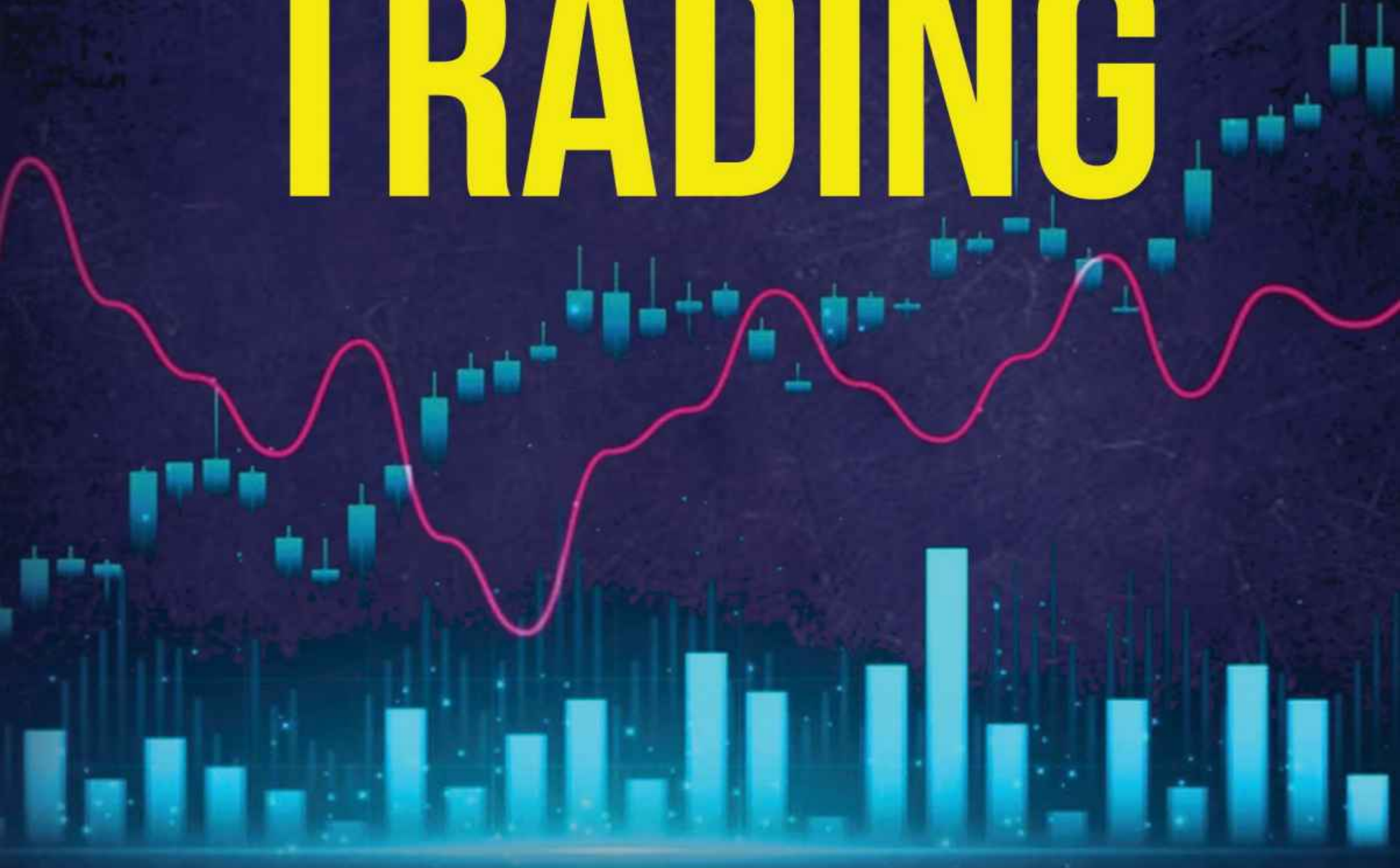
SECRETS ON REVERSAL TRADING



MASTER REVERSAL TECHNIQUES IN LESS THAN 3 DAYS

FRANK MILLER

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INTRODUCTION

While I agree that trading should be simple (i.e do not use too many systems and indicators at the same time), it must be done with good organization skills.

Traders fail to organize their trades when they neglect to put their system operation into the big picture of the market. This would lead to more unexpected losses that will affect their trading beliefs and attitudes. Once they lose necessary positive energies during your trading, things would be much harder in the endeavor.

Think about it… You must optimize everything in your life, from basic skills such as how to speak, how to listen, how to influence others, etc. We are taught to implement things in a way that generates the best possible results. However, the fact is that we cannot perform well until lots of effort have been made. We learn from mistakes, understanding which should be improved and which ought to be retained to achieve better results while suiting our style. In short, we need to optimize strategies, techniques and tips via “trial and failure” to find a way to consistent success.

Things are exactly the same in trading. Although there are many “profitable” strategies and patterns existing for a long time, not everyone makes good use of them. As a matter of fact, not understanding enough market momentums behind these candlesticks costs them a lot of hard-earned money. In this edition, you will see how I identify these momentums using pure price actions. These techniques on reversal trading presented in the book would help you make BIG steps on the way of achieving consistent success in trading. They are proven methods that have been consistently used for years, which would save you a lot of time unlocking trading mysteries. Yet, it is not to free you from necessary back-tests via your trading platform so that you can get a deeper understanding of what I have been conveying for the first time. Most importantly, you need to be patient, sticking to my secrets on **market structures** and **3MS principles** no matter what happens, and profits will find you. Remember that all good things in life take time, and success in trading is not an exception.

Now, let's get started.

CHAPTER I: WHAT IS PRICE ACTION?

The core of my trading strategies presented in this book is price action. Therefore, let's take a look at a very popular concept among traders.

Price action is a trading style which all traders may have heard about. Hence, I would like to summarize just some characteristics of the price action trading below. I believe that after reading and grasping what I convey about reversal trading in this book, you will have a much clearer understanding of price action, and all strategies and techniques I present in this book are the best answer to the question: what is price action.

Price action is the movement of the price of a stock, currency, commodity, crypto, or any other entities plotted over time. Price action forms the basis for all technical analysis in trading.

Price action trading means basing your trading decisions on the price movements of an asset. You won't use indicators or other methods of analysis, even if you do, you'll give them very little weight in the trading decision process. A price action trader believes that the only reliable source of information comes from the price itself. If a stock goes up, that tells the price action trader that people are buying. The trader then assesses, based on the aggressiveness of the buyers, whether it is likely to continue. Price action traders don't typically concern themselves with why something happens.

Once you master a price action strategy, it won't require much research time. Find an asset with the specific price conditions you need, or wait for those conditions to develop. Although indicators use price as their basis, they often lag behind it. By simply focusing on the price, you get the information in real-time instead of waiting for a lagging indicator to give you information.

As a price action trader, you should be patient, waiting for opportunities to come and analyze using techniques about price, with the combination of some self-made tools such as trend lines, triangles, to make trading decisions. Trading setups do not appear so often to price action traders (especially for swing and trend traders), but when they spot any good entries in the chart, chances are that they are truly deserved to try.

Candlestick patterns such as the Pin bar, engulfing pattern and double top are typical examples of visually interpreted price action formations. There are many more candlestick formations that are generated from price actions to set up an expectation of what may come next.

All traders can benefit from learning price action trading. It doesn't guarantee 100% profits, but it makes a great trading style and is preferred by many successful traders in the world.

CHAPTER II: SHAPE YOUR MINDSET FOR SUCCESS IN TRADING

As you might have heard, trading psychology accounts for around 60% of traders' profitability in trading. Before discovering any trading system or strategies, it is important you understand the importance of an appropriate mindset in trading and how to make it part of yourself. Without a correct understanding of the way the market operates, what the opportunities and dangers are, you will be overwhelmed by a lot of market signals, causing an imbalanced state of mind.

Below are some of the most basic yet important characteristics of trading:

The unpredictability of the market

If you have read the classic book "Trading In The Zone – Master the Market With Confidence, Discipline and a Winning Attitude" by Mark Douglas, you would agree with me that the market is just unpredictable. In its purest form, the market is the reflection of what all traders all over the world think and act. Meanwhile, candlestick charts are the visualization of the overall market momentum which traders base on to analyze possible market movements.

In fact, it is nearly impossible to tell with certainty where the market is going next. There are so many institutions, banks, funds, and individual traders participating in the market. Each entity has its own thoughts and courses of action. You might think that this price is high and that price is low, however, others may think and act oppositely. You cannot know what others are thinking about the same candlestick patterns you are witnessing. Also, you cannot affect others in a way that they will follow your thinking and trading preferences. As a matter of fact, each time in the market is unique and nothing is to be known for sure.

Instead, trading in its purest form is a field of probabilities. If you join each trade with high chances of stacking the odds in our favor, you are likely to win in the long term. Throughout my trading career, I have seen many traders generating negative feelings after losing trades. Yet, we should all keep in mind that we cannot avoid losses in any way. Even the most successful traders in the world suffer from losses, even many losses. The key is how you manage your losses within a safe and acceptable zone, in a way that these losses cannot affect your psychological state of mind. Consistently profitable traders are well aware of this, and they never violate their rules on money management, which serves to give them an appropriate frame of mind to join the market.

I want to emphasize the unpredictability of the market because I fully understand how stressful most traders are when they experience losses. In fact, losses have little to relate to the market or the system (unless the system is brand-new without any back-tests). Successful traders never let these losses undermine and drive them to self-sabotaging actions. For them, the market is unpredictable, and the core elements in any success in trading lie in their own thoughts and beliefs. Specifically, if one is loyal to his trading rules and philosophy, they would eventually make consistent profits.

This is also my first advice when it comes to trading in any market. When you are in an environment with lots of uncertainties, the adoption of proper mindsets is a MUST. One single loss or even a number of losses will not be able to tell anything about your analysis and your system. In fact, the best systems still generate many losing trades. It is how you remain disciplined and objective in the market that matters most. Strict compliance with rules would help to free you from unexpected pains resulting from losses. The better you are at avoiding psychological shocks, the better you are at identifying opportunities via candlesticks. While the market is full of unpredictability, it offers unlimited chances of making profits. The question here is whether you are willing and committed to doing the right things to acquire desired results.

Trading should be flexible

After all, trading should be flexible. This means that you should let your mind be open to movements in the market. Sometimes, candlesticks move in accordance with your analysis and expectations, but in many other cases, their movements make you puzzled. As I mentioned above, the market is comprised of a large number of participants and you cannot know what others are thinking. A price level you consider as high may be seen as low in others' eyes. To successfully exercise in this endeavor, you need to accept the "uncertainty characteristic" of the market.

When you are flexible, you would be able to analyze charts based on what the market is actually telling instead of what you feel or hope. Flexibility puts you in the best position to discover potential opportunities when it comes. Moreover, this also serves to free you from negative feelings or psychological shock when things go against your expectations. This is to differentiate from a rigid style, in which you rely too much or put too much expectation on any single trade.

Let's take a hypothetical example of a trader when he is seeing a "seemingly" similar pattern on the chart to one that he successfully traded a few months ago. I use the word "seemingly" because I cannot ensure everything behind the candlesticks is identical to the situation in which he traded before. In fact, what I mean by "similarity" is just on the surface. However, he is completely confident that the history would repeat and place a trade with a high volume. The market then generates some initial signs of opposition movements to what he has thought of, but he ignores and continues with his original analysis. He criticizes any opposing ideas on the understanding that if he could win once with this trade, he can win many more times. He considers anyone who is not in favor of his trade as silly because he is "experienced" in trading this candlestick pattern. He becomes overconfident and cannot grasp what the market really wants to tell him. Finally, he ends up losing a big unexpected amount of money that is far beyond his imagination.

I bet this scenario is not strange to most traders. These unexpected losses greatly contribute to wiping out traders' accounts all over the world. In the above example, our trader is lacking an objective mindset to pick up what is happening in the market. In other words, he is not flexible enough to understand a fact that each moment in the market is unique, and a pure copy of previous actions may lead to disaster. Only by staying calm, open-minded, and flexible can someone be able to uncover any potential opportunity the market offers.

This is what I want to convey in relation to my analysis techniques that you will discover in the next Chapters of the book. In fact, these techniques are the result of a large amount of time I spent in front of my computer screen to study, trade, and summarize. Yet, I do not guarantee these techniques will work each and every single time you trade with them. I am just confident that if you apply them consistently, you would be profitable in the long term. Be adapted to market movements. In trading, flexibility is a MUST.

The role of identifying the correlation between bulls and bears

The market is characterized by the battle between buyers and sellers, or bulls and bears. Each candle on the chart illustrates the correlation between the two sides. If the bears are more powerful than the bulls, the market is showing a downtrend, forming lower highs and lower lows, and vice versa. On the other hand, if the bears are tired, the market fails to create lower highs and lower lows.

During those times, traders should watch out for signals of the bulls joining the market. It seems simple, but they are key things in determining whether or not we should buy or at least be in a position for a buy order. If the market is telling us that sellers are losing steam and buyers are gaining strength, it would be better to prepare to buy the currency pair. Failing to do that means that you are planning to fail.

Furthermore, the identification of which is stronger should be based on a big picture. One single candlestick does not count in many cases. A big picture should include but not limited to an overall trend determined on a weekly or daily chart, supports and resistances, and trend lines. Later in this book, I will describe in more detail when the sellers and buyers are tired, and what we should do in those times. On trading the market, you should always wonder which side is stronger at a specific time. It can only be done by analyzing charts by yourself. No robot can replace a human to do this task.

After understanding the big picture, you will start looking for good trade setups in the market and then find an entry price, stop-loss, and profit-taking level. While the battle between bulls and bears never ends, each opposing force from the inferior side would be ideal for placing orders in the direction of the superior power. For example, if the bears are dominating the market, any correction created from the bulls is ideal for placing an entry, and vice versa. In reality, I never enter any trade without correction (also referred to as a retest which I will reveal in detail in the following Chapters of the book). This not only helps me reap greater profits but also allows me to acquire a better risk-to-reward ratio, which benefits me in the long term.

CHAPTER III: EVERYTHING STARTS WITH THE WAY YOU THINK

It is important how you think to be a successful trader. Without proper mindsets, it is nearly impossible for you to succeed in a challenging endeavor like trading. Hence, before going deeper into my secret techniques regarding market structures, let's talk about thoughts in trading.

In trading, I will divide thoughts into two types:

- **Correct thoughts** will generate correct courses of action, which leads to favorable results.
- **Wrong thoughts** will lead to wrong courses of action, which brings about bad results.

In trading, correct thoughts help you to generate overall profits through time while wrong thoughts cause you to lose money, as simple as that. Honestly, I have not witnessed anyone who owns wrong mindsets and makes consistent profits from the market.

WRONG THOUGHTS AND ACTIONS

Let's take a look at the wrong mindsets first. Which is actually preventing traders from making profits? Remember the moment you decided to join the trading journey. What were the top reasons for you to open a real trading account at that time? Did you study the market long enough (i.e at least 6 months) and felt so attracted that you opened an account to follow your new passion? Actually, I don't deny a fact that some traders join the trading journey for some good reasons like discovering themselves, studying market secrets that inherently entails lots of practice and patience, winning over themselves, acquiring a feeling of conquering, or just simple as learning about something new, etc. In my opinion, these are positive reasons for a start. However, many traders join this market for another reason – MONEY. The majority of traders join the market with “profits” the TOP reason, and that is the problem.

Many traders think that trading is a simple way to make money. In fact, money can be earned within minutes or even seconds, and there is a lot of money out there to pick. If truth be told, I do not see any other endeavor where people can increase their account balances by just a few mouse clicks like trading. As a matter of fact, the attractiveness of trading is so big that sometimes it is hardly possible to say “no” to invitations from brokers or some of your friends. These newbies are seduced by Introducing Brokers (IB) who constantly showed winning trades of hundreds or thousands of USD. Many traders join with the hope of doubling their account balance in just one or two months. They dream about financial freedom in which they can make money anywhere in the world with only a laptop connected to the Internet. The very thought of money and profits is what I define as “a wrong thought”, and trading will be so difficult then.

So, what are the possible wrong actions that may result from this wrong thinking?

- You only focus on profits and do not care about possible losses. You do not accept losses and do not set any stop loss for your trades. On encountering a floating losing trade, you often hope that on a beautiful day, the market will make a reversal and go in your expected direction.

- You will add another trade when you are already in a losing position. For example, if you own a rigid belief that the market would make a reversal, you will sooner or later add another buy order although the market is moving lower and lower. You will find that your greed is immeasurable. To make matter worse, you just cannot identify how much profit is acceptable in each trade. What you are aware of is that “the more, the better”. The mere addition of trades itself is not a bad act. In fact, it is one of the secrets to increasing your potential profits if you understand and apply appropriately. However, adding another trade arbitrarily is among the quickest ways to wipe out your account. In some cases, you may be right and turn losses into profits. However, sooner or later you will encounter unexpected results from the full focus on your profits.

- You will take revenge against the market. Let's see if this scenario is familiar to you or not. You are entering a buy trade but the market is trading lower and lower. After adding some buy orders in order to make up for the first one (in case of a potential reversal), the market is still in a strong downward trend with long bearish candlesticks. There will come a time when you nearly lose hopes about a reversal. Then, you enter a sell order with much a higher volume with revenge in your mind like: "***I will get all the losing money back with this trade***". You put a very high expectation on this trade. Unfortunately, the bears are "getting tired" of pulling prices lower and start taking profits, which serves to push the price higher and higher. You panic and look your account equity moving closer and closer to the zero level. You cannot do anything else but close your remaining sell order. Your day ends with an overwhelming red color of losses in your trading history.

- You constantly jump from one trading strategy to another. All you need is a trading strategy that can generate profits consistently. If it fails a few times, you move to another. In this way, any strategy in your hand can hardly exist for more than a few months, even a few weeks. Consequently, you may find yourself using dozens of strategies while you are not sure which ones work and which don't. In short, failing to consistently follow a method of trading long enough leads to many arbitrary actions where your trading decisions are based on what you feel instead of what you see.

- Worse, feeling that you cannot win trading by yourself, you may look for a robot. Robots in trading are advertised by many blogs, e-commercial sites with very high rates of winning. If you still believe in robots, ask yourself this question: "if trading using robots can bring consistent profits, why do 95% of traders lose?". If there is one robot that can turn losers into winners, everyone will be celebrating their victories each day.

- Finally, when you have tried everything possible to help build your account without success, you QUIT. Your mind will then be ingrained into some thoughts like "success in trading is impossible", or "success in trading needs secrets that successful traders never tell you", etc. Your frustration comes to a peak that you become really afraid of entering any trades, and giving up is unavoidable. To make matters worse, because it is a financial failure, it may lead to other unexpected problems between you and your family, your co-investors, or your money borrowers, etc. At that time, it is very much likely that you hear a comment like "trading is gambling" from people around you.

An obstacle that prevents you from realizing your mistake is your psychological breakdown. Upon enduring too many losing trades, you are totally numb towards the market and cannot discover any drawbacks to fix. Inevitably, this leads to a negative outcome: loss.

CORRECT THOUGHTS AND ACTIONS

From my personal experience, success in trading mainly lies in good money management. You should and must focus on how to **PROTECT YOUR CAPITAL** before thinking of anything else. In other words, *instead of finding a system that brings you winning trades, you should find systems that save you from losing money*. Imagine you have just made $100 in the market. If you are too concentrated on profits, then you will try to multiply this number to turn you into a millionaire soonest possible. However, as I mentioned above, this thought just serves to ruin your account sooner or later. Whereas, when you focus on protecting your capital, you are protecting your profits as well, and you will become profitable, as simple as that. No matter how right or wrong the market is, you have to own a right mindset first, which generates correct actions, specifically:

- Improve the entry, stop-loss, and profit-taking levels. You will find out that optimizing these levels is not an easy task. The market is not about entering an order when an engulfing pattern or pin bar appears. It is how well you communicate with the market to understand what it is telling you. Sometimes the market is waving at you "***hey, this pin bar is a reliable signal, buy the EUR/USD pair now***", but in many cases, they are just false/ unreliable signals. Hence, in order to protect your capital, you have to spend more time studying the market and exercise your trades in a much more prudent way. A fixed stop-loss level will free you from emotional pains because it is an acceptable figure that you set by yourself.

- Concentrate on the risk-to-reward ratio. The market is a game of probabilities. It is not important if you win or lose in any individual trade. It is important how much you earn when you win and how much you lose when your trade hits the stop loss level. This simultaneously emphasizes the importance of the risk-to-reward ratio. More on that on the next Chapter.

- You will trade using higher time frames (weekly, daily, 4hour). In my opinion, these time frames offer much more reliable signals than smaller time frames do. Moreover, you will realize that in trading, LESS IS MORE. Some newbies may of the opinion that the more trades they enter, the more profits they will gain. However, the truth is the opposite. You should keep in mind that good setups do not appear quite often in the market. Hence, entering so many trades just serve to take you to various inherent traps in the market, and losses are inevitable. In the next Chapter, I will show you an example of how you can avoid this type of trap with a higher time frame.

- Build a market scenario. Trading patterns tend to repeat in some ways. Studying chart history will give you more insights into the market, from that you can apply patterns and movements into future projections. To win in this market, you must be well-organized. In fact, one of the best ways for any trade execution is to build a potential scenario for the market. If the market continues its movements with your expected analysis, then trade the market based on what you have pre-defined. If not, just stay on the sideline. One thing to remember is that the market is always full of opportunities. Stay patient!

In short, if you are losing without understanding the reasons, ask yourself whether you are too concentrated on profits. It is the primary reason traders constantly wiping their accounts. If you are focusing on profits then try to pull yourself out of this way of thinking. Instead, how to protect your hard-earned money should be put on top priority.

CHAPTER IV: PRICE ACTION CANNOT WORK WITHOUT THESE THINGS

Besides preparing an appropriate mindset in trading, setting up an effective trading system should be carefully taken into account. Below are some tips that help you build a profitable trading system. They have been part of my trading for years.

Later in this book, you will see how I describe my powerful trading strategies in a close combination with these elements.

Tip No. 1: Higher time frames

In my price action strategies, trading on higher time frames is a must. It filters out all the turbulence in the market and paves the way for highly reliable trade setups. My favorite time frames for trading are weekly, daily and 4-hour charts. Among these, I use the weekly chart (even monthly chart) to understand the big picture of the market. The daily chart is used to catch the best trade setups in the market and the 4-hour chart (sometimes 1-hour chart) is for finding entry and stop levels. Let's talk a little bit about why the three above time frames are my favorite choices for implementing my techniques:

First, let's think about a relationship between two individuals. Do you agree that the longer you are with someone, the more you will know about her/him? When you meet someone for the first time, it seems impossible to have a good sense of character within 5 minutes of talking with her/him. Naturally, you really cannot make any deep comments in one way or another about a person until you spend enough time with them.

Things are similar in choosing time frames to trade.

High time frames such as weekly, daily and 4-hour charts give you more information about the market in comparison with the

5-minute or 15-minute charts. By using the 5-minute chart, you are missing out on many important movements.

Let’s look at the below example to see why the 5-minute chart fails to tell you about the “big picture” of the market. The below USD/JPY chart cannot really tell us whether the dominant trend is an uptrend or a downtrend.

Next, let’s compare the USD/JPY 5-minute chart with the USD/JPY daily chart. From the below chart, even a 6-year-old can see an obvious uptrend. Looking at the daily chart, you could at least be sure that you would not sell the currency pair at the current rate. The uptrend is so strong and there has been no sign of tiredness from the bulls. This is how a higher time frame saves you from unexpected losses that many scalping traders often encounter. In short, higher time frames minimize a lot of turbulence in the market, thus increasing your chances of stacking the odds in your favor.

I will mention the concept "key support/ resistance" many times later in this book. In these cases, you should understand that they are support and resistance levels on higher time frames (i.e weekly and daily time frame). In fact, I am a big fan of trading on these time frames.

Tip No. 2: Ideal risk-to-reward ratios

As I have said, the market is full of uncertainties and no technique can ensure a high win rate each and every single time you trade. Now, when we talk about success in trading, we are referring to long-term success, aren't we? In fact, when talking about long-term success, we think of factors that the more we apply them, the more understanding and money we have about this endeavor. In my experience, a good risk-to-reward ratio is one of the said factors.

Why risk-to-reward ratios?

Because we can choose an ideal risk-to-reward ratio each and every time we trade using candlestick patterns. This is a simple task that we can consciously control. Put differently, no other forces, from the market to the brokers or traders can prevent you from trading with an ideal risk-to-reward ratio.

Let's take an example that for each trade, you risk just $1 (stopping loss at $1) for every $3 (taking profit of $3) of potential profit. In this way, the risk-to-reward ratio is 1:3. In each trade, what you possibly achieve is three times bigger than what you possibly lose. Hence, if you trade for a long enough period of time, you can lose 75% of all your trades and still do not lose overall. This is not to mention the fact that you are using a rather bad system (losing 75% of total trades). Regarding my systems, I have been using them for a number of years now, and with strict capital management execution, I have been enjoying consistent profits.

Turning back to the above-mentioned ideal ratio I just mentioned. What I mean as "ideal" is at least 1:3. In fact, it is even better if it is 1:4 or 1:5. However, finding a trade of 1:5 ratio is much harder than finding one with a 1:3 ratio. On the other hand, I do not object to using the 1:2 or 1:2.5 ratio, which I believe would bring profits in the long term. Yet, my favorite ratio is at least 1:3, and it is what I recommend all of you use during your trading journey.

With an ideal risk to reward ratio, strict money management and a good system, you would be closer to profitability. You won't be too tense upon encountering a loss because you are fully aware that loss is unavoidable in the market. The market is basically full of opportunities. With a 1:3 ratio, for example, after you win 1 trade, it will take at least 4 losing trades to make you lose overall. Thinking this way, you are just relaxed after each loss. Nothing makes you more enjoyable than a belief that you would be profitable eventually. This is one of the secrets of this venture.

Tip No. 3: Support/ Resistance

In trading, any candlestick pattern must be traded in connection with support/ resistance areas. Put differently, I never trade any pattern unless it is present in support/ resistance areas.

While I state that the market is full of uncertainties, it often remembers what happened in the past and tends to respect history in some ways. For example, if the 1.2000 level of the EUR/USD pair is represented by a top in the past, the market tends to react when the price touches this level again. It may either bounce back after touching the level or breaking it and turning the resistance into a support level.

When the price is about to touch a level, you should watch out for any potential candlestick pattern or chart pattern, because these patterns are offering higher chances of winning than ones not presented on any key levels. Trading this way, we are able to filter out a number of false patterns which in many times cost us a lot of hard-earned money.

Furthermore, trading with support/ resistance helps us to be patient. We need to wait and wait only for trades that are shown on any key spots we have pre-defined. If you haven't known, patience is among the most important characteristics in trading. Patience helps you to understand more about what the market is telling and saves you from trading too much.

From my experience, patterns not present on any key levels are often false signals which may cause disasters. They may show that the market is tired and a correction is occurring, but then the dominant trend strongly continues. Even though some of these patterns may work and the market makes a reversal or so, it is better to stay on the sideline. In fact, there are unlimited opportunities in the market, and missing out on one or two opportunities should not be treated as a bad thing. From now on, you need to treat trading on key support/ resistance as a MUST. It is the secret of all successful traders in the world. The more you comply with this rule, the better you are at filtering out false signals in the market, increasing your profits.

Tip No. 4: Risk management

Maintaining a good risk-to-reward ratio in each of your trades is not enough if you increase your risk amount arbitrarily.

You may probably hear about the 2% rule. The main idea is that you must not risk more than 2% of your trading capital in each trade.

For example, if your trading account balance is $5,000, you must not risk more than $100.

If you want to risk more, increase your trading capital. It may seem difficult for traders to follow, but it is what you should and must do. Trading is a long-term journey, instead of overnight prosperity.

Good risk management helps you on this journey. As you may already hear, the No.1 priority in trading is capital preservation. The No.2 rule is “never forget the No.1 priority”.

Now, let’s look at a hypothetical example.

You are spotting a seemingly perfect trade setup on the chart. More ideally, you did win with a similar setup a few days ago. You are confident that history will repeat. You decide to risk five times as it should be, and a trade is opened.

Suddenly, the price goes against your expectation, hitting your stop-loss. You are shocked.

Your over-expectation, coupled with a violation in risk management, costs you your hard-earned money. Now, the stress of looking for a winning trade to make up for what has been lost is bigger and bigger. You may not be as comfortable finding a trade set-up as before. Such circumstance is an ideal condition for some negative feelings to appear such as revenge, stress, depression.

Hence, to each trader, risk management should be seen as a top priority in trading. Just one violation may cost you not only money but a lot of time to rebuild what you had in the past. To make matter worse, the re-building process may not be as comfortable as before. This is the problem.

Before discovering the main part of the book, I would like to share with you a little treasure of mine – trading books, notes and templates and indicator plugins which I believe you would be interested in. **Get them for FREE here**.

CHAPTER V: FIRST, LET'S DEFINE THE TRENDS CORRECTLY

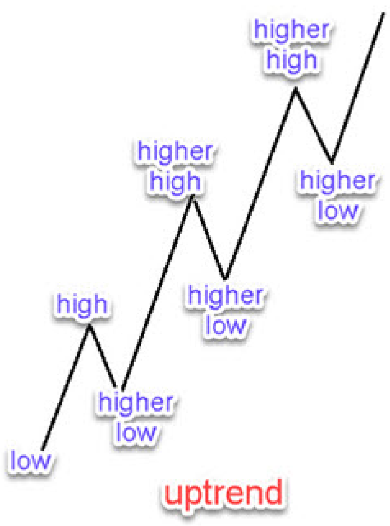
Determining the trends correctly helps to avoid false signals. It is well connected with the understanding of market momentum, i.e whether the bulls or the bears are stronger. You should not think of buying a pair when the price is about to drop or when the buyers show signs of tiredness and vice versa. A wrong determination of trend is likely to cause losses. I use the word "likely" because basically, I don't want to make any "100% statement" about wins or losses in trading.

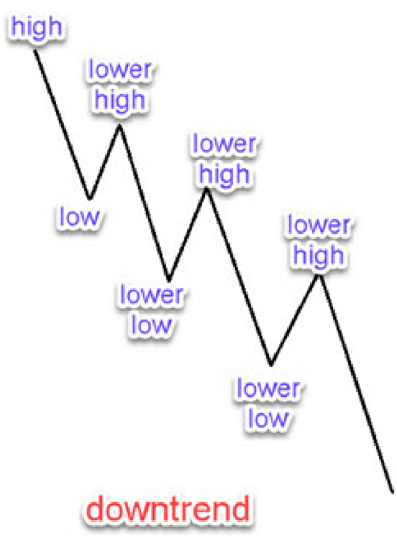
The method I apply below is a popular method that can be displayed on a plain chart (i.e no indicators required). In other words, it is very easy to use. If you have read some popular books on trading (my favorite one is "trading in the zone" by Mark Douglas), you would agree with me that the simpler, the better. Hence, all I convey in this book is what I consider simple but effective tips and techniques that I have summarized from my trading journey.

In trading, there are two types of market, namely trending market and non-trend market.

1. Trending market

A trending market can be either an uptrend or a downtrend. Let's take a look at the below example:





Simply put, in an uptrend, the market forms higher highs and higher lows. Thus, when the market fails to create higher highs and lows, the uptrend is about to end. You should be prepared for a sell order those times. I will describe this technique in detail later in this book.

On the contrary, if the market is in a downtrend, it creates lower highs and lower lows. Hence, if for some reason the market fails to form lower highs and lower lows, the downtrend is likely to end. You should watch out for a buy signal then.

Although we are talking about two opposite trends in the market, the technique is similar. In other words, if you can apply what I share about trading in an uptrend (i.e trading a reversal from a downtrend to an uptrend), you will be completely confident in trading in a downtrend using the same principle.

For a simple trend determination, please remember that:

- *A minimum condition for an uptrend to form is that it creates at least ONE higher high and TWO higher lows. In general, the more highs and lows, the stronger the trend is.*

- *Similarly, a minimum condition for a downtrend to form is that it forms at least TWO lower highs and ONE lower low. The more highs and lows, the stronger the trend is.*

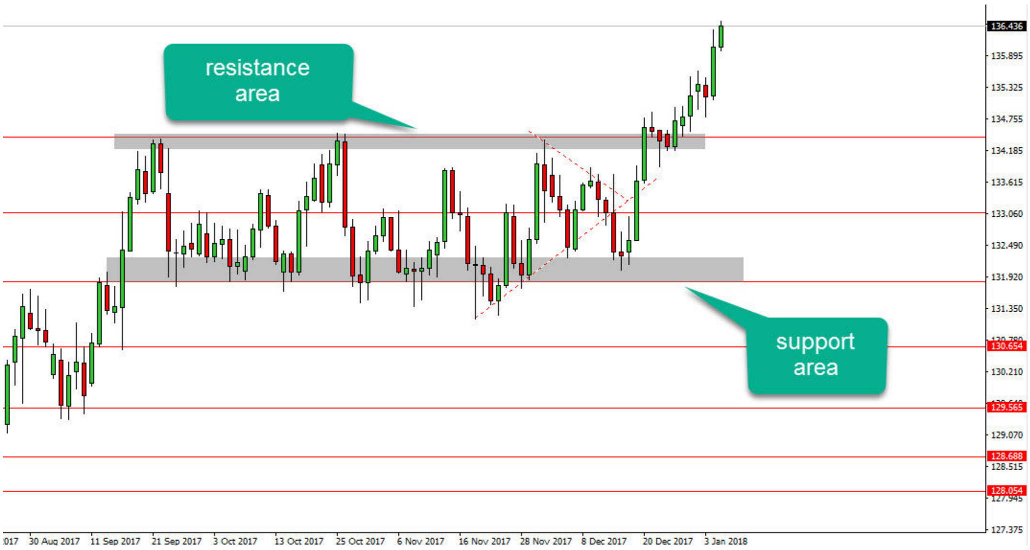
These definitions are based on my reversal trading techniques that have been harvested through the years. Later in this book, you will fully grasp why I set these criteria for a reliable trend determination.

Please notice that in a downtrend, the upcoming lower high tends to touch the newest low on the chart. Meanwhile, in an uptrend, the upcoming higher low tends to touch the newest high on the chart. Take a look at the below example.

You can see how the market tends to retest the latest resistance area before moving with the dominant trend. Such retest will play a very important role in determining the entry point, which serves to bring you ideal risk-to-reward ratios. In the following Chapters of the book, I will reveal when a retest can be seen as an entry signal.

2. Non-trend market

A non-trend market, also referred to as a sideways market, appears when the prices constantly move between a support area and a resistance area. Notice I use the word "area" instead of a specific price level. Using a price area brings about an overall price action in the chart, and saves us from missing good opportunities in the market. Let's take a look at the below example:



You could easily see that the prices were constantly moving between two key support and resistance areas. By determining key zones instead of fixed price levels, traders could maximize their profits trading sideways. Let's take a look at the 131.92 price level for example. While I agree that the level itself is a very strong support price when the prices usually bounced back upon touching the level, using a support area as in the example brings us more profitable buy entries. Once again, I recommend the use of what is considered better than other options. In this endeavor, we need to optimize every single aspect of any trade, and using support and resistance areas is of prime importance.

In trading, I am not a big fan of sideways trading. Yet, if you trade this type of market, I recommend the use of key areas in connection with some other important tools.

(In this book, sometimes you will see I use the phrases "support/resistance line" or "support/resistance level". Please do not misunderstand that I am mentioning a specific price level. In fact, I always recommend the use of areas regarding support and resistance. However, as support/ resistance is illustrated as a horizontal line in all pictures, I am using these phrases for easy references. To avoid any misunderstanding, let's assume I am telling about "key areas").

As I stated above, the determination of market trends depends on which time frames you use. To me, the weekly and daily charts are the best. You should avoid using low time frames for such identification, such as a 5-minute chart or so.

It is important to note that no trend can last forever. It is ideal to trade the market when a trend is about to terminate and an opposite trend is highly likely to start. Nothing is more satisfactory than success in determining tops or bottoms on a weekly or daily chart, which serves to remove many unnecessary worries on the relevant trades. Yet, how to identify a termination in a trend needs to be carefully considered. In the following Chapters, I am going to disclose my favorite methods which I have been using for a few years now.

CHAPTER VI: SECRETS ON IDENTIFYING RELIABLE MARKET REVERSALS

Throughout my trading career, I have seen many traders applying candlestick patterns in a rigid way, leading to many unexpected losses. To make matters worse, these losses then cause emotional pains and lead to more severe disasters for traders.

For example, you buy a currency pair right after a bullish engulfing pattern appears. Or if you are more careful, you will place a long order when this pattern appears at a support area.

Not enough. Trading is not as simple as that. As I said in some of my previous books, effective use of candlestick patterns requires much more than a lot of traders may think of, including but not limited to psychological preparation, money management, and secrets on market analysis that I am going to reveal.

You may have read some books that guide you through how to trade with candlestick patterns such as pin bars, engulfing patterns or double top, etc. You are taught how and when to enter trades, how to set stop loss and profit-taking targets… However, the fact is that not all signals provide a high chance of success. Your mission as a trader is to filter only the very best trade setups, which is what successful traders often do. They carefully judge every single trade in the market, understanding that such prudence will benefit them in the long term.

I am a fan of trading market reversals. There are many turnaround patterns on the market. However, before mentioning these patterns, let's get a definition of a trend reversal in the market, which will drive our course of action.

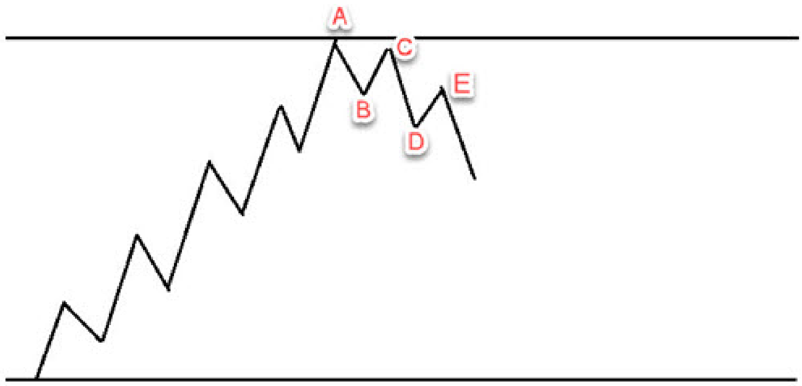
A market reversal needs to meet three criteria:

- First, the prices need to be presented on a key support and resistance area. (COMPULSORY).
- Second, there is a change of the **market structure**, i.e from an uptrend to a downtrend or from sideways movements to a downtrend. (COMPULSORY).
- Third, only for trading reversal candlestick pattern: In this case, the pattern itself must carry a clear sign of a turnaround in connection with market structure analysis (more on this later).

(Please remember these three bullet points for they closely support my analysis in this book. It is better you write them down on a piece of paper for easy reference later).

I would try to restate these criteria in connection with some real examples below. To me, they are just invaluable holy grails.

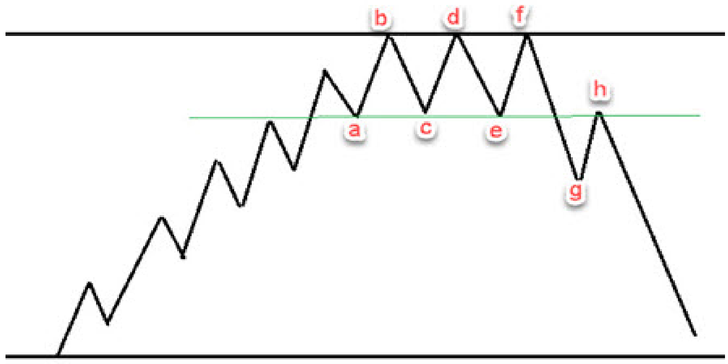
Let's take a look at the below picture:



As you have learned from the previous Chapters, the market is well in an uptrend by making higher highs and higher lows. Until B, there has been no sign of a market reversal. For any turnaround to be confirmed, we need to wait for a break from this structure, which is best represented by ***the creation of lower highs and lower lows.*** While the peak A is located at a ***key level***, let's see how the market fails to make a new higher high at C. After a new low at D is formed, we are now having a lower high and a lower low at C and D. The market has lost its upward momentum and a downtrend is clearer and clearer. Yet, it is not until E that we should consider an entry order.

More on that later when I will disclose the secrets behind the expected appearance of E.

In another example below, prices are getting access to a resistance level and are moving sideways from A to F before breaking the support line and dropping to the below zone. It can be seen that before the long dip, the bottom level of the sideways zone has been successfully broken, creating a low at G. Such break indicates a change in the market structure when the sellers have controlled the game and dragged the prices lower and lower.



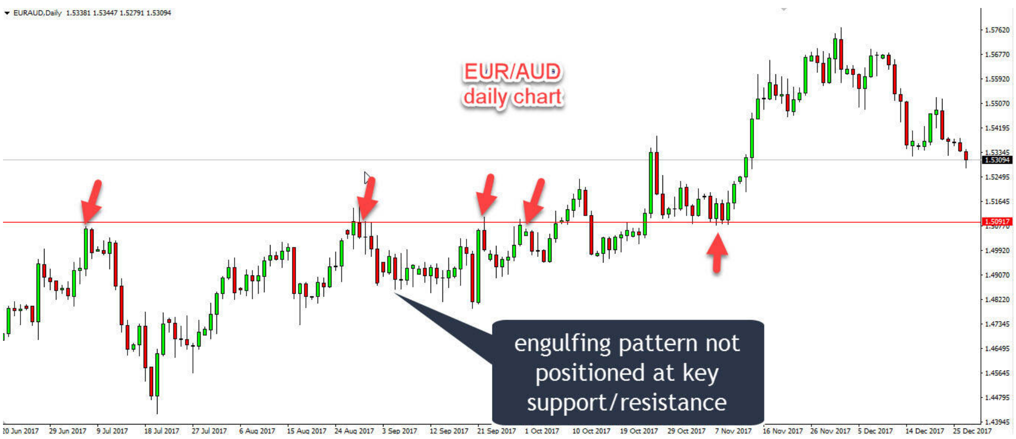
Personally, I don't trade sideways so often. Yet, I still mention this example to help you gain a better overall understanding of a market structure's change.

So, we have scanned through two out of three criteria in identifying a market reversal. Regarding the third criterion, which relates to the reversal analysis within the candle itself, we will take some looks at real examples later.

In short, we have gone through simple key concepts in trading market reversals. As I mentioned, these signals MUST be consistently used by traders should they aim at long-term success. In the following Chapters, I will show you how you can apply these key principles to specific candlestick patterns' trading. Also, I will go into details about **market structure** – the biggest secret in this book.

CHAPTER VII: ENGULFING PATTERN TRADING WITH 3MS PRINCIPLES

Engulfing pattern is one of my favorite trading setups. Identifying good engulfing bars can help you yield big potential profits. Yet, there are also a lot of false signals in the market. Let's refer to the below example.

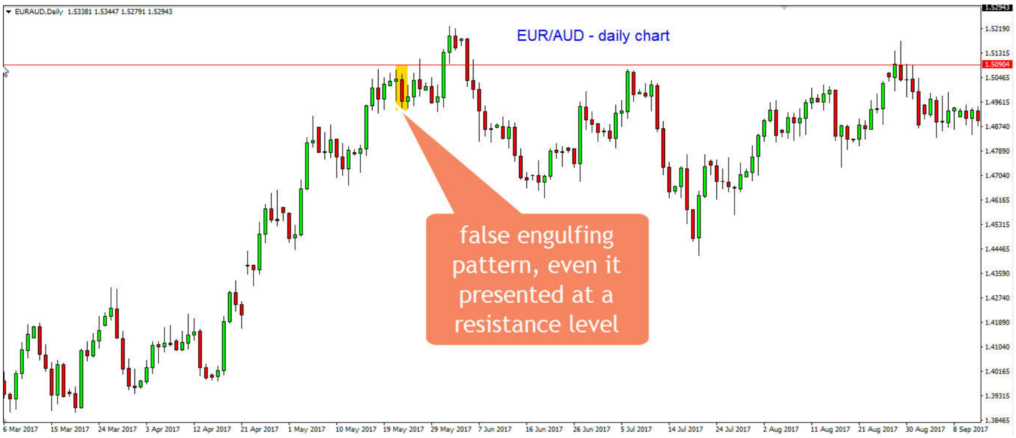


As can be seen, the market had formed a strong resistance level at 1.5091 (the red horizontal line) before the engulfing pattern appeared (see the first two arrows). The market failed to break the resistance level twice, which clearly indicates how strong the resistance is. You can see the resistance remains unbreakable two more times (the third and fourth arrow) before becoming very strong support later (notice the fifth arrow).

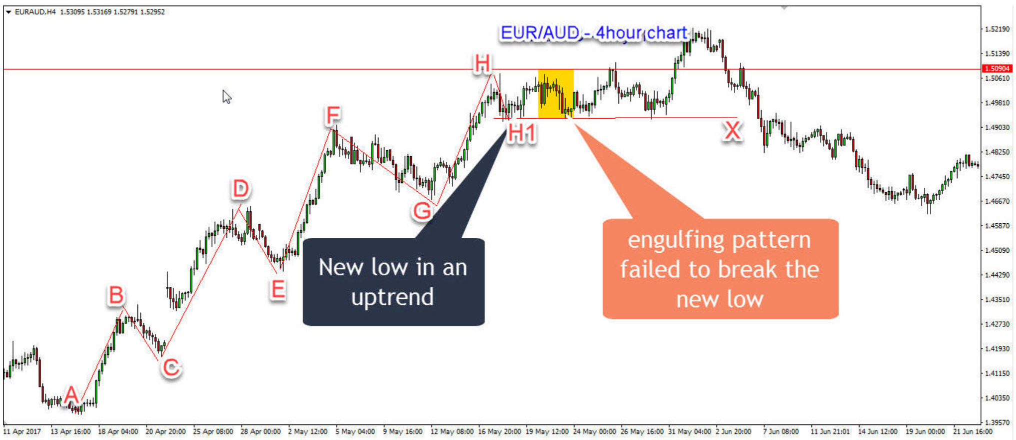
The engulfing pattern in the picture did NOT appear on a resistance level, meaning that its chances to attract seller pressure is not so high (consequently, it failed to work as a reversal signal). In these cases, it is advisable not to enter any trades. You will not stack the odds in your favor if the candlesticks do not reach any key support and resistance levels.

Principle 1: Do not trade any candlestick pattern if it is not present on a key support or resistance level.

Let's take a look at another example when an engulfing pattern that does not meet all entry criteria may bring unexpected losses to traders.



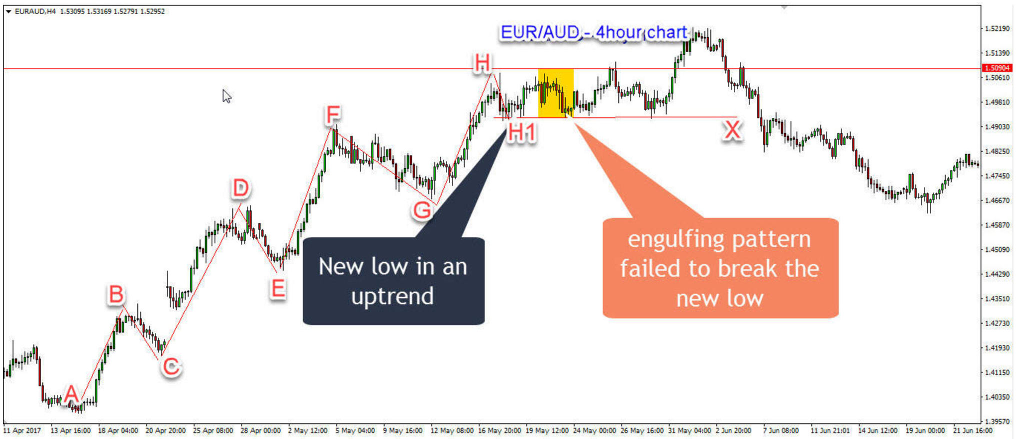
In this case, a daily engulfing pattern was present at a strong resistance area, which meets the first condition of a turnaround. However, it failed to start a reversal of the trend. We are going to look at a smaller time frame to see the reason behind its failure to initiating a downtrend.



In the 4-hour chart, things are much clearer. First, please be noted that the engulfing pattern on the daily time frame is the totally highlighted area in yellow in the picture.

From the 4-hour chart, it is obvious that the market was creating a strong upward trend from A to H. Afterwards, the

H1 low was formed during the process. From H1, the market failed to create a higher high than H, signaling that the bulls are taking a rest. Yet, we still do not have any confirmation about a downtrend. Remember a minimum condition for a downtrend to form is the creation of at least two lower highs and one lower low. In this example, if we see H as the first high and H1 as the first low in a downtrend, then we are lacking one lower low and one lower high.

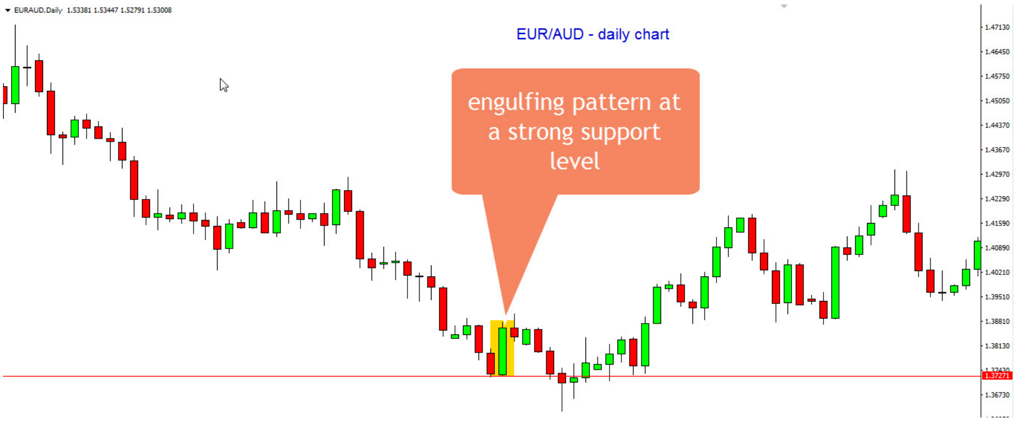


Once again, let's take a look at the yellow area which illustrates the bearish engulfing pattern on the daily chart. You can see how the engulfing candlestick and even a few following candles constantly failed to break the X line - a horizontal line drawn from H1. This indicates that the market structure still remained unchanged, i.e the uptrend still prevailed at least until the close of the daily engulfing pattern. In other words, the selling pressure was not strong enough to win against the bulls' force. When we observe the 4-hour chart, it is obvious that the above-mentioned engulfing candlestick did not carry in it any signs of a reversal in connection with market structure. Put differently, it also failed to meet the third condition of an ideal reversal.

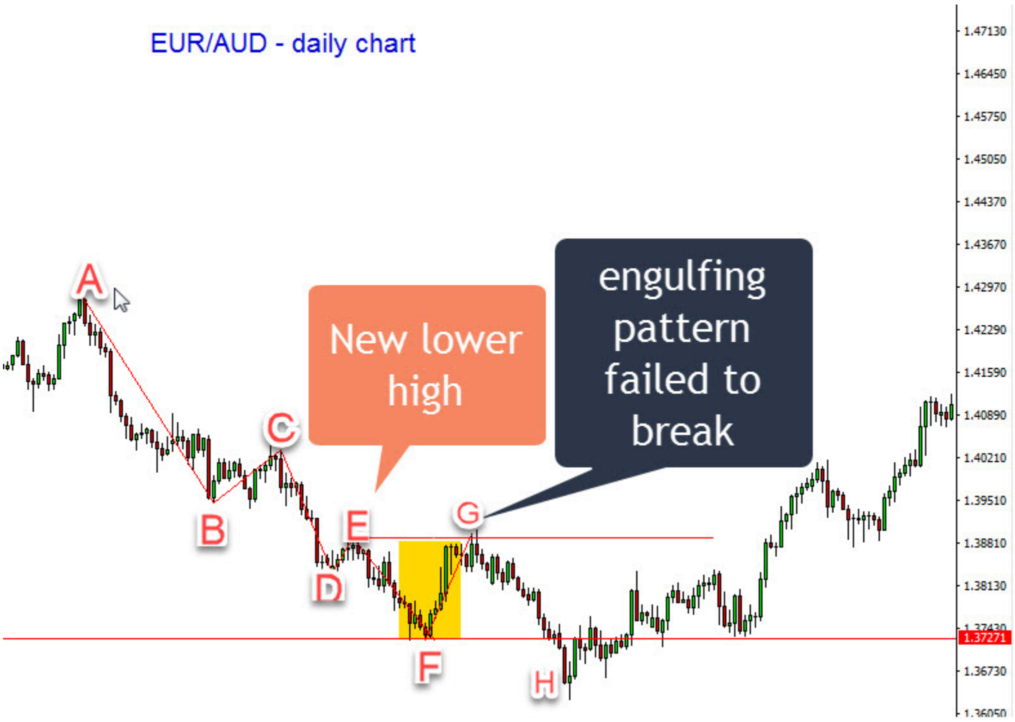
If you are not careful in analyzing this candlestick pattern, you may feel something of a betrayal when a considered profitable pattern failed to work. However, once you know that it failed to meet two out of three needed criteria for a reliable function, you will be relaxed watching the candlesticks move without putting yourself in danger. In a "probability market", we should be prudent and calm.

Trading any reversal after successfully confirming all three conditions would greatly increase the chances of stacking the odds in your favor. Below is another example of a bullish engulfing pattern present at a key support level but fails to start a reversal.

On the daily time frame, things might be ideal for a reversal to the upside…



However, if you had entered a buy entry right after the highlighted bar, you would have encountered a loss. Let’s see what happened on the 4-hour chart below.



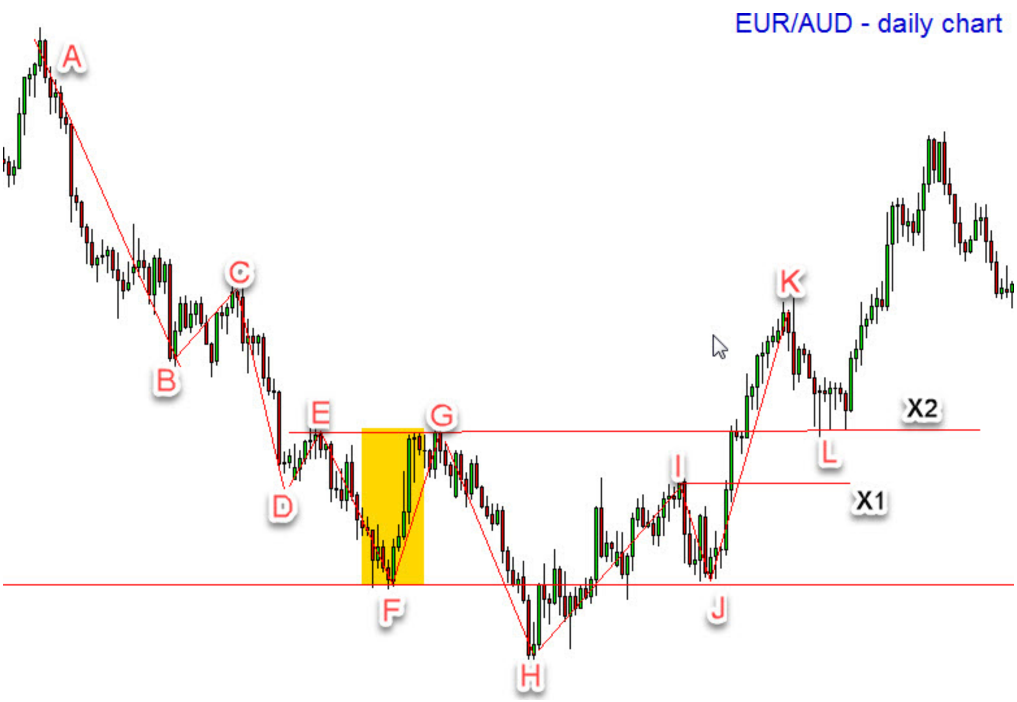
Notice that the daily bullish engulfing pattern is comprised of a few 4-hour candlesticks which are in the yellow box.

Still basing on the above method of analyzing the market, we all see the engulfing bar is located in a key support zone, which satisfies the first criterion of a reversal.

As can be seen, the market was in a clear downtrend from A to F, forming lower highs and lower lows. Then, the bullish engulfing bar tried to break the dominant trend by preventing the market from forming a lower low. Unfortunately, it failed to close above E – the newest lower high at that time. Such failure indicated that no change in the market structure was made, thus any ideas of buying the currency pair should be re-considered. You can see how the market continued its strong downtrend and formed a lower low at H. An uptrend had not been formed till several 4-hour candlesticks later. Once again, the second and third criteria of a reversal were not satisfied. Trading right after the bullish engulfing bar would put you in great danger.

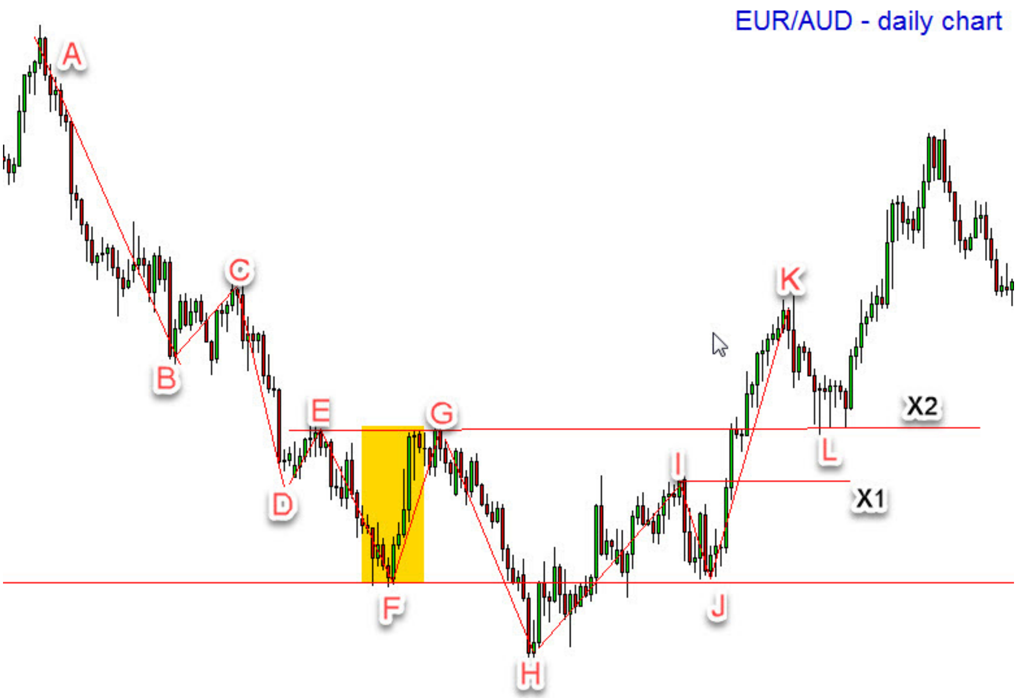
Principle 2: Do not join a reversal trade until the overall market trend/structure has been successfully broken/ changed.

Let's see when and how we could join the market in this situation.



Still on the downtrend, the market continued to make a lower high at I (compared to G). The problem with the downtrend initiated when the market failed to create a lower low at J. This tells us that, upon touching a strong support zone, the sellers were encountering a strong opposing force from the bulls. They then lost the battle at J, pushing prices higher. Should you be in a position like this, be prepared for a buy signal.

The market's effort to touch a key support level at J could also be seen as a retest before a strong upward trend. Trading on retests has always been my indispensable principle in every trade.



On analyzing any market structure, for example from a downtrend to an uptrend, the break of the newest high plays a very important part in whether we should enter a trade or not. In this case, notice how the prices strongly broke the X1 level from J, meaning that the nearest/ newest high during a downtrend was broken. And if you were patient enough, such break served to form a higher high at K.

There we have it. Notice that after the market created another low at L, it was then having two higher lows (J and L) and one higher high (K), which meets the minimum conditions of an uptrend. A change in the market structure was confirmed by L, which is also the ideal entry price in this case. And here is the interesting point. ***Any market structure's reliable change is comprised of three components that will be revealed in the next part of the Chapter.***

Here are the two core reasons I would place an order at L for a high chance of winning.

- Always trade on a retest. Do not be seduced by the market to enter a buy order when a very long bullish bar appears or enter a sell order in case of a long bearish bar. As I mentioned, let’s connect the price with a ball and you will get the explanation. Imagine how a ball quickly bounces back after strongly hitting the floor. And this is how prices work. Prices need a strong base for any strong climb or drop. Before a rally or plummet, just look for a correction of the overall trend. Technically speaking, it is when buyers and sellers are recharging energy for an imminent powerful move.

- When a support level is broken, it is likely to turn into a resistance level, and vice versa. Let’s see how the X2 line played as a strong resistance area in the case of E and G points. After being broken, it turned into a support area and prices tended to make retests upon the X2 level. Do not join any trade without a retest. What is the worst outcome of complying with this rule? Missing a trade.

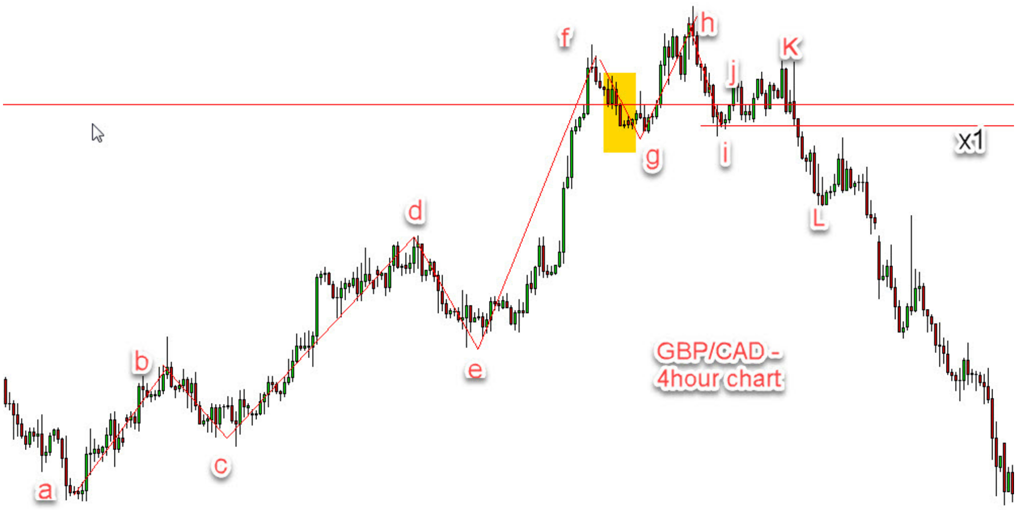
In fact, there is no need to worry if you know there are unlimited opportunities ahead.

And most importantly, your capital is safely protected by trading this way.

Coming back to the daily time frame, the break of the X1 line was clearly illustrated by the second engulfing bar. A strong upward trend was followed by that candlestick.

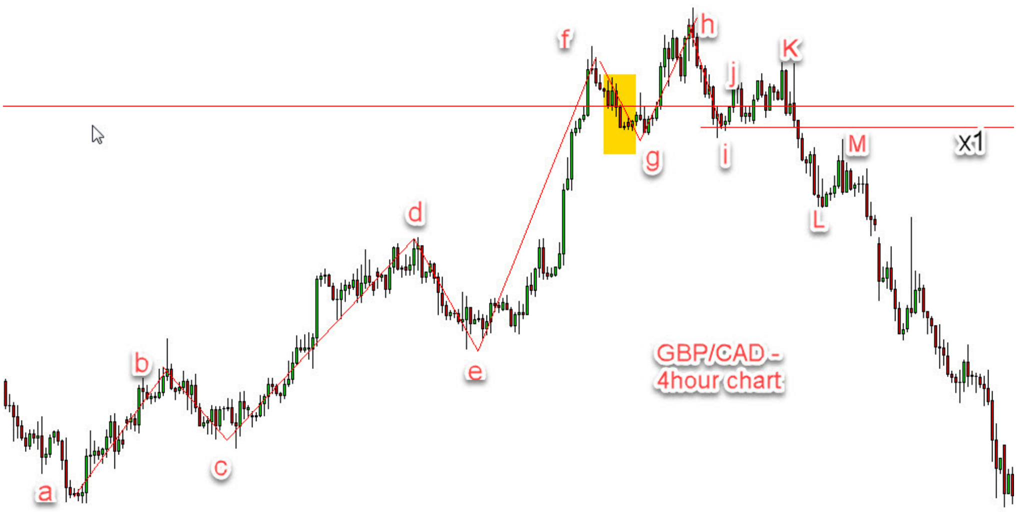
Let’s take a look at another example regarding the GBP/CAD currency pair, and see why the engulfing bar failed to forecast a reversal in the market.

On the daily time frame, an engulfing bar appeared at a key resistance area. However, it failed to trigger a strong enough selling force to pull the price to the below right away. In other words, if you had placed a sell trade right after the engulfing pattern, your order would have hit the stop loss level. With the same way of explanation as in the previous examples, let’s see what happened in the 4-hour chart time frame.



From the 4-hour chart, an uptrend had been prevailing before the bearish engulfing pattern appeared (the daily engulfing pattern is comprised of a few 4-hour candlesticks in the yellow box). It is clear that the engulfing pattern only served to create a new higher low during the overall uptrend (at G). Hence, no reliable bearish signal was present at that moment, and it was best to stay on the sideline.

On looking further in the chart, let's see how the market continued to make a higher high and a higher low at H and I respectively. Yet, the failure to create another higher high at J released the first signal for a downward move.



Then, we have I as the newest/nearest low during the uptrend. From this, I draw a horizontal line, making the X1 line as in the picture. Notice that from J, the market tried two more times to push prices higher but it failed, again and again, forming a top at K. This was when the sellers gathered and battled with the bulls' force which was becoming weaker and weaker. The sellers then won the battle and pulled prices below the X1 line, breaking the nearest low in the uptrend. A new low was formed at L and this was when you should be prepared for a sell signal.

If you still remember a simple characteristic of a downtrend – the creation of at least two lower highs and one lower low – then you will see the importance of M's appearance. It was when the downtrend was confirmed and we had two lower highs (K and M) and one lower low (L). M was what we need to look for an entry price. In fact, it was better if M could touch the X1 line as a retest of the new resistance. Yet, in the picture, the bears seemed so powerful that they prevented the bulls from reaching the level. You can see how strong the downtrend was after the formation of M as the second lower high.

Now, let's stop for a minute for the clarification of MARKET STRUCTURE.

While we can easily identify support/resistance zones on the chart, correct identification of a change in **market structure** is not a simple task at all. In the above examples, I just identify an uptrend or a downtrend based on one basic characteristic. In fact, it is an effective way of explaining the malfunctions of candlestick patterns. Yet, reliable confirmation of a market structure's break should be based on specific components, which will help to determine appropriate entry and stop levels.

As market structure is a concept that has been mentioned in a trading material for the first time here, let me break it down into smaller criteria for you to grasp and best apply in your trading.

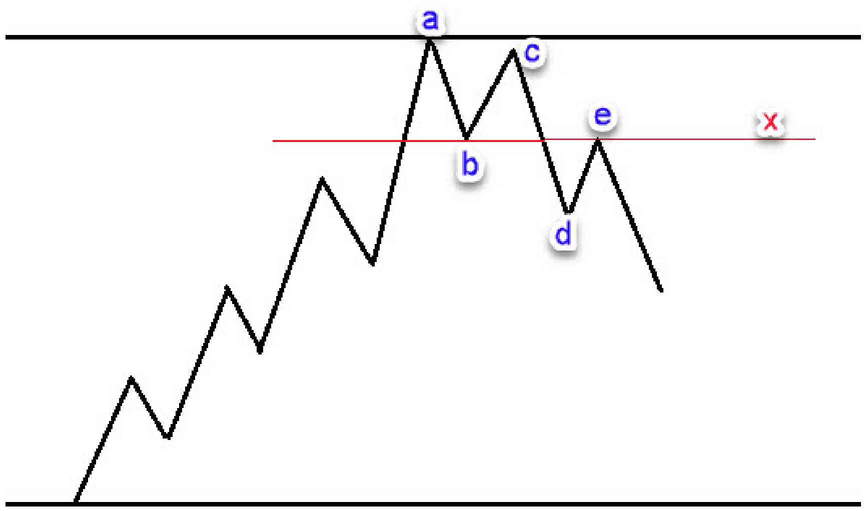
MARKET STRUCTURE – UPTREND TO DOWNTREND

To begin with, reliable confirmation of a change from an uptrend to a downtrend must include:

- Firstly, the market fails to create a higher high. This (not any other criterion) should be the very first sign of signaling the tiredness of buyers on pushing the price higher.

- Prices break the last low in the initial uptrend.
- The market successfully creates two lower highs in the new downtrend, and the second high must not be higher than the last low in the previous uptrend.

To avoid any obscurity, let's take a look at an ideal market structure's change from an uptrend to a downtrend:



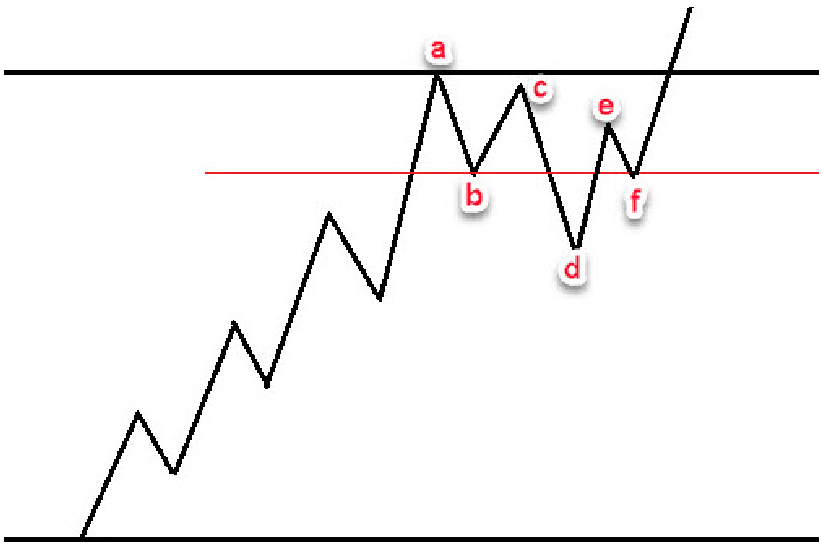
From the example, we can see:

Firstly, the market fails to create a higher high than A. In fact, C could be at the same or lower price than A. It would be preferred if C is located lower than A.

Secondly, prices break the X line, which is drawn from the last low in the uptrend (B), creating a lower low at D.

Last but not least, the market successfully creates two lower highs at C and E, in which E is not higher than B.

Now, let's come up with a popular false pattern that you should watch out for:



In this example, the third criterion is not satisfied. Although the market forms two lower lows than A (at C and E), the second lower high (E) is higher than the last low during the uptrend (B). This may pave the way for another retest at F before an advance. In these cases, it is advisable to stay on the sideline and watch for other reliable market signals.

MARKET STRUCTURE - DOWNTREND TO UPTREND

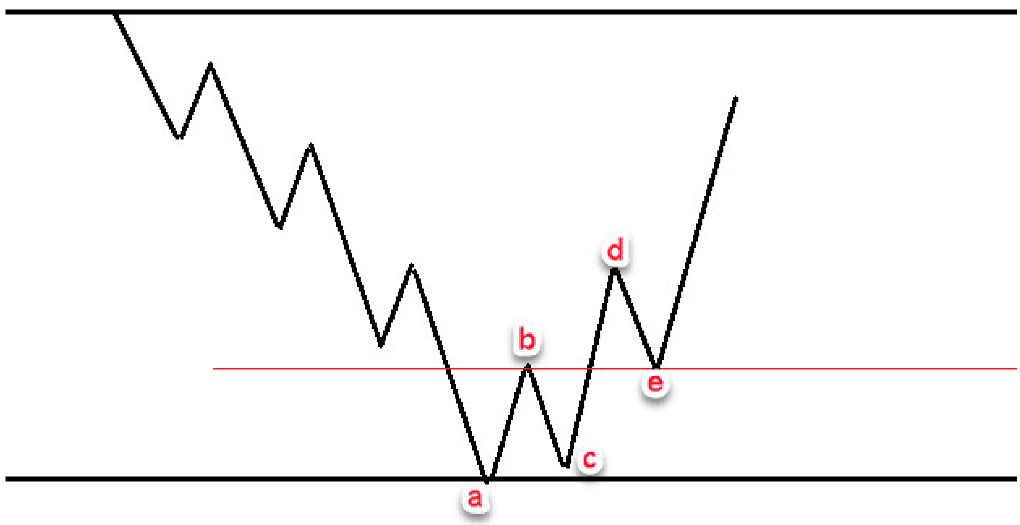
Similarly, for a reliable change from a downtrend to an uptrend to be confirmed, three following criteria must be met:

- Firstly, the market fails to create a lower low. This (not any other criterion) should be the very first sign of signaling the tiredness of sellers on dragging the price lower.
- Prices break the last high during the initial downtrend.
- The market successfully creates two higher lows in the new uptrend, and the second low must not be lower than the last high of the previous downtrend.

Although these three signals are opposite to ones when we consider a change from an uptrend to a downtrend, they are all based on the same principle. Thus, for a quick reference, let me call these three above bullet points "**3MS principles**". Later, when I mention "3MS principles", just understand that I am referring to three conditions for a market structure's change, either from up to down or vice versa.

Once again, it is better you write it down for easy reference later.

Now, let's see how an ideal market structure's change from a downtrend to an uptrend looks like:



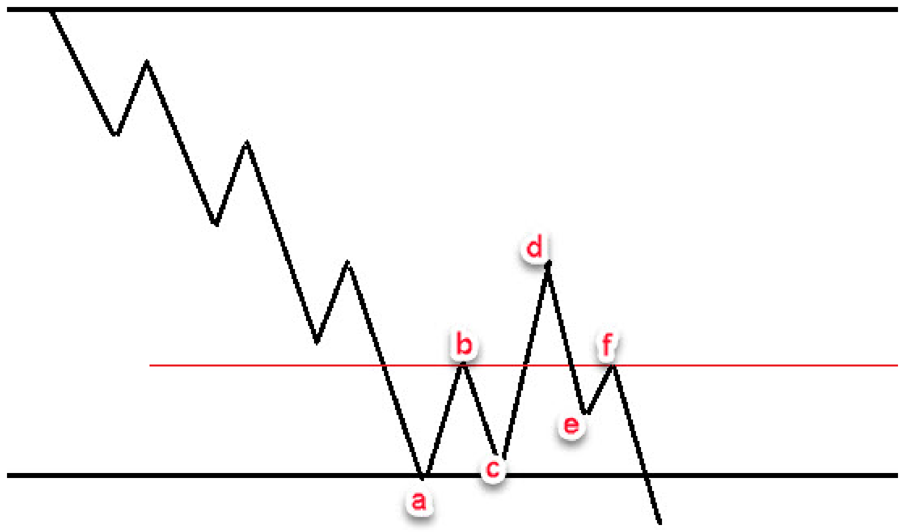
From the picture:

Firstly, the market fails to create a lower low than A. C could be at the same or higher price than A. It would be ideal if C is located a little bit higher than A as we can see in the picture.

Secondly, prices break the last high during the previous downtrend (B), forming a higher high at D.

Last but not least, the market successfully creates two higher lows at C and E, in which E is not lower than B.

Similar to the previous examples, you should be careful when the 3MS principles are not fully satisfied, especially the last criterion. Let's take a look at the below picture:



In this example, one problem arises. Although the market forms two higher lows than A (at C and E), the second higher low (E) is lower than the last high during the uptrend (B). This may pave the way for another retest at F before a plummet. In these cases, it is better not to enter any trade and to wait for more market signals.

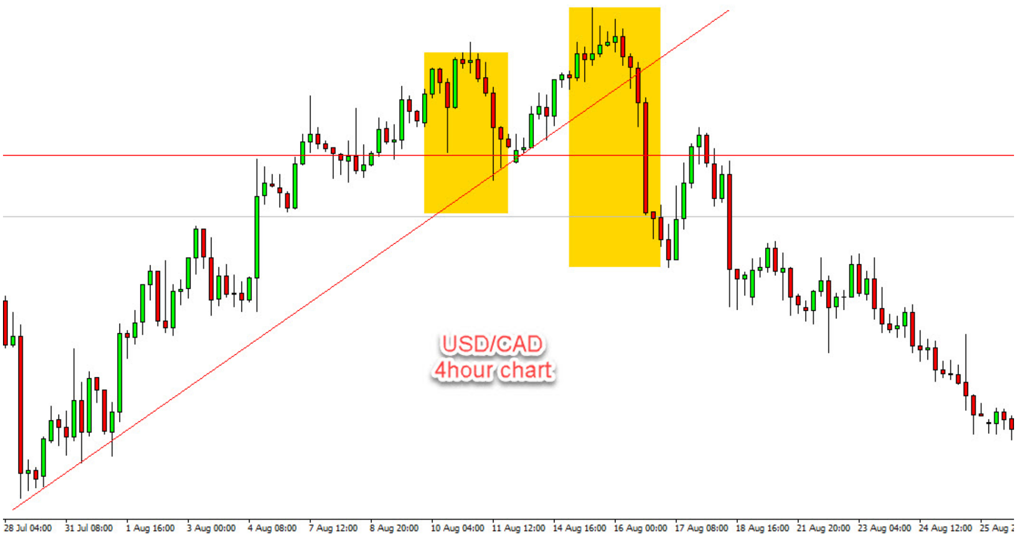
During my trading career, I don’t enter any trades until the presence of all three 3M principles in the chart. This is not to refute the fact that sometimes, we just need two or even one out of the three components for a successful trade. Yet, as I always state, we should be prudent in trading. The more signals we gain for our trades, the better we are at stacking the odds in our favor. I will illustrate this point later in this book.

Coming back to market analysis, I always suggest that the more factors you collect in proving your setups, the more chances of success you will have. In many cases, you can analyze market structure in connection with a trend line, which is, in my opinion, a very powerful method for determining potential market movements.

Let’s come up with another example regarding the USD/CAD pair.

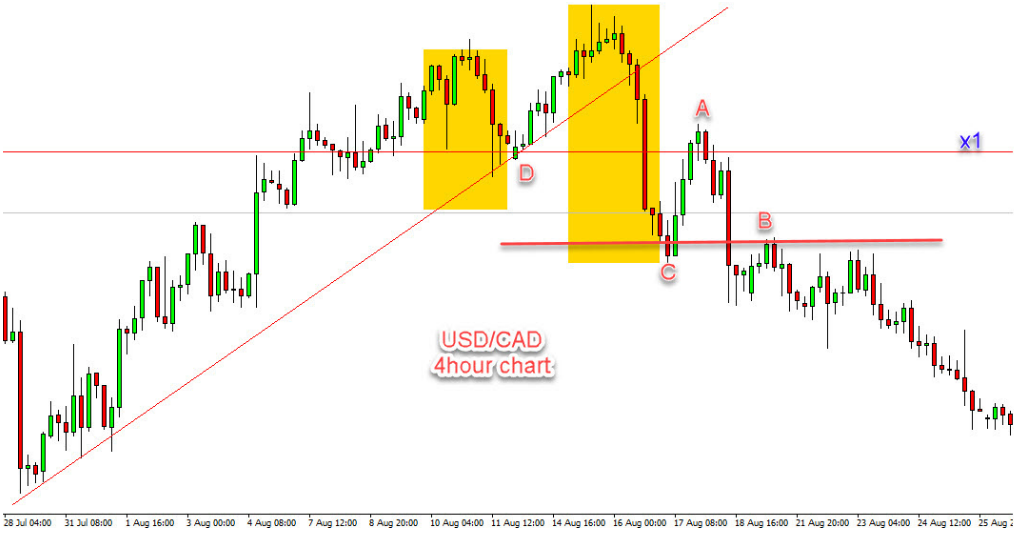
In this example, we have two daily bearish engulfing patterns not far away from each other. However, just one of them works.

Ideally, you can combine with a trend line to see how strong the bearish signal was regarding the second engulfing pattern. Let's take a look at the 4-hour chart time frame, where I often use to determine entry points.



Here it is. Please be noted that the two yellow boxes indicate two daily engulfing bars. First, by using market structure analysis, you can easily explain the first one's failure to drag prices to the below price area, as well as how the second one provided an apparent evidence of selling force dominance.

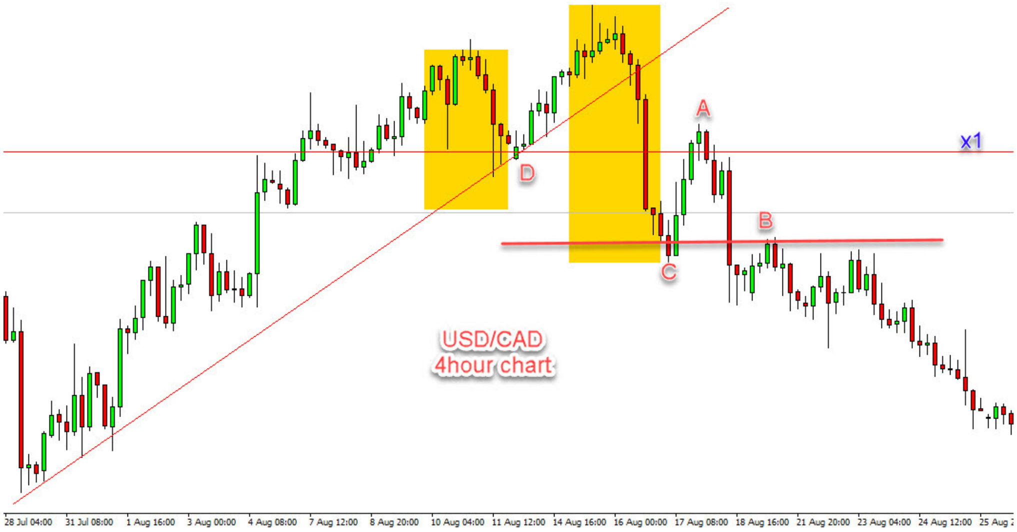
While the two engulfing patterns are locating at a key resistance area, their voices on telling about market structure's change are different. On applying 3MS principles, it is clear that the first engulfing bar failed to meet all three criteria of a reliable change. Put differently, at the time of the first bar's presence, all three characteristics of the 3MS principles were not met, which accounts for its failure to work that time.



On analyzing market structure's change in the second engulfing bar, we can see it **strongly broke the last low** during the uptrend (D) and then **formed two lower highs** (A and B) in which the second low (B) was located at a lower level than the last low in the uptrend (D). The highest peak during the prior uptrend played as the highest top during the following downtrend. The 3MS principles are fully completed (though the **failure to create a higher high** (forming a top at A) came later than expected).

Moreover, you could see how the second engulfing pattern (the second yellow box) was obviously present during the break of the X1 line. This means that the bar itself carried one component of the market structure's break.

All of these account for the reason behind this bar's function on market reversal's angle.



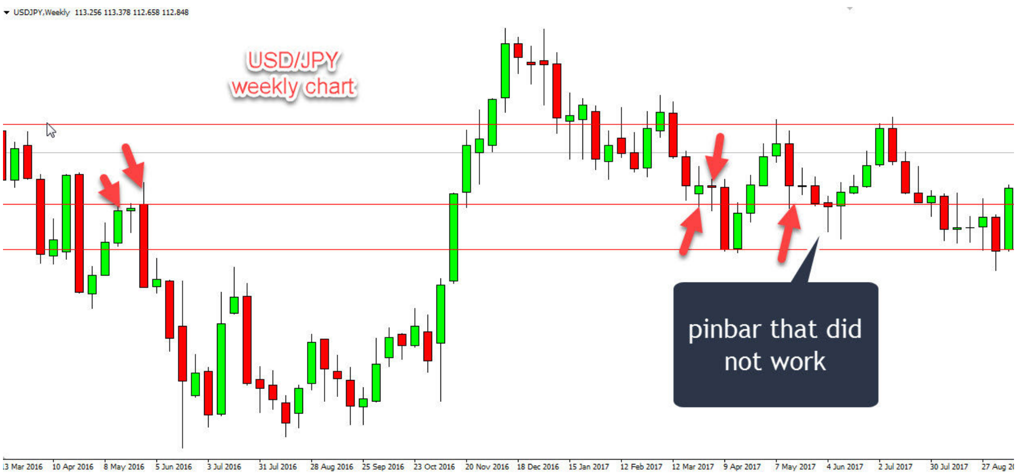
Moreover, by drawing an upward trend line, it is even clearer the first engulfing pattern failed to break the trend line on the 4-hour chart. Conversely, the second engulfing pattern indicated a much stronger selling pressure, breaking the trend line and pulling the price to the below area.

In short, the market structure clearly tells us the correlation between bulls and bears, which side is stronger. Ignoring this may mislead you and result in unexpected losses. In trading, nothing is 100% certain. Hence, the more criteria you have gained through technical analysis, the higher chance you stand on winning trades. This is how you put the odds in your favor.

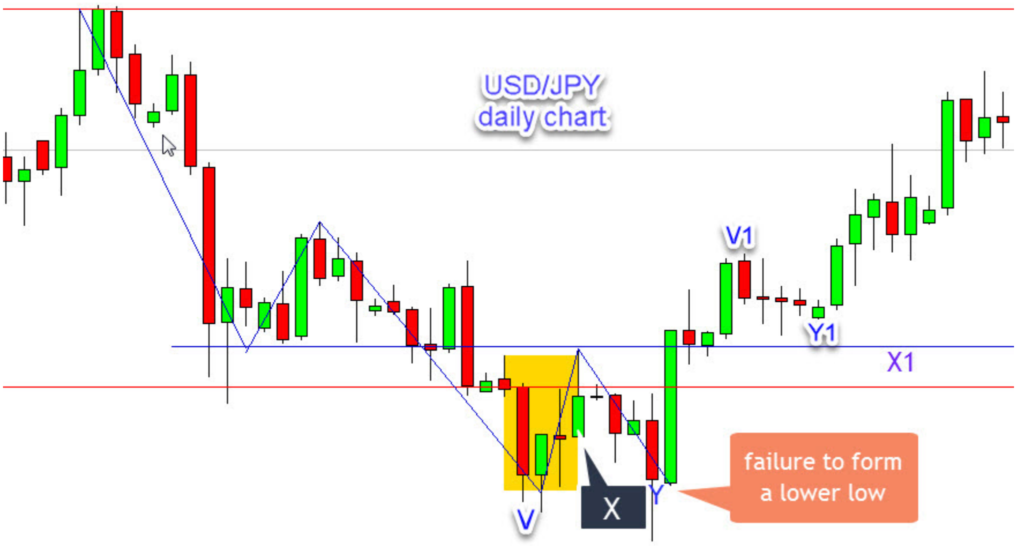
CHAPTER VIII: PIN BAR TRADING WITH 3MS PRINCIPLES

Things are similar when we consider pin bar setups. You need to put any pin bar in a big picture, i.e ask yourself whether candles indicate a reliable market reversal using the two compulsory conditions of a turnaround that I mentioned. Furthermore, regarding pin bar trading, you also need to determine (on the closing price of the pin bar) whether it carries any signal of a reversal in connection with market structure analysis or not. If not, stay on the sideline and wait.

Let’s take a look at a weekly pin bar on the USD/JPY chart:

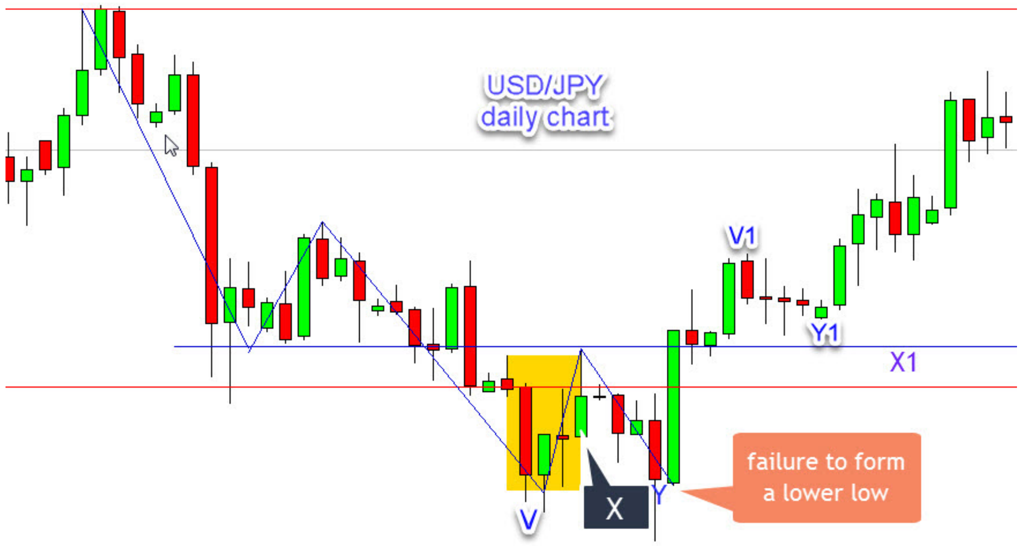


Notice how a pin bar pattern was present at a key support and resistance area. This level had been touched a few times before (see “arrows”) without being broken. At first glance, trading this pin bar seemed to bring about a high chance of success. However, things were not that wonderful. In fact, if you had entered a buy order after the first pin bar (the red one) appeared, you might have made a loss. Let’s see what happened on the daily time frame when we break down the weekly candle into daily candlesticks.



The first weekly pin bar is comprised of five daily candlesticks that are highlighted in the yellow box. It can easily be seen that the last daily candlestick (the X one) in the yellow box tried to reach the X1 line. This line was originally a support level, yet it was broken and turned into a resistance level. The X candle's failure to get access to the X1 line indicated that the buying force is not strong enough to beat the bear's strength. In other words, when the price moved closer to the X1 resistance level, the sellers constantly jumped in to dominate the game. After all, the X candlestick just served to form a new lower high in an overall downtrend. The market structure remained unchanged then.

The first signal of a reversal only appeared at Y, when the market failed to create a new lower low. At this time, sellers are losing their steam and the buyers jumped into the battle to form a long bull candlestick right after the red candlestick Y. What is interesting about this bullish candlestick? Yes, it was an obvious engulfing pattern and it closed just above the last high during a downtrend, paving the way for the market structure to change to an uptrend. You can see how the prices escalated after this directional bar.

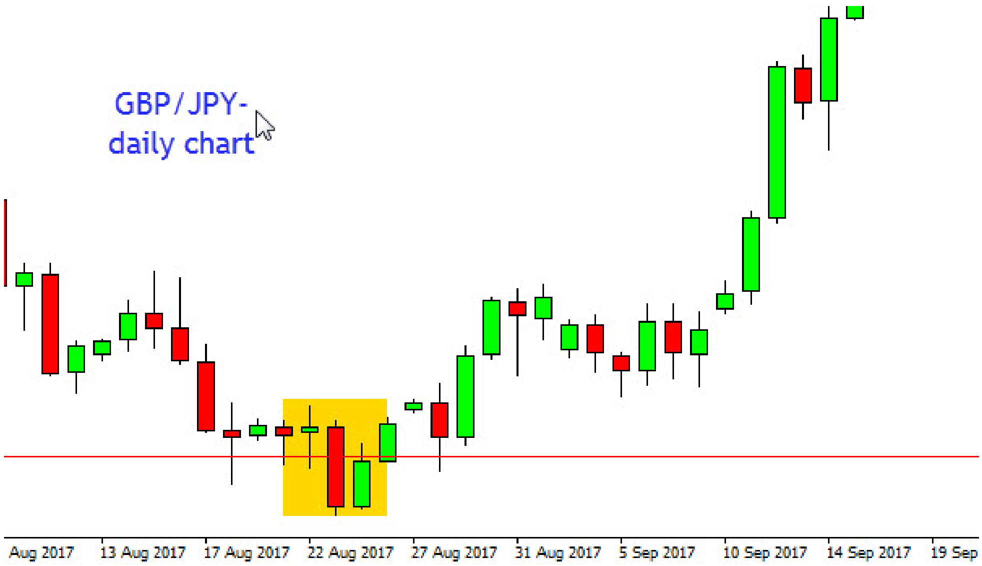


Notice that a change in the market structure was not confirmed after the long bullish engulfing candle. On applying the 3MS principles, we need at least two higher lows. Given that, it was only advisable to place a buy trade after the Y1 low had successfully been formed. Then we were having two higher lows at Y and Y1, and trading at Y1 is much safer than trading right after the bullish engulfing bar.

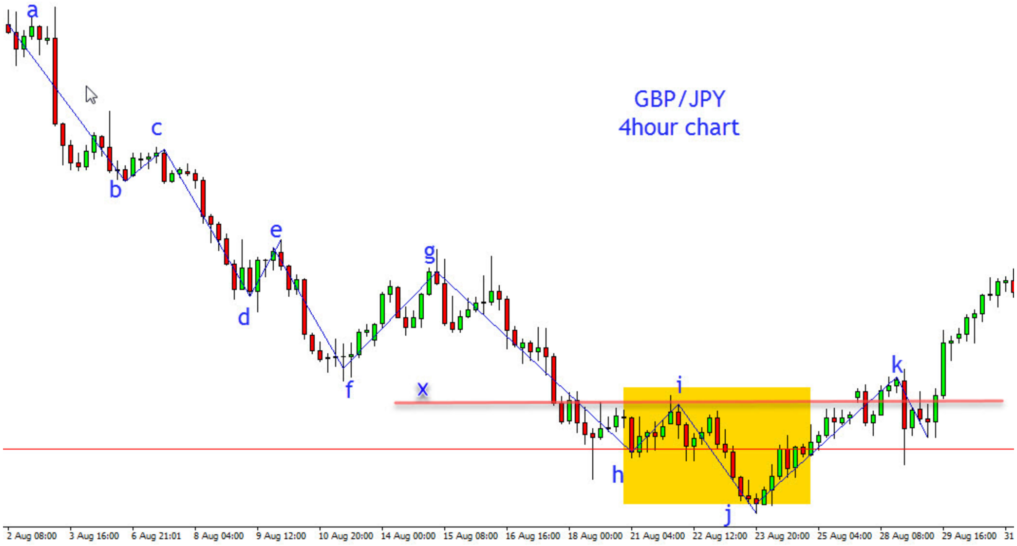
You can see how ideal this pattern was in connection with my philosophy on market structure analysis. First, the market **failed to create a lower low at Y**, then it **broke the last high** during the previous uptrend. And after **two higher lows were formed (Y and Y1)**, the place of a buy order following the formation of Y1 low (the second higher low) would be a safe choice. While a relevant stop loss would be below the X1 line a few pips, the profit-taking level should be the next resistance.

We have seen various examples of false engulfing patterns and pin bar setups due to the failure to break the market structure. Let’s see how an ideal pin bar looks like in the following example:

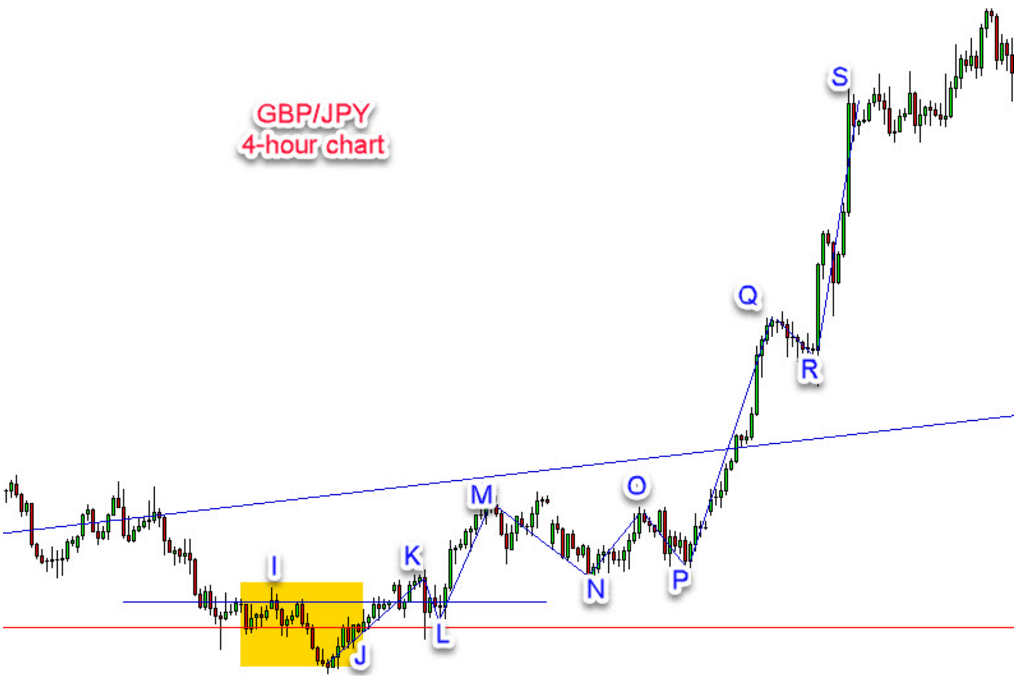
We start with the weekly chart. As I always emphasize, an ideal pin bar (or any other candlestick pattern) must be present in a key support or resistance area. The pin bar we mention here fully met this criterion. Notice how a lot of previous weekly candlesticks tried to push through the support/ resistance level without success, making it an ideal level to consider trade setups.



On a daily chart, the above weekly candlestick is comprised of five daily candlesticks in the yellow box. On Wednesday of the week, the market formed a strong bearish candlestick (the long red one). However, during the two following days, buyers completely dominated the market, making two strong bullish candles that engulfed the prior red candlestick. This indicated that the sellers had tried to drag the price lower and continued the overall trend. However, they seemed to lose their energy and lost the game to buyers, who successfully closed the market with a price level above the key support area. To gain a deeper understanding of the market structure, let's take a look at the 4-hour chart to see how the buyers managed to control the game.



Let’s start with an overall downtrend picture with the starting point at A and the ending point at J. The weekly candle was comprised of all 4-hour candles in the highlighted yellow area. It was apparent that by the end of the week, the market structure hadn’t been changed. However, in the following weeks, the market successfully broke the X line drawn from I (the last high during the downtrend). Such break **initiated** a change in the market structure from the downtrend to the uptrend, resulting in creating a new high at K.

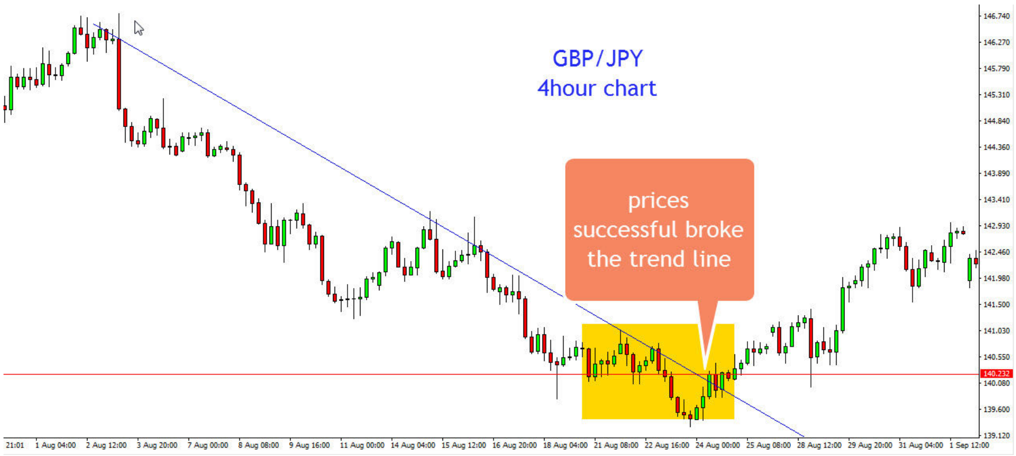


Notice how the 3MS principles worked well in this case. While the market **broke the last high** (I) during the previous downtrend and formed the first high during a new uptrend (K), it **failed to create any lower low than J**. As I have stated, a reliable signal of a market structure's change (in this case from a downtrend to an uptrend) must include at least two higher lows (in comparison with the lowest low). As you may observe, after **forming two higher lows at L and N (N was not lower located than I** – the last high during the previous downtrend), the market made a strong rally.

Some people might be in favor of placing a buy order at L when the market failed to break a very strong support area (illustrated by the red line). While I admit that the signal here was quite reliable (analyzed on a key support zone), I still warned that by trading this way, you were ignoring the last criterion in the 3MS principles (at least 2 higher lows). If I had been in that case, I would have traded after N was formed (for more safety).

I do agree that in some cases, you do not need all the three factors in the 3MS principles for a successful trade. This lies in how you weigh risks and rewards in your choices. While trading should be prudent, it should not be too rigid. A buy order at L would be preferred by many traders, and they have reasons to risk there. Sometimes you have something of a gut feeling on entering trades and making (big) profits. What I have provided to you here is a "proven framework" that I believe if you apply consistently, you will be consistently profitable. I hope you have got my point.

Also, I always recommend traders combine more indicators in their market analysis. In this example, a combination with a trend line would boost your chances of success. Let's see how the above-mentioned weekly pin bar successfully broke a strong trend line (a trend line that had been touched many times without being broken) on the 4-hour chart. Take a look at the below picture.



A very interesting point of the market structure is that you can trade with pure price action without relying too much on candlestick patterns. In this way; trend line, support and resistance as well as retests all play an important role in any trade entry and stop levels. Having said that, I do not mean to ignore candlestick patterns or so. What I want to convey is that in any price action analysis, we should combine as many market factors as possible to obtain the “confluence” effects from the market. A confluence occurs when at least two indicators turn the green light for you to join the market. The more approval we receive from these factors, the higher chance we stand to win the trade. Yet, the sole use of market structure analysis can still bring higher chances of success in comparison with mere candlestick patterns because it tells us about core market movements.

CHAPTER IX: INSIGHTS INTO DOUBLE TOP/BOTTOM TRADING

Along with pin bars and engulfing patterns, double top patterns are among the most common setups on the chart. In fact, the use of market structure analysis can be easily connected with double top or double bottom trading. We will discover more in the following examples.

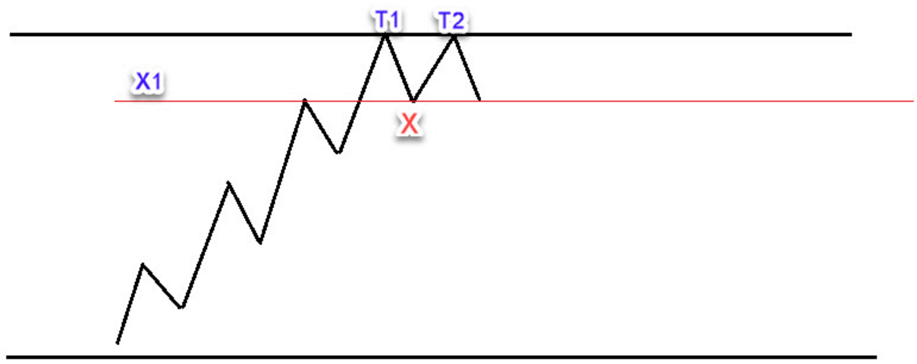
1. Reliable conditions for a double top/bottom to work:

- It is positioned at a support/ resistance level

As I have stated, any candlestick pattern must be analyzed in connection with support/ resistance level. In other words, trading candlestick patterns without referring to support/ resistance levels could put you in great danger. The stronger any support/ resistance level is (when it is touched many times without being broken), the more reliable it is. In fact, candlestick patterns occurring on these key levels are more likely to generate a reversal in the market.

To avoid repetition, let's take a look at the double top pattern. The double bottom pattern is just similar. If you can grasp my intention regarding double top trading, the other would not cause you any puzzles.

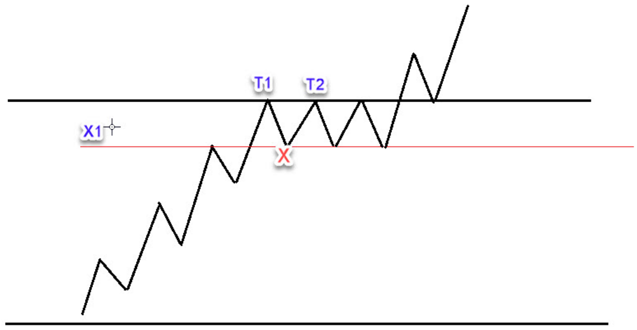
To begin with, please note that like a pin bar or engulfing pattern, the double top/bottom is considered a reversal signal in the market.



From the picture, the market is in an uptrend before it encounters a key resistance area. From there it creates the first top at T1 before bouncing back to X and forming the second top at T2. In any double top pattern analysis, the X point (clearly illustrated by the X1 line drawn paralleled with the support and resistance line) is a very important point in determining the entry-level in the market. More on that later. In the meantime, X1 is called the neckline.

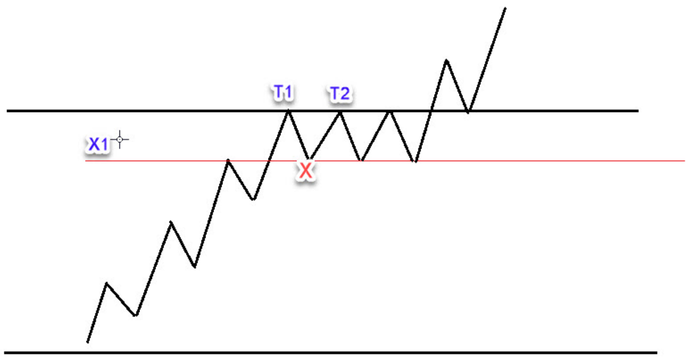
After we have found a double top/bottom pattern situated on key levels, let's take a look at the market structure. The market is strong in its uptrend until T2 appears. Before the presence of this "second top", T1 and X play as the newest high and low, and those who are in favor of an uptrend would expect a formation of a higher high than T1. Yet, the second top at T2 negates this scenario and paves the way for a double top to form. Please be noted that T2 is not necessarily the same height as T1. In fact, **it would even be better should T2 be present at a lower level than T1**. The appearance of T2 also meets the **first criterion in 3MS principles** – failure to form a higher high during an uptrend.

One point I want to note here is that we still cannot confirm a complete formation of a double top after T2 appears. Let's take a look at an unexpected scenario in which a potential double top fails to work with its original function.



In this scenario, the appearance of T2 opens the first opportunity for sellers as buyers show signs of tiredness. However, prices cannot break the X1 line a number of times. Instead, it moves sideways between the upper resistance and the X1 line before breaking the resistance and continuing its uptrend. This is an unfavorable situation that costs traders a lot of money for the fears of missing out (FOMO – as you often hear about in trading).

If you have grasped my 3MS principles, you could easily avoid unexpected loss in this case. The market fails both **to break the X1 line** (drawn from the last low during the previous uptrend) and **to form at least two lower highs than T1**.

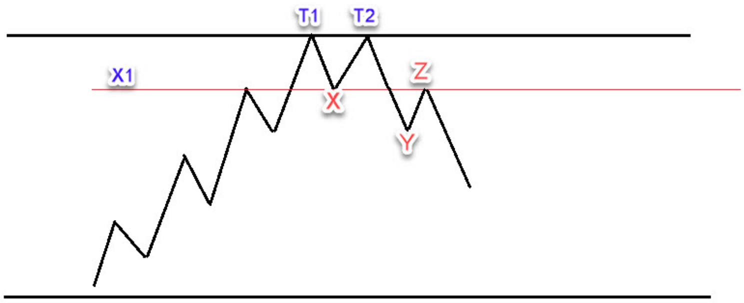


We can see this scenario from another angle. Remember which characteristics of a downtrend movement are. Yes, they are "lower highs and lower lows". Think about it. If you assume the uptrend has officially ended and a downtrend has been launched, problems may arise. In fact, the X could be seen as a low during a potential downtrend, however, we have not witnessed any lower low, thus the downward signal here is not obvious indeed. Put differently, the uptrend is still prevailing and should be given priority on trading. Simple as that.

Remember that trading obscure or unclear patterns is unlikely to stack the odds in your favor. I have always tried to state one principle in all my books that you should just **stay on the sideline** and **wait for good setups** upon encountering unclear signals.

- Wait for the price to break the neckline

It is exactly what the **second condition in my 3MS principles** is about. In fact, a double top pattern is only confirmed after prices break the X1 line (the neckline). Take a look at the below picture.

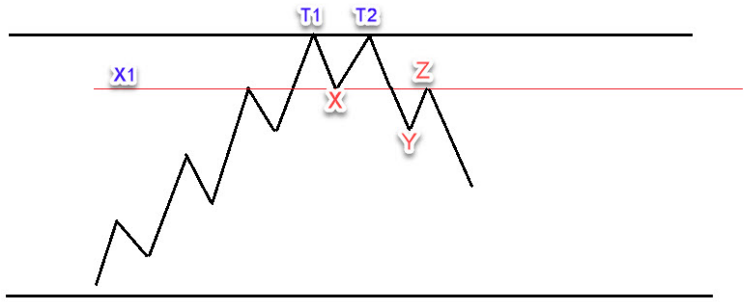


Yes, we've found it. Y is exactly what we are looking for. Once the price breaks the neckline and forms a lower low at Y, the double top pattern is "officially launched" and we just wait for one more retest at Z to enter a trade with much more chances of winning. Also, the formation of Z meets the **third criterion in my 3MS principles**. Now we are having two lower highs at T2 and Z (Z is not at a higher level than X).

2. How to trade double top/bottom

In the above picture, the best trade entry should be placed around Z when the market retests the new resistance level (X1 line, once broken would turn into resistance). Meanwhile, the stop-loss should be placed just above the T2 and profit-taking should be targeted at the next support area. More on stop loss and profit-taking levels later, and this is how my strategy is a little bit different from those in other books.

- Let’s take a look at the entry point first.

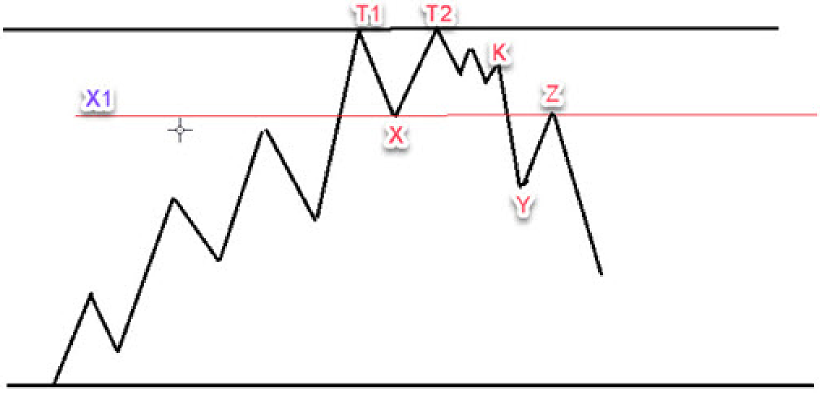


Some of you may ask me: “Hey Frank, why not enter a sell order at T2, which seems to be a better price for sellers?”

A good question indeed. I always recommend traders do things that bring them more chances of winning. In trading, nothing is predictable. It is a game of probabilities. You would understand more about this very crucial characteristic of the market after you read the classic book “Trading in the zone” by Mark Douglas.

Let’s get back to my advice that you should not do things that are just a matter of luck. Trading at T2 might be an example of placing your trade on luck as sellers’ pressure is not obviously overwhelming the buying power. I shall not deny the fact that sometimes you can be right on trading at T2 and yielding big profits for yourself. Yet, to me, it is more secure to enter your trade at Z when all the three 3MS principles have been confirmed. I will not guarantee that you will a hundred percent win on trading at Z. Trading does not have anything to do with being right or wrong on any individual trade. It is closely connected to your long-term view. Honestly, I believe that a consistent practice of these mindsets and techniques presented in this book would benefit you in the long term. If you repeat the best possible actions with a large enough number of trades, you would find yourself gradually joining the “consistent profit group”.

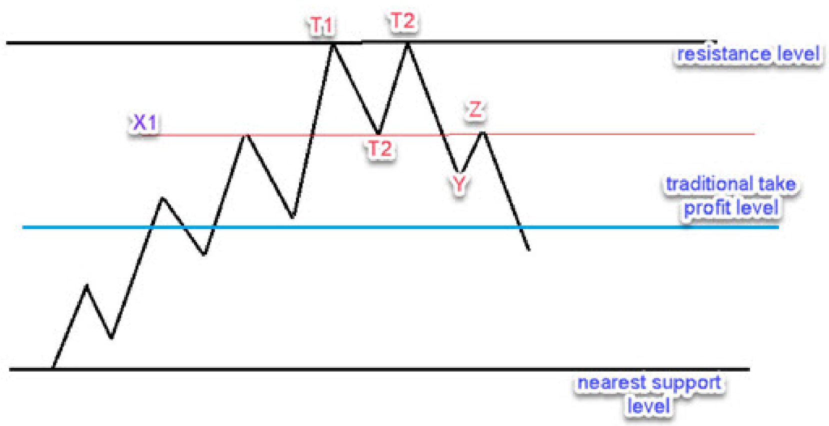
- How to set stop-loss and take-profit levels.



While I strongly agree that, basically, you should apply the traditional use of stop-loss setting, i.e a few pips above T2 (a safe/prudent stop loss level), I suggest you consider specific market movements and structures before deciding on your best possible stop-loss levels. The above picture should be seen as a typical example.

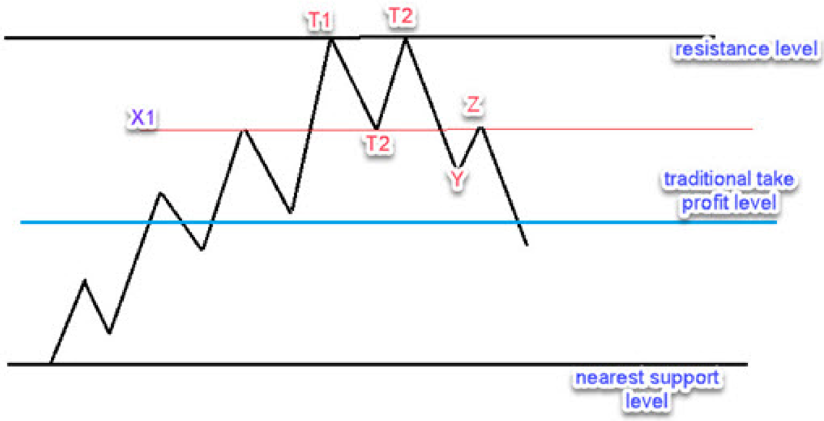
Before creating an obvious lower low at Y, the market makes certain hesitance from T2 to K. The seller's side is a little bit stronger than the buyers, though not distinct. From K, the market strongly breaks the key X1 line and confirms the formation of a double top pattern. If you have traded long enough, you may somehow share with me the idea that on trading at Z, the stop loss is not necessarily placed above T2. Instead, placement of stop loss just above K could save you from unexpected losses while bringing you a better risk-to-reward ratio. Notice how the market constantly creates minor lower highs and lower lows from T2 to K, signaling that the sellers are gaining strength more and more. While increasing your risk-to-reward ratio, a stop loss above K would not be likely to deprive you of any opportunities in case of a rally above the K level. In other words, if the price closes above K level, it will be better to stay out of the market.

Where to take profit?



If you have read some books on the double top pattern, a recommended profit level would be a distance similar to a distance from the entry point (the neckline) to the top, i.e 1:1 ratio. This is a safe profit level in my opinion, yet the risk-to-reward ratio is not preferable in trading. In fact, in order to maximize your trade efficiency, I do not recommend the above 1:1 ratio. Not only it is not a "long-term profitable ratio", but it also goes against the necessary flexibility in trading. It is a fixed ratio, which indicates rigidity in trading. You should be rigid in your money management, i.e never risk more than 2% of your capital per trade or do not risk more than 6% of your capital per month. This is clearly described in other books of mine.

However, a rigidity in profit-taking often serves to deprive you of potentially bigger profits. In fact, the situation of watching the market moving down more hundreds of pips after you have closed your sell order is highly likely to create a FOMO (fear of missing out). At that time, emotions are getting the best of you and it is the shortest way to encounter losses.



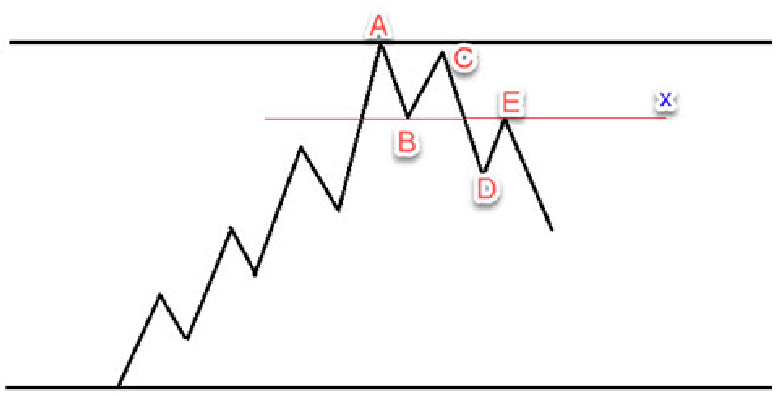
In my opinion, the best profit level in double top trading should be the nearest (key) support level. It is where there is a higher chance of price reversal. Take a look at the above picture. The nearest support level gives a better risk-to-reward ratio, and you would be able to yield more profits from your trades. After a large enough number of trades, you would find how effectively it works.

CHAPTER X: 3MS PRINCIPLES – FROM DOUBLE TOP/BOTTOM'S ANGLE

Now, let's dig deeper into market structure analysis in connection with double top/ bottom patterns. For example, let's take a look back at what I mentioned above regarding a reversal from an uptrend to a downtrend. If you still remember, there are three criteria for determining a change in market structure:

- Firstly, the market fails to create a higher high. This (not any other criterion) should be the very first sign of signaling the tiredness of buyers on pushing the price higher.
- Prices break the last low in the previous uptrend.
- The market successfully creates two higher highs in the new downtrend, and the second high must not be higher than the last low in the previous uptrend.

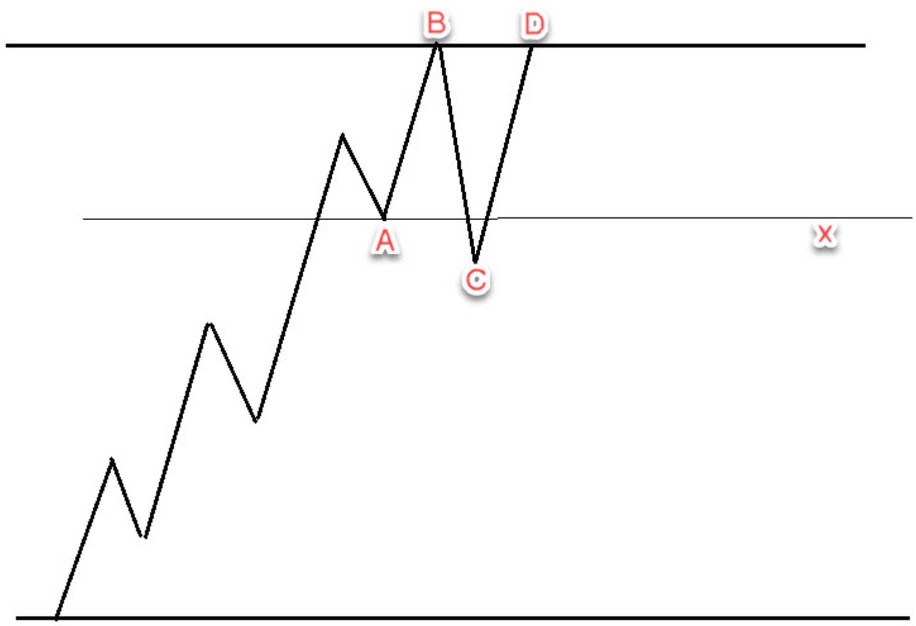
Have you ever wondered why I emphasize the failure to create a higher high should occur prior to the break of the last low in the previous uptrend? Looking at the big picture, it is when the market is strongly dominated by the sellers and the chance of winning the trade is high. The picture below clearly illustrates the point. Moreover, notice that I often recommend you trade on setups that satisfy all three 3MS principles. Look at the below example for an ideal double top trading:



Notice that in this example, the market **fails to make a higher high** than A before **breaking the neckline**, and this is my favorite scenario.

To start with, the market is in a strong uptrend until A, before it fails to create a higher high at C, forming a double top pattern. In any trade, it is better if C is a little bit lower than A. This shows that buyers try to retest the A level, however, the bears are so strong near the resistance and immediately negate the bulls' force, dragging the price to the below area. It is the first signal of the market failing to remain the uptrend momentum. When prices break the X line and form a lower low at D, you should be prepared for an upcoming sell order. Then, another retest at E is ideal for a sell order. This setup fully satisfies all my 3MS principles on market structure's change, which is more likely to turn your trades into winning ones.

On the other hand, things are a little bit riskier on trading the below pattern.

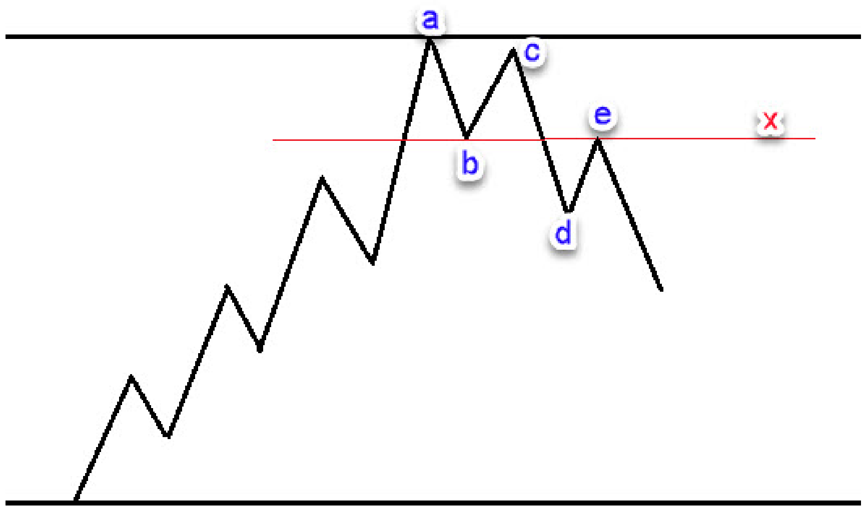


In this picture, the uptrend is strong until B. While the market has yet to express any signs of failure to break the highest high (B), it suddenly breaks the last low in the initial uptrend.

The bears seem to outshine the bulls this time. Starting from B, which is the highest high and is positioned at a key resistance area, many traders may be confident in a reversal in the market. They try to pull the prices lower than the X line (drawn from the last low during the uptrend, parallel to the resistance level), forming a low at C. While it may seem that a break at X line paves the way for the formation of a downtrend, there are two potential dangers that traders need to take into consideration.

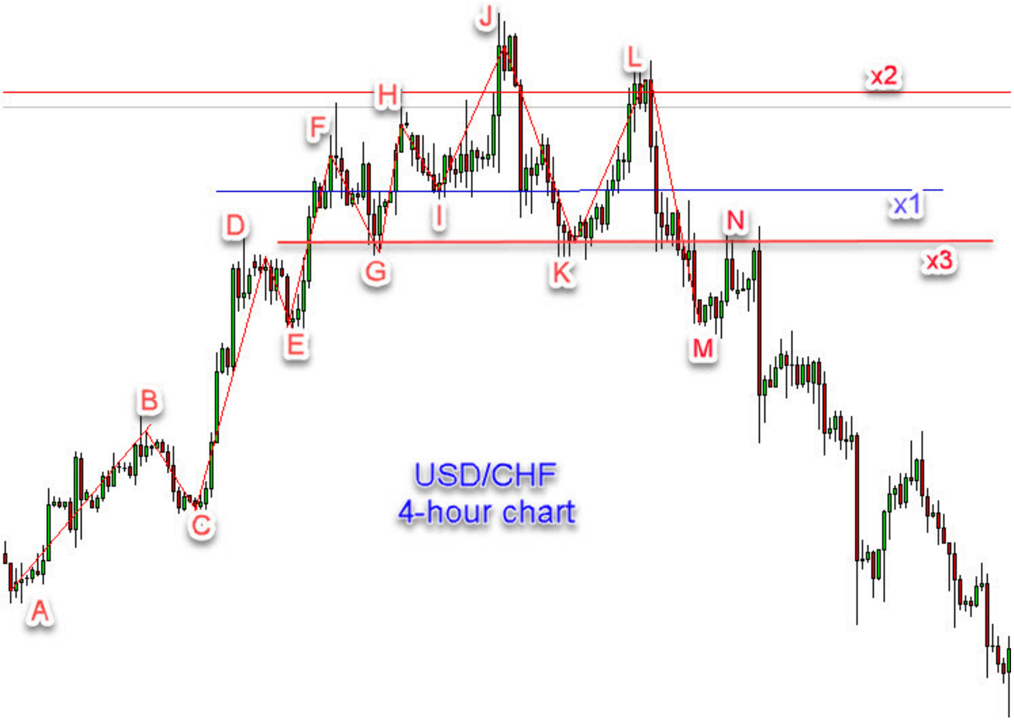
First, as I have mentioned, in order for a market structure to change from an uptrend to a downtrend, there should be enough criteria of **3MS principles**. As such, this pattern fails to meet the third criterion. Hence, in this example, an “official” downtrend has not been launched. As the downtrend has not been confirmed, the chance of winning the trade is not as high as in the previous example. I always state that in an unpredictable environment, if method 2 is better and more secure than method 1, stick to method 2.

Second, as I mentioned in the previous Chapters, in most cases, the market tends to come back to retest support/ resistance. To be honest, it is normal you find numerous double top/bottom patterns on any currency pair’s charts. Considering that, it is not advisable to enter a sell trade (or a buy trade in case of a reversal to the uptrend) until a double top appears. This is exactly what many successful traders apply in their trading. Turning back to the previous example, let’s see how the market beautifully creates a double top pattern, coupling with signaling a clear change in market structure by forming two lower highs at C and E.



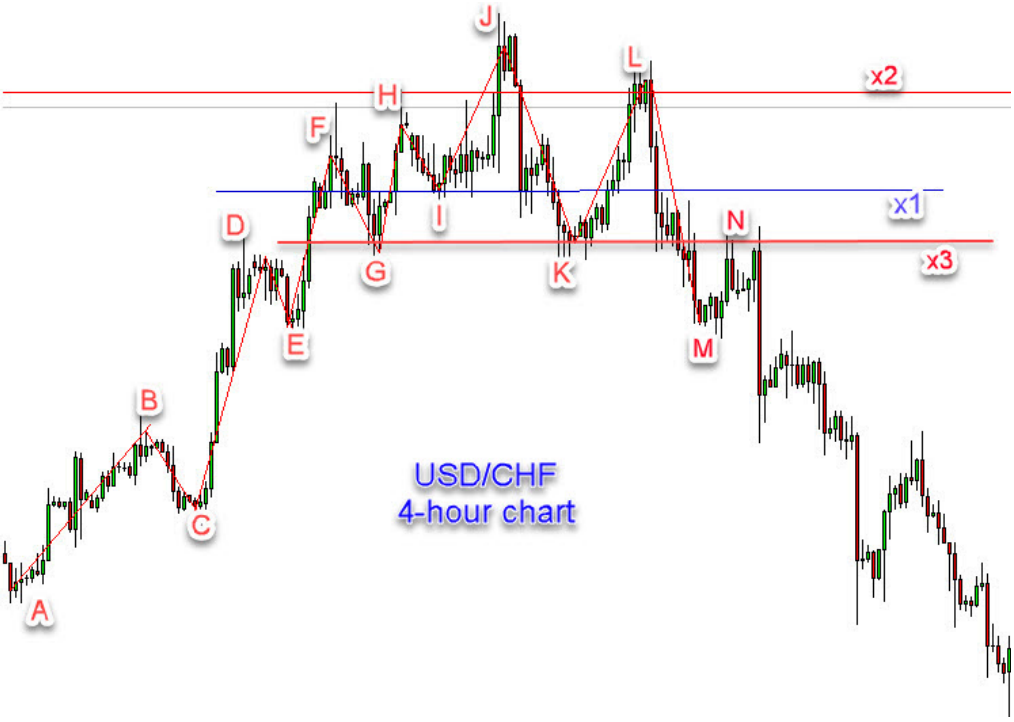
Honestly, I do not refute a fact that in some cases, the market would plummet without retesting support/ resistance. And in these cases, you can still make profits without waiting for the market to form an "official" downtrend (forming at least two lower highs after the top A). However, to me, the more prudent, the better. It is not advisable to take unnecessary risks in this market.

Below is a real example of a market reversal from an uptrend to a downtrend. Notice how an early sell entry could bring about an unexpected loss.



In this example, there was a clear uptrend from A to J. From there, the market successfully broke the last low in the uptrend (i.e the I low) and formed a lower low at K. You can see how risky it was to enter a sell order without waiting for the market to form the second top at L (double top pattern).

While it was not ideal when the market broke the last low right from the uptrend peak, let's see how patience could help you with the case, which puts the pattern into 3MS principles' application.



As can be seen, from L, the prices broke the X3 line (drawn from the newest low in the market) and the market formed a new low at M. It was when you should be prepared for an upcoming sell order. Another retest at N would be ideal for a sell entry, with a stop-loss just above X1 (nearest resistance) and a profit-taking level set at the next support area. You can see how effectively the 3MS principles work upon entering your trade at N. Put differently, a sell order at N fully satisfied all three 3MS principles, which puts the odds in your favor.

On another view, remember that in any analysis, a combination with trend lines (if any) should not be ignored, because it is among the easiest and most effective market tools to use on any market reversal. In the below example, let's see how the trend line gives us another option for an entry point.

As can be seen, the break of both horizontal support line and cross trend line brought about a great entry point for the bears. Prices then plummeted, forming a strong downtrend to the below.

Please be noted that to avoid certain repetition, I just mention the downtrend trading. Uptrend trading regarding the double bottom pattern just bases on the same principle. I believe if you clearly understand the former one, you will surely grasp the latter.

After all, trading is not a rigid venture and your decisions should be made based on specific market movements. In fact, how the market moves is unique each and every single time. You should not expect any future market movements identical or similar to the examples I use in this book. However, I am fully confident the all principles presented in this book will work and bring you consistent profits because they are what I have summarized after having tried hundreds of times during my trading career. Results cannot lie.

WHAT'S NEXT?

While there are many other reversal trading techniques out there, I believe the techniques that I have brought to you via this book are among the most effective. Successful traders are simple ones. Have you ever heard a comment like this (either on the internet or in real life): "*Good trading should be boring because we just need to use only one system and make profits again and again with it"*?

If there is one thing that urges me to write this book, it would definitely be the ***market structure analysis*** that brought me an "aha" moment.

I suggest you back-test as many candlestick charts as possible using the **3MS principles** presented in the book. I really hope you can grasp my shared techniques because I strongly believe they all benefit you both in short-term and long-term trading.

If you learned a few things and found them interesting, I would be very grateful if you would consider leaving me a review with a few kind words. Click here to write a review.

—***[FRANK MILLER]***

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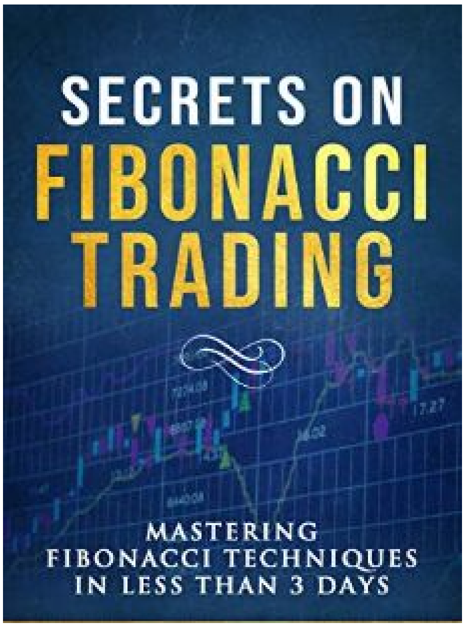	Click here to download my No.1 book on Fibonacci trading.
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