RATH MOVING AVERAGE CROSS STRATEGY
PART 1
by Drew Rathgeber
Rath Moving Average Cross Strategy: Part 1

THE RISK OF LOSS IN TRADING FUTURES CONTRACTS OR COMMODITY OPTIONS CAN BE SUBSTANTIAL. YOU SHOULD CAREFULLY CONSIDER WHETHER SUCH TRADING IS SUITABLE FOR YOU IN LIGHT OF YOUR CIRCUMSTANCES AND FINANCIAL RESOURCES. YOU SHOULD READ THE “RISK DISCLOSURE” WEBPAGE ACCESSED AT WWW.DANIELSTRADING.COM AT THE BOTTOM OF THE HOMEPAGE. DANIELS TRADING IS NOT AFFILIATED WITH NOR DOES IT ENDORSE ANY TRADING SYSTEM, NEWSLETTER OR OTHER SIMILAR SERVICE. DANIELS TRADING DOES NOT GUARANTEE OR VERIFY ANY PERFORMANCE CLAIMS MADE BY SUCH SYSTEMS OR SERVICES.
Rath Moving Average Cross Strategy: Part 1

THE RATH MOVING AVERAGE CROSS STRATEGY - A POWERFUL, YET SIMPLE TRADING TECHNIQUE

Introduction

My opinion is that most day traders tend to over think when trading. They tend to seek out the most complex strategies possible with the expectation that the more rules there are, the more successful they will be. Are you one of those traders who feverishly researched different trading strategies on the internet only to be disappointed?

I feel most trading educators talk in terms that the general public doesn’t easily grasp. All this adds up to more confusion and emotions, the exact thing you don’t want when trading commodity futures markets. Do these complicated, fancy, over-the-top strategies/indicators really work? I doubt it, so I created something so simple even my 11-year-old can understand it.

Psychology of Trading

An obstacle many traders typically don’t consider is the psychology of trading. My goals when using this trading method are to have the trader relax and look at the markets in a simplified way. Furthermore regarding the psychology of trading you must have a plan. The reason for this plan is to identify exactly what and how you will be trading. By creating a plan with the “what” and “why” I believe you also move closer to removing emotion during this process. From there you must discipline yourself to always follow this plan and never emotionally trade.
Rath Moving Average Cross Strategy : Part 1

CHART SET-UP

A Two Step Process

The reason I like Exponential Moving Averages versus other variations is that you have consistency on all charts and in my opinion get the best flow of the markets. I’m not ruling out other moving averages, just based on my experience I like to keep it as simple as possible removing brain clutter.

Step 1

15 Day Exponential Moving Average (EMA)

You will need to open a fresh chart and start preferable on the daily (I’ll explain why later). We will add the 15 day moving average, colored green. (See below)
Rath Moving Average Cross Strategy: Part 1

Step 2

40 Day Exponential Moving Average (EMA)

Repeat the same process as you did to create the 15 day moving average, but make sure it’s a 40 day exponential moving average and colored red. (See below)
Guidance Chart and Trading Charts

Using a Guidance Chart

Now that you have set up the EMA indicator it is important to understand the value of a Guidance Chart. The purpose of the Guidance Chart, as the name suggests is to provide guidance on the potential future trend of the market. The EMA indicator, when applied to the Daily chart (each bar represents one day’s worth of price activity) can give us some clues as to the potential direction of the market. As shown on the image above, you can see the 15 and 40 day EMA’s lines have crossed and are pointing upwards, indicating potential bullish momentum. When the two lines cross and point down, this is a bearish indicator for potentially falling markets. Now that we have established what we believe to be the potential, big-picture trend in the market, we need to sharpen the focus to assist us in determining potential entry and exit points.

To be sure, these are indicators and not purported to be absolute guarantees of market direction.

Trading Chart

Once we have used a Guidance Chart to determine which way the perceived direction of the market is, we need to utilize smaller time frame charts to assist us with entry or exit points. While many components to the strategy lack subjectivity, selecting the best Trading Chart does have room for interpretation. The goal of this process is to take the EMA indicator that you built and apply this to various timeframes in an effort to do two things:

1. Find a chart that exhibits a smooth trend. The following two examples of “Bad” and “Good” charts attempt to illustrate this. Note the large up and down market swings on the “Bad” example. This could suggest that the market is choppy and could be difficult to predict its next move. Remember, we are trying to find something that is moving in a consistent manner in one direction or the other.

2. Find a chart that when the EMA indicator is applied, matches the market direction of the Guidance Chart. For example, should the indicator on the Guidance Chart exhibit indicator lines crossing and pointing upward (bullish signal) we now are trying to find a matching bullish indicator movement on the shorter time-frame, Trading Chart.
Turner Breakout Reversal (TBR)

To begin testing various Trading Charts, begin with a 15 minute chart. Apply the EMA indicators and determine if the trend is smooth and equally important is the trend in the same direction as the MAJOR trend found in the Guidance Chart. If this does not occur, move out to a 30 minute chart. Keeps this same process going with 1 hour, and 4 hour in the effort to meet the two criteria of trend mentioned above.

If you are unable to create a match of Guidance and Trading Chart, then try a different market or wait until such a time that you can get confirmation amongst the charts. In the next section, I will share with you the process of placing an order.

Example of a chart you don’t want to trade:
Rath Moving Average Cross Strategy : Part 1

Example of a chart you want to trade:

Example of a trading chart, higher time frame, smoother intact up trend.
Rath Moving Average Cross Strategy: Part 1

Placing Limit Orders (Entries)

Placing entry orders is a very simple process and I always use limit orders. A limit order is a standing order to buy/sell a specific market at a specific price. When entering the markets using the Rath EMA trading strategy I suggest the following: For aggressive traders I enter on the green (15) day moving average, for more conservative traders, place your order on the red line (40) day moving average. Placing your order on the red (40) day moving average will create less filled orders; therefore you have to exercise patience.

STOP ORDERS DO NOT NECESSARILY LIMIT YOUR LOSS TO THE STOP PRICE BECAUSE STOP ORDERS, IF THE PRICE IS HIT, BECOME MARKET ORDERS AND, DEPENDING ON MARKET CONDITIONS, THE ACTUAL FILL PRICE CAN BE DIFFERENT FROM THE STOP PRICE. IF A MARKET REACHED ITS DAILY PRICE FLUCTUATION LIMIT, A “LIMIT MOVE”, IT MAY BE IMPOSSIBLE TO EXECUTE A STOP LOSS ORDER.
Rath Moving Average Cross Strategy: Part 1

Placing Exit Orders

This can vary dramatically as every account has different capital amounts. For each trade I believe that you should not risk more than 2% of your account, but have a risk/reward ratio of at least 3:1 preferably even a higher at 4:1 or 5:1. One of the shortfalls I see day traders do is they have their risk/reward ratios reversed. You can’t risk $400, to make $100 this will definitely deplete your funds. So for instance if you have a stop loss of $250, try to aim for a profit of $750, minimum.

One strategy you can do to alter the risk reward of an individual trade is to trade using a higher time frame, due to being in the trade for a longer period of time. For example, if you are examining the risk reward of a 15 minute chart and you don’t believe the risk/reward ratio meets the criteria above, seek to look at higher time frames, such as hourly charts.

Here is how you execute a Trading Plan

Below is a recap of what we have covered in terms of rules for my trading strategy as well as some additional points you may wish to consider incorporating into your individual trading plan:

Trading Plan

- EMA Parameters: 15 time Period (Green) / 40 time Period (Red)
- Risk no more than 2% on any given day trade.
- Risk no more than 7% for any given month.
- Trade using buy limits and stop losses.
- Trade no more than 3-5 times per day.
- Place stop loss at breakeven when possible, without being stopped out.
- Trade from highest trending time frame possible.
- Trade (1) contract for every $3,000
Rath Moving Average Cross Strategy : Part 1

Which Markets?

Using the Rath Moving Average Trading Strategy is not just for one market, it can be traded on all futures markets. What I do recommend is focusing on 3-4 markets. Often traders focus on just one market, when they should be identifying the best trend in other markets. In terms of which markets to select, I would recommend using the following criteria:

- High volume/liquid
- Over the last twelve months, the market has exhibited sustained trends
- Ease of connectivity. Especially some foreign futures may meet the above criteria but are difficult to connect to

Once again, we are trading from a picture, so you are looking for the most well defined, intact trend.

Wrap-Up Review

Things I have discussed:

- Focus on 3-4 markets, Emini’s and S&P 500, Euro Dollar, Crude Oil, and Australian Dollar
- Setting up a chart with correct Exponential Moving Average parameters
- Using a Guidance Chart
- Using a Trading Chart
- Trade entries and exits
- Risk vs. reward ratios

To gain proficiency at this method I recommend practicing with a demo account. While you will get even greater insight when you use real funds, using a demo account will allow you to become better at using the various time frames and getting, or not getting confirmations. Here is a link to get a free, two-week demo for the DT Pro futures trading platform:

http://www.danielstrading.com/offers/310/8/
Drew Rathgeber

Drew began his commodity career at one of the nation’s largest physical precious metals dealers in 2003. His passion for understanding the fundamentals and technical analysis of today’s economy gave him the foundation to ultimately make the transition to the futures side of the business with a futures and options broker position at Trade Center, LLC in 2007. With the acquisition of Trade Center, LLC by Daniels Trading in 2011 brings a host of new products and services which are now at Drew’s disposal.

He has hosted many training sessions, webinar, and written numerous articles regarding the commodity futures industry. You can often find him teaching, coaching, and mentoring his clients to help them achieve their trading goals. As he knows every client has different needs so with his years of experience he can quickly identifies these, and creates solid solutions.


**Articles Written by Drew Rathgeber**

1. [Pros and Cons of Trading the E-mini Futures Contract](#)
2. [10 Things You Can Do to Become a Better E-Mini Futures Trader](#)
3. [Crude Oil Futures FAQ](#)
4. [Understanding the Basics of How to Trade E-mini SandP Index](#)
Rath Moving Average Cross Strategy : Part 1

THE RISK OF LOSS IN TRADING FUTURES CONTRACTS OR COMMODITY OPTIONS CAN BE SUBSTANTIAL. YOU SHOULD CAREFULLY CONSIDER WHETHER SUCH TRADING IS SUITABLE FOR YOU IN LIGHT OF YOUR CIRCUMSTANCES AND FINANCIAL RESOURCES. YOU SHOULD READ THE “RISK DISCLOSURE” WEBPAGE ACCESSED AT WWW.DANIELSTRADING.COM AT THE BOTTOM OF THE HOMEPAGE. DANIELS TRADING IS NOT AFFILIATED WITH NOR DOES IT ENDORSE ANY TRADING SYSTEM, NEWSLETTER OR OTHER SIMILAR SERVICE. DANIELS TRADING DOES NOT GUARANTEE OR VERIFY ANY PERFORMANCE CLAIMS MADE BY SUCH SYSTEMS OR SERVICES. STOP ORDERS DO NOT NECESSARILY LIMIT YOUR LOSS TO THE STOP PRICE BECAUSE STOP ORDERS, IF THE PRICE IS HIT, BECOME MARKET ORDERS AND, DEPENDING ON MARKET CONDITIONS, THE ACTUAL FILL PRICE CAN BE DIFFERENT FROM THE STOP PRICE. IF A MARKET REACHED ITS DAILY PRICE FLUCTUATION LIMIT, A “LIMIT MOVE”, IT MAY BE IMPOSSIBLE TO EXECUTE A STOP LOSS ORDER.