

Tips for Traders | 6/8/2009 10:17:00 AM

How I Set Stops and Profit Targets

The US dollar has been in a freefall against the Canadian dollar. Although I have a long-term core position in this currency pair, I also like to take shorter-term trades. Many traders find it difficult to find entries in strongly trending markets, so I wrote "[How to Catch a Trade in a Vertically-Trending Market](#)" last week to show how to identify a high-probability entry in these types of markets. As I finished the article last week, the position was not closed and I showed several ways to "book" profits, depending on your own trading style. Let me show you how I booked profits in this trade:



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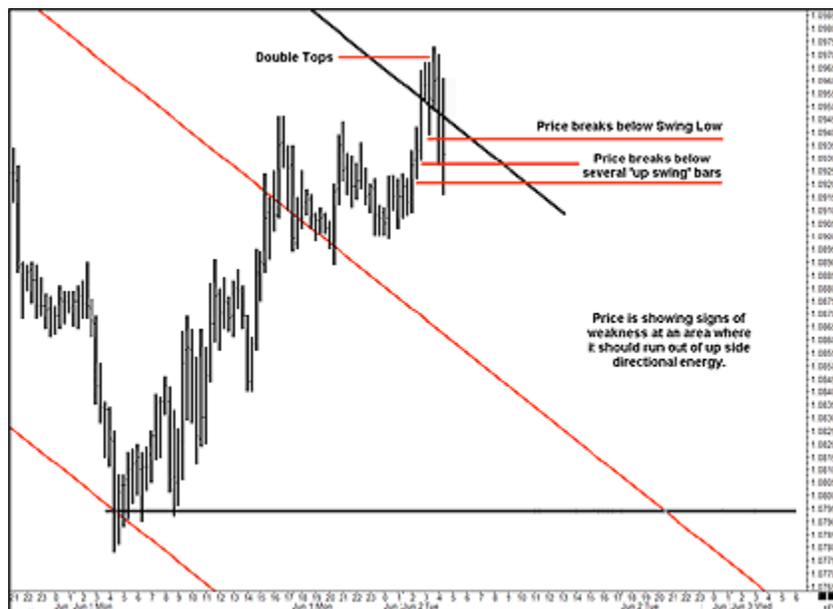
I chose to let my profits run, "boxing in" profits by hiding stop profit orders above each swing high until price finally tested the red, down-sloping Median Line, where I locked in 439 pips of profit. You can view the stop profit orders in part four of "[How to Catch a Trade in a Vertically-Trending Market](#)."

Once I have taken my profits, does the fun end there? Of course not! The market is always moving, and I find that if I am patient and attentive, there are lots of trades that come along. An old mentor of mine once told me that if I could learn to successfully trade the "squiggles" inside a trend, there are times when I would be able to make two, three, four, or even five times the profits I would have made if I had simply sold the top and bought the bottom in a long downtrend (the reverse being the case in an uptrend). Not every trader has the ability or the capital to hold longer-term positions, and it should be mentioned that not every trader has the ability to trade the squiggles either, so each trader should find a style that fits their talents—but that is another article, yet to be written!

While preparing to give my live, pre-market charting session, Market Maps, the next morning, I noticed that the US dollar had rallied against the Canadian dollar to test the same down-sloping sliding parallel that I had used to enter the short US dollar/long Canadian dollar position I had just closed out for such a nice profit. As I continued to get ready for the live session, I kept coming back to the Canadian dollar chart. Price was dancing

around the down-sloping sliding parallel but it hadn't yet shown me any sign of weakness, and until it did, I wasn't interested in entering a trade.

Then price broke below a swing low, as well as several of the upswing bars, and it was beginning to look like I might get another opportunity to ride this same sled lower again. Let me show you what I saw:



One of the concepts I work on over and over in my live morning charting sessions and when I mentor traders is that the market is always right! This sounds incredibly simple, but remember that to be a trader, you have to possess a certain amount of ego. It's easy to feel that if you think price has reached a place where it should turn, it will turn. But the truth is, there are many times when price has a mind of its own and your best-laid plans end up ruined. One way to limit the damage is to let price play its cards before you enter a trade. I mean that if you are looking to go short against a particular line, let price approach that line, dance with that line, and let price show you it is beginning to show weakness before you place your order to get short.

You can see price approached the black, down-sloping sliding parallel and pushed through it a handful of times. But it was having trouble making any further progress above the down-sloping sliding parallel. And after a handful of bars, it began to trade below the sliding parallel. When it broke and closed below the prior swing low, in my mind, price had played its cards and I was ready to try to catch another ride on the slide!

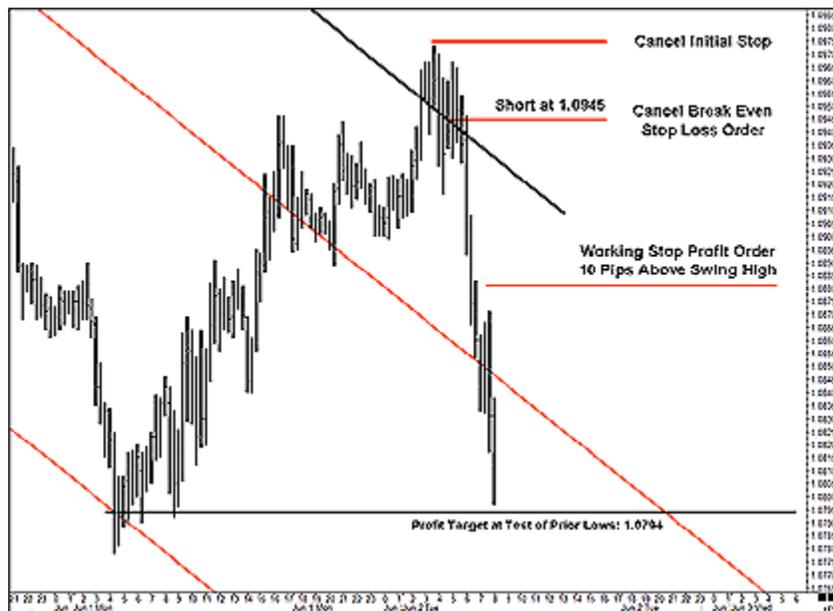


My orders were quite simple:

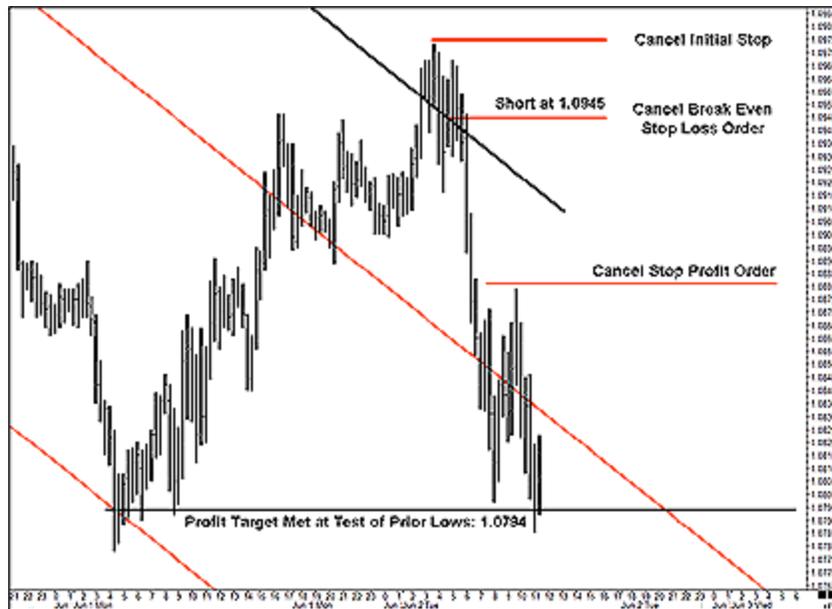
1. I wanted to sell a re-test of the black, down-sloping sliding parallel at 1.0945.
2. My initial stop loss order would be five pips above the recent swing high at 1.0978.
3. If I managed to get short US dollars/long Canadian dollars, I would use a profit target of the prior lows, at 1.0794.

I double checked my math, put my limit sell order and initial stop loss order in the market, and then started my live "Market Maps" charting session.

When I began charting the currencies during the live session, I opened a new 20-minute chart of the Canadian dollar and found that my limit sell order had been executed, getting me short the US dollar against the Canadian dollar at 1.0945. And more important, the trade was going quite well! I still had more than 30 minutes of live charting to present and price was beginning to sell off. I couldn't simply watch my new intraday position while several hundred traders watching live waited for me to move to the next market. I showed the live Internet audience the new position and then while they watched, I cancelled my initial stop loss order and moved my stop order to break even.



After charting commodities and beginning to chart the stock index futures, I told everyone online that I wanted to peek at my new intraday Canadian dollar position. The US dollar had plummeted and the position was near my profit order at 1.0794. I briefly considered just going to the market and taking my profit, but instead, I cancelled my break even order and changed it to a stop profit order ten ticks above the swing high at 1.0881. Then I went back to charting the stock index futures, eager to finish the live charting session and get back to trading! Let's see what the market did while I finished up my charting session:



After I finished my charting session, I pulled up a Canadian dollar chart and found that the US dollar had mounted a nice rally. Price had just missed filling my profit order and had now climbed back against me about 50 pips. I watched as price got closer and closer to my profit stop at 1.0881 and at one point, I was certain my order was going to be filled there. Instead, price came within two pips of my stop profit order, turned on a dime and headed right back down. Four bars later, price re-tested the prior lows and my profit order at 1.0794 was filled for a nice profit of 151 pips.

There are three keys to this trade:

1. There are lots of “squiggles” to catch, even in a near vertically-trending market.
2. Wait for price to play its cards before putting your orders in the market.
3. Hide your stop loss or stop profit order behind prior swing highs or prior swing lows. Once you start using market structure to your advantage, you'll be surprised how many times your stop orders survive by a few pips!

I wish you all good trading!

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