

The five-minute momo trade looks for a momentum or "momo" burst on very short-term (five-minute) charts. First, traders lay on two indicators, the first of which is the 20-period exponential moving average (EMA). The EMA is chosen over the simple moving average because it places higher weight on recent movements, which is needed for fast momentum trades. The moving average is used to help determine the trend. The second indicator to use is the moving average convergence divergence (MACD) histogram, which helps us gauge momentum. The settings for the MACD histogram is the default, which is first EMA = 12, second EMA = 26, signal EMA = 9, all using the close price. (For more insight, read *A Primer On The MACD*.)

This strategy waits for a reversal trade but only takes advantage of it when momentum supports the reversal move enough to create a larger extension burst. The position is exited in two separate segments; the first half helps us lock in gains and ensures that we never turn a winner into a loser. The second half lets us attempt to catch what could become a very large move with no risk because the stop has already been moved to breakeven.

Rules for a Long Trade

1. Look for currency pair trading below the 20-period EMA and MACD to be negative.
2. Wait for price to cross above the 20-period EMA, then make sure that MACD is either in the process of crossing from negative to positive or has crossed into positive territory no longer than five bars ago.
3. Go long 10 pips above the 20-period EMA.
4. For an aggressive trade, place a stop at the swing low on the five-minute chart. For a conservative

trade, place a stop 20 pips below the 20-period EMA.

5. Sell half of the position at entry plus the amount risked; move the stop on the second half to breakeven.
6. Trail the stop by breakeven or the 20-period EMA minus 15 pips, whichever is higher.

Rules for a Short Trade

1. Look for the currency pair to be trading above the 20-period EMA and for MACD to be positive.
2. Wait for the price to cross below the 20-period EMA; make sure that MACD is either in the process of crossing from positive to negative or has crossed into negative territory within the past five bars.
3. Go short 10 pips below the 20-period EMA.
4. For an aggressive trade, place a stop at the swing high on a five-minute chart. For a conservative trade, place the stop 20 pips above the 20-period EMA
5. Buy back half of the position at entry minus the amount risked and move the stop on the second half to breakeven.
6. Trail the stop by breakeven or the 20-period EMA plus 15 pips, whichever is lower.

Long Trades

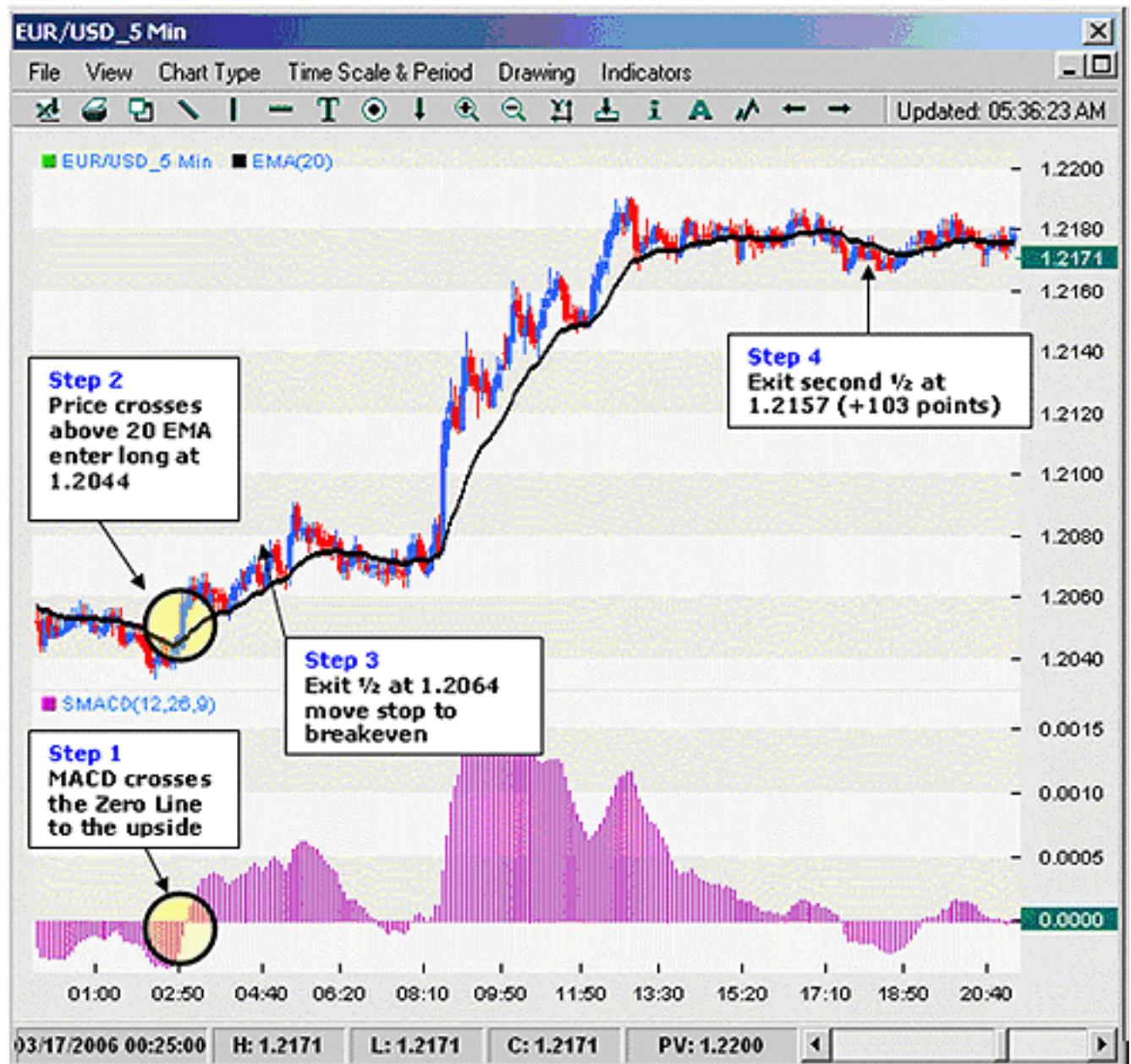


Figure 1: Five-Minute Momo Trade, EUR/USD

Source: FXtrek Intellichart

Our first example in Figure 1 is the EUR/USD on March 16, 2006, when we see the price move above the 20-period EMA as the MACD histogram crosses above the zero line. Although there were a few instances of the

price attempting to move above the 20-period EMA between 1:30 and 2am EST, a trade was not triggered at that time because the MACD histogram was below the zero line.

We waited for the MACD histogram to cross the zero line and when it did, the trade was triggered at 1.2044. We enter at $1.2046 + 10 \text{ pips} = 1.2056$ with a stop at $1.2046 - 20 \text{ pips} = 1.2026$. Our first target was $1.2056 + 30 \text{ pips} = 1.2084$. It was triggered approximately two and a half hours later. We exit half of the position and trail the remaining half by the 20-period EMA minus 15 pips. The second half is eventually closed at 1.2157 at 9:35pm EST for a total profit on the trade of 65.5 pips.

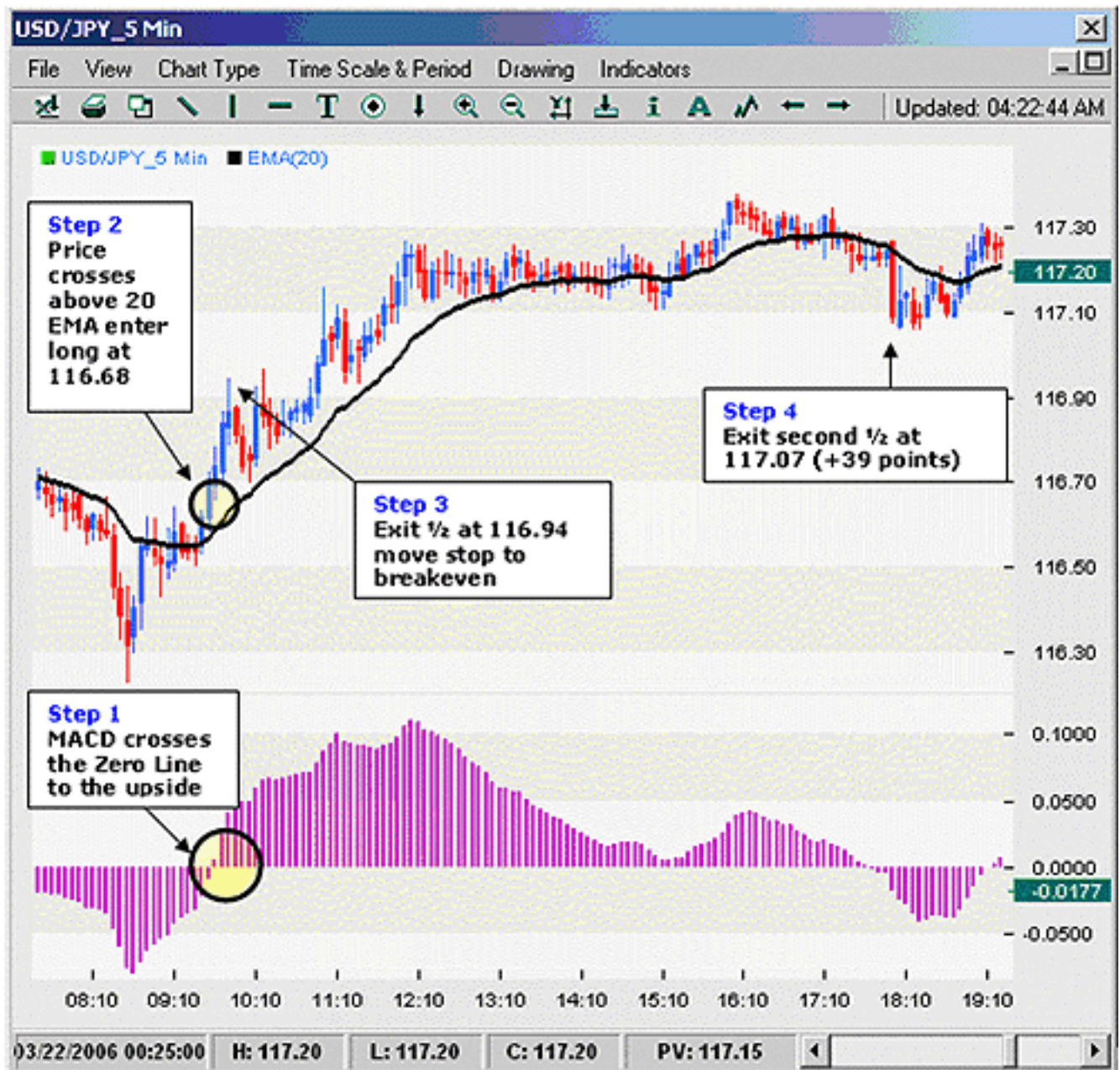


Figure 2: Five-Minute Momo Trade, USD/JPY
Source: FXtrek Intellichart

The next example, shown in Figure 2, is USD/JPY on March 21, 2006, when we see the price move above the 20-period EMA. Like in the previous EUR/USD example, there were also a few instances in which the price crossed above the 20-period EMA right before our entry point, but we did not take the trade because the MACD

histogram was below the zero line.

The MACD turned first, so we waited for the price to cross the EMA by 10 pips and when it did, we entered the trade at 116.67 (EMA was at 116.57).

The math is a bit more complicated on this one. The stop is at the 20-EMA minus 20 pips or $116.57 - 20 \text{ pips} = 116.37$. The first target is entry plus the amount risked, or $116.67 + (116.67 - 116.37) = 116.97$. It gets triggered five minutes later. We exit half of the position and trail the remaining half by the 20-period EMA minus 15 pips. The second half is eventually closed at 117.07 at 6am EST for a total average profit on the trade of 35 pips. Although the profit was not as attractive as the first trade, the chart shows a clean and smooth move that indicates that price action conformed well to our rules.

Short Trades

On the short side, our first example is the NZD/USD on March 20, 2006 (Figure 3). We see the price cross below the 20-period EMA, but the MACD histogram is still positive, so we wait for it to cross below the zero line 25 minutes later. Our trade is then triggered at 0.6294. Like the earlier USD/JPY example, the math is a bit messy on this one because the cross of the moving average did not occur at the same time as when MACD moved below the zero line like it did in our first EUR/USD example. As a result, we enter at 0.6294.

Our stop is the 20-EMA plus 20 pips. At the time, the 20-EMA was at 0.6301, so that puts our entry at 0.6291 and our stop at $0.6301 + 20 \text{ pips} = 0.6321$. Our first target is the entry price minus the amount risked, or

$0.6291 - (0.6321 - 0.6291) = 0.6261$. The target is hit two hours later and the stop on the second half is moved to breakeven. We then proceed to trail the second half of the position by the 20-period EMA plus 15 pips. The second half is then closed at 0.6262 at 7:10am EST for a total profit on the trade of 29.5 pips.



Figure 3: Five-Minute Momo Trade, NZD/USD
 Source: FXtrek Intellichart

The example in Figure 4 is based on an opportunity that developed on March 10, 2006, in the GBP/USD. In the chart below, the price crosses below the 20-period EMA and we wait for 10 minutes for the MACD histogram to move into negative territory, thereby triggering our entry order at 1.7375. Based on the rules above, as soon as the trade is triggered, we put our stop at the 20-EMA plus 20 pips or $1.7385 + 20 = 1.7405$. Our first target is the entry price minus the amount risked, or $1.7375 - (1.7405 - 1.7375) = 1.7345$. It gets triggered shortly thereafter. We then proceed to trail the second half of the position by the 20-period EMA plus 15 pips. The second half of the position is eventually closed at 1.7268 at 2:35pm EST for a total profit on the trade of 68.5 pips. Coincidentally enough, the trade was also closed at the exact moment when the MACD histogram flipped into positive territory.

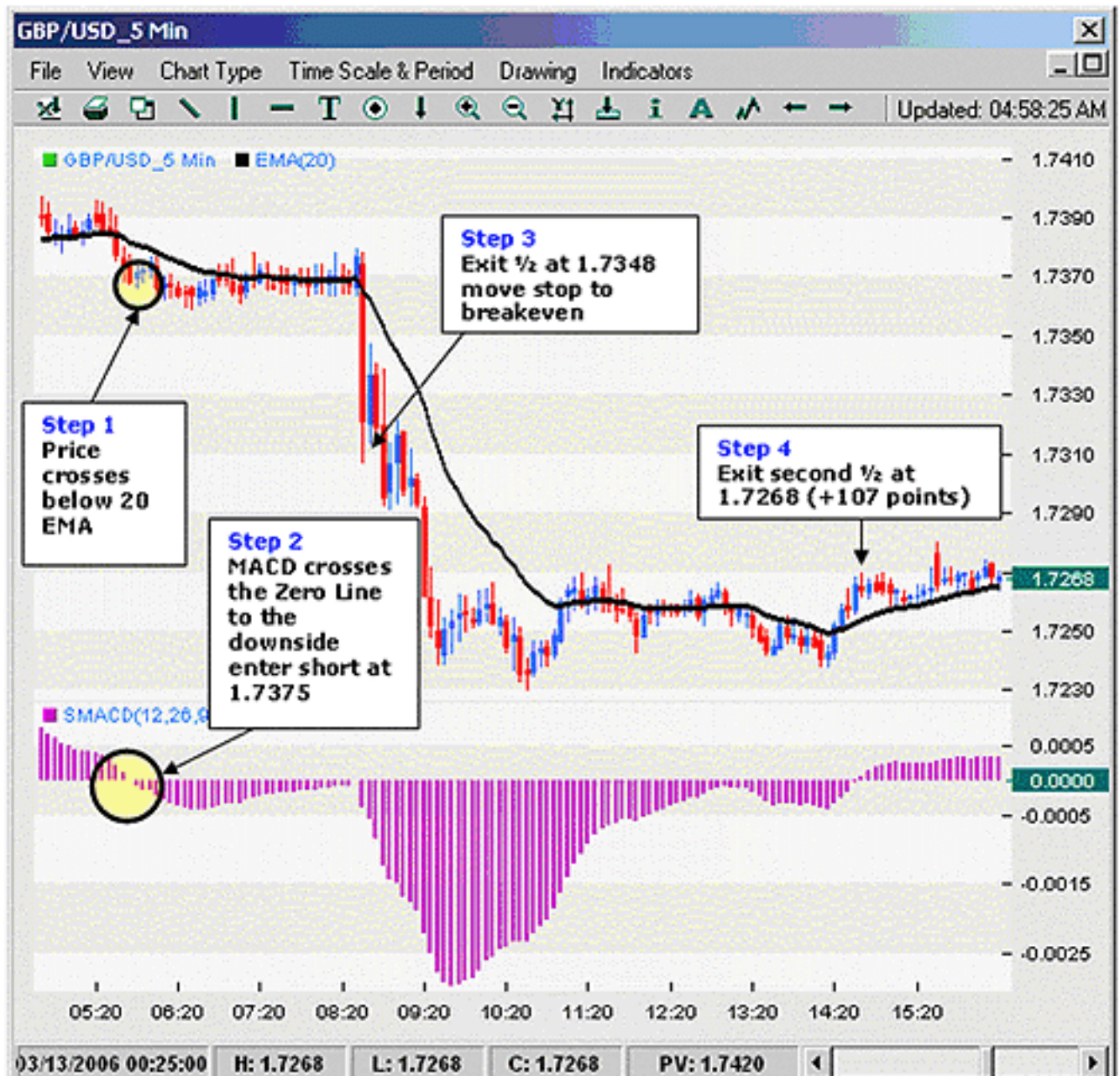


Figure 4: Five-Minute Momo Trade, GBP/USD

Source: FXtrek Intellichart

Momo Trade Failure

As you can see, the five-minute momo trade is an extremely powerful strategy to capture momentum-based reversal moves. However, it does not always work and it is important to explore an example of where it

fails and to understand why this happens.



Figure 5: Five-Minute Momo Trade, EUR/CHF

Source: FXtrek Intellichart

The final example of the five-minute momo trade is EUR/CHF on March 21, 2006. In Figure 5, the price crosses below the 20-period EMA and we wait for 20 minutes for the MACD histogram to move into negative

territory, putting our entry order at 1.5711. We place our stop at the 20-EMA plus 20 pips or $1.5721 + 20 = 1.5741$. Our first target is the entry price minus the amount risked or $1.5711 - (1.5741 - 1.5711) = 1.5681$. The price trades down to a low of 1.5696, which is not low enough to reach our trigger. It then proceeds to reverse course, eventually hitting our stop, causing a total trade loss of 30 pips.

When trading the five-minute momo strategy, the most important thing to be wary of is trading ranges that are too tight or too wide. In quiet trading hours where the price simply fluctuates around the 20-EMA, the MACD histogram may flip back and forth causing many false signals. Alternatively, if this strategy is implemented in a currency pair with a trading range that is too wide, the stop might be hit before the target is triggered.