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# The **Double** Trend RSI

## - a rules-based trading methodology

Foreign exchange traders have to navigate through trending, retracing, reversing and sideways markets. Currency analyst/trader Doug Schaff developed the Double Trend RSI (DTR) to give traders an accurate picture of market momentum. This indicator combination signals the start of market trends, market reversals and trading ranges. Traders can use the DTR to initiate trades, capture profits and pinpoint price range highs and lows.

**T**rade with the Trend<sup>®</sup> is a fairly standard piece of advice. Yet in order to practically accomplish this, we, as traders, need to gather as much information as we possibly can about the market we are trading.

The Schaff Trend RSI Indicators are used to:

- Measure Trend Strength on a scale between 0 and 100.
- Provide short-term warning that a Trend may be ending.
- Confirm Trend Cycle peaks and bottoms.

The DTR is based on a study of two Schaff Trend RSI Indicators (described below) in concert with Bollinger Bands.<sup>1</sup> The key to using the DTR is to understand how to interpret the interaction of the two Schaff Trend RSI's and the Bollinger Bands.



Chart 1: The Double Trend RSI applied to a 5-minute Euro chart.

|                    |   |
|--------------------|---|
| Upper Chart Panel: | <ul style="list-style-type: none"> <li>&lt; Yellow Bollinger Bands are based on a 50-period moving average.</li> <li>&lt; Green and purple SchaffTC1 Buy and Sell Triggers show trend RSI turns.</li> </ul>   |
| Lower Chart Panel: | <ul style="list-style-type: none"> <li>&lt; A Faster, purple Trend RSI is based on the SchaffTCD RSI(STCDR).</li> <li>&lt; A Longer-term, green, Trend RSI is based on the Schaff Trend RSI (STR).</li> </ul> |

### Schaff Trend RSI™ Indicator (STR)

The longer-term green oscillator in Chart 1 is the Schaff Trend RSI Indicator. It is an advanced RSI study of trend. STR measures the strength of a MACD measure of trend against its own past performance. Instead of price, the STR takes as its input the difference in two exponential moving averages (also known as a MACD Line).

The Schaff Trend RSI uses three inputs:

1. MA1 Period: Shorter-term Exponential Moving Average. DTR: 100.
2. MA2 Period: Longer-term Exponential Moving Average. DTR: 115.
3. RSI Period: Price bars used to calculate the RSI value. DTR: 9.

### Schaff TCD RSI™ Indicator (STCDR)<sup>1</sup>

The faster purple oscillator in Chart 1 is the Schaff TCD RSI™. It takes as its input a detrended measure of the difference in two exponential moving averages (a MACD Line). The MACD Line is run first through a detrended price oscillator, and then through the RSI; the result is the STCDR.

The SchaffTCD RSI uses four inputs:

1. MA1 Period: Shorter-term Exponential Moving Average. DTR: 100.
2. MA2 Period: Longer-term Exponential Moving Average. DTR: 115.
3. Period Len: Periods used to calculate the moving average of MA1-MA2. Often set at half the presumed cycle length. DTR: 10.
4. RSI Period: Price bars used to calculate the RSI value. DTR: 3.

Dotted lines are drawn at 20 and 80 in the lower chart panels. A rise above the buy line or break below the sell line of the Trend RSI alerts traders to potential changes in Trend.

| Schaff Trend RSI Inputs on the 5-minute Chart   |                          |                   |
|---|--------------------------|-------------------|
| Schaff Trend RSI (STR) -                        | Schaff TCD RSI (STCDR) - | Bollinger Bands - |
| 100, 115, 9                                     | 100, 115, 10, 3          | 50, 2, SMA        |
| Optional: Schaff TC1 Trigger - 20, 100, 115, 10 |                          |                   |

### Using Bollinger Bands with the Double Trend RSI



Bollinger Bands indicate trending versus retracement or range trading markets.

#### Background:

Bollinger Bands are plotted at standard deviation levels above and below a moving average.

In high volatility trending periods the Bands expand

In low volatility, sideways markets the Bands contract.

The 5-minute Bollinger Bands are based on a Simple Moving Average (SMA) and have two inputs:

1. MA Period = 50
2. Std. Deviations = 2

Note: Prices touching the Upper or Lower Bands should not be used as Buy or Sell signals.

### A Rules-Based Approach

The Double Trend RSI has five main readings:

- Long Position
- Long Reversal
- Short Position
- Short Reversal
- Consolidating

The position of the two Trend RSI indicators, relative to the Bollinger Bands will tell you what the market is doing, and therefore what position to take.

### Long Position

| Longer-Term RSI           | Faster RSI                       | Bollinger Bands -          |
|---------------------------|----------------------------------|----------------------------|
| Rising or Steady near 100 | Rising or Turns up below 20-line | Widening Upper Band Rising |

### Short Position

| Longer-Term RSI          | Faster RSI                        | Bollinger Bands -          |
|--------------------------|-----------------------------------|----------------------------|
| Falling or Steady near 0 | Falling or Turns up below 80-line | Widening Lower Band Rising |

### Consolidating

| Bollinger Bands -               |
|---------------------------------|
| 1. Retracement: Narrowing or    |
| 2. Range: Steady and Horizontal |

### Long Reversal

| Longer-Term RSI           | Faster RSI                                      | Bollinger Bands - |
|---------------------------|---|-------------------|
| Rising or Steady near 100 | Turn down above 80-line and Prices follow Lower | Begin to Narrow   |

### Short Reversal

| Longer-Term RSI          | Faster RSI                                      | Bollinger Bands - |
|--------------------------|---|-------------------|
| Falling or Steady near 0 | Turn down above 20-line and Prices follow Lower | Begin to Narrow   |

Let us take a look at a couple of historical case studies to see how the Double Trend RSI follows and anticipates price action.

### Going "Long" using the Schaff Double Trend RSI



Chart 2: The Double Trend RSI highlights two buy-points in the 30-minute USD/JPY chart.

Monday, August 5<sup>th</sup>. Tokyo and Europe sold the Dollar down to near 118.60, where it had held, and then rallied to the 119.40 area.

At 7:00<sup>h</sup>, the Dollar-Yen was back down at 119.00, which was also the lower end of last week's trading range.

Which way would this market break? Always a big question in the Forex markets on Monday morning. The Faster Trend RSI on the 30-minute chart (Chart 2) had followed the market down from the day's high, then leveled out while the market traded sideways.

At 11:00 the Faster RSI turned up from below the 20-line. The green Longer-term RSI was also rising. This is a time to buy. The market was at 119.07.

The upmove got going and both Schaff Trend RSI's rose to 100 and stuck there as Dollar-Yen prices followed the Upper Bollinger Band higher.

In early evening the Faster purple RSI turned down. Dollar-Yen was at 119.65. But prices did not follow lower, so there was no reason to sell.



Chart 3: After following prices higher, both Schaff Trend RSI's turned down, indicating sideways and, eventually, weaker USD/JPY prices.

The Dollar-Yen hit a high of 121.01 early Tuesday before upward momentum slowed. Prices closed inside the Upper Bollinger Band and the Faster Trend RSI turned down from above the 80-line (Chart 3). Dollar-Yen was 120.72.

If prices follow lower, this is a reversal signal, even an early sell signal if the longer-term trend is bearish. The close on the next 30-minute bar was 120.60, so exit the long position there. Result: a profit of 1.53 yen (120.60 - 119.07).

Of course, the market took off right after that, to make a new high at 121.24. Well, I cannot remember that last time I sold at the high. Still it takes a structured trading methodology (and some profits!) to keep me from trying.

The market wound up trading sideways, forming a wedge with the 120.60 area as its base. It was not until 2:00 on Wednesday, August 7<sup>th</sup>, that the green Longer-term RSI turned down on the 30-minute chart. Dollar-Yen was 120.72.

That is early morning for me, so I was asleep. But the pattern indicated the possibility of a good correction lower. And traders (who were awake) could have sold the USD/JPY there, and placed an initial stop loss above the previous day's high or above the descending wedge-line (not shown).

Bearish momentum increased and the Dollar-Yen reached and broke the Lower Bollinger Band, trading down to 120.08 before the Faster RSI turned up.

### Using the DTR in Multiple Timeframes ... to target High-Probability Currency Trades

Double Trend RSI signals on the 30-minute chart work pretty well. After entering long or short positions with it, however, the market often pulls back 20 to 40 points before it moves in the direction of the signal. I could not help wondering if there was a way to use a 5-minute chart to minimize this "pullback" phenomenon.

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After all, every trend sits within a larger trend that influences it. Price momentum in the daily chart affects trends in the hourly chart. Similarly, trends in the 30-minute chart affect price behavior in the 5-minute chart. Knowing the direction of prices in the 30-minute chart gives a context for what to expect of trends in the 5-minute. In this sense two trends are better than one.

The idea is that signals in the 30-minute chart provide the market direction. While signals in the 5-minute chart provide the timing of trade entries and exits. The key assumption here is that, until the 30-minute trend reverses, corrections, tracked in the 5-minute chart, will resolve themselves in the direction of the bullish 30-minute chart. In my experience, this is always a good working assumption. Let the market tell you when a trend is over; guessing can be hazardous to your trading capital.

Using this approach, apply the following trading rules:

1. 30-Minute Bullish and 5-Minute Bullish  
Go long with buy signals in the 5-minute chart.
2. 30-Minute Bullish and 5-Minute Bearish  
Exit long positions with 5-minute sell signals.

#### Adding Triggers to the Double Trend RSI

The SchaffTC1 indicator has been added to the 5-minute charts below. It serves to highlight prices bars where market momentum may be shifting. Similar to the faster TCD RSI, the SchaffTC1 is also based on a detrended measure of a MACD Line.<sup>4</sup>

On a 5-minute chart you need two closes above the high of a setup bar to initiate a long position. You need two closes below the low of a setup bar to initiate a short position.<sup>5</sup>

#### Study Results: 30-Minute Trend / 5-Minute Timing

| Trade#  | Time         | Double Trend RSI Reading                             | Buy/Sell Action     | P/L Result    |
|---------|--------------|--|---------------------|---------------|
| 1 entry | 8/5<br>11:00 | 5-minute buy trigger and 30-minute fast RSI turns up | Go Long at 119.13   |               |
| 1 exit  | 15:40        | 5-minute sell trigger                                | Exit Long at 119.64 | 51 pip profit |

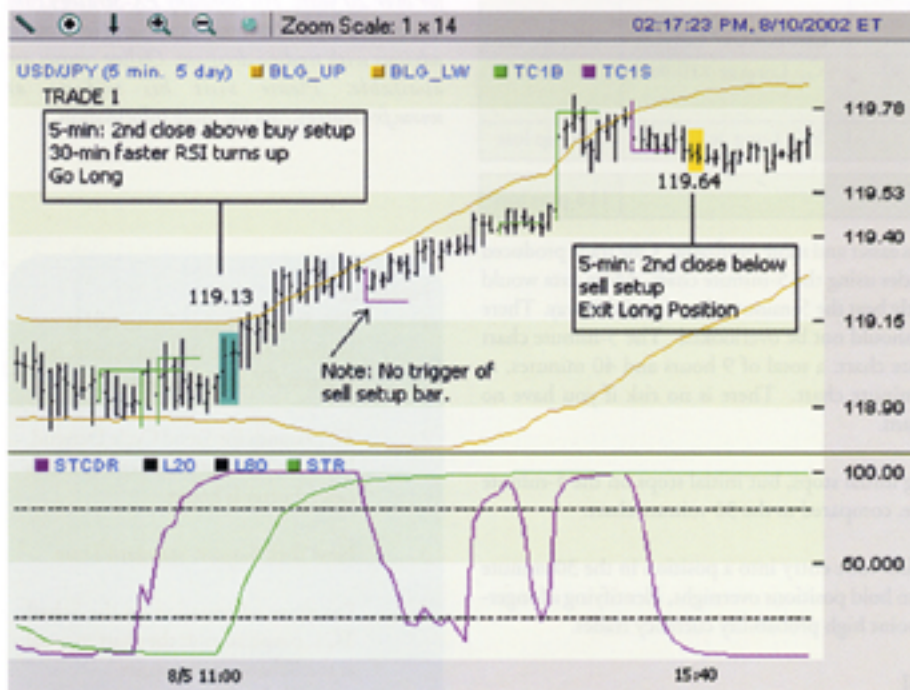


Chart 4: Intermediate corrections in the 30-minute uptrend provide low-risk buying opportunities, as identified by the Double Trend RSI in the 5-minute chart.

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U S A

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Knowing the bigger picture gives a trader more confidence of what to expect in the trading timeframe. For instance, while the faster RSI in the 30-minute chart is falling, do not take 5-minute buy signals. There was no position for 8 hours and 20 minutes, from 15:40 until midnight. That was the next time the 30-minute Double Trend RSI became bullish. Here are the details of the next two long positions

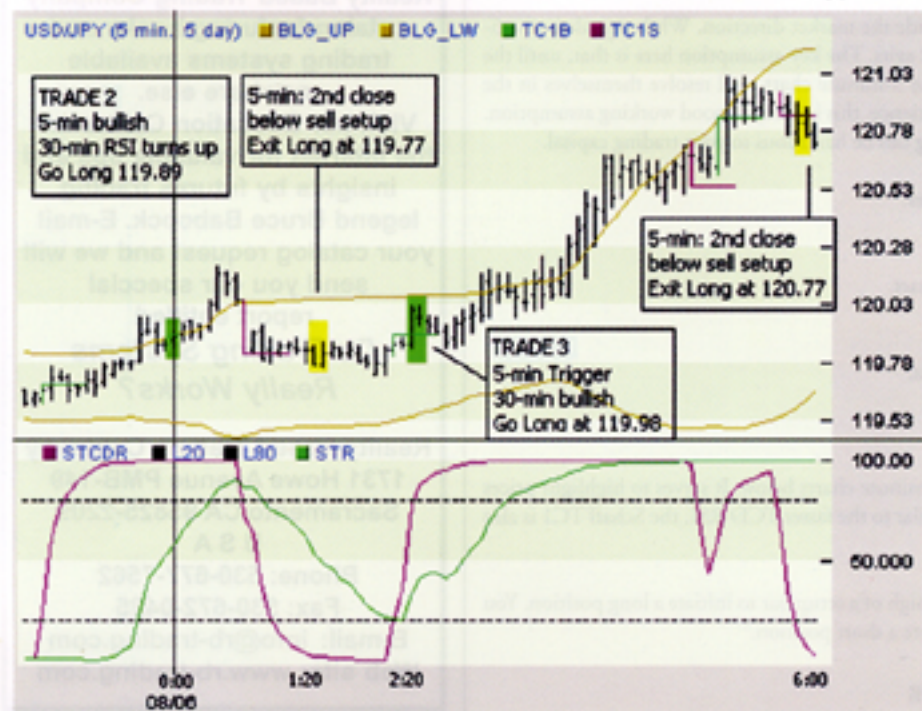


Chart 6 shows how to use the Double Trend RSI in the USD/JPY 5-minute chart to buy into an uptrend in the 30-minute timeframe.

| Trade#               | Time            | Double Trend RSI Reading                         | Buy/Sell Action     | P/L Result    |
|----------------------|-----------------|--|---------------------|---------------|
| 2 entry              | 8/6<br>Midnight | 5-minute bullish and 30-minute fast RSI turns up | Go Long at 119.89   |               |
| 2 exit               | 1:20            | 5-minute sell trigger                            | Exit Long at 119.77 | -12 pip loss  |
| 3 entry              | 2:20            | 5-minute buy trigger and 30-minute bullish       | Go Long at 119.98   |               |
| 3 exit               |                 | 5-minute sell trigger                            | Exit Long at 120.77 | 79 pip loss   |
| Total P/L - 3 trades |                 |  |                     | 118 pips loss |

Taking a position using the straight 30-minute chart was easier and more profitable. One trade produced a 1.51 Yen profit, as compared to 1.18 Yen in three trades using the 5-minute chart. More data would be needed to find out if the 30-minute chart consistently beat the 5-minute chart, used this way. There are benefits to using the 5-minute chart though that should not be overlooked. The 5-minute chart had positions less than half the time of the 30-minute chart: a total of 9 hours and 40 minutes, as compared to 22 hours and 30 minutes for the 30-minute chart. There is no risk if you have no position, so the 5-minute chart is less risky in this regard.

It is beyond the scope of this article to discuss placing initial stops, but initial stops on the 5-minute chart would generally be closer to the trade entry price, compared to the 30-minute chart.

A practical benefit of using the 5-minute chart is to fine-tune entry into a position in the 30-minute trend. Also, for short-term FX traders who prefer not to hold positions overnight, identifying a longer-term context for their short-term trades can help pinpoint high probability currency trades.

#### Making Currency Trades with the Double Trend RSI

The Double Trend RSI offers traders a structured trading methodology, applicable in any timeframe, to take positions in trending currency markets, control risk and hold onto winners until price momentum shifts. This tool is useful in all major currency markets, more so in the volatile currency pairs, such as

USD/CHF, EUR/USD, USD/JPY, AUD/USD, and less so in the more stable currencies, such as EUR/CHF or, at times, EUR/GBP and EUR/JPY.

Traders are encouraged to practice the methods described before using them as a trading tool. A mistake made with RSI's generally, and Trend RSI's are no exception, is to rely on them for overbought and oversold levels. Trying to determine when a trend is "overbought" or "oversold" can be a frustrating if not futile experience. It is a much safer proposition to buy into a market after a longer-term Trend RSI has "bottomed" and begun to move up, or after it has "topped" and begun to move down.

The DTR can be used on a single chart or within a multiple timeframes approach. Currency prices normally rise and fall numerous times within a trend. The DTR can be used to identify the start of intermediate trends in the direction of a trend of longer duration. For example, intermediate corrections in the 30-minute trends, as uncovered with a 5-minute DTR, can identify low-risk trading opportunities in the direction of the longer trend.

SchaffChart can be set up to automatically open the Double Trend RSI on multiple charts of your choice. This live charting service offers a complete set of Trend RSI's, Trend Cycle indicators and triggers. All *Chartpoint* readers are welcome to test it out, for free, at [www.fx-strategy.com](http://www.fx-strategy.com).

The author, Doug Schaff has traded the FX markets for over 20 years. His company *FX-Strategy.com* was created to assist currency traders and investment advisors with trading decisions. Online courses are available. Please visit his website at [www.fx-strategy.com](http://www.fx-strategy.com) for more information.

#### Footnotes:

- 1 The Schaff Double Trend RSI is available, for free trial, on SchaffChart at [www.FX-Strategy.com](http://www.FX-Strategy.com).
- 2 TCD stands for Trend Cycle Detrend. I like clear indicator names but in this case, shorter is better.
- 3 New York Eastern Standard Time
- 4 For more information on the Schaff TC1, please consult the chart manual at the SchaffChart website.
- 5 Closes need not be consecutive for either buys or sells.