

A Mechanical Trading System For Profit

The 4 Week Rule



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A Forex Trading System for Bigger Long Term Profits

Introduction

Here we are going to look at a simple mechanical trading system which will make sure that you are on the right side of every big trend. It's so simple (just 1 rule) you don't even need a computer to implement it. Everything you need to know about this forex trading system is enclosed in this PDF. The system should be considered by any serious trader, seeking long term consistent profitability from forex markets.

It's made traders around the world huge profits For nearly half a decade, is based on timeless logic and can be used by any trader novice or pro and you don't have to pay for it – it's completely FREE.



The Rise of Forex Robots & Why Most Don't Work

Before we start lets look at other forex trading robots for sale online and the reason most fail is a clue to why the one enclosed works.

There have always been mechanical trading systems sold but the rise of online trading has seen a vast number of vendors selling forex robots, all with fantastic track records on paper which will see you lose if you trade them.

Let's look at why the performance doesn't match the track record.

If you look at any of the forex robots sold online and you see a great track record check for the disclaimer below. You will normally find it in the small print at the end and you need to read it carefully.

"CFTC RULE 4.41 - Hypothetical or simulated performance results have certain limitations. Unlike an actual performance record, simulated results do not represent actual trading. Also, since the trades have not been executed, the results may have under-or-over compensated for the impact, if any, of certain market factors, such as lack of liquidity. Simulated trading programs in general are also subject to the fact that they are designed with the benefit of hindsight. No representation is being made that any account will or is likely to achieve profit or losses similar to those shown".

So there you have it – the track records are made up!

The track records are meaningless simulations done in hindsight KNOWING the closing prices - anyone can do that. Forex trading however is a lot more difficult, we need to trade not knowing the closing prices!

Most of the mechanical systems you see for sale are "curve fitted" i.e. the system rules are bent to fit the data and show a profit.

A trader I once knew likened this to shooting at a barn door with a shotgun and then afterwards getting some chalk and drawing a circle around each one to make it look like a bulls-eye!

Vendors curve fit in many instances knowing the system will never make a profit in real time.

They are just relying on the greed and naivety of the buyer and clever marketing copy to sell the system. In conclusion, the vast amount of systems sold online, the vendor is looking to make a guaranteed profit from the sale of the system and of course doesn't trade it himself – that's why you never see a real time track record.

So the next time you see a mechanical trading system for sale, that looks too good to be true for a few hundred bucks look for the disclaimer above before you buy and save yourself a lot of money.

The Dangers of Curve Fitting

We have looked at curve fitting from the point of someone knowingly doing it - but most systems that are back tested by forex traders are curve fitted in their quest to get the best results without them doing it on purpose. They simply are trying to make the system work as best they can and curve fit without considering the implications

It's tempting to try and get the track record to look its best by adding in extra rules and parameters - but the more complex you make a system (curve fit it) the more chance it will fail in real time trading. No two portions of price data are going to be EXACTLY the same, so if you curve fit too much, the system will break in real time.

Today personal computers have far more number crunching ability than Mission Control Houston which landed man on the moon. This however has not helped but hindered traders in their quest for success – they simply equate complexity with success.

Fact:

50 years ago 95% of trading systems lost today it's the same ratio.

This is despite all the advances in technology which have taken place. Technology and complexity simply leads to curve fitting and losses.

There is no way to beat the market by being clever or complex as many traders believe and it's a fact that:

Simple Systems Work Best!

You don't get paid for being clever in forex markets you get paid for being right with your trading signal. This means a simple, robust forex trading system – this was true 50 years ago and is still true today.

In fact, the trading system we are going to look at below doesn't even require a computer and has been used by savvy traders for nearly 50 years, to produce above average profits. The system was developed by the father of modern trend following Richard Donchian.

Richard Donchian

Richard Donchian was born in Hartford Connecticut in September 1905 over 100 years ago and although the vast majority of traders have never heard of him, he is one of the most influential traders of all time.

Many modern trend following systems, such as the Turtle Trading system, are based on his work and legendary traders such as Richard Dennis and Ed Seykota were inspired by his work and if it's good enough for them, its good enough for us!

Richard Donchian didn't begin trading his successful trend following system until the age of 65. He started making large returns after that and continued to trade until into his 90s! While he operated mostly in the field of commodities his technical analysis is applicable to any market. Here we will look at the 4 week rule which was devised in the late seventies to trade commodity markets and is still popular today.

The 4 Week Rule

The 4 week trading rule system has been at the heart of many successful trading systems and is one of the simplest, easiest and most profitable ways to trade trending markets.



The Rules

The original rules were used for trading commodities and can be summarized by:

- 1) Close short positions and go long whenever the price exceeds the highs of the previous 4 calendar weeks.
- 2) Close long positions and go short whenever the price falls below the lows of the previous 4 calendar weeks.

If run with a SAR (stop and reverse), the above system will always maintain a position in the market (either long or short).

That's it!

The Advantages of the System

It's robust and will put you on the side of ALL the big trends.

The Disadvantages of the System

The market works very well in trending markets - but like most trend following systems, it will have problems when markets consolidate or go sideways. This will of course affect performance and cause drawdown.

Filters

A common solution to this problem is to enter on the 4 week rule (the breakout), and to exit on a shorter time frame such as 1 or 2 weeks.

Traders can also use other exit rules i.e. exit when a moving average is broken. For example, applying a 10-day moving average as the exit - A 10-day moving average is one-half of the entry signal (four weeks is of course 20 trading days), but any time period shorter than the entry signal can be used.

Another use of the system is as a trend filter on the overall market.

The system can objectively tell you if the market is bullish or bearish on a short-term basis. If the market's most recent signal under this system is a buy, the trader can conclude that the market is in an uptrend. Downtrends can be defined as times when the latest 4WR signal was a sell i.e. the market has made a new four-week low more recently than it made a new four-week high.

Using the system as a filter, the trader would look for the 4 Week Rule to be on a buy signal before entering new long positions. Conversely, short positions would only be entered when the market is on a sell signal.

Customization

The 4 Week Rule makes a great addition to any trader's toolbox and can be customized in a number of ways.

Entry and exit signals can be changed and adapted. For example, entering on 4 Week Rule signals but exiting on two-week new lows. As noted, moving averages can also be used to generate exit signals. The system can be combined with indicators, such as the Relative Strength Index (RSI), Average Directional Movement (ADX) or Moving Average Convergence Divergence (MACD) as filters.

The 4 week rule tends to benefit from uncorrelated markets i.e those that do not tend to move together, so when some markets are trading sideways the spread means others are trending, this smoothes the overall equity curve.

You can of course diversify within currencies and trade uncorrelated ones and you could also throw in some other great trending markets (not currencies) for diversification such as, energies and interest rates. You should experiment a little and find out which system produces the best results for you.

Why Most Traders Wont Use it and Why You Should

Despite the fact the system is profitable longer term, most traders won't bother looking at it, or using it for the following reasons:

1. Its to Simple

Today, as we have said - traders feel more comfortable with complicated trading systems and think science can beat the market. As we have said earlier this is not the case - simple systems work best.

2. **Its Not Trendy**

Goes with the above - it's not trendy is it? It's not mystical like Fibonacci and Elliot Wave and it doesn't include complex theories such as - Chaos Theory or Artificial Intelligence. People think these systems can beat the market but more often than not, the market hands them a lesson - an equity wipeout.

3. **Its not Fussy about Market Timing**

Most traders are obsessed with buying market highs or lows (even though prediction is another word for hoping or guessing) and when a price is not considered "the best" by a trader - they wait for the pullback. Of course this system is based on breakouts and is not fussy where it enters, it just wants to be in on the big trends and it will get in on them ALL.

The trader, who sits waiting for a better price, simply misses out on profit.

You are not going to catch tops and bottoms so don't try; if you could catch just 50% of every big trend you would be very rich.

This system is not fussy or clever about its entry levels and doesn't try and predict - it acts on the reality of price change and trades the truth and that's why it makes a lot of money.

Sure, it's not perfect but no system is.

Why You Should Use It.

If you have read and understood this document you will know why already.

1. It's based on timeless logic of breakouts and that markets trend and will continue to do so.
2. It's incredibly simple, with just 1 rule and 1 filter, so it's very robust in the face of brutal ever changing market conditions.
3. Its totally mechanical so trading signals require no subjective judgment
4. It is easy to understand and have confidence in. From confidence, comes discipline - keep in mind, if you don't have the confidence to follow a trading system - you don't have one!
5. You can test it and know real time performance is likely to be in line with a simulation as its so simple, tested performance is a good indication of actual performance. Curve fitting which skews tests is kept to a minimum.

A Simple Powerful System for Profits

This system will appeal to traders who are looking for an automatic trading system, they can understand, have confidence in and follow with discipline. It's also very time efficient, just 15 - 30 minutes a day is all you need to run and trade the system.

So before you buy a mechanical trading system from a vendor with a worthless simulated track record, consider Using the 4 Week Rule. The system is FREE and a simple way to seek profits longer term. As we have seen and can add an extra edge to your trading. Consider incorporating the 4 Week Rule in your forex trading strategy and you may be glad you did.

Best Wishes
Sacha

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