some additional risk on the trade. In other words, the odds might not be quite as much in our favor. When this happens, we can easily stand down and pass on the trade. The trade didn't cut the mustard so, let's take a pass.

Sure we'll miss some winning trades. Nothing is perfect and one has to be very careful that along the quest to try to improve something, you don't wind up making it worse. But if you had to miss out on a winning trade but also could avoid 2 losing trades, for example, that would be worth it, right? This works well on some markets abut perhaps not as well on others. Before using this idea with real money you should definitely test it out for yourself. Do a quick count of wins and losses over a few months and see what you find.

We were talking about it today (Oct 17th) and a member in the traderoom mentioned that he too, was thrilled with the Cutting the Mustard idea. He's been using it on the European Session Crude Oil Tradeplan. Today he was excited to share with us that over the last 100 trades or so, he's been enjoying an 88% win rate and by avoiding the trades that 'didn't cut the mustard,' he has helped his cause in being able to achieve such an amazing result. Congrats on his excellent trading! AND, a big congrats and thanks to Everett Kelley for such a great idea that could have only come about by somebody who rolled up their sleeves and did the necessary foundational work to actually take full 'ownership' and make the SST their own.

CAN IT REALLY PAY OFF TO BE A QUITTER *Mike Rykse*

If you have been around the NetPicks products for any length of time, you are familiar with the term Power of Quitting. It is the idea of getting in, getting out, and getting done. We do this by setting a goal for ourselves each day. For example, on many markets we aim for 2 wins and a positive result and then we are done. This could take 10 minutes or it could take 4 hours. In this case we would be looking for 2 winners and a positive result. This could mean we start out with 1 winner followed by a loser and then a second winner. Or it could mean we get 2 wins right out of the starting gate. As long as we have 2 wins and we are positive then we are done for the day. It all depends on what the markets are doing that day.

In working with hundreds of traders over the years the topic of Power of Quitting is one that comes up most frequently. It's difficult for traders to get their minds around the idea of quitting after a few trades. A common response that I get is, if your system were proven to produce a positive edge, then why wouldn't you want to trade it all day? You could make even more money. There are many problems with this statement.

First, more time in front of the computer can lead to mistakes being made. If you can't execute your system and trade plan flawlessly then how can you take advantage of the system's edge? It's much better to be focused for a defined block of time each day instead of spending hours on end staring at the charts. We all know how stressful trading can be. Taking steps to limit this stress will lead to you becoming a better trader. Power of Quitting does just that.

Second, there are costs that add up very quickly when trading all day. Even though commissions are very inexpensive, these days they can add up very quickly if you are trading all day long. This is true of any market you trade including forex. I know a common marketing practice is to advertise forex as a commission free market but keep in mind you are paying the spread on every buy order that you place. Keep track of your trade costs throughout the year and you will be able to see how important it is to limit your trades as much as possible.

Last but certainly not least is the profitability of Power of Quitting. When first introduced to Power of Quitting in my own trading I was skeptical. I was worried that I was leaving profits on the table. However, as I dove in and back tested many different markets I was amazed to see that in just about every case my results were improved by using a Power of Quitting approach. What is the point of trading all day when you can maximize your profits in just a few trades each day? All you are going to end up doing in the long run is racking up commissions.

So how do you get started with this approach? It is very important to test each market that you are interested in. This is important to see what Power of Quitting approach is best. You really need to record at least 100 trades in order to see reliable patterns developing. Analyze your data set to see the difference in your results by taking just a few trades each day compared to taking every trade all day long. In most cases you will find the 2 wins and positive approach to work best. However, you might find through testing that stopping after 1 win is best. Let your test results determine which approach is best. The final option is to trade a block of time. You might find through your testing that the first 30 minutes of the

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trading session produce the best results. In that case trade the first 30 minutes and then shut things down.

While it is tempting to trade all day long and make thousands of dollars each day, it is just not realistic to do so. You will be much better off to limit your trading with a Power of Quitting approach. Book your profits and then move on with your day. Go play golf, go spend time with your family, or just relax by the pool. Whatever it is that you do it will sure beat spending hours staring at your charts all day. This will limit your costs, your stress, and as you will see it will lead to a better bottom line.

ATR: KEEP EXPECTATIONS IN REALITY *Shane Daly*

We have seen some very crazy moves in the currency markets. It does not take a genius to realize that volatility is up.

The ADR (average daily range) has really increased in many of the popular currency pairs. This can be a major drawback especially for the inexperienced trader. They see these big sweeping moves and are rubbing their hands together thinking of "letting profits run" and taking the huge chunk of the move. With zero knowledge of the range a particular pair, traders are shocked when the move fizzles. Now, there are many reasons for this. Not to get too involved in this subject but it could be something as "simple" as a trader taking a long trade right into a resistance level. This article is going to focus on something a little easier.

> **" Traders, as opposed to others, seem to have some absurd expectations. 100% returns. 100% wins. "**

One thing great about the London trading session is that it can be considered as the "start" of the trading day. This is generally where the big moves truly happen. By the time the U.S. session starts, it is very possible that the bulk of the average range has been completed. When this happens, several things can occur.

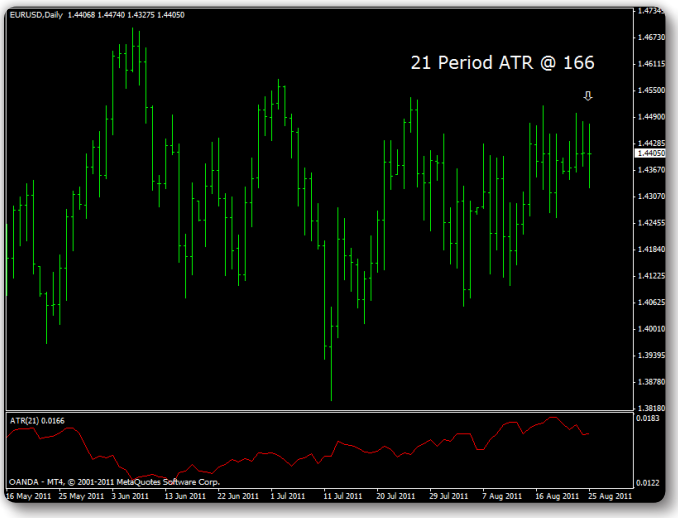
1. Markets simply range for the remainder of the day
2. Profit taking occurs or fading of the dominant trend of the day, occurs

Of course, nothing is written in stone. There is no reason, given the right ingredients, that the markets can exceed the average by a sizeable amount.

Expectations. We all have them. Traders, as opposed to others, seem to have some absurd expectations. 100% returns. 100% wins. Retire in Bora Bora trading their $5k account. Hey, I am all for dreams because without them, life can be pretty drab. The problem is with trading, absurd expectations can lead to a blown out account.

To help keep your expectations in check during your trading day (this applies to trading week, month…), let's give ourselves a rule: Check how far the currency pair has travelled by the time you get to your computer.

How do we do that?



21 period ATR applied to chart. Average range is observed (166 pips)

So now I know that this pair averages 166 pips over the last 21 trading days. If you come into your trading day and your favorite pair has travelled a distance close to the average, would your expectation of a 80 pip move be realistic? Probably not. Do you hang up the charts? You could or you could do the same thing with another pair to see if the average range is close. Many times, you may find one pair is near the average and another has only travelled 40%.

For those that trade the "hub" of Forex activity, you certainly can use a percentage of the range for a target.

Is this flawless? Nothing in trading is. It is designed to keep your expectations in check…keep them real. From the many emails I have received from traders, keeping expectations rooted in reality is a problem. This certainly can help.

ARE WE TRENDING YET? *Will Feibel*

The last few articles in this series have focused on identifying chop in the market. We started out with an overview, listing several technical analysis indicators that can help in the process, next we focused on the Bollinger Band Squeeze to identify consolidations, and finally we looked at a noise filter to highlight noise, or choppy price action, in the market. In this article we'll take a look at the ADX (Average Directional Index).

What Is It?

The ADX was developed by Welles Wilder to identify periods of trending price action. The calculations for the indicator are based on changes in consecutive bar highs (+DI) and consecutive lows (-DI). DI stands for Directional Indicator. These values are combined and smoothed to yield the ADX. The exact calculations are too complex for this article, but you can find the details on line. As originally designed by Wilder, the ADX, +DI and –DI were the basis for a full system. All that had to be added was a stop management strategy. The ADX itself however is often used as a standalone filter for trend following systems. Traditionally an ADX value above 20 indicates a trending market. The exact threshold can vary, and some use 21 or 25 instead. Any time that the ADX is above this value we use a trend following strategy, when it's below we use a fading strategy or stand aside. Note that the ADX itself does not indicate the direction of the trend, it simply tells us that the market is trending, either up or down. What we can say though is that as long as the ADX is rising, the trendiness in the market is increasing, and as the ADX drops the trend is weakening.

What Do We Do With It?

Figure 1 shows the ADX at its simplest. This uses the default smoothing period of 14. Note the highlighted areas where ADX is above 20. You can see that it signals a trend a bit after the price move starts, and also marks the end of the trend only after the market starts to chop. This is because of the smoothing used to create the indicator. Like all the other trend/chop indicators we've looked at, the ADX lags price. Because of this you would not use the ADX to set up your trade, but you can definitely use it to filter your setups. In this figure you would take signals from your trend following system during the highlighted periods, whether they are long or short signals, and stand aside otherwise.

Figure 1

A variation of the standard approach uses a separate threshold to indicate the end of the strongly trending period. Traditionally in a strong trend we would stop taking setups when the ADX falls below 40. If the ADX never rises above 40, then you wait until it falls back below 20. Wilder himself uses 25 in his ADX/+DI/-DI strategy. Figure 2 shows this approach, the highlighted area ending once ADX falls below 40. Note that this approach has us missing the rest of the nice move up, but it also avoids the chop at tail end. It does however capture the cleanest portion of the move.

Figure 2

Since a rising ADX indicates a strengthening trend, and a falling ADX a weakening trend, we can reformulate the filter to focus only on the periods where the indicator is rising. A simple technique to use is to add a moving average to the ADX. Figure 3 shows an example using a nine period average of the ADX. Using this approach we would take setups from our trend following system only when the ADX (blue line) is above its moving average (red line). Those areas are highlighted in the chart. Compared to the prior two approaches, this gets us into the trend sooner and has us standing aside sooner. Because the trend can still continue

even though it is weakening we will miss out on a portion of the price move however. Furthermore it's possible to get situations like the middle highlight just because this approach gives more frequent trending/not trending transitions than the earlier ones. You can also plot the difference between the ADX and the average as a histogram for a nice clean look. A positive histogram says you can take setups, a negative one says stand aside.

Figure 3

Remember that the ADX should be used as a filter, not as its own setup. Use it in combination with a trend following system and only take setups when you have ADX confirmation using any of the approaches discussed. A good trend following system should also include a sound stop management strategy, don't wait for the ADX to tell you to get out of the trade, it will be too late.

What's Next?

We're getting close to the end of this series on trending and chop indicators. With what we've covered so far you have a set of tools that you can use in combination with your favorite system. Place them all on your chart and do a back test to see which works best for that instrument and time frame. Some of tools may try to accomplish the same thing, for example the Bollinger Band Squeeze and the ADX both have the goal of identifying trending vs. consolidating periods. Other tools may be more complementary, such as the noise filter which attempts to directly measure choppy price action. None of them are the holy grail of trading, and all of them will keep you out of some profitable setups, but they will help you restrict your trading to the most favorable market conditions. So load up your charts and get to work.

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TIPS TO LIMIT DISTRACTIONS WHILE TRADING

Mark Soberman

In many ways, trading is an ideal occupation. You are your own boss, and not limited in your earning potential by an hourly wage rate. One of the main attractions for many people is the fact that the Internet makes it possible to do it from home, and the investment in terms of computer, screens, software and connections is reasonable, given the prospect of large profits.

However, successful trading is a mental challenge, perhaps more than any other factor. Although fear and greed are cited as the overriding psychological difficulties, and must be dealt with, working from home can also be a challenge, as distractions can easily break your concentration, leading to failure.

To deal with the distractions, you must approach your home office in a businesslike way, setting aside a special place if not a separate room for your work. If possible, the room should have natural light or a window, as this creates a psychologically positive atmosphere; but the light should not interfere with your display, or give you a view of the neighborhood that could capture your interest.

Make sure that your office is quiet. It can help to post hours on the door, telling other occupants of the house that you should not be interrupted. Make arrangements for kids and dogs to be otherwise engaged, and ask your spouse to restrict noisy activity, such as vacuuming or electric power tools.

If you are day trading, then you might want to install a television and leave it tuned to CNBC. News can be a valuable tool, and should you decide to monitor the news via TV, try not to switch channels to check on the score in the Mets game, or watch your favorite soap. To avoid this, most TV sets can be restricted via the menus in the channels that they view. While this does not stop you overriding the restriction, it will make you think twice before changing channels.

You will probably have a phone in your office. Many phones have the facility to turn off the ringer, and you should let calls go to voicemail while you are working. You have to explain to friends that you can't chat during market hours, and then stick by this principle without exception so that they learn that you mean it.

Another potential distraction is having other things cluttering your desk. As far as you can, keep other paperwork in a different place, and separate the time for paying bills from your trading time. All you need on your desk is your computer with additional screens if you have them, and your trading log. Your trading log will give you quick reference to stop loss positions and trades to watch, and should have all you need to implement your strategies.

Finally, try not to leave any volatile positions open if you need to go to the restroom. Even if you think that you will not be long, interruptions and distractions can happen when you are out of the office, and by the time you get back you may be sitting on an unintended loss.