RSI PRO Forex Trading System

Trading Examples Vol. 1

Paul Dean

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RSI PRO FOREX TRADING SYSTEM
Trading Examples

The purpose this book is simply to help traders using the RSI PRO Forex Trading System to improve by seeing different currency trades and expanding their vision and understanding.

I don't plan to write at length here as the important information is in what follows. There are 40 trading exercises which were actual trades that were taken from February 2009 up until July 2010. At the end of the this book are 10 Trading Exercises that will lead your through some of the basic concepts that should come to mind whenever you place a trade. Each Trading Exercise has an answer and they are the type of exercises that you can continue on your own.

I learned a great deal myself going over each of these trades and writing the step-by-step comments and explanations. I think that if you use this as a resources, referring to it often it will help you become a better Forex trader.

The most important thing that a Forex trader can develop is his or her decision-making process. Many times we enter trades and realize that we failed to think about something. By spending time understanding how to think we become more aware of our surroundings and we begin to perform at a higher level.

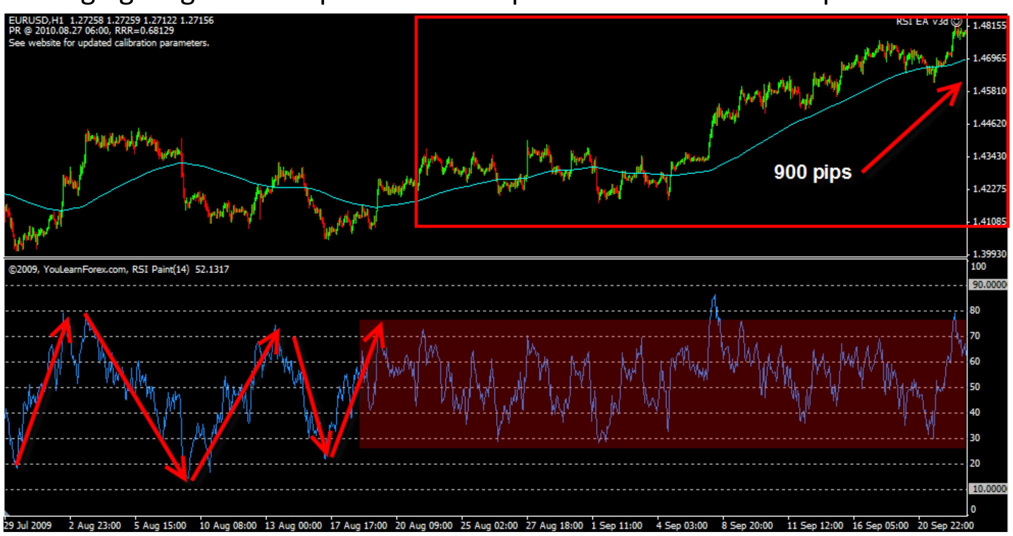
Each Trade Example is numbered and titled. You may start from the beginning or scroll through the pages stopping where ever you like to read about the thinking behind a trade.

I hope you enjoy the book and recommend the RSI PRO Forex Trading System to your friends.

Paul

Example 1 – Range Shift and Context

This is an example of a **Range Shift**. A shift in the range of RSI. Depending on the time frame and currency pair, RSI will range between a higher set of number on uptrends(example: 40 to 80 RSI) and a lower set of numbers on downtrends (example: 60 to 20). A **Range Shift** is when you see RSI move from a low RSI as shown here with the first red arrow at 20 RSI and then move steadily up to 80, as shown here, and then remain in the upper range. Although prices have moved sideways after the **Range Shift** in this example, the RSI has stayed in its range giving us the expectation that prices would continue up. This is not a signal to enter however.



On the lower picture we see that there were 5 **Range Shifts** which could be considered consolidation or oscillation. Notice however, as RSI settled into a range of mostly 40 to 80 with some drops to 30. The box outlines where after the last shift RSI stabilized and then prices began to move up, eventually 900 pips. As a trader you should continually look at RSI zoomed out so that you can see things in context.

Example 2 – Reading RSI Signals and Momentum

This trade begins at the yellow circle. Prices move up steadily and several RSI Negative Reversals appear. These are **Momentum Type 1** (M1) type signals because prices have been moving up and RSI has been above 40 RSI. Typically divergences are M1 type signals but in uptrends Negative Reversals can also fall into that category.

M1 Type momentum signals show up because **Momentum Type 3** (M3) is moving up with more force than price. Once RSI gets to 80 RSI the signal has more weight but even then consideration must be given to the current trading conditions and market direction i.e. Main Channel of the trend. Any of the Negative Reversal or Divergence signals that appeared in this trade could have been exit points or places where position size could be reduced or added to. This will depend on the traders trading style.

The red circle shows a Positive Reversal at a RSI above 40. This would be a good re-entry if the trade had been completely exited depending on the time of day and the trading style of the trader. As prices are sliding sideways after the two PR signals this is probably an indication that the trading was at the end of the New York trading session.

Example 3 - How RSI Shifts Range; a Stair Step

Step 1: RSI hits a low at 20 RSI, this could be a buy but at this point it is uncertain.

Step 2: Price has moved slightly but as the previous signal was a Positive Divergence we would expect a Negative Reversal to follow or another Positive Divergence. A 2 period PD appears but RSI creates a valley at around 35 RSI.

Step 3: We get two NRs at 50 and then 55. With the previous trend being down we would enter here. We enter and price drops but RSI makes a valley at 40 RSI. We would have liked to see if fall lower. Step 1, 2 and 3 are going up, not going down. So we exit with a small gain.

Step 4 Price and RSI move up, RSI to 75. We are more cautious here as price momentum up is stronger than price momentum down.

Step 5: Again RSI is supported and stopped at 40 RSI. RSI rises to 75 and another NR forms. We get a sideways movement and several NDs that drive the RSI to above 40 again with a PR above 40 RSI. This is an excellent entry to the upside.

Example 4 - Range Shift

This chart looks complicated but go through it carefully (several times if necessary) because it can give you a strong indication of what is to come when it happens.

Anytime price is trending down the trader should be watching for **Range Shifts** up, and when price is trending up the trader should look for **Range Shifts** down. The shorter the time frame traded the more often this will happen.

Here the thin red arrow shows that price was heading down severely. Now look at the two yellow circles. The earliest is below RSI 20. That may or may not indicate that price is headed up but with the severity of the drop in prices we might not have thought that to be true. This is where patience is important.

Certainly you could have entered at the two PRs in the yellow circle however, you might have decided to wait until you were more certain and the range was established. Notice the second yellow circle goes all the way to 80 RSI. A continued downtrend would have slowed near 50 RSI. This is a **Range Shift** possibility at this point.

What confirms it? The RSI drop after the circle only drops slightly below 40 RSI and then maintains that level into the area of the yellow box and it stays above 40 RSI with PRs from April until November with plenty of exits and re-entry areas. Prices continued up until the last week of December.

As price moved up we would have looked for a **Range Shift** down, until then we were looking for uptrending trades.

Example 5 - Using RSI for Short-Term or Scalping and Minor Drawdowns

There are several key things to point out here.

1. RSI PRO can be used to trade any time frame. This is the EURUSD M5 (5 minute)
2. As can be seen the market is moving up and down with respect to the signals i.e. Positive and Negative Reversals.
3. Previous to the last down move price moved up with at a Positive Reversal with almost no **drawdown** and nowhere near the standard **drawdown** location.
4. The green line on price is drawn for two reasons:
    a. The first is that price paused here which could be attributed to the price where the previous low had been or there were blocks of trades that needed to be unloaded before prices could continue their fall.
    b. A new PR was formed at that point and it would have been a good place to exit and take partial profit.
5. Because of the short time frame it is quite likely that price would have reacted to the upswing of the PR. Some of that might have been left to the overall direction of the market at the time, the time of day and the condition of the economy.

Example 6 - Tight Drawdown

1. This is a place and hold trade. These trades hold their position for longer then perhaps anticipated yet the trader has a high level of certainty that the trade is going to move in the direction of the signal. Why?
    a. A Negative Divergence signals a Positive Reversal at a fairly high level, 30 RSI.
    b. The Main Channel Trend is and has been up.
2. **Tight drawdown** means that position size can be increased.
3. The trade is placed at the Positive Reversal Point 1. Notice the two horizontal lines (yellow). The top yellow line is where the entry would have been after the confirmation. The second is the stop loss area based on a 10% drawdown which is based on the location of the Positive Reversal's ABC point.
4. Point 2 and 3 with arrows are showing where price was when RSI created a strong V on RSI (red circle). Even though price had stayed on the horizontal, RSI was moving up. These are all positive signs that the trade was going to move up.
5. Point 4 is where price took the largest jump (175 pip trade)

Example 7 – Short-Term Trade M5 Below the Last Low

The set up is the red dashed line indicating the last low on price. Price moves along that line until the Positive Reversal that occurs after a significant penetration of the line (red arrow).

The confirming bar on the Positive Reversal was weak in comparison to the Valley Bar and there would be some question as to whether the penetration was going to take prices lower.

If the trader entered at the signal, the stop could be anywhere from the spread plus 1 to 10 as our expectation would be that price would at least get back to the support level and perhaps penetrate it. However, in this kind of trade two other considerations could be taken.

1. Take a tight stop at the lowest point of the Confirmation or Valley bar.
2. Wait until prices breaks through the Last Low line and then enter.

We could exit at either of the Negative Reversals or wait for RSI to break a channel trend line (green dashed line) drawn from the signal through the first "V" formation on RSI. As long as RSI was climbing we are in the trade. When RSI falls through the channel trend line we exit. *This is the case for short term trades but not necessarily true for longer term trades.*

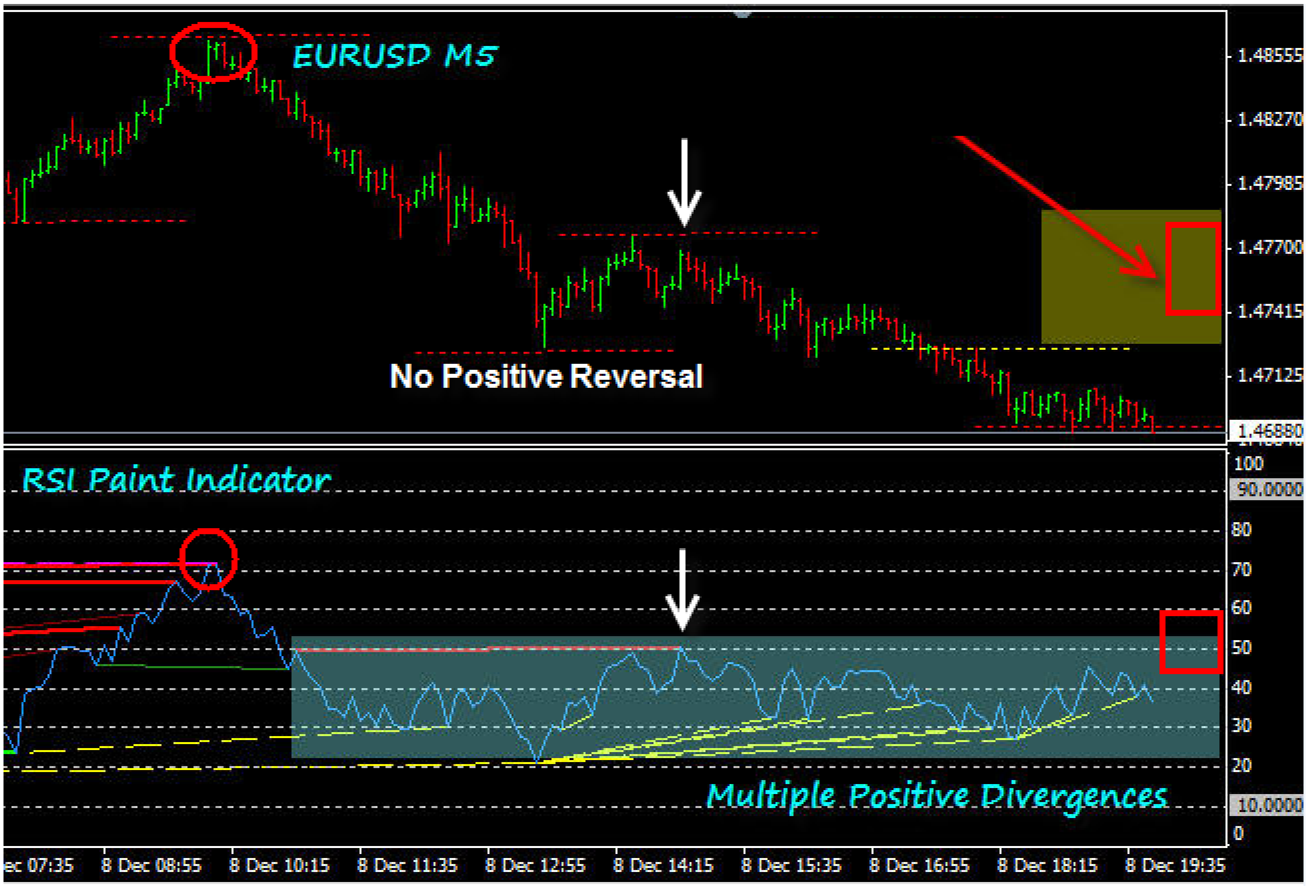
Example 8 – Short term M5 trade Negative Reversal

This trade sets a marker for the last high (red resistance line). The objective is to see if price returns to that line and to see if we get a Negative Reversal signal.

There is a Negative Reversal before resistance is hit (see the white arrow on RSI). If we had taken that we would have had a much larger draw down. A signal at resistance didn't occur but it did occur after price penetrated the resistance.

The risk was the spread plus 1 which was not needed and price dropped 100 pips.

Example 9 – Looking Ahead



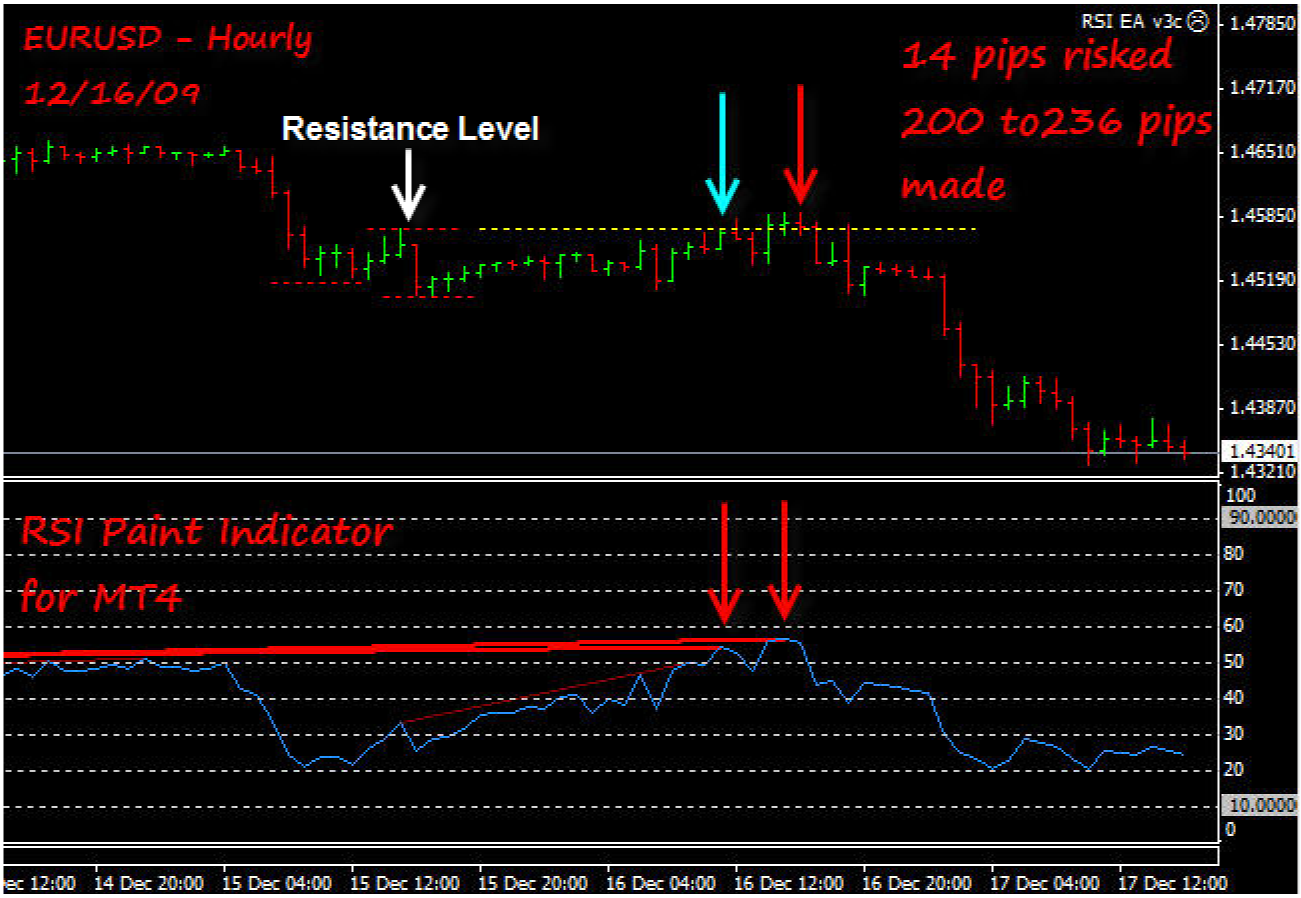
Can you predict what is coming next? There are clues that the 4 RSI Trading Signals will give you in reading the charts.

This M5 EURUSD chart shows that a Negative Divergence signaled price to go downward at the red circle which happened. At the lowest point where we might have expected to get a Positive Reversal we instead got a Positive Divergence(s). This would then have us looking for a Negative Reversal as we know that this is what typically follows Positive Divergence.

The white arrows show that the Negative Signal came and produced a nice trade. Price above is currently moving sideways under the support of many Positive Divergences.

Where will the next trade come? We don't know for sure but the red boxes are high probability locations for a new Negative Reversal signal.

Example 10 - Negative Reversal with Tight Stop



This trade is based on where resistance and support **had** been at the white arrow. The trade involved locating these two areas and then waiting for a signal at resistance; a Negative Reversal. One other key factor was not taking the earlier signals before economic news and before the NY Stock Exchange had opened. Once we had the signal at the time we wanted we placed the trade with a 14 pip drawdown so that we could maximize our position size. As can be seen the trade made very good profits and in a short time period.

Example 11 – Trading off a Resistance Level for a Whole Week

This shows how simply trading off a resistance level in a period of consolidation made very good profits. The Positive Reversals could also have been traded and although not with the same results through the same period would have added to profits. The trader would have traded from signal to signal in this case rather than waiting for prices to come back to or through the resistance level.

Example 12 – Trading Every Signal can Produce Profits

Here is an example of trading every signal. This works best when there is consolidation. Most of these trades took off immediately or they stopped out. This is about one week of trading on the hourly chart.

Example 13 – Trading in Hourly Consolidation

This is an example of trading at resistance and support on an hourly chart. The color and shapes on Price correlate to the color and shapes on RSI. The yellow circle is one trade where you might have had trouble even if you knew you should wait until it reached resistance. You could have entered with a large stop, or waited for the resistance along the top orange line. There was a large price move that went through that line that might have caused most of us to take a loss. Overall this would have been 5 solid trades.

Example 14 – Trading a Main Channel

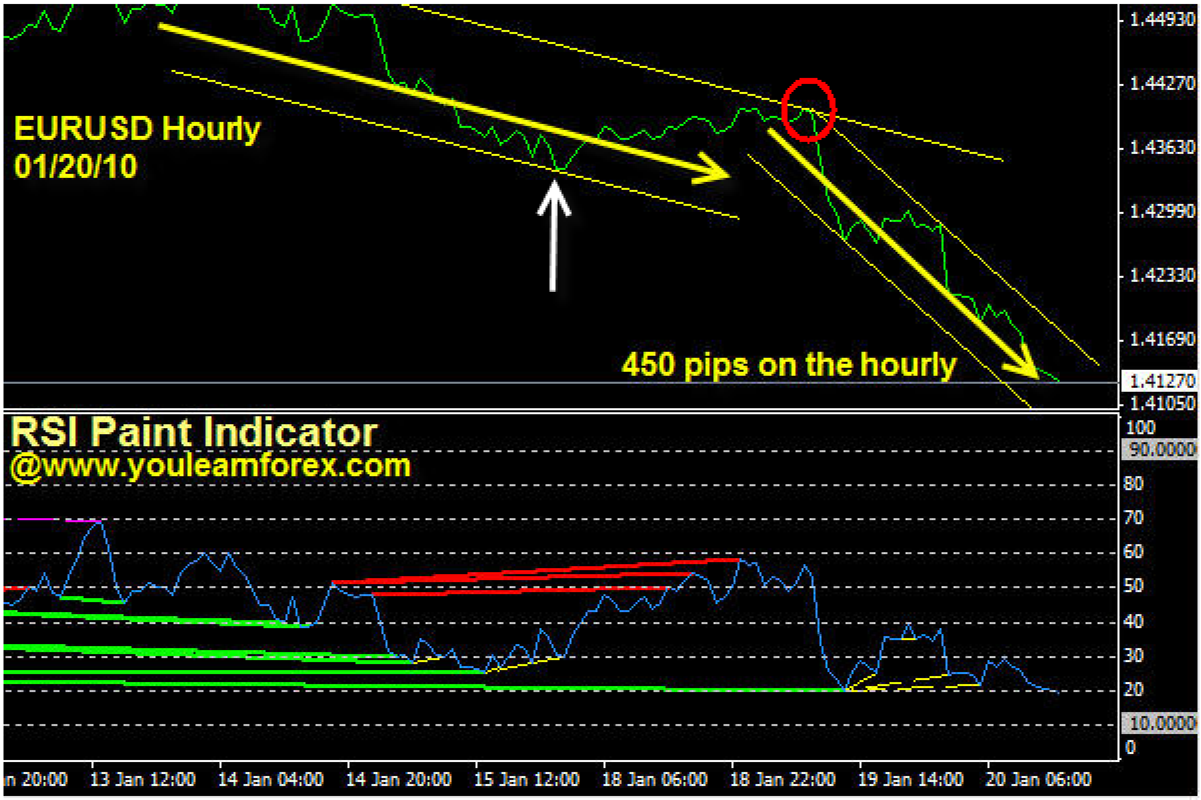
This trade includes the use of the **Main Channel** concept. The **Main Channel** is outlined by the descending green lines on the price. As price reaches the upper channel line (red arrow) we get an RSI signal, a Negative Reversal. The best place to trade a signal is at the edges of the Main Channel or an inner channel when the Main Channel becomes too large.

Drawing channels are subjective however they can help to provide additional information that is helpful when placing a reversal trade. This is discussed at length in **RSI Fundamentals: Advanced.**

Example 15 – When to Ignore Signals

This is the chart above (Example 14) several hours later. As can be seen price dropped then recovered slightly before dropping again. The Positive Reversal that is circled was created as a result of the slow down in price and was what I call retracement signal more than a reversal. It is signally that momentum has slowed, not that it is changing. This is determined by its location in the overall price movement of this downtrending Main Channel.

Example 16 – Trend Channel Change

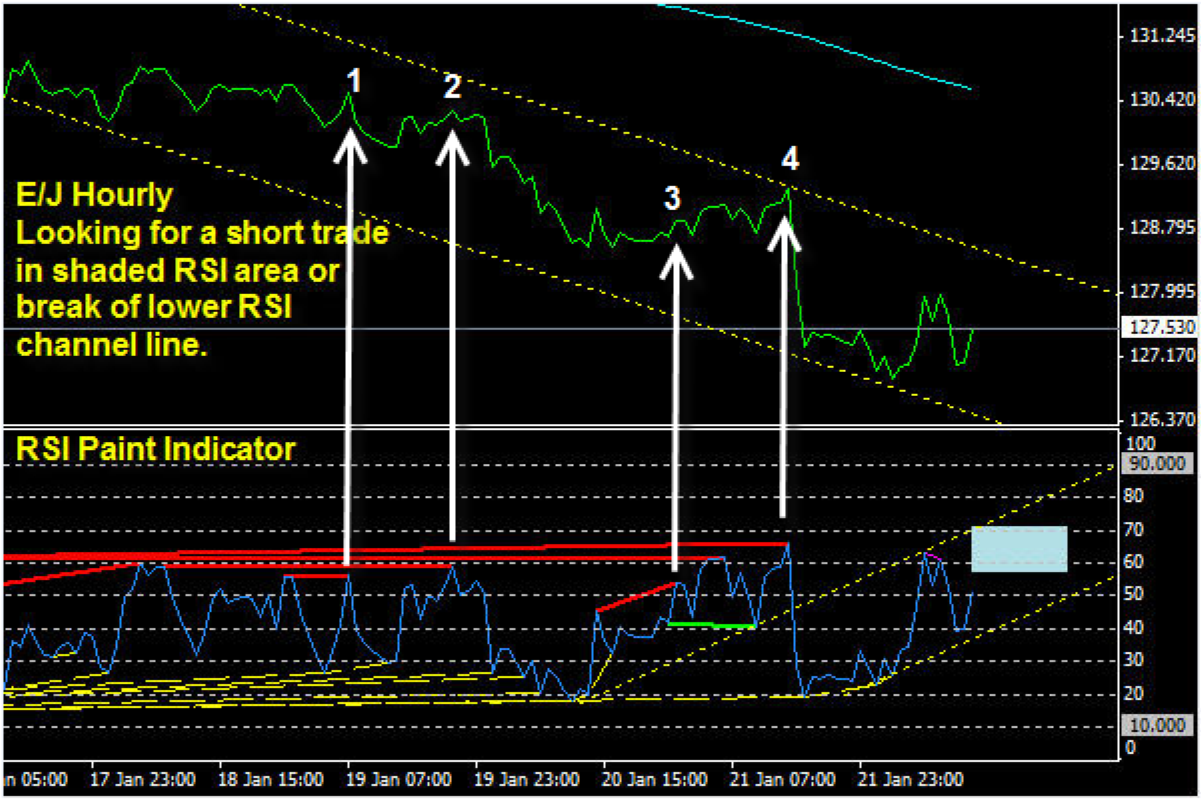


Here we see the Main Channel moving down and then it shifts into a steeper decline. The red circle is the perfect spot to have caught this. The actual Negative Reversal signal occurred a few hours before. Depending on the time of day we might have delayed taking this trade or entered at a smaller position to allow for the additional risk.

For example, the Asian session might have had less momentum as prices tend to taper off and trade in a tight range until nearing the London session. Secondly, even though I often write about trading Negative Reversals in a downtrend and Positive Reversals in an uptrend there are clear points (white arrow) that the risk to trade against the trend is rewarding. You can see diagrams of these points in the chapter on Bi-Channels.

Last, with the severity of the second decline, trading against the trend – Positive Reversals and Negative Divergence – would not be recommended.

Example 17 – Risk and Reward



This chart is about risk and reward. As you progress as a trader you may decide to take more risks or less, that will depend on your personality and also on the size of your trading account. However, regardless of the size of your account taking unnecessary drawdowns should not be part of any traders plan.

Certainly entering at points 1 or 2 would have been good trades in particular if the trader had stayed in the trade to the current price. Depending on the time of the day and if Momentum Type 3 would have been present then this would have been a good entry. Also, the Main channel would have been against these two points as it has now been adjusted for Point 4. Chances are as price began to rise just ahead of Point 3 many traders would have exited the trade.

Position number 3 was not a place to enter, however Position 4 was a perfect location with the exit coming when prices began to leave the lower channel trend line.

The point is that trading every signal is not necessary. If you have one large loss you now have to make up for that trade. One trade for example at Number 4 with a small risk may have been better than the three previous trades with a loss and small position size.

Example 18 – **RSI Channels**

Let's go through this trade step by step. Follow this sequence.

Number 1 is pointing out the current trend of the GBPUSD at the time of the trade. The trader may need to zoom out on the trading chart in order to find this Main Channel.

Number 2 points to the first Inner Channel that leads to the top of the Main Channel and the start of a second Inner Channel at **Number 3**.

Number 4 shows the Negative Reversal that occurred at the same time on the RSI.

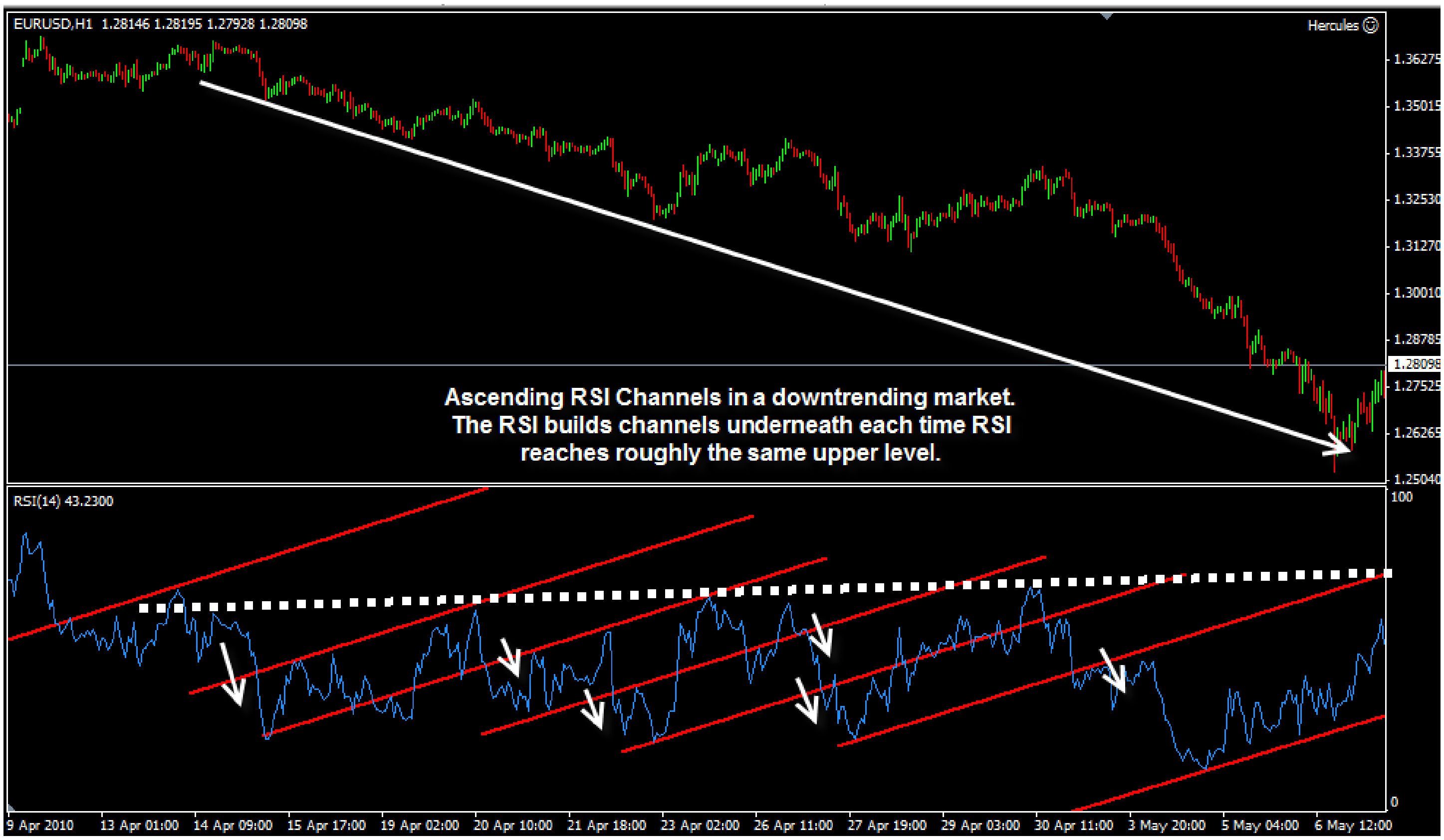
Number 5 is a channel that is drawn around the RSI points during the latest price fall. Notice that the channel (yellow lines) is moving upward. Downtrending prices create ascending channels on RSI. As long as prices penetrate the bottom of the channel as we see here and continue to create new channels underneath this one, prices will continue down. However, when RSI moves in this channel to higher prices the RSI channel will tilt and begin to descend as long as RSI Channels are continuously built on top of it.

Example 19 – Channels and Channel Shifts

This example shows how nicely RSI signals coincide with channels drawn on price. Notice how the first channel (yellow) shifted to a steeper channel (blue) and then shifted back (purple). The shallower shift back (purple) did not change the direction of price, it was still down just not as steep. Many traders wonder when a channel is broken does that mean price has changed. It does not as you can see here. When price drops steeply or rises steeply in relation to previous moves, price will even out for a variety of reasons. It is not necessary to know why, just that price will eventually reach stability for a least some period of time.

Also, notice how RSI over this period stayed within a 30 point RSI range (between 60 to 30 RSI). The Range Shift came at the far left that culminated in a number of Positive Reversals that set the stage for the first Negative Reversal (first white arrow on left) that began a series of trades over this 10-plus day period. Notice after the Range Shift there was one Positive Reversal that failed to make much of an impact. All that followed were Negative Reversals and Positive Divergences. This is further testament to the fact that PDs do not reverse prices and create Momentum Type 1 or retracement momentum.

Example 20 – **Downtrending Prices Mean Ascending RSI Channels**



This is a simple illustration of how prices are dropping while RSI continually builds channels underneath each other. RSI moves up in these channels until it reaches typically a 60 RSI level and then begins to move downward again. It will then start down and penetrate the existing channel, establish a new low and start another channel. Notice however, just because RSI is climbing does not mean prices are climbing (so much for overbought and oversold).

Example 21 – Uptrending Prices, descending RSI channels

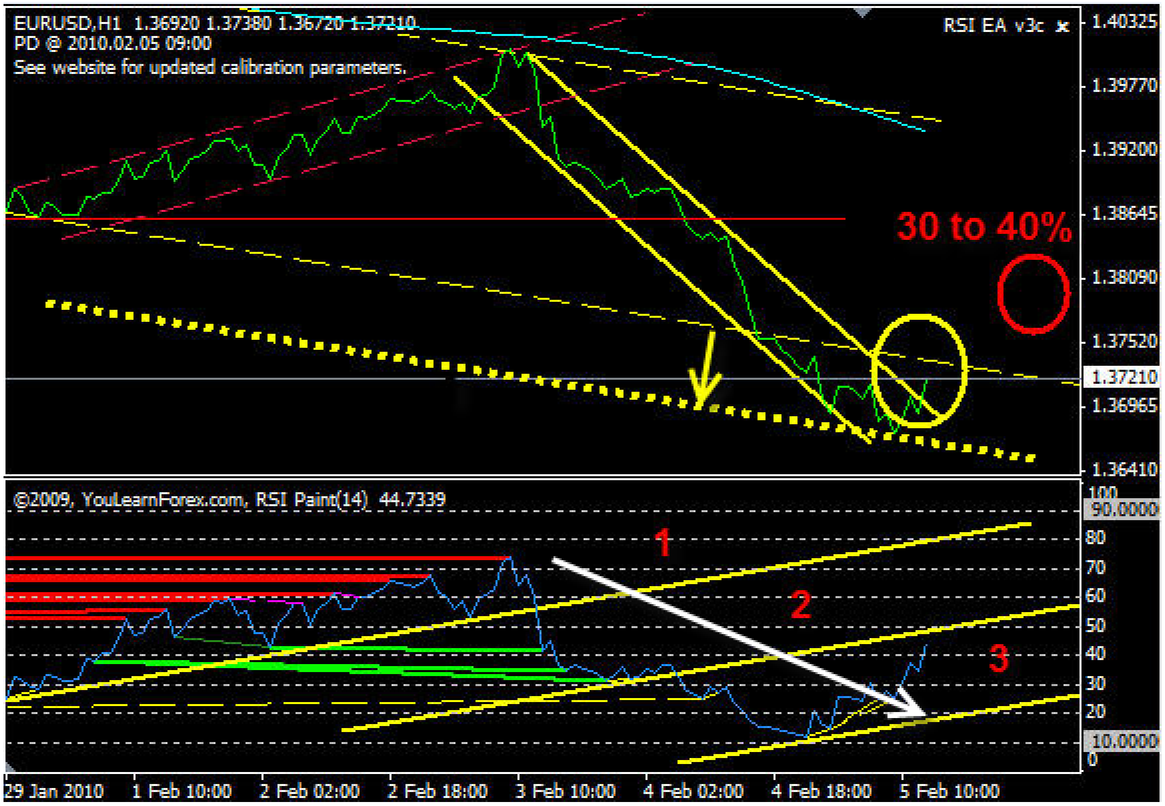
This is the exact opposite of the example above. Prices are going up and the RSI channels are descending and building new channels above the old. Starting on RSI on the lower left side RSI moved down to roughly a 35 RSI then started back up and broke through the channel where it rises to around 70 to 80 RSI before moving back down to the 35 range. Again notice that it would not be prudent to be buying and selling on the overbough and oversold signals that RSI gives as this would have created many losses.

Example 22 – **Range Shift and Reversals**

Price has dropped steadily while RSI was in the yellow box. RSI has remained below 50. When RSI had moved up to a higher level (White Box) price was beginning to move up. Notice how many Negative Reversals were signaled. Also notice on price how often price fell short of the channel top line (purple). The Last Negative Reversal was a high probability trade simply because the Negative Reversal was at both the top of the Main Channel for price (yellow dashed line on price) and at the top of the Inner Channel (purple dashed).

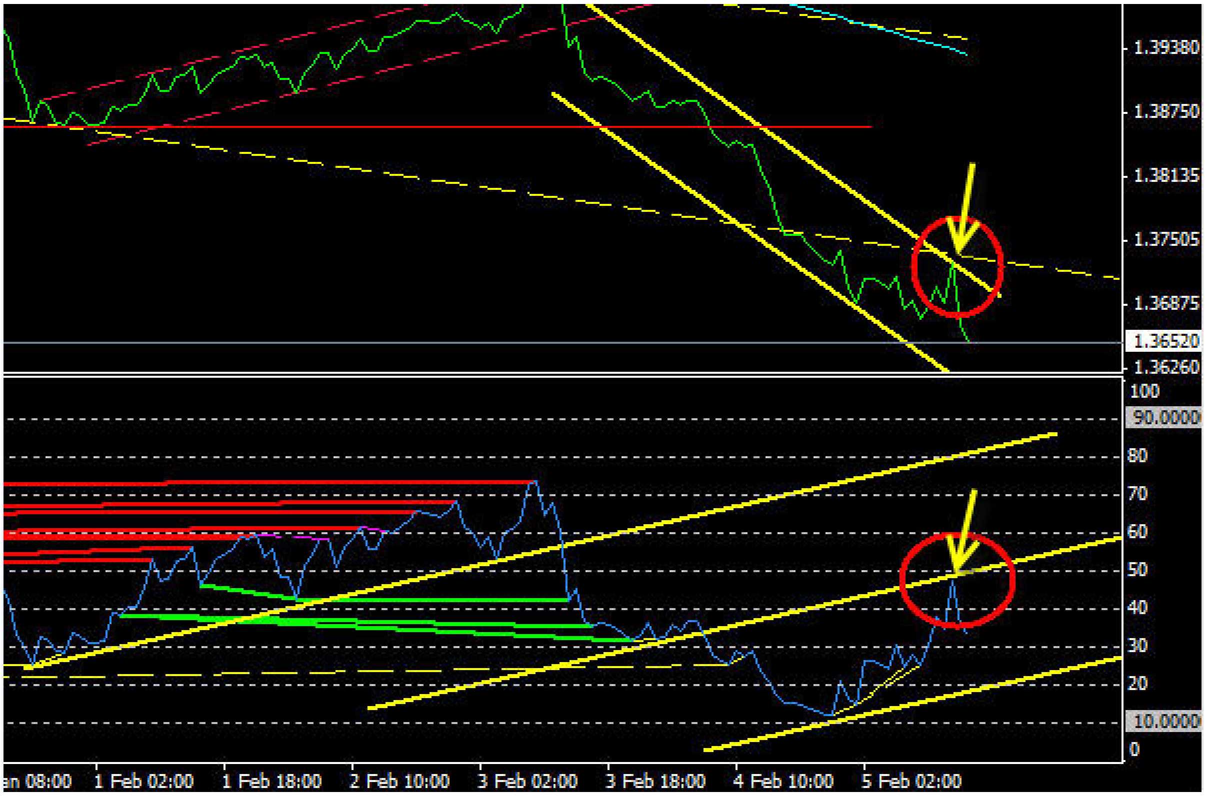
The circle (yellow) shows what appears to be the completion of another Range Shift.

Example 23 – RSI Channels



This is a perfect and clear example of RSI moving through and creating new channels on RSI. Notice that RSI is reaching for 50 RSI in Channel 3. We would be looking for RSI to stay under 50 or 60 RSI at this point and move down through the existing Channel 3 to establish another channel under Channel 3.

Example 24 – RSI Channel Bounce



This is a continuation of the previous chart. Notice how price went to the 50 RSI right at the channel line and began to drop again. We would now be looking for RSI to drop below the lowest yellow channel line on RSI creating another lower ascending channel. If the conditions are right a trader may take a trade at this spot or drop down to lower time frames to see if a Negative Reversal is signally at that point. This would be a short-term trade.

Example 25 – RSI Channels

This is a continuation of the two previous charts. The White Arrows locate where we were on the previous chart with RSI bouncing off the RSI channel at 50 RSI and making a nice gain. But notice that RSI did not fall through the lower channel line and establish a new floor for a lower channel. Instead, at the large Purple Arrow in the RSI area, a Positive Divergence formed right at the bottom of the Price Channel (small purple arrow pointing up) outlined in yellow. The solid yellow channels formed the Inner Channel on price and the dashed lines formed the outer Main Channel on price.

This was a crucial spot and required an exit or profit taking. The trader could have played this long and would have done so with a tight spot in particular if the Positive Divergence was at a time where Momentum Type 3 was in place or had a high probability of being in place. The severity of the previous downtrend made the upswing in price inevitable.

Last notice how RSI is drifting upward in this RSI channel and has reached near 70 which could cause a tilting of the RSI channel to a descending channel. However, before we consider that price has changed to an uptrend the Main Channel on price would need to make a significant change. As this was February 2010 we know that prices continued downward.

Example 26 – **Negative Reversal with Channels and Clear Exit Point**

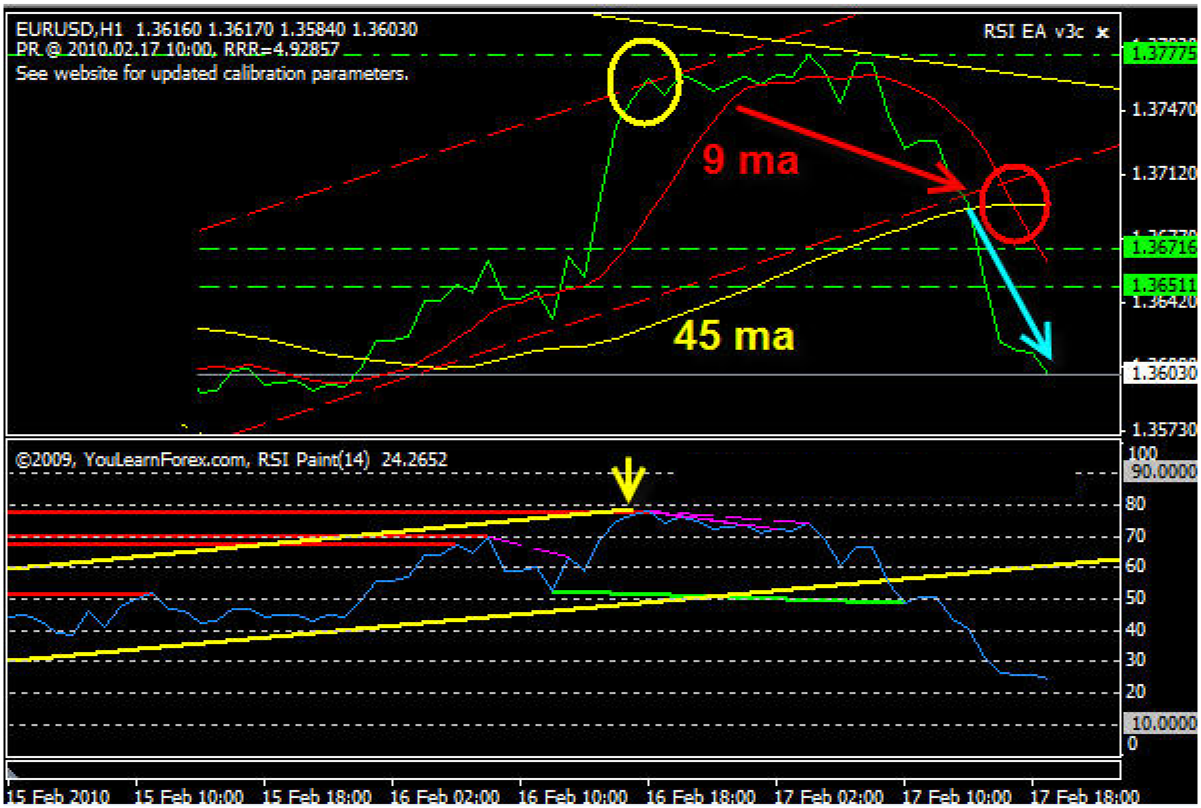
This trade took place at the Negative Reversal point and dropped over 150 pips. Notice where RSI was (red circle) at the yellow RSI channel line. Also there was a good exit point where a Positive Divergence and Positive Reversal both were signaled at the same time.

Example 27 – Break of the Inner Channel

There are a number of lines here but this trade was rather simple to locate. We know that we want to have the Main Channel of the currency trend to determine the direction we would prefer to be trading in. In this case those are the parallel line on price that are barely visible (yellow dashed).

There are two Inner Channels on price. The first is the purple dashed channel tracking price upward. Price broke that channel and then retested it at the red arrow. We did not know that the next Inner Channel would be there until prices fell but at the red arrow on price we also have the red arrow on RSI. It is also at the RSI Channel. This trade dropped until the Positive Divergence/Reversal where it went sideways. This would have been a good place for taking profit. The more aggressive or long term trader may have wanted to stay in this trade however.

Example 28 – Moving Averages versus Reversal



This trade illustrates several important points.

This trade has dropped 150 pips from the point of the yellow circle where a Negative Reversal signaled the trade. Notice that we have also put a 9MA and a 45MA (MA = moving average). Some traders who trade RSI are taught to wait until the moving averages cross. This is designated at the red circle. This is very late after the actual signal and there is no indication that price will continue downward after the cross. In this case it does but the earlier signal gave us the biggest profits.

RSI is a **leading** indicator thus the signal will obviously lead a moving average that is a **lagging** indicator. This defeats the purpose of using a leading indicator. Although Andrew Cardwell teaches this method in his trading I am not a proponent of it. It is much better to use a single moving average and trade in relation to it not because of what it does.

Example 29 – Help Finding When to Exit or Take Profit.

This trade did what might be expected after the last drop in price. Momentum began to move up. Now when would you exit? This depends on the type of trader you are. Short-term traders would have exited here but longer term traders who are willing to wait through the cycles of Momentum 1, 2 and 3 would perhaps want to hold on to this trade for a longer catch of pips.

RSI feel deeply to 20 before establishing the next channel. Channels on RSI are always drawn parallel but they can occur different distances apart as is shown here. The yellow arrow locates the most recent RSI channel and the red arrow and red lines project what might be the next move in price. A break through the yellow channel line would set up another channel, etc.

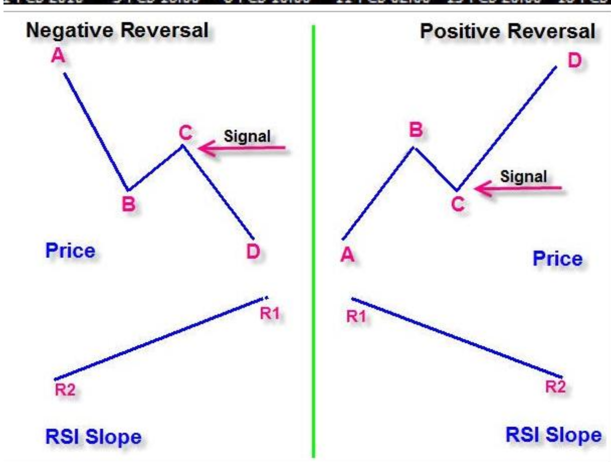
Example 30 – How Reversals Can Work with Divergences

In this example we are looking at RSI that has been ranging very high (70-40) but it has been working itself upward from February 4th where it stood around 30. All of the Negative Reversals would have been ignored in this particular climb of price.

However, after the last signal price moved up and stabilized along the upper Main Channel and the Inner Channel. This in my mind is a perfectly good place to take a trade short. There is risk but often you may catch a Range Shift which is always a bonus. Second, Negative Divergences often lead into the first point of a Negative Reversal. Because of the location of price here, the risk might be well worth taking.

You would be looking to exit at the bottom of the channel unless the lower channel is broken and shifts the Main Channel downward.

Example 31 – The Levels of Success



Here is an example of the Levels of Success for a Negative Reversal on a trading chart. The blue letters on price indicate where the letters would be and as you see on the diagram to the right. The signal is at C and CD is the projected target where CD in pips is expected to equal AB in pips. As you can see in this graphic CD is roughly 63% of the way to its target.

This is important for long term traders or traders willing to stay in a trade for several days. Notice also that the the CD part of the trade has gone through several different changes of the Inner Channels, three to be exact.

Example 32 – Set it and Forget It.

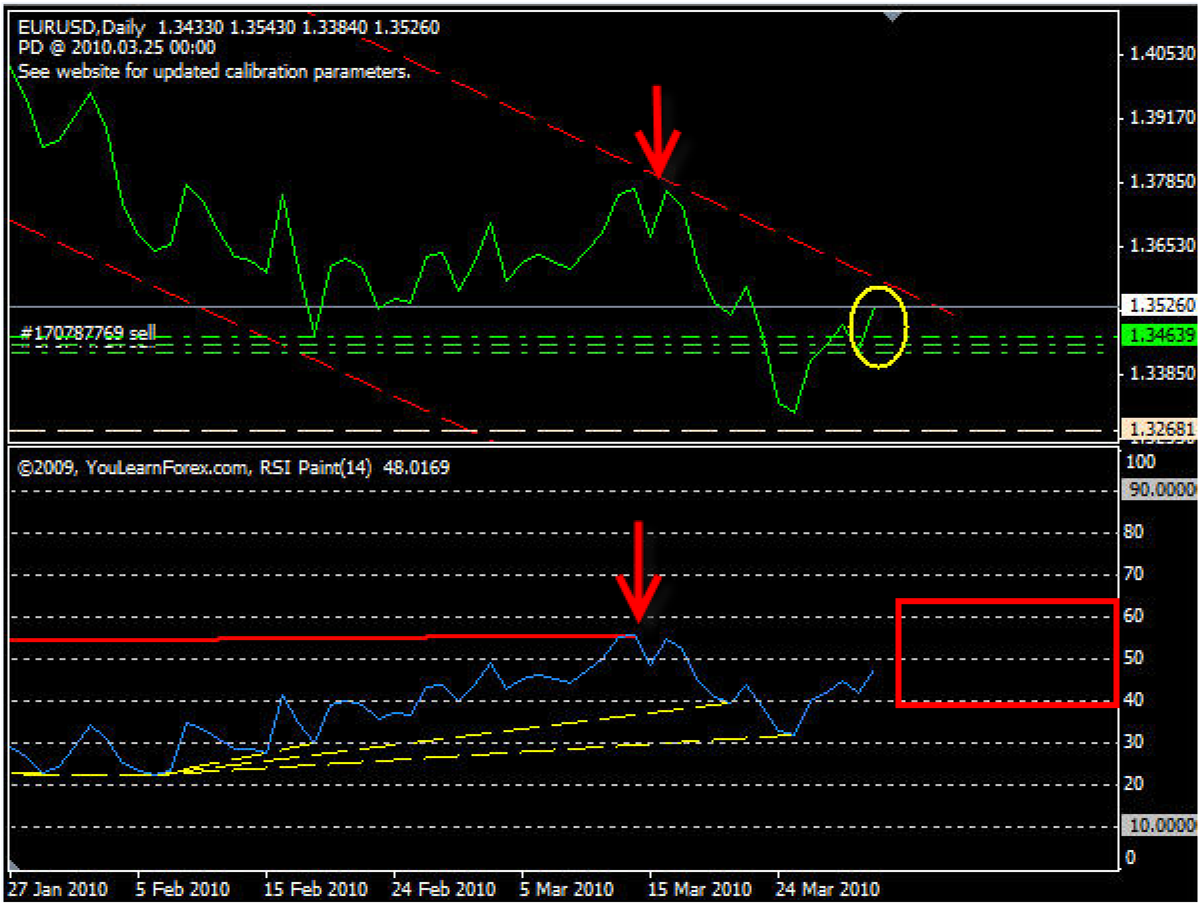
There were two trades that signaled at the yellow arrows under 60 RSI. Notice that price was at the top of the channel (red dashed lines) on price. Price never got above the white dashed line on price. The funny looking objects on this chart are price histograms and are not significant.

Example 33 – Multiple Trades Over a Short Period of Time Can Make for a Good Year.

These trades are over about 2 a twp week period. The Main Channel is down and all of the trades were short. We are looking for short trades primarily when the Main Channel is down and vice versa when prices are up.

This is a good trading concept. When the Main trend is down then stay with the mainstream with your trades especially if you are wanting to be conservative. When the Main Channel is up then stay with uptrending signals or Positive Reversals. Always check the Main Channel of prices before you trade any time frame. If you are trading the hourly you may need to zoom back to the H4. If you are trading shorter time frames make sure you zoom back far enough to see the Main Channel, then to trade conservatively, find your signals in that direction.

Example 34 – Anticipating the Future



This trade began with a Negative Reversal at the red arrows. There were two exits at the Positive Divergences. If you are only trading short because you are trading with the Main Channel then you will want to anticipate where the next Negative Reversal will come. Here RSI will have to get above the previous RSI high with a lower price which is pretty much assured of happening. Depending on the time of day and the velocity of the market you should be able to predict the next area where the signal will come. Learn to do this and you will become much more predictive in your trading.

Example 35 – Conservative Trade Entry and an Aggressive Trade Entry

Here are two trade entries. **Trade 1** (Conservative Trade) is at the bottom of what is the Inner Channel. This is a good location to trade as the current Main Channel of the USDJPY is up. Notice that we have a Positive Reversal at the same point. With price moving up as dramatically as it did, price would need to retrace some and we see the shower of Negative Divergences that begin to occur. We get a number of PRs as price retraces which we expect in the range of RSI and because of the Negative Divergences which are Momentum 1 Type (retracement momentum signals).

Learn to let the first few Reversals in this sequence go as they form as a result of retracement, however as price gets to the lower level of your range then a Reversal signal to the upside as in Trade 2 (Aggressive Trade) could be taken with reward.

Example 36 – Two Strong Moves Against the Trend.

The Main Channel is down so we are looking to trade short on the USDCAD. Prices shot up previous to the signal with little retracement and then the last peak was straight up (red arrow). This is a good place to look for a short trade. We may have tried at the previous NR and we would have been stopped out. That would not have been a bad trade. That should not keep us from taking the second NR in particular after the straight up move. As it turned out this trade made 600 pips with almost no retracement which would have easily exceeded the loss we might have taken with the earlier NR. Also, there was no drawdown.

Example 37 – Moving Average Opportunities

Often price responds well to a single moving average. The MA above is a 100 MA. The first arrow shows a NR that appears right at the 100 MA. When price began to climb the NRs begin to appear again. The last NR would have needed a little room for risk but it could have been taken as a good trade in particular when it fell below the second PR below the yellow arrow.

This brings forth another point, it is not imperative that trades always be entered right at the signal to make a profit in particular if this signal comes at a time of no momentum.

Example 38 – Moving Average Opportunities

Three more illustrations where price and moving averages tie in with Reversals. The reason this often works is that many larger trading systems operate on moving averages.

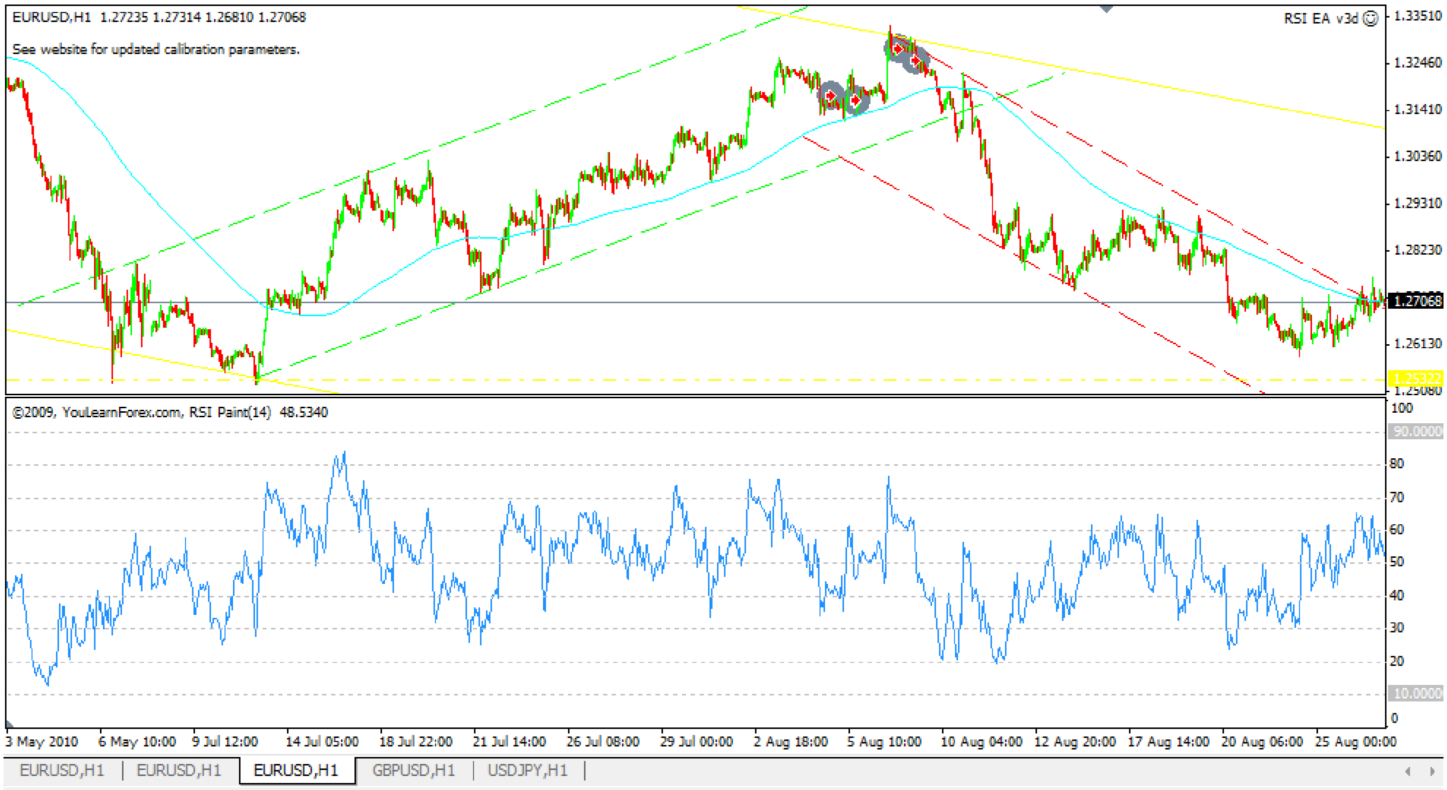
Example 39 – **Entering and Holding**

The large red arrow at the top of this daily chart was the first retrace of the downtrending price that began in the beginning of 2010. Notice the NR at the same point at the top of the Main Channel. Had you entered at that point and held, the bottom would have been 2000 pips away, something to think about. A possible way to take this kind of long-term position and still trade short term is to take a partial position size on the long term trade and let it run. This can act as a hedge against short term losses, not to mention you can use other entry points on the Daily chart to add to your position.

Example 40 – How Long to Stay in a Trade?

How long should you stay in this trade? If the market falls it should drop along the line of the blue arrows. Key to the move is what will be the bounce in particular if the bounce does not rise about 50 or 60 RSI. This would mean that prices would continue to fall.

Trading Exercise 1 – A Trading Exercise – Range Shifts



This chart is in white so that you can make a copy of it or just mark on this page. Take a pen or pencil and see if you can mark the Range Shifts from left to right. Also, draw a box around where the ranges stayed within a particular area after a Range Shift. Hint: There are at least 4 Range Shifts and 2 ranges. The answers are on the following pages.

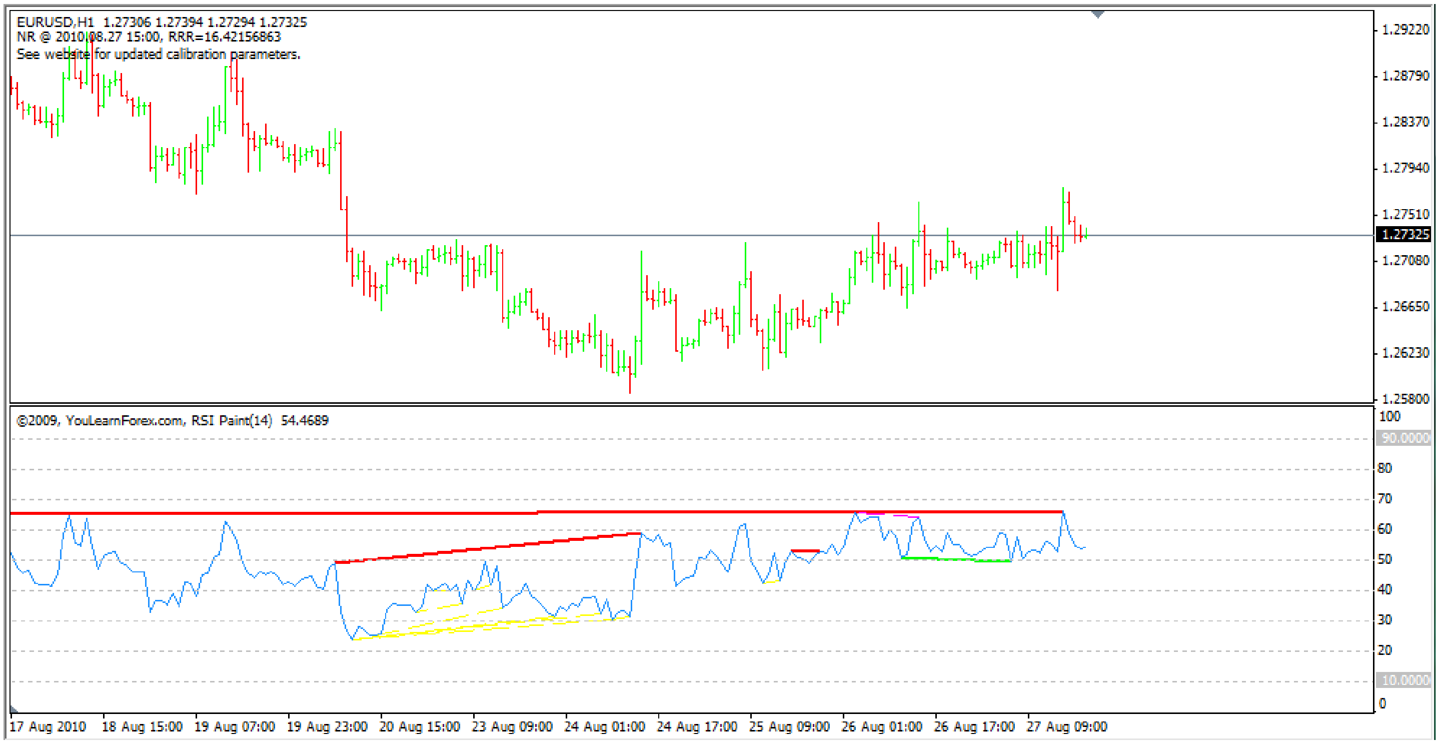
ANSWER BELOW

ANSWER TO 1

The first Range Shift moves price up but is immediately followed by a 2nd then a 3rd. This typically happens when prices are in consolidation. Notice however after the 3rd shift RSI did not drop to the same levels it had before. This would be your first clue that prices might be stabilizing into an uptrend. The green shaded area shows that this is what occurred. The 4th range shift is down and then RSI stays in a lower range. Notice the difference on of the range tops and bottoms.

This chart is the same chart but with the 4 RSI Signals added. Notice how in A there is an equal mix of all 4 signals. When prices move up the predominate signals are NDs and PRs. When prices begin to move down, PDs and NRs.

Trading Exercise 2 – Seeing Ahead



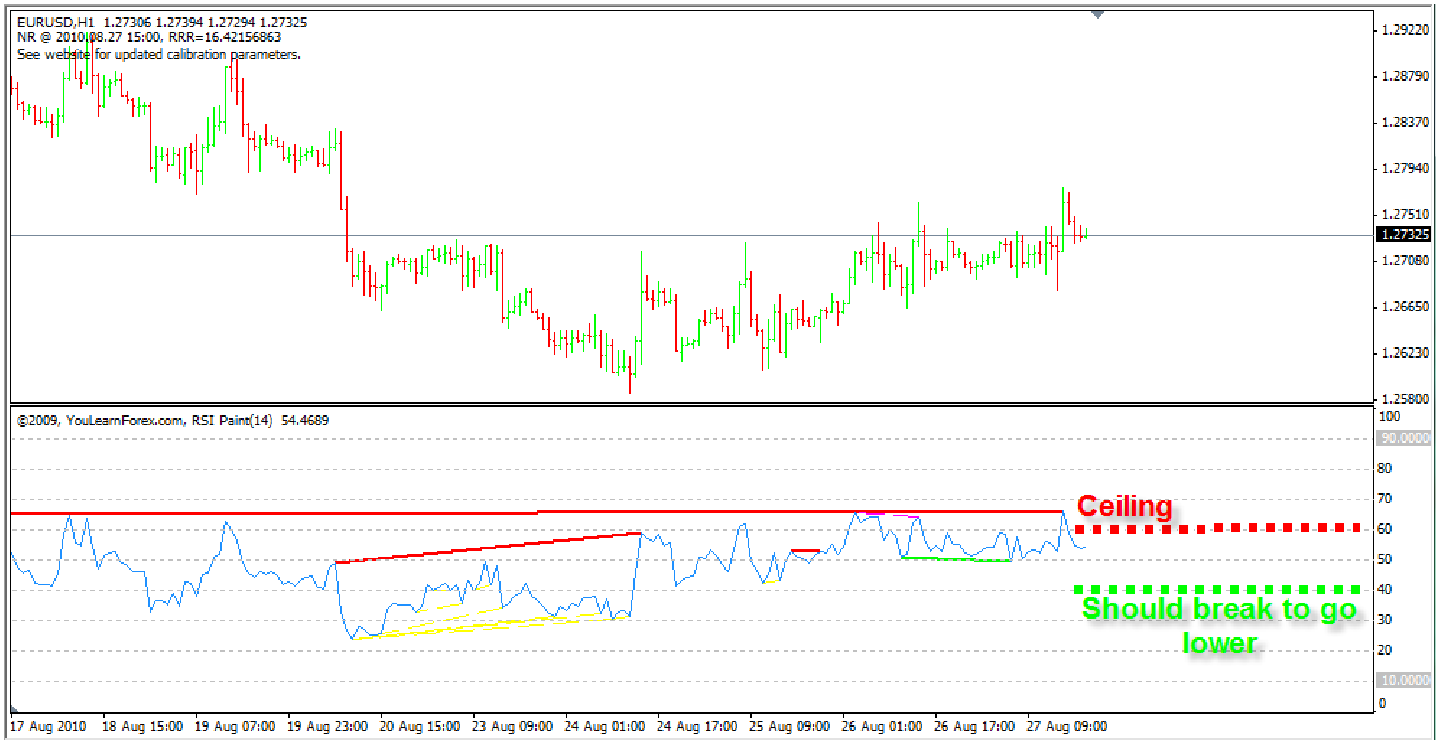
Take this chart and draw where you think RSI will go if prices drop.

1. Draw a horizontal ceiling line where RSI would need to remain below if prices were going to continue to drop.
2. If prices resist falling, where would RSI mostly likely stop in this next move?

This chart is the EURUSD H1 at the end of trading on Friday, August 27, 2010. Go back and see if you were right or how close you came to being correct.

ANSWER BELOW

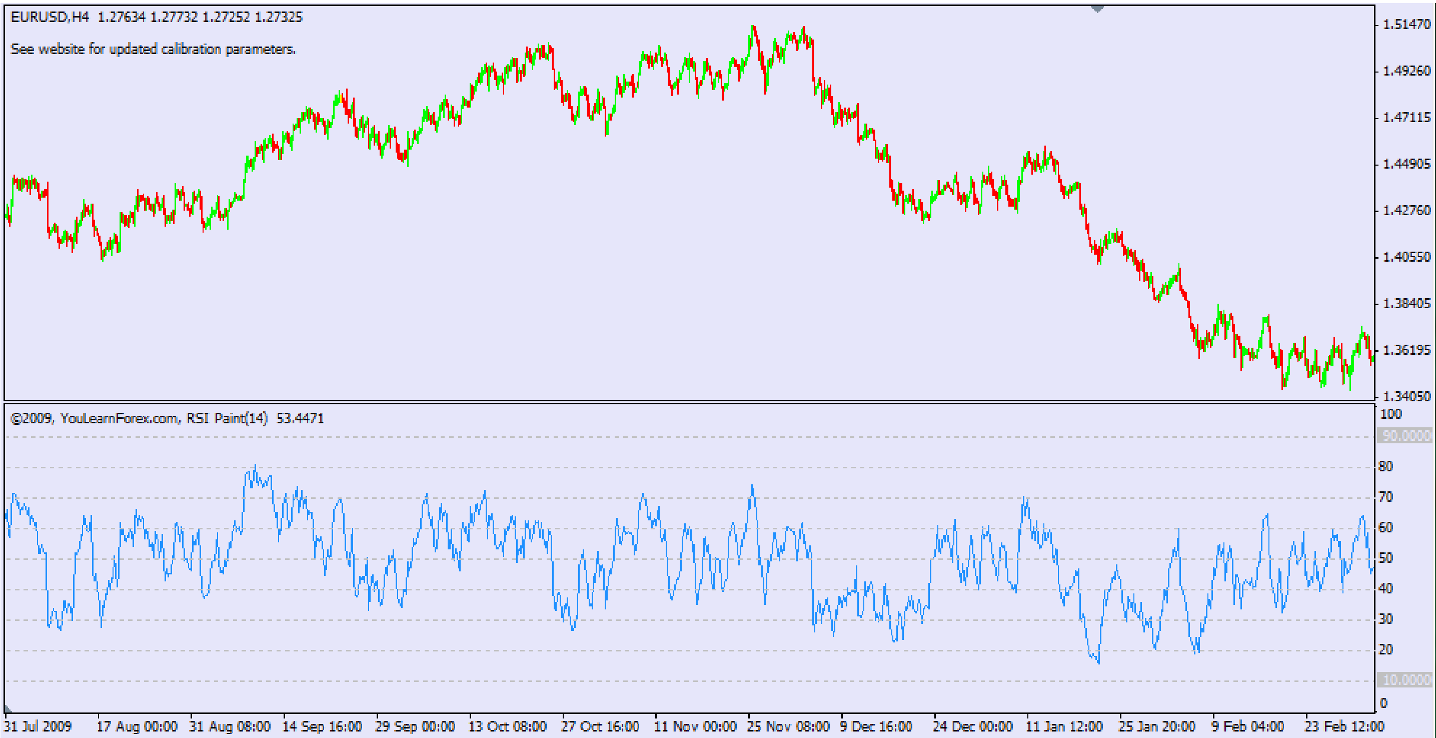
ANSWER TO 2



For price to continue lower RSI would need to stay under 60 RSI for the most part and break below the 40 RSI level. These are relative as there might be drops slightly below or above these numbers but on the hourly charts these areas would be representative of where price would range.

This is a good habit to get into as you trade to create the possible scenarios where RSI needs to go. With the 4 RSI Signals you have good clues to help you.

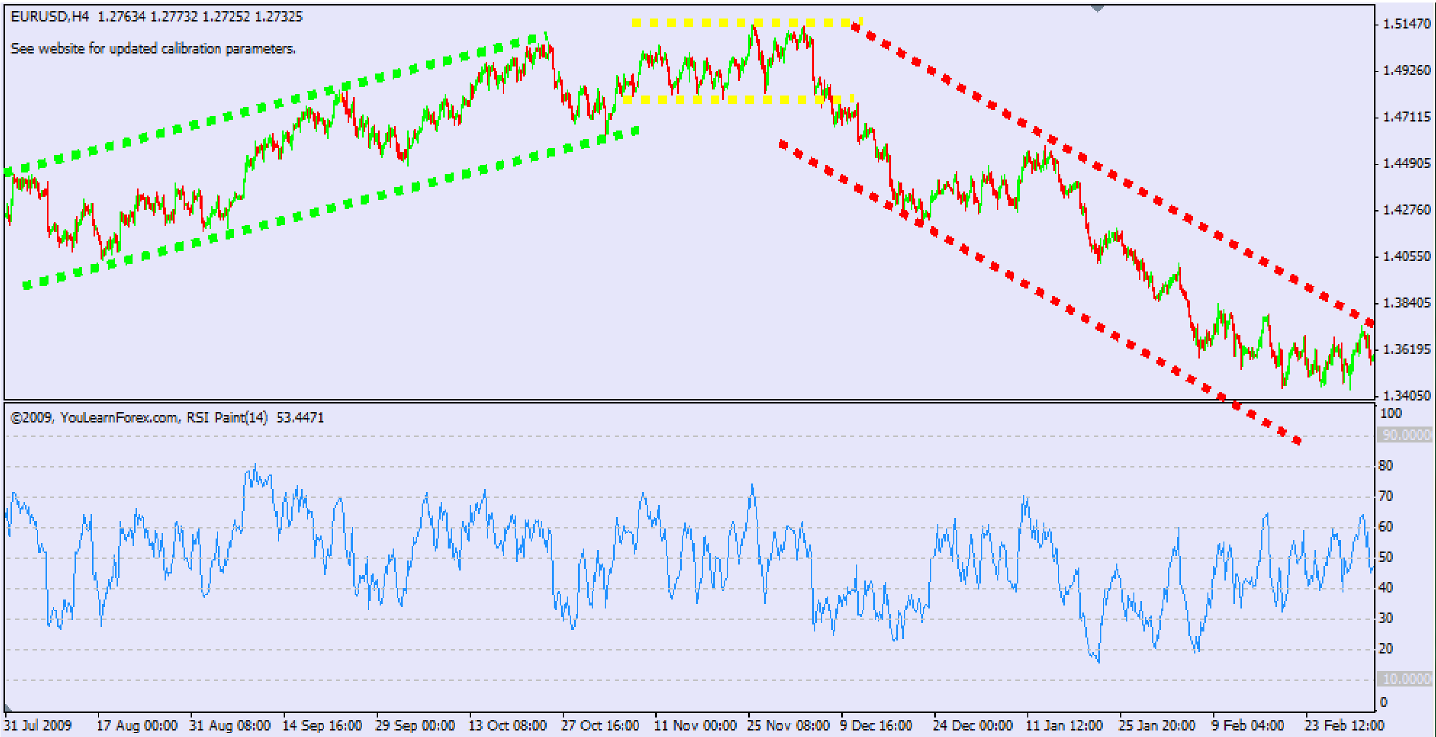
Trading Exercise 3 – **Consolidation and Trends**



Mark the Main long-term trends on this chart and the consolidation.

ANSWER BELOW

ANSWER TO 3



Your trend lines would look something like this. The uptrend ended when the last higher high could not be taken out leading to a short period of consolidation. When the last higher low in the uptrend was taken out the downtrend began. This is the H4 time frame. If you are trading the H1 time frame dropping back a time frame and getting a feel for the direction of the trend will help in making decisions about which reversal signals to take.

Trading Exercise 4 – **Drawing Main Channels**

Draw the current Main Channel on this Chart

ANSWER BELOW

ANSWER TO 4


EURUSD,H4 1.27637 1.27642 1.27432 1.27508
NR @ 2010.08.27 12:00, RRR=25.32444444
See website for updated calibration parameters.
1.49690
1.47450
1.45140
1.42830
1.40590
1.38280
1.36040
1.33730
1.31490
1.29180
1.27508
1.26940
1.24630
1.22390

Trading Exercise 5 – Drawing Main Channels

ANSWER BELOW

ANSWER TO 5


GBPUSD,H1 1.55324 1.55377 1.55137 1.55254
1.61930
1.61230
1.60530
1.59830
1.59130
1.58450
1.57750
1.57050
1.56350
1.55650
1.55254
1.54950
1.54250
1.53550
1.52850
1.52150
1.51470
2 Aug 2010
3 Aug 17:00
5 Aug 01:00
6 Aug 09:00
9 Aug 19:00
11 Aug 03:00
12 Aug 11:00
13 Aug 19:00
17 Aug 05:00
18 Aug 13:00
19 Aug 21:00
23 Aug 07:00
24 Aug 15:00
25 Aug 23:00
27 Aug 07:00

Trading Exercise 6 – Drawing Inner Channels

Draw the Inner Channels on this Main Channel

ANSWER BELOW

ANSWER TO 6

EURUSD,H4 1.27637 1.27642 1.27432 1.27508
NR @ 2010.08.27 12:00, RRR=25.32444444
See website for updated calibration parameters.
1.49690
1.47450
1.45140
1.42830
1.40590
1.38280
1.36040
1.33730
1.31490
1.29180
1.27508
1.24630
1.22390

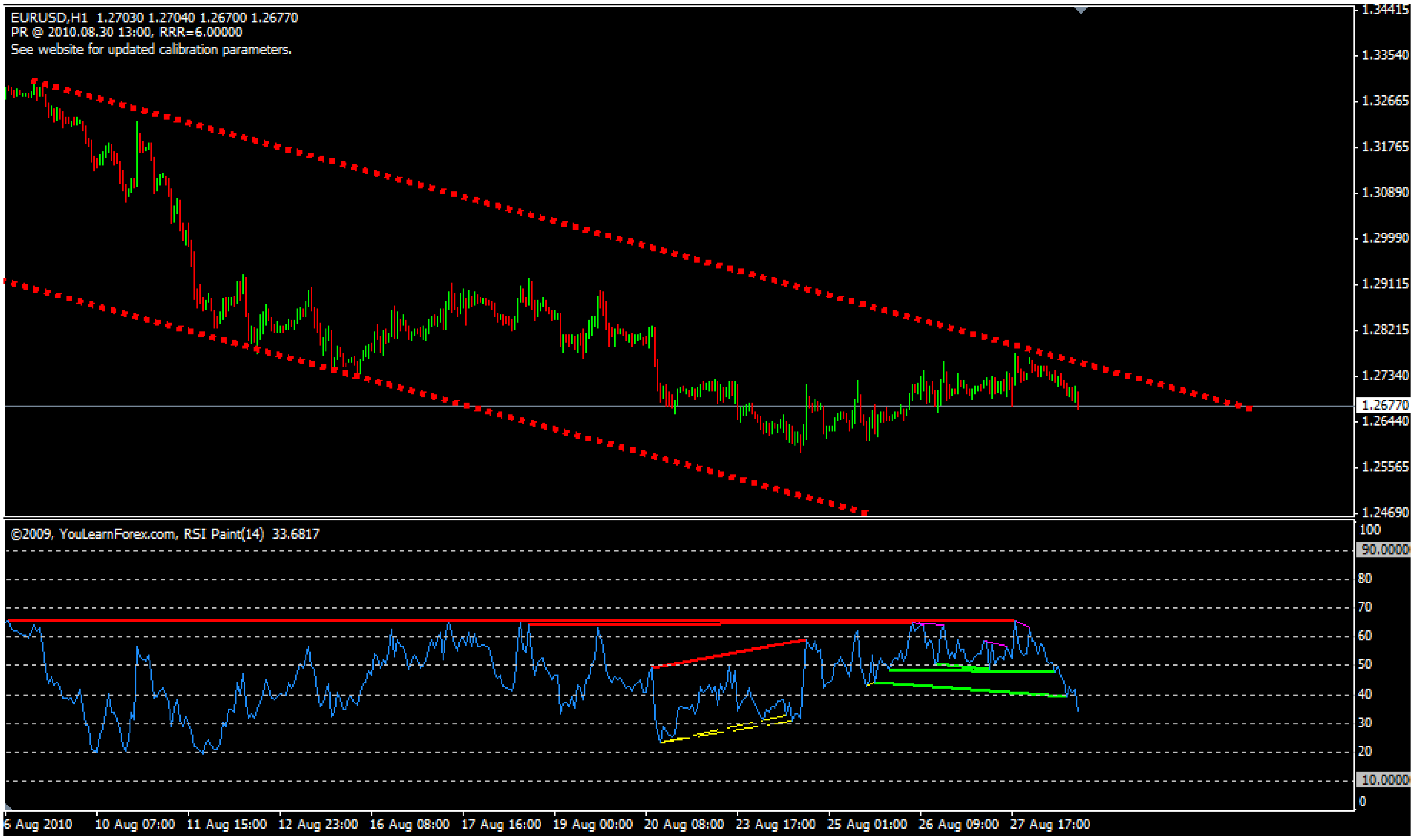
Trading Exercise 7– Drawing Inner Channels

ANSWER BELOW

ANSWER TO 7


GBPUSD,H1 1.55324 1.55377 1.55137 1.55254
1.61930
1.61230
1.60530
1.59830
1.59130
1.58450
1.57750
1.57050
1.56350
1.55650
1.55254
1.54950
1.54250
1.53550
1.52850
1.52150
1.51470
2 Aug 2010
3 Aug 17:00
5 Aug 01:00
6 Aug 09:00
9 Aug 19:00
11 Aug 03:00
12 Aug 11:00
13 Aug 19:00
17 Aug 05:00
18 Aug 13:00
19 Aug 21:00
23 Aug 07:00
24 Aug 15:00
25 Aug 23:00
27 Aug 07:00

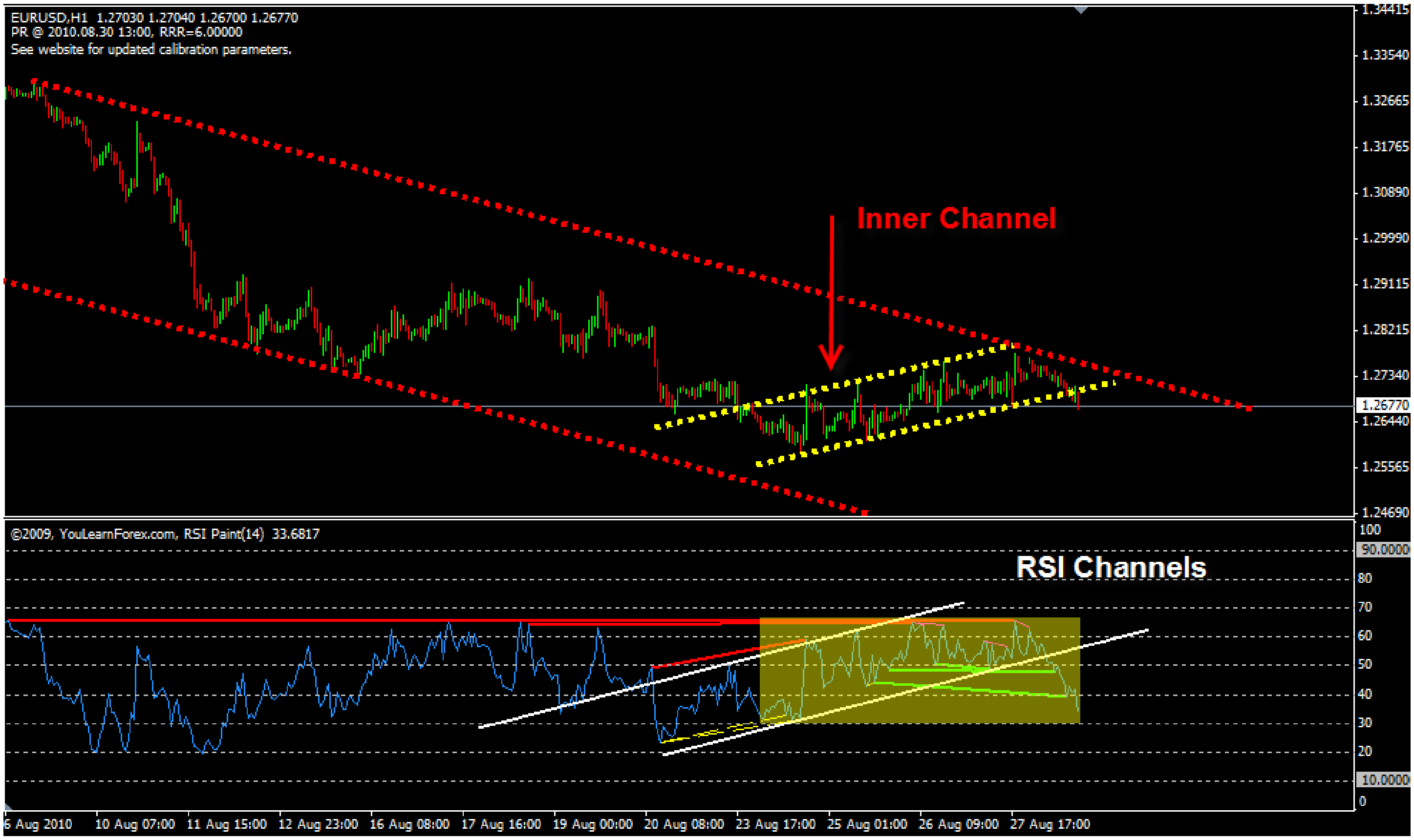
Trading Exercise 8 – What is Missing?



What is missing from this trading chart that would help in the execution of this trade?

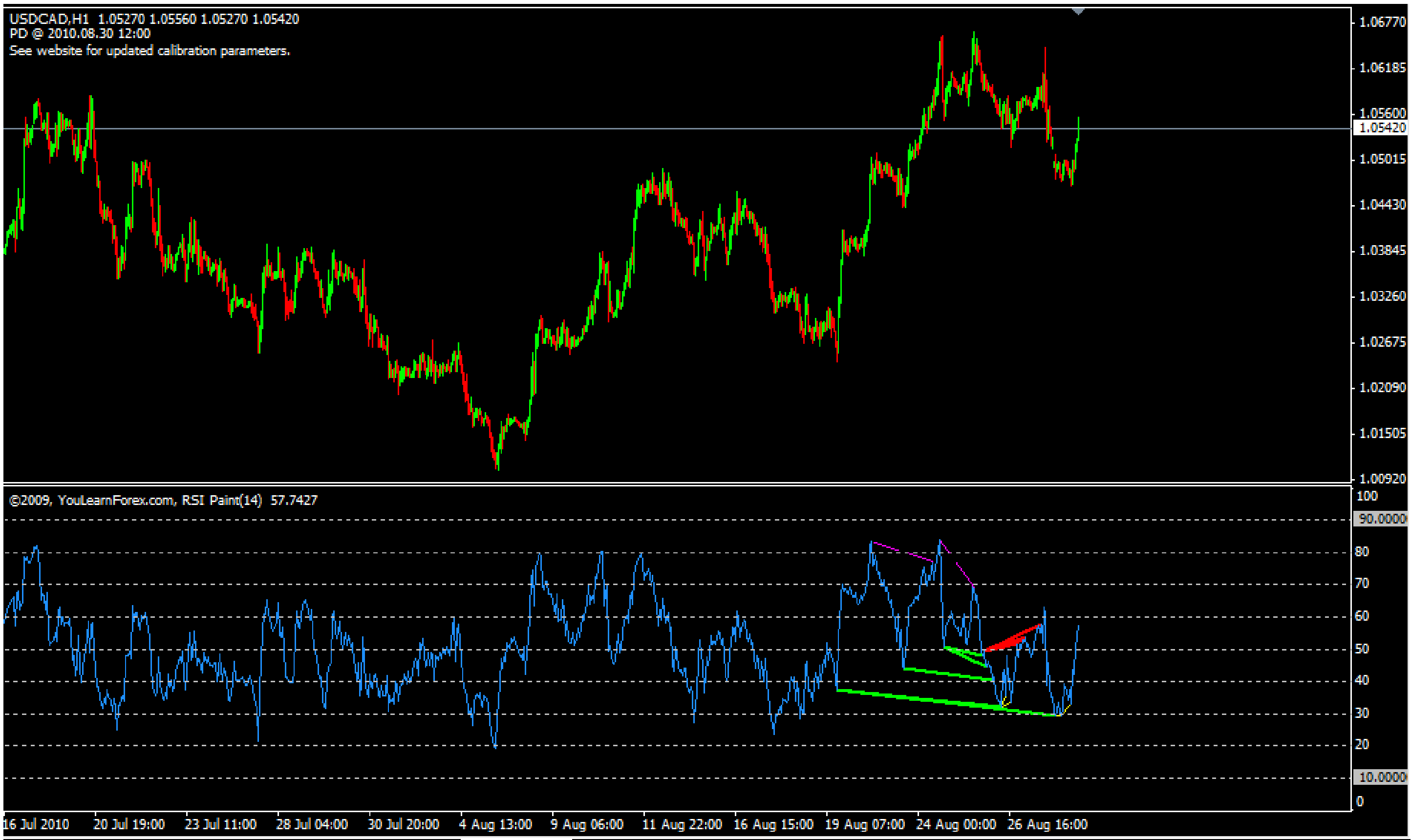
ANSWER BELOW

ANSWER TO 8



1. Adding the Inner Channel on price will help track where price is going. It will also be of benefit when there is a shift in the channel
2. On RSI, mark the RSI Channels. Simply outline where price is going. When the Main Channel is down the channels on RSI will be ascending as above and as price breaks through the bottom, new channels will be formed. Vice versa for uptrending Main Channels.
3. Locate the range that RSI is trading in. Here the range in about 65 to 40. What this means is for price to continue downward, RSI must drop to a lower range and then not recover to the previous range but stay below it.

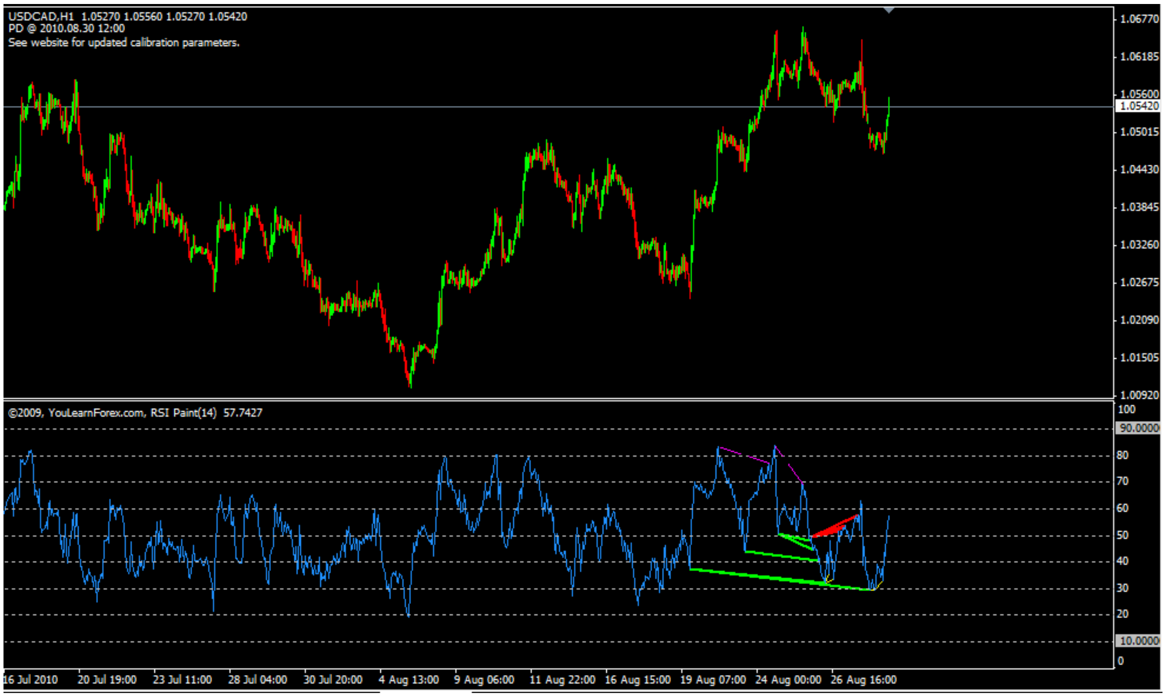
Trading Exercise 9 – Main Channel



Question: What is the Main Channel direction for this currency pair?

ANSWER BELOW

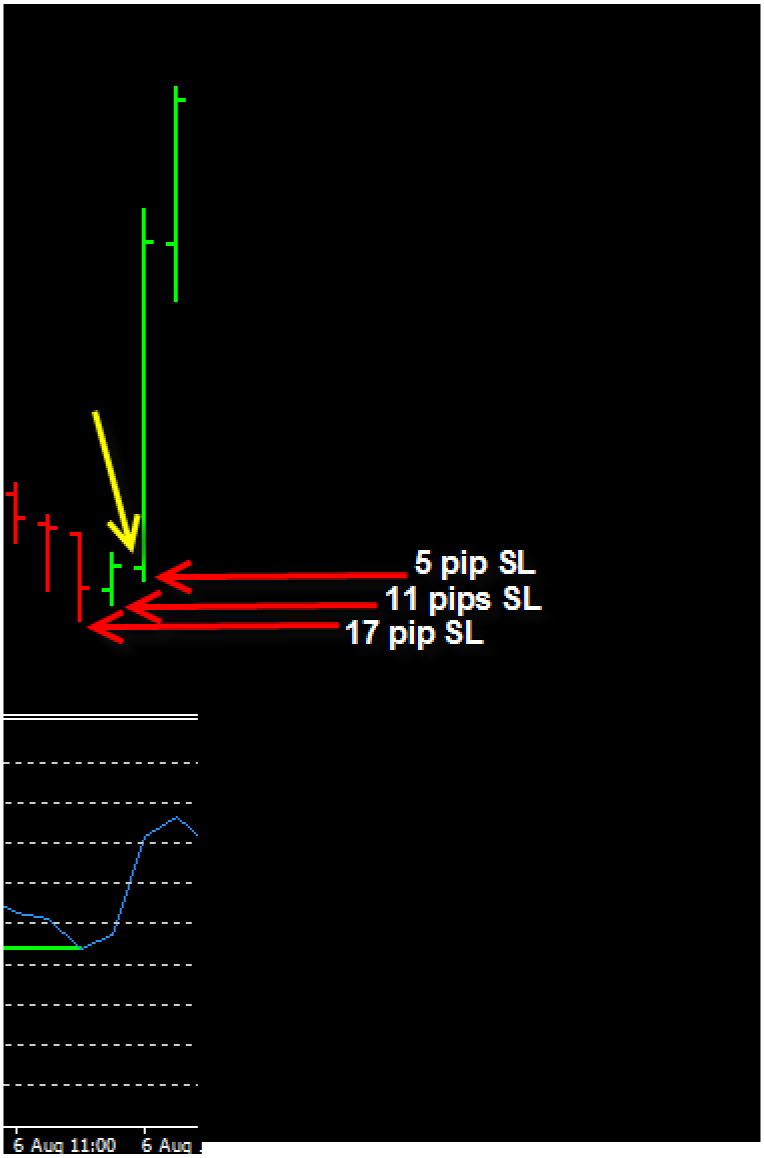
ANSWER TO 9



This is somewhat of a trick question. This is an hourly chart with the widest view possible. Prices are going up but the time period up is about 15 trading days, but what about the preceding days? The downtrend on the left side of the chart is just about equal to the current. We want to find the overall direction.

To get the proper perspective we need to drop back to the H4 time frame and zoom out. We see a 4 month consolidation of prices with a wide range from top to bottom. In this case 500 pips. This can be traded using both Negative and Positive Reversals rather than using just the Reversal signal compatible with the Main Channel direction or trend.

Trading Exercise 10 – Entry Point



This is a trade at 9am EST which is a key momentum time based on the RSI Statistical Studies that are available at the Member Area each week. The entry is at the open of the first bar after the Positive Reversal has been confirmed (yellow arrow is pointing at the open/entry point).

Where would you place your stop loss if you wanted to maximize you chances to successfully trade this Positive Reversal?

A. 5 pips SL (stop loss) plus the spread and 1?
B. 11 pips SL (stop loss) plus the spread and 1?
C. 17 pips SL (stop loss) plus the spread and 1?

ANSWER: There is perfect answer but statistically trades with Momentum Type 3 could be placed at any of the locations. Obviously, answer A offers the largest position size but also the greatest risk. Answer B offers a more moderate entry and slightly less risk. This would be more aggressive. Answer C is probably the best answer as strong momentum trades rarely take out the low of the valley bar in a Positive Reversal.