Escalator to Pips
Pipping Your Way to The Top

Presented April 4, 2007
To the reader's of Forex Factory

May all your trades be successful ones

If you have been following my journal entries in Forex Factory, you will notice that I have been making extremely short term trades to capture small pips. This I have been doing to demonstrate the use of stochastics over multiple time frames. I also wanted to demonstrate that you can make low gain pip trades and make a consistent income from it.

Now, I will show you what I call the "escalator to pips". From this time forward this is the more often method I will be using to trade in my journal. I am providing you samples of charts to refer to so that you may understand what dictates my decision making for a trade. In my journal I will be trading live and invite everyone to discuss trades and ask questions, or provide insight of their own.

Escalator to Pips Methodology

I use this only on GBPJPY however I am sure it can be used on any pair. One pair is enough for me to concentrate on and earn pips from.
I set up 4 charts at 15 minutes (15M), 30 minutes (30M), one hour (1H) and 4 hours (4H). I use and only need one single indicator, the stochastic slow set at 5,3,3.

Our trades are always initiated by a simple series of events that happens over multiple time frame stochastics. If you need an explanation of stochastics you will not find it here, please look on the Internet.

Entry Rules
1. Ignore the %K, %D cross.
2. Always wait for the 4H chart to lead our entry.
3. Long trades are entered when all 4 time frame stochastics are moving upwards and the solid lines are all above or at 20.
4. Short trades are entered when all 4 time frame stochastics are moving downwards and the solid lines are all below or at 80.

These four rules are our foundation for entering a trade. I wish it was this simple for every trade entry, and most of the time it is. However, there are always some variances to watch for and these are explained in the following charts.

Exit Rules (choose any of the below)
1. Exit at a pre-determined pip amount
2. Exit when you see a reversal in one or more time frames
3. Exit when the 15M hits the line (80 long; 20 short)
4. Exit when any of the other time frames hits the line (80 long; 20 short)
5. NEVER use the 4H chart 80 or 20 line to exit.

By looking at the exit rules you can see why I call this the escalator to pips. As we enter a trade we will ride the 15M, then the 30M and finally the 1H stochastic chart to either the 80 line (long) or 20 line (short).

Stops

I think I could actually write a book on stops. In fact this is one of the hardest sections to write and keep short. So, I am just going to tell you how I use stops and leave it at that.

Stops are used to either protect my account or my profits. I never use a stop to stop a bad trade. The stochastics stop my trade, not the stop. That means I am in full control of my trade and it is based on the same exact method I use to make pips. I give my trade lots of room…usually 70-100 pips away from price. My stop is going to get hit if there is something abnormal happening in the world or the market, not because the stochastics are wrong.

You can never lose taking profitable pips. You only lose when you lose a pip profit. Always move your stop to protect your profits. Never cry over lost pips if you made at least 1 pip. You'll have another trade to make more pips, but how many pip losses can you survive?

The more margin you have the less risk you'll be at for any single trade. $500 mini account traders carry lots of risk every trade…you have to accept this and have your next $500 ready when something bad happens. If you are trading to protect $500, you are going to have an extremely tough time making pips in Forex because you'll simply set too low a stop trying to protect too low a margin. I'm not saying you need to lose your $500 on a single trade. What I am saying is don't set your stops like you only have $500 to trade with…even if that is all you have.

If your in doubt about my stop theory. Sit and watch my trades in my journal and watch how often I hit my stops or how much I lose from stops. Then look at how much I lose. Then you will understand what I am writing about and you will have more confidence in what I suggest.

Charts

All charts are only stochastic indicators from GBPJPY. All times are GMT. All charts have stochastics from top to bottom of 15M, 30M, 1H and 4H. Vertical dashed line in each chart identifies a significant time as discussed in each chart. Dashed horizontal lines at the top and bottom of each chart identify the 80 (top) and 20 (bottom) lines.

I have purposely left the price out of each chart to show you that we do not need the price chart to know where our trade is (although knowing how stochastics and price move together is extremely beneficial). We really only need price to know how many pips we are making, or how close we are to our stop.

Chart 1a – March 14, 2007 at 12:00 Long Entry

Every long trade you enter should resemble this chart. In this sequence, the 15M is higher than we would like and the 4H has just cleared the 20 line which is not ideal.

Notice every time frame stochastic for this long trade is above 20.

Notice too, that we did not enter this trade until the 4H crossed the 20 line. There is a huge misleading idea in trading that long term charts identify the trend. This is false. Long term charts tell us only what the short term charts have been doing. There is no guarantee because a long term chart is just starting an up trend it will continue to go up. However, we do know if our short term charts reverses, our long term chart will be affected.

You might think I'm splitting hairs on a definition here, but I am not. I am trying to dispel a false train of thought that you probably have. I don't know how many times people state that "the 15M is doing such and such but it is too short a time frame to matter". All I can say is "open your eyes, the 15M chart is telling you something".

Statistically we know that stochastics will behave a certain way. I know in this situation we have about a 99% chance that we will see continued up ward movement in price based on all four time frames. The only thing I do not know is how far up the price will move. What will dictate the limit of the move will be the 15M, the 30M and the 1H charts. The higher the time frame I ride on the "escalator" the greater my risk is of a price move in the opposite direction. However the higher up I go the more pips I have already gained.

Getting back to my explanation of trends and time frames. Each movement in a lower time frame will affect the time frames above. It is the degree that a lower time frame affects a larger time frame that will indicate what our price will do. Why? Because lower time frame movements build longer time frame trends.

You have to remember this to trade stochastics over multiple time frames successfully.

Chart 1b – March 14, 2007 at 16:00 Exit the Trade

All our exits appear at the same time; 16:00 however each will give us a different exit price:
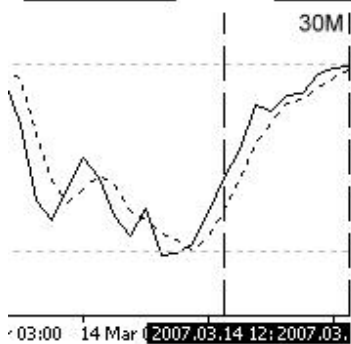
Entry was at 223.50 Long
      Exit on 15M is at 224.14   +64 pips
   Exit on 30M is at 224.07   +57 pips
      Exit on 1H is at 224.81   +131 pips

The discrepancy here is exiting at highs, lows or closes during each time frame. However, it does not matter, all gained pips.

Look at the charts and you can see the 15M chart going for a wild ride up. If we pay attention to our other time frames, especially the 30M as it is closest to the 15M, we can see things are fairly stable.

Can you see how the 15M builds the 30M, the 30M build the 1H chart?
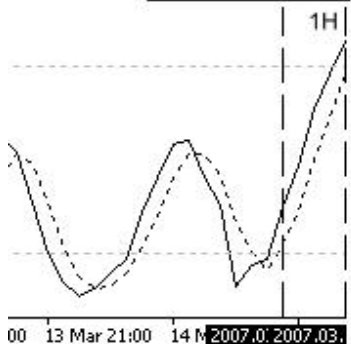
I can tell the price is going to continue going up in the 15M chart because the downward moves on the 30M chart and even the 1H chart are almost non-existent. As wild as the 15M chart is, it is building an upward trend for the longer time frame charts
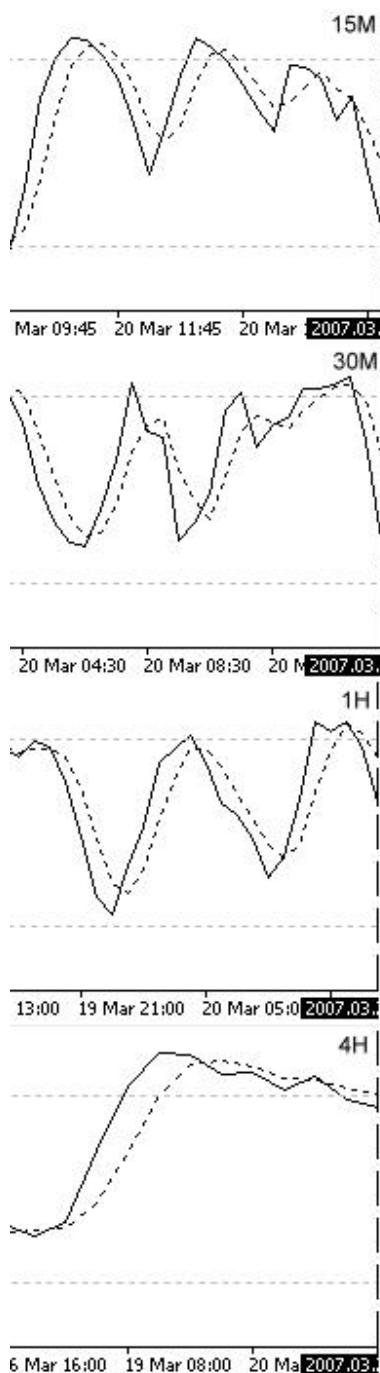
The 4H chart during any trade is merely a reference point to our direction and what the short terms are building.
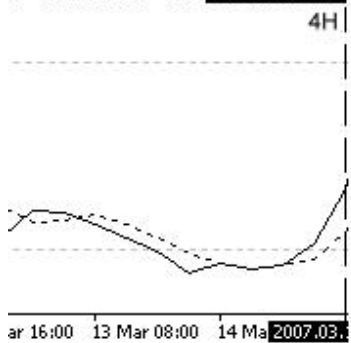
I can show you a dozen more long trades and they will all look like this. Shorts are just the opposite.

So how about something tricky and bad. Let's go on to the next charts.

<u>Chart 2a – March 20, 2007 at 16:00 A Bad Trade Short?</u>

As you can see by this chart our 4H has just crossed the 80 on the way down on March 20, 2007 at 16:00.

Here again we would much rather have the 15M and 30M much higher up the stochastic scale than they are to jump into a trade. In fact you would have to consider this a pretty risky trade because of where the 15M and 30M are together.

I will tell you that the 4H didn't go down much further in this trade when it was entered here. This is about as bad as the trades go under "normal" conditions.

It is not an ideal trading position so already we are at risk, There is a possibility that we could have enjoyed a better trade since we could have entered the trade before the 4H closed it's candle. I don't like to trade that way unless the movement is clear or it is late in the candle.
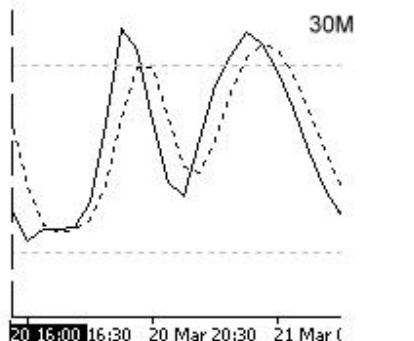
However, I went with the trade here so let us see what happened that turned this into a bad trade.

Chart 2b – March 20, 2007 at 16:00 A Bad Trade Short?
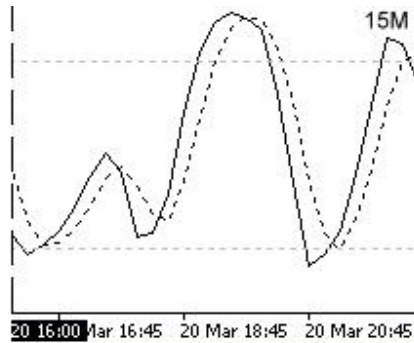
The 15M and 30M both turned up rather quickly. Here's what happened to price:

Entered short at 229.95
15M hit 20 at 229.38   +57 pips
30M did not hit 20
1H did not hit 20

Technically if you exited at 15M you still gained 57 pips and hopefully you protected some of those pips when you went to 30M.

When the 15M and 30M both turned up you should be exiting but definitely when the 1H turned up and closed.

So what would you have lost if this happened and you waited for the 1H to turn up and close?
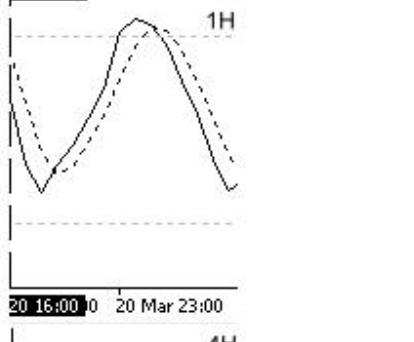
You actually would have gained about 4 pips and lost that to your spread.

Here is a great example how the small time frames build the 4H trend and why my stops are rarely ever hit for a loss. During our trade the 4H is still moving down and the net effect of the upward movement of the short term charts was small. Small enough anyways to allow us to gain some pips.
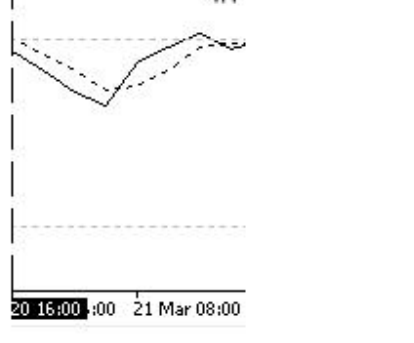
The short term stochastics told us what was happening and started to move up. It was time for us to bail out when two moved against us and one did not hit the 20 line. When 3 moved against us, we were in trouble. At worst we would have hit our profit stop.

The 4H didn't lead us astray, it was just a weak down turn and we entered this trade knowing there was some risk attached. The short term stochastics showed us they were starting to build an up trend and the 4H was just slow in reacting…which it always is.

### Chart 3a – March 6, 2007 at 2:00 The Optimum Long Entry
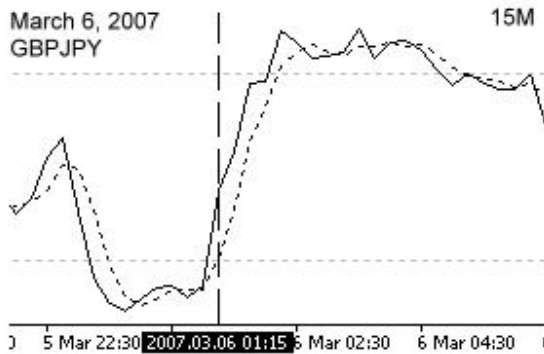
This chart is a good example of the what an optimum entry point looks like for a long trade.

Notice first that the 4H actually led the entry to the trade and broke the 20 line first. This is the best possible situation as we know that the lower time frames are building a strong up trend.
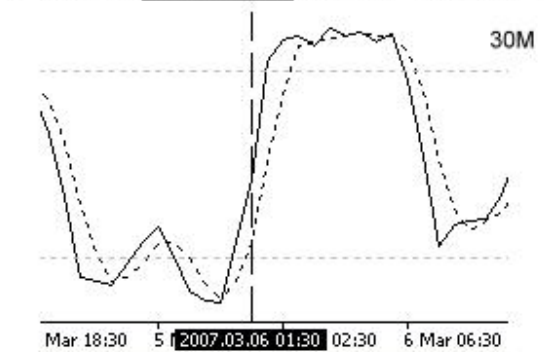
The rest of the time frames have nice parallel lines, they are all moving at the same slope and all have their stochastic lines about the same distance apart. In other words the stochastics are almost identical on each chart.

Just for the record, this trade would have netted you anywhere from 50-200 pips!
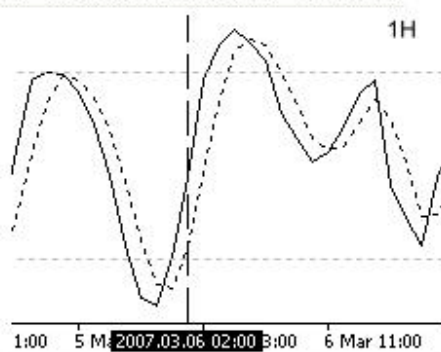
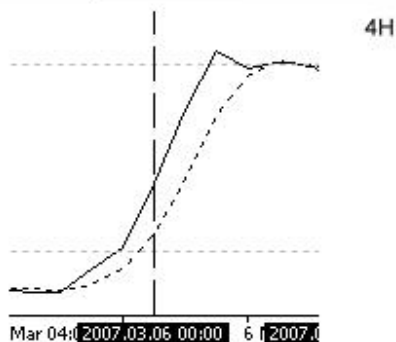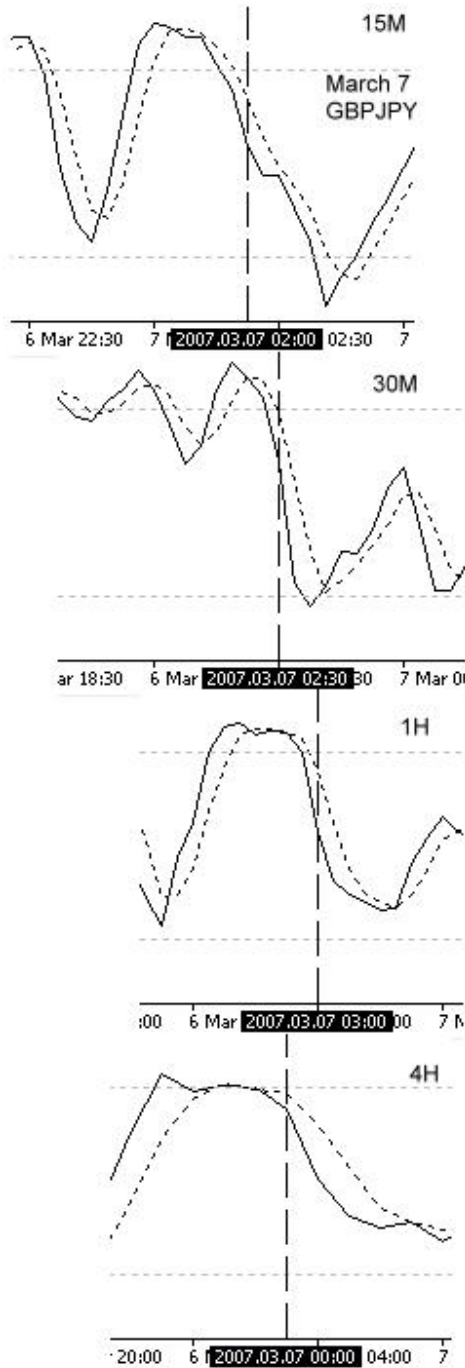Take this chart and post it on your wall as a reference.

Chart 3b – March 7, 2007 at 2:30 The Optimum Short Entry

This is a chart of the optimum short entry setup.

This is an example of cheating a little and entering when the 1H is halfway through the candle. Trading live is much different than looking at historic charts. During this time frame the movement was quite simple to see.

Again the 4H leads the trade entry and the downward stochastics of the other time frames are making identical moves.

Another easy trade and the pips gain anywhere from 90-200 pips.

<u>Trading Forward Live</u>

I left the price out of my charts in this document so that you would concentrate on the stochastics. As you trade more and more using this stochastics you will learn how price reacts to the stochastics. This is a valuable tool and becomes second nature to you without even having to think about it.

Let the stochastics rule your decisions not the price. The price will move to make you think you are wrong. The price movements are used to manipulate your decisions. The stochastics tell the naked truth.

Practice with stochastics. Cover the price on your monitor and watch the stochastics move over multiple time frames and write down what you think the price is doing and will do. You will be amazed in a short time how well you can interpret what is happening in the market and how you can "predict" moves long before they happen as your brain absorbs the patterns.

Your greatest enemy will be human error and that feeling that you might miss a great trade if you don't act now. If you are feeling that anxiety, take a step back and think it out. Am I too early? Too late? Does something not feel right? As you trade stochastics learn to listen to your gut. It is actually your brain saying "this pattern is not right" or "this pattern is right".

Look at the charts I included here. This is about as close to fail-safe trading as you will find. If you get into a losing slump go back and just trade the optimum setups until you feel like a winner again.

Always, it is never about how many pips you make, but what the pips are worth that counts!