

the original turtle trading rules

the original turtle trading rules represent one of the most influential and well-documented trend-following trading systems in financial history. Developed in the early 1980s, these rules were designed to systematize trading decisions, allowing traders to capitalize on market momentum across various asset classes. This comprehensive article explores the foundational principles, entry and exit strategies, risk management techniques, and position sizing methods that define the original turtle trading rules. By understanding this systematic approach, traders can appreciate the blend of discipline, psychology, and quantitative analysis that underpins successful trend trading. The discussion further delves into the historical context and practical application of these rules, highlighting why they remain relevant in modern financial markets.

- Overview of the Original Turtle Trading Rules
- Entry and Exit Strategies
- Risk Management and Position Sizing
- Historical Context and Development
- Practical Applications and Adaptations

Overview of the Original Turtle Trading Rules

The original turtle trading rules were established to create a mechanical trading system that removes emotional decision-making from market speculation. These rules focus on capturing large market trends by entering positions when certain price breakouts occur and exiting trades based on predefined signals. The system applies to multiple markets, including commodities, currencies, bonds, and equities, ensuring diversification and risk spreading. Central to the rules is the concept of trend following, where traders seek to profit from sustained market movements rather than short-term fluctuations.

Core Principles

At the heart of the original turtle trading rules lies a disciplined methodology emphasizing systematic entries and exits, strict risk controls, and the use of volatility measures to determine position size. The approach hinges on two primary breakout systems: a shorter-term breakout for entries and a longer-term breakout for exits. By adhering to these principles, traders minimize guesswork and maintain consistency, which is vital for long-term profitability.

Markets and Instruments

The original turtle trading rules were designed to be applied across a broad spectrum of liquid markets. This multi-market approach helps reduce portfolio risk by capitalizing on trends wherever they occur. The system was originally tested on futures markets, including energy, metals, agricultural products, currencies, and interest rate instruments, reflecting its versatility and robustness.

Entry and Exit Strategies

The entry and exit rules of the original turtle trading rules form the operational backbone of the system. These rules define when to initiate trades and when to close them, based on price action and volatility measures. The clarity and precision of these rules help maintain objectivity and prevent emotional biases from influencing trading decisions.

Entry Rules

Entries are triggered by price breakouts above or below specific historical price ranges, typically calculated using the highest high or lowest low over a set number of days. The two main entry systems are:

- **System 1:** A 20-day breakout used for aggressive entries aiming to capture early trends.
- **System 2:** A 55-day breakout for more conservative entries following well-established trends.

When the market price exceeds these breakout points, the original turtle trading rules dictate opening positions in the direction of the breakout with calculated size and risk parameters.

Exit Rules

Exits are equally systematic, designed to protect profits and limit losses. The primary exit signal is a price crossing below or above a different historical range, commonly a 10-day low for long positions and a 10-day high for short positions. This mechanism ensures that trades are closed when the trend shows signs of reversal or exhaustion. Additionally, stop-loss orders are used to exit losing trades quickly, based on the Average True Range (ATR), a volatility measurement that adapts stop distances to market conditions.

Risk Management and Position Sizing

Effective risk management and position sizing are crucial elements of the original turtle trading rules, ensuring that no single trade jeopardizes the overall portfolio. These

components emphasize controlling downside risk while enabling participation in significant market moves.

Volatility-Based Position Sizing

One of the hallmark features of the original turtle trading rules is the use of volatility to determine position size. The system calculates the Average True Range (ATR) for each market to quantify volatility. Position sizes are then adjusted so that the dollar risk per trade remains consistent, regardless of market volatility. This approach prevents oversized positions in highly volatile markets and underweighting in calmer ones.

Risk Limits and Stops

Risk is typically limited to a small percentage of the total trading capital per trade, often around 1-2%. The original turtle trading rules prescribe setting stop-loss orders at a multiple of the ATR away from the entry price, commonly two ATRs. This technique allows for normal market fluctuations without premature stop-outs, while still capping losses to manageable levels.

Adding to Positions

The rules allow traders to pyramid into winning positions by adding units as the trend continues favorably. Each additional unit is sized based on the same volatility and risk parameters, ensuring disciplined growth without overexposure. This scaling technique enhances profits during strong trends, a key advantage of the system.

Historical Context and Development

The original turtle trading rules were developed in 1983 by legendary commodities trader Richard Dennis and his partner William Eckhardt. Dennis believed that trading could be taught and sought to prove this by recruiting novices to follow a strict set of mechanical rules. These recruits, known as the "Turtles," were trained over a short period and then sent to trade real money using these rules. The experiment was remarkably successful, generating significant profits and validating the efficacy of systematic, rule-based trading.

Richard Dennis and the Turtle Experiment

Richard Dennis was a self-made commodities trader who amassed substantial wealth by using trend-following techniques. To demonstrate that trading success was not solely dependent on intuition or innate talent, Dennis recruited a group of individuals with no prior trading experience and taught them his methods. The original turtle trading rules emerged from this experiment, codified to guide these new traders in entering, exiting, and managing trades systematically.

Impact on Trading Strategies

The success of the turtle experiment had a profound impact on the trading community, popularizing trend-following and systematic trading strategies. It illustrated that a disciplined approach based on clear rules could outperform discretionary trading, especially in markets prone to trending behavior. The original turtle trading rules have since influenced numerous trading systems and remain a benchmark for mechanical trend-following methodologies.

Practical Applications and Adaptations

While the original turtle trading rules were designed for futures markets, their principles have been adapted for various financial instruments and trading platforms. Modern traders often customize the rules to fit different timeframes, asset classes, and risk tolerances, while maintaining the core philosophy of trend following and risk control.

Adapting to Different Markets

Traders apply the original turtle trading rules to equities, forex, cryptocurrencies, and ETFs, often modifying breakout lengths and volatility measures to suit market characteristics. The adaptability of the rules allows for flexibility while preserving the mechanical nature of the system.

Integration with Technology

The rise of algorithmic trading has enabled the automation of the original turtle trading rules, allowing for faster and more precise execution. Automated systems can monitor multiple markets simultaneously, apply consistent risk management, and execute entries and exits without human emotion, enhancing the effectiveness of the strategy.

Common Modifications

Some traders adjust the breakout periods, ATR multipliers, or position sizing methods to better align with their trading style or market conditions. Others incorporate additional filters, such as trend strength indicators or fundamental analysis, to improve signal quality. Despite these modifications, the foundation remains the same: disciplined, rule-based trading focused on capturing market trends.

- Systematic entry and exit based on price breakouts
- Volatility-adjusted position sizing using ATR
- Strict risk management with predefined stop losses

- Multi-market application for portfolio diversification
- Trend-following philosophy to capture sustained moves

Frequently Asked Questions

What are the original Turtle Trading rules?

The original Turtle Trading rules are a set of trend-following trading guidelines developed by Richard Dennis and William Eckhardt in the 1980s, focusing on breakout entries, position sizing, and risk management across multiple markets.

Who created the Turtle Trading system?

The Turtle Trading system was created by commodity traders Richard Dennis and William Eckhardt in 1983 as an experiment to prove that trading could be taught.

What markets do the original Turtle Trading rules apply to?

The original Turtle Trading rules were designed to be applied across a diversified portfolio of futures markets, including commodities, currencies, bonds, and stock indices.

How do the Turtle Trading rules determine entry points?

Turtle Trading entry points are determined by breakouts above the highest high or below the lowest low over a set number of days, typically using a 20-day breakout for entries.

What is the position sizing method in the Turtle Trading system?

The Turtle Trading rules use a volatility-based position sizing method called N , which measures the average true range to calculate the number of contracts to trade, aiming to risk a fixed percentage of the account per trade.

How do the Turtle Trading rules manage risk and stops?

Risk is managed using a stop-loss placed at $2N$ (two times the average true range) away from the entry price, with adjustments to protect profits and limit losses according to volatility.

What is the role of the 55-day breakout in the Turtle Trading system?

The 55-day breakout is used as a secondary entry signal to add to positions or initiate trades if the price breaks out beyond the 55-day high or low, indicating a strong trend.

How do the Turtle Trading rules handle position scaling?

The rules allow for pyramiding by adding units when the price moves favorably by 0.5N increments, up to a maximum number of units, to maximize profits during strong trends.

Are the original Turtle Trading rules still effective today?

While markets have evolved, many traders still find the original Turtle Trading rules effective as a trend-following strategy, especially when combined with modern risk management and technology.

Where can I find the original Turtle Trading rules?

The original Turtle Trading rules can be found in various trading books, online resources, and articles detailing Richard Dennis's experiment, including the book "The Complete TurtleTrader" by Michael Covel.

Additional Resources

1. *Way of the Turtle: The Secret Methods that Turned Ordinary People into Legendary Traders*

This book by Curtis Faith, one of the original Turtle Traders, provides an insider's view of the Turtle Trading experiment. It reveals the exact rules and strategies used by Richard Dennis and William Eckhardt to teach novices how to trade successfully. The book combines practical trading advice with personal anecdotes, making it a valuable resource for aspiring traders.

2. *The Complete TurtleTrader: How 23 Novice Investors Became Overnight Millionaires*

Written by Michael W. Covel, this book chronicles the story of the Turtle Traders and their groundbreaking experiment. It covers the original trading rules in detail and explains how these simple mechanical systems generated significant profits. The narrative also explores the psychology and discipline required to follow the Turtle Trading approach.

3. *Turtle Trading: The Legend and the Lessons*

This book delves into the fundamentals of the Turtle Trading system, explaining the core principles behind trend following and risk management. It breaks down the original rules and provides insights into how traders can adapt them for modern markets. The focus is on practical application and maintaining discipline in trading.

4. Trend Following with Managed Futures: The Search for Crisis Alpha

Written by Michael Covel, this book expands on the Turtle Trading philosophy by exploring trend-following strategies with managed futures. It discusses how the original Turtle rules fit within a broader context of systematic trading and risk control. The book is ideal for traders interested in applying Turtle principles to diversified portfolios.

5. Following the Trend: Diversified Managed Futures Trading

By Andreas F. Clenow, this book offers a quantitative perspective on trend following, echoing many of the concepts found in the Turtle Trading system. It explains how to build and manage a trend-following portfolio with clear rules and disciplined execution. Readers will gain a deep understanding of trend strategies inspired by the original Turtle approach.

6. The New Market Wizards: Conversations with America's Top Traders

Jack D. Schwager's collection includes interviews with successful traders, some of whom discuss the Turtle Trading methodology. The book provides context and commentary on how the original rules influenced modern trading. It's a valuable resource for understanding the mindset and tactics behind successful trend followers.

7. Systematic Trading: A Unique New Method for Designing Trading and Investing Systems

Robert Carver's work focuses on the design and implementation of systematic trading strategies, including those inspired by the Turtle Trading rules. The book emphasizes the importance of backtesting, risk management, and emotional discipline. It's well-suited for traders looking to build robust, rule-based trading systems.

8. Trade Your Way to Financial Freedom

Van K. Tharp's book explores various trading strategies, including trend following and mechanical systems similar to Turtle Trading. It highlights the psychological and strategic elements essential for consistent profitability. The book serves as a comprehensive guide for traders aiming to develop their own disciplined trading approach.

9. Quantitative Trading: How to Build Your Own Algorithmic Trading Business

Ernest P. Chan's book introduces readers to algorithmic trading, incorporating principles aligned with the Turtle Trading rules. It covers the development of mechanical trading systems, risk controls, and execution techniques. This book is perfect for traders interested in automating Turtle-style trend-following strategies.

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