

## The Path to Trading Success

# Part 9: Combining Everything to Create a Strategy and Checklist

In this article the author is going to take the price action analysis he discussed in the previous three articles (TRADERS' 02, 03 and 04/2013) and combine them together in order to demonstrate how you can create a simple strategy and checklist.

## » What Constitutes a Trading Strategy?

A trading strategy must have three components: 1) Entry criteria, 2) Risk Management and 3) Trade Management. We will cover risk and trade management in the next article so for now let's focus on entry criteria only.

This is how your strategy should look:

1. Contain between eight and 20 technical ingredients. Less than eight and your strategy risks being too simple, more than 20 and your strategy risks becoming overcomplicated.
2. Are written down in a checklist format so it will never be forgotten and can be flawlessly applied consistently.
3. The checklist is divided into essential factors and bonus factors.
4. The essential factors are all of those technical factors which must be present in order for a setup to be valid. If even one of the essential factors is missing then there is no valid trade setup.

5. The bonus factors are those technical ingredients which are 'nice to have' but not essential. If they are present then that's great as it will increase the probability of the trade being successful. However, if they aren't present then it won't prevent us from entering a trade provided all the essential factors are met. Bonus factors will also allow us to rank all potential setups in the order of highest to lowest probability. With everything else being equal, the setup which meets all the essential factors and the most bonus factors will have the highest probability of success.

## Creating a Simple Trading Strategy

The author will now use some of the price action analysis he has discussed in this series to demonstrate how a trading strategy can be created. Then he will demonstrate how that strategy can be improved by implementing the use of essential and bonus factors into the strategy checklist.

Let's take for example the popular strategy of trading breaks of support or resistance. The following simple checklist could be created for this strategy:

1. Trade only in the same direction as the trend.
2. Look for a flat level of support or resistance (defined by a price level which has been tested a minimum of three times).
3. The next higher time frame chart is also trending in the same direction as the trade setup.



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- Ensure price and indicators converge on the break.
- Enter one tick above (long) or one tick below (short) of flat level.
- Price has tested the flat level 4 or more times.

The next step in strategy development is to classify each of the factors as either an essential or bonus factor. One such way that exercise could be undertaken is:

#### Essential factors:

- Trade only in the same direction as the trend.
- Look for a flat level of support or resistance (defined by a price level which has been tested a minimum of three times).
- Ensure price and indicators converge on the break.
- Enter one tick above (long) or one tick below (short) of flat level.

#### Bonus factors:

- Price has tested the flat level four or more times.
- The next higher time frame chart is also trending in the same direction as the trade setup.

Remember each and every one of the essential factors must be present in order for there to be a valid setup. Whereas the bonus factors are used to rank all of the valid setups from highest to lowest probability of success (provided everything else about the set up is equal).

#### Improving the Strategy

Hopefully you have noticed that the strategy is currently only comprised of six technical factors. As the author mentioned earlier in this article it is optimal to have between eight and 20 technical factors for each strategy. Consequently, one simple way to improve the success of this strategy would be to add additional essential and bonus factors.

#### F1) Essential Factors



All four of the essential factors for this breakout strategy are present therefore it's a valid setup.

Quelle: www.tradestation.com

#### Conclusion

Having a strategy which contains too few technical factors and isn't written into a checklist format are often two of the major reasons why traders aren't as successful as they would like to be. In this article we have demonstrated how any trader can easily implement both of these simple techniques into their own trading.

#### Next Month

In the next article the author will discuss the last two remaining components of a trading strategy; risk and trade management. «

#### F2) Bonus Factors



Both of the bonus factors for this breakout strategy are also present therefore it would have a higher probability of success than a similar set up which only has one or none of the bonus factors.

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