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Momentum Trading Explained

Used For Decades



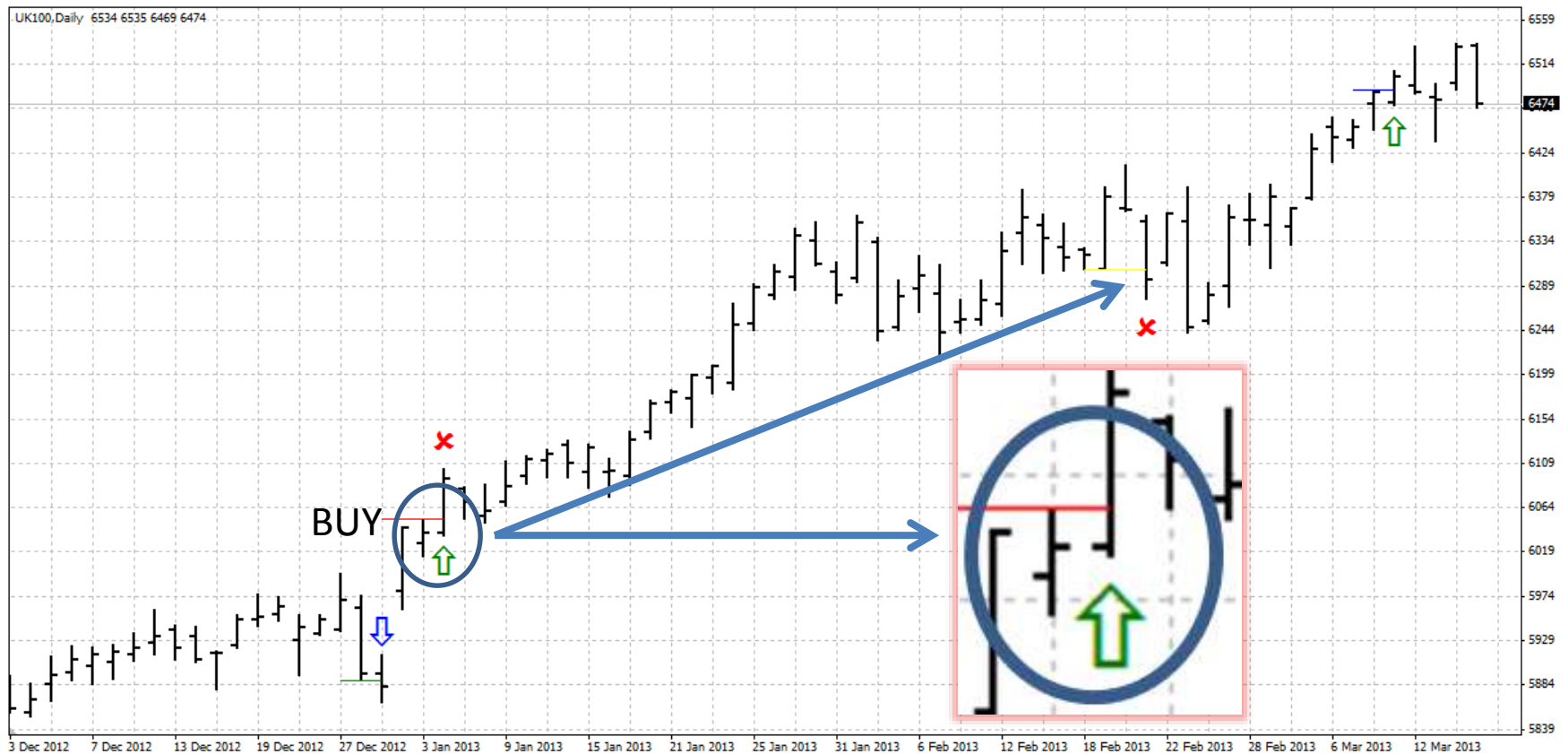
- \$ Bruce Kovner is worth more than \$4.5 billion.
- \$ John W. Henry is worth \$840 million.
- \$ Bill Dunn made \$80 million in 2008.
- \$ Michael Marcus turned an initial \$30,000 into \$80 million.
- \$ David Harding is now worth more than \$690 million.
- \$ Ed Seykota turned \$5,000 into \$15 million over 12 years.
- \$ Kenneth Tropin made \$120 million in 2008.
- \$ Larry Hite has made millions upon millions over 30 years.
- \$ Louis Bacon is worth \$1.5 billion.
- \$ Paul Tudor Jones is worth \$3.3 billion.
- \$ Trend following trader Man Group trades \$68.6 billion in assets.

OHLC bar





How Does Momentum Trading Work: Follow Trends

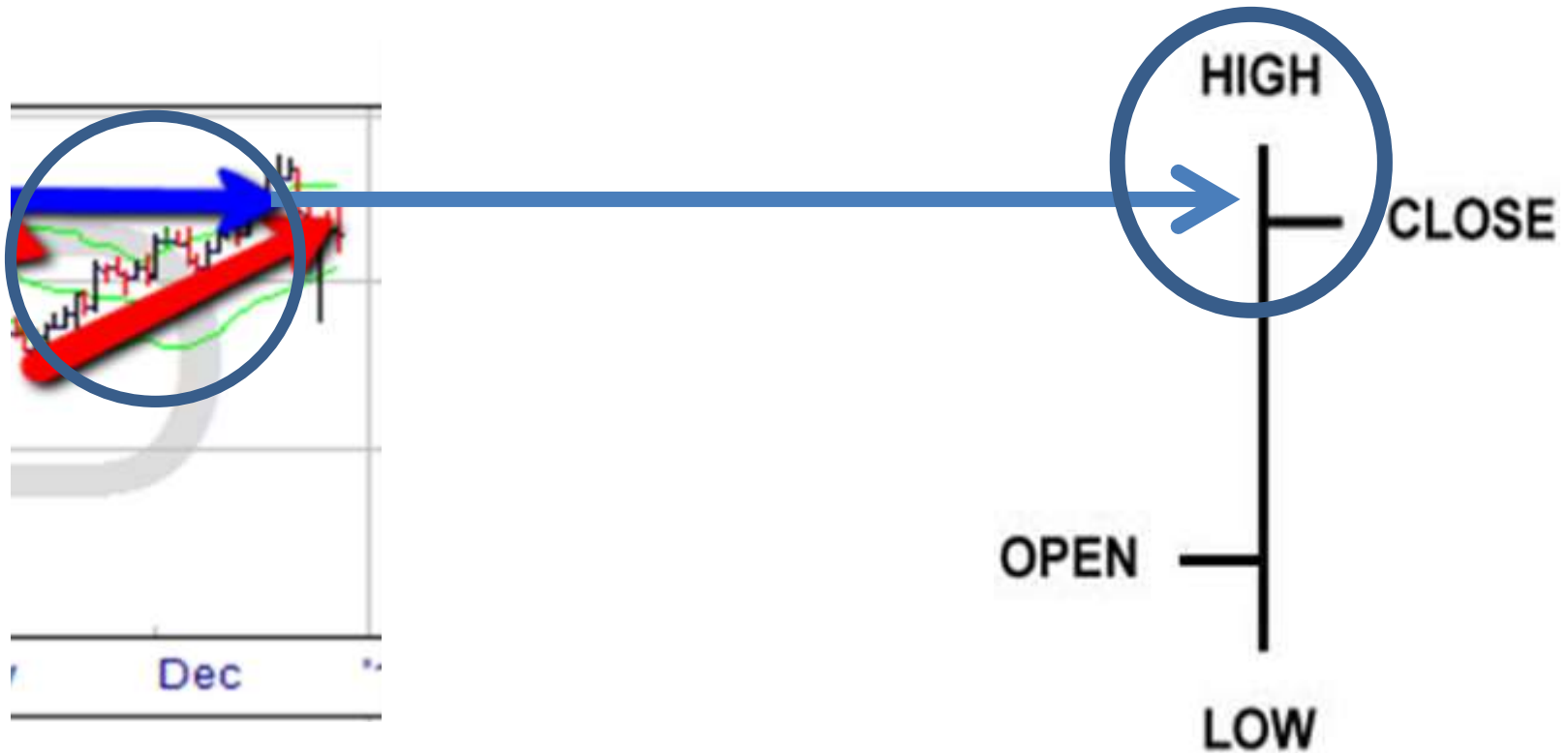




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How Do You Tell Which Direction The Price Will Move

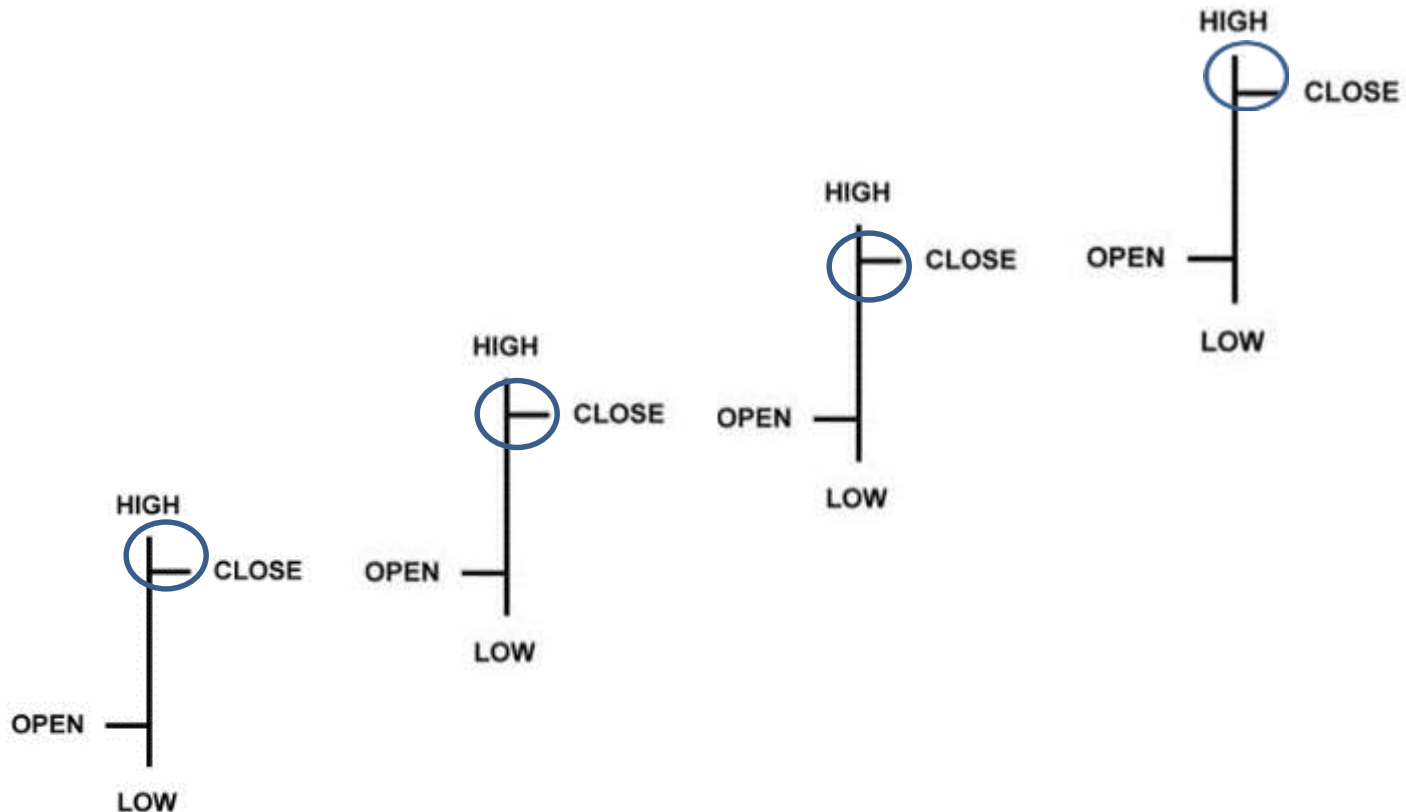




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How To Identify Momentum

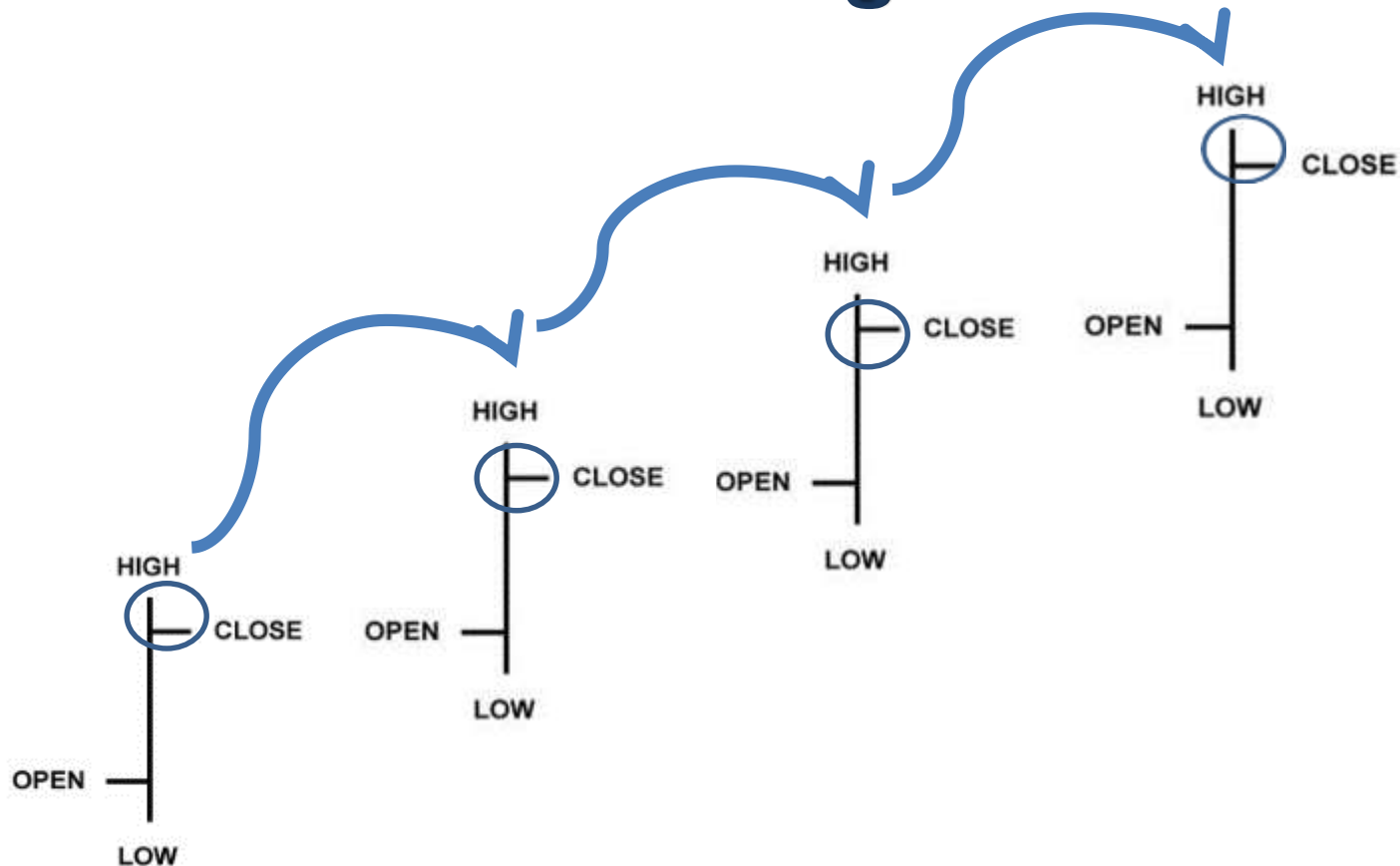




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Higher Price Each Period AND Close Price Near High Each Period

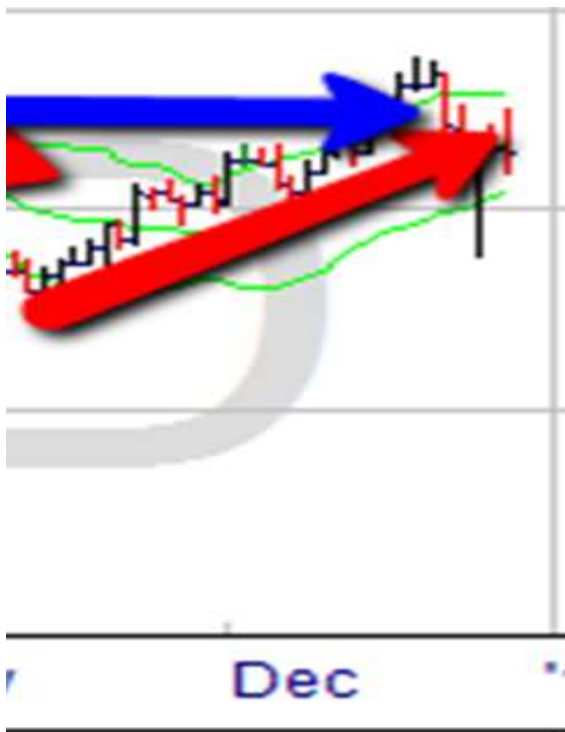




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How To Identify A Stall In Momentum Price Close Near Low (even if rising prices)



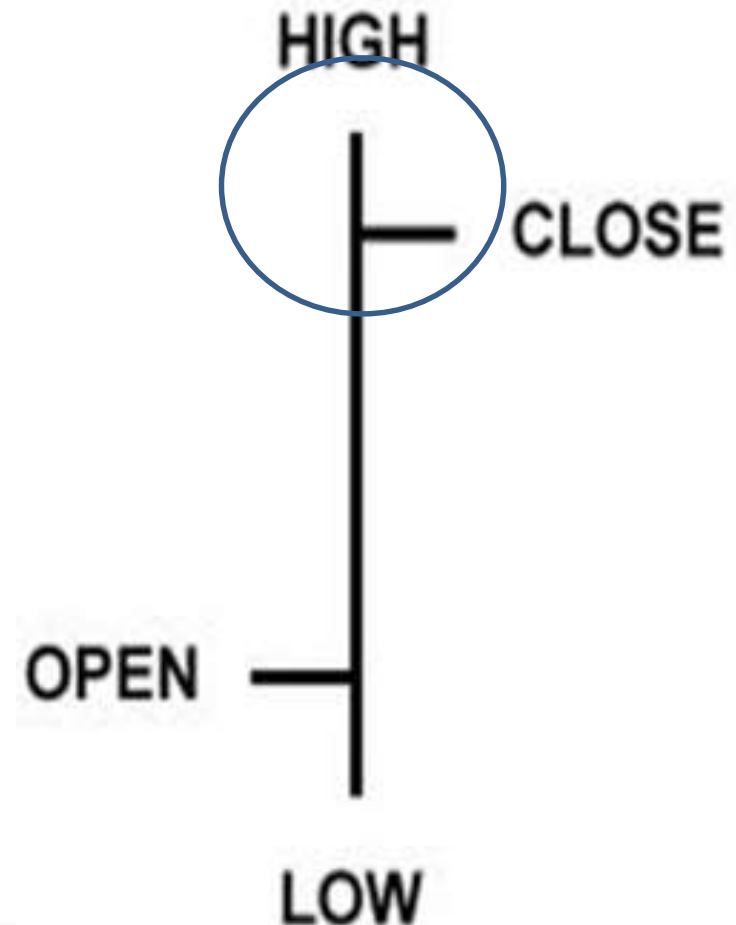


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How To Measure Strength of Momentum

- ✓ Measure how close to the high the price closes that period





How To Calculate Momentum

- ✓ I use 'MACD' indicator (Moving Average Convergence Divergence Indicator)
- ✓ This Measures the Difference Between the 26 period and 12 period average of the price

Exponential Moving Avg = $\text{Price}(t) * k + \text{EMA}(y) * (1 - k)$
 t = today, y = last period, N = number of periods in EMA, $k = 2/(N+1)$

For any given stock or underlying security:

1. Calculate a 12 day EMA of closing prices
2. Calculate a 26 day EMA of closing prices
3. Subtract the longer EMA in (2) from the shorter EMA in (1)
4. Calculate a 9 day EMA of the MACD line gotten in (3)



What is MACD?

- ✓ **M**oving **A**verage **C**onvergence **D**ivergence
- ✓ Measures Momentum, Direction, Trends
- ✓ But I Have Created My Own Modified System



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A Rising MACD Tells Me A Trend Will Continue With Momentum



This Is The MACD Indicator
Starting To Rise Showing The
Price Momentum Will Likely
Rise Too



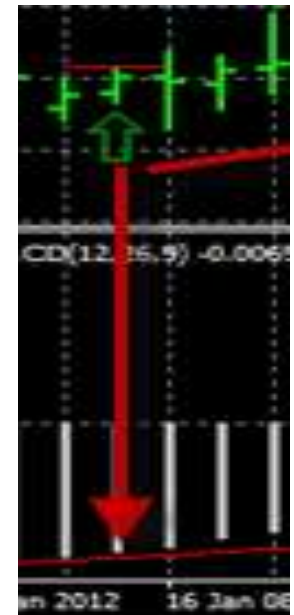
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Buy Signal: Momentum in Place



1. Momentum in this and next time frame is not negative

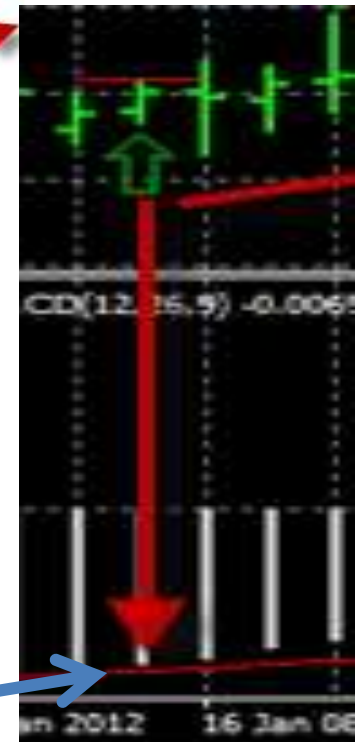




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Identifying Positive Momentum



MACD is not negative in this time frame



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Confirming A Buy Signal



2. Only buy when price in next period moves above high of the past two periods



Past 2 periods

"Next period"



When To Exit A Trade

- ✓ Momentum Lost:
MACD flat or falling
- ✓ Close out half of
position as soon as
price moves below 2
period low (see red
line above pink cross)
- ✓ Close out remaining
half of position at a 3
period low (see red
line above red cross)





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Example 1: Entry



Entry price : \$1.59425 because price moved above 2 period high and momentum in this (hourly) and next time frame (4 hourly) was positive



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Example 1: Exit In Stages



Exit 50%:1.61080 and exit remaining 50% at 1.61265 (ie total at **1.61172** average)



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Example 1: Profit Made

Trade size: \$3,000.
(Leverage of 100:1. \$300,000
\$300,000 x 0.0001)
So each point/pip = \$30

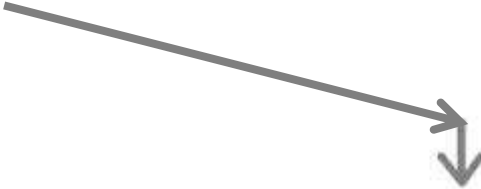
Exit: 1.6117

Entry: 1.5942

Profit = 0.0175 (ie 175 pips)

= 175 x \$30

= \$5250 Profit



1.3100



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Where Other Systems Go Wrong

- A** Their Entry Is Too Late Or Too Early
- B** Their Stop Losses Get Hit Too Often And Cost Too Much
- C** They Do Not Know How To Run Profits



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Where Other Systems Go Wrong 1: Entry



They Signal Buy Too Early or Too Late and So Give You a Loss or Little Profit

Difference between Good Timing & Too Late: 200 pips.

If gbp10 per pip then gbp 2000 opportunity cost



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Why My System Is So Effective

Triple Filtered To Ensure Optimal Entry
(MCQ Filter)

Filter 1: Measures Momentum To Ensure Consistent Positive Buy Signal on Hourly/Daily/Weekly Charts To Give Best Timed Buy Signal

Filter 2: Confirms Momentum Across Multiple Time Frames





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Designed To Minimise Risk of False Entry

*Filter 3: Price Move
Qualifies Trend To
Produce Buy or Sell
Signal*

- 1. Measure*
- 2. Confirm*
- 3. Qualify*



Past 2
periods

"Next
period"



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Where Other Systems Go Wrong 2: Stop Loss



Even after entry, we may still be wrong. So a good system like mine gets us out for a small quick loss, not a big loss, like other systems.