

Our guide to ten popular Auto-Trading Strategies

No 7. Parabolic SAR Reversal System

CITYINDEX

The City Index AT Pro platform offers over 100 Automated Trading Strategies which can be used to generate trade signals and place automated trades on your account.

We appreciate that when looking at automated trading systems for the first time, they can be intimidating, and it's hard to know where to start or what strategy will work best for you. That is why we have put together these guides to getting started with ten of the most popular strategies as used by our clients.

Of course, there's no such thing as a 'holy grail' trading strategy that will work on all products, over all time frames, all of the time, but by learning what each strategy does and their strengths and weaknesses you can start to get an idea of what strategies suit your trading style.

The Advantage Trader Auto-Trading strategies currently work on a 'Complete Bar' mode, which means that trading systems request a trade on the open of the next, newly forming chart interval, rather than placing a trade at the point in time a signal is generated.

Please note: Auto-Trading strategies can be high risk – you are permitting the trading platform to trade automatically on your behalf. We highly recommend that you test whatever strategy you are planning on using thoroughly, and start with small stakes to control your exposure. City Index will not be responsible for any losses incurred as a result of using the Auto-Trading Strategies. You can learn how to run the Back-Testing tool to test strategies on the product you are thinking of trading by visiting the Auto-Trading Systems section of the City Index website.

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Parabolic SAR Reversal System

Risk: Low.

Strategy type: Reversal.

Recommended timeframes: Longer timeframes (1hr +).

Attention required: Medium to low.

Overview

The Parabolic SAR Reversal System uses the Parabolic Stop and Reverse (SAR) indicator to generate signals for potential trading opportunities.

The Parabolic Stop and Reverse (PSAR) follows the instruments' price and is a good trend following indicator. If an instrument is in a downtrend and then reverses and starts trending upwards, the PSAR follows the prices like a trailing stop. The dotted line continuously rises, as long as the uptrend continues. The PSAR never decreases in an uptrend and continuously protects profits as prices advance. The calculation of where the dotted line is plotted is quite complicated, if you want to find out more this site has a good explanation: http://stockcharts.com/school/doku.php?id=chart_school:technical_indicators:parabolic_sar

Once the price stops rising and reverses and drops back through the PSAR line, this is a signal to close long positions and/or open short positions. At the point it cuts back down through the downtrend PSAR, a new dotted line starts above the candle which cut the lower PSAR.

The new PSAR line follows prices lower like a trailing stop, and in that sense it's quite similar to the Trailing Stoploss Reversal System. The difference is that the TSRS points move one-for-one with the price, whereas the PSAR line dots can 'accelerate' depending on the volatility of the price.

The stop continuously moves lower as long as the downtrend extends. Because SAR never rises in a downtrend, it continuously protects profits on short positions. Similarly to the uptrend, once the price stops falling and reverses back up through the dotted PSAR line, then the strategy generates a buy signal.

The signals are generated using the following logic:

Long Entry = Close price crosses above the Parabolic SAR

Long Exit = Close price crosses below the Parabolic SAR

Short Entry = Close price crosses below the Parabolic SAR

Short Exit = Close price crosses above the Parabolic SAR

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Fig. 1

The Parabolic SAR strategy is a popular strategy and can be used on many different time frames, depending on your preferred trading style. It's a lower risk strategy that works well in a market that trends strongly in both directions, as in the chart above (Fig. 1).

It is relatively low risk, in that if the market flips around quickly and the strategy generates a trade that closes off a losing position, the positions are generally not too far away from the original entry point, so losses are usually kept quite small.

This strategy can take the emotion and bad decision making out of a winning position, keeping a disciplined stop loss on a trending market, looking to lock in a profit on each trade. Shorter time frames may display more trade signals than you might be comfortable with, so ensure you experiment with different markets and different time frames to ensure you are comfortable with the strategy.

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More information on how to back-test your strategies can be found on the Auto-Trading systems section of the City Index site at www.cityindex.co.uk/platforms-and-tools/auto-trading

Risk Warning

Trading CFDs, Spread Bets and Foreign Exchange carries a high level of risk to your capital with the possibility of losing more than your initial investment and may not be suitable for everyone. Ensure you fully understand the risks involved and seek independent advice if necessary. Trading using auto-trading strategies carries additional risks so please ensure you understand the risks involved in auto-trading strategies and test your strategies using demo accounts and the back-testing tools until you are comfortable with using real-money accounts.

Our Risk Warning Notice can be found in the Terms and Policies document. It summarises the key risks involved in trading on an underlying product. It also explains leverage, the nature of margined trading, and volatility.

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