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Price Action Trader

Intraday Swing
Trading for the
Forex, FX Futures
and Emini
Futures Markets

www.YourTradingCoach.com

Volume Three – Trading Strategy

YTC Price Action Trader
by Lance Beggs

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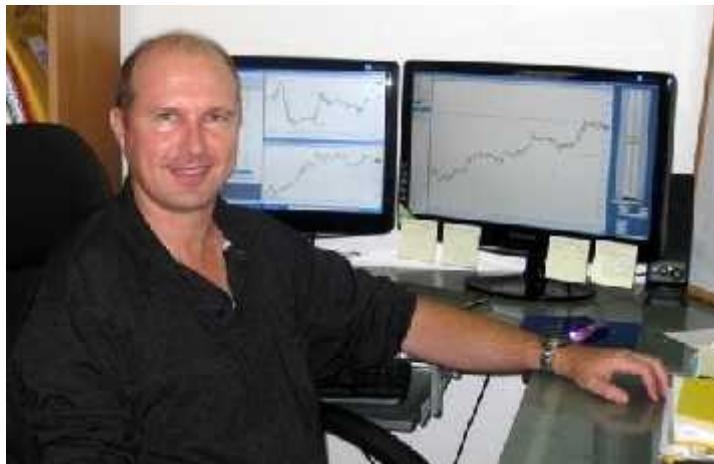
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**“So in war,
the way is to avoid what is strong
and to strike what is weak.”**

...Sun Tzu

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VOLUME THREE

TRADING STRATEGY

Chapter Four – Strategy – YTC Price Action Trader

4.1 - Strategy – YTC Price Action Trader

We've prepared our battlefield. We've conducted our market analysis; defined our structural framework and the trend that moves within that framework. We've established a bias for the likely *future trend* direction and monitored price action bar by bar to update that bias as new information comes to light.

Now it's time to find and manage the trade opportunity within this market action – high probability, low risk trade opportunity.

In this chapter, we'll examine the YTC Price Action Trader strategy.

And we'll work through examples showing how to identify, execute and manage these trade opportunities.

4.2 - Setup Concept

4.2.1 The Expectancy Formula

All traders should be familiar with the expectancy formula:

- $\text{Expectancy} = (\text{Win\%} \times \text{Average Win}) - (\text{Loss\%} \times \text{Average Loss})$

The expectancy formula provides a means of quantifying your edge over a series of trades. A trading strategy that makes money over the sample of trades will have expectancy greater than zero. A losing strategy will have a result less than zero.

Consistent success requires a positive expectancy.

A positive expectancy requires your trading strategy (and your implementation of that strategy) to maximise the following two ratios:

- Win%
 - Win% = number of winning trades divided by total number of trades in the sample.
 - We aim for our percentage of winning trades to be as high as possible.
 - Note that maximising this ratio also minimises the Loss%.

- Win/Loss Size Ratio (WLSR)
 - WLSR = average win divided by average loss
 - We aim for our average win to be larger than our average loss.

Most traders focus all their energy on maximising their Win%. Very little effort is devoted to maximising their WLSR.

As professional traders we must be aware at all times of the need to maximise **both** ratios.

The YTC Price Action Trader manages this through the following means:

- Win%:
 - Setups designed for immediate price movement in our trade direction, as a result of orderflow created by human emotion and decision making. (*Section 4.2.2 – Principles Behind the YTC Price Action Trader Setup Locations*)
 - Early entries within the price swing in order to increase the likelihood of securing a profit before the inevitable reversal. (*Section 4.4.3 – Entry*)
 - Active trade management strategy in order to ensure any profits are retained rather than given back to the market when the market bias changes. (*Section 4.4.4 - Trade Management and Exit*)

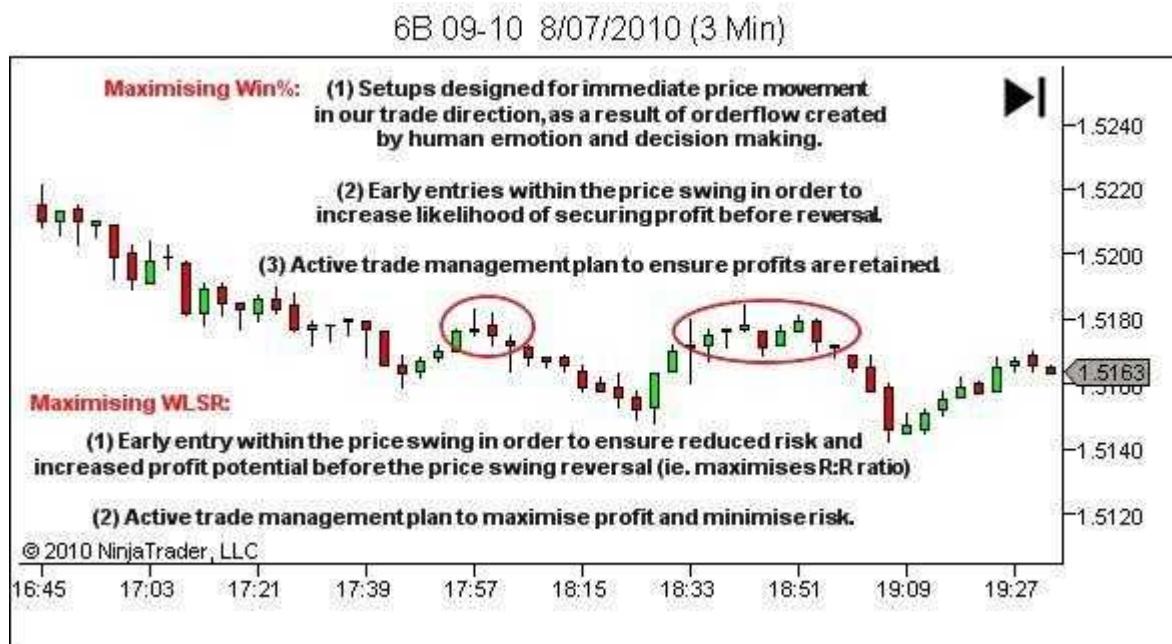


Figure 4.1 - Maximising Expectancy Formula Ratios

- WLSR:

- Recognising that each price swing only has limited movement available, an early entry minimises risk and maximises potential reward (ie. Increased reward:risk ratio). (*Section 4.4.3 – Entry*)
- Active trade management strategy in order to maximise any profits and minimise any risk. (*Section 4.4.4 - Trade Management and Exit*)

4.2.2 Principles behind the YTC Price Action Trader Setup Locations

You should recall the following from Chapter 2:

Markets are not price movement. They are traders making trading decisions.

The way to profit on a consistent basis is through finding those opportunities where there is a higher probability of a sufficient number of traders making trading decisions, which will lead to net order flow in a particular direction, and then acting to trade with this orderflow.

We've seen that individual trader decisions are usually unpredictable, leading to no or minimal edge in the markets. However at times of stress they become much more predictable.

Our trading approach therefore needs to be based on this fundamental understanding of how to profit from the markets:

- We identify areas at which sufficient numbers of traders will be experiencing stress, and will make trading decisions to relieve them of that stress, and then act before or with them in order to profit from the resultant orderflow.

That is the basis behind the YTC Price Action Trader strategy and setups.

Find the areas on a chart where other traders will make trading decisions and you've got yourself an edge.

Enter at or before the change of net order flow and you've got a great opportunity to profit (provided you manage the trade well).

Another way of looking at this is that we are fading those who fight the market bias. Chapter 3 taught us a method of identifying the market bias – the path of least resistance – the likely *future trend* direction.

We now aim to find places on the chart where other traders are fighting the bias. We identify the areas where they realise they're wrong and are forced to exit.

There are two primary concepts behind all my setups – fading weakness and fading trapped traders.

Fading Weakness

The *future trend* moves in the direction of strength and against the direction of weakness.

We therefore aim to always trade in this direction – with strength and against weakness.

We don't do this by identifying new strength, and jumping aboard in that direction – typically that will be too late an entry. Instead we prefer to identify weakness and enter in the opposite direction at or before the point when weakness gives way to more strength.

This is the point at which those who are trading with the weakness will realize they're wrong and be forced out of the market, either by a discretionary exit decision or by their stops being triggered.

Chapter 3 already showed us how to identify weakness. We now use the same analysis concept to identify our areas of trade opportunity. We look for weakness in several key areas – around S/R (higher timeframe S/R, range S/R, key swing H/L) and at pullbacks in a trend.

- Traders entering in the direction of weakness, right into an area of S/R, are taking very low probability trades. The push into this region is most likely to fail.
- Traders entering into a breakout which shows weakness are taking very low probability trades. The breakout is likely to fail.
- Traders fading a breakout, which shows weakness on its first pullback, are taking very low probability trades. The breakout pullback is likely to fail, leading to continuation in the breakout direction.

- Traders trying to catch a trend reversal, entering against a trend on a weak pullback, are taking very low probability trades. The pullback is most likely to fail, leading to continuation of the trend.

You'll notice how our understanding of *future trend* direction has also provided us with the areas of trade opportunity.

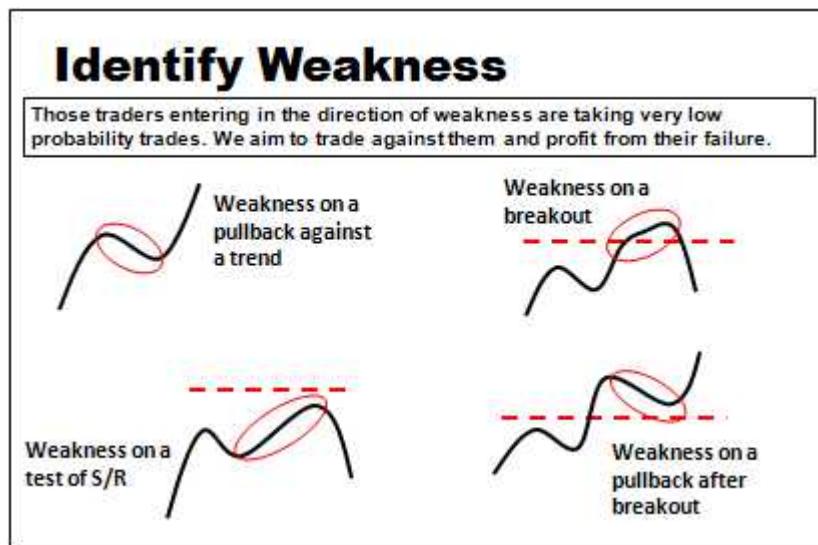


Figure 4.2 - Identify Weakness

The YTC Price Action Trader strategy is a contrarian approach to trading.

You may have heard the term contrarian, when used with regards to investing or trading. It means to go against the crowd, and is often mentioned as the basis for many successful trading approaches. Novices then assume that the way to succeed is to simply trade against any market move. This is not the way to succeed through a contrarian approach. It's just stupidity. The way to succeed through a contrarian method of trading is to be selective. Do not just blindly oppose every market move; just those when the crowd is taking a very low probability position. We selectively identify those times when the move is weak, aiming to enter when they are overwhelmed by the greater force of strength.

Fading Trapped Traders

Another way to look at the concept behind our setups is that we are identifying and trading against trapped traders.

We aim to find places on the chart where other traders are fighting the *future trend* bias. We identify the areas where they are (or will be) trapped in a drawdown, realise they're wrong and are forced to exit. I call these people *trapped traders*.

The concept of the trapped trader is important to this strategy, and should be on your mind throughout your trading session. Watch out for traders getting trapped in a losing position.

You know what this feels like. We've all taken these trades. Remember your entry into the picture-perfect breakout which suddenly reverses back below the breakout point, placing you instantly in a drawdown and a low probability trade. Panic sets in as you watch price threaten your stop; you hold on in hope of a recovery; but more often than not stopping out seems an inevitable outcome.

Trapped traders show on the chart in numerous ways. You'll see them in every YTC Price Action Trader setup.

To introduce the concept though, two examples have been provided in figure 4.3 below.

On the left hand side, we see an uptrending market with a strong bullish bias. A pullback occurs against the bias, showing a strong bearish candle (low close bear candle) followed by a break below a swing low support area. Shorts will enter here hoping to catch a reversal.

However, much to their disgust, the breakout candle turns out to be a narrow mid close bear candle. Momentum has not carried through to the downside. This is followed by a high close range candle. Still no sign of continuation downwards! And then the market traps the shorts with a massive move back upwards (high close bull candle). The large range of this green candle is a result of the first of the stops being executed as trapped shorts are forced out of the market. The new bullish pressure drives price up to new highs.



Figure 4.3 - Trapped Traders

On the right hand side we have a different type of trapped trader situation. The market has a bearish bias as price breaks below an area of consolidation, and then crawls back upwards towards the point of breakout.

The bulls who enter the market long, late in the rally and right into the area of resistance, are taking a very low probability trade. Quite likely these are the traders entering on lagging indicator based triggers. These are the traders who pay our wages.

The rally pauses and then breaks back downwards. The strong low close bear candle is a result of the first of the trapped longs" stops being executed, as they're forced to exit at a loss.

There are other trapped traders in this same example. Consider those traders who bought in the resistance area, prior to the original break downwards. They suffered through an intense drawdown and much psychological pain, desperately holding out for price to come back to at least breakeven. Hope was growing brighter as the rally brought price back to the breakout point. If they were smart, they got out there for a small loss. Most won't though; the small hope they hold for continuation through resistance and into profit is enough to keep them holding just a little longer. They'll then be forced to bail out as price falls again from resistance – angry with themselves and the market for denying them a breakeven exit.

So, you see how this one setup includes two sets of trapped longs – those from prior to the original breakout, and those entering late in the rally.

As you look at any setup, throughout the remainder of this book, then throughout your future trading, always be on the lookout for the trapped trader. Identify them and trade against them; be part of the orderflow that springs their trap.

These trapped traders provide your trading edge. Learn to love them.

An important point before we continue...

Don't get caught up in looking for setups. The most important task in your market analysis is maintaining awareness of the structure of the market and a feeling for the bias and likely path of future orderflow.

Maintain situational awareness and trade setups will show themselves to you. The trapped trader patterns will jump out at you.

Go searching for setups and you'll lose situational awareness with respect the bigger picture structure of the market. You'll end up finding and taking setups and trades that are lower odds when considered within the context of *higher timeframe* market action.

You'll see what appears to be trapped traders, but instead find yourself getting trapped.

Figure 4.4 shows an example of this. Looking at the left hand side chart, it's easy to convince yourself you've found trapped shorts. The market has moved down to the round number area 1.5100 and found support. Bullish pressure is coming into the market. You determine that the late shorts will be trapped on a break above this price action and place a stop entry order above the high of the last green candle, in order to get in early.



Figure 4.4 - A Failed Trapped Trader Pattern due to Poor Market Analysis

Bad Analysis!

The right hand side chart shows the quick loss, as the trapper becomes trapped. Market analysis failed to consider (1) the strength of the bearish bias, and (2) the fact that the 1.5100 level was not a significant support level (there was no evidence of past S/R or swing H/L support).

This trade failed to take into account the fact that we trade with strength and against weakness.

Typically I find myself doing this sort of trade when my focus has been off. Finding myself easily distracted with my attention diverted elsewhere, my mind somehow returns to the screen just in time to see a stall at the 1.5100 level, and a potential *entry long*. Rushing to place the trade, rather than pausing to conduct analysis from first principles, costs me money.

When might you take an entry in this area? Why not wait for the market to provide a clear reversal and then a weaker retest of the level? Then we're trading at a proven area of supply/demand imbalance and against weakness.

Don't rush into trade entries. Identify weakness. Identify trapped traders. Fade the weakness and be a part of the orderflow which springs the trap.

The most important factor in looking for your trade opportunities is... maintaining a good awareness of the structure of the market and the likely future trend direction.

Trading is not about objective analysis.

It's about identifying weakness in the market and then having the confidence to get in at a wholesale level fading that weakness.

It's about actively managing that trade, in order to maximise opportunity if you're proven right and minimise risk if you're proven wrong.

4.3 – YTC Price Action Trader Setups

Opportunity is found at S/R levels (higher timeframe S/R, range S/R, swing H/L) and on pullbacks within a trend. It is identified in these areas by weakness within the price action, trapping other traders into low probability positions.

Let's start by looking in detail at each of the setup types, and then following that up with some discussion about which setups we look for in each particular market environment.

Don't worry about entry and exit yet – just identify the locations for the trade setups.

4.3.1 – Setup Definition

There are five primary YTC Price Action Trader Setups.

Three which occur as price interacts with levels of support or resistance:

- 1) TST – a test of support or resistance which is expected to hold.
- 2) BOF – a breakout failure, as price breaches an area of support or resistance and then reverses.
- 3) BPB – a breakout pullback, as price breaches an area of support or resistance and it holds.

And two which occur within a trend:

- 4) PB – a simple (single-leg) pullback within a trend.
- 5) CPB – a complex (multi-swing or extended duration) pullback within a trend.

TST Setup

The TST setup is a test of support or resistance which is expected to hold.

The support or resistance will ideally be *higher timeframe* S/R or the upper or lower boundaries of a sideways trading range.

It may, in a weak trend environment be a *trading timeframe* swing high or low, offering a counter-trend entry for a short scalp pullback (and possible early entry to reversal if lucky) although this is a much lower probability setup.

When our principles for future trend direction lead us to expect an area of support or resistance to hold, we anticipate a TST setup in that area. We only trade if the setup provides acceptable R:R parameters and a wholesale entry trigger within the S/R area.

Figure 4.5 displays a diagrammatic representation of a TST setup at both resistance and support.

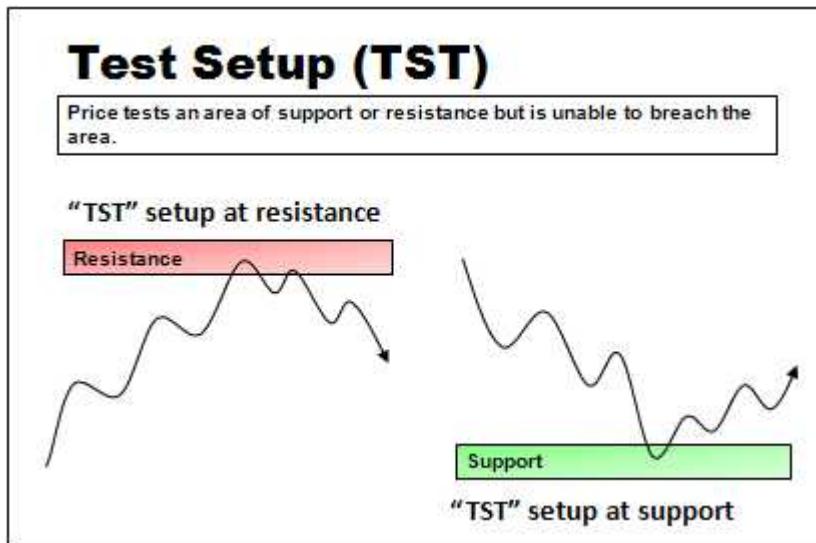


Figure 4.5 - Test Setup (TST)

This setup typically shows weakness into the area of S/R, although may be considered for any grossly overextended move into S/R. The traders entering late on this move into S/R are taking a low probability entry, and will become trapped should price stall and reverse.

This reversal will trigger their stops, adding to the reversal orderflow.

We aim to trade with the reversal orderflow, profiting from the action of the trapped trader stops.

Figure 4.6 (below) shows a chart example of a TST setup at *higher timeframe* (30 min) resistance.



Figure 4.6 - TST at Resistance

As price approaches the area of resistance, we remain alert for the TST setup. Only if we achieve acceptable trade R:R parameters and an appropriate trade trigger (more on those later) will we actually trade. For now, just identify the setup locations.

Note that the setup price action does not touch my resistance line; but it does touch the resistance area. It's important to remember that S/R is an area, not a line. The lines on charts just alert us to the presence of S/R. Look left to find the actual area of influence.

Figure 4.7 (below) shows a chart example of a TST setup at *higher timeframe* (30 min) support. Once again, as price approaches the area of support, we remain alert for a TST setup. We trade if, and only if, we achieve acceptable trade R:R parameters and an appropriate trade trigger.

Note that in this case, the test involved two pushes into the area of support, and two potential trade entry locations.

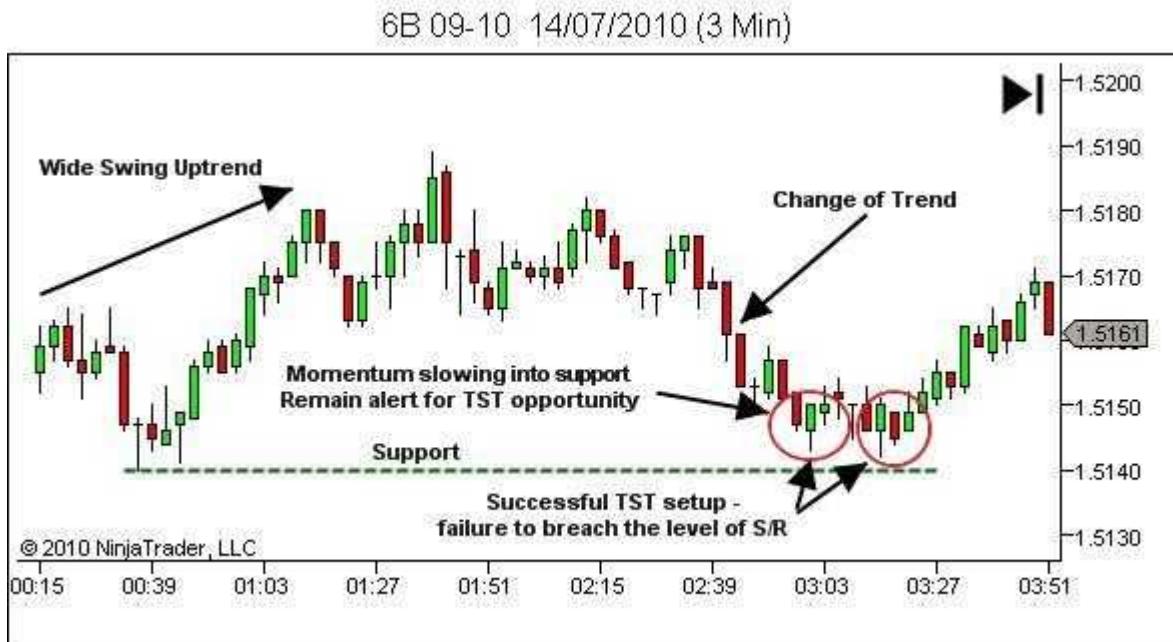


Figure 4.7 - TST at Support

BOF Setup

The BOF setup is a breakout of support or resistance which fails.

The support or resistance will be *higher timeframe* S/R or the upper or lower boundaries of a sideways trading range. In a weak trend environment it may also provide a counter-trend trading opportunity at a swing H/L (however this is a lower probability opportunity)

When our principles for *future trend* direction lead us to expect an area of support or resistance to possibly break, we watch price action closely on any breakout for further signs of weakness. Weakness on the breakout will alert us to a possible BOF opportunity. A trade is only entered if the setup then provides acceptable R:R parameters and a wholesale entry trigger.

Figure 4.8 displays a diagrammatic representation of a BOF setup at both resistance and support.

This setup works due to the break through S/R attracting the breakout traders. However, the breakout is unable to attract sufficient new orderflow to continue the move and therefore shows weakness. The breakout traders are trapped. Failure back to the area prior to S/R forces them to exit their position, adding orderflow against the original breakout direction. We aim to trade the failure, back into the area prior to S/R.

A common question is, "How many price bars will you accept beyond the breakout before you stop looking for a breakout failure?"

There is no fixed number. Every occurrence should be treated on its own merits, and considered from the perspective of how it appears to the breakout traders. Is the price action causing them fear and the potential to abandon their position? If so, it's still a potential BOF setup regardless of how many price bars have printed.

An example is when the market makes two attempts to move price after the breakout. A second failure to do anything is often a good indication the market will do the opposite. If after a breakout I see two attempts to push higher fail, I'll be trying to establish a BOF entry.

However, with all of that being said, I'd say it would be rare to see it hold beyond say 3-5 *trading timeframe* bars. The quicker the better!

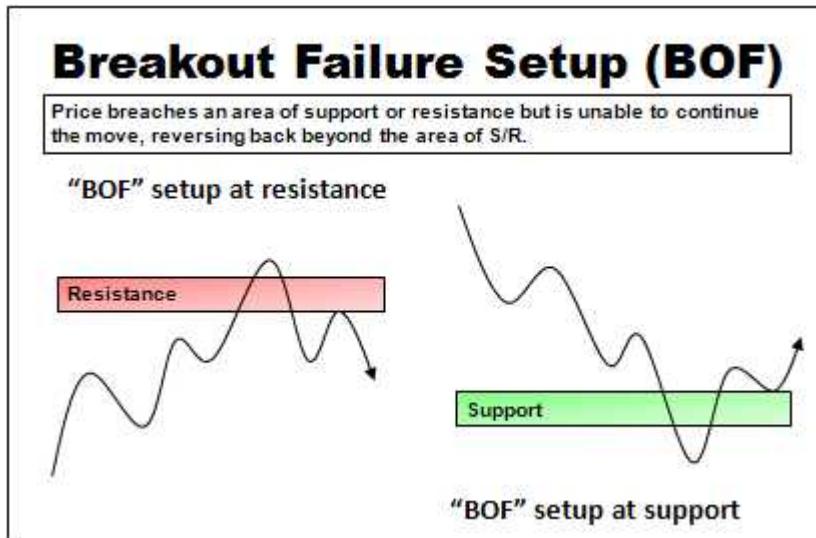


Figure 4.8 - Breakout Failure Setup (BOF)

Figure 4.9 (below) displays a BOF setup at resistance.



Figure 4.9 - BOF at Resistance

In this case, the breakout of a sideways trading range was initiated by a news event - the monthly non-farm payroll (NFP) release, which at the time of writing this book is considered the most potentially volatile of the monthly economic releases.

So, a breakout was considered a high probability.

Watching the breakout, we see price clearly stalled immediately above the resistance area. This is a sign of weakness. Had the breakout contained strength, it would have continued.

Provided we then have acceptable R:R parameters and a suitable entry trigger, we have found ourselves a trade.

Note: Caution is required on highly volatile news spikes. I recommend no entry until price has returned to normal rates of movement. In this case the setup occurred 6 mins after news release and had clearly stopped any post-release volatility.



Figure 4.10 - BOF at Support

Figure 4.10 above shows a breakout failure at support.

While the price action was slowing into the area of support we would initially be looking for (and possibly trading) any TST setups.

However you'll note that each TST setup was unable to take price to new highs. This is showing weakness in the bullish direction. While not displaying great strength in the bearish direction, the *failure to continue* long is an indication that the stronger direction is down.

We remain alert for a breakout and any signs of weakness in the post-breakout price action.

In this case, the breakout was not able to attract sufficient bearish orderflow to continue. The orderflow that it did attract is now trapped short and will be forced to exit if price should break back above the area of support.

BPB Setup

The BPB setup is a breakout of support or resistance which shows price acceptance in the new area, through price holding beyond the breakout point and establishing a weaker pullback.

The support or resistance will be *higher timeframe* S/R or the upper or lower boundaries of a sideways trading range.

When our principles for *future trend* direction lead us to expect an area of support or resistance to possibly break, we watch price action closely on any breakout for further signs of weakness. Weakness on the breakout will alert us to a possible BOF opportunity. Weakness on a pullback will alert us to a possible BPB opportunity. A trade is only entered if the setup then provides acceptable R:R parameters and a wholesale entry trigger.

Figure 4.11 displays a diagrammatic representation of a BPB setup at both resistance and support.

This setup works due to the tendency for many traders to automatically fade a breakout, in expectation of its failure. If that failure is not sufficiently supported by other traders, any pullback will be weak and will itself fail. A failed breakout-failure is a breakout pullback (failed BOF = BPB).

Those trading the weak pullback will become trapped should the breakout continue. Their exit orderflow will assist in pushing the breakout to new highs/lows.

Note: Any BOF setup which you enter prior to crossing back over the S/R level must be managed quite aggressively. Remain alert for signs of weakness, and ready to scratch your position and reverse, should a BPB opportunity present itself.

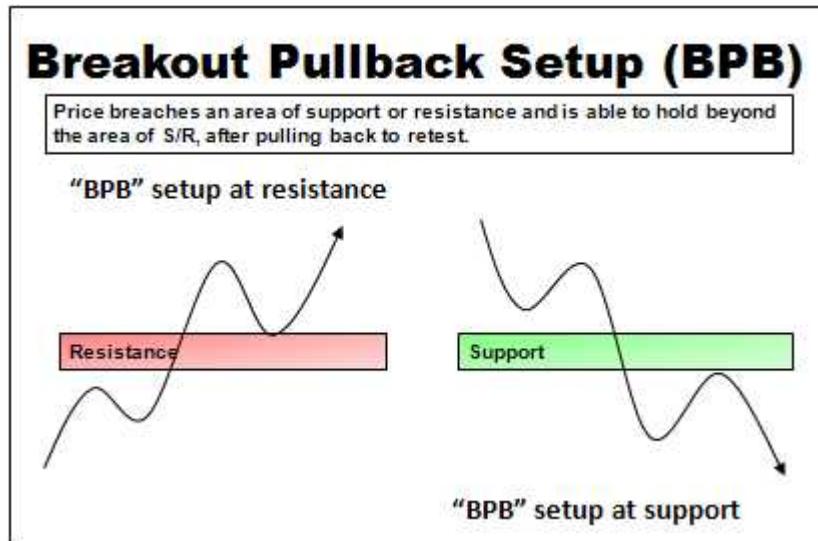


Figure 4.11 - Breakout Pullback Setup (BPB)

Figure 4.12 (below) shows two breakout pullback opportunities.

The first occurred within ten minutes of the initial breakout. The price action displayed weakness on breakout and would in all likelihood have had you searching for BOF opportunity. The pullback though was also weak. As noted previously, a failed BOF is a BPB setup. The scratched BOF would have provided a small loss. The first BPB then offered a small profit.

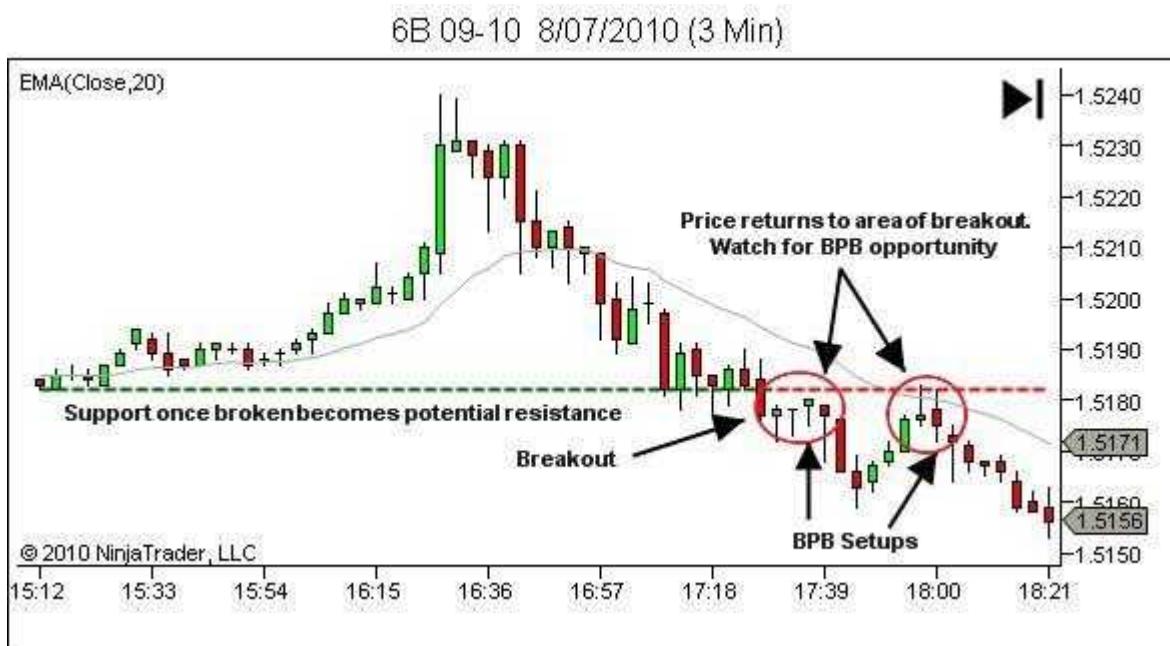


Figure 4.12 - BPB - Support becomes Resistance.

The second BPB opportunity presented approximately half an hour after the breakout, showing a much nicer stall into resistance, with upper tail rejection. This BPB setup provided much greater opportunity (assuming acceptable entry R:R parameters and wholesale trigger).

Figure 4.13 (below) shows a breakout which offers both a BOF scalp and BPB opportunity, for the more nimble trader.



Figure 4.13 - BPB Support becomes Resistance

PB Setup

A PB is a simple (single-leg) pullback within a trend.

When our principles for *future trend* direction lead us to expect continuation of a current up or downtrend, we watch price action closely on any pullback for signs of weakness. Weakness on the pullback will alert us to a possible PB opportunity. A trade is only entered if the setup then provides acceptable R:R parameters and a wholesale entry trigger.

Figure 4.14 (below) displays a diagrammatic representation of a PB setup within a trend.

This setup works due to the tendency for MANY traders to attempt to pick reversal points. While everyone says they understand the saying, „the trend is your friend“, human nature has the majority of us always seeking counter-trend opportunity.

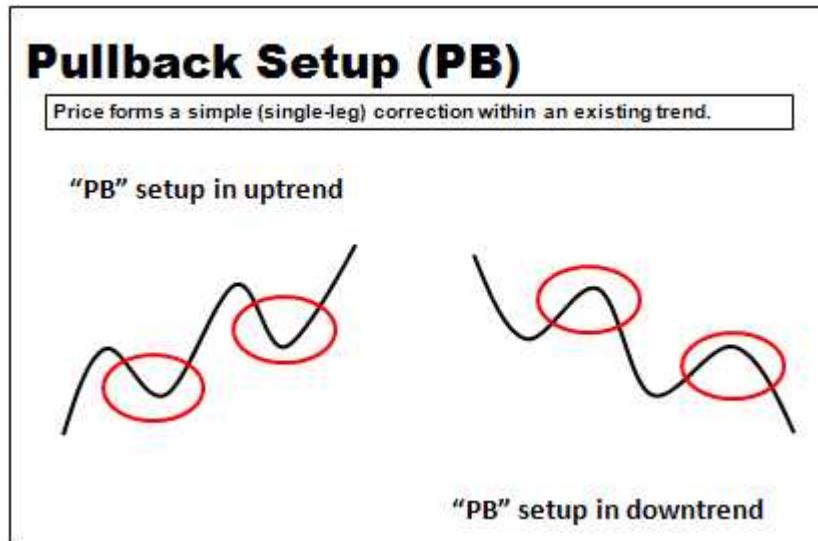


Figure 4.14 - PB Setup

The reality is that the market moves in the direction of strength and against the direction of weakness. We watch these weaker pullbacks for signs of failure, which will trap the *counter-trend* traders in a losing position and force their exit. Their exit orderflow helps take our PB trade to profits.

While a pullback may fail at any point, we watch price closely at areas of prior swing H/L. These areas will be sources of potential new orderflow and will provide clues as to the strength or weakness of the pullback and the timing of any failure. This is shown in figure 4.15 below.

This is not to say that these are the only places we expect pullback failure and trade entry. Simply that we watch these areas closely, observing the interaction of price with these swing H/L areas in the search for clues as to the way forward.

Ongoing bar by bar analysis of price action will tell you when the pullback is failing, and monitoring of the *lower timeframe* chart will provide your trade entry opportunity, should it arise before these swing H/L areas.

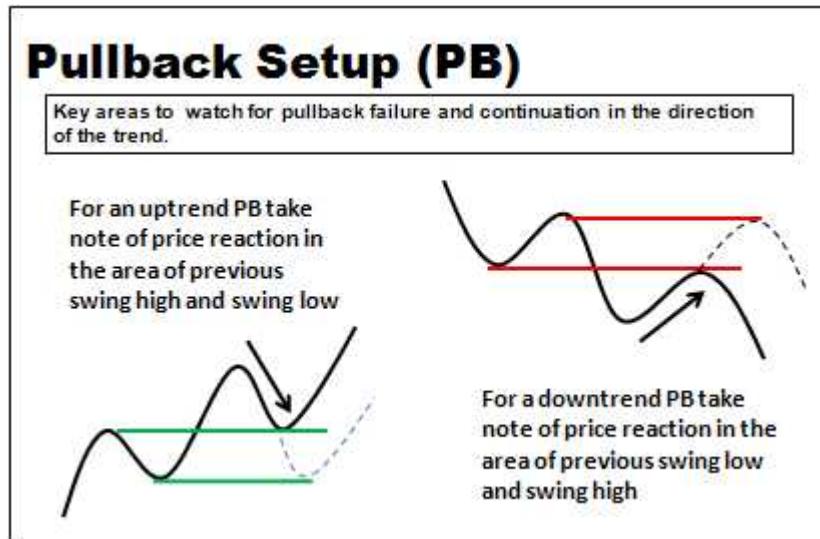


Figure 4.15 - Key Areas For Pullback Failure Clues

Figure 4.16 below shows a chart example of a PB setup within a downtrend.



Figure 4.16 - PB Within a Downtrend

Note that both pullbacks A and B are simple, single-leg pullbacks which lead to continuation of the downtrend.

Pullback A reaches the previous area of swing low support, now resistance, before price stalls and then resumes the downtrend. The stall is clear evidence of weakness within the pullback.

Likewise with B that also stalled prior to continuation of the trend. This time though price pulled back to the previous swing high area (remember that it's an area not a line; in this case pulling back to the lower part of the swing high area).



Figure 4.17 - PB Within an Uptrend

In figure 4.17 we see single-leg pullback C, which stalls abeam the area of congestion D.

And then pullback E which stalls abeam the previous swing high G. Note also the breakout above swing high G at F; evidence of a strong supply/demand imbalance. Any area of rapid price movement is worth watching for future support or resistance, should price return to that area.

CPB Setup

A CPB is a complex pullback within a trend environment – either consisting of multiple legs and/or an extended duration.

When we identify a weakening trend, our principles for *future trend* direction lead us to expect a complex retracement rather than a simple retracement. We remain alert during this complex retracement for a CPB opportunity.

In addition, a failed PB which does not reverse the trend can set up a possible CPB opportunity.

As always, a trade is only entered if the setup then provides acceptable R:R parameters and a wholesale entry trigger.

Figure 4.18 displays a diagrammatic representation of a CPB setup within a trend.

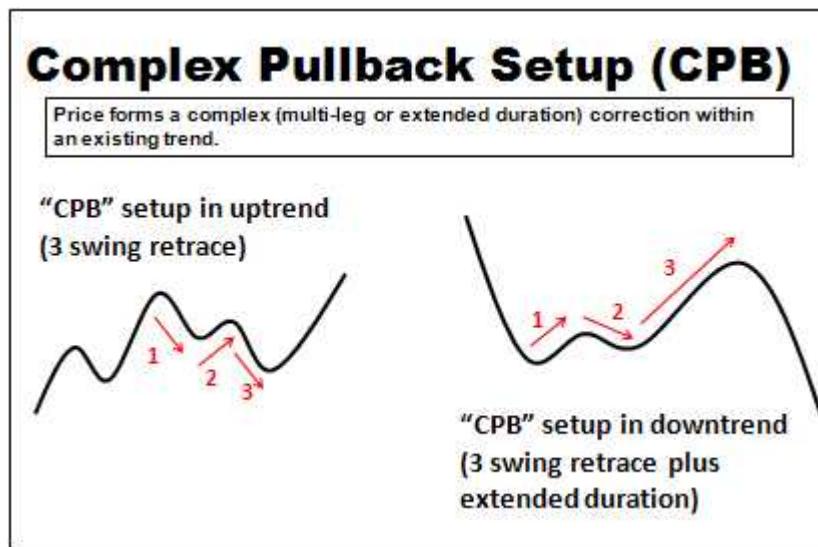


Figure 4.18 - CPB Setup

A multiple swing pullback can provide a quite powerful setup opportunity. In fact, a CPB is often a more powerful setup than a simple PB.

Consider the uptrend on the left hand side of figure 4.18. As price swing 3 breaks below the low between swings 1 & 2, it will attract shorts attempting to enter a reversal. The subsequent stall

and reversal (continuation in the direction of the trend) traps these traders. Their exit orderflow helps propel our trade to profits.

How do we judge when to wait for a CPB rather than take a PB entry? A large part of it is you *feel* for the market flow. You'll gain some sense of this with experience.

As mentioned, weakness in the trend will usually lead us to expect for a CPB. But we often also expect them when a price swing has overextended in the direction of the trend. Quite likely it will need to correct this via a multiple swing pullback.

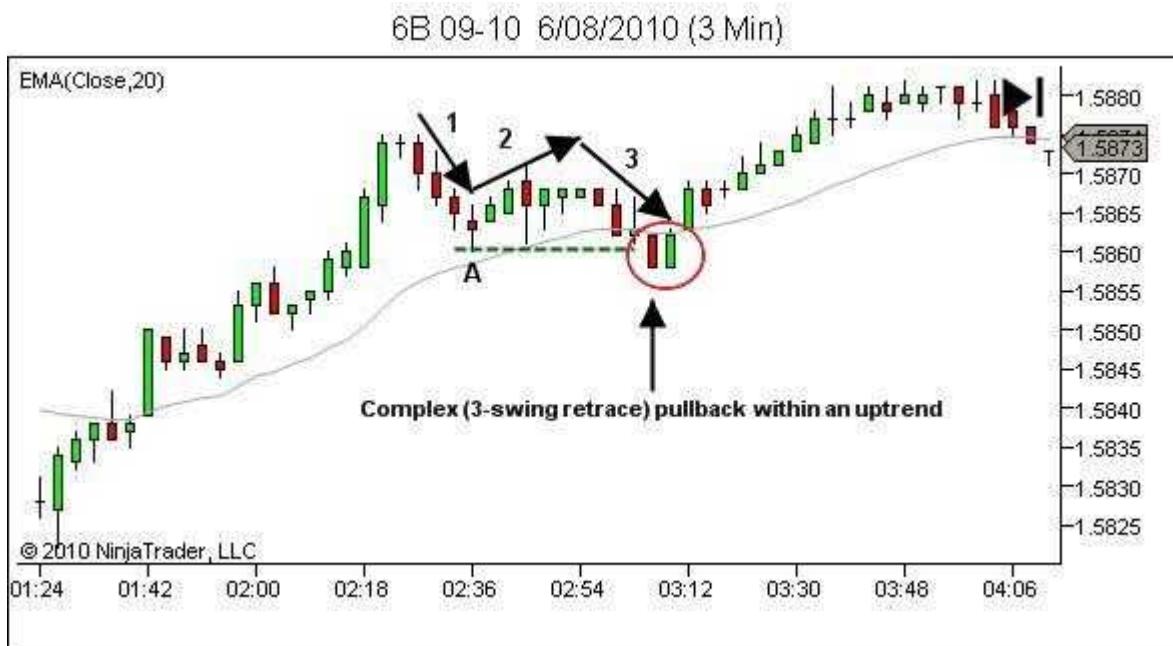


Figure 4.19 - CPB Setup – 3-Swing Retrace

Figure 4.19 demonstrates this concept through a price action chart.

Note the three swings of the pullback, in which the third swing breaks below point A. This will attract some shorts who are hoping to get an early entry into a reversal. To their disgust, they're quickly trapped as price breaks back above level A and triggers their exit order.

This 3-swing retracement trapped trader orderflow is often sufficient to kick start a stalled trend.

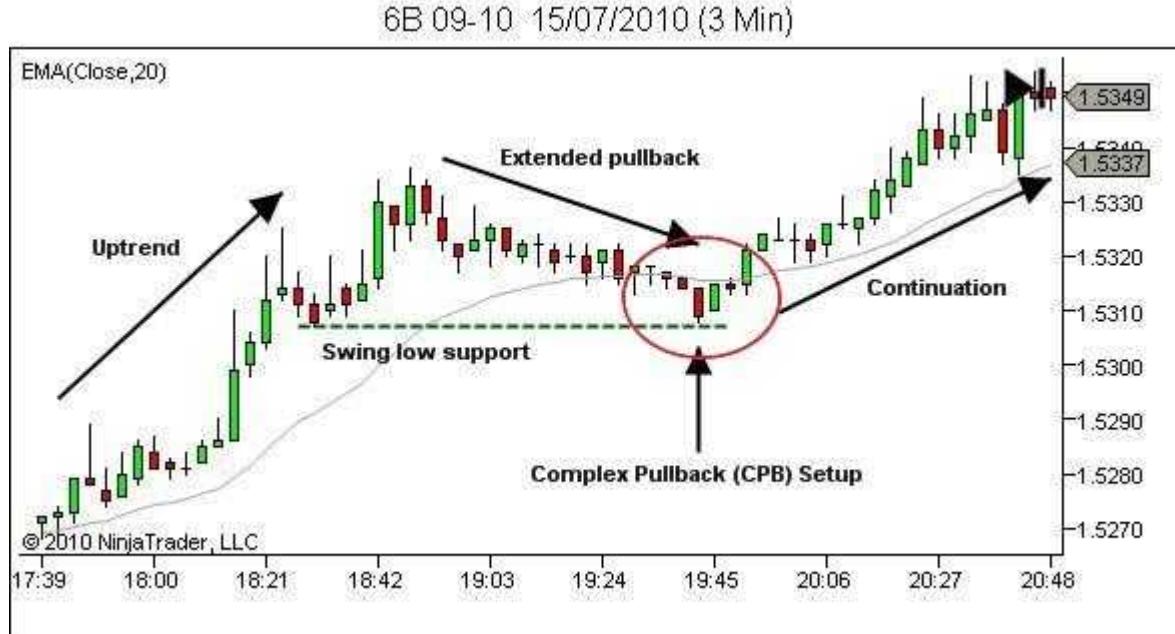


Figure 4.20 - CPB Setup – Extended Pullback

In figure 4.20 above we see an uptrend that pulled slowly back to previous swing low support.

Unlike the 3-swing retrace version of CPB's, which are easy to trade, these extended duration pullbacks are sometimes difficult to trigger into. There is always a temptation to hold for more grinding action and further pullback. Confidence should be provided when a *lower timeframe* (1 min) trigger occurs at previous swing H/L areas.

4.3.2 Setups Appropriate for each Particular Market Environment

Let's discuss the setups that are typically traded for each particular market environment.

By *market environment*, I don't mean the past trend, but rather our expectations for *future trend*.

Within the S/R framework:

First Principle – We expect an up or down trend to continue in its current state until the next S/R barrier, unless displaying evidence of weakness within the trend.

- Opportunities will be via a PB or CPB setups within the trend, as demonstrated in the previous section.



Figure 4.21 - PB Opportunity Within a Trend

- Trends that overextend well above an uptrend MA line, or well below a downtrend MA, will typically require a CPB correction before continuing, except in a very fast trend.



Figure 4.22 - Over-Extension Requiring a CPB

Second Principle - When an up or down trend shows evidence of weakness, we expect a higher likelihood of a complex correction rather than a reversal, until such time as the market shows both price acceptance and strength in the new trend direction.

- Primary opportunity, as mentioned, is via a CPB setup. PB setups should only be taken when price moves nicely into an area of lower swing low support (uptrend) or upper swing high resistance (downtrend), preferably breaking that swing low or high before failing. Otherwise, stick to the higher probability multi-leg CPBs. By trading only these deeper PB or multi-leg CPBs, we have the advantage of greater trapped trader orderflow.

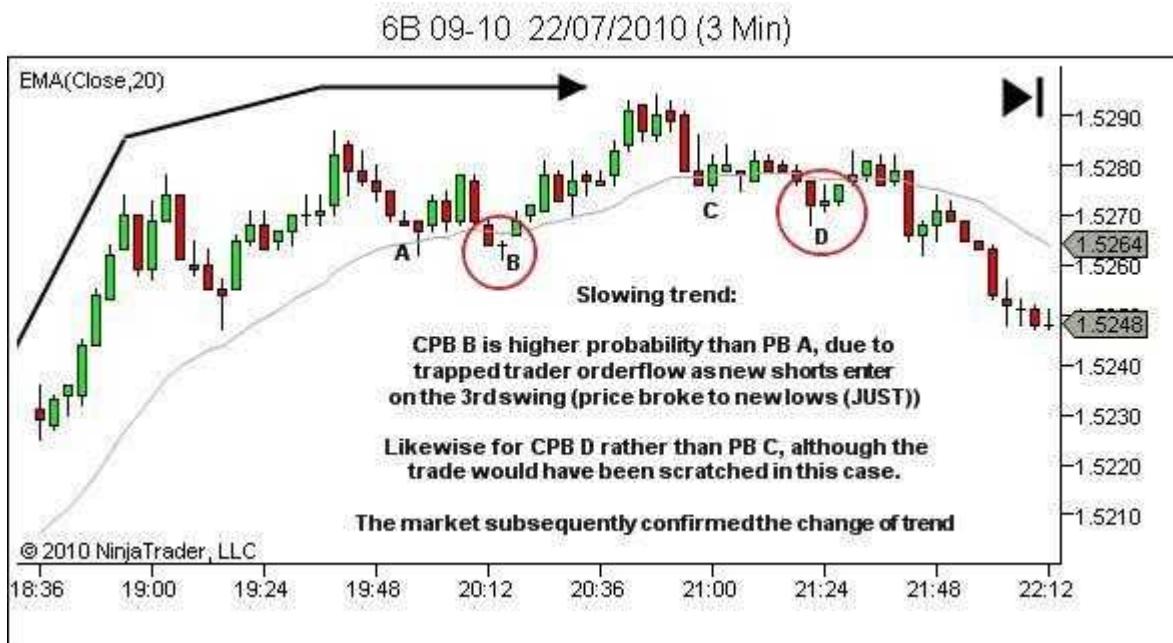


Figure 4.23 - CPB Opportunities Within a Slowing Trend Environment

- Lower probability counter-trend opportunities may be available via either a TST or BOF at previous swing high resistance for an uptrend, or swing low support for a downtrend. Typically these will only be considered in a wide-swinging slow trend, or a trend which is clearly slowing down, both showing relatively small projection. Manage these trades aggressively if you choose to take them. As shown in the example below though, they can offer an early entry into a reversal.



Figure 4.24 - Counter-Trend BOF Setups Within a Slowing Trend Environment



Figure 4.25 - Counter-Trend TST Setup Within a Slowing Trend Environment

Third Principle – A sideways trend within the framework is expected to continue in its current state, unless displaying evidence of strength towards the range boundary.

- Higher probability trades at the boundaries will always be BOF setups, due to the presence of breakout trapped trader orderflow. However in the absence of any real strength showing towards the boundary S/R we need to be alert for simple TST setups.



Figure 4.26 - TST Setups within a Sideways Trend

- Where the intra-range price action shows a bias towards trending in one direction, you may consider PB/CPB entries within that trend. CAUTION: Lower probability trades.



Figure 4.27 - Trend Opportunity within Sideways Trend Trading Range

Fourth Principle - When a sideways trend shows evidence of strength towards the range boundary, we expect a break of the boundary. We observe the behaviour of price post-breakout for clues as to future direction:

- Weakness following the breakout – the expectation is for a breakout failure and reversal back within the trading range.
- Weakness on the pullback – the expectation is for a breakout pullback and continuation.
- The principle provides clear direction here – watch the post-breakout price action for weakness, for either a BOF and/or BPB opportunity. As discussed earlier, weakness may be evident on both legs. Any BOF trade should be managed cautiously until showing strength. Subsequent weakness on the pullback will indicate a likely BOF failure. Remain alert for any BPB trigger, allowing a BOF exit and reversal for BPB entry.



Figure 4.28 - Sideways Trading Range Providing BOF Setup Opportunity



Figure 4.29 - Sideways Trading Range Providing BPB Setup Opportunity

At the edges of the S/R framework:

Fifth Principle – We expect a test of our framework S/R to hold, unless strength is displayed on approach to the S/R boundary.

- The principle provides clear direction as to the expected setup. As price approaches the *higher timeframe* S/R level we remain alert for a TST setup.



Figure 4.30 - TST Setup at Higher Timeframe (30 min) Resistance

Sixth Principle - If strength is shown on an approach to an S/R barrier, we expect a breakout and watch the behaviour of price post-breakout for clues as to future direction:

- Weakness following the breakout – the expectation is for a breakout failure and reversal back through the area of S/R.
- Weakness on the pullback – the expectation is for a breakout pullback and continuation.
- The principle provides clear direction here – watch the post-breakout price action for weakness, for either a BOF and/or BPB opportunity. As discussed earlier, weakness may be evident on both legs. Any BOF trade should be managed cautiously until showing

strength. Subsequent weakness on the pullback will indicate a likely BOF failure. Remain alert for any BPB trigger, allowing a BOF exit and reversal for BPB entry.

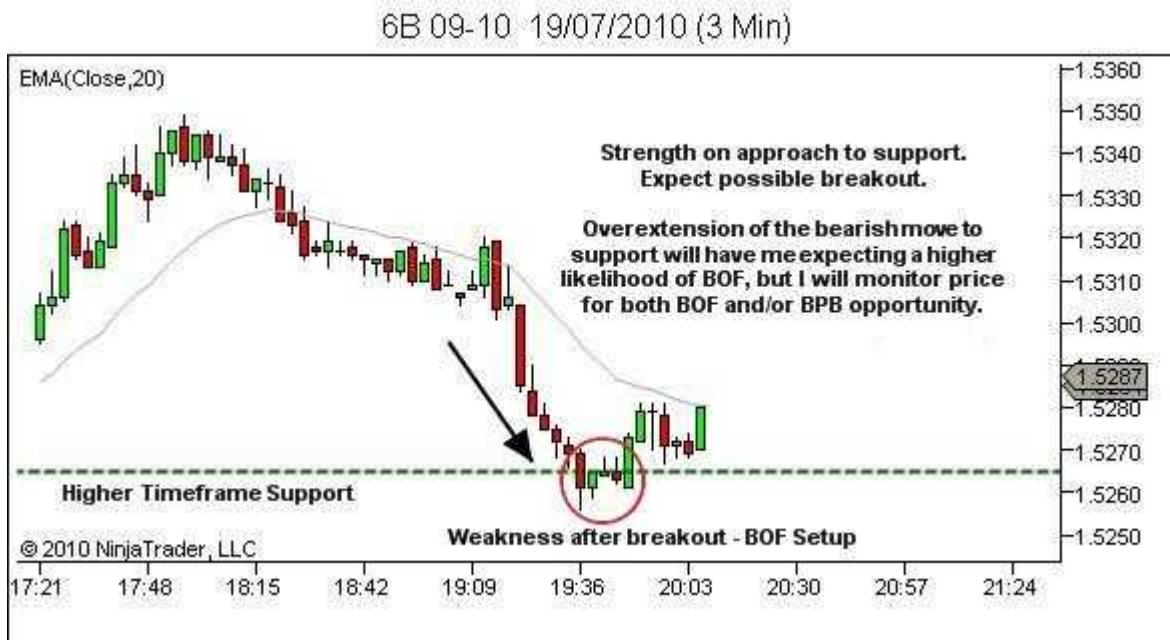


Figure 4.31 - BOF at Higher Timeframe (30 min) Support



Figure 4.32 - BPB at Higher Timeframe (30 min) Resistance

Summary

Steady trend environment:

- Higher Probability
 - PB and CPB

Weakening trend environment

- Higher Probability
 - CPB
 - PB if they break a previous swing low (uptrend) or swing high (downtrend)
- Lower Probability
 - Standard PB (single leg; not breaking any prior swing low (uptrend) or swing high (downtrend))
 - Counter-trend TST or BOF of swing high (uptrend) or swing low (downtrend)

Within a Sideways Trading Range with a clear intra-range trend

- Lower Probability
 - PB and CPB

Approaching higher timeframe S/R or range S/R, with no sign of potential breakout

- Higher Probability
 - TST

Approaching higher timeframe S/R or range S/R, with strength showing signs of potential breakout

- Higher Probability
 - BOF or BPB

A Note on Counter-Trend Trading in a Strong Trend Environment

Counter-trend trades are ALWAYS going to be a lower probability trade when a trend is moving strongly.

Even more so for a climactic move!

Human nature is such that having hesitated and missed a good with-trend entry; our tendency is to seek revenge over the market through looking to catch the early reversal. The market will offer many counter-trend setups which will typically all look very tempting. But more often than not this will be a trap.

Trust the trend to continue, until it shows clear evidence of weakening.

Approach S/R barriers with the expectation they'll break. Watch for an opportunity on the first pullback after breakout.

Expect pullbacks to be shallow, possibly reversing even before they reach previous swing high/low areas.

If you find what appears to be a tempting counter-trend setup, pass on it with the knowledge that many others will also see it and take this low probability entry. Watch for subsequent the counter-trend setup failure and use that as your entry with-trend. Profit from the stop-out orderflow of those trapped counter-trend in a strong trend environment.

Avoid the temptation to trade counter-trend until the market has shown a clear weakening of the trend. Not just a pause or short term weakening – look for a strong and deep pullback (increased depth compared with previous pullbacks, on increased strength) followed by a weaker retest of the lows/highs. Even then the preference is for a BOF counter-trend entry rather than TST due to the greater short-term trapped trader orderflow. Treat all CT opportunities with caution.

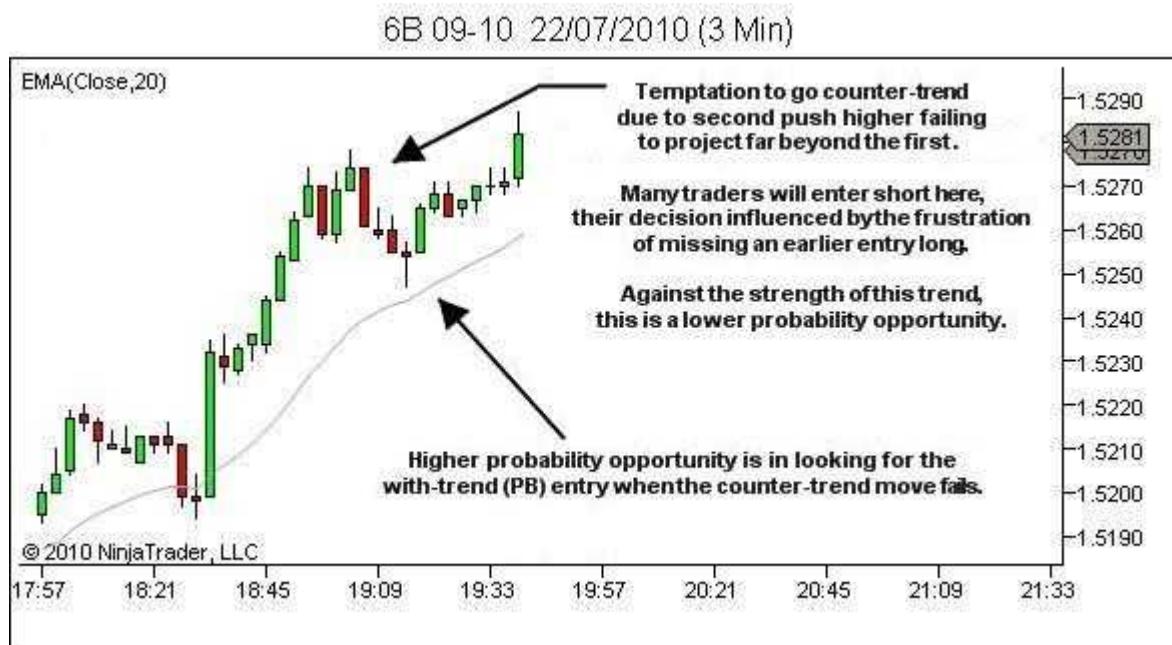


Figure 4.33 - Counter-Trend Failure Against Strong Trend

What Happens After S/R Holds?

You should recall in the analysis chapter, we discussed the period after an area of S/R holds (test or breakout failure). We observe signs of strength and weakness in order to determine the likely future trend direction – is the price going to form a reversal, or return for a subsequent retest.

The following diagrams show potential setups available following the original TST or BOF setup.

- In the absence of weakness in the trend (when having tested S/R) expect a continuation of the trend (First Principle) which will take us back for another test of S/R (Fifth or Sixth Principle). So, we look for both PB and a TST or BOF/BPB setups.

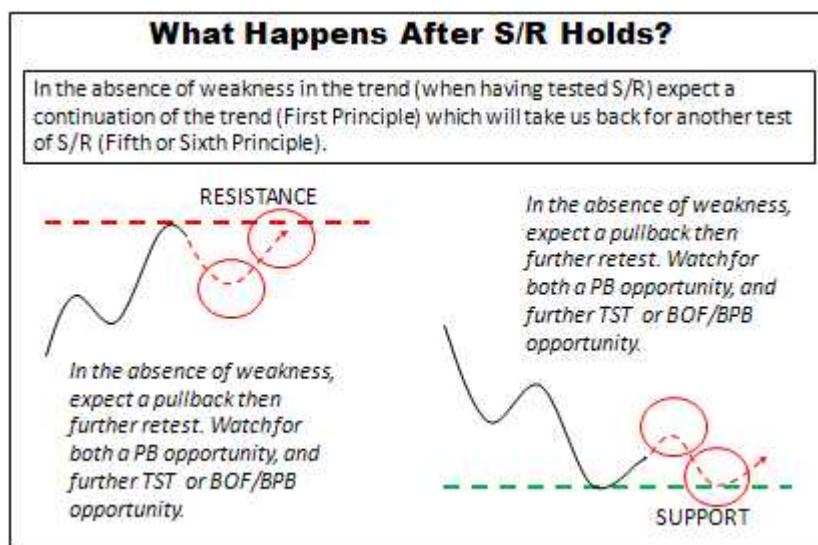


Figure 4.34 – What Happens After S/R Holds – In the Absence of Weakness

- If weakness is present in the trend (when having tested S/R), but there are no signs of strength in the reversal direction, expect a complex pullback (Second Principle) prior to taking us back for another test of S/R (Fifth or Sixth Principle). So, we look for both CPB and TST or BOF/BPB setups.

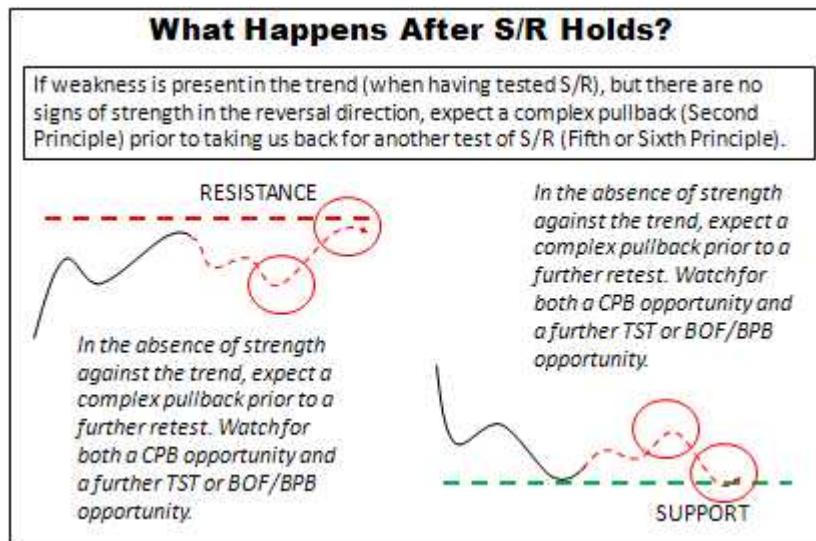


Figure 4.35 – What Happens After S/R Holds –
In the Absence of Strength Against the Trend

- If strength shows against the trend, expect a reversal. In this case, any retest of the S/R can be treated like a pullback in the direction of the new trend (First Principle). Watch for a PB setup in the new trend direction.

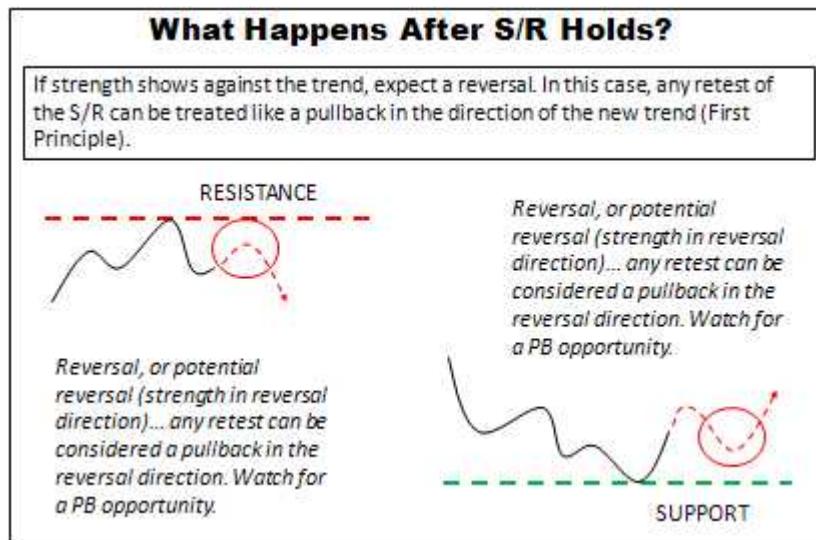


Figure 4.36 – What Happens After S/R Holds –
In the Presence of Strength Against the Trend

4.3.3 - Revisiting the Initial Market Analysis Process and Checklist

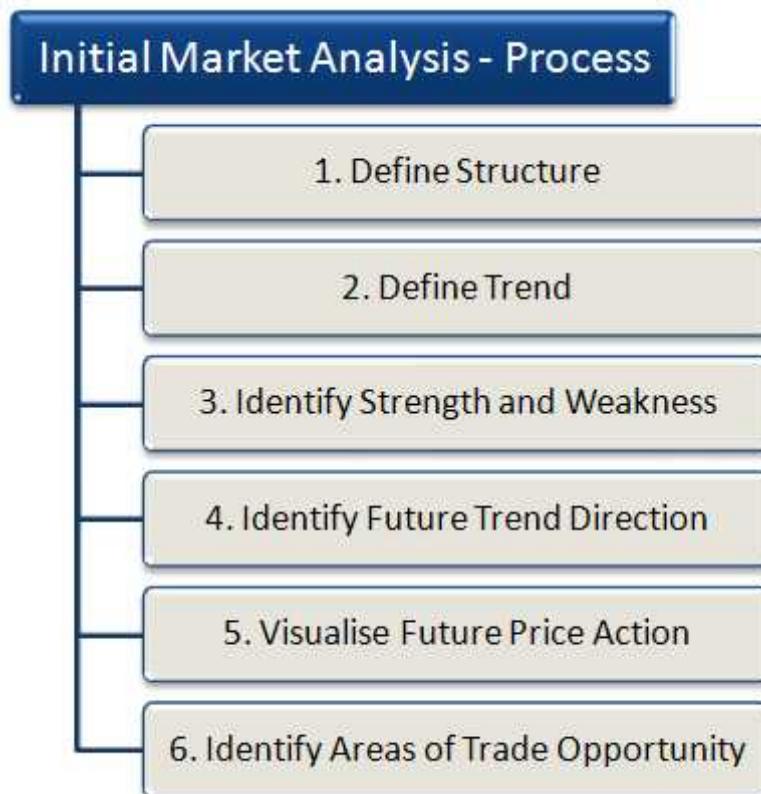


Figure 4.37 - Initial Market Analysis Process

You'll recall this process diagram from the Analysis chapter. At the time we ignored step 6 – Identify Areas of Trade Opportunity.

We can now include the actions for step 6 within our checklist.

Step 6 - Identify Areas of Trade Opportunity

Based upon your expectations for *future trend* direction and how it should interact with areas of S/R and swing highs / lows, identify the next potential setup areas. Areas of trade opportunity are found where weakness plays out against S/R and swing highs / lows (TST, BOF, BPB), or within a trend (PB, CPB).

Actions:

- Identify potential future setup areas
 - Steady trend environment:
 - Higher Probability
 - PB and CPB
 - Weakening trend environment
 - Higher Probability
 - CPB
 - PB if they break a previous swing low (uptrend) or swing high (downtrend)
 - Lower Probability
 - Standard PB (single leg; not breaking any prior swing low (uptrend) or swing high (downtrend))
 - Counter-trend TST or BOF of swing high (uptrend) or swing low (downtrend)
 - Within a Sideways Trading Range with a clear intra-range trend
 - Lower Probability
 - PB and CPB
 - Approaching higher timeframe S/R or range S/R, with no sign of potential breakout
 - Higher Probability
 - TST
 - Approaching higher timeframe S/R or range S/R, with strength showing signs of potential breakout
 - Higher Probability
 - BOF or BPB
- Implement Trading Process if/when price enters the setup area.

4.3.4 – More Action – Trading In-between Setup Areas

The number of opportunities provided per hour will vary depending on your chosen market and timeframes. Using the timeframes shown in the examples within this book, I would expect around 1-2 setups per hour on average. Sometimes it will be more. Other times it will be less.

If you’re using higher timeframes and find yourself bored and seeking more action, do not try to find additional opportunity in-between setup areas. If you want more action then I encourage you to stick to the same strategy but just reduce timeframes.

If you get down to timeframes less than those in this book, then I recommend you read the supplementary ebook – YTC Scalper – for additional considerations.

4.3.5 – When Price Enters Setup Areas

Price approaching a setup area is not a guarantee that we’re going to trade. It is however a time to place yourself on high alert for trade opportunity. Remove any distraction and focus. Ensure you follow the price action bar by bar maintaining your feel for sentiment.

And remain alert for areas suitable for stop positioning, targets and entry point, as discussed in the following sections.

Before reading the following sections on Exits and Targets, please review the following information, which will provide a quite detailed overview:

- The Importance of Exit Strategy ebook
 - You should have downloaded a copy from the YTC Price Action Trader download page. It provides a consolidated copy of the three articles from my website on The Importance of Exit Strategy.
 - This is essential background information, required before proceeding with this book.
- Alternatively watch the video version here (four videos total):
 - <http://www.yourtradingcoach.com/Videos-Risk-Management/The-Importance-of-Exit-Strategy-Vid-1.html>

4.4 - Trading the Setups

4.4.1 - Stop Placement

Initial Stop Loss Placement

As soon as price is entering a setup area, I'm searching for a stop location. This is something that should be done before seeking an entry trigger.

The initial positioning of the stop is always to be at a price level which invalidates your trade premise. Identify a point in the market to which price will NOT go if your expectation for future price action is correct.

Should you subsequently enter a trade and price triggers your stop, it indicates that either:

- 1) Your trade premise was wrong (or was right but the market sentiment has since changed and is now wrong); or
- 2) Your trade timing was wrong.

In either case, you WANT to be out of the market. Being stopped out is a risk management exit, designed to minimise loss and keep you in the trading game. It should be welcomed.

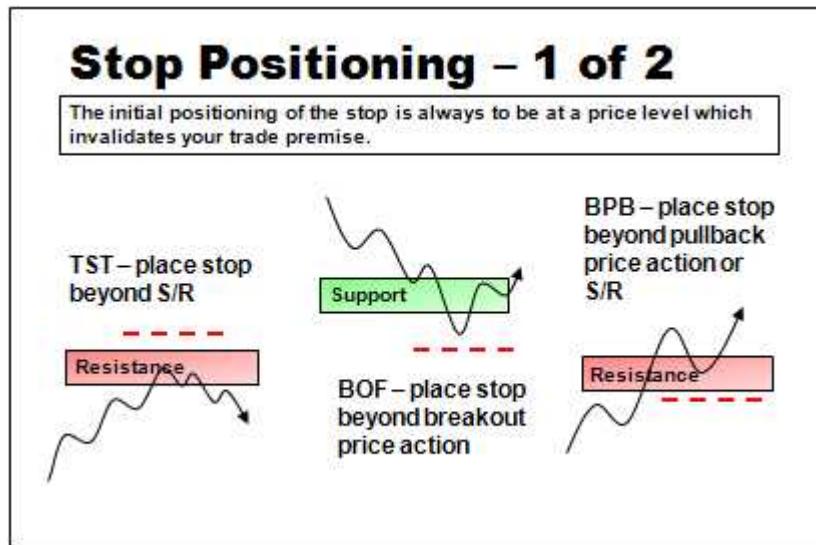


Figure 4.38 - Stop Positioning – TST, BOF and BPB

Figures 4.38 and 4.39 show the stop position for each of our setups.

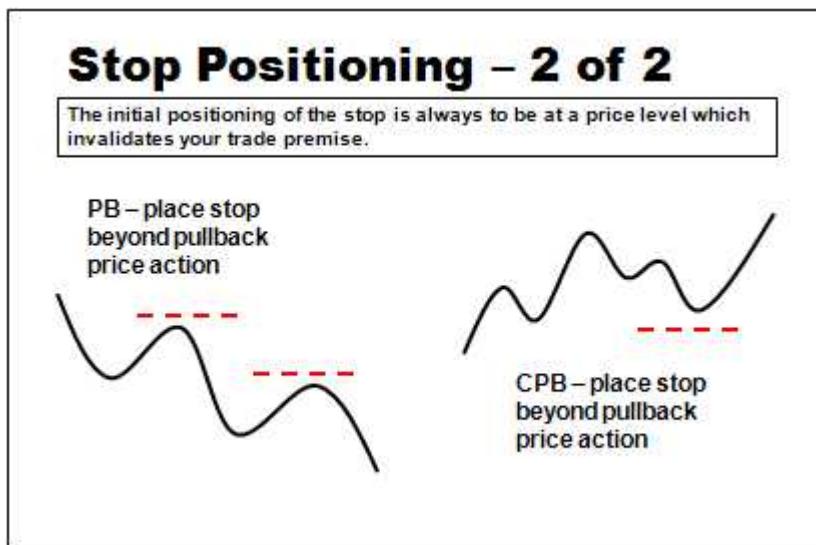


Figure 4.39 - Stop Positioning – PB and CPB

Stop positions will be clearly visible on the *trading timeframe* but I prefer to use the *lower timeframe* chart to identify their position. It allows us to see the inner workings of the *trading timeframe* candles, identifying strength and weakness on a lower time scale.

It's easy for a TST setup. If you're expecting a test of some type of S/R level, and price action does not show sufficient strength to suggest a breakout, then the stop position should be just beyond the S/R level extremes.

Figure 4.40 below shows price in a TST setup area at resistance.

If correct, price should not exceed the resistance area, so (if a trade was entered) we would currently plan to place the stop just above the resistance area.

Having identified a (tentative) stop location, we move on to identifying potential targets and an entry trigger. If price should fail to offer an entry trigger and continue moving higher, we'll adjust our expectations (and possibly adjust our premise and prepare for BOF or BPB setups).

If price should offer an entry trigger short, we then place our stop order at the position indicated. If we're subsequently stopped out at this level, it will indicate that our trade idea and in fact our whole premise were wrong. It's good to be out, having minimised loss. We then move on to look for the next opportunity.

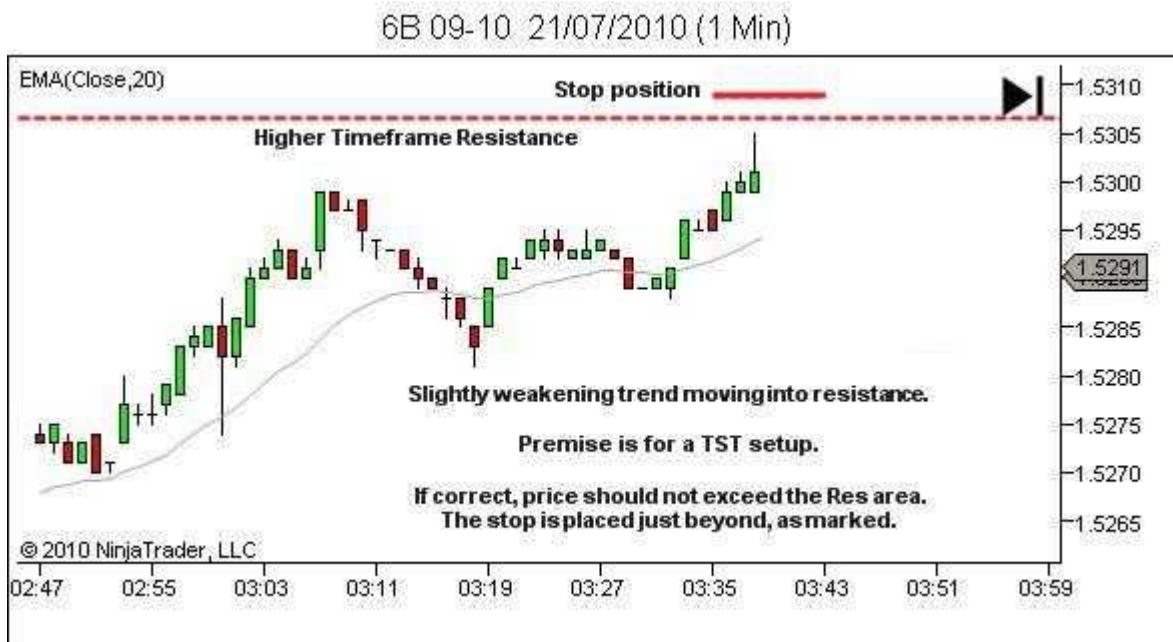


Figure 4.40 - Stop Positioning – TST Setup at Resistance

Another option in this case, had the trigger occurred immediately after the last candle shown, would be to place the initial stop lower, just above the upper tail. While this offers less risk it comes at the cost of potential stop-out, which may not have stopped out the original higher (above resistance) stop.

Please note in these examples... any stop order should be attached to an entry order. They're not placed in the market yet. We're just simply identifying its location, should a trade entry trigger.

All other setups (BOF, BPB, PB, CPB) are not so easy. There is not necessarily going to be a nice S/R line beyond which we can place our stop. Stop positioning will be dependent on price action.

The idea is the same though – we place the stop at a location where price should NOT go, if the trade premise is proven valid.

If you're waiting for a bullish trade setup, watch for the bears to show you all they've got; then define your stop position as the place the bears could not reach.

If you're waiting for a bearish trade setup, watch for the bulls to show you all they've got; then define your stop position as the place the bulls could not reach.

This may involve initial (tentative) identification of a stop level, adjusting it as more price action unfolds. The actual entry trigger may then also alter the stop location.

Other times you may just not have any indication of a stop position until the trigger candle.

Figure 4.41 below reproduces one of our earlier BPB setup examples, showing the 3 min setup on the LHS and the 1 min price action on the RHS.

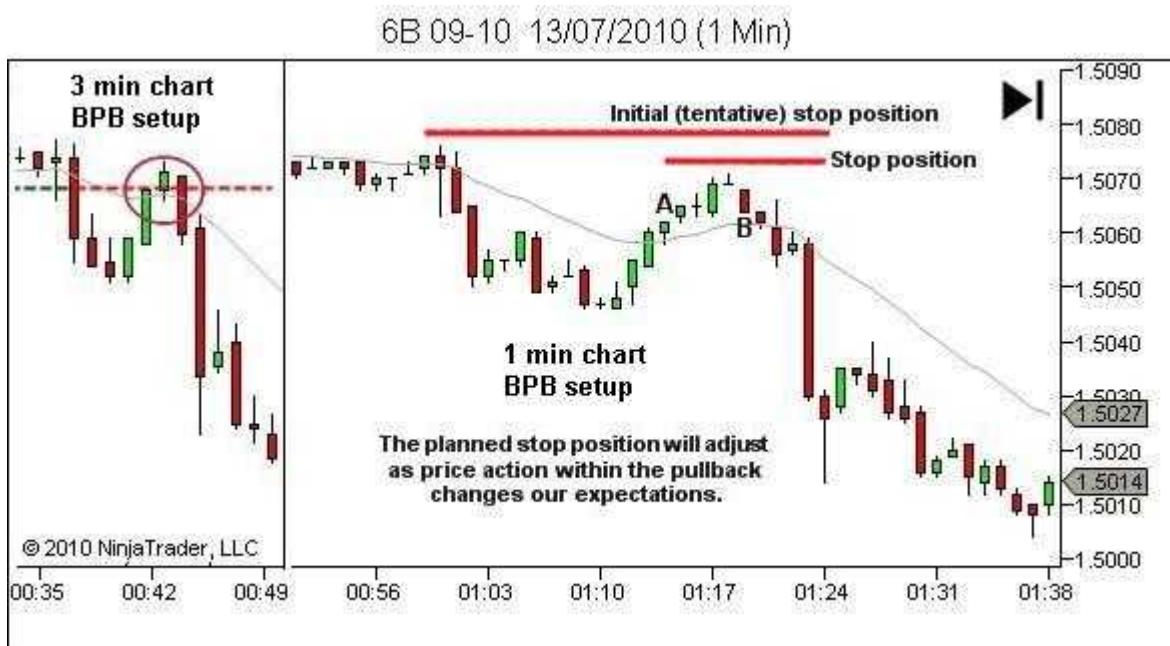


Figure 4.41 - BPB – Stop Positioning

Our expectation is for price to pull back towards the resistance area.

My attention diverts to the 1 min chart in order to see finer detail. Noting price slowing at A, I would tentatively identify a (potential) stop position above the pre-breakdown congestion as shown on the RHS above.

If price should get there at all, then the whole premise is wrong.

This doesn't necessarily become my stop location though. I continue to monitor as more 1 min bars appear and adjust the stop if price action shows a closer area beyond which price should NOT go.

At B we have a clear sign of bearish sentiment. The tentative stop is moved above price action at the swing high (shown as „Stop position“).

This is the stop position that would be placed in the market IF price subsequently triggers an entry, which it did on the following candles (we'll get to entries shortly).

Figure 4.42 shows one of our earlier BOF examples on the LHS. 1 minute detail is shown on the RHS.



Figure 4.42 - BOF Stop Positioning

Looking at the first BOF...

A stop position would tentatively be planned for below the lower tail of candle A, should an entry trigger.

No entry triggered. Candle B then provided a lower low, again with lower tail rejection. Should a BOF entry trigger, the stop would now be planned for below candle B.

Still no entry triggered. Candle C provides a further low. The stop is now planned for below this low at stop position SP1, should the entry trigger,

As the trade entry is subsequently triggered, the order will be placed into the market at SP1.

Just quickly, looking at the further BOF opportunities...

Candle D shows a second opportunity. Note that had the stop been placed below the most recent swing low at SP2, you would subsequently be stopped out, while a wider stop at SP3 (equal to SP1) would not stop out.

SP3 is obviously the preference, below all recent swing low support areas. It will be the preferred stop location, provided it still offers suitable R:R. If not, SP2 is acceptable.

The third BOF opportunity was at candle E, with the stop placed below all price action at SP3.

Figure 4.43 below shows stop positioning for one of our earlier 3-min PB examples. The RHS shows the 1 minute detail.



Figure 4.43 - PB Setup – Stop Positioning

As price slowed in the pullback, initial planning for the stop would have been tentatively at SP1, below the pre-breakout price action to the left.

As candle A prints, we might move this to position SP2, which will then provide the stop location, should an entry trigger and the trade orders be filled.

That's all there is to it. Just position the stop at a place where price should NOT reach, if you get into the trade – ideally beyond some form of technical (price action) barrier such as *higher timeframe S/R* or *trading timeframe* swing H/L.

Two final points...

(1) A common question is... how far beyond these levels should the stop be placed.

The answer is that it depends on your premise. Referring back to the last chart in figure 4.43, if price action gives you sufficient confidence that SP2 should not be hit, then that is your stop – immediately below the recent lows.

If you don't have sufficient confidence, and expect a possibility that price may retest these recent lows, possibly even exceeding them by a pip or two, then place the stop further away. Maybe even as far as SP1.

Personally, 'immediately below' for me means two pips (or points). For no other reason than I absolutely hate those occasional occurrences of stop out, when price breaks the lows by one pip before moving in my direction. This of course comes at the cost of 1 extra pip loss when I am stopped out.

(2) Please note as well that we don't just simply place our stop and target orders and then hold till either is hit. I use an active approach to trade management and will attempt to exit any losing trades well before their stop. The stop loss position is a worst-case stop. More on that later!

Great email Q&A with a YTC newsletter reader:

Q. I keep hearing traders (and, I believe you have said this as well), say that they'll put their stop where "the market invalidates the trade" or where "they know they are wrong" or "where the market should not go". Who says that piercing a support/resistance level invalidates a trade and therefore makes it "wrong"? Can't quite wrap my mind around this! Maybe it just needed to go down a little bit lower than the reference level low before going off in the intended direction. The market does what it does. It is only us traders who put impositions on the market and claim such statements as "market goes here then I am wrong". Just wondering what your thoughts are on this.

A. Market movement is never right or wrong. It just is what it is. However, my trades are designed around my interpretation of market action. It's my interpretation that says a particular setup and entry are in place and the stop should be positioned at xxx because that level will NOT be hit. And if it is, then it's my interpretation of market sentiment that is wrong (or my timing that is out). It's not the market that's wrong. It's my read of the market. Two different things! And if my read of the market is wrong, then I should NOT be in this trade.

4.4.2 - Targets

At this point, price is in a setup area and we've identified a potential stop location, a point to which price should NOT go.

We now aim to identify targets, should price trigger an entry.

Note that we do not wait for an entry, and then just simply target a reward 2 times our risk. Many people recommend simply placing a target such that it achieves a 2:1 reward:risk ratio, or even a 3:1 reward:risk ratio, and then simply walking away until price hits one or the other.

Absolute rubbish, in my opinion!

This amateur technique affords no consideration for where orderflow is expected to oppose future price action (ie. areas of support or resistance providing barriers to price movement). With our better understanding of the nature of markets and price movement, we will identify potential price targets based upon these areas of S/R.

And it fails to consider the fact that the market sentiment is constantly changing, and the premise they used for entry may not persist long beyond their entry.

Multiple Part Positions

I prefer to trade in two part positions, for reasons as described in the ebook, “The Importance of Exit Strategy”. (*If you haven’t read it, please do as it provides a lot of essential background information on stops, targets and trade management*).

Part 1 will always operate with a price target, T1.

Part 2 will have a tentative target, T2. However this part of the position may be allowed to run beyond T2 if price action shows the potential for a trending move. We’ll discuss more on this when we talk about trade management. For now, let’s just identify two targets, T1 and T2.

Identifying Price Targets

Our ultimate aim is to trade the swings on the *trading timeframe* chart, so we use it for defining our targets. Once again though, the *lower timeframe* may be used for fine-tuning if necessary.

The first price target T1 will be the next level which is expected to provide opposing orderflow.

The second target T2 will be just prior to the next level of *higher timeframe* S/R. If price is at all-time highs or lows (or at least long time highs or lows), and so offers no real „next level“ of S/R, I will target the first area of *trading timeframe* price stall beyond T1, or allow the price to simply trend with a trailing stop (an example follows shortly).

Let’s look back at some of our setup charts in order to identify appropriate targets.

Again though, remember that we don’t simply set our stops and targets and then walk away. These are just initial areas we expect price to reach, based on our expectations for future price action. We’ll be actively managing the trade and may take profits earlier if our expectations change and our premise is no longer believed valid.

In figure 4.44 below we show a BPB setup, with T1 identified at 1.5940, just short of potential swing high resistance, and T2 identified at 1.5955, just below the next resistance level. This is clearly (with the benefit of hindsight) one example which would have benefited from running part 2 rather than targeting T2.



Figure 4.44 - BPB Targets

Figure 4.45 below shows a CPB setup within an uptrend.

Initial stop placement is below the low of the pullback at 1.5890. T1 would be prior to the swing high, at 1.5920.

Price has been in a longer timeframe uptrend for over a month at this stage. The *higher timeframe* (30 min) chart does not provide any higher resistance areas which would serve as a potential second target. The daily chart provides potential resistance at 1.6070. Depending on my feel for price action I'll either exit at the first stall above T1, or trail a stop up to a T2 level of 1.6060.



Figure 4.45 - CPB Targets

With the benefit of hindsight, targeting the first price stall got us out around 1.5945. The trailing stop would have exited at some lower point, depending on how tight it was held.

Figure 4.46 below shows a BOF setup, as post-NFP price action stalls and fails above the sideways trading range.

With us re-entering a sideways trading range, I'd use the same target for both T1 and T2. T1 is just above the next support level. I don't have great faith in price getting to the next lower one, and would rather take T2 profits at the same place (T1) and look for another opportunity. In hindsight, T2 could have been a bit closer to the first support level, but that's trading – we rarely get it perfect!

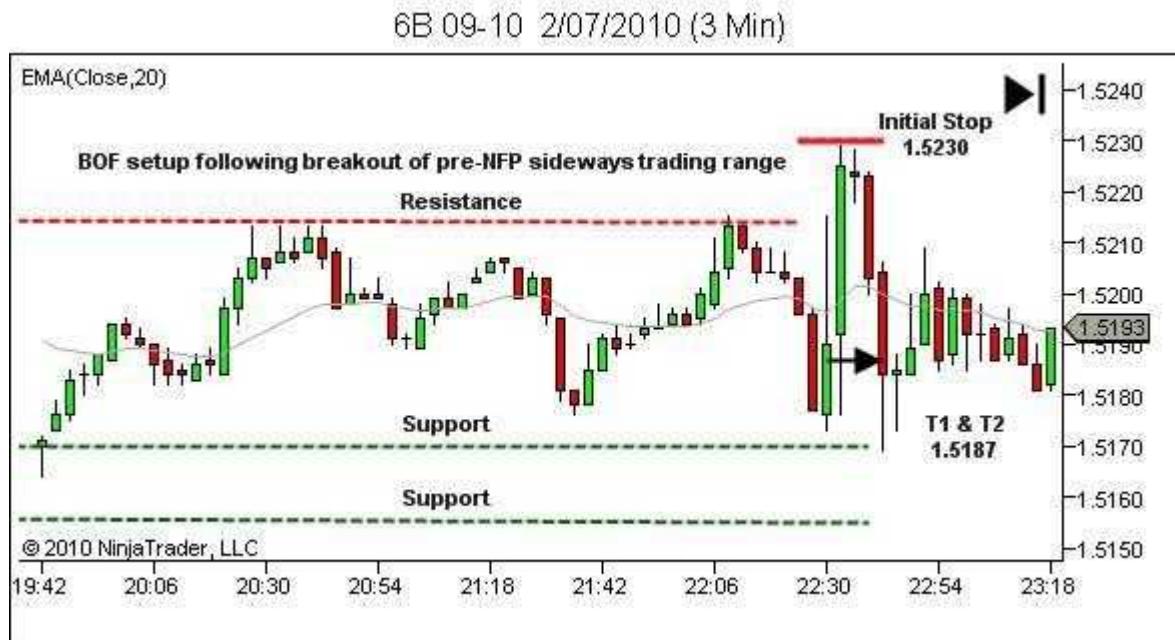


Figure 4.46 - BOF Targets

The T1 and T2 position was fine-tuned on the *lower timeframe* (1 min) chart, placed just above the high of the lowest candle at the last swing low, as shown below.



Figure 4.47 - Fine-tuning BOF Targets on the Lower Timeframe (1 min) Chart

Figure 4.48 below shows targets for a TST setup at resistance.



Figure 4.48 - TST Targets

The initial stop is above the TST price action reversal. T1 is just above the next 3-min swing low, at 1.5023. T2 is above the next support at 1.4989.

As you've seen, assigning targets is a simple process.

T1 is the next *trading timeframe* (3 min) area expected to provide opposing orderflow (swing H/L, S/R level).

T2 is the area of *higher timeframe* (30 min) S/R beyond T1, although much more flexibility is afforded with T2 and you can adjust it closer if you wish, or trail beyond it for (hopefully) greater profits.

4.4.3 - Entry

**“Take time to deliberate,
but when the time for action has arrived,
stop thinking and go in.”**

...Napoleon Bonaparte

Entry Principles

Let's start with some basic principles of entry.

Imperfection

Should we use a breakout style entry (stop entry order) or work a better price through a pullback style entry (limit entry order)?

Unfortunately, the best entry technique for a particular price action setup CANNOT be known until the trade is over and reviewed with the benefit of hindsight.

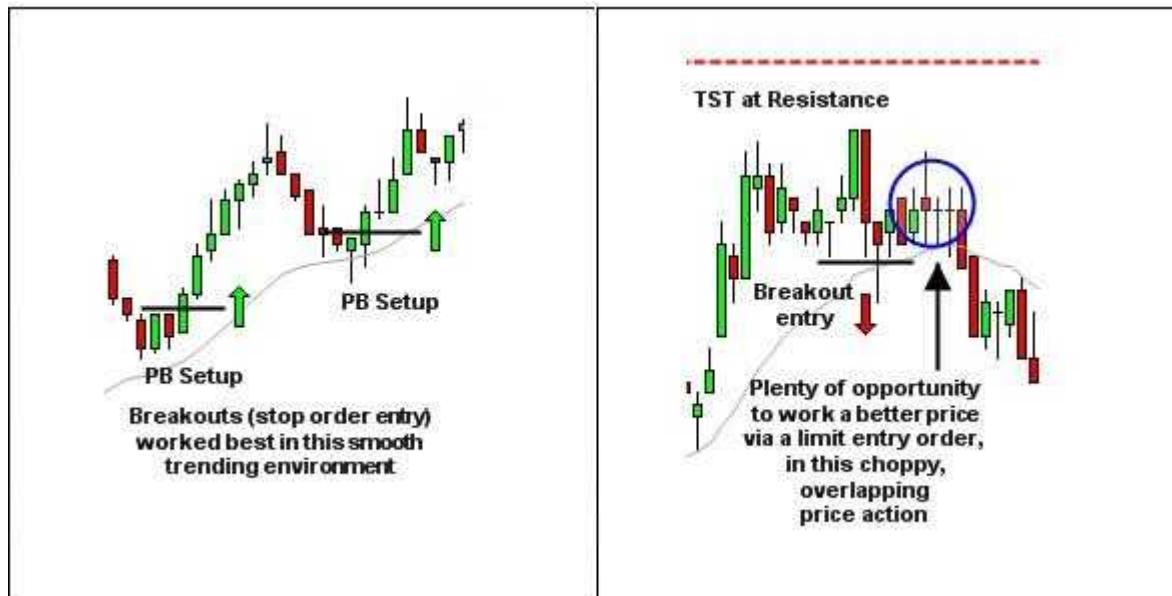


Figure 4.49 - Entry Uncertainty – Stop Entry or Limit Entry?

In figure 4.49, LHS, a breakout (stop order entry) was the best way to get into the trade. Price broke through the entry price and then didn't look back. There was very limited opportunity to get into a pullback (limit order) entry prior to the trigger, and certainly no opportunity after the

trigger. Those trying to work a better price risked missing this opportunity altogether. In this example, the breakout style entry was clearly the better option.

On the RHS, we see choppier action which provided significant opportunity to work a better limit order entry price, and gain increased profit potential and reduced risk compared with the breakout style entry. The limit order entry was the preferred option.

In figure 4.50, LHS, we see a breakout entry triggering us into a long position, right before price collapses and stops us out. Working a better pullback entry price via a limit order allowed us a small buffer, in which our trade was in profit, giving us the opportunity to perhaps scratch the trade at breakeven, or for a reduced loss. The limit order was clearly the best option in this case.

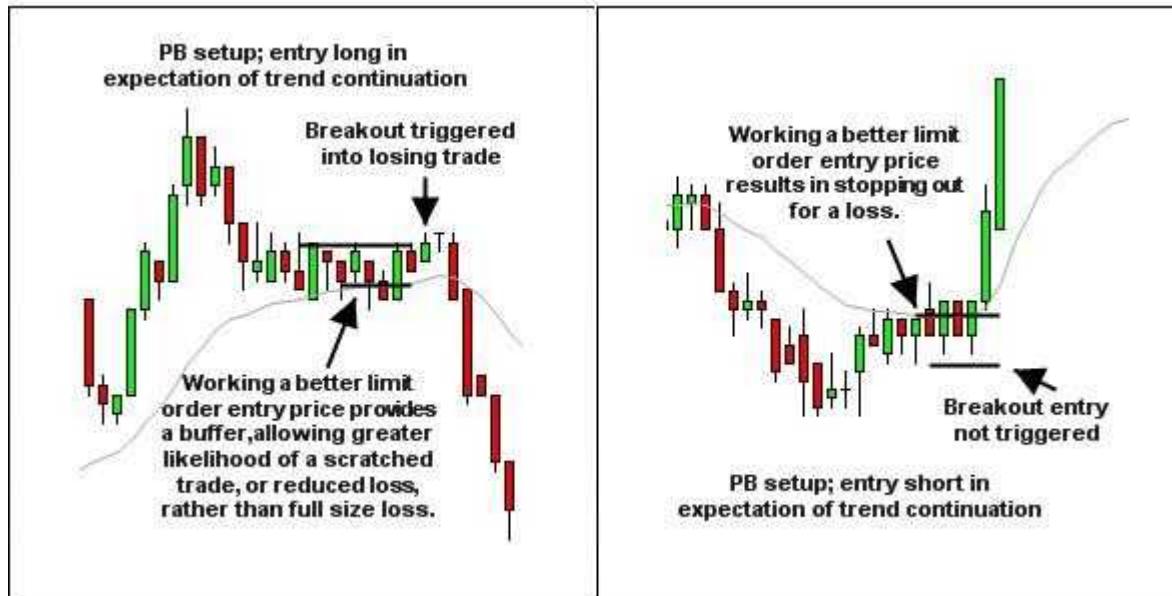


Figure 4.50 - Entry Uncertainty – Stop Entry or Limit Entry?

On the RHS though, we see an example in which we attempted a PB entry short. The market reversed, meaning the breakout order was never even filled, while the limit order provided us with a loss. In this case a breakout style entry was vastly superior, through avoiding a losing trade.

The nature of the market structure and price action environment can provide some good clues as to the preferred option. A smooth and flowing market may lean the probabilities towards a breakout style entry. A choppy and overlapping market may provide better opportunity through a pullback, limit order entry. However, that's not always the case.

The fact is... **we cannot know what the best entry strategy will be until we review the trade with the benefit of hindsight.**

So, all we can do is ensure that price is within an area in which we're happy to enter, and try to get the best price possible within that area. Then manage the trade!

If it turns out to be the best entry possible – great!

If not, accept it. Review the entry, seeking clues as to how you could perhaps have identified the better option, but don't stress over it too much.

Find an area where you're happy to enter a trade, and just work the best entry you can. Provided it's within your entry zone, accept whatever happens and just manage whatever the market throws at you. (How you manage and exit the trade is far more important than entry!)

So... how do we define our entry zone?

Wholesale vs Retail

Wholesale entry is a term which has been popularised lately by Don Miller (in his excellent blog (<http://donmillerjournal.blogspot.com>)). It's a term he's used quite a bit to describe his entry locations. I don't believe my use of the term is the same as his (so I apologise if this causes any confusion), but it's just a great descriptor for this entry concept.

Its standard business principles – buy wholesale; sell retail.

Why wouldn't we want to trade the same way; entering at wholesale prices and closing the position at retail prices?

My aim is to trade the *trading timeframe* swings. As we see below in figure 4.51, price swings have limited profit potential. They only go so far before reversing. Of course, we don't know how far each will go with absolute certainty, but we know they must end eventually.

This is the space we have available in which to gain an entry and secure a profit, hopefully before the reversal takes away our gains.



Figure 4.51 - Limited Profit Opportunity

Wholesale prices are early in each of the price swings; the professionals are entering short in expectation of lower prices where they can close out their position and secure a profit.

Retail prices are late in each price swing; the amateur, retail public are entering short in response to some TA trigger such as the break of the prior swing low, or a moving average cross. Quite likely it's the professionals who are on the other side of their trade, buying back to close out their short position.

My intent is to enter as EARLY AS POSSIBLE, along with the wholesale, professional crowd.

Some traders may argue that trying to enter as early as possible in a move is attempting to pick tops or bottoms. Absolutely! Why wouldn't you want to – that's where risk is lowest and profit potential is at a maximum!

Retail entries increase risk and reduce profit potential, as shown in figure 4.52 which demonstrates entry on a break of the previous swing low.

Wholesale entries ensure reduced risk and greater profit potential, as shown in figure 4.53.

6B 09-10 8/07/2010 (3 Min)

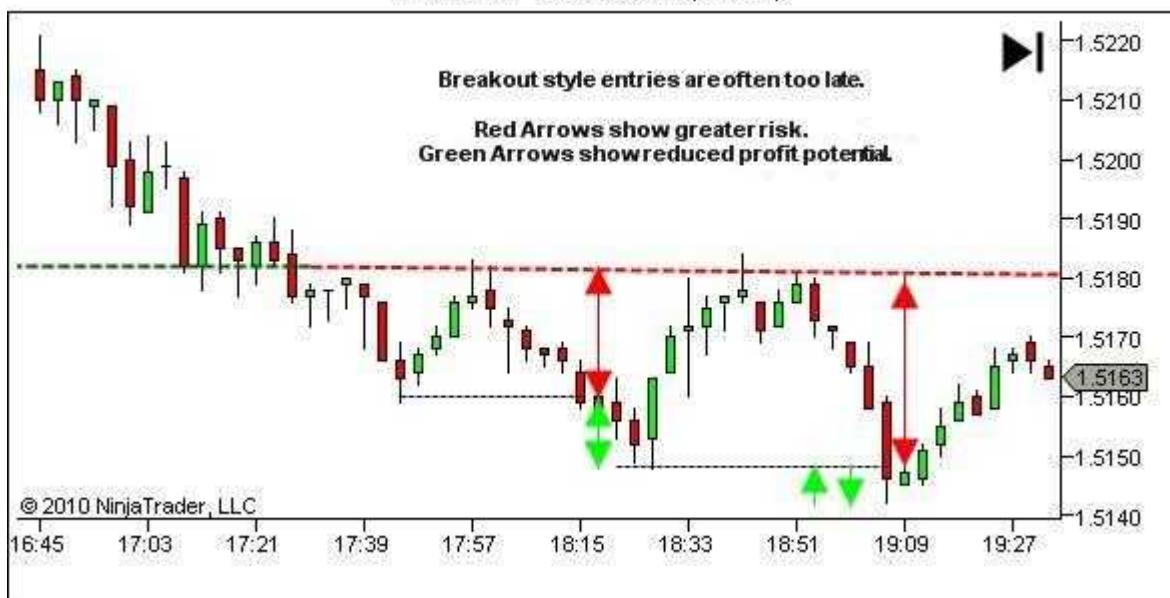


Figure 4.52 - Breakout Style Entries are Often Too Late for Swing Trading

6B 09-10 8/07/2010 (3 Min)



Figure 4.53 - Wholesale Entries – Reduced Risk & Greater Profit Potential

How do we define the wholesale area?

Consider the *trading timeframe* chart. Our setups are designed around identifying weakness moving into S/R, weakness moving into swing H/L or weakness in pullbacks within a trend. We identify the retail traders entering late in this move, becoming trapped in a low probability trade and being forced to exit. We aim to enter at or before point when the trapped traders realize they need to get out.

This point is really easy to identify. It's essentially a breakout of some form of reversal pattern or area of congestion at the setup area.

Anything at or before this point is wholesale. Anything after this point is retail.

I call this point the **Last Wholesale Price (LWP)**. I aim for entry at or before the LWP. I will not chase entry after the LWP under any circumstances, as to do so increases risk and reduces potential reward. If I miss an entry before it passes the LWP, I'll be patient and wait for any second-chance retest opportunities, or the next setup.

Please note, we do not simply enter at this point. We use the lower timeframe to try to seek a better price, if at all possible. This is simply the last price we will accept in order to ensure wholesale prices.

All examples below are taken from the *trading timeframe* (3 min).

Figures 4.54 and 4.55 demonstrate the Last Wholesale Price (LWP) for several setups. In example (A) we see a BPB setup. A breakout through support has occurred and price returns to the point of breakout before showing a change of sentiment – two bull candles followed by a low close range candle. Continuation below this candle will start to trigger stops (in this case both the late longs and also the trapped longs from before the original breakout downwards). This point is the last wholesale price. Entry must be achieved at or before the breakout below this low close range candle.

In example (B) we have a BOF; actually a second chance BOF entry. Price is testing the earlier lows. LWP is a break above the last low close bear candle. This will trigger a failure of two pushes down below support. The first of the stops will be triggered helping push our price higher. Entry must be achieved at or before the LWP, or else I will pass on this trade.

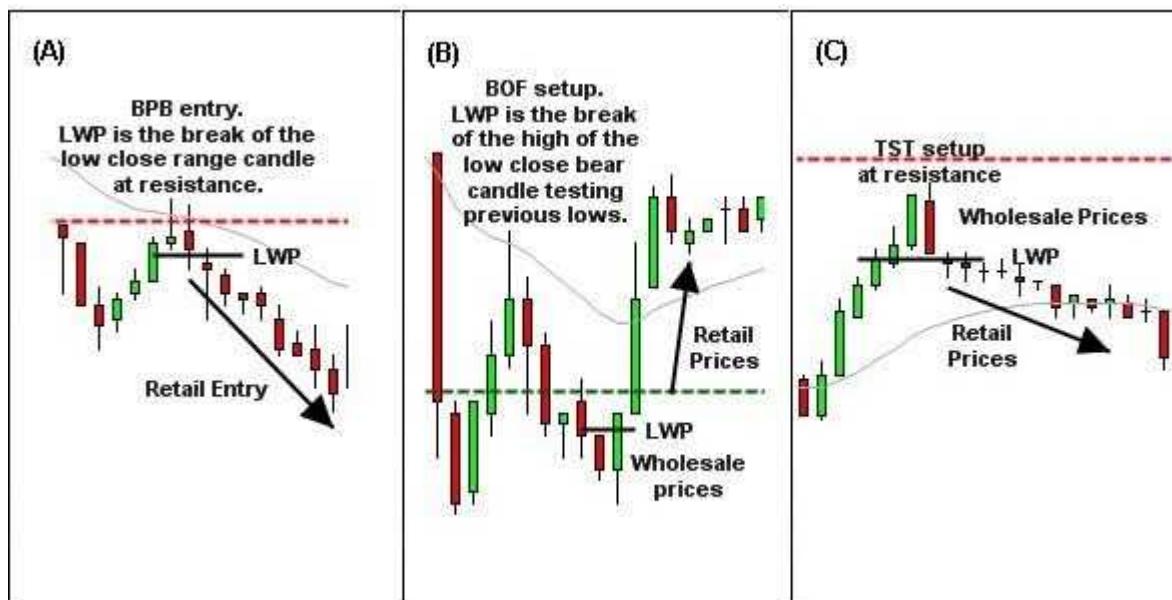


Figure 4.54 - Last Wholesale Price (1 of 2)

In example (C) we see a TST at resistance. A sequence of bull candles have suddenly given way to a low close bear candle, completely reversing the previous large high close bull candle. This is a rapid change of sentiment. Continuation lower will start to trigger the stops. This is therefore our last wholesale price (LWP).

Example (D) shows a PB setup within an uptrend. The last wholesale price (LWP) is above the green candle with lower tail that rapidly reverses sentiment. Entry must be achieved at or before this area.

Example (E) shows a CPB setup within an uptrend. The LWP is above the two candle pattern (low close bear candle followed by the high close range candle which completely reversed sentiment). Stops will be triggered on continuation above this pattern.

Example (F) shows a TST of lower range support from a sideways trend. Price is slowing into the support area, as shown by the lower tail on the mid close bear candle and then the mid close range candle. Stops will be tightened above this pause (along with new longs simply entering on a breakout of price at the lower support area). This is our LWP. Our entry must be achieved at or before this point.

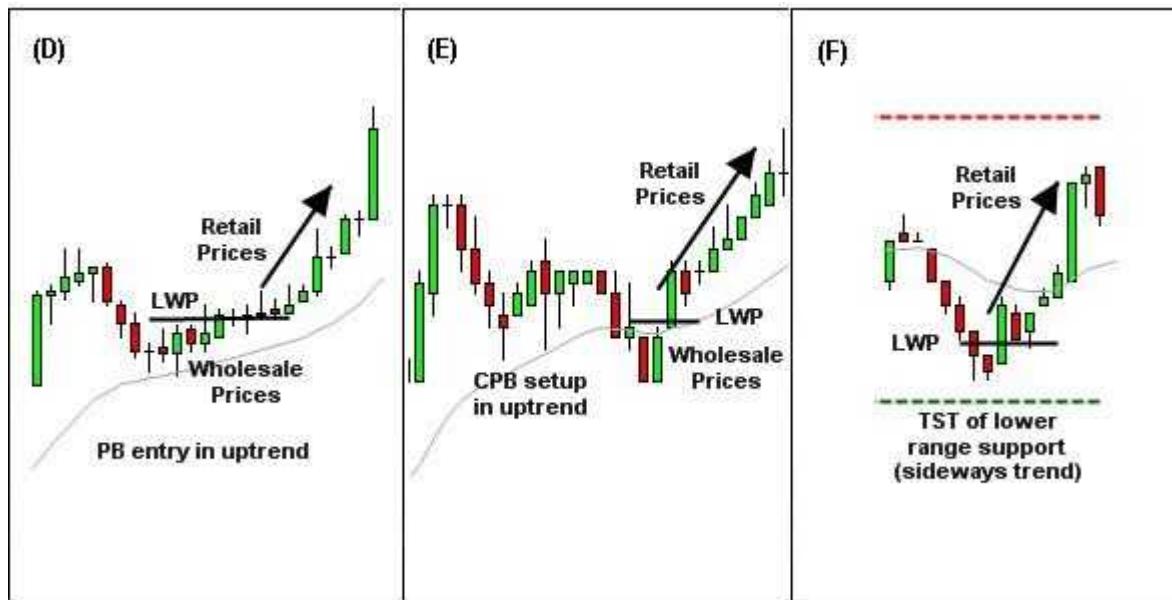


Figure 4.55 - Last Wholesale Price (2 of 2)

Our wholesale area is up to and including the breakout of the *trading timeframe* reversal price action; the point at which stops will start to be triggered by those trapped in a losing position.

We aim to enter at or before this area.

We do not chase price beyond this area if an entry is missed. We wait for either a second chance retest, or the next setup.

Reward:Risk Ratio

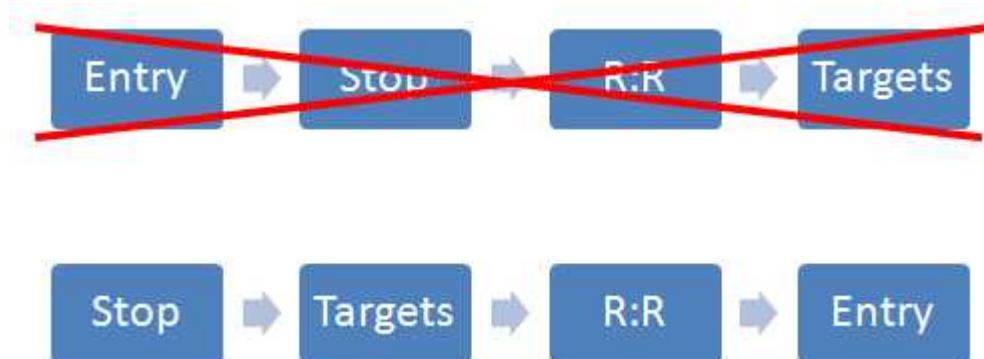


Figure 4.56 - Stop-Targets-R:R-Entry

Most traders find an entry trigger, then place their stop beyond recent price action swing H/L, measure their risk, set a target 2-3 times the amount of risk, and sit back and wait till either the stop or the target is hit.

Not good!

They don't even check market structure or price action to see whether or not that target is realistically achievable.

Market structure provides us with our setup areas – areas with expectation of orderflow from losers exiting their trades.

Price action provides us with a stop point – an area where price should NOT go, if our trade idea is valid.

Price action also provides us with a target – an area where orderflow will oppose our trade, which may just pause price temporarily, but which also may reverse it completely.

Why would you place a 3:1 R:R target beyond S/R barriers, and then just hope price breaks through them? That's just plain dumb.

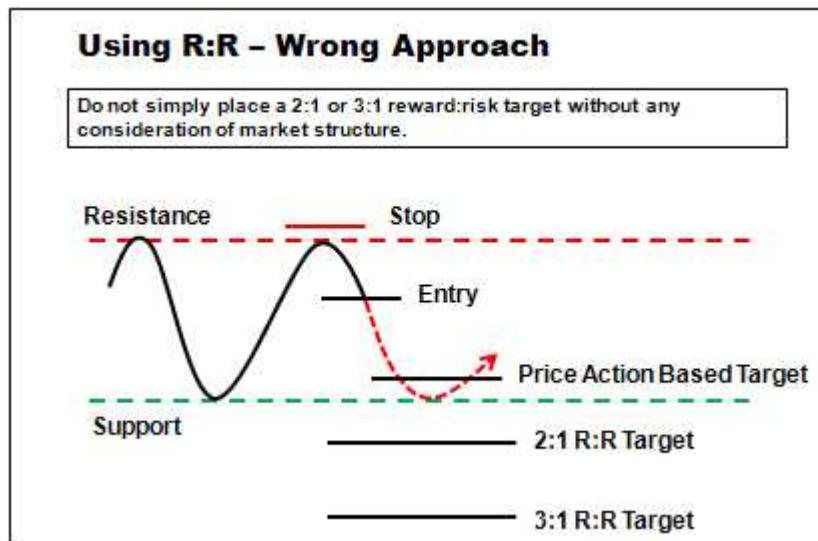


Figure 4.57 - Using R:R – Wrong Approach

Our approach differs. We start with our stop and target and then apply our desired R:R ratio over top of that, to define a Last R:R Price (LRP), beyond which we can't enter.

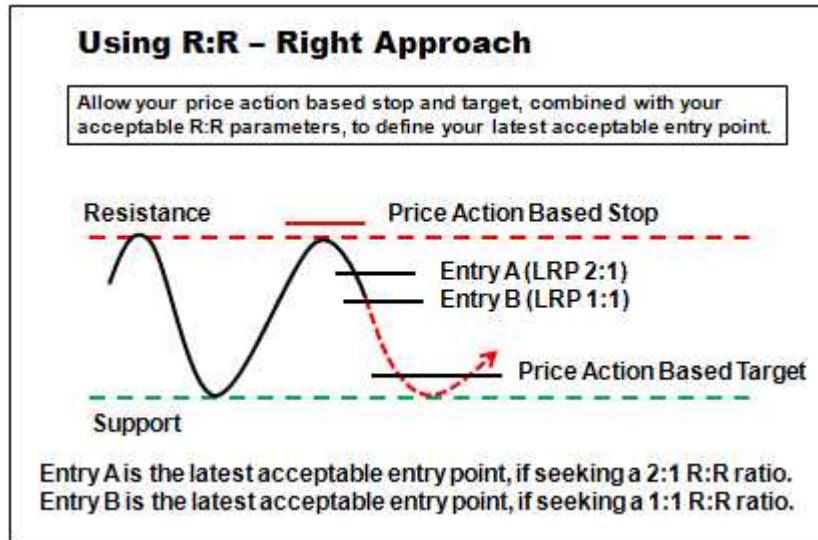


Figure 4.58 - Using R:R – Right Approach

What R:R ratio do I use?

I aim for a 1:1 R:R ratio for my part one entry. So, the LRP is defined as exactly half way between the stop location and the first target, T1 (the next *trading timeframe* swing H/L or area of S/R).

You might argue that 1:1 is insufficient. Remember, my active management strategy aims to ensure that I rarely exit my losers at the stop; I aim to scratch them before then if the premise is in doubt. If managed effectively, this will reduce the risk side of my actual R:R ratio.

Also, this is only part one. Part two is available to run to a further target (or till it hits a trailing stop), aiming to maximise the reward side of my actual R:R ratio.

Entry Zone

We now have two latest entry points. One defined by price action (LWP). And one defined by our risk management parameters (LRP).

The entry zone is between the stop and the closer of the two last entry prices (LWP or LRP).

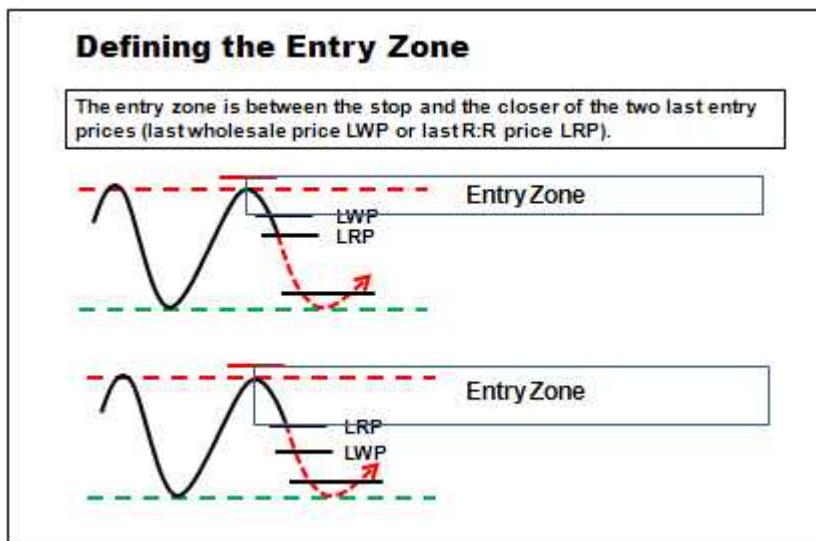


Figure 4.59 - Defining the Entry Zone

Aiming to work an entry within this Entry Zone ensures that (a) our entry price is within the wholesale price area and (b) our entry price meets our acceptable R:R parameters.

Please note: Everything in this book requires multiple pages to describe in detail. That doesn't mean it's complex. Don't get in the habit of calculating and recording your LRP and LWP. You can visually see your LWP (it's the breakout of any trading timeframe reversal pattern in your setup area) and you can visually eyeball the LRP (exactly half way between your stop and target). Don't create complexity when it's not needed. While fine-tuning our entry on the lower timeframe, we simply ensure we don't chase price beyond the closer of these two areas.

Entry Preconditions

- Price is in a setup area
 - We're fading weakness as price interacts with S/R or a swing H/L; or fading weakness on a pullback within a trend
- A stop has been identified
 - An area is identified beyond which price will NOT go, if our trade idea is valid.
 - Ideally S/R or swing H/L
- Targets have been identified
 - Next trading timeframe swing H/L or S/R
- The entry zone is identified
 - Having considered LWP and LRP

Once all this is in place, it's time to trade.

Fade the weakness!

Spring the Trap!

Entry Technique - Simplified Entry

The first option I will provide is the simplified entry technique. This is not my preference. I prefer to monitor the lower timeframe price action in an attempt to work a better entry price. We'll discuss that later.

However, many traders who are still working to achieve consistent profitability will find it difficult to make active entry decisions, while their decision making is subject to all kinds of negative psychological influence which lead to hesitation and second-guessing. The simplified entry technique will assist them in getting entry to trades.

The simplified entry technique involves placing a stop entry order at LWP, as soon as we have identified that position.

The order will be adjusted if not triggered, and subsequent price action offers a better LWP. And the order will be cancelled if subsequent price action invalidates the setup.

This is about as simple as entry can be made. Place a stop entry order and wait.

Important condition: this is only to be used when the entry offers a R:R of 1:1 or greater. If it doesn't, pass on the trade and wait for either a better entry or the next setup.

The simplified entry technique will of course come at the cost of a worse price, than may be achieved through working an entry, and therefore a reduced R:R. However, it is still effective. After all, the LWP is the point at which orderflow should be assisting our trades. Any entry before then may offer a better R:R, but this comes at the risk of LWP not being achieved.

You may wish to review figures 4.54 and 4.55, which offered examples of the LWP. In using the simplified entry technique, we would simply place a stop entry order at this price, await the market to trigger us into our trade, and then commence our trade management. Nice and simple!

As mentioned earlier, my preference is for attempting to work an improved entry price.

When you're comfortable with the remainder of the trading process I'd recommend that you start using the lower timeframe to try to work a better entry. Start this process using a market replay feature – play the entry first using LWP, and then play again several times working a better entry. Over time you'll become comfortable with the process.

Please note that all trade examples throughout the book will use the active entry process rather than the simplified entry, for education purposes. If you choose to use the simplified process, it will be obvious where the entry occurs – the explanation of the trade entry will identify the LWP.

Entry Technique - Working an Improved Price through an Active Entry Process

For those that wish to actively manage their entry through *lower timeframe* (1 min) price action, in an attempt to achieve a better price than LWP, this section will discuss the process that I use.

Entry Decision

You should recall these sentences from earlier:

The fact is... we cannot know what the best entry strategy will be until we review the trade with the benefit of hindsight.

So, all we can do is ensure that price is within an area in which we're happy to enter, and try to get the best price possible within that area. Then manage the trade!

In a perfect world, entry within our entry zone would be a result of our finely tuned intuition. Unfortunately most of us will never achieve expertise in that area. The best we can hope for is gradual improvement with experience.

During the learning phase most of us need some kind of trigger for entry. Some sign that will provide us with sufficient confidence to hit that buy or sell button.

Primarily I look for one of two signs in order to make my entry decision.

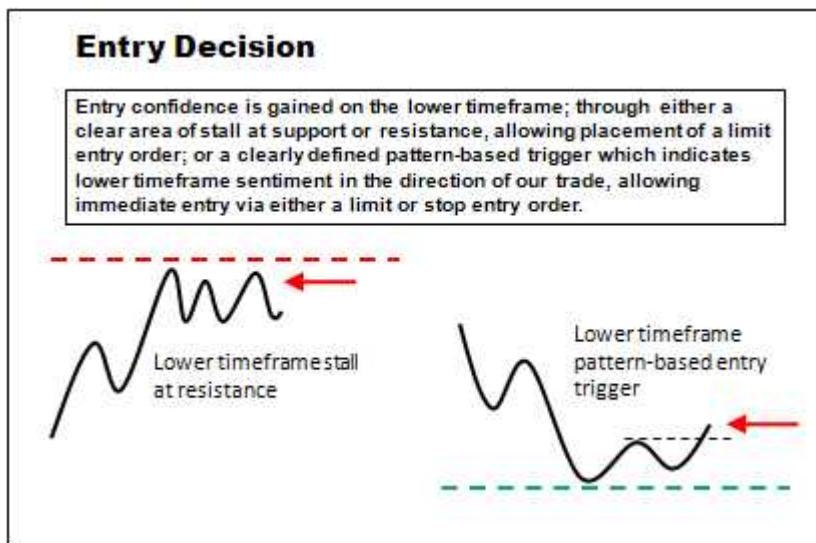


Figure 4.60 - Entry Decision Stall or Trigger

The first is a stall in price action. The second is a pattern based trigger. The stall is rarer, and more complex. We'll look at it first including some examples; then move onto the easier pattern based triggers.

Stall

A stall is evident when price displays a clear inability to continue beyond an area of setup support or resistance (whether higher timeframe S/R, swing H/L or range S/R).

The number of candles in a *stall* is difficult to define – every situation is unique, and you'll know it when you see it – but I'd usually expect at least 3 *trading timeframe* candles.

Confidence in a level holding allows you to place a limit entry order close to the area of S/R. The stalled price action offers good potential for another test of that area allowing a massively discounted wholesale entry price. If you're subsequently proven wrong (or early) then the risk has been minimised. If you're right however, the reward potential has been maximised. Either way... assuming your setup area is valid, it's a great entry.



Figure 4.61 - TST of Swing Low – Entry Trigger via Stall

Figure 4.61 above shows a TST of a swing low in a wide swing uptrend. You could also call it a CPB if you wish. I prefer TST in this case simply because the last move from the area provided a stronger surge of momentum which led to a change of trend to upwards. This area would be expected to provide support, should price return to the area.

Price did return to the area just 45 mins later, demonstrating bullish pressure at this level of swing low support, through forming a stall pattern.

Looking at the *lower timeframe* (1 min) on the RHS, confidence in the stall was gained after the larger green (high close bull candle) allowing a BUY LIMIT order to be placed closer to the lows of the stall at E1. This provides a low risk entry with higher potential reward, well before the LWP entry point.

Note of course that the risk with this sort of entry is that, should the support level break we will have been triggered into a losing trade, which would not have been entered had we relied simply on a BUY STOP at LWP.

However, risk has been minimised, and profit potential has been maximised. Provided our analysis identifies a quality setup area and a clear stall in the area, this is a risk worth taking.

A second risk is of lost opportunity, should price not hit the BUY LIMIT order. We will later look at a way of ensuring that you don't miss these opportunities.

We have a much more complex example in figure 4.62 below, which displays a CPB setup in a downtrend.

Looking at the *trading timeframe* (3 min) on the LHS we have a clear area defined as a stop, S1 at 1.5619.

T1 caused some problems though. Normally, in accordance with the definition of a downtrend, we expect our extensions to break the next swing low. So in a nice orderly trend I'd be happy to place T1 beyond the swing low. However in this case price action was not being orderly. I was not greatly confident in the fact that price would break the swing lows, so I placed T1 just above the swing low at 1.5603.

LWP was based on a break below the congestion, which places it at 1.5605. Clearly this is inappropriate (14 pips risk for 2 pips reward). LRP is midway between 1.5603 and 1.5619; or 1.5611.

I would NOT be interested in this trade unless I could get an entry at or above LRP, 1.5611.



Figure 4.62 - CPB Setup – Entry via Stall

Looking at the *lower timeframe* (1 min) on the RHS, I am satisfied that a stall has developed after the second attempt to push the resistance area (which is the fourth candle at the stall on the *trading timeframe* (3 min) chart). An entry limit order placed at E1, 1.5611, would be filled within two minutes providing us with a wholesale entry that also meets our minimum R:R requirements.

Note that this trade offered an opportunity to take profits at T1 and then re-enter again at E1 for a second bite. Personally I would have passed on this second opportunity due to the price action at T1 resembling too much of a spring (*see next section for the ‘spring’*).

Price did however continue down to T2 allowing greater profits on the second part.

Pattern Based Triggers

Now let's consider the pattern based triggers. These include ANY *lower timeframe* (1 min) price action pattern which:

- 1) Confirms short-term sentiment in the direction of our trade premise, and
- 2) Indicates an area where price should NOT go. This area may then be used as our stop loss.

Examples include:

- 1) Any standard candlestick reversal pattern
- 2) Any standard price bar reversal pattern
- 3) Any trap pattern which proves the loser wrong
 - a) spike & ledge
 - b) double top or bottom
 - c) spring or upthrust
 - d) 3-swing retrace
 - e) 123 top or bottom
 - f) test of breakout point
 - g) expansion bar

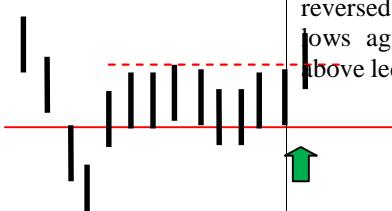
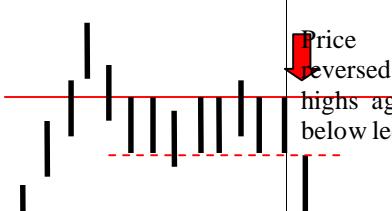
Refer to the video series at: http://www.yourtradingcoach.com/Videos-Technical-Analysis/Candlestick-Charting-Videos.html	Candlestick Reversal Patterns
Refer to the video series at: http://www.yourtradingcoach.com/Videos-Technical-Analysis/Complete-Price-Bar-Reversal-Video-Series.html	Price Bar Reversal Patterns
	Spike and Ledge (bullish)  Price spike down, quickly reversed, then unable to meet lows again. Trigger = break above ledge.
	Spike and Ledge (bearish)  Price spike up, quickly reversed, then unable to meet highs again. Trigger = break below ledge.

Figure 4.63 - Lower Timeframe Triggers (1 of 4)

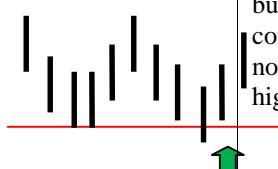
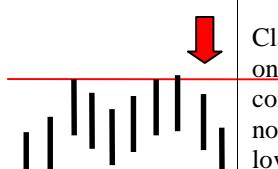
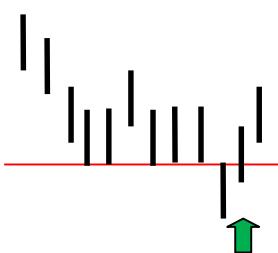
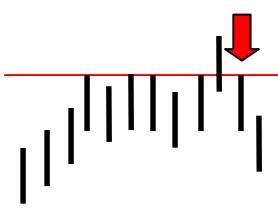
	<p>Double Bottom</p>  <p>Classic double bottom setup, but on micro scale. Enter on confirmation of second low, no later than break of swing high.</p>
	<p>Double Top</p>  <p>Classic double top setup, but on micro scale. Enter on confirmation of second high, no later than break of swing low.</p>
	<p>Spring</p>  <p>Price spike below support which is rapidly reversed within one or two candles, such as hammer or bullish engulfing pattern. Trigger is a break above the high of the spring candle.</p>
	<p>Upthrust</p>  <p>Price spike above resistance which is rapidly reversed within one or two candles, such as shooting star or bearish engulfing pattern. Trigger is a break below the low of the upthrust candle.</p>

Figure 4.64 - Lower Timeframe Triggers (2 of 4)

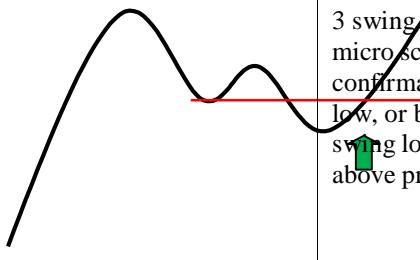
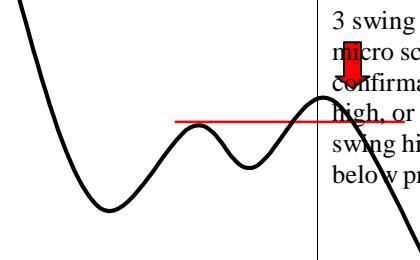
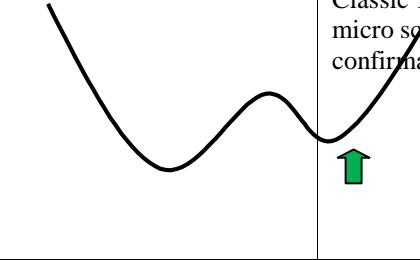
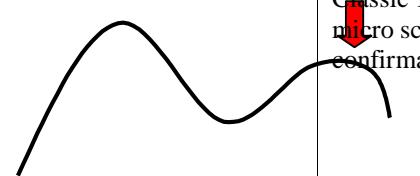
	3 swing retrace (bullish) 3 swing retracement, but on a micro scale. Enter on confirmation of second swing low, or break above previous swing low (or even close above previous swing low)
	3 swing retrace (bearish) 3 swing retracement, but on a micro scale. Enter on confirmation of second swing high, or break below previous swing high (or even close below previous swing high)
	123 bottom Classic 123 bottom, except on micro scale. Enter on confirmation of higher low.
	123 top Classic 123 top, except on micro scale. Enter on confirmation of lower high.

Figure 4.65 - Lower Timeframe Triggers (3 of 4)

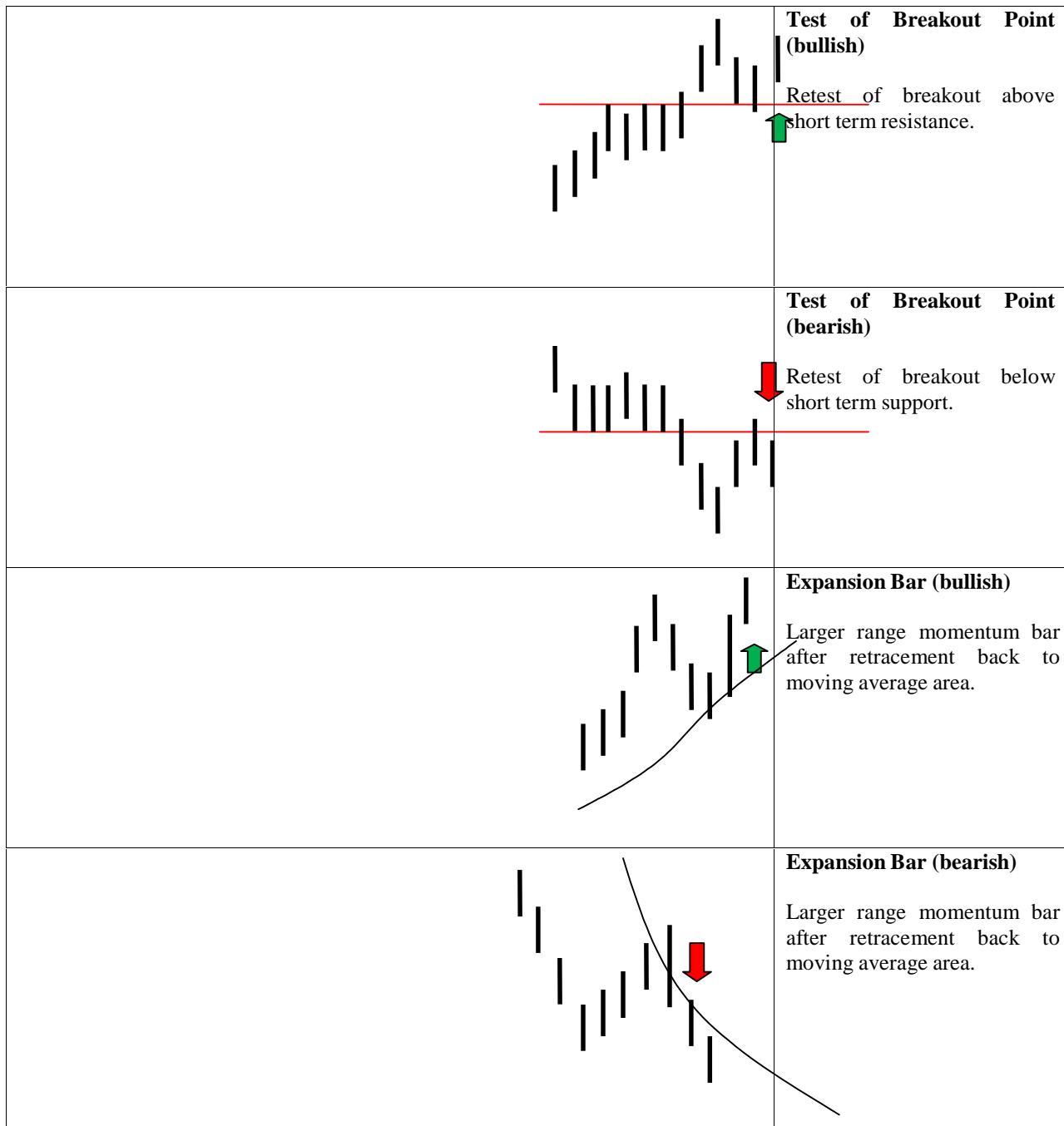


Figure 4.66 - Lower Timeframe Triggers (4 of 4)

My preference for entry order type is for a LIMIT order, trying to sell at the ask or buy at the bid. I'll then adjust if required. However I'll be careful not to chase price beyond the LWP / LRP.

You may prefer the use of a STOP entry order, to ensure entry. I do not ever recommend MARKET orders for entry, due to the risk of slippage.

The following charts display examples of entry decisions, showing the *trading timeframe* (3 min) price action and setup on the left and the entry decision trigger on the right.

In figure 4.67 below we have a quite aggressive setup in which we are taking a BOF against a swing low rather than any *higher timeframe* (30 min) S/R.

While lower probability, I do quite like these setups when there is a clear weakening of the trend, or in cases such as this which involve a weaker retest of a climactic low (or high).

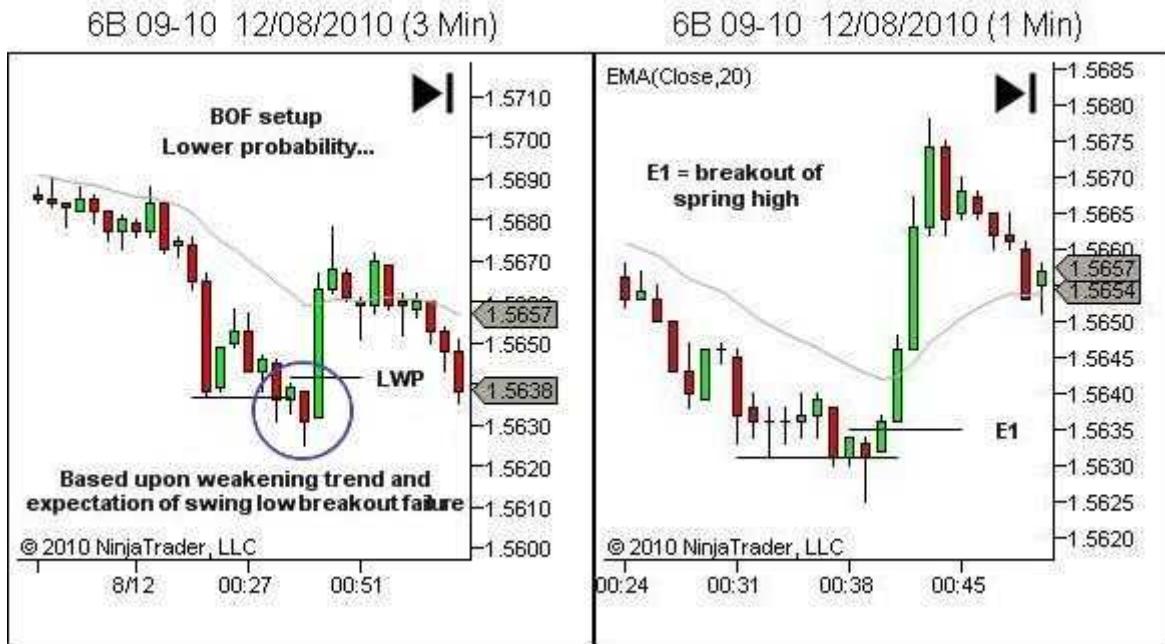


Figure 4.67 - BOF Setup – Entry Trigger via Spring

The *lower timeframe* (1 min) price action to the right shows an area of short-term support being formed at the lows, with a spring below that support rapidly failing. The entry would be on a break above the spring, at E1.

This is an example in which entering via the *lower timeframe* (1 min) entry trigger rather than at LWP gained us an extra six pips,



Figure 4.68 - TST Setup – Entry Trigger via Double Bottom Pattern

In figure 4.68 above, we have a TST of *higher timeframe* (30 min) support. Entry E1 on the *lower timeframe* (1 min) chart (RHS) is triggered on the close of the high close bull candle confirming the double bottom price pattern. Note that in this case you could not take an entry on the break of the swing high between the double bottom lows (the traditional double bottom entry location), as doing so would result in an entry beyond the LWP. While it would have worked fine in this case, to do so would lower the probability of the trade while also reducing the potential R:R ratio.

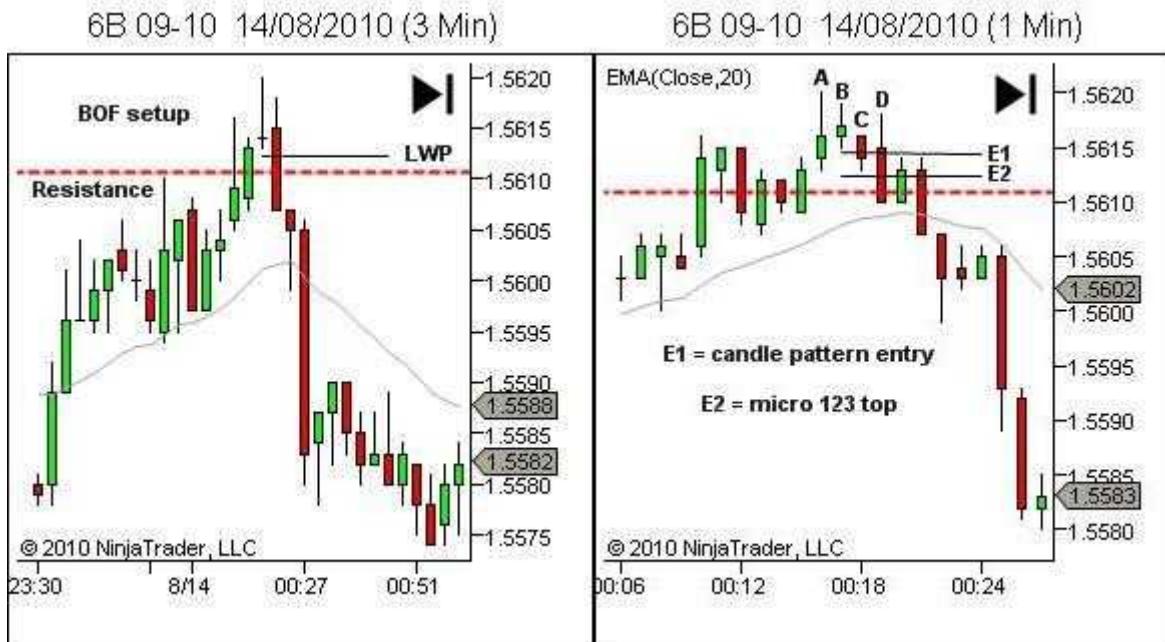


Figure 4.69- BOF Setup – Entry Trigger via Candle Pattern or 123 Top

In figure 4.69 above, we see a BOF setup offering two pattern based entry options. The first at E1 is a break below the low of candle B; a candle based pattern trigger based on candle A (kind of a shooting star!!) and candle B (spinning top). The second at E2 (in case you didn't like E1) is a micro 123 top (lower high) formed by the move up to the high of A, to the low of C, then to the high of D, before breaking down below the low of C and continuing downwards.

This second (E2) entry option is also right at our LWP based on the *trading timeframe* (3 min) chart to the left. So, in this case, E2 offers no advantage over just entering at LWP, apart from possibly greater confidence in the entry through observing the *lower timeframe* (1 min) sentiment change.

Ensuring We Don't Miss an Entry

We have two competing requirements:

- 1) To work the best price possible; and
- 2) To ensure we do not miss the entry by having it rapidly move beyond our entry zone without us.

When the last wholesale price (LWP) is within our entry zone, we have an opportunity to ensure we do not miss the trade opportunity by bracketing price.

Bracketing works as follows:

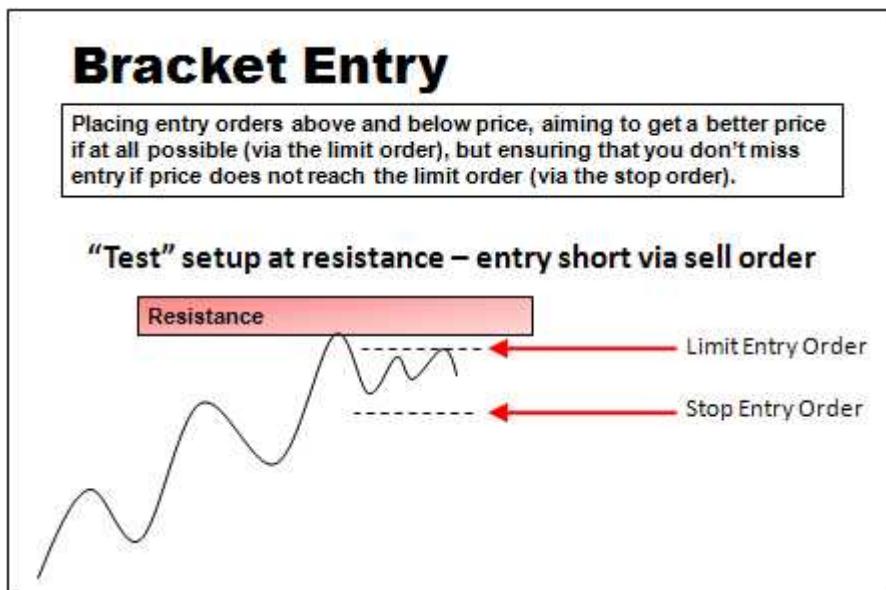


Figure 4.70 - Bracket Entry example – Test Setup at Resistance

In the example above, you would simply place both your limit and stop entry orders. The stop entry is placed at LWP (ie. our simplified entry technique) to ensure you are filled IF the market suddenly moves lower. Then you work the limit order as required to try for a better price against the resistance area.

Be sure that the other order is cancelled upon receiving a fill, otherwise you risk having two positions established.

If the LWP is beyond our entry zone, we don't place a stop entry order. To do so would risk an entry beyond our acceptable R:R parameters. And we don't place one at the last reward:risk price (half way to target), as to do so is not based on any technical level. In this case, we don't bracket price but simply attempt to work the limit order, accepting a missed trade if it happens.

Missed Entries

If you miss an entry, never chase it beyond acceptable wholesale or R:R limits.

Entries must **only** occur at the setup areas, as they exist at areas of proven supply/demand imbalance. The further we move from the areas, the less the likelihood of profit and the greater risk.

Take note of the missed opportunity in your journal to allow a post-session review and market replay – to identify any errors, review the setup with “hindsight perfect” performance, learn and improve.

Then wait for the next opportunity. Another will be along shortly.

Alternate Entry Techniques

My trading style involves multiple part positions. I prefer an all-in-scale-out approach, in which all parts of the trade are placed on at once, and each part is scaled out at different targets. We'll talk more about how I scale out in the next section on Trade Management. However you may also wish to test some means of scaling in, perhaps entering part one via a worked limit order and part two via a stop entry order at LWP.

Testing on a simulator (demo) platform will allow you to determine the method that is psychologically best for your own trading.

Entry Examples

The above sections offered several examples. Let's work through two more though; just to be sure we get it.

Figure 4.71 below shows a BPB setup – previous support becoming resistance. The *lower timeframe* (1 min) offers two great opportunities to enter the BPB, both triggering off candlestick pattern. Entry is at E1 below the bearish engulfing pattern, or E2 below the shooting star.



Figure 4.71 - BPB Setup – Entry via Candlestick Patterns

Figure 4.72 below shows a CPB in an uptrend, with the *trading timeframe* (3 min) chart forming a nice spring pattern. The LWP is the breakout of the spring candle, although (as is often the case) we don't know that till the close of that candle. Trade decision often comes quickly!

Looking at the *lower timeframe* (1 min), we see a breach of the short-term support area (formed by the swing low at the end of the first pullback swing). Entry E1 is on a break of these candles, effectively making this both a spring trigger and a candle pattern trigger (dragonfly doji and morning star).

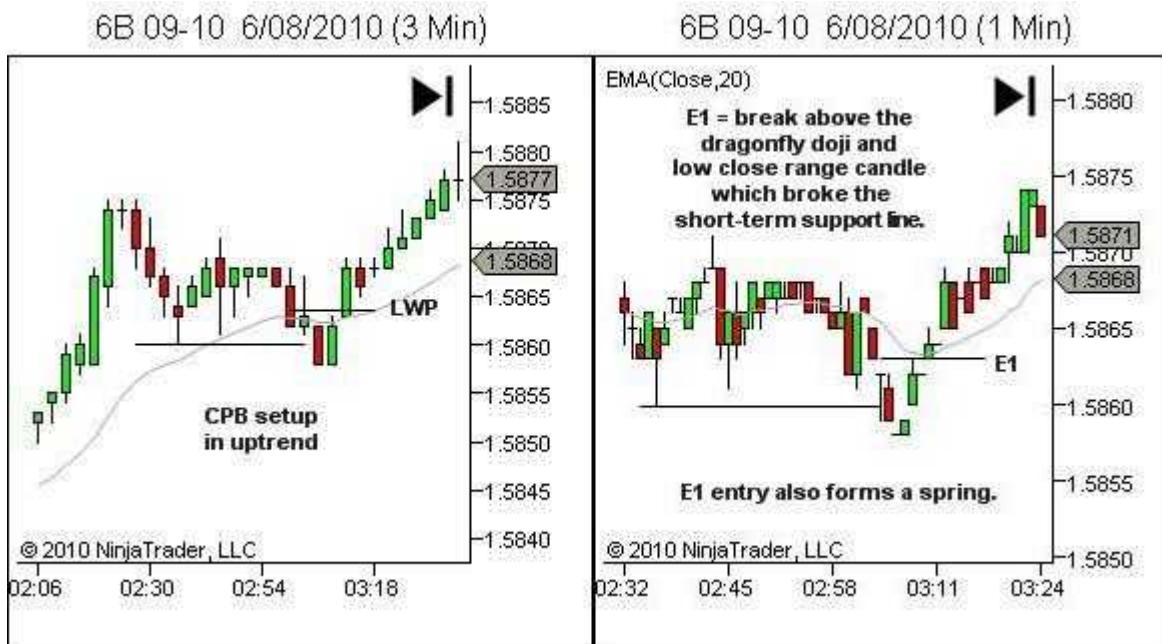


Figure 4.72 - CPB Setup – Entry via Spring and Candle Patterns

Entry Summary

The *Trading timeframe* defines the places we want to trade.

The *Lower timeframe* is used to time entry.

We note when price enters our *trading timeframe* setup zones. But we don't automatically enter. We watch how price reacts. We search for weakness, and traders trapped in a low probability position. Entries are taken at or before the point where the losers realise they're wrong.

We recognise that the optimal entry can never be known, except with the benefit of hindsight. So we simply aim for the best entry possible within our entry zone. We work a limit order for a stall or pattern based trigger entry. And we place a stop entry order at or near the last wholesale price, in order to ensure we don't miss an opportunity.

A final word of warning... the use of limit orders does come with risk. Price action may produce a nice looking setup, with a clearly defined stop area and entry zone, tempting you to work a *lower timeframe* entry at a great wholesale limit order price. It then may reverse rapidly only to stop you out BEFORE price even gets to the LWP.

Remember, the LWP is the *trading timeframe* point at which the losers will start exiting.

That's where our orderflow enters the market, driving our trade to profit.

Caution needs to be applied to earlier entries as they do not yet have the benefit of this trapped orderflow. However, they do have the benefit of S/R or swing high/lows to their back, and if triggered based on stall or a *lower timeframe* pattern based entry, they still provide good odds.

The following section, Trade Management, will touch on the concept of scratching a trade. This will be particularly useful for our early entries, which then fail to follow through past the LWP.

4.4.4 - Trade Management

**“Once you have taken a decision,
never look back on it.”**

...Field Marshal Viscount Allenby

Once you have taken a decision to trade, never look back on it. It's time to manage it.

Active vs. Passive Trade Management

I want to commence this section by sharing some email Q&A (also posted on my website) which explains my reasons for preferring an active trade management style to a passive (set and forget) style...

Excerpt from email received:

A couple of questions about stop and profit target management. I'm not a probabilities expert, but can't one make the "argument" that once the trade is actually put on, accepting anything less than the initial risk/reward outcomes actually interferes with the probabilities and in the long run can neither help nor hurt because even decisions to adjust are subject to probabilities and will even out over time?

In other words, tightening my stop may help me some and hurt me some, but isn't it likely to be a wash over the course of 1000 trades? Also, once the trade is set, even if stops are immediately adjusted, the full risk of the initial stop was incurred once the trade is entered, so the possibility full reward should be allowed to occur. As an example, with a 9 tick profit and 5 tick stop loss, as soon as I enter a trade, I am assuming a 5 tick risk. It doesn't matter that I tighten the stop, the risk was already undertaken. So, for my ratios and probabilities to work in the long run, shouldn't I just let the trade be what it will be?

Excerpt from response:

Should we use an active or a passive trade management style? This question really gets to the heart of who we are as a trader and how we believe the market works.

Are you a mechanical / systems trader or a discretionary trader?

A mechanical trader who has conducted extensive backtesting and identified a pattern which provides an edge over a larger sample of trades, should NOT be using any discretion to actively

manage their trades. Their edge is based on the fact that historical performance shows a positive expectancy, so trade management should be conducted EXACTLY as in the testing. This will either be holding until the stop or target is hit, or will be in accordance with some fixed rules for stop movement.

If that works for you, great! Stick with it. It doesn't work for me.

Systems traders generally see this game as one of probability. Although probability is a feature of the game, my beliefs are somewhat different, and this difference means I'm (psychologically) a discretionary trader and therefore unable to trade this systems approach.

Systems testing is done over a very large sample, and while there are great methods of ensuring reliability of data through back and forward testing of different samples from different market environments, it's still a large sample; and within that large sample you'll find considerable variability - periods of underperformance and periods of outperformance. Systems traders need to persevere through the drawdown that comes from the periods of underperformance. Any one system may extend its period of drawdown for quite a while, maybe a whole week, maybe a month, maybe longer. And this could be quite normal - within the expected variability of results.

There are several problems with this, for me.

Firstly, I don't trade over a large sample. As a short timeframe discretionary trader, I'm aiming to grind out a living day to day. I hate a weekly drawdown. And even more so I hate monthly drawdowns. Each day I'm trading in a small subset of the larger sample. Whether it's a period of outperformance or a period of underperformance is unknown, until the market can be looked back at with the benefits of hindsight. My goal is to manage the day's opportunities as best I can at the time. If a better yearly result could statistically be obtained by sticking to the original stop or target, then that's just too bad for me. That doesn't help me today. So, I choose active management in order to get the best result I possibly can over a small sample. I'll leave the 'hoping' to achieve a longer-term statistical average result to those with more patience and deeper pockets.

Secondly, and perhaps more importantly, I just don't believe in the ability to apply a mathematical model to the markets. Yes, it does provide good approximations, but I'm just not happy staking my money on approximations. While systems traders believe in a probabilistic market, my belief is better described as an 'uncertain' market or an 'emotional' market. A subtle difference, perhaps! Yes there are probabilities, but the probabilities themselves shift.

To blindly trade systems or patterns and to hold till the preplanned stop or target, is to place your faith in the fact that the future market will be similar enough to the past markets in order for the edge to still be intact. Trade management is a matter of 'hope', based on trust in the power of the setups or patterns.

Market movement though is a function of orderflow imbalance, and this orderflow imbalance is the result of traders' decisions and actions. While future orderflow can be somewhat influenced by the setups or patterns, this systems method is limited in its ability to take into account the context of the market in which the pattern is occurring, or the psychology of the current market. Both are factors which will also have a great influence on future orderflow.

So, 'hope' doesn't work for me. Like in most areas of my life where I'm a bit of a control freak, my beliefs as to the nature of the market require me to actively manage my trades.

My entries are not based on any belief in the power of the setups, but rather on my assessment of the underlying forces of supply and demand, the market context within which the current pattern is occurring, the potential future actions of other traders, and my assessment of high probability and low risk opportunities within that environment. This gives me a trade idea which is then executed.

This is a key difference – the real power behind my entry is not a pattern based entry trigger, but rather a discretionary entry based on my read of the market and my 'feel' for the price movement. Therefore, my edge does not exist in just blindly holding till the stop or target. My edge exists only while my original trade premise is valid.

If I therefore enter a trade, and the trade does not act in accordance with my original idea, the edge is gone (or at least its likelihood is reduced). So, it's time for me to work the best exit possible and then reassess and/or wait for the next opportunity.

This is not blindly just moving the stop or target out of fear. It's a realisation that my original assessment of the future net orderflow is either no longer valid, or was perhaps even entirely wrong.

End result... I accept that sometimes I would have achieved better results by simply holding till either the stop or target. However, other times my active management approach will yield better results, because for example I'll recognise stronger than expected orderflow and be able to extend the target. Maybe it works out even over the next year or so, maybe not. It doesn't worry me either way. I don't actively manage my trades because it's optimised for better results. I do so because it's the optimal trade management approach for both my market beliefs and for my psychological needs.

Why hold a trade that moves to one tick from your target and then drives all the way back to your stop, just because taking it earlier would 'destroy' your edge? I just don't get that. If you assess the market environment has changed, and bearish pressure is reducing the likelihood of the price pushing that one tick further, take profits.

As with everything in trading though, there's no black and white. If the systems approach works for you, stick with it.

(end of email excerpt)

If you feel a passive style suits you better, then work out a way to make it profitable. It doesn't work for me. That doesn't mean it won't work for you.

Thorough testing will be required.

However, if an active management approach is suited to your personality, the following outlines how I do it...

General Trade Management Concepts

- I trade with two part positions.
- The entry is all-in. That is, both parts are placed on at once.
- The exit is scaled out. Part one aims for a target at T1. Part two aims for either a T2 target, or continues until exited by a trailing stop, depending on market environment.
- All positions are managed via an active trade management approach.

Active Trade Management Principles

Remain in the Trade While the Premise Remains Valid

The idea behind active trade management is that you remain in the trade while your trade premise remains valid.

Exit (prior to achieving a target) is only to occur as a result of one of the following three scenarios:

- 1) Your bar by bar analysis shows evidence of a sentiment change which invalidates your trade premise; or
- 2) The market has failed to move in your required direction after a reasonable amount of time has passed, raising doubt as to the validity of your premise; or
- 3) You're unsure about the current state of the market and future trend direction.

If none of these situations has occurred, hold the trade.

If (1) has occurred, work an exit and move on to the next trade opportunity.

If (2) or (3) have occurred, work an exit and reassess.

Note that (1) and (2) are different. In scenario (1), the price action invalidates your premise. In scenario (2) it fails to validate it. Scenario (2) does not mean that it won't work. Just that it's taking longer than it should so the odds of success have been reduced. It's best to get out and reassess.

Active trade management requires a constant bar by bar reassessment of short-term sentiment and the likely path of future price action.

Keep your awareness ahead of price. What will you do if price goes up from here? What will you do if price goes down from here? What will you do if price stalls? Pre-consider all scenarios, so that you are prepared for whatever eventuates.

Continue ongoing analysis to confirm price movement matches the behavior previously anticipated. If price action differs from expectations, adjust the management or exit plan as required.

Appropriate Timeframe

The real challenge you will face though is which timeframe chart to use for your bar-by-bar analysis.

If you conduct all your ongoing sentiment analysis on the *lower timeframe* (1 min) chart, you will be whipped in and out of the trade. I can offer no rules here, apart from my focus is initially on the *lower timeframe* (1 min) chart while at or around the initial entry zone, transitioning to the *trading timeframe* (3 min) chart as soon as I'm comfortable that it will define further price action.

You'll probably find that the sooner you make this transition, the more comfortable you'll be.

If you find that you're scratching trades too soon, replay these trades after the session (use a replay feature if available, otherwise step through the chart bar-by-bar) in order to practice earlier transition to the *trading timeframe* (3 min).

Largely, it's a matter of trust, which will come through more exposure to setups and trade management. Practice, practice, practice!

Here's one hint though – if part one has achieved its target, and you have not yet transitioned to the *trading timeframe* (3 min), do so now for management of part two. While this obviously won't always provide the best outcome, it's generally good advice, helping to provide a little more wriggle-room for part two and preventing over-zealous management.

From Entry to Part One Exit

Psychologically Managing Drawdown

There is nothing more draining psychologically than seeing an entry almost immediately move to drawdown.

Here's something to consider though – do you really expect that you should be able to pick the optimal entry point every time?

In the section on entries we established that it was not possible to know the best point of entry, except with the benefit of hindsight, once the trade had come and gone. We identify zones in which we're happy to trade, and then work the best entry we can within that area.

Is it therefore not reasonable to expect that a good proportion of your trades will move to a worse price after entry? Absolutely!

Of course, that doesn't make it easy to accept when you're in a losing trade.

The best way to psychologically manage these situations is to expect them. In our analysis, we considered the nature of future price action – how should price look and behave if our premise is correct; and how should price look and behave if our analysis is wrong?

Use the same process here. On entry, consider the following... Assuming your trade entry is early and price will enter drawdown to retest the highs/lows, how should it look and behave if our trade idea is actually valid and our stop will hold? How should it look and behave if it is likely to take out our stop?

Pre-considering the nature of future price action prepares you for the worst case scenario, and helps you to hold during drawdown if price action is such that it still supports your trade premise.

Psychology of Trade Management

One of the greatest challenges I face is a tendency to over-manage my positions, especially around the entry zone.

Typically in hindsight (post-trade review) I find that more patience should have been applied.

I find a simple tool for improving my performance, is a set of action statements that I repeat during this phase of trade management.

- Patience
- Trust (myself and my strategy)
- Where's the strength?
- Where's the weakness?
- Hold while the premise remains valid

This provides a simple reminder for patience in my decisions and actions, and has me focusing on the important information – assessing changes in strength and weakness – rather than worrying about potential trade loss.

We'll talk more about this concept in Volume Four. I raise it now simply because, in my experience, the early stages of trade management provide some of the greatest challenges for many traders. You may wish to incorporate a similar concept.

Working an Exit - Scratching a Trade

I refer to the process of working an exit prior to T1 as scratching the trade.

Why do we scratch a trade?

We said earlier, exit (prior to achieving a target) is only to occur as a result of one of the following three scenarios:

- 1) Your bar by bar analysis shows evidence of a sentiment change which invalidates your trade premise; or
- 2) The market has failed to move in your required direction after a reasonable amount of time has passed, raising doubt as to the validity of your premise; or
- 3) You're unsure about the current state of the market and future trend direction.

So, we're exiting because either the trade premise is now believed to have changed, or is in doubt.

The real benefit of exiting is that it allows you to reassess the situation with the objectivity that comes from having no open position. Analysis while in a live trade can become clouded by emotions, in particular through fear of loss. Exiting removes you from that negative influence, allowing clear and objective analysis.

You have two options to choose from, depending on the urgency with which you need to exit:

- 1) Hit the CLOSE POSITION button to immediately close out any open position.
- 2) Make this an active process in which we try to gain a better exit price through movement of the stop loss and/or target orders.

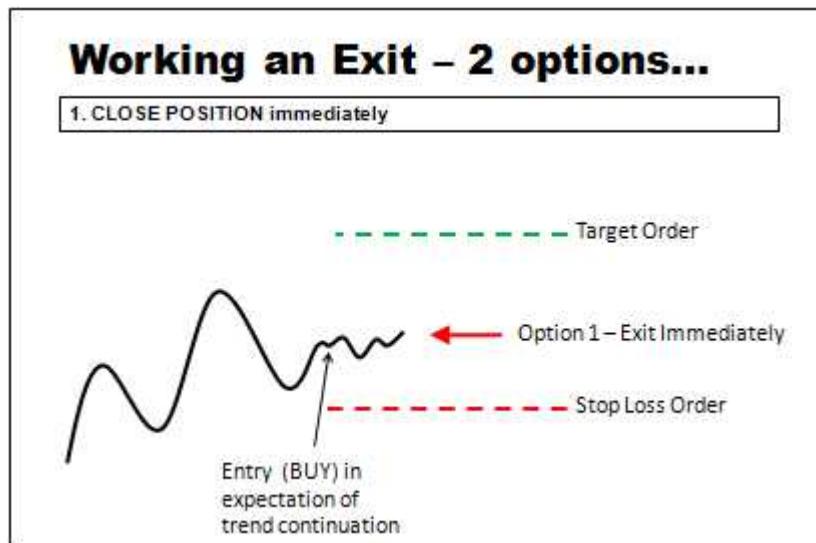


Figure 4.73 - Working an Exit – Option 1

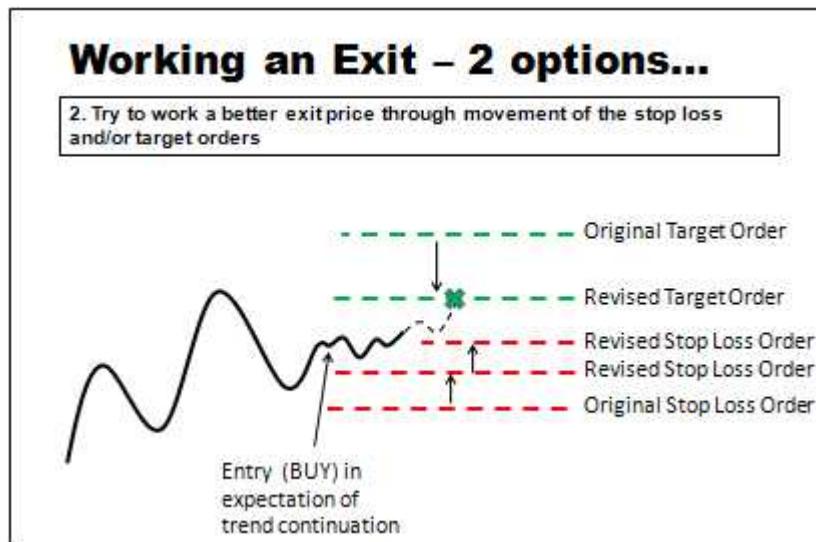


Figure 4.74 - Working an Exit – Option 2

The first option, immediately closing the position, is obviously used for the most urgent exits when the trade premise is strongly threatened and you want out immediately.

The second option is more discretionary. You're not immediately threatened, but you're ongoing assessment of market sentiment has you doubting the ability of price to reach the target area. In this case I'll use a combination of moving the stop order and/or moving the target order. The exact same principles apply – move the target to new areas which will provide limits to price movement – and move the stop to new areas where you'd like to be out if it's hit. Reference to the *lower timeframe* (1 min) chart will provide these locations.

How do we handle multiple parts?

If the premise is proven invalid and I want out, I'll scratch the whole trade immediately.

However if I'm working my exit orders then I'll usually manage both parts one and two separately. My intent will be to give part two more room, and more opportunity to prove itself.

So for example, let's say the trade is moving slowly in my direction but I now doubt its ability to break the next swing high. I'll tighten the target for part one to just prior to that swing high and aggressively trail the stop behind price, until exiting part one at the best price I can get. Part two however will have its target and stop orders remaining in their original location for now, in case my revised analysis is incorrect and price does subsequently break the swing high. Once part one is exited, I'll then reassess and manage part two.

Let's look at an example...

Figure 4.75 shows the sideways market in the leadup to the Aug 6th 2010 NFP release. With 17 minutes till the news release a BOF was entered long in anticipation of a test of the range highs.

The entry was on the close of candle A. The stop was placed below the BOF lows. The target was placed inside the upper range highs, both T1 and T2 located together due to the sideways trend action.



Figure 4.75 - Working an Exit Following a Change of Premise

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Candle B was a concern intra-candle, but the close was strong (high close range candle). The stop was tightened below this candle, as a second push lower would indicate stronger supply than anticipated at a lower level.

Following candle C (low close bear candle), I no longer had expectations of price reaching the original target and it was time to work an exit (I needed to be out prior to the NFP release in 6 more minutes, in any case). The target was tightened to just below the recent highs.

Following the bearish strength of candle D (low close bear candle, initially teasing higher then trapping longs as it moved to new lows), the target was again tightened to inside the highs of D. The part one stop was moved for a breakeven exit (not shown) which occurred on the start of the next candle. The part two stop was held below the candle B position, then moved below D as candle E rallied. Candle E subsequently achieved the revised target, exiting the trade for part one breakeven and part two providing +5 pips.

Not enough to retire, but sometimes we just have to be happy with whatever the market provides.

Re-entry

Re-entry may be considered if you have scratched a previous trade for an objective reassessment of sentiment and market analysis, and decided that entry is again desirable.

However it's also an option at the following two times:

- 1) You have taken profits on part one (with part two remaining live) and the market has provided an opportunity to re-enter a new part one.
- 2) You were stopped out, and the market has again set up for another entry.

You should however ONLY reenter on a valid trigger. Price action should be such that this would be a valid entry if it was the first entry in this entry zone.

The number of entries per setup area is unlimited. You can scratch and re-enter as many times as you wish (provided the market offers valid entry triggers each time). However, I allow no more than two max-size losses per setup area.

If I have been stopped out twice for a full loss, or a greater number of losses adding up to an equivalent dollar or point loss, then my read of the market is obviously out of sync with reality.

Step back and let this one pass. Move on to the next opportunity.

Let's look at an example demonstrating a trade scratch and reentry.

Figure 4.76 below shows a BPB. We've seen this one before in the Entries section.

The first entry is on the break below candle A at point E1.



Figure 4.76 - BPB Setup – Re-entry

A BPB trade should provide reasonably quick movement to its target. However, recognising potential for some support to oppose my trade at the blue outlined area, I will be on alert for any signs of bullish strength coming off this support area. Candle B puts me on alert. The stop is moved to just above B to scratch the trade (both parts one and two) and allow reassessment. The following candle is reassuring, showing a pause in the upswing. Candle C breaks above B and scratches the trade out for a 2 pip loss.

Re-entry is taken on the break below candle C at point E2, before the market moves in the anticipated direction.

Had we just held, the move up to C would not have stopped out our position, but the precautionary exit allowed us the following advantages:

- 1) The ability to objectively re-analyse the market price action, without any negative emotional influence that comes with an open trade; and
- 2) A very minimal risk compared with that which would have occurred had the trade premise been wrong and the market stopped us out.

This is active management – making decisions to minimise risk and maximise opportunity.

Movement of the Stop Loss to Breakeven and Beyond

Movement of the stop loss to breakeven provides you with a free trade. There is no longer any loss potential (barring slippage on exit). However, if you do this too soon you will likely also have very limited profit potential, due to ensuring you get stopped out by normal market fluctuations.

When do we move the stop to breakeven?

The initial stop was placed in a position that invalidated the original trade premise. The same concept is used for stop loss movement.

As price moves in our favor, we move the stop to breakeven when we would no longer wish to be in the trade if price retraced to the entry point.

Note that part one and two can be managed differently. You may wish to be more aggressive with part one, moving its stop to breakeven while part two is given more room to prove itself.

The same concept again applies for any movement beyond breakeven.

As price moves further in our favor, we move the stop to new levels where we would no longer wish to be in the trade if price retraced to that point.

Key locations for movement of the stop would be beyond any new swing highs or lows, or beyond any large candles that reach new highs/lows (large high close bull candle in an uptrend, or low close bear candles in a downtrend).

Let's look at an example and consider the management of the stop for part one of our position.



Figure 4.77 - Movement of Part One Stop Order

In the example above we see a PB setup within an uptrend.

Entry is on the break of the hammer which settled nicely on the previous swing high support. Entry price is 1.5309. Stops for both part one and two are below the hammer at 1.5301 (S1). Target T1 is at 1.5330, based upon price action to the left (not shown).

After the initial bullish surge and retracement of candle A I would move the stop for part one to breakeven (S2). While the bullish strength was welcome, the immediate pullback was not. Further retracement may indicate I was too early. The part two stop would remain in its current location.

The following range candles are reassuring though, and as candle B moves to new highs I'd move S1 to below the recent low close range candle (S3) (the last push down before new highs).

Further tightening of the stop to below candle C (S4) would occur as we approached T1, not for any technical reason, but simply to ensure acceptable R:R.

Active trade management requires a constant reassessment of the reward:risk ratio. How much are you risking if the trade should stop you out vs. how much more potential reward is there available to your profit target.

In the above example, as price approached the target at the end of candle C it only offered another 4 pips of potential reward, compared with 16 pips of risk to the stop. This R:R doesn't make sense, so I've tightened the stop below the last bull candle.

This type of tightening the stop does increase the risk of premature exit, so needs to be considered carefully. The market in this case was showing great strength to the upside and I did expect continuation to the target. Had it stopped me out I would have been searching for the next PB re-entry.

In these R:R situations, you may also consider just taking profits.

For example, if price stalls a couple of pips from your target for a minute or so, is it worth holding on to try for that extra 2 pips, while risking 20 pips on drawdown to your stop? Even if your stop is nicely placed below an intervening area of support, it doesn't make sense from an R:R perspective.

If price stalls there, take profits.

Consider targets to be a zone, rather than an exact price.

Erroneous Entry

You will from time to time find yourself having made an entry in which you suffer immediate feelings of unease. Quite likely your entry decision was influenced by emotion rather than proper analysis.

You may also from time to time find yourself in an inadvertent entry, if using a one-click entry method.

Common advice is to just exit immediately. I would offer a different suggestion though. Pause for a second and consider – can you salvage something out of this trade?

It wasn't the best planned entry, but that doesn't mean you're immediately in a dangerous position. Review the price action; identify signs of *lower timeframe* (1 min) strength and weakness and assess the likelihood of price moving in a profitable direction, even if just a short distance. If there is some potential, then manage the position; but manage it very aggressively. Anything you can gain out of this will be a bonus. If there is no potential though, work a rapid exit.

Managing Part Two

Movement of the Stop Loss Beyond Breakeven

The principles for movement of the stop for part two are exactly the same as for part one, except that more room is typically applied. More opportunity is given for this part to prove itself.

As price moves in our favor, we move the stop to breakeven when we would no longer wish to be in part two if price retraced to the entry point.

As price moves further in our favor, we move the stop to new levels where we would no longer wish to be in part two if price retraced to that point.

Key locations for movement of the stop would again be beyond any new swing highs or lows, or beyond any large candles that reach new highs/lows (large high close bull candle in an uptrend, or low close bear candles in a downtrend). This time though, we will be primarily referencing the *trading timeframe* (3 min) rather than the *lower timeframe* (1 min) chart.

At all times we aim to remain in the trade while the premise is still valid.

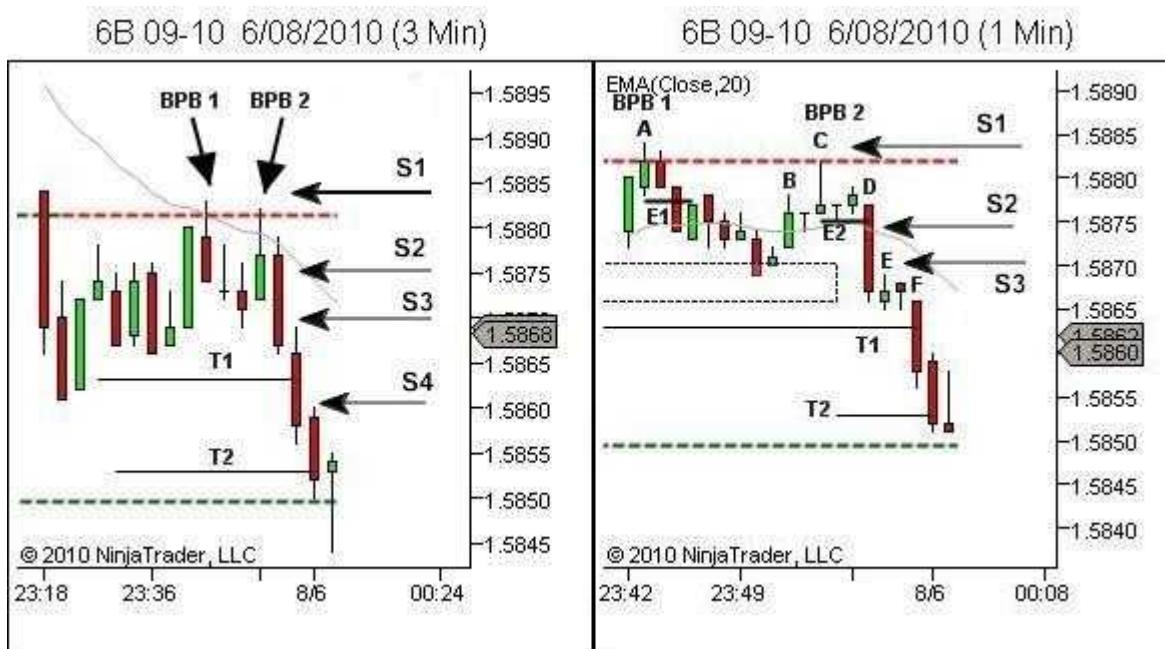


Figure 4.78 - Trade Management - Movement of Stop Loss

In figure 4.78 above we revisit the BPB setup that was used to discuss re-entry (previously figure 4.76). We'll look at the second entry, BPB 2, entering via the trigger E2 on the break below the shooting star candle (RHS), discussing management of both parts one and two.

To stick with the earlier convention, the *trading timeframe* (3 min) chart is on the left and the *lower timeframe* (1 min) chart is on the right. However, as our trade management starts with the *lower timeframe* (1 min) we'll need to start over on the RHS.

Using an all-in, scale-out approach, the initial trade parameters were as follows:

- Both part one and two entered at E2, 1.5875
- Stop loss for both parts at S1, 1.5884 (-9)
- T1 at 1.5863 (+12)
- T2 at 1.5853 (+22)

On the close of candle D (low close bear candle breaking to new lows), the stop for part one would be moved to breakeven at S2. Being a re-entry into this setup I will NOT tolerate a second failure at the blue boxed area. The stop for part two remains at its original location, S1, allowing it greater room for now, although will likely be tightened up as well if price action rallies.

Candle E (mid close range candle) shows expected support although support should fail quickly if the premise is valid. No change to the stops.

Candle F (low close bear candle) reaches T1. Part one takes profits. Part two stop loss is moved to breakeven at S2. From here, my focus moves to the *trading timeframe* (3 min) chart.

The initial low close bear candle from the trade open shows great support for our premise, expecting continuation to T2. The presence of subsequent low close bear candles makes trade management very easy. With such strong bearish sentiment shown within each candle, I should not expect to see it retraced. The stop for part two simply trails above these *trading timeframe* (3 min) candles, at position S3 on the close of its candle, and position S4 as price started approaching T2.

The stops were never threatened with T2 being achieved easily.

Working an Exit - Tightening of the Stop and Target

The principles for working an exit of part two are exactly the same as for part one.

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Should weakening of the price movement place your premise in doubt, use a combination of tightening of either the stop and/or the target to work the best price you can under the circumstances.

Adapting for the Market Environment

Consider adjusting your plan for T2 based upon your read of the current market environment. Is it trending or ranging? Is it a volatile market, or smooth with shallow price swings?

For example, in a trending environment you should be more willing to allow part two to run. In a ranging environment, allowing part two to run is a low odds scenario. The higher probability is for a reversal, so stick to your T2 target, or even have both targets at the T1 price. Whatever you feel is necessary for that price action!

Consider also the impact of any key market structure features.

For example, if your current trade entry appears to have got you in near a potential high or low of the day, then hold for longer, especially in a trending environment. Provide the trade with more room. Be willing to take it all the way back to breakeven if necessary (within reason of course).

Adjust and adapt your plan, to fit the state of the current market.

Extension of the Target

Similarly, be ready to adjust during the trade.

If your original plan was to take profits at T2, but the market sentiment and your bias for future trend direction now show the market strengthening in the direction of your trade, with a good likelihood of breakout and continuation, then consider allowing price to move past T2. Reassess your bias beyond this point. If price does continue then trail a stop. If it doesn't, this may cost you money, but the increased gains when right usually make it a risk work taking.

We return to the example used for discussion of part one management (figure 4.77), which is reproduced below as figure 4.79.

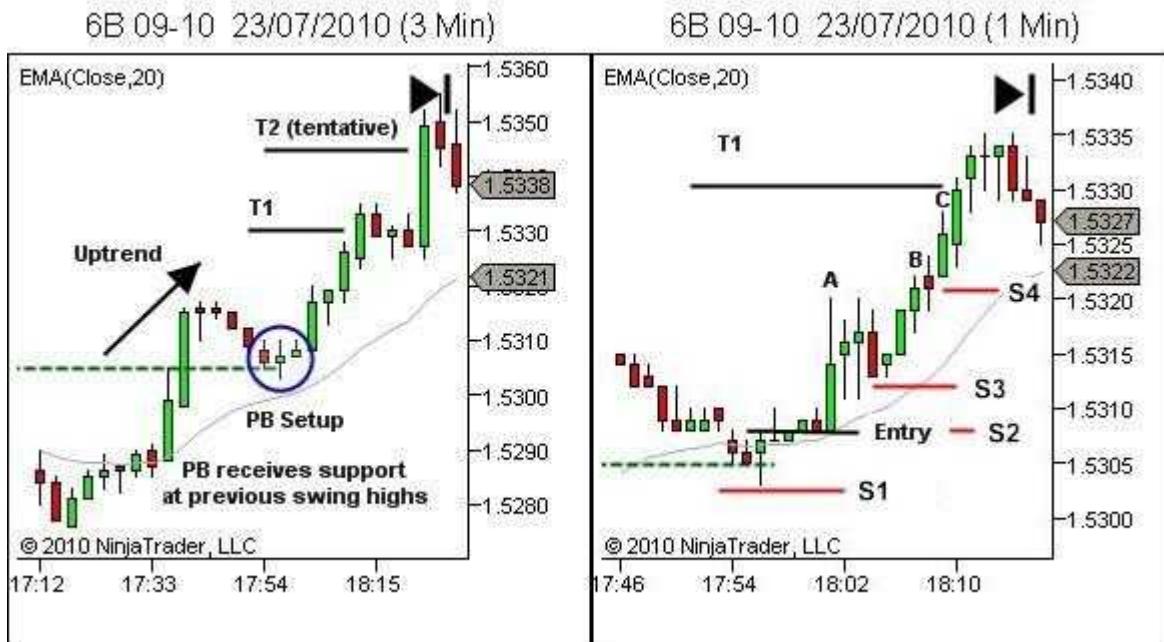


Figure 4.79 - Movement of Part One Stop Order (repeat)

When the part one stop was moved to its trailing position (S3) at 1.5312 (below the red low close range candle), I would have moved the part two stop to breakeven (S2). If this second push higher were to fail, I'd be happy to get out of the trade.

It would then remain at breakeven until T1 was hit.

My focus would then be moved to the *trading timeframe* (3 min) chart, if not already there.

The *trading timeframe* (3 min) is displayed below as figure 4.80.

You'll note that the second part target, T2, was initially placed at 1.5345 based upon the next *higher timeframe* (30 min) resistance.

My analysis though identified good strength in the bullish direction and weakness in the bearish direction. My expectation was for this trend to continue.

The T2 target was removed (accepting risk of loss if I was wrong) with the exit now being defined by a stop trailing behind significant price action (swing lows and large bull candles).

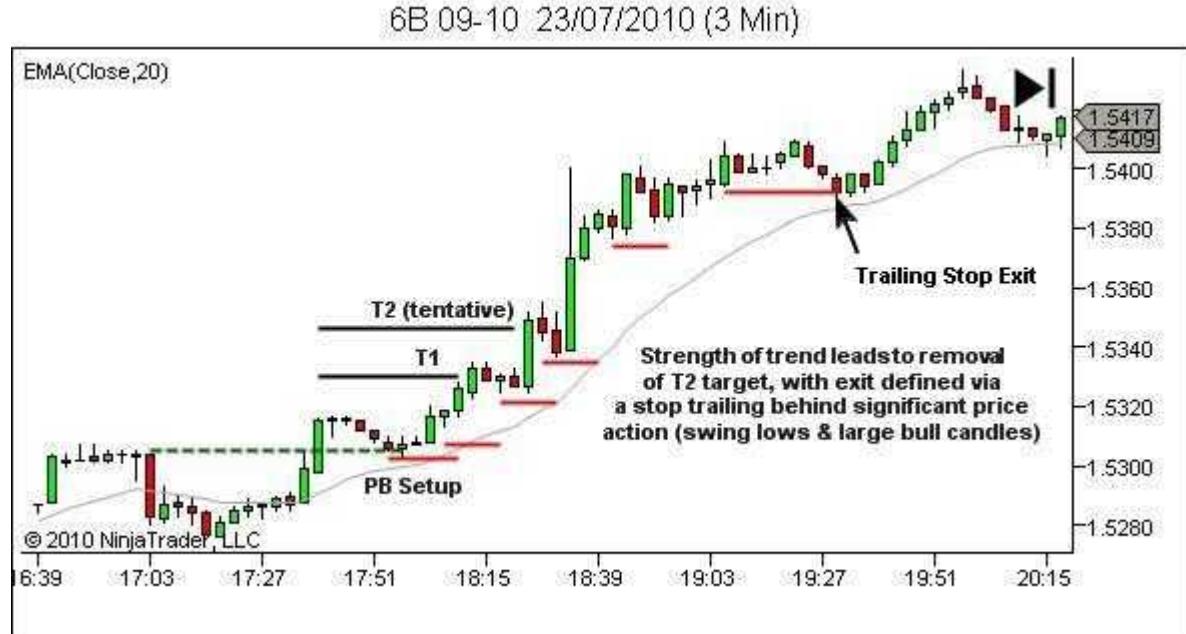


Figure 4.80 - Movement of Part Two Stop Order

The red stop lines demonstrate the movement of the part two stop order, behind significant price action.

On exit, our trade totals were:

- Part one: +21 pips
- Part two: +83 pips

4.5 – The Trading Process

Let's combine the above material into one summary diagram and process checklist. The checklist will later become a part of our Procedures Manual.

4.5.1 – Trading Process Diagram



Figure 4.81 - Trading Process

The trading process involves four steps, as per figure 4.81 above.

The following checklist will guide you through the actions required for each step.

4.5.2 Trading Process Checklist

Step 1 – Trade Preparation

Prepare for possible trade opportunity as price enters the vicinity of a setup area.

Actions:

- Monitor price movement confirming it matches the behaviour previously anticipated. If price action differs from expectations, return to the initial analysis and recheck premise and assumptions.
- Identify trade parameters
 - Stop loss location
 - Targets T1 & T2
 - Confirm entry zone
 - Consider both LWP (if identified) and LRP
- Identify preferred entry plan
 - Stop and/or limit order
- Final confirmation
 - The setup and trade is valid for this market environment
 - Price action is supporting the trade premise.

Step 2 – Trade Entry

Manage the entry into the trade, achieving the best possible price within the entry zone.

Actions:

- Monitor price movement bar by bar, until the entry locations are identified. Ensure price continues to support the trade premise.
 - Determine candle pattern sentiment
 - Consider the context
 - Does it support my premise
- If bracketing price, place a stop entry order at the LWP as soon as it's identified.

- If working an entry, place an appropriate order in the market as soon as the entry decision is made.
 - Limit entry order in area of stall
 - Limit or Stop entry order on price action trigger.
- Confirm pending order details are correct.
 - Entry price, direction, size,
 - Contingent stop and target orders
- On fill:
 - Cancel other no longer required pending orders.
 - Confirm full or partial position filled
- Post-fill confirmation (gross error check)
 - How do I feel about the entry?
 - Confirm the setup and trade are valid for this market environment
 - Confirm the price action is supporting the trade premise.

Step 3 – Trade Management & Exit

Manage an open trade in order to minimise risk and maximise opportunity. The trade should remain live while the premise remains valid.

Actions:

- Continue monitoring price movement bar by bar. Ensure price continues to support the trade premise.
 - Determine candle pattern sentiment
 - Consider the context
 - Does it support my premise
- Part One
 - While premise remains valid:
 - Move the stop to breakeven when we would no longer wish to be in the trade if price retraced to the entry point.
 - Move the stop to new levels where we would no longer wish to be in the trade if price retraced to that point.
 - When premise is threatened
 - Cancel position if immediate exit is required.
 - Else work an exit through tightening both the stop and target orders, based upon lower timeframe price action.

- Part Two
 - While premise remains valid:
 - Move the stop to breakeven when we would no longer wish to be in part two if price retraced to the entry point.
 - Move the stop to new levels where we would no longer wish to be in part two if price retraced to that point.
 - When premise is threatened
 - Cancel position if immediate exit is required.
 - Else work an exit through tightening both the stop and target orders, based upon lower timeframe price action.
 - When market shows increased strength
 - Consider extension of T2 or replacement with a trailing stop.
- On partial exit
 - Confirm order correctly filled.
- On total exit
 - Confirm flat.

Step 4 – Post-Trade

Conduct post-trade administration and recovery.

Actions:

- Reconfigure order entry screens or DOM.
- In the event of a loss:
 - Consider the need for a recovery process.
- Is price setting up for a possible re-entry or subsequent setup?
 - Delay any trade log entries and prepare for the new trading process.
- When time permits:
 - Update trade log.
 - Monitor and record significant observations:
 - Market structure or price action.
 - My trading process.
 - My physical and psychological state.

(Some of the post-trade actions are new... and will be covered in more detail in later chapters)

4.6 - Practice

The analysis chapter provided direction regarding the practice of both initial and ongoing market analysis, after explaining the theory behind the concept.

This chapter on strategy will differ. As much as I'm sure you would love to get to charts, I ask that you don't at this stage.

Chapter 5 provides ten complete trade examples, from analysis to exit. I'd like you to work through those first.

And then in Volume Five we'll talk about the process of becoming a trader, part of which will be development of a plan for the practice of the strategy.

4.7 - Conclusion

Our market analysis process had us identifying strength and weakness in the market in order to determine the likely *future trend* direction; the path of least resistance for future price action.

Our trading strategy makes use of the same principles.

Trade setups are based around the concept of trading in the direction of strength and against the direction of weakness, in areas where price interacts with support and resistance (higher timeframe S/R, range S/R or swing H/L) or where price pulls back against a trend.

The traders entering in these areas, in the direction of weakness, are taking very low probability trades. Price reversal will trap them in a losing position, forcing their exit as price again resumes its movement in the direction of strength.

We aim to profit from the exit orderflow of these losers.

We recognise that the perfect entry method cannot be known until the trade is over, so we identify an entry zone which satisfies our criteria (wholesale entry and acceptable R:R ratio) and then work the best entry possible within that area.

Exit targets are based upon price action and the market environment, targeting areas where orderflow is expected to oppose our trade, or running with a trailing stop whenever a trending market allows this possibility.

Like in our analysis phase, price action is monitored bar by bar, in order to maintain focus and situational awareness, remaining aware of the shifting forces of supply and demand, ready to identify any threat to our trade.

The trade should remain open while our trade premise remains valid. If threatened, we will work an exit of our trade and reassess for further opportunity.

Ok, now some of you might be thinking, I've just read through that massive number of pages just to be told to buy pullbacks in an uptrend, sell pullbacks in a downtrend, buy tests of support, and sell tests of resistance.

That's right. That's all it is. Of course, if you're asking that then you haven't really got the concept yet and I'd suggest you repeat all the material. The trading plan, at a conceptual level, is very simple. It's the deeper understanding of why it works, that allows you to trade the setups. And it's the experience and intuition that develops from deliberate practice (coming soon in Volume Five) which allows you to gain experience in dealing with all the different nuances and variations of each setup; and in gaining trust in yourself to be able to manage these nuances and variations without causing irreparable damage to either your financial or psychological capital.

If I had just said to trade a pullback in a trend or a test of S/R (which could probably be done in 10-20 pages), you'd try it once or twice, get a loss or two, and dismiss the concept as yet another waste of money.

With the background material in Chapter 2 as to why this strategy works, and in fact why it's the underlying reality behind all successful trading approaches, you're now more likely to believe it. And in fact you'll probably find that you can't ever go back to your old indicator ways; you just won't believe them any more.

And with the analysis skills you learnt in Chapter 3, you're well placed to start to identify market sentiment and likely future trend direction, as well as modify that analysis as new information comes available, bar by bar at the right hand side of your screen.

It's all about identifying shifts in order flow. It's all about identifying shifts in sentiment. It's all about finding where some group of traders is wrong, and capitalising on the order flow caused by their exit. If you get that, then you've progressed far. And you'll understand the value in this strategy. Well done.

Chapter Five – Trade Examples

5.1 – Trade Example 1 – BPB – T1 & T2 Achieved

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 18 Aug 2010

Time: 18:33 on charts (09:33 London)

We start this example right at 18:33; three minutes after release of the MPC Meeting Minutes; an event with significant potential to move the market.

Step 1 – Define Structure



Figure 5.1 – Example 1 – Define Structure

Support is below the market at 1.5500. Resistance is above at 1.5645 and 1.5690.

Note the last green candle. This is only three minutes in duration, with a high of 1.5612 and a close of 1.5604. As expected, the release of the MPC Meeting Minutes has provided significant volatility, smashing price straight through a congested area of resistance at 1.5565, 1.5580 and 1.5600.

Step 2 - Define Trend



Figure 5.2 – Example 1 – Define Trend

Prior to news release, at 18:15, price broke through the upper level of a sideways trend that had developed between 1.5500 support and 1.5535 swing highs, forming an uptrend.

The news release has continued this uptrend, breaking through three levels of higher resistance.

Step 3 - Identify Strength & Weakness

Momentum analysis on figure 5.3 below shows clear signs of strength on the bullish price swings and weakness on the bearish price swings.

The *lower timeframe* (1 min) chart is helpful in this case in confirming that the single *trading timeframe* (3 min) post-news candle was not one straight bullish move.

Rather, it consisted of a mid-close bull candle, a mid-close range candle, and a high close bull candle (although still within the range of the first post-news candle).

While showing post-breakout strength, there are signs of supply coming into the market, possibly a result of profit taking in the vicinity of the 1.5600 resistance.



Figure 5.3 – Example 1 – Identify Strength and Weakness

Step 4 – Identify Future Trend Direction



Figure 5.4 – Example 1 – Identify Future Trend Direction

The Sixth Principle of *future trend* direction states:

If strength is shown on approach to an S/R barrier we expect a breakout and watch the behavior of price post-breakout for clues as to future direction:

- Weakness following the breakout – the expectation is for a breakout failure and reversal back through the area of S/R.
- Weakness on the pullback – the expectation is for a breakout pullback and continuation.

In this case, the bullish move has already broken through the resistance area. We're now looking for the direction post-breakout.

Given the strength of the post-news move, my expectation is for a breakout pullback and then continuation of the trend to the next higher resistance area at 1.5645.

I will monitor price closely for signs of weakness which may indicate a breakout failure. However it's unlikely to offer any great trade opportunity due to the three tightly grouped resistance areas (1.5565/80/5600) which would now be expected to offer potential support.

Step 5 – Visualise Future Price Action



Figure 5.5 – Example 1 – Visualise Future Price Action

In order to validate our premise (highest likelihood being a breakout pullback and trend continuation), price action will have to show a weaker pullback into support.

Potential support is available at any of the three previous areas of resistance.

Any signs of continued strength on the bearish side will invalidate the premise and demand a reassessment. Given the depth of potential support, any breakout failure will possibly set up for a period of sideways congestion (although it's all speculation at this stage).

Step 6 – Identify Areas of Trade Opportunity

Any weaker pullback into support will offer a potential BPB opportunity.



Figure 5.6 – Example 1 – Watching for BPB Opportunity

Ongoing Market Analysis

Step 1 – Determine Candle Pattern Sentiment

Step 2 – Consider the Context

Step 3 – Does it Support my Premise?

It's a little difficult to demonstrate an ongoing process through an ebook, without adding 2-3 charts per candle, and a significant amount of pages. As such, the following charts and description will attempt to provide a summary of thoughts, as price progresses through the next six *trading timeframe* (3 min) candles and we repeat all three steps of the ongoing analysis process.



Figure 5.7 – Example 1 – Ongoing Market Analysis Process

Candle A is a high close bull candle, but it demonstrates both bullish and bearish pressure within the candle, as evidenced by the lower and upper tails. Its inability to project far above the previous candle shows an initial weakening of the post-breakout action.

Candle B and C (both low close range candles) confirm the breakout has stalled. This is supporting our premise so far – there’s been no great strength in the bearish direction – and we now watch for signs of weakness in a pullback.

Candles D and E are both low close bear candles, which imply bearishness. But the reducing range and inability to project far in the bearish direction show weakness. Putting this into context, we see weakness appearing in the post-breakout pullback, confirming our premise.

Candle F is a classic candlestick analysis doji (mid close range candle), once again showing continued weakness in the pullback and supporting our premise of a breakout pullback and trend continuation, and a potential BPB setup.

The right hand side of Figure 5.7 displays the *lower timeframe* (1 min) price action, even more clearly showing the extent of stall in the pullback.

Trading Process

Step 1 – Trade Preparation

Let's now prepare for a potential BPB setup and trade.

Note that the bar by bar ongoing market analysis process continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.



Figure 5.8 – Example 1 – Trade Preparation

The current stall in price offers a potential stop location (S1) at 1.5592, two pips below the pullback price action.

The last wholesale price (LWP) is identified at 1.5603, as shown on the above chart. This is the area, which if hit, would trigger the first of the pullback stops and accelerate price upwards.

T1 is identified at 1.5616, just inside the previous highs. This confirms that the LWP also gives us just over 1:1 R:R (13 pts reward to 11 pts risk), allowing the LWP to define the upper limit of our potential entry zone.

T2 is positioned just inside the next resistance area at 1.5643.

Step 2 - Trade Entry

Continuing to reference Figure 5.8 above, I would place a stop entry order at the LWP, 1.5603, ensuring that I don't miss an entry if price should surge upwards from its current level. The entry order would also have attached contingent orders for S1, T1 and T2.

I will now attempt to work a better entry than LWP.

In this case though, I will not simply place a limit order towards the lower part of the stall. Firstly, the recent stall action is only a couple of pips wide. And secondly, price could easily push lower for another swing down (producing a complex pullback down to maybe the 1.5580 or 1.5565 support areas).

Should it do so, this will necessarily involve a reassessment of both S1 and LWP.

So, we simply wait, for a better stall or a price action trigger.

Refer now to Figure 5.9 (below) for following price action.



Figure 5.9 – Example 1 – Entry

The left hand side of the above diagram shows us that the next *trading timeframe* (3 min) candle triggers our stop entry at LWP, 1.5603.

There was no opportunity to work any better entry. Had there not been a stop entry at this position, the 1 min candle (*lower timeframe*) would have triggered a pattern based entry based upon what could be called either a micro 3-swing retracement and/or an expansion bar off the MA.

Entry is at 1.5603.

Stops for both part one and two are at S1: 1.5592 (risk -11 pips)

Target T1 is at 1.5616 (reward 13 pips). Target T2 is at 1.5643 (reward 40 pips).

Step 3 – Trade Management & Exit

Figure 5.10 below demonstrates our management of part one of the position.

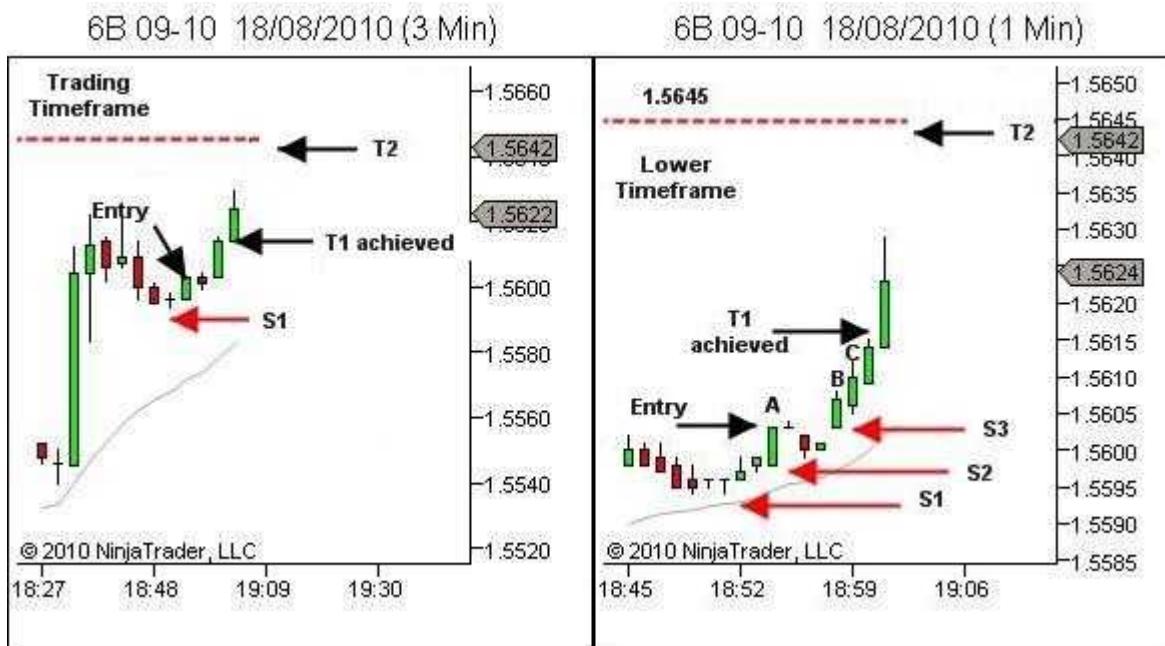


Figure 5.10 – Example 1 – Trade Management and Exit – Part One

Looking at the right hand side (*lower timeframe, 1 min*), we see candle A showing the entry candle which triggered right on the close. The stop was at S1.

Price then stalled for three minutes. While price action does not demonstrate any real bearish strength, this is an indication that I was too early in my assessment of when price would start triggering the stops of the pullback / reversal traders.

Candle B started the real move higher. The stop was moved to position S2, below the recent post-entry pullback. If there is to be a surge of stop-induced bullish orderflow, price should not get back to this area.

Candle C gets to within 3 pips of the target, T1. The stop, if not already done, would be moved to breakeven (S3), or if you like to 1.5604, below candle C, and providing one pip to cover the cost of commission.

Target T1 is easily achieved.

The left hand side of figure of 5.11 (below) demonstrates the management and exit of part two of our position.

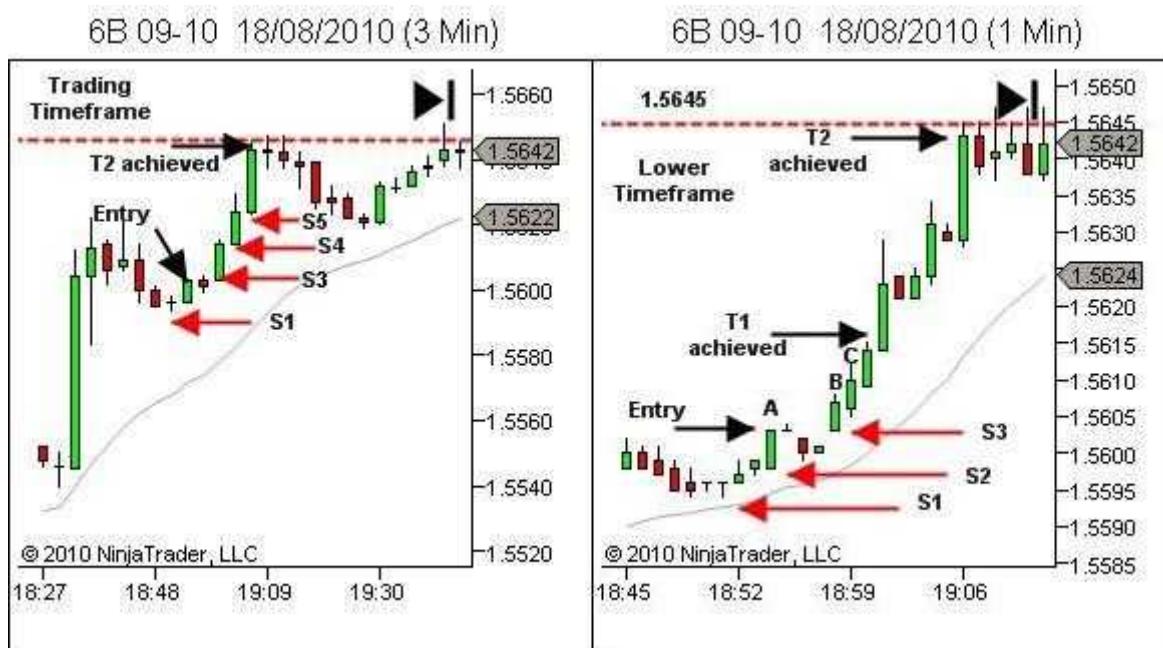


Figure 5.11 – Example 1 – Trade Management and Exit – Part Two

On achievement of target T1, the stop for part two is moved to breakeven (S3).

The left hand side demonstrates the *trading timeframe* (3 min), which is where the majority of our focus should remain.

The stop for part two in this case trails the *trading timeframe* (3 min) candles till achievement of T2, 1.5643, just prior to the next resistance area.

Step 4 – Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups as price now interacts with the next resistance level (watching for a possible TST setup, or a BOF/BPB if price continues with bullish strength and breaks through to higher prices).

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

- Part one: Achieved T1 +13 pips (less commission)
- Part two: Achieved T2 +40 pips (less commission)

5.2 – Trade Example 2 – PB – T1 Achieved – Part Two Worked Exit

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 23 Aug 2010

Time: 24/8/10 00:27 on charts (15:27 London)

Most days will not offer nice trending price action. This session was a Monday in which there were no economic news releases planned in both the UK and USA. We start the following example midway through the UK/US forex session overlap, where we see a largely choppy and directionless market so far. The remainder of a session such as this is not expected to offer much different.

Sometimes though, if we display patience we'll get clear signs of strength or weakness. Positioning ourselves to trade against the weakness will always offer higher probability trades.

Step 1 – Define Structure



Figure 5.12 - Example 2 – Define Structure

In this example we see higher resistance at 1.5575, 1.5595 and 1.5620. Note that the recent move up to the last swing high broke up through a previous resistance area at 1.5560 before failing and moving lower. 1.5560 is now invalidated.

Lower support exists at 1.5460, 1.5475 and 1.5520. Price is approaching the 1.5520 support area for the third time this day, the previous time having broken slightly through before failing (see the lower tail on the third-last candle).

Step 2 - Define Trend

The last candle has resulted in a change to a downtrend, as demonstrated in the *trading timeframe* (3 min) below.



Figure 5.13 - Example 2 – Define Trend

Step 3 - Identify Strength & Weakness

In the chart below we see earlier bullish strength in swings A and C, combined with bearish pullback weakness in B and D. Beautiful uptrend signals. However, swing E was unable to carry price any further. The breakout above the previous 1.5560 resistance (as demonstrated in step 1 above) was unable to attract sufficient buying to ensure continuation of the trend – not surprising on a quiet, news-free day.

Price then collapsed with swing F accelerating downwards as all the longs were stopped out of their positions and new shorts chased the market lower.

Momentum analysis shows weakness in the bullish direction (swing E) followed by accelerating strength in the bearish direction (swing F)



Figure 5.14 - Example 2 – Identify Strength and Weakness – 1 of 2

The *lower timeframe* (1 min) chart below shows beautiful signs of weakness appearing at the top reversal, with each extension unable to project to new highs, and each pullback extending to a depth of greater than 100%.

The chart also shows clear signs of strength in the subsequent move downwards.



Figure 5.15 - Example 2 – Identify Strength and Weakness – 2 of 2

Step 4 – Identify Future Trend Direction

The Sixth Principle of *future trend* direction states:

If strength is shown on approach to an S/R barrier we expect a breakout and watch the behavior of price post-breakout for clues as to future direction:

- Weakness following the breakout – the expectation is for a breakout failure and reversal back through the area of S/R.
- Weakness on the pullback – the expectation is for a breakout pullback and continuation.

Given the strength of the move downwards, my expectation is for a breakout of the support area. I'll then watch subsequent price action for signs of weakness which may indicate a breakout failure or a breakout pullback opportunity. My gut feel is for a BPB opportunity due to the increasing downwards momentum.



Figure 5.16 - Example 2 – Identify Future Trend Direction

In general though, an accelerating move can be difficult – sometimes indicating strength and likely continuation of the trend (usually following some form of complex correction), other times leading to a climactic reversal with a strong area of support established at the reversal point.

In any case, the higher probability setups are in the direction of strength and against weakness. Higher probability opportunity in this case would be with either a PB or BPB entry (both with trend). Lower probability would be a BOF reversal (counter-trend). A better counter-trend entry would occur if a low was established, then a pullback (and possible PB opportunity), then a weaker retest of the lows for a TST or BOF entry.

Step 5 – Visualise Future Price Action

Assuming a BPB opportunity, I'll be looking ideally for some strong extension below the support level, followed by a weaker pullback which fails in the vicinity of the support-turned-resistance area.

To invalidate the premise, extended weakness may indicate lack of new selling below the support area. This will look somewhat like the previous top reversal, involving 2-3 attempts to push lower which fail. In this case, I'll need to reassess and consider the possibility of a low being established.

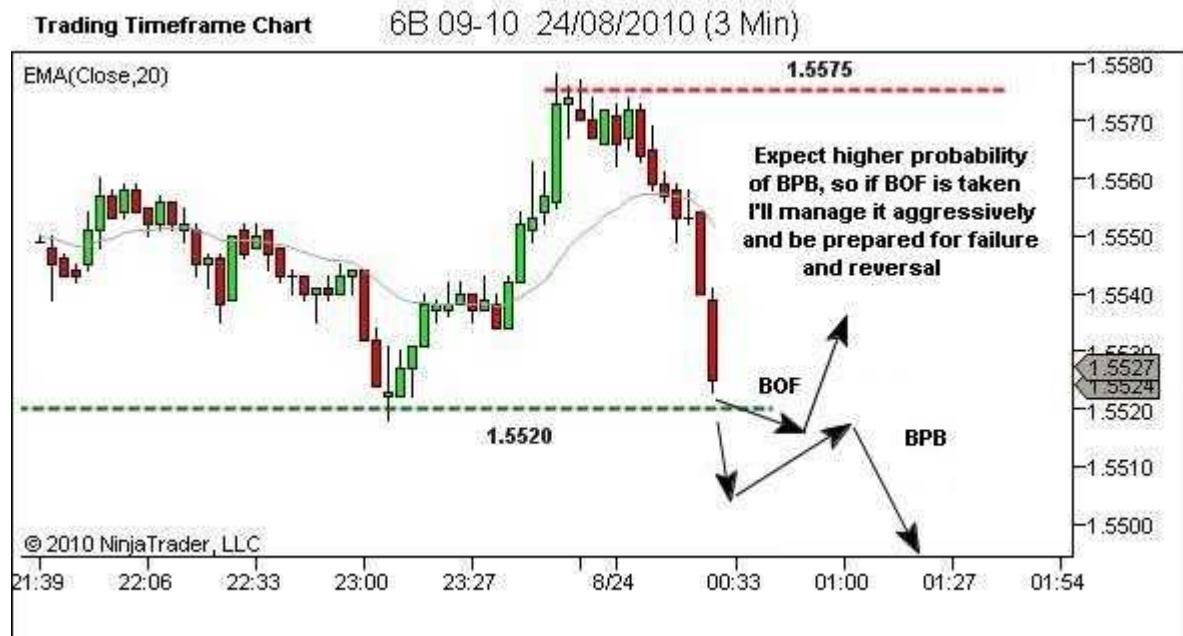


Figure 5.17 - Example 2 – Visualise Future Price Action

Step 6 - Identify Areas of Trade Opportunity

Our visualization of the future price action provides our possible setup areas (BOF and BPB); with BPB being the higher probability opportunity.

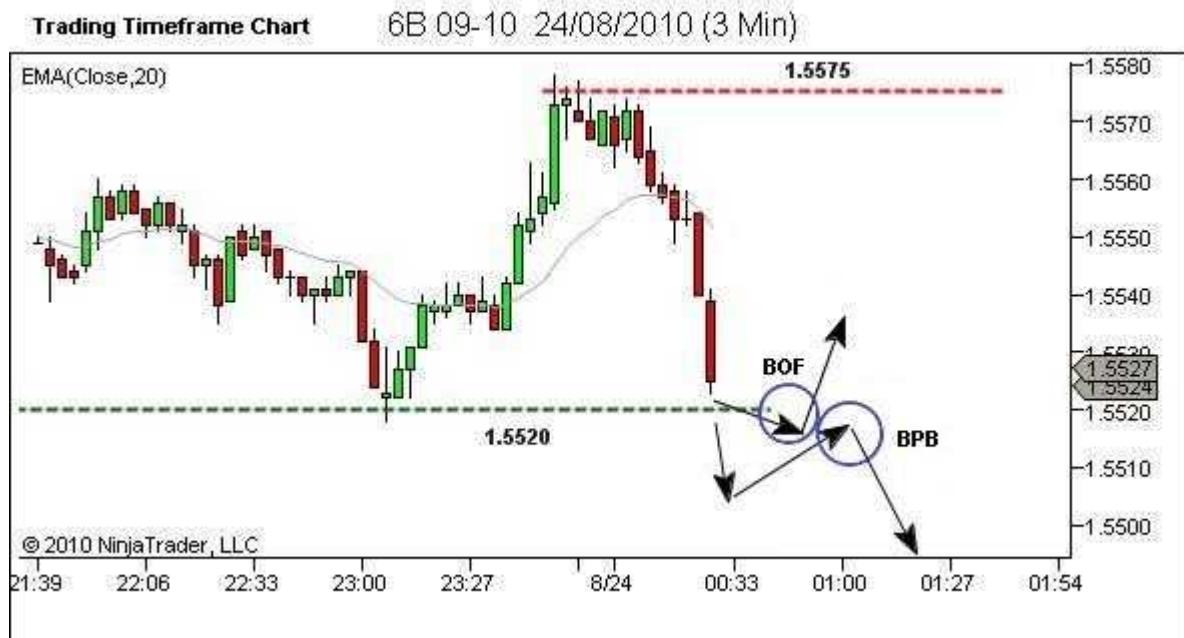


Figure 5.18 - Example 2 – Identify Areas of Trade Opportunity

Ongoing Market Analysis

Step 1 – Determine Candle Pattern Sentiment

Step 2 – Consider the Context

Step 3 – Does it Support my Premise?

Once again, in summary form...

Let's look at the following two *trading timeframe* (3 min) candles...



Figure 5.19 - Example 2 – Reassessment of Future Trend Direction

Candle A (low close range candle) followed by candle B (high close range candle) both show evidence of demand (bullish pressure) coming into the market right at the support area. I'm not interested in looking at a TST entry just yet, although may consider that if a second or third push to support both hold.

However, the next candle or two will be critical. Continuation lower will involve sticking with my original assessment of *future trend* direction, expecting a breakout below support. Continuation higher though will have me looking for a weaker pullback and a potential PB opportunity down towards support (in accordance with the First Principle).

First Principle - We expect an up or downtrend to continue in its current state until the next S/R barrier, unless displaying evidence of weakness within the trend.

The next candle shows continuation higher. We're now operating with a pullback premise, and searching for a PB opportunity short. Price action required to validate our new premise will be weakness on the pullback.

Candle C (mid close bull candle) displays an upper tail, evidence of selling coming into the market, which would be expected at or around the area of the black horizontal line.



Figure 5.20 - Example 2 – Ongoing Market Analysis Process

Trading Process

Step 1 – Trade Preparation

Note that bar by bar ongoing analysis continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.

Candle D (high close range candle) continues the pullback. Again we see the pullback weakening, this time through the smaller range, indicating difficulty in the bulls overcoming any bearish orderflow.

We tentatively identify a possibly stop location above this candle at 1.5548 (marked as S1). Of course, this will be adjusted higher if price continues higher.

And we tentatively identify T1 as 1.5523, just above the support level, and T2 as 1.5478, just above the next lower support level.



Figure 5.21 - Example 1 – Trade Preparation

Assuming a break below candle D will trigger the first of the stops from those trapped long in a low probability trade; we will assign a break below D as the LWP, 1.5538. This provides 10 pips risk and 15 pips potential reward, easily meeting our 1:1 requirement. A stop entry order is

placed at LWP, with S1, T1 and T2 attached as contingent orders. We now attempt to work a better entry.

Step 2 - Trade Entry

Entry occurred either on recognition of the *lower timeframe* (1 min) upthrust pattern, at 1.5540, or if not quick enough then on a stop entry at our LWP 1.5538.

When the *lower timeframe* (1 min) trigger is this close to the LWP stop entry order, be *very* careful you don't end up with two entries, for double your normal position size.

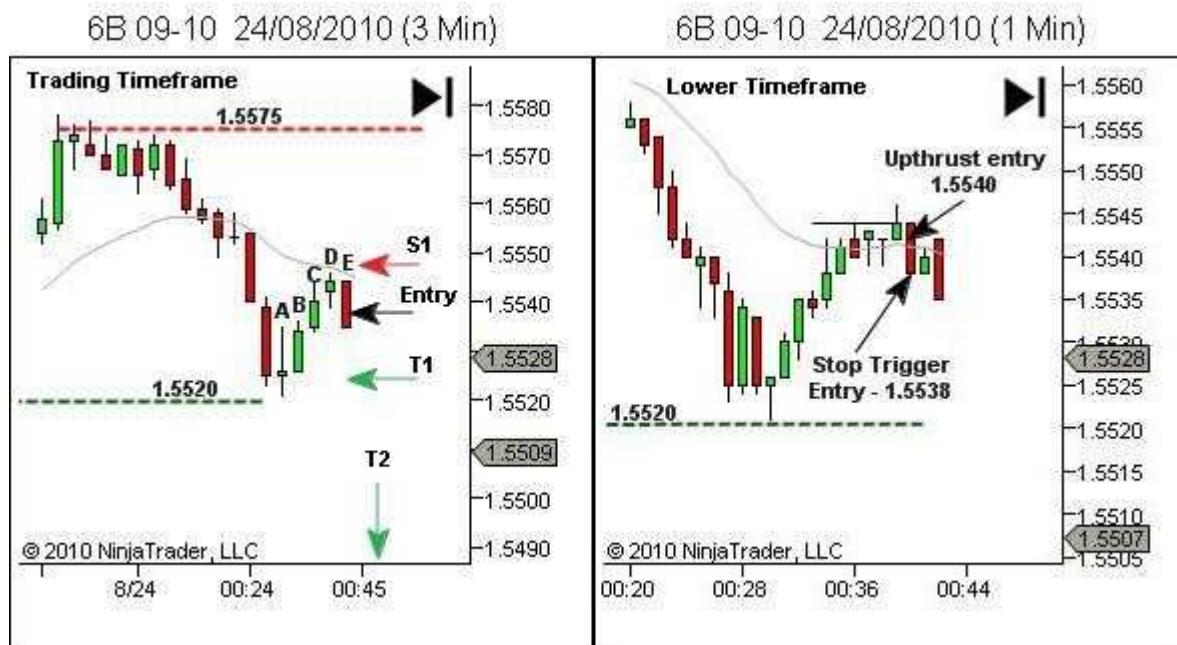


Figure 5.22 - Example 2 - Entry

Let's assume we missed the upthrust trigger and got in at LWP.

Entry is 1.5538.

Stops for both part one and two are at S1, 1.5548 (risk -10 pips).

Target T1 is at 1.5523 (reward +15 pips). Target T2 is at 1.5478 (reward +60 pips).

Step 3 – Trade Management & Exit

Trade management was quite easy in this example, as price moved reasonably quickly to the first target. The strength of the initial downswing has reasserted itself, overcoming the weaker pullback. The bearish orderflow created by the stops of the bulls (attempting to catch a reversal) helps drive our trade to profit.

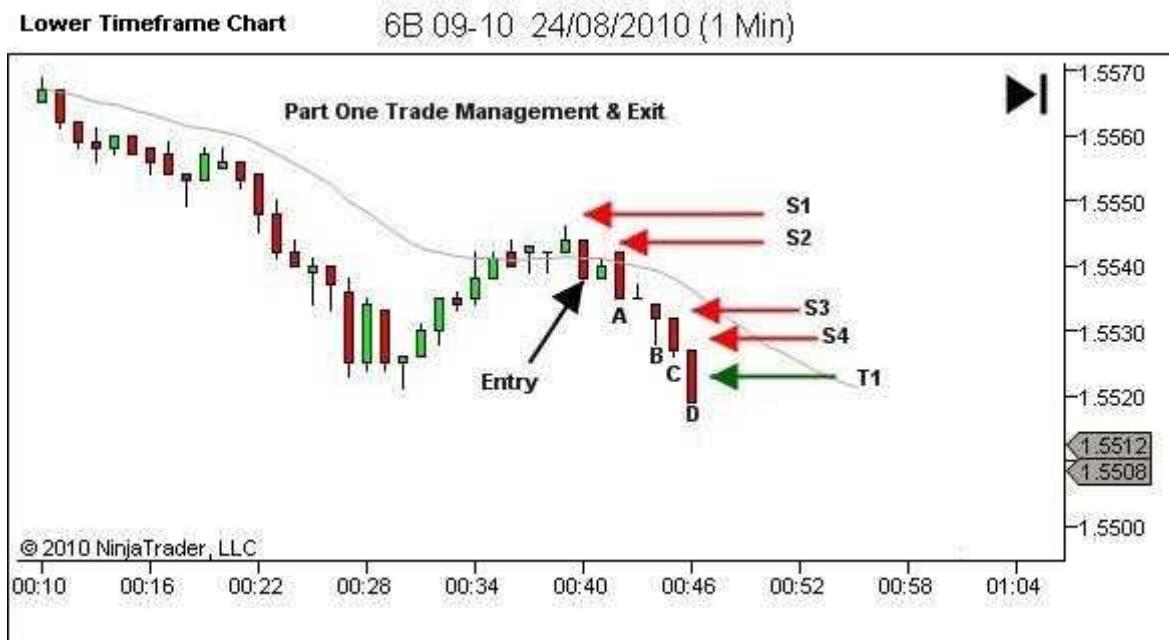


Figure 5.23 - Example 2 – Trade Management and Exit – Part One

The stop for part one was simply trailed behind significant bearish candles on the *lower timeframe* (1 min) chart. After the low close bear candle (A) the stop was moved to S2. Candle B (high close bear candle) caused a little concern, indicating potential for a retest of the entry area. Candle C (low close bear candle) closed at new lows, allowing us to move the stop to S3. As price approached the target, the stop was moved to S4 to tighten it up and ensure a more appropriate R:R for the remainder of the trade. T1 was easily achieved.

Part two was trailed behind candles as well, with focus initially on the *trading timeframe* (3 min) chart of Figure 5.24 below. On achievement of T1, the stop was moved to breakeven (S5). On the close of candle A it was moved above this candle to S6. On the close of candle B it was moved to S7. You can see here how I like to reassess the stop position after any bear candle in a downtrend (and the same for a bull candle in an uptrend).

Candle C caused some concern showing a real weakening of the trend. By candle D (if not earlier) you should be considering some way to work an exit, as downside momentum had disappeared and price shows potential to rally higher.



Figure 5.24 - Example 2 – Trade Management and Exit – Part Two – 1 of 2

Figure 5.25 (below) shows the *lower timeframe* (1 min).

Working an exit can involve two options – tightening the stop and/or the target. I chose to leave the target at T2 in this case, as any continuation lower which broke 1.5500 would possibly get enough breakout orderflow to move to T2. The area I wanted to protect though was the upside. Having seen three pushes lower all fail to take price towards T2, it's quite likely that a break higher would occur, rather than a break down. The stop was tightened to just above current price action at S8.

The trade was stopped there at 1.5513.

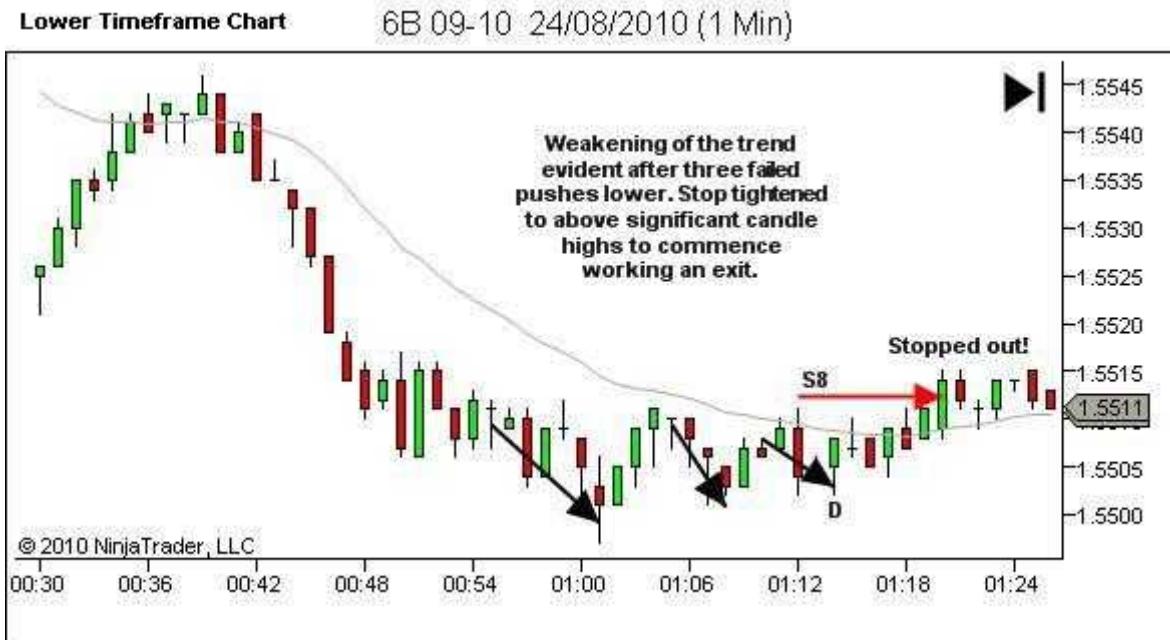


Figure 5.25 - Example 2 – Trade Management and Exit – Part Two – 2 of 2

In hindsight, it would have been best to also work the target price, perhaps getting us out towards the lower edge of the congestion, just above 1.5500. I didn't do that in this case, as I was leaving the option open for continuation lower. Had price broken 1.5500, I felt confident it would carry on to the original target. Active management decisions don't always provide the best outcome. Still, in this case, the outcome was better than simply waiting for the stop or target to be hit.

Step 4 – Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

- Part one: Achieved T1 +15 pips (less commission)
- Part two: Worked Exit +25 pips (less commission)

5.3 – Trade Example 3 – BOF, BPB, TST – Sideways Trend within another Sideways Trend

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 26 Aug 2010

Time: 22:30 on charts (13:30 London)

Let's look at another messy example with sideways, choppy price action. This is the reality of the markets; it's not always smooth, flowing trends. Often we have to battle through grinding action. All we can do is to identify our setup areas, aim to achieve the best entry possible and then manage our risk.

Remember though – if in doubt, get out. If you're not reading it well, get out of the markets. You don't have to trade.

Step 1 – Define Structure



Figure 5.26 – Example 3 – Define Structure

Figure 5.26 defines our structure. We have identified two close levels of support below the market at 1.5370 and 1.5385; and two close levels of resistance at 1.5460 and 1.5475.

Note, you could also have identified other support and resistance at the swing lows and highs within the 1.5385-5460 area. This is an example of the subjectivity that can be applied to our structural definition. While technically correct, to do so would likely just crowd the charts with too many S/R levels. It's better to visually step back a bit from the charts and select those levels which stand out the most. If the other levels are significant, they'll still play a part in our analysis, showing up on the *trading timeframe* (3 min) as significant swing highs and lows (as we'll see below in this example).

Step 2 - Define Trend



Figure 5.27 – Example 3 – Define Trend

Our trend is identified as a sideways trend (trading range) between range support at 1.5400 and range resistance at 1.5435.

Interestingly, this trading range exists within the bounds of an outer trading range between *higher timeframe* (30 min) support at 1.5385 and *higher timeframe* (30 min) resistance at 1.5460.

Step 3 - Identify Strength & Weakness



Figure 5.28 – Example 3 – Identify Strength and Weakness

The *trading timeframe* (3 min) chart shows a sideways trend in which neither the bulls nor the bears are showing greater strength.

However, the time is 22:30 which is the scheduled release time for the potentially volatile US Core Durable Goods Orders. It is expected that the next candle or two will show clear signs of strength in one direction.

Step 4 - Identify Future Trend Direction

Step 5 - Visualise Future Price Action

Step 6 - Identify Areas of Trade Opportunity

With the release of economic news pending, any identification of *future trend* direction, price action to validate it, and identification of setup areas, will have to wait. We will conduct this as part of our ongoing market analysis, based upon the first couple of post-news candles.

Ongoing Market Analysis

Step 1 – Determine Candle Pattern Sentiment

Step 2 – Consider the Context

Step 3 – Does it Support my Premise?

Once again, in summary format; due to the fact that books are not the ideal medium for demonstrating ongoing processes...



Figure 5.29 - Ongoing Market Analysis – Post-News Release

The first candle post-news release was a high close range candle. More information required!

This was followed however with an explosion higher, producing a high close bull candle closing right on its highs.

Having no original premise, we now establish one as per the initial analysis process.

Strength is to the bullish side within a sideways trading range. We therefore anticipate a breakout, in accordance with the Fourth Principle of *future trend* direction.

When a sideways trend shows evidence of strength towards the range boundary, we expect a break of the boundary. We observe the behavior of price post-breakout for clues as to future direction:

- Weakness following the breakout – the expectation is for a breakout failure and reversal back within the trading range.
- Weakness on the pullback – the expectation is for a breakout pullback and continuation.

The principle defines the price action required to validate our premise – we're searching for signs of weakness after the breakout.

The principle also defines the potential setup areas – a BOF and/or BPB setup.

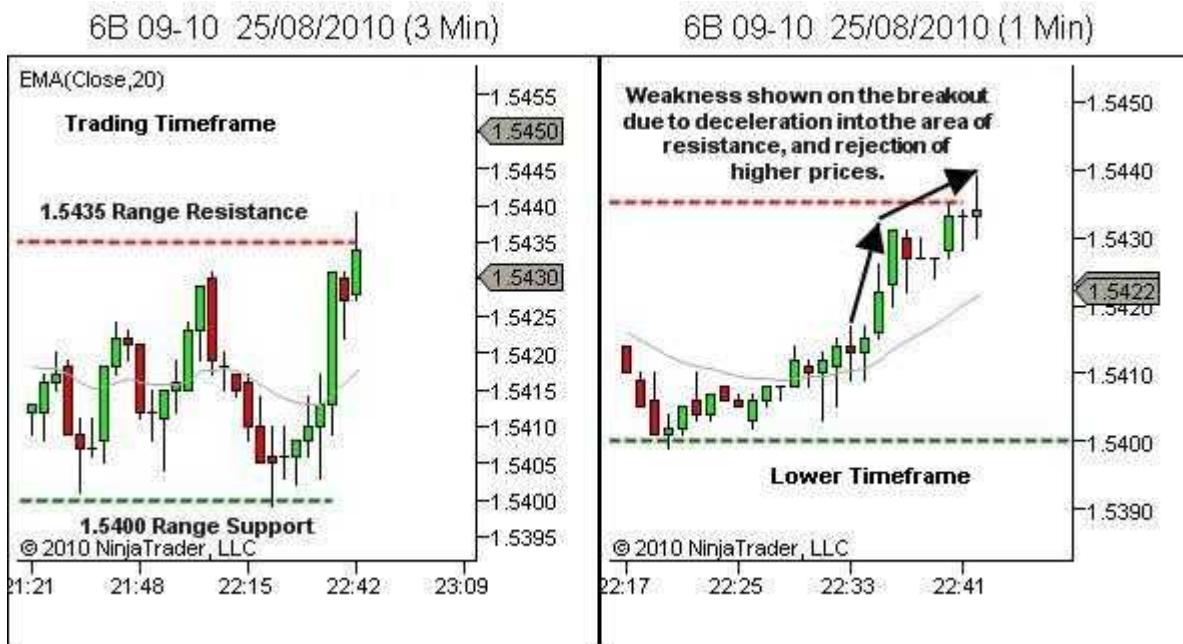


Figure 5.30 - Example 3 – Ongoing Market Analysis – Identification of Weakness

The following two *trading timeframe* (3 min) candles show weakness actually coming into price before it gets to the area of range resistance, through deceleration in the price swing. Price does breach the area of resistance though, however quickly rejects higher prices as shown by the upper tail.

We have a clear sign of weakness following the breakout; it's time to prepare for BOF trade.

Trading Process

Step 1 – Trade Preparation

Note that bar by bar ongoing analysis continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.

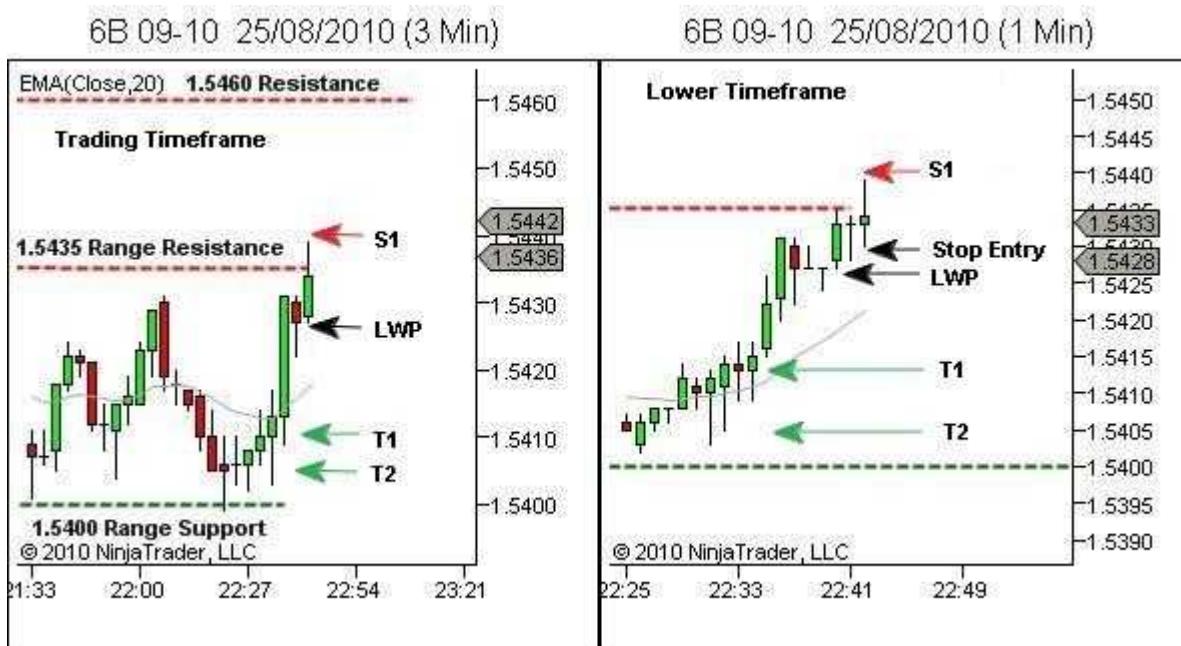


Figure 5.31 - Example 3 – Trade Preparation

S1 is tentatively identified as above the area of price rejection (upper tail) at 1.5441. LWP is the break of the 3 min candle low at 1.5426. T1 is identified as the open of the first candle post-news, 1.5413. T2 is just above range support at 1.5405. While T2 is usually placed at *higher timeframe (30 min) support*, that wouldn't be wise in this case with the 1.5400 support sure to oppose prices IF they should get there.

Risk is therefore 15 pips while potential reward for part 1 is 13 pips. This is unacceptable (although close). The LRP would be the price that offers 1:1, being 1.5427. Therefore I cannot take this entry unless I can achieve 1.5427 or higher.

Looking at the *lower timeframe* (1 min), a stop entry order on the breakout below the upper candle, would trigger at 1.5429, allowing risk of 12 pips and potential reward of 16 pips. This is acceptable.

A stop entry order is placed at 1.5429 (candle pattern trigger on break of the doji low at resistance; NB. Candle open to close is only one pip, so I'm happy to call this a doji).

The stop entry order has attached S1, T1 and T2 contingent orders.

Note that all orders are *tentative* at this stage. If subsequent price action does not trigger entry, but moves higher, I'll be sure to adjust the entry and stop loss orders as required.

So, we now await the next candle, with the intent of trying to work a better wholesale entry price (if price should offer such an opportunity), safe in the knowledge that if price should collapse from here we will be triggered into our entry at 1.5429.

Please note: despite the weakness shown just prior to and on breakout, the market had shown some initial strength into the area of range resistance. This is an aggressive entry, and any BOF trade entered must be managed aggressively. If triggered, it should prove itself to us immediately through strength to the downside. If any signs of weakness display post-entry, we will prepare for either an exit or a reversal to BPB. This should be standard practice for any BOF setup.

Step 2 – Trade Entry

No opportunity was provided to work a better entry. The trade triggers on the next *lower timeframe* (1 min) candle (1 min candle pattern trigger; breakout of doji).

Entry parameters are:

Entry: 1.5429

Stop at S1: 1.5441 (risk -12 pips)

Target T1: 1.5413 (reward +16 pips)

Target T2: 1.5405 (reward +24 pips)

Lower Timeframe Chart

6B 09-10 25/08/2010 (1 Min)



Figure 5.32 - Example 3 – Entry

Step 3 – Trade Management & Exit

Referring to the right hand side below, Candles A and B confirmed our plan, both offering low close bear candles. C then produced a low close range candle showing a slight pause in momentum. D continued lower but E then showed a further pause via a mid-close range candle.

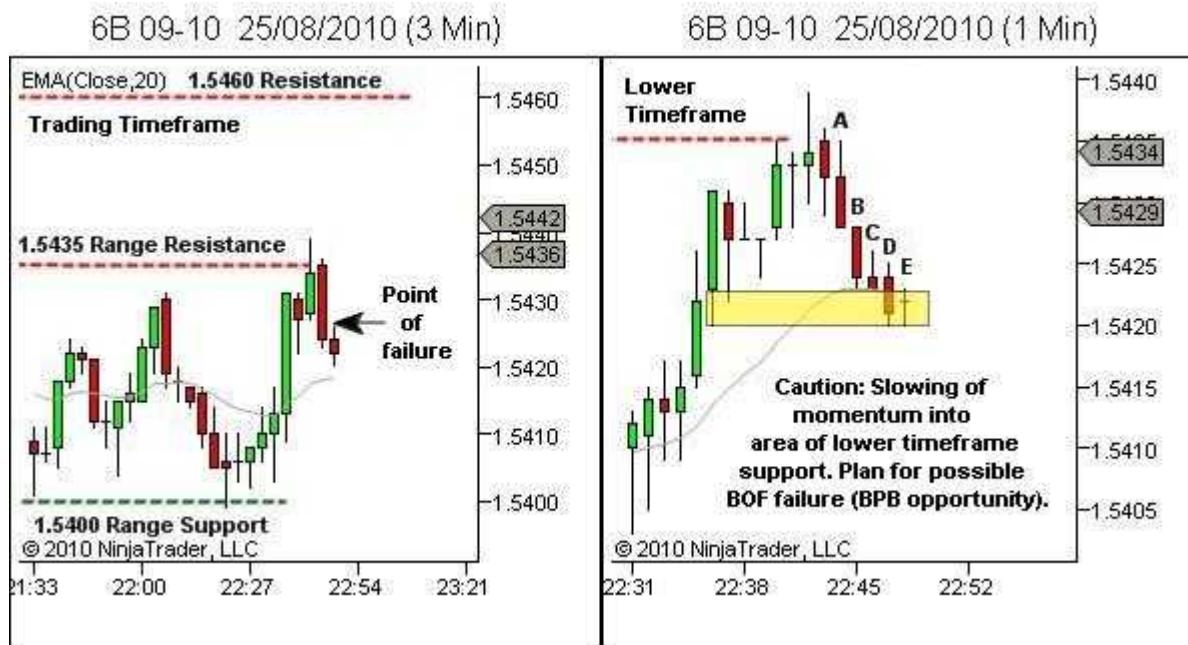


Figure 5.33 - Example 3 – Trade Management

Managing this one aggressively, I'm seeing potential support at the lower tails to the left, on the *lower timeframe* (1 min) chart (yellow shaded area).

I'm still trading the move down, but will move both stops to the point of failure, identified on the *trading timeframe* (3 min) (LHS) as above the last candle. If price reaches here it confirms a lack of strength on the downside, and should move to retest the highs again. This point of failure is above candle C on the *lower timeframe* (1 min) chart to the right, at 1.5427.

Step 1 – Second Trade Preparation

I also place orders to reverse to a BPB trade, with entry at 1.5427, stop loss below the D&E lows at 1.5419, target T1 at the highs of A, 1.5435, and T2 just below *higher timeframe* (30 min) resistance, 1.5455.

Please note that this may not be triggered if the down swing continues to new lows. It's simply placed in anticipation of a trade reversal, should price break the high of the last *trading timeframe* (3 min) candle and indicate weakness on the downmove.

Step 2 – Second Trade Entry

The original trade was stopped out at 1.5427, both part one and two achieving +2 pips each (before commissions). This is a good example of the benefits of FX Futures over spot forex. The commission (which should be less than one pip) still leaves you with two +1 profits, as opposed to a standard 3 pip spread on spot forex meaning your exit would have actually been at 1.5430, for two losses of 1 pip each. Small amounts, but they add up. We'll discuss more on that when we talk about other markets and other timeframes.

Trade reversal is seen below in Figure 5.34.

Step 3 – Second Trade Management & Exit

Post reversal price action clearly shows how strength exists in the bullish direction, both before and after the pullback, with weakness during the pullback.

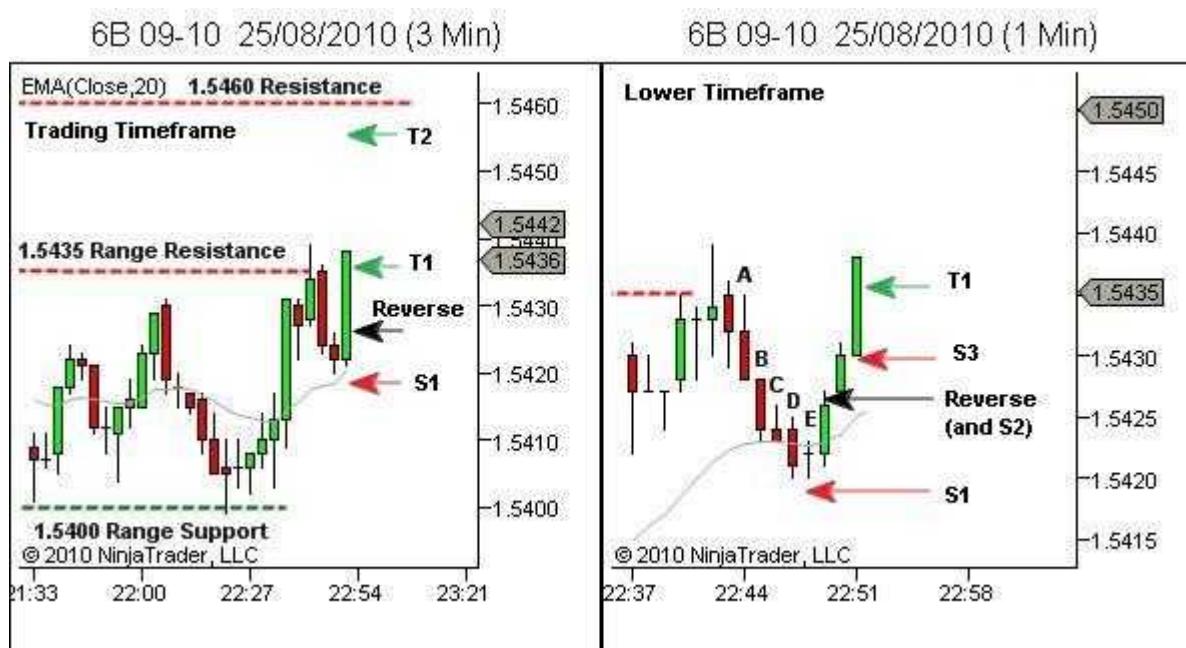


Figure 5.34 - Example 3 – Reversal, Trade Two Entry and Part One Management

Trade two quickly moved to the target T1 (1.5435), with the stop trailed behind the *lower timeframe* (1 min) candles at S2 (breakeven) and S3.

The stop for part two is moved to breakeven +1 (to cover commission). Given the new display of strength to the upside price should not get back to here again. If it does, we have evidence of supply coming in at the 1.5435 level for the second time and I have no further confidence in price moving up to the 1.5460 resistance.

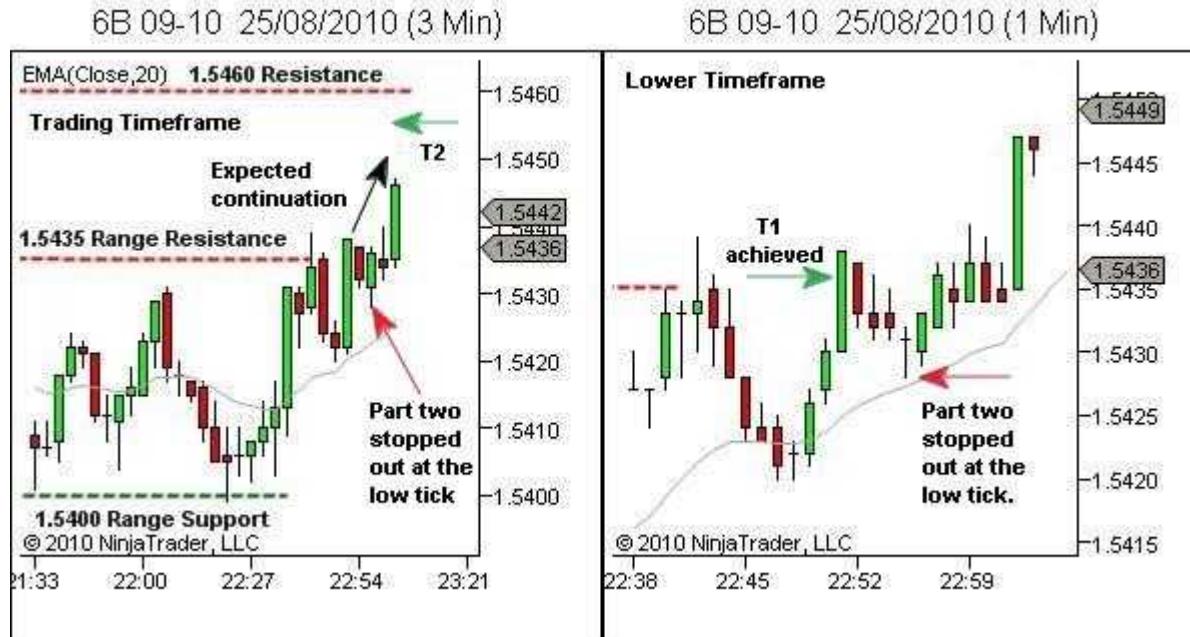


Figure 5.35 - Example 3 – Trade Two Stopped Out

Hmmm. Good plan, but part two is stopped out to the tick. No worries. It happens.

Step 4 – Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results – Trade One (BOF):

- Part one: Scratched +2
- Part two: Scratched +2

Results – Trade Two (BPB):

- Part one: Achieved T1 +8
- Part two: Stopped out +1

Let's continue this example, as follow-up price action appears to be offering another trade setup.

Step 1 – Third Trade Preparation

As shown below, price has continued higher towards to 1.5460 level. You'll recall from figure 5.27 that the 1.5460 resistance is actually the upper range resistance of a sideways trading range.

Candle A provided the only true display of strength, as price broke the upper range of the inner sideways trend. Candles B, C, E and F are all varying forms of range candles, showing either selling and/or some supply coming into the market as we approach resistance.



Figure 5.36 – Example 3 – Setup Area – Trade Three

Our expectation of *future trend* direction is for a test rather than a breakout, in accordance with the Third Principle; a sideways trend within the framework is expected to continue in its current state, unless displaying evidence of strength towards the range boundary.

For price to validate this premise, we need to see continued weakness on approach to the resistance area, and a stronger fall.

We are on alert for a TST setup.

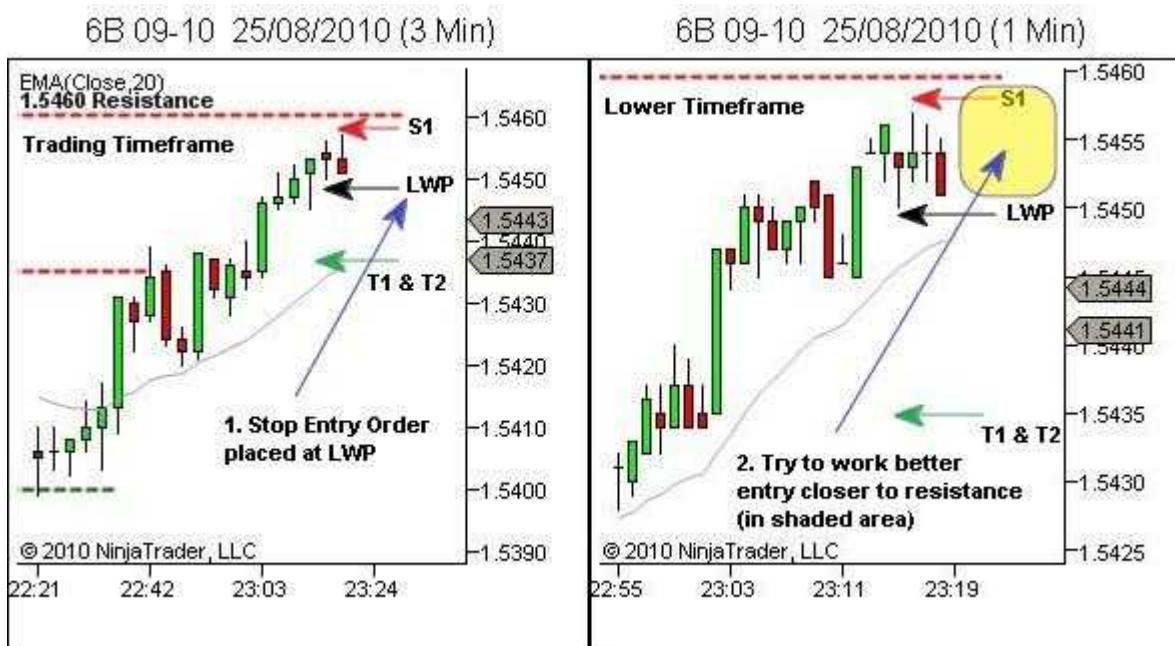


Figure 5.37 – Example 3 – Trade Preparation – Trade Three

Current price action on the *trading timeframe* (3 min) (LHS) shows a great LWP. The third last candle (high close bull candle) would have brought in more new bulls. Failure to continue higher through the next two candles will cause these people some concern. The first of their stop orders will start triggering on a break below the last two red candles.

A stop entry order is placed at LWP, 1.5449.

S1 is above the price action highs at 1.5459. T1 and T2 are both at the previous breakout area 1.5435.

We now try to work a better entry, closer to resistance, as shown in the shaded area above.

Step 2 – Third Trade Entry

There was no opportunity for a better worked entry, and we“re triggered into the trade at LWP, 1.5449.

Step 3 – Third Trade Management & Exit

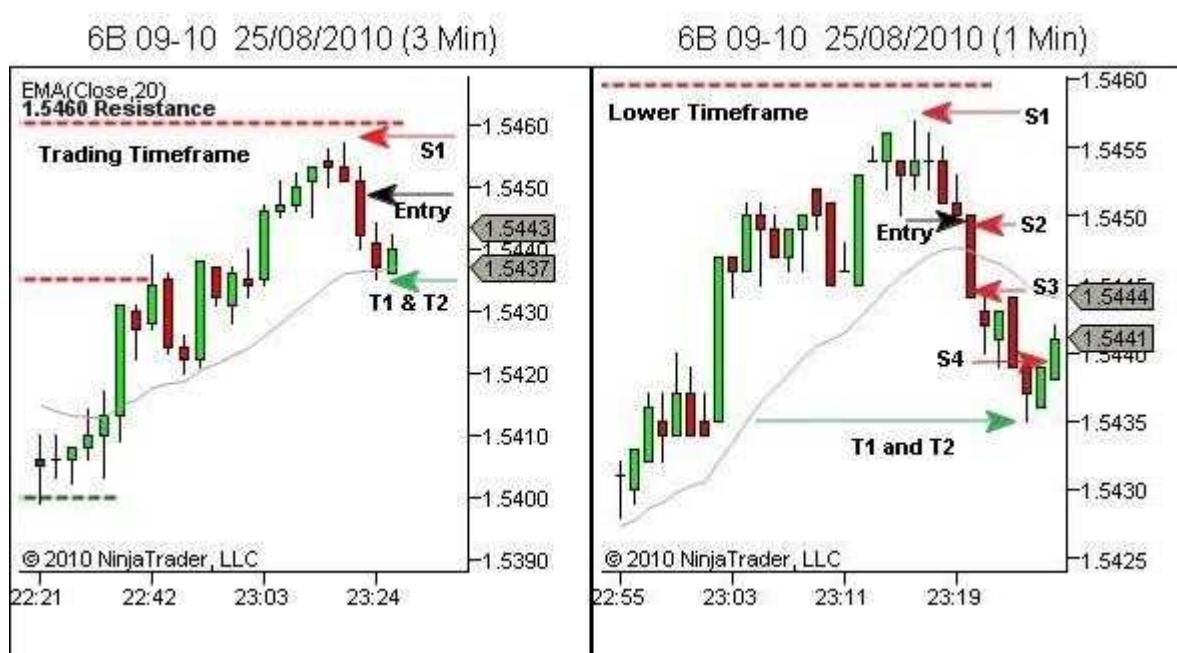


Figure 5.38 – Example 3 – Trade Three – Trade Management and Exit

The stop for part one was trailed behind significant candles (the low close candles), to breakeven (S2) and then S3. As price approached the target it was moved to S4.

The stop for part two was moved with the part one stop to breakeven (S2) and remained there until moved to S4 with part one (giving it a little more room intra-trade if necessary).

Although price touched our target 1.5435 we were not filled. Price stopped us out at S4, 1.5440.

Step 4 - Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results – Trade One (BOF):

- Part one: Scratched +2
- Part two: Scratched +2

Results – Trade Two (BPB):

- Part one: Achieved T1 +8
- Part two: Stopped out +1

Results - Trade Three (TST):

- Part one: Achieved T1 +9
- Part two: Achieved T2 +9

TOTALS:

- Part one: +19 pips (less 3 x round turn commissions)
- Part two: +12 pips (less 3 x round turn commissions)

A lot of work for only +31, but that's the way trading goes sometimes.

5.4 – Trade Example 4 – CPB – T1 Achieved – T2 Trailed

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 30 Aug 2010

Time: 23:55 on charts (14:55 London)

I like this example. It demonstrates the awkward period that can sometimes exist following a test of S/R (support in this example). Do we seek a pullback entry for a further retest of the support area? Or do we trade in the new counter-trend direction now?

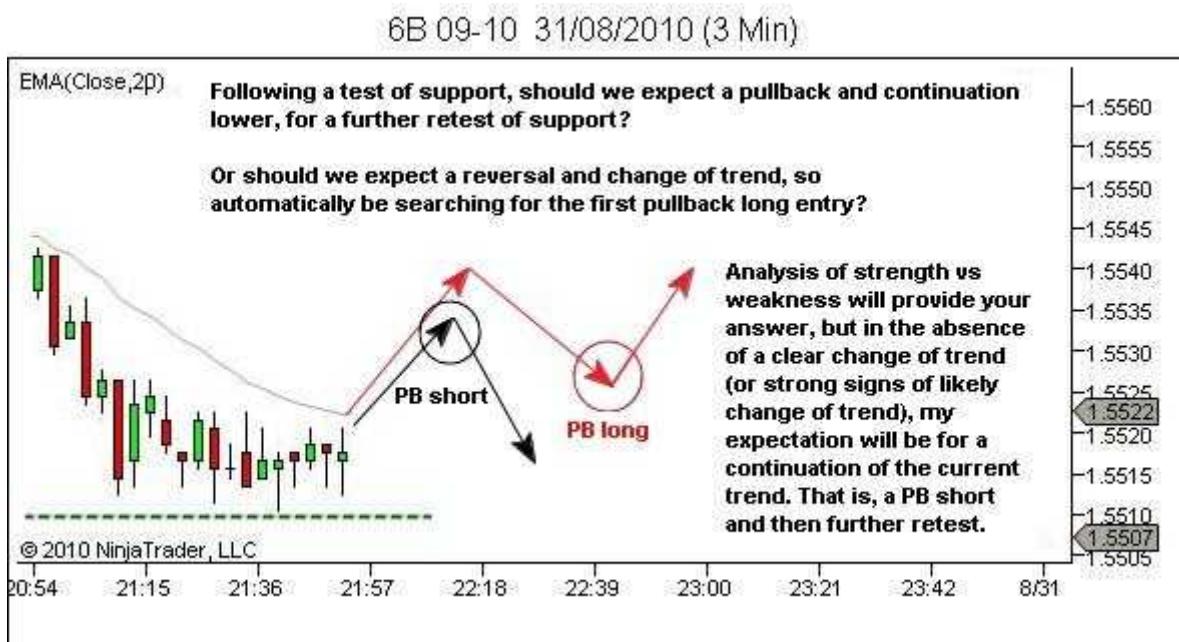


Figure 5.39 - Expectations following a test of S/R

As always, it depends on how the price action shows strength and weakness. The default decision though is the first of these options. Until there is a clear sign of change of trend, we continue with the First Principle, expecting continuation of the trend towards S/R. Until we have signs of a change of trend, we will keep looking for pullback opportunities (PB or CPB) for a further retest of S/R; and of course TST and BOF/BPB opportunities at the S/R level.

The Second Principle often applies as well, as in this case, where we do see weakness against the support area. As stated with the second principle, we expect a complex pullback rather than reversal, until clear signs of reversal are shown.

Don't be too quick to expect a reversal.

Sometimes several PB opportunities will be present as the trend tests the S/R level several times, before either breaking through or reversing.

Step 1 - Define Structure

The chart below shows our structure with resistance above price at 1.5575 and support below price at 1.5440, 1.5495 and the recently tested 1.5510 level.



Figure 5.40 - Example 4 – Define Structure

Step 2 – Define Trend

As shown in figure 5.41 below, at 23:55, price has broken above the recent congestion, but the trend is still downwards.

Technically, a change of trend will not be triggered until a breach of the 1.5548 level, the last swing high which preceded the recent swing lows.

This recent move is therefore a pullback within a downtrend.



Figure 5.41 - Example 4 – Define Trend

Note: See if you can identify where you may have entered a TST long off support. This area would have provided a great opportunity to work a limit entry quite close to the support level. However, we are not considering any such trade in this example. We commence this example from the point displayed on the chart – two candles into the pullback.

Step 3 – Identify Strength & Weakness

Figure 5.42 below shows clear signs of weakness into the area of support.

We also have a surge of bullish momentum coming off support. While this could be a sign of strength, it's really a little too early to tell. This surge of momentum is a result of breakout orderflow, as price broke above the area of congestion at support (breakout entry orders long combined with stops from anyone short).

Continuation of this bullish surge is required to confirm strength in the bullish direction. Failure to continue will show weakness.

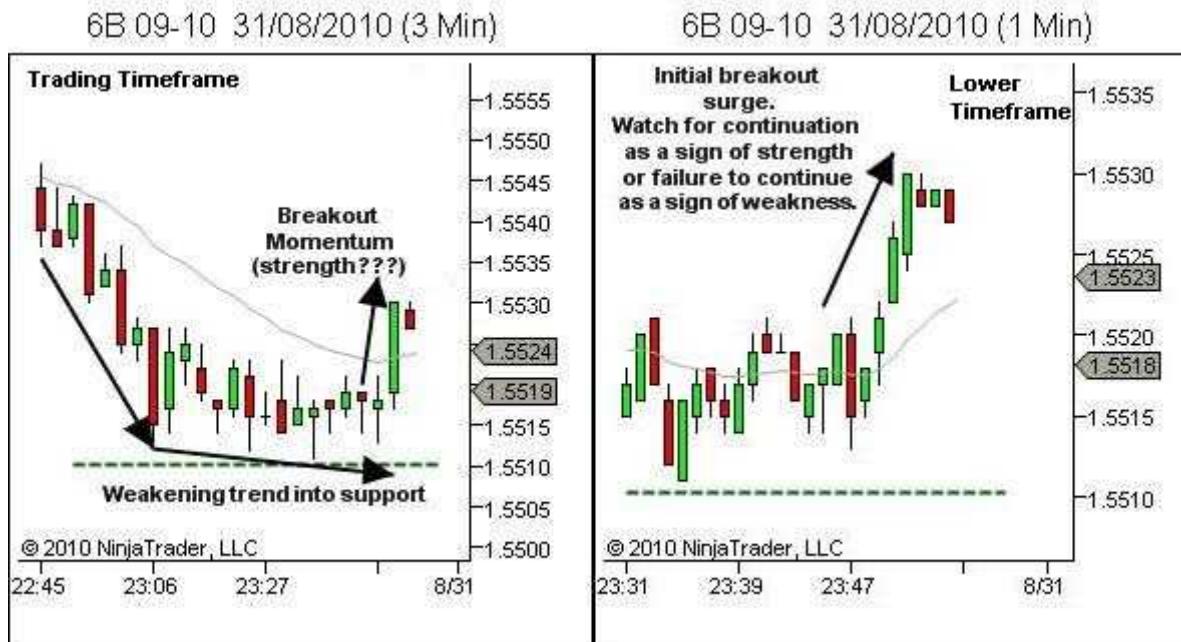


Figure 5.42 - Example 4 – Identify Strength and Weakness

Step 4 – Identify Future Trend Direction

Step 5 – Visualise Future Price Action

Step 6 – Identify Areas of Trade Opportunity

Let's combine some steps here in summary form.

Having seen weakness in the downtrend we expect some form of complex pullback, then continuation lower to again retest the support level, in accordance with the Second Principle of *future trend direction*.

Price action required to validate our premise will be some form of continuation of this current move to new highs which then fails to show strength (ie. a second push higher which fails).

This will provide our trade opportunity – a CPB entry on failure of the second push higher.

Price action showing continued strength higher and subsequent change of trend will invalidate our plan; requiring reassessment and identification of new trade setups.

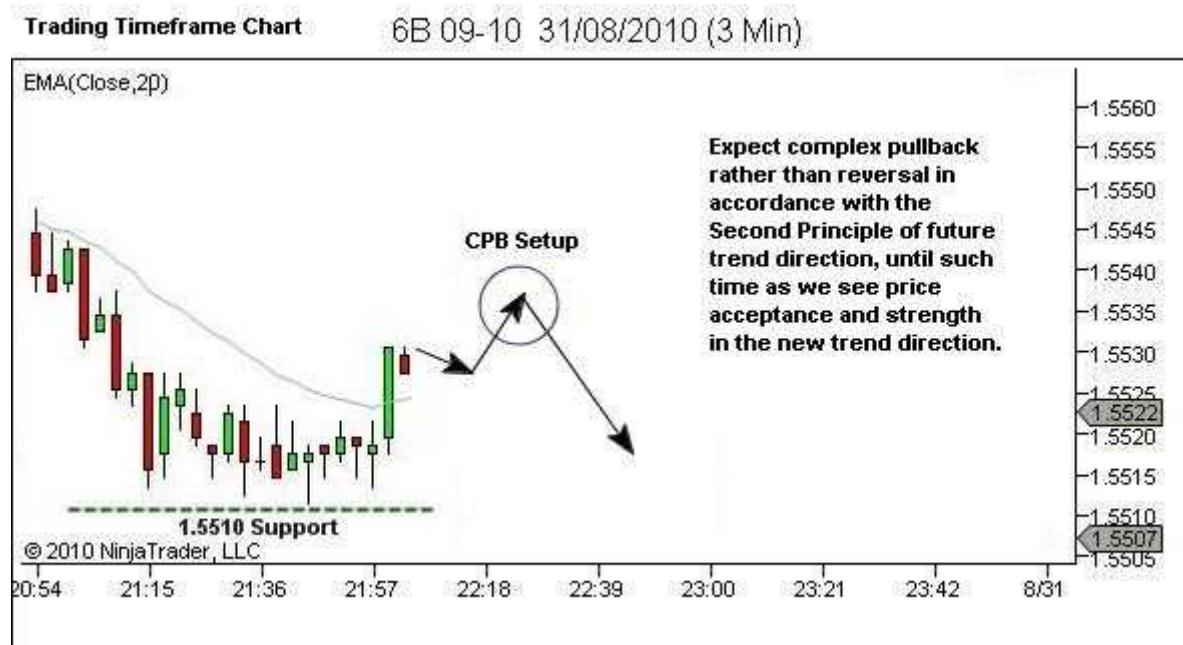


Figure 5.43 - Example 4 – Future Trend Direction; Future Price Action; Setup Area

Ongoing Market Analysis

Step 1 - Determine Candle Pattern Sentiment

Step 2 - Consider the Context

Step 3 - Does it Support my Premise?

Sometimes setups and entries appear quite quickly. **Remain focused.**



Figure 5.44 - Example 4 – Ongoing Analysis – Rapid Setup Identification

Candle A (low close range candle) provided our first pullback against the initial bullish surge.

Candle B (high close range candle) showed an end to the pullback, but certainly no continuation of strength due to the inability to break to new highs. We've had six minutes pass since the initial surge, with no signs of continuation. This is possibly confirming weakness in the pullback.

Candle C initially moves to higher prices. If our analysis is correct, we expect to see this push higher show weakness, providing us with our opportunity to enter short at the CPB setup.

In this case, the failure to continue higher occurs a LOT quicker than expected.

The right hand side of our previous chart shows the *lower timeframe* (1 min) fine-tuning of our analysis, where you can clearly see the three swings of this complex retracement.

I was expecting swing three to carry further before failing, but sometimes these things happen quite quickly. You need to remain focused. Now let's see if we can get an entry...

Trading Process

Step 1 & 2 - Trade Preparation & Entry

Price has broken below the previous two *trading timeframe* (3 min) candles after first moving to new highs, providing a CPB setup and entry (assuming it provides appropriate R:R and we can get a fill). The 1 min trigger pattern would be an upthrust.

While this may seem rushed, remember that the last *lower timeframe* candle is a whole minute in duration – plenty of time to confirm R:R and place an order.

S1 is identified at 1.5534. LWP (on break of the previous 2 *trading timeframe* (3 min) candles) was 1.5526. T1 is identified as 1.5515. This offers 1:1. An entry order is placed for 1.5526 and filled during the last one min candle.

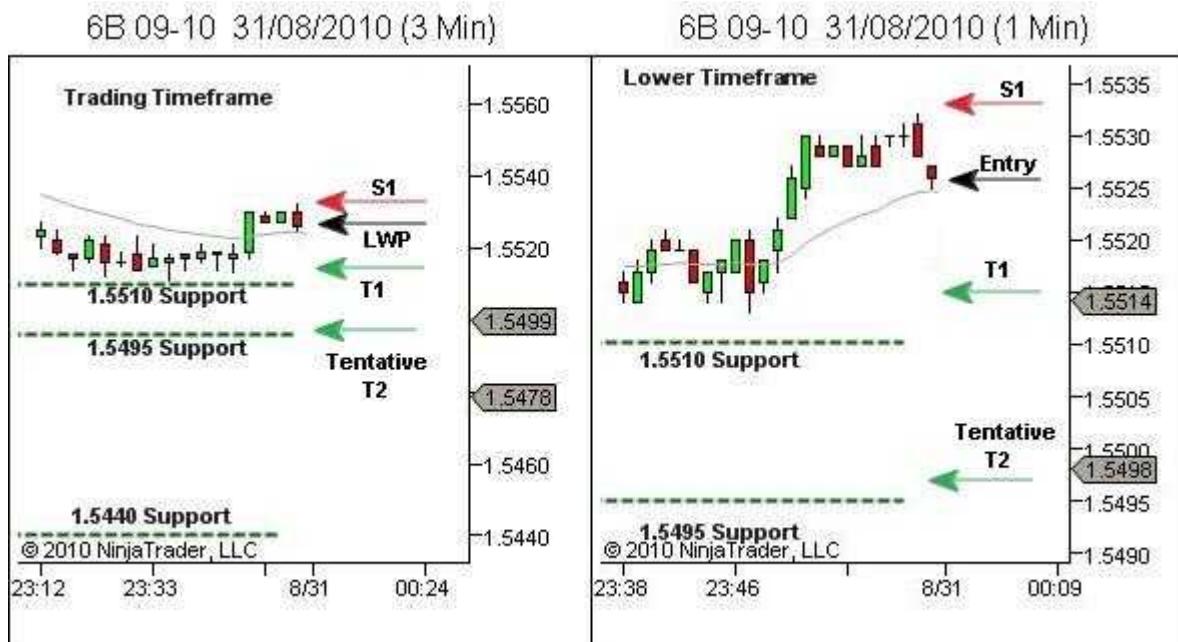


Figure 5.45 - Example 4 – Trade Preparation and Entry

T2 is tentatively identified as the next support level 1.5495. I say tentatively because there is potential for another breakout surge, this time below the congestion at 1.5510 rather than above it.

The T2 target order is in the system, but I'll watch price as it breaks 1.5510, and if surging lower I'll drag the target order to just above the next support at 1.5445, and apply a trailing stop down to that level (effectively bracketing the price).

Before we manage the trade, let's have final word on the speed with which this setup was identified and entered. While not ideal, this is the nature of the trading game. It's not always neat and tidy. Faith in your analysis and your ability to manage risk is essential, otherwise hesitation would likely have resulted here leading to a missed entry.

I have faith that the failure of the second push higher (albeit a short one) will lead to a continuation of the trend and a retest of the support level.

I was able to identify this setup and enter because I was focused, and actively watching for any sign of trapped longs, whose exit would provide an entry trigger short.

However I can't tell the future – any position is actively managed in order to minimise risk. If the push lower is a trap and price surges upwards again, my loss will be minimised via the stop for a loss of -8 pips. If price stalls, I'll work an exit. If I'm right, I'll manage it as best I can to achieve maximum profits possible.

The confidence required to enter here only comes through experiencing lots of price action and lots of setups. We'll talk more about that in chapter 16, when we discuss the learning process.

Repeat of entry parameters:

Entry 1.5526
S1: 1.5534 (risk -8 pips)
T1: 1.5515 (reward +11 pips)
T2 1.5495 (reward +31 pips) (tentative) or trail to 1.5445 (+81 pips)

Step 3 – Trade Management & Exit

Candle A on the RHS of the chart below shows the power of a trapped trader pattern, as the first of the stops are triggered from those trying to get an early entry into a reversal. Bearish orderflow pushes price strongly down.

Part one stop is moved to breakeven on the close of candle A, and then to S2 after the small stall following A. T1 is then achieved.

Part two stop is moved to breakeven, then S2 after candle B. The acceleration as price continued falling led to movement of the tentative T2, to 1.5445. However a stop was trailed behind significant price developments, via S3 to S7.

Part two was stopped out at S7 for +44 pips.

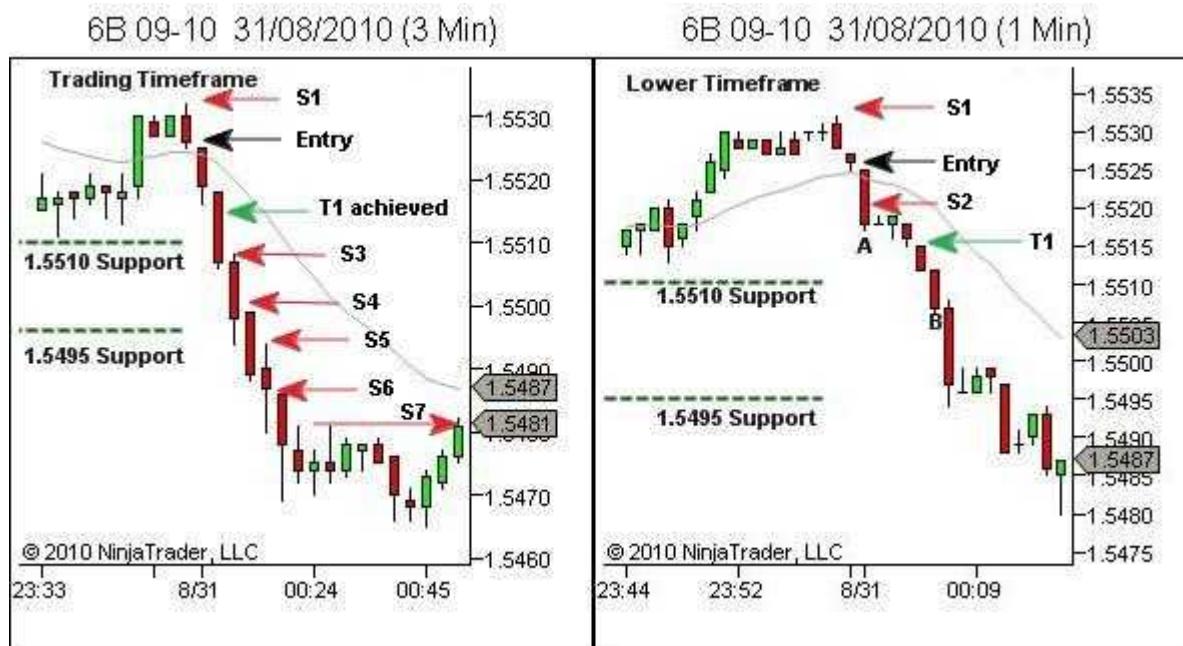


Figure 5.46 - Example 4 – Trade Management and Exit

Step 4 - Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

- Part one: Achieved T1 +11 (less commission)
- Part two: T2 Trailed +44 (less commission)

As Al Brooks says in his great book, “Reading Price Charts Bar by Bar”, a trending market always offers what seems like great counter-trend entries. The higher odds trades though, are always for a continuation of the trend. Watch any counter-trend move for signs of failure. The point of failure provides a great entry for a continuation of the trend.

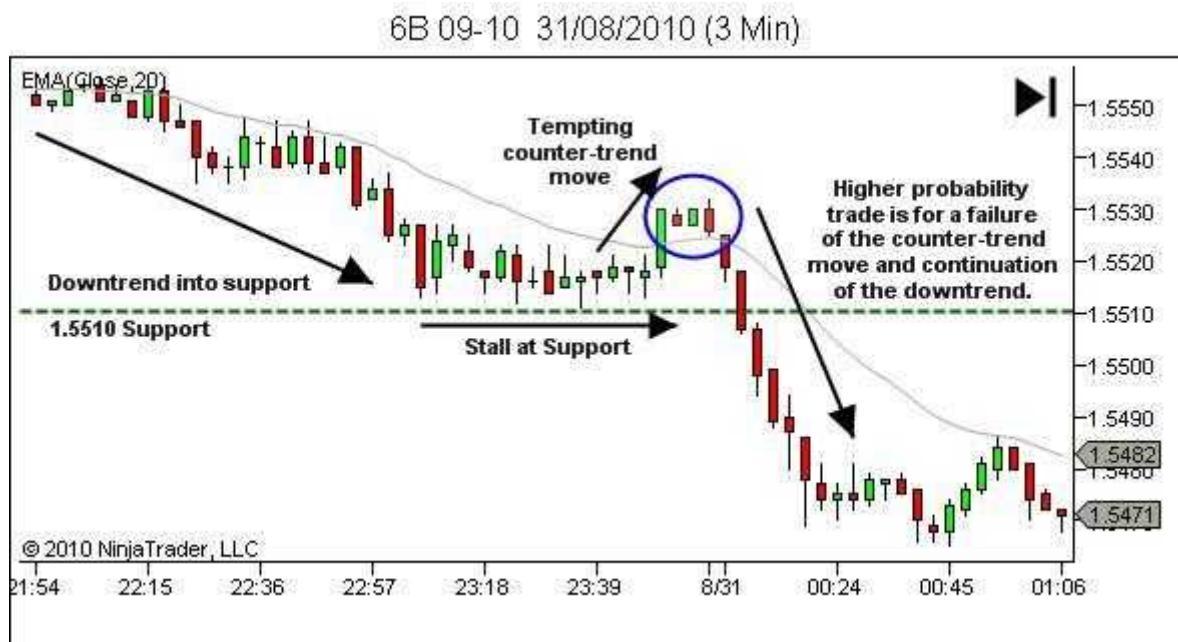


Figure 5.47 - Example 4 – Hindsight Review – Downtrend Continuation

5.5 – Trade Example 5 – TST – Part 1 Stopped Breakeven - Part 2 Trailed.

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 31 Aug 2010

Time: 18:30 on charts (09:30 London)

The last example showed a situation where a move off S/R did not lead to a reversal; rather it was simply a pullback before continuation of the trend.

As a reminder of the fact that every situation in the markets is unique, let's now look at an example where a test of S/R did offer a reversal.

Step 1 – Define Structure

We start with the *higher* timeframe (30 min) chart. Resistance is identified above current price at 1.5575, 1.5475 and 1.5450. Support is identified below the market at 1.5395.



Figure 5.48 - Example 5 – Define Structure

Step 2 - Define Trend

The *trading timeframe* (3 min) chart shows a change to uptrend. Price is currently on a pullback within that uptrend, although I'm not watching for a pullback entry just yet due to the upcoming release of an economic indicator.



Figure 5.49 - Example 5 – Define Trend

Step 3 - Identify Strength & Weakness

Step 4 - Identify Future Trend Direction

Step 5 - Visualise Future Price Action

Step 6 - Identify Areas of Trade Opportunity

As mentioned above, I'm not watching for a pullback entry opportunity as news is about to be released. Similarly, I'm not going to conduct analysis of strength and weakness, *future trend* direction or potential setup areas – my expectations are neutral. I'll reassess on completion of the first post-news candle. Being the UK Net Lending to Individuals m/m, it's only a medium impact report so not likely to offer any great volatility. However I'll hold any expectations for now.

Volume Five will identify my source of economic releases, including their expected impact.

Ongoing Market Analysis

Step 1 – Determine Candle Pattern Sentiment

Step 2 – Consider the Context

Step 3 – Does it Support my Premise?

Ongoing market analysis steps are combined, as mentioned earlier, due to the difficulty in demonstrating a dynamic process in book form. Thoughts from these three continual steps are provided in summary form below.

The next candle (post-news release) is a large range high close bull candle, taking price right to the first resistance area, 1.5450.

We have no existing premise, so let's develop one now.

This push of post-news momentum clearly shows strength to the bullish side, within the timeframe of that candle. However the question is (as it is with all post-news candles) whether or not this move can be sustained.



Figure 5.50 – Example 5 – Identify Strength and Weakness

As shown above, while the large high close bull candle is bullish in nature, this candle takes price right into the lower boundary of a significant area of resistance, between 1.5450 and 1.5475 (we will consider this as one area).

Given the display of strength into resistance, my initial bias must be for a break of that level (ie. continuation through 1.5475), watching then for signs of weakness post-breakout for either a BOF and/or BPB opportunity. This is of course in accordance with the Sixth Principle of *future trend* direction.



Figure 5.51 – Example 5 – Identify Future Trend Direction

The price action required to validate this premise is a continuation higher through resistance. Strength will have to continue to be shown on the bullish side, with weakness on the bearish side.

That being said, I do have a great liking for areas of support which turn to resistance (and vice versa). The nature of trader decision making tends to make them particularly strong levels. Combining this with the width of the resistance area, I wouldn't be surprised to see it hold. If weakness appears in the current push, prior to breakout, I'll need to adjust my premise and watch for some kind of test opportunity short (in accordance with the Fifth Principle of *future trend* direction).

Let's look at the next candle - a mid-close range candle (LHS).



Figure 5.52 – Example 5 – Ongoing Market Analysis

Having shown a failure to continue higher, we see that bearish orderflow did enter the market at the resistance level. Price has pulled back. However the *lower timeframe* (1 min) action to the right shows some signs of bullish strength / bearish weakness, via the lower tails. The pullback so far still supports our premise – some bearish orderflow is to be expected. Continuation needs to happen soon though if this market is going to be able to push through the resistance area.

The next candle (LHS) is also a mid-close range candle, offering the same message – continuation of the pullback.



Figure 5.53 – Example 5 – Ongoing Market Analysis - continued

What is concerning though, is the duration of this pullback. The post-news bullishness has perhaps failed to attract a wider bullish following.

Strength needs to continue to new highs. Any weakness, through either a weaker retest of 1.5450, or a failure to exceed the previous swing high, will indicate lack of support for the bulls at this time and a greater likelihood of supply overcoming demand. In either case we will require an immediate reassessment of our premise, anticipating a test of resistance, and a possible TST setup.

The next *trading timeframe* (3 min) candle shows us a failure to continue higher.

Price rallied to again test the 1.5450 level, but was immediately rejected. Current price action is not acting how it should, if market participants were acting with a bullish bias.



Figure 5.54 – Example 5 – Ongoing Market Analysis - continued

The premise requires immediate adjustment. My expectation is now for a test of resistance (fifth principle), followed by at least a complex pullback (and retest in accordance with the second principle) or a complete reversal.

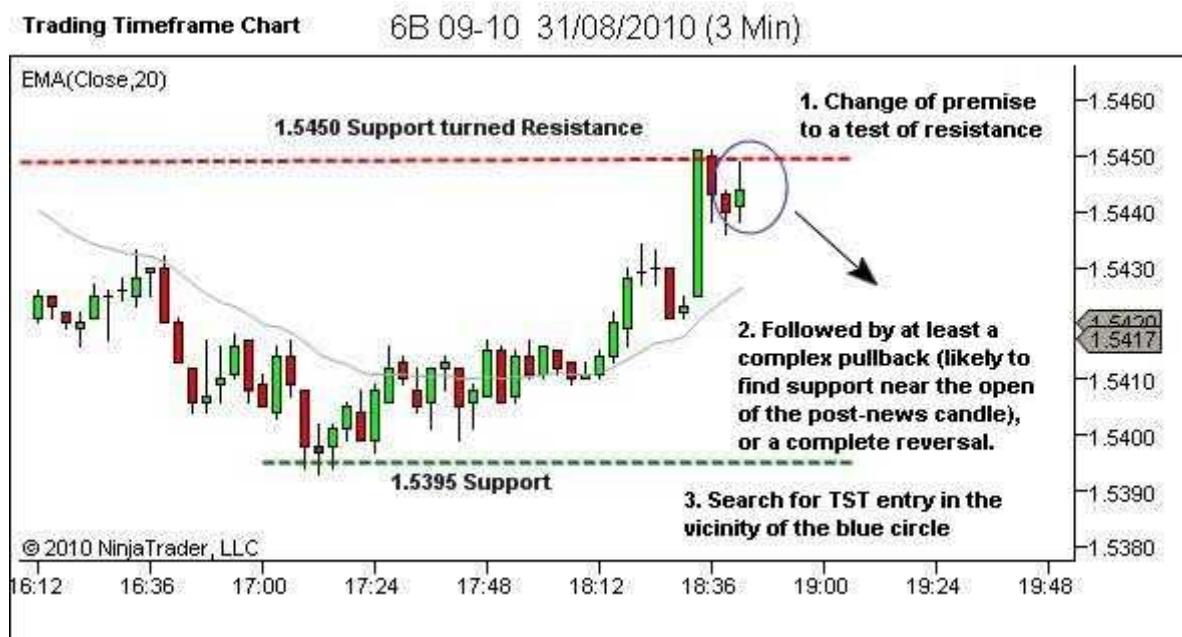


Figure 5.55 – Example 5 – Change of Premise

Trading Process

Step 1 – Trade Preparation

Note that bar by bar ongoing analysis continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.

Price action is as per the *trading timeframe* (3 min) and *lower timeframe* (1 min) charts below.

Any immediate entry (if filled) would involve a stop at 1.5452 (S1) and a part one target of 1.5425 (T1), where the post-news bullish orderflow first appeared.

LWP is the point at which the first of the *trading timeframe* (3 min) stops would be triggered. This would be below the lowest candle in the pullback, at 1.5435. Entry here would incur a risk of 17 pips for a potential reward of 10 pips. Entry at LWP is therefore not wise – we'd be entering too late in the move; too close to potential support at T1.

LRP is the mid-point; the price which allows us a 1:1 R:R. This is midway between S1 and T1, or at 1.4438. Entry must be achieved at or before 1.4438 in order to ensure a 1:1 ratio.



Figure 5.56 – Example 5 – Trade Preparation

Remember, on fast intra-day timeframes we don't need to be this accurate. The price which offers 1:1 is at the mid-point between the stop and target. It's sufficient to simply eye-ball it. LWP in this case is not within the first half of the stop-to-target price region. So, we search for an entry trigger which is.

Step 2 - Trade Entry

The *lower timeframe* (1 min) chart already provides a pattern based trigger, forming a 123 top. Movement below the current candle will signal a failure of the latest push towards new highs, the second push to resistance.

I am happy to enter on such a trigger, so place a stop entry order immediately below the 1 min candle as it approaches its close. Stop entry order price is 1.5443.

While recognising that it's likely to fill fairly quickly, having the previous candle close on its low, I am also prepared to work a better limit order if possible. I place a limit at 1.5447 (mid-range of the previous candle).



Figure 5.57 – Example 5 – Trade Entry

The stop entry order is filled on the next candle open. The limit order is cancelled.

Trade entry parameters are as follows:

Entry: 1.5443
 Stop Loss: 1.5452 (risk -9)
 Target T1: 1.5425 (reward +18)
 Target T2: 1.5405 (reward +38)

Step 3 – Trade Management & Exit

Figure 5.58 demonstrates our trade management and exit. There is a whole lot of information on this diagram, so let's work through it slowly.

As with earlier convention, the *trading timeframe* (3 min) chart is on the left and the *lower timeframe* (1 min) chart is on the right.

Look first at the right hand side, where we manage part one on the *lower timeframe*.



Figure 5.58 – Example 5 – Trade Management and Exit

As will usually happen if you correctly identify trapped traders, price surges in our direction quickly, via candle A (low close bear candle). However it then stalled through candles B (again a low close bear candle, but with very little range) and candle C (mid close range candle). Candle D broke above the stalled area to commence a pullback. I became concerned here about a potential 3-swing retracement long which would retest resistance again before failing. I moved the

part one stop to breakeven plus one (to cover commission), with the intention that I'd try to work a better entry if price retested resistance. The part two stop remained at S1.

Part one stopped out to the tick before price moved on to T1 without me; and didn't offer a re-entry that I was happy with.

This happens. In hindsight, the stop was moved too early.

The setup was good, with a strong resistance area twice rejected. I was confident price would not get up there again. And it was obvious through watching the slow pullback of candles C, D and E that bullish pressure was much weaker than the bearish pressure shown in candle A.

Still, it's always easy to see in hindsight.

Looking at the left hand side for part two...

The stop was moved to breakeven on achievement of T1. It was then trailed behind significant price action – moved to S2 on the break to new lows; S3 then S4 on the close of the next two low close bear candles; then tightened up above price action as price approached our target (reaching 1.5407; two pips from our target).

You'll recall that I like to tighten up stops as I approach the target. I don't see value in keeping the stop at S4 where we risk 12 pips, just to get an extra 2 pips reward. That's a bad R:R.

The stop was tightened up, taking us out at 1.5412.

Step 4 - Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

- Part one: Achieved T1 +1 pips (less commission)
- Part two: Achieved T2 +31 pips (less commission)

I particularly love this kind of setup – on a quick glance it appears we’re trading against strength, which goes against the whole premise of our trading strategy which is to fade weakness at S/R or weakness in a pullback.

However, the news-initiated strength is short-lived. It moves against a larger timeframe trend (not part of our analysis, but clearly obvious on the 30 min *higher timeframe* chart), quickly moving into an area of resistance where it stalls. Failure to follow through indicates bearish pressure at that level opposing the bullish strength. An initial failure, followed by a slower momentum retest and second failure, provides us with the weakness at resistance that we like to fade.

We aim to enter with the first of the stops, as the post-news bulls are either stopped out or bail out after realising they’re in a low probability position.

So, despite initial appearances, this is not going against strength.

Of note also, is the fact that this example produces 30+ pips that you would not have gained had you used the simple entry strategy (*trading timeframe* only; entering at LWP). The trade would not have been taken at all due to poor R:R. Once you’re comfortable with the strategy concept, I do encourage you to start working to identify better entries on the *lower timeframe*. Provided they offer a clear stall, or a pattern based trigger, they’re usually a risk worth taking.

5.6 – Trade Example 6 – BOF – T1 & T2 Achieved

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 31 Aug 2010

Time: 22:30 on charts (13:30 London)

One factor which makes trading so difficult is the seemingly infinite variations of the same themes. No one setup is the same as the others. Take the last trade for example, which was a strong test of S/R followed by a slower retest. Let's look at another one; same idea, very different trade.

Step 1 – Define Structure

Our *higher timeframe* (30 min) chart identifies resistance above the market at 1.5475 and 1.5450. Prior support at 1.5395 and 1.5385 have been broken and invalidated, although the 1.5395 level is identified as possible future resistance.

The 1.5370 support level was broken on the second last candle, although the break failed. It has just been retested.



Figure 5.59 – Example 6 – Define Structure

Step 2 – Define Trend



Figure 5.60 – Example 6 – Define Trend

The market is clearly in a downtrend, based upon our *lower swing highs / lower swing lows* definition.

The current candle has broken to new lows, so the recent swing high must be taken out in order to change the trend to upwards. Until that occurs, we remain in a downtrend.

Step 3 – Identify Strength & Weakness



Figure 5.61 – Example 6 – Identify Strength and Weakness

Figure 5.61 shows a significant weakening of bearish momentum between swing A and swing B.

Approximately 45 minutes ago, price hit the 1.5370 support level with strength. While managing to break the level, there was no continuation of bearish orderflow beyond the breakout point and so the breakout failed. In swing B, price has now moved to retest this level, albeit on much reduced momentum.

The trend is weakening, and possibly failing at the 1.5370 region.

Once again we have moved to new lows (only just). The next few candles will be critical in defining the way forward – will the breakout fail a second time, or will price continue its march lower?

Step 4 – Identify Future Trend Direction

Step 5 – Visualise Future Price Action

Step 6 – Identify Areas of Trade Opportunity

Combining these three steps on one chart...

Having broken the area of support, our expectations are in accordance with the Sixth Principle of *future trend* direction.

We will watch the behavior of price post-breakout for clues as to future direction:

- Weakness following the breakout – the expectation is for a breakout failure and reversal back through the area of S/R.
- Weakness on the pullback – the expectation is for a breakout pullback and continuation.

That being said, my gut feel is for a breakout failure, given the weakness of the trend. If this eventuates, it will lead to either a complex pullback testing the recent swing high, or a reversal up to the 1.5395 resistance level.



Figure 5.62 – Example 6 – Future Trend Direction and Areas of Trade Opportunity

Ongoing Market Analysis

Step 1 – Determine Candle Pattern Sentiment

Step 2 – Consider the Context

Step 3 – Does it Support my Premise?

Combining these three ongoing steps into summary form:



Figure 5.63 – Example 6 – Future Trend Direction and Areas of Trade Opportunity

The very next candle shows bullish orderflow. While a high close range candle is by itself only slightly on the bullish side of neutral, placing this candle into the context of a slow momentum retest of a previous breakout, once again failing to hold new lows, it's decidedly bullish.

It's time to prepare for a potential BOF trade.

Trading Process

Step 1 – Trade Preparation

Note that bar by bar ongoing analysis continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.

The stop is tentatively identified as below the swing low at 1.5359. If I'm entered into a trade, and price hits this level, I want OUT. My premise is wrong and price is possibly going lower.

T1 is identified as 1.5379, the highest 3-min close on the swing high. T2 is identified as 1.5393, just inside the potential resistance of 1.5395.

Stop (1.5359) to first target (1.5379) is 20 pips. LRP would be at midway, 1.5369. Any entry must be at or before 1.5369.

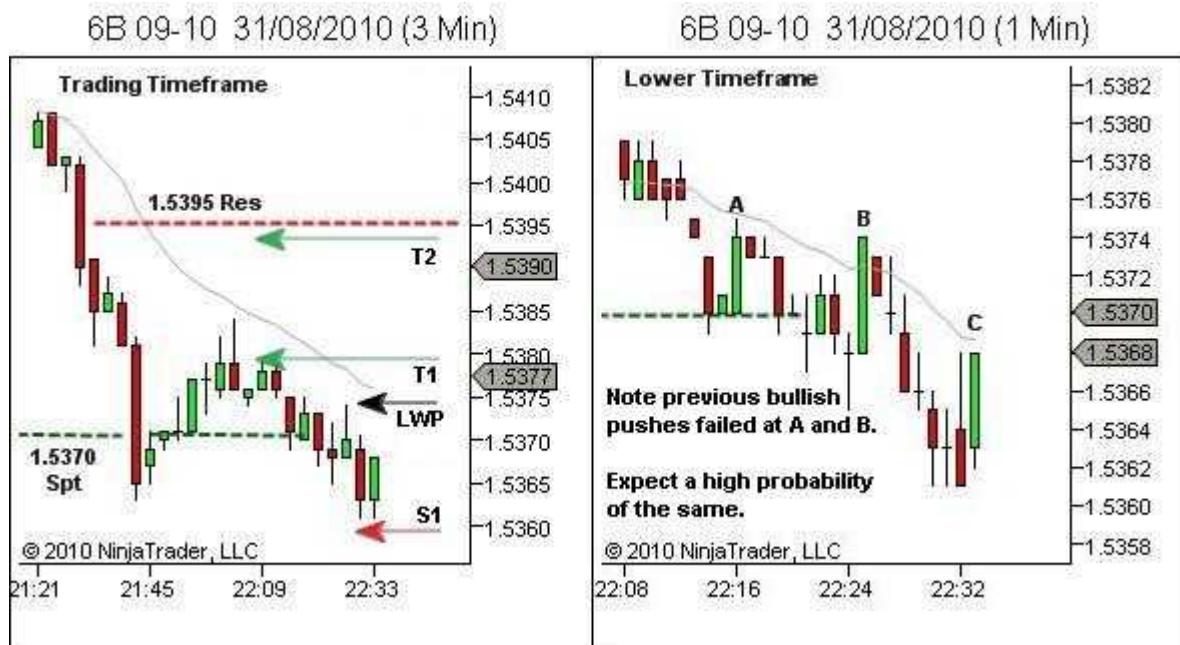


Figure 5.64 – Example 6 – Trade Preparation

LWP is a little harder to identify. Note how the 3-min price action is grinding downwards, with lots of candle overlap, but very little breakout above the previous candle. Placing a stop entry order above the high of the last 3-min candle would not necessarily be effective. Looking at the 1-min candles on the RHS, we can see that previous bullish thrusts were quick to fail. It's not likely that sufficient orderflow will enter on an immediate breakout from this point.

When in doubt, and when faced with grinding action such as this, it's best to think back to first principles. LWP is the last wholesale point, but we define it as the area at which the first of the stops will start being triggered, for anyone trading this low probability down-swing.

Sure, some may trigger on the break above the latest 3-min candle (high close bull candle). Some may trigger above the prior candle (low close bear candle). But for me, the place I expect most shorts would have their stop, is above the short upthrust formed by the third-last candle, as marked on the chart as LWP.

LWP is at 1.5375, outside of our entry zone which is formed by the stop to LRP.

As determined earlier, any entry must be at or before 1.5369.

Step 2 – Trade Entry

We're unable to simply place a stop entry order at LWP. To do so means we are too close to the first target; the first level which may provide opposing orderflow. An entry at this point would provide inadequate R:R; a losing proposition over the long haul.

So, we are left with trying to find a *lower timeframe* (1 min) entry. Ideally we're looking for a 1-min pattern based trigger (which will hopefully provide sufficient *lower timeframe* (1 min) orderflow to get the price to our *trading timeframe* (3 min) LWP, where we expect the orderflow to help push us to T1), or through identifying a nice stall against support allowing a limit order entry close to support and offering a great R:R.

Let's watch subsequent price action as it unfolds.



Figure 5.65 – Example 6 – Working a Limit Order Entry

The next 3-min candle produces a stall. We have 3 candles now, stalled at the same level.

Note on the 1-min chart we also have another bullish thrust with candle D. This time it initiated from the same level as the previous bullish thrust (C), not from a lower level as occurred with B and C. There is buying coming into the market at the lower levels.

I place a BUY LIMIT order at 1.5363, the lowest body open/close above the low point (ie. the body from candle E and doji F).

Note that if we get filled here it provides us with a risk of only 4 pips and a potential reward of 16 to our first target (and potential reward of 30 to our second target). This is the power of a limit order entry within a stall area, when it gets filled. Sometimes they may fail, but they offer great R:R when they work. They're usually a risk worth taking.

However, figure 5.65 below shows that we weren't filled during the following 3-min candle, with price missing our entry by one pip.

Candle G shows yet another bullish surge. Price is pushing higher. This thing is ready to go and we're at risk of missing an entry.

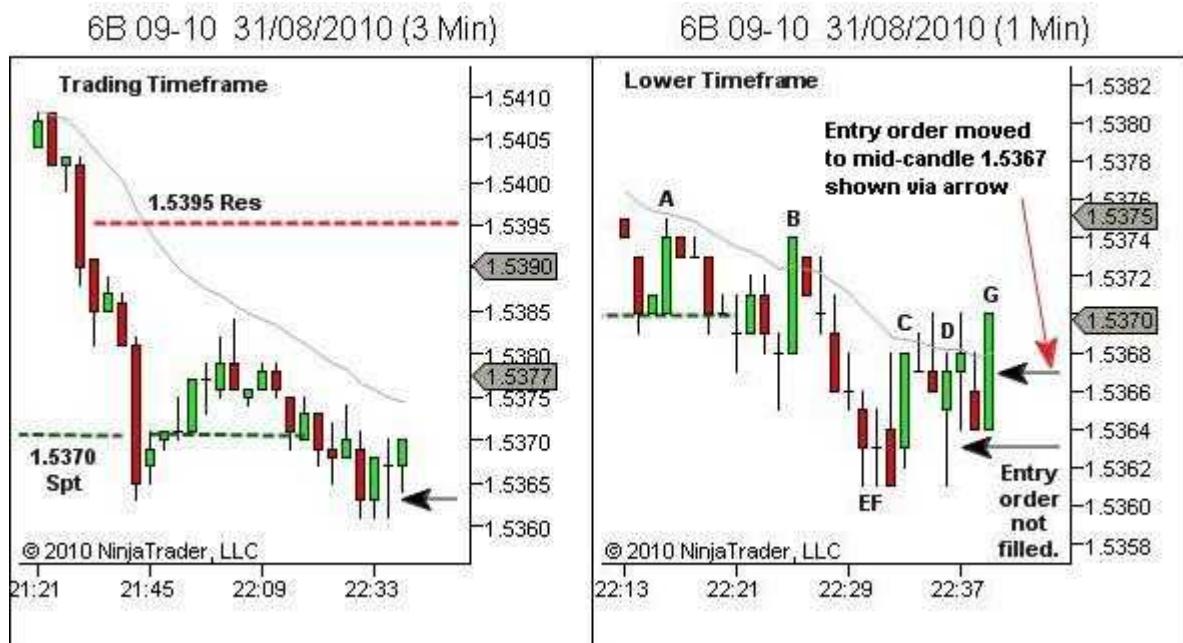


Figure 5.66 – Example 6 – Not Filled

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The limit order is raised to the mid-point of candle G (1.5367), chasing price, but ensuring we do not exceed our LRP 1.5369. We're filled two minutes later at 1.5367.



Figure 5.67 – Example 6 – Filled

Lucky? Yes, perhaps. But through working the entry we have secured a fill which exceeds our required 1:1 reward:risk ratio, at a price which was never in drawdown for the remainder of the trade (as we'll see shortly).

Entry parameters are:

Entry price: 1.5367

Stop loss: 1.5359 (risk -8)

T1: 1.5379 (reward +12)

T2: 1.5393 (reward +26)

Step 3 – Trade Management & Exit

There's not much to say on trade management here. The stop was never threatened. The trade was never in drawdown. Price moved in an orderly manner towards both T1 and T2. Stops were simply trailed behind bull candles, on both the 1 min chart (part one) and 3 min chart (part two).

The traders entering short into an area of support (or in this case an area of previous breakout failure) are taking a low probability position. The first of their stops will start triggering on the break of LWP. Rather than trade with these consistent losers, we chose to fade the weakness. We chose to be part of the orderflow which springs their trap. And then we ride their bullish orderflow to profit.



Figure 5.68 – Example 6 – Trade Management and Exit

Step 4 - Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

- Part one: Achieved T1 +12 pips (less commission)
- Part two: Achieved T2 +26 pips (less commission)

So, there we have the same concept as the last trade – a slower momentum retest of S/R. But as you see, every trade presents its own challenges. While example 5 did not penetrate the resistance level, example 6 did break support. While example 5 occurred quickly, example 6 stalled at the support level for around 10 minutes. While example 5 offered a price at which we could place a stop entry order, ensuring we didn't miss the trade, example 6 did not allow this (with acceptable R:R), so required us to fight for a good entry.

Every trade is unique, and must be treated as such.

5.7 – Trade Example 7 – TST – Part 1 Scratched, Re-entered & Stopped Out – Part 2 Stopped out

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 31 Aug 2010

Time: 22:55 on charts (14:55 London)

Not every trade is a winner. In this example here, I take a loss due to some weak analysis. See if you can spot it as we work through the example. We'll talk about it later.

Step 1 – Define Structure

Our *higher timeframe* (30 min) chart shows resistance overhead at 1.5475 and 1.5450. Price is currently at an area of support turned resistance, 1.5395 (the level where we took profits in example 6).

Support is below at 1.5360, although we do not yet have sufficient candles to properly define a swing low. It's only tentatively noted at this stage.

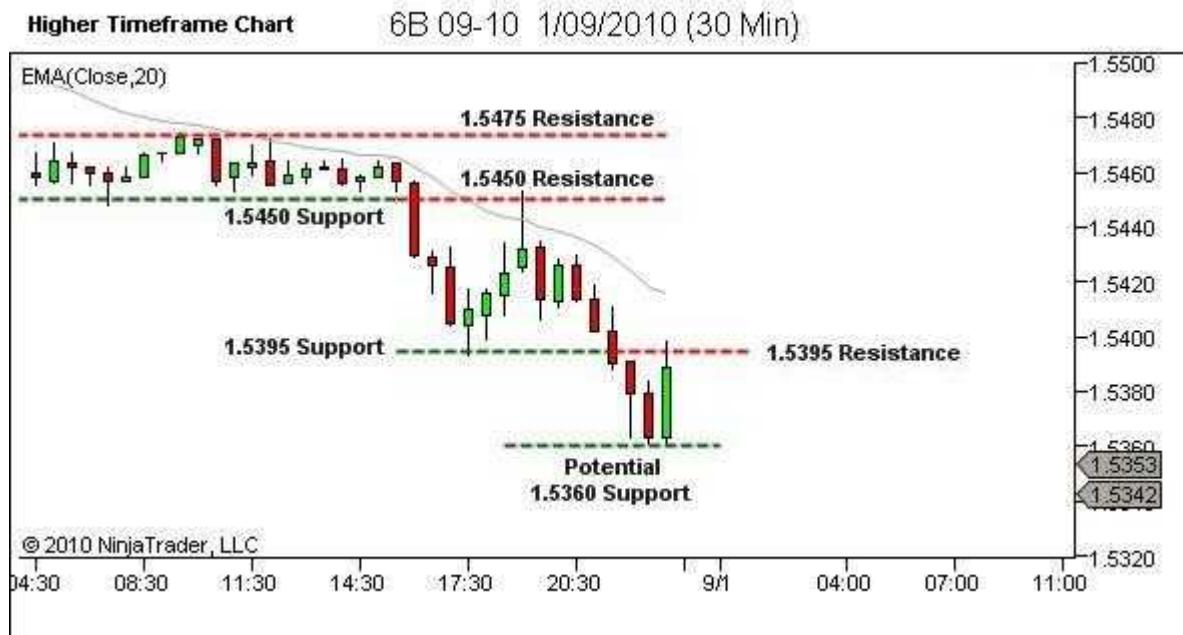


Figure 5.69 – Example 7 – Define Structure

Step 2 - Define Trend

As we see below, the market was in a downtrend for most of the chart. The third candle from the right (high close bull candle) strongly broke above the swing high which preceded the lowest low; thereby causing a change of trend.

The market is currently in an uptrend.



Figure 5.70 – Example 7 – Define Trend

My feelings here though, are that this could be a form of complex pullback rather than reversal. Note the distance that price dropped below the moving average at about 21:40. This could be a form of 3-swing retrace (a messy one due to the second swing reaching new lows!!!). It's likely that the 1.5395 resistance will hold price, which will then enter either a period of sideways action, or resume the downwards trend.

Step 3 – Identify Strength & Weakness

The *trading timeframe* (3 min) clearly shows weakening bearish momentum via swings A and C; and strengthening bullish momentum via swings B and D.



Figure 5.71 – Example 7 – Identify Strength and Weakness

Looking inside the price action to fine-tune our analysis, the *lower timeframe* (1 min) shows the latest bullish swing to be slowing as it reaches the 1.5395 resistance.

Strength however is to the bullish side.

Step 4 – Identify Future Trend Direction

As we are approaching a resistance area with strength, my expectations are in accordance with the Sixth Principle of *future trend* direction.

If strength is shown on an approach to an S/R barrier, we expect a breakout and watch the behavior of price post-breakout for clues as to future direction:

- Weakness following the breakout – the expectation is for a breakout failure and reversal back through the area of S/R.

- Weakness on the pullback – the expectation is for a breakout pullback and continuation.

Just a reminder – S/R levels are not a single price level, but an area. Looking left to prior price action, the 1.5395 level is actually an area within the range 1.5393 – 1.5402.

Step 5 – Visualise Future Price Action

My expectation then is for strength to continue through to above 1.5402. Any failure to breach the level will invalidate the premise and require reassessment.

Step 6 – Identify Areas of Trade Opportunity

Weakness through the breakout area will provide a BOF setup, allowing us to trade a failure of the resistance level short.

Strength through the breakout area with a weaker pullback will provide a BPB opportunity trading the first pullback after the breakout.



Figure 5.72 – Example 7 – Expectations for Future Trend Direction

Ongoing Market Analysis

Step 1 – Determine Candle Pattern Sentiment

Step 2 – Consider the Context

Step 3 – Does it Support my Premise?

This dynamic (bar by bar) process will be presented in summary form, as per the previous examples.

Moving on to the next *trading timeframe* (3 min) candle, we see a mid-close range candle. By itself a mid-close range candle implies neutral sentiment. But let's put it into context. Price has rallied to a strong resistance level (recent support turned resistance), and now twice rejected the level producing long upper tails.



Figure 5.73 – Example 7 – Ongoing Market Analysis

This is a clear sign of weakness and does not support my premise.

I now reassess my expectations, believing that price will not break the resistance level. With weakness shown at resistance, I am expecting a test of the level only, and a potential TST setup, in accordance with the Fifth Principle of *future trend* direction.



Figure 5.74 – Example 7 – Reassessment of Bias

Trading Process

Step 1 – Trade Preparation

Note that bar by bar ongoing analysis continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.

Trade preparation is shown on the chart below.

The stop is easy (as always)... S1 is placed above the recent swing high which was twice rejected, at 1.5400.

The first target (T1) is at the start of the momentum move higher, 1.5371. The second target (T2) is a little lower, just above potential support at 1.5365.

The point at which I expect the longs to start exiting is the lows of the third-last candle (mid-close range candle). LWP is identified as one pip below this candle low, at 1.5386.

Risk at LWP is 14 pips. Potential reward is 15 pips. Entry at LWP is therefore acceptable, although I will try to work a better entry.



Figure 5.75 – Example 7 – Trade Preparation

Step 2 - Trade Entry

A stop entry order is placed at LWP, 1.5386, in case price continues lower from its current position.

I also place a limit entry order higher at 1.5395, the lowest part of the body of the highest 1-min candle.

The charts below show the next 3 minutes of data.

Entry occurs within the next 1-min candle at 1.5395. The stop entry order at 1.5386 was cancelled. Once again, note the improved entry available through the use of limit orders (a saving of 9 pips).

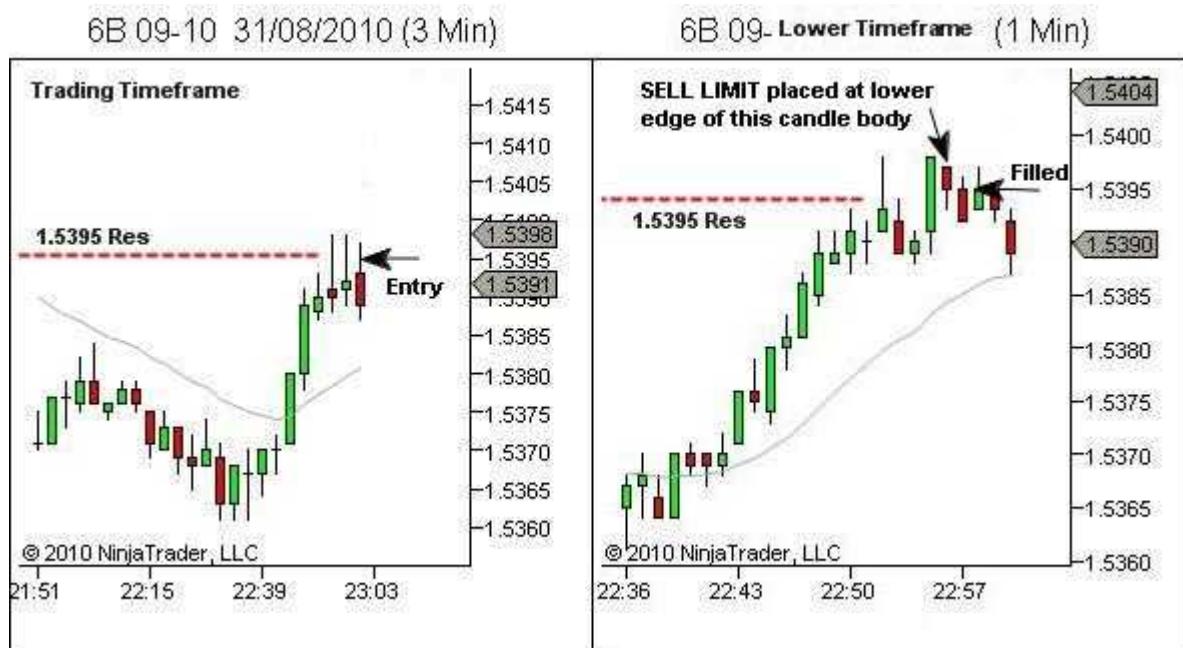


Figure 5.76 – Example 7 – Trade Entry

Trade parameters:

Entry price: 1.5395

Stop loss: 1.5402 (moved it just above the round number (comfort thing) due to better entry price allowing improved R:R) (risk -7 pips)

T1: 1.5371 (potential reward 23 pips)

T2: 1.5365 (potential reward 30 pips)

Step 3 - Trade Management & Exit

You'll get some trades during your career where you immediately feel unease upon entry. This was one of them. Despite the initial price movement going in my direction, something didn't feel right. Let's look at the 1-min chart to see the first few candles after entry...



While I was happy to get a limit entry, it was observed that the second "failure" did not continue lower at all. This didn't feel like a "failure" any more.

Price stalled for two minutes. I was very close to scratching the trade when it broke below recent congestion and fell.

The drop failed to continue; failing to reach LWP. The LWP is required to be achieved in order to gain confidence in the trade. That's where the loser orderflow should really start to kick in, driving our trade to profit.

The next candle reversed, and I decided to scratch part one at breakeven if touched.

Looking at the lower chart now, we see the next candle exited part one at breakeven (loss of commission only).

We now watch for signs of either strength or weakness, which will lead to either (a) scratching part two as well if we doubt the trade premise, or (b) re-entering part one.

The stop out candle rallied straight to 1.5397 (it's high price) and then found solid resistance there for the next 15-20 seconds.

Given this further evidence of support I reentered part one, achieving the same price 1.5395.

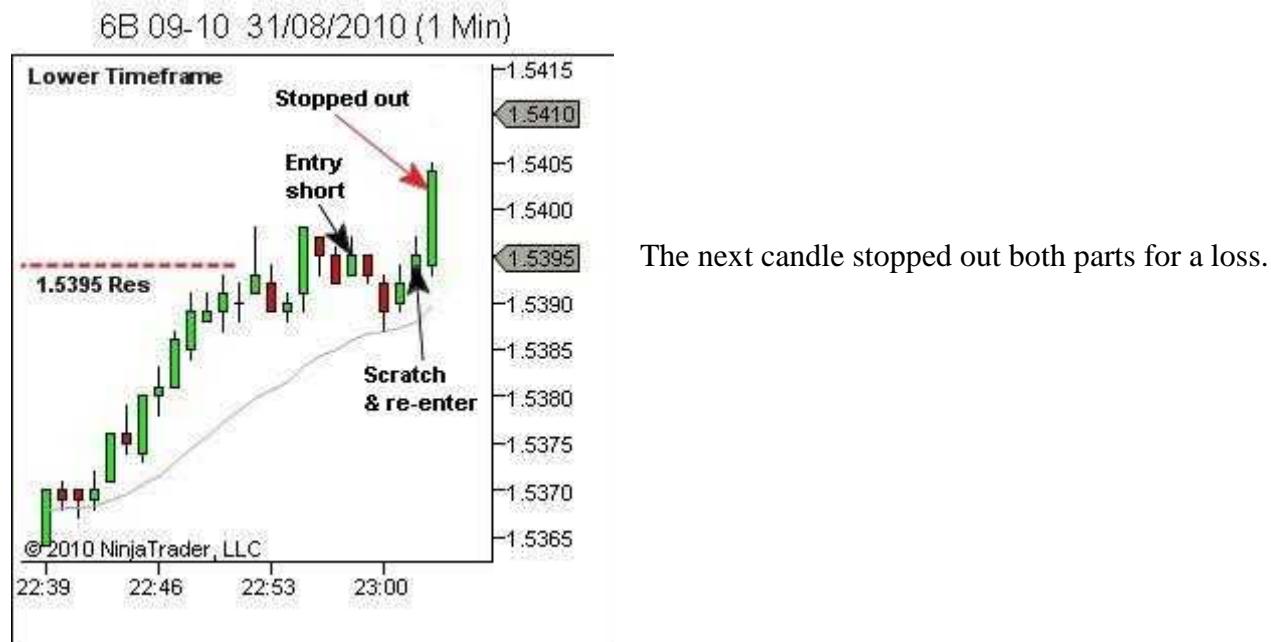


Figure 5.77 – Example 7 – Trade Management (3 charts)

Step 4 – Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

- | | |
|--|---------------------------|
| ■ Part one: Scratched at breakeven | 0 pips (less commission) |
| ■ Part one: Re-entered and stopped out | -7 pips (less commission) |
| ■ Part two: Stopped out | -7 pips (less commission) |

Let's conduct some review.

With the benefit of hindsight once completely out of the trade, it was easy to see the source of my uncertainty. I had convinced myself that I really liked this resistance area and was expecting it to hold. I was also partially influenced by the upper tails on the two 3-min candles, confirming

my belief in this resistance area. I failed to accurately assess the strength and weakness within the market, and the impact that would have on potential future price action.

This example showed strength into the resistance area. Short-term weakness at the resistance area is to be expected (resistance should provide some bearish orderflow to at least temporarily stall price). But this is not evidence of weakness in the bulls.

The most obvious way to demonstrate this is to compare the setups for examples 6 and 7.

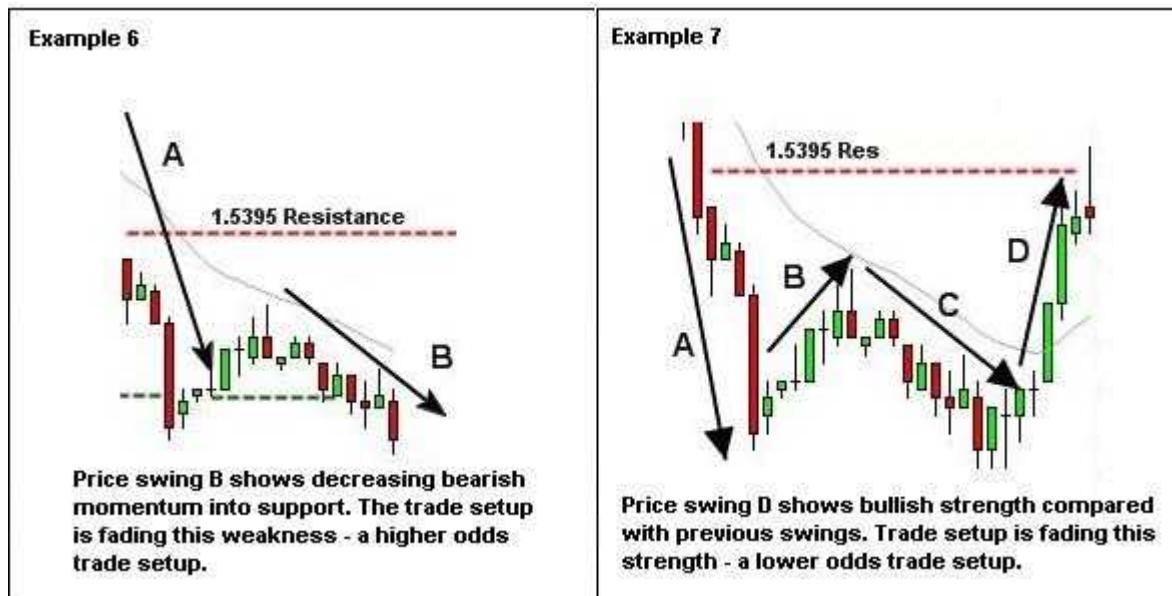


Figure 5.78 – Example 7 – Comparison with Example 6 Setup

Example 6 was fading a weaker move into support. Example 7 was fading a move of strength into resistance. The higher probability is always when fading weakness.

While fading strength can offer great R:R (when you get it right), they are lower probability trades and I'll usually only take them if they provide a much better one minute trigger (involving trapped traders). This example did not provide a great trigger.

If any trade was an option in this area, it was this one...



Figure 5.79 - Example 7 – A Better Trade Option

My analysis correctly recognised (initially at least) the strength into resistance, and an expectation of a breakout. In accordance with the First Principle of *future trend* direction (expecting a trend that shows no signs of weakening to continue in its current state), price action offered an excellent entry long via a 1-min spring pattern-based trigger. You had to be quick to see it – remaining focused and alert – as it occurred prior to the breakout. But it was a great opportunity.

In chapter 16 we'll talk about conducting setup and trade reviews via a market replay. This is a great example of a trade which will benefit from a good replay of price action, allowing us (with the benefit of hindsight) to re-feel the strength in the bullish moves and weakness in the bearish moves; allowing us to observe the signs that should have kept us out of the short opportunity; and experience the signs that may have led to an entry long. More on that later.

Here's another lesson (not for me, but for you)... even when stopped out of this trade, for the first couple of minutes I was watching patiently for a stall on the breakout, in anticipation of a re-entry short. It took that few minutes for me to realise that it wasn't coming, because the strength was to the bullish side.

Many traders have difficulty taking a loss, especially when they still expect they're right, but just slightly out with the timing. Some will question, "why didn't I just stay in and hold through the drawdown?", or "why didn't I average into it and get a better entry price?"

To do so is a loser strategy. My entry short was due to the resistance level holding. When it didn't hold any longer, my premise was proven wrong. It's time to be out.

If price did subsequently fall from here, maybe I could have profited. But what about the times when it doesn't fall (as in this example)? How far do you let it go against you, in order to prove you're right?

ALWAYS EXIT WHEN YOU'RE PREMISE IS INVALIDATED. NO QUESTIONS.

Enough of that!

To wrap up... poor analysis has led to a loss. However, risk was minimised, lessons were learnt, and it's time to move on to the next opportunity.

5.8 – Trade Example 8 – PB – Scratched – No Re-entry

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 2 Sep 2010

Time: 3/9/10 00:22 on charts (15:22 London)

Saving a loss can be as good as a win. It's still money in your pocket that could well have gone elsewhere. That's why I choose to operate with an active trade management policy, rather than just setting the stop and target and hoping for the best.

Step 1 – Define Structure



Figure 5.80 - Example 8 – Define Structure

At 00:22 we have support below the market at 1.5335 and resistance above at 1.5415, 1.5450, 1.5475 and 1.5490.

Step 2 - Define Trend

Price has been in a downtrend for the last two and a half hours, currently pulling back to the vicinity of the last swing high.

A break of the swing high, which then holds and shows price acceptance at these higher prices, would be required in order to trigger a change of trend.

Until then, the downtrend remains intact.



Figure 5.81 - Example 8 – Define Trend

Step 3 - Identify Strength & Weakness



Figure 5.82 - Example 8 – Identify Strength and Weakness

As shown above, the recent down move has been via two bearish swings, A and E, separated by an area of sideways congestion.

Note the nature of bullish momentum within the area of congestion. You'll note that the steep slope of C indicates it was actually stronger than B, but it was short-lived, failing to project beyond B's swing high. Swing D then showed reduced momentum. Bullish pressure was weakening throughout this area of congestion. This is a great example of how the analysis of momentum within an area of congestion can provide clues as to the possible breakout direction.

The key price swings for me are the two bearish swings, A and E, both showing a steep slope and therefore indicating strong bearish pressure.

However we also note that F, while slightly weaker than E, does show increased strength in the bulls. Demand has entered the market at these lower prices. E also failed to project as far as A, once again showing evidence of buying.

Overall, strength is still to the bearish side of this market. However the bulls are showing some signs of life. The next down swing will be a key indicator of future strength.

Step 4 - Identify Future Trend Direction

Step 5 – Visualise Future Price Action

Step 6 – Identify Areas of Trade Opportunity

Combining these three steps into one chart...



Figure 5.83 - Example 8 – Identify Future Trend Direction

My expectation is for continuation of the downtrend in accordance with the First Principle:

- We expect an up or down trend to continue in its current state until the next S/R barrier, unless displaying evidence of weakness within the trend.

There are insufficient signs of weakness within the trend at this stage, to have me looking for a complex pullback. My expectation is for a single pullback to the vicinity of previous swing highs, then a continuation lower (at least for one more push).

To validate my premise, I will need to see signs of weakening of the current price swing within the next few candles, such as reduced candle range and/or upper tails. This will be followed by a break lower, offering a PB style entry (if not entered earlier at a stall or 1-min pattern based trigger).

To invalidate my plan, price will need to either continue its current strength right through the previous swing high, forcing a change of trend direction. Or price could stall at the area of swing high resistance, but fail to carry through lower. This would indicate a lack of bearish pressure and a high likelihood of continuing higher (if it's not going down, then it'll probably go up!!).

Ongoing Market Analysis

Step 1 – Determine Candle Pattern Sentiment

Step 2 – Consider the Context

Step 3 – Does it Support my Premise?

Let's look at the next two *trading timeframe* (3 min) candles. Candle A is a mid-close range candle, while B is a high close range candle. Both have reduced price range (distance from low to high).

These candles are evidence of price slowing into the area of swing high resistance, validating our expectations. A break below this recent action will likely trigger the first of the stops for the longs, as well as bring in new selling. We now prepare for a possible PB opportunity.

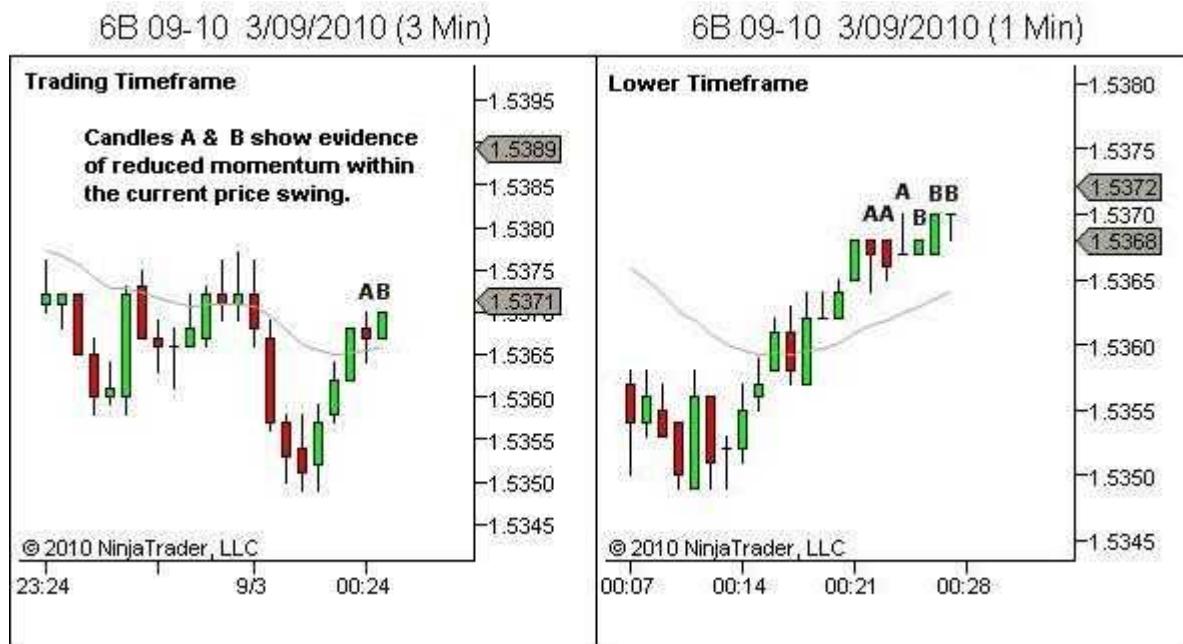


Figure 5.84 - Example 8 – Ongoing Market Analysis

Trading Process

Step 1 – Trade Preparation

Note that bar by bar ongoing analysis continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.

Based upon current price action we have the following potential trade parameters:

LWP is the point at which I expect the stops would start triggering, for those trading long in the pullback. This will be below the second-last 3-min candle (red mid-close range candle; spinning top). The LWP trigger would be at 1.5363.

S1 is above price action at 1.5372, providing a potential risk of 9 pips. If price falls to the LWP from this point, I do not expect S1 to be hit, and would like to be out of any trade. My trade premise would be invalidated.

T1 is above the lowest 1-min candle (the doji), providing a target of 1.5354. This is a potential profit of 9 pips, allowing a 1:1 R:R. T2 is lower at 1.5340, just above the 1.5335 support, offering a potential reward of 23 pips (2.5:1 R:R).

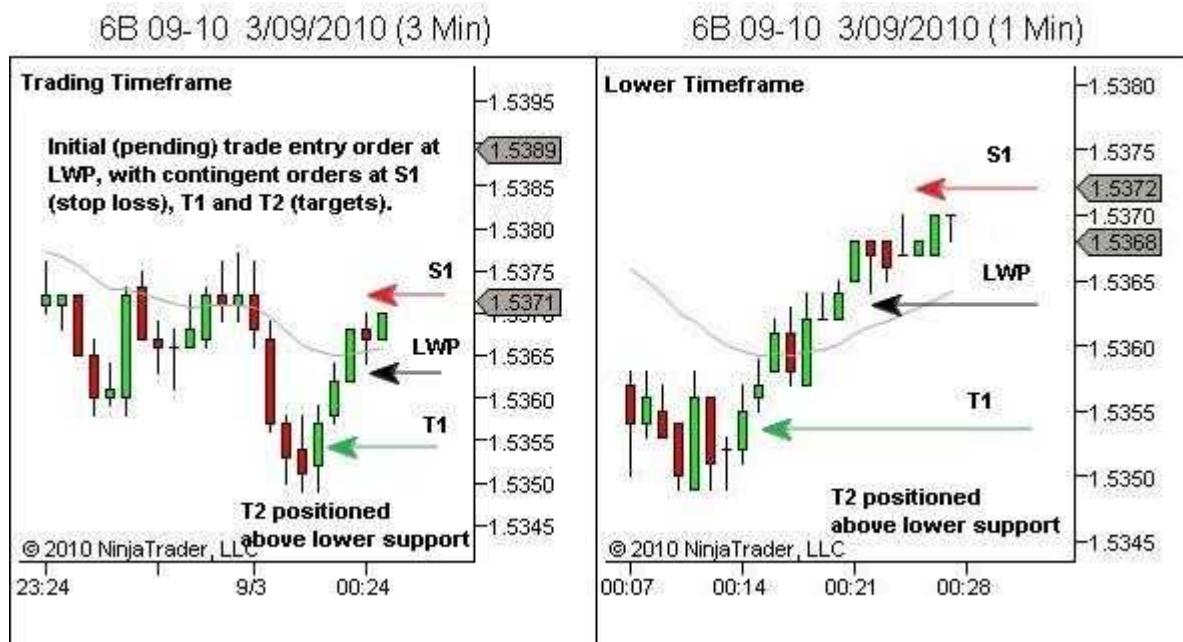


Figure 5.85 - Example 8 – Trade Preparation

Step 2 - Trade Entry

A stop entry order is placed at LWP, 1.5363, to ensure I don't miss entry in the event of immediately lower prices. While waiting for this to trigger, I will attempt to work a better entry through either a 1-min stall or pattern based trigger.

Let's look at the next 3-min candle.

Candle C has moved higher, above our previous high point. This has not yet triggered a change of trend, so I simply adjust my pending entry order as required, based upon this new information.

LWP moves up below the equal lows of candles B and C, to 1.5366. S1 is now 1.5378 (12 pips risk). T1 remains at 1.5354 (12 pips reward). T2 also remains at its present location 1.5340 (26 pips reward).

If price moves lower through LWP, I will be triggered into a trade.

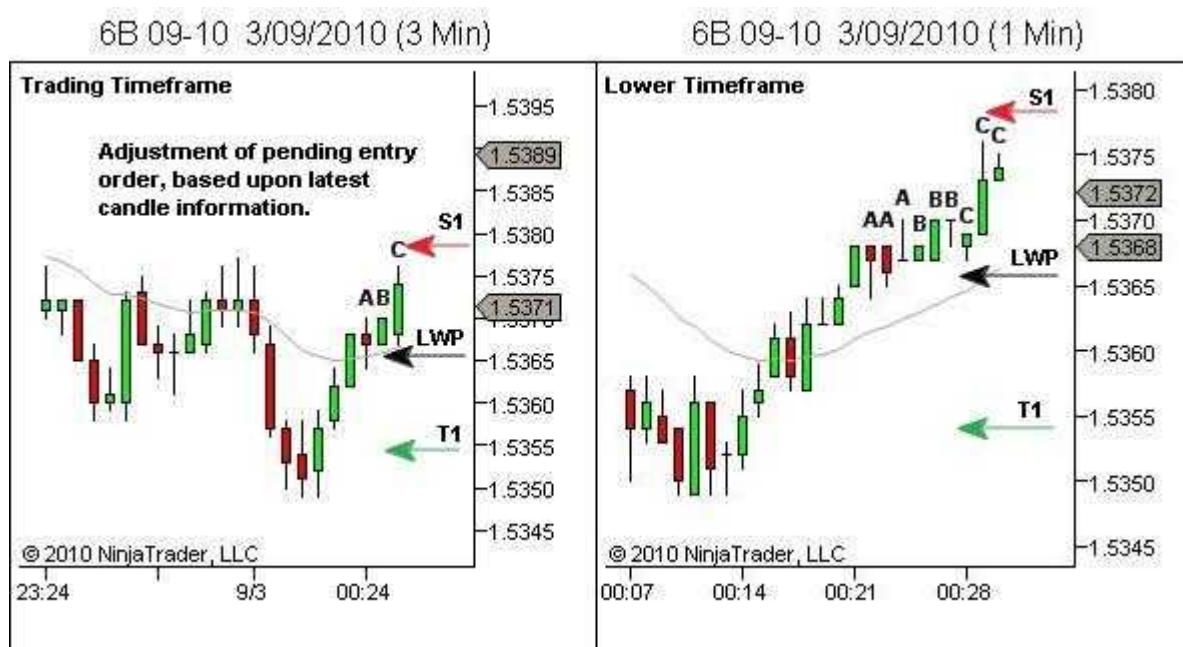


Figure 5.86 - Example 8 – Trade Entry Pending – Adjustment of Orders

Looking at the 1-min chart though, I see a potential pattern-based trigger.

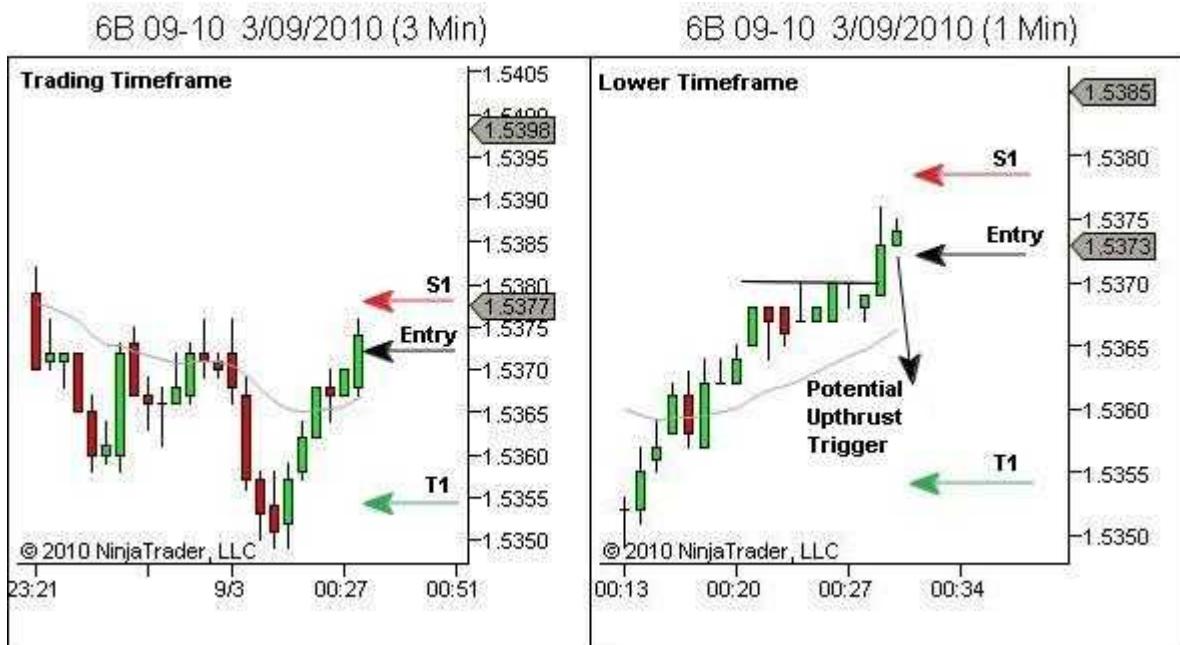


Figure 5.87 - Example 8 – Trade Entry – Potential Pattern Based Trigger

The latest 1-min price action shows a breakout of the recent highs which was unable to continue higher (upper tail, followed by mid-close range candle).

Although price has to move below the breakout candle to complete an upthrust pattern, it's likely an entry below the latest mid-close range candle would benefit from 1-min chart bearish orderflow, as some of the early breakout traders exit due to the stall. I expect that this will be sufficient orderflow to complete the upthrust pattern. Subsequent upthrust orderflow will move price further to our LWP, triggering the move to T1.

So, I decide to move our stop entry order to just below the recent 1-min candle. Although this is an early entry (and therefore a little more aggressive), it benefits from greater R:R if it is subsequently filled.

Continuation above recent highs will indicate a potential change of trend. If the current high gets taken out, I'll cancel my pending entry orders and reconsider my analysis.

Lower Timeframe Chart

6B 09-10 3/09/2010 (1 Min)

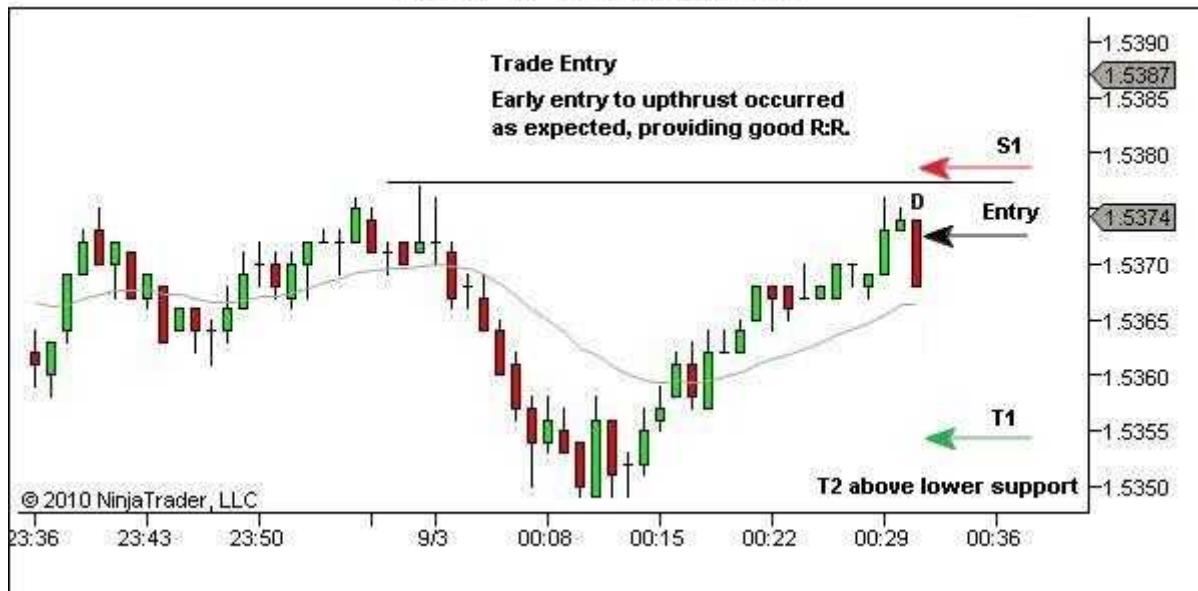


Figure 5.88 - Example 8 – Trade Entry

The next candle (candle D in the chart above) triggers the entry. As expected, this entry benefited from short-term bearish orderflow, driving our trade to immediate profit. Our expectation is for this bearish orderflow to continue lower, triggering more bearish orderflow as it passes through the LWP.

Trade entry parameters:

- Entry: 1.5372
- S1: 1.5378 (risk 6 pips)
- T1: 1.5354 (reward 18 pips) (3:1 R:R for part one)
- T2: 1.5340 (reward 32 pips) (5.3:1 R:R for part two)

Step 3 - Trade Management & Exit

Having not yet triggered LWP (which is required, to create the bearish orderflow to drive price to T1), this trade should be managed quite aggressively. Any failure to continue lower to LWP (or beyond), should raise some concern.

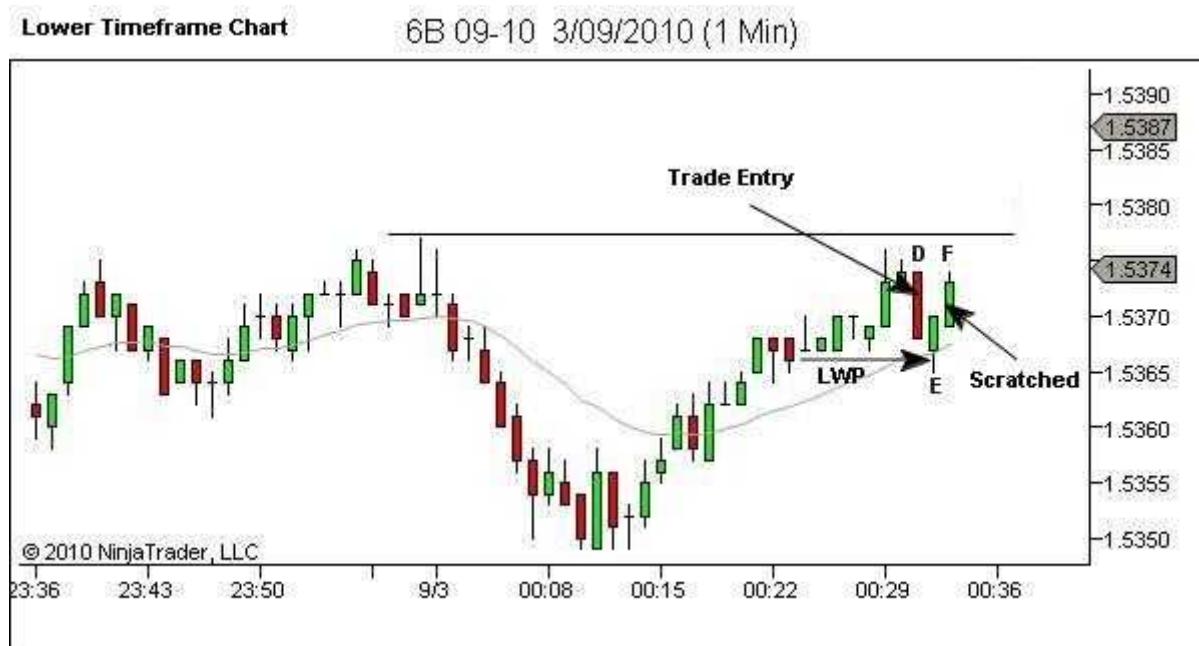


Figure 5.89 - Example 8 – Scratched

Candle E does exactly that... having moved through the LWP, price immediately rallied to close on the highs. Although a high close range candle is by itself considered slightly on the bullish side of neutral sentiment, this raises some concern at this point in time. It's a clear indication of a lack of bearish pressure. Price is not acting in accordance with our expectations, so the stop is dragged just above candle E and is quickly triggered by F.

The trade is scratched at 1.5371, for a total of +1 (less commission).

We now wait for a further entry trigger or stall.

Ideally at this point in time I'd love to see a break above the swing highs which rapidly reverses...

Lower Timeframe Chart

6B 09-10 3/09/2010 (1 Min)



Figure 5.90 - Example 8 – No Re-entry Opportunity

Candles G through J continued a stall at the swing high resistance. The bullish nature of F and H had me continuing to wait for a second upthrust, ideally above the swing high, rather than searching for a limit entry towards the top of the stall region.

The breakout and potential upthrust occurred at K (high close bull candle).

Trade entry now requires a rejection of higher prices and break back below the lows of K. I tentatively plan for a stop entry order below K. However price continues higher showing acceptance of the change of trend.

The price action provides no re-entry opportunity.

Step 4 - Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

- Part one: Scratched +1 pips (less commissions)
- Part two: Scratched +1 pips (less commissions)

This is basically a breakeven trade.

It's also another example where FX futures traders would have profited maybe a dollar or two, while spot forex traders would have lost a few pips due to the spread (more on that in chapter 6).

As mentioned in the introduction to this trade example, a scratched trade which saves us from a loss, is as good in my books as a win. It's money in my account, rather than someone else's.

Looking at the *trading timeframe* (3 min) chart for review purposes, we see that the setup was quite valid, however the increasing strength of the bullish swing leading into the setup, was followed by an inability for the bears to push price lower for one more swing. Their failure, followed by the subsequent break higher confirms strength now to the upside. We would now prepare for a potential long PB trade, following the weaker bearish pullback.



Figure 5.91 - Example 8 – Trade Review

5.9 – Trade Example 9 – CPB – T1 & T2 Achieved

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 6 Sep 2010

Time: 18:27 on charts (09:27 London)

Let's look at a simple example. It's an interesting one, as it occurs at a time when I usually won't trade, unless a perfect opportunity presents itself.

In the event of a public holiday in the US I will only trade during the UK session, and even then ONLY IF a great opportunity presents itself. Likewise for a public holiday in the UK; I'll only trade during the US session, and then ONLY IF a great opportunity presents itself. The default position in both cases is to NOT trade, as usually these sessions are dull and lifeless.

September 6th was the Labor Day Holiday in the USA. So, the UK session was open on the charts and glanced at from time to time (unlike my usual process which requires focus during every *trading timeframe* (3 min) candle).

Step 1 – Define Structure

Resistance sits above the market at 1.5490. Support is below at 1.5435, 1.5420 and 1.5390.



Figure 5.92 - Example 9 – Define Structure

Step 2 - Define Trend



Figure 5.93 – Example 9 – Define Trend

Following the open of the UK session, price tested the previous swing high and 1.5490 resistance area at A. Price was rejected at this level and so fell.

Had we been clearly focused on this session, this could have presented a great TST short opportunity at A.

The downtrend was confirmed at B.

Price is currently in a complex (3-swing) pullback after having tested the 1.5435 support area.

Step 3 – Identify Strength & Weakness

The *trading timeframe* (3 min) chart clearly shows greater momentum on the downswing, although the recent rally off support occurred on the largest range bullish candle we have seen since the start of the UK session. Being a high close bull candle, this has potential to indicate a change to bullish sentiment and an increase in strength to the upside.

However, it was followed by a mid close range candle (doji) indicating a failure to continue. We have mixed signals here.



Figure 5.94 – Example 9 – Identify Strength and Weakness

The *lower timeframe* (1 min) chart shows that the break to new highs on the complex (3-swing) pullback occurred on one candle only. Candle B strongly broke above swing high A, and then stalled for the following four minutes.

I still assess strength to be to the downside, although any continuation higher may indicate a change in sentiment.

Step 4 – Identify Future Trend Direction

Step 5 – Visualise Future Price Action

Step 6 – Identify Areas of Trade Opportunity

Steps 4, 5 and 6 are combined in one diagram.

As mentioned in the introduction to this example, I usually won't trade the holiday sessions, unless a good opportunity presents itself. A "good opportunity" is hard to define. But typically it involves a market that is moving (as shown via the strong momentum move from the 1.5490 resistance to 1.5435 support) and some sort of *textbook-perfect* trapped trader pattern, such as a complex (3-swing) pullback in the direction of the trend (as is setting up right now).

The market gained my attention during the fast downmove. The 3 swing retracement now has me focusing closely on price.

We're in that transition period after a test of support. Will price continue downwards to new lows (scenario A), return for a retest of support (scenario B) or continue higher confirming a reversal (scenario C)?



Figure 5.95 – Example 9 – Identify Future Trend Direction & Trade Opportunity

In accordance with the First Principle of *future trend* direction, I expect a continuation of our trend until I see evidence of weakening of the downtrend.

The strength shown on the downmove, and the pause after the recent push higher, has me expecting a scenario A or B, rather than C.

Any break below the recent pause (doji) will start to trigger stops from the longs, pushing price at least to retest the 1.5435 level (scenario B). A break of that level will trigger a much larger supply of bearish orderflow, as all the longs from the recent 3-swing pullback will exit, and new bears will enter short (scenario A). Scenario A is my expected outcome.

As such, I will skip the ongoing analysis and move straight to trade preparation.

Any break below current action will have me entering a CPB trade short. Any break higher will have me standing aside.

On CPB trigger, part one would only target the recent lows, in case I've incorrectly assessed the strength to the downside. Part two will skip the weaker 1.5420 support, taking us all the way to the stronger 1.5390 support, due to my expectation for a second strong push downwards.

Trading Process

Step 1 – Trade Preparation

Note that bar by bar ongoing analysis continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.

I don't expect much opportunity to work an entry here. It'll be a case of a break below the doji offering an entry short, or a break higher leading me to stand aside.

LWP is immediately below the doji at 1.5448.

S1 is tentatively placed above recent highs at 1.5454.

T1 is the lowest 1 min open/close above 1.5435 support, at 1.5438, offering greater than 1:1 R:R for part one.

T2 is above the next expected support at 1.5395 (part two reward 53 pips). The 1.5420 support is ignored, as I expect bearish orderflow to push price quickly lower for a second strong bearish price swing.

A stop entry order is placed at LWP, with S1, T1 and T2 attached as contingent orders.

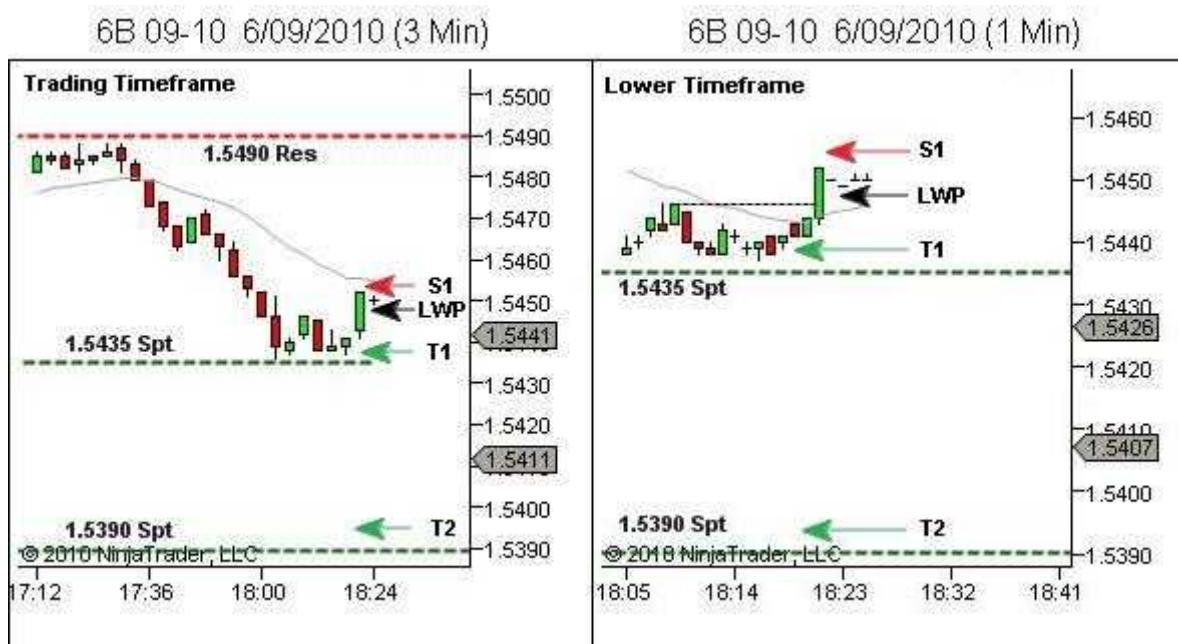


Figure 5.96 – Example 9 – Trade Preparation

Step 2 – Trade Entry

An entry is provided two minutes later as price reaches LWP 1.5448.

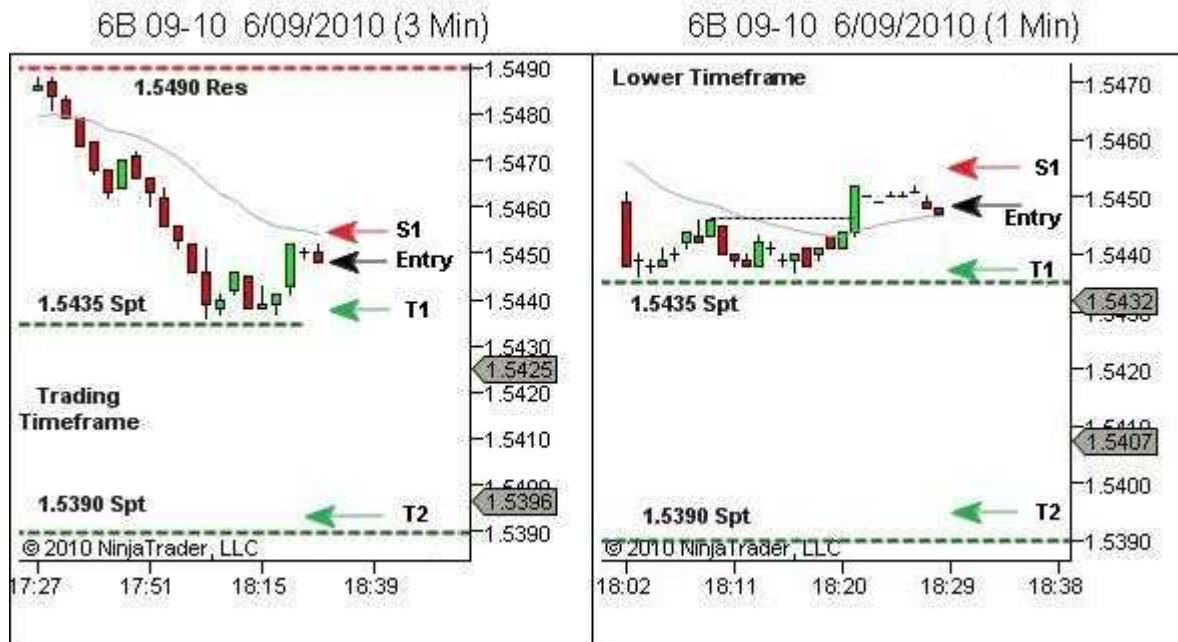


Figure 5.97 – Example 9 – Trade Entry

Trade entry parameters:

- Entry: 1.5448
- S1: 1.5454 (risk 6 pips)
- T1: 1.5438 (reward 10 pips) (1.5:1 R:R for part one)
- T2: 1.5395 (reward 53 pips) (9:1 R:R for part two)

Step 3 – Trade Management & Exit

As expected, the break below the doji has triggered the first of the pullback stops, pushing price quickly to T1.

The stop was moved from S1 to S2 (breakeven) after candle A (low close bear candle) closed 3 pips from the target.

T1 was achieved shortly after the open of the next candle.

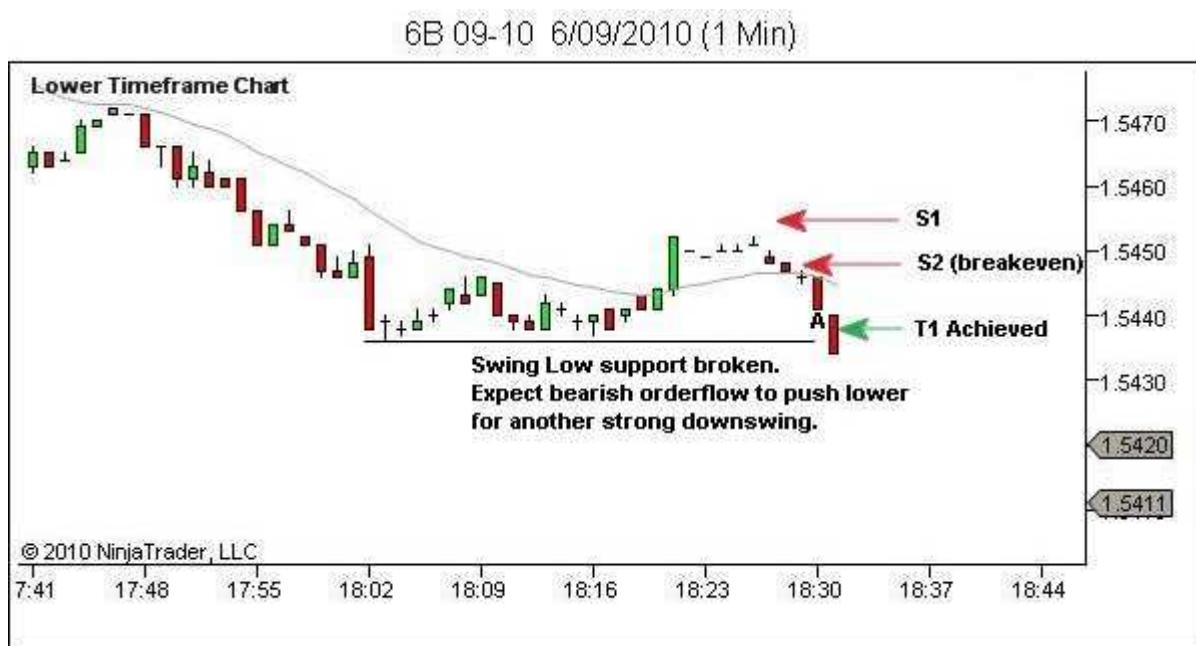


Figure 5.98 – Example 9 – Trade Management – Part One
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Price has also broken the previous swing low, as expected. Bearish orderflow should now push price lower for a second strong move downwards.

The part two stop is moved to breakeven (S2) on achievement of T1.

Like with part one, management of part two is quite simple, as the bearish orderflow met our expectations and continued strongly lower.



Figure 5.99 – Example 9 – Trade Management – Part Two

The stop was trailed above significant candles (those closing to new lows) or areas of congestion.

After candle A (low close bear candle), the stop was moved to S3, 1.5442.

After candle B moved below its preceding candle, the stop was tightened to S4, 1.5425. Note I did not wait for the close in this case. It was moved immediately the (weaker) 1.5420 support level broke. If price moved higher here, I would take this as a sign of unexpected bullish orderflow, and be happy to exit the market.

After the second doji at C, the stop was moved above the area of congestion to S5, 1.5415.

T2 was achieved in the following candle.

Step 4 - Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

- Part one: Achieved T1 +10 pips (less commission)
- Part two: Achieved T2 +53 pips (less commission)

5.10 – Trade Example 10 – TST – Scratched & Reversed – PB – T1 Achieved – Part 2 Stopped (Trail)

Initial Market Analysis

Market: 6B (British Pound FX Futures); equivalent to the spot forex pair GBP/USD.

Session: 10 Sep 2010

Time: 17:13 on charts (08:13 London)

In this example, we'll see price interaction with S/R, involving a scratched trade and reversal. I don't often reverse, as every trade has to stand on its own merits. A failure in one direction does not usually imply market movement in the opposite direction. However, in this case it did.

Step 1 – Define Structure

The *higher timeframe* (30 min) chart shows support below the market at 1.5335, with resistance above at 1.5410, 1.5440 and 1.5470. Note that the 1.5410 area is formed from Asian session price action, so is likely weaker than the higher resistance levels. Still, we watch price action at all levels to determine the likely impact on future trend direction.



Figure 5.100 – Example 10 – Define Structure

Step 2 - Define Trend

Figure 5.101 shows a *trading timeframe* (3 min) chart, allowing us to identify the trend.



Figure 5.101 – Example 10 – Define Trend

I would call this an uptrend, due to the UK session opening with price holding above the recent swing high at A.

However, the trend can be difficult to define early in a new session. If you called this a sideways trend, within the range of 1.5350 to 1.5410, I wouldn't have any problems with that at all.

As mentioned earlier, if in doubt just make a decision. Ongoing price action will correct it if you're wrong.

For me though, it's an uptrend.

Step 3 - Identify Strength & Weakness

The slope of the recent bullish move is much steeper than the slope of the previous bearish price swing, indicating strength to the upside.

However, it's worth noting that this is to be expected on the open of the UK session. The first price swing will more often than not be stronger than the last Asian session price swing.

Although we see bullish strength at this time, caution needs to be applied to our analysis. The next downswing will allow a more accurate assessment of momentum.

Note also, the upper tails on candles A and B, indicating some supply opposing our bullish price swing.



Figure 5.102 – Example 10 – Identify Strength and Weakness

The bulls are clearly in charge, but until we can make a more accurate comparison I will assess this as a normal rally, rather than a dominant sign of strength.

Step 4 - Identify Future Trend Direction

Step 5 - Visualise Future Price Action

Step 6 - Identify Areas of Trade Opportunity

As with previous examples, we will combine these three steps into one chart.

Based on current price action, my expectations are for a test of resistance which holds, in accordance with the Fifth Principle of *future trend* direction (We expect a test of our framework S/R to hold, unless strength is displayed on approach to the S/R boundary).

This provides a TST opportunity as demonstrated below.



Figure 5.103 – Example 10 – Identify Future Trend Direction and Areas of Trade Opportunity

The price action required to validate this plan is for continued signs of slowing momentum or bearish pressure as price rallies towards resistance. This will be evident by a reducing slope, further upper tails, and/or narrowing candles.

Should a TST trade be taken, trade management should be aggressive as price is at a critical area.

Strong continuation lower would confirm a reversal and quite likely lead to prices below the pre-session lows.

However a shallow or slow move off resistance would indicate a greater likelihood of a pullback rather than reversal, setting up for a further test of the resistance level. Should the price offer this scenario I will scratch and reassess, considering a potential PB entry long.

The premise will be proven invalid if the market continues strongly towards the level; likely indicating a breakout and then subsequent BOF/BPB opportunity.

Let's move on to the next few candles...

Ongoing Market Analysis

Step 1 – Determine Candle Pattern Sentiment

Step 2 – Consider the Context

Step 3 – Does it Support my Premise?

As previously, we will combine this 3-step dynamic bar-by-bar process into one summary discussion.

The next two candles are displayed below. Candle A is a mid-close bull candle showing some upper rejection. Candle B is a mid-close range candle, once again showing rejection of higher prices. In both cases, the range of the candle (high to low) is narrow.

Price is showing no signs of potential breakout at this stage. Our premise is supported by this action, and as price is now within the setup area we commence our pre-trade routine.



Figure 5.104 – Example 10 – Ongoing Bar-by-Bar Analysis

Trading Process

Step 1 – Trade Preparation

Note that bar by bar ongoing analysis continues throughout the trading process, both within the setup area prior to entry, and throughout the life of the trade.

The initial stop is defined as just above the resistance area at 1.5411. LWP is difficult to identify when price just grinds higher like this, but we should start to see some stops trigger below the last candle, so we place it at 1.5401. This trade is one that needs to work fast, or not at all. Price is at a level at which it should either reverse lower, or push higher through the weak Asian session resistance.

T1 is all the way down at 1.5368, just above the congestion at the swing low. The trade offers a great R:R. T2 is off the chart, at 1.5340.

We place the stop entry order at LWP and then work to enter at a better price if at all possible, based on a lower timeframe stall or pattern based trigger.

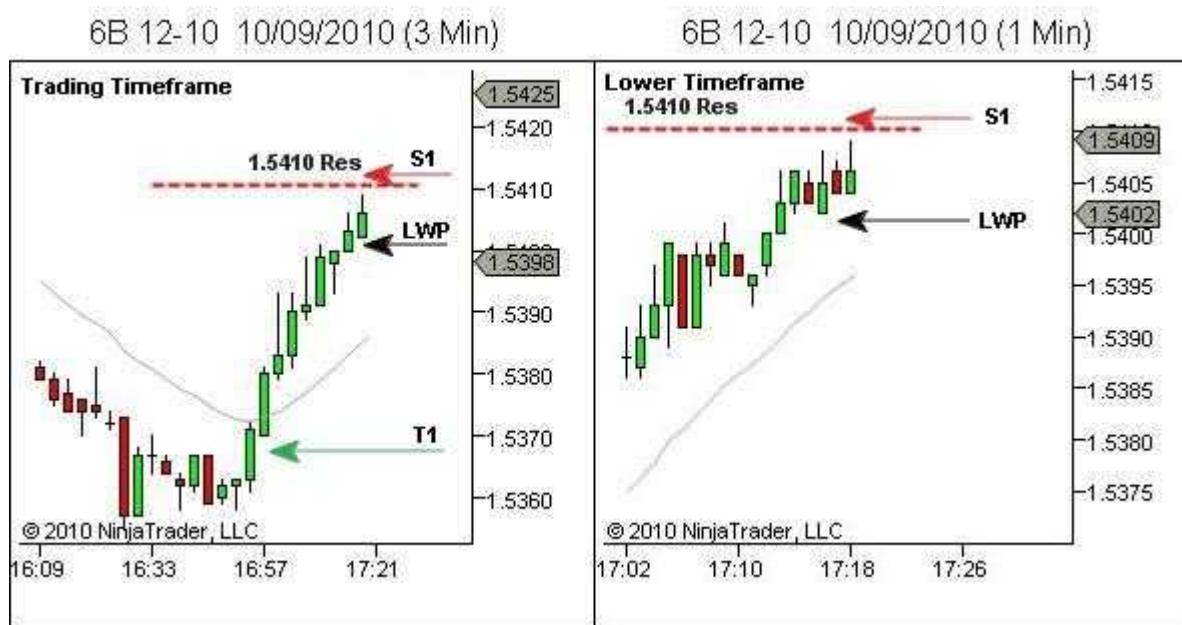


Figure 5.105 – Example 10 – Trade Preparation

Step 2 - Trade Entry

There is unfortunately no opportunity to work a better entry, as the trade is triggered at LWP.



Figure 5.106 – Example 10 – Trade Entry

Trade entry parameters:

- Entry: 1.5401
- S1: 1.5411 (risk 10 pips)
- T1: 1.5368 (reward 33 pips) (3:1 R:R for part one)
- T2: 1.5440 (reward 61 pips) (6:1 R:R for part two)

Step 3 - Trade Management & Exit

Note the last candle on the RHS of figure 5.106 above. The initial break through LWP did profit from bearish orderflow driving price initially in our direction, but it was short-lived. The lower tail indicates there is more demand at lower prices. This is a sign of strength. The stop for part one will be moved just above this candle.

Let's look at further price action.

The following three minutes failed to trigger the stop at S2, continuing lower. Candle A was able to reach new lows, however once again failed to bring in new selling, holding at this level to result in only a narrow range candle.

This lack of selling is a second failure to support my premise. The stop for part one is moved above candle A (breakeven).

Part one is stopped out on the next candle (the green high close bull candle).

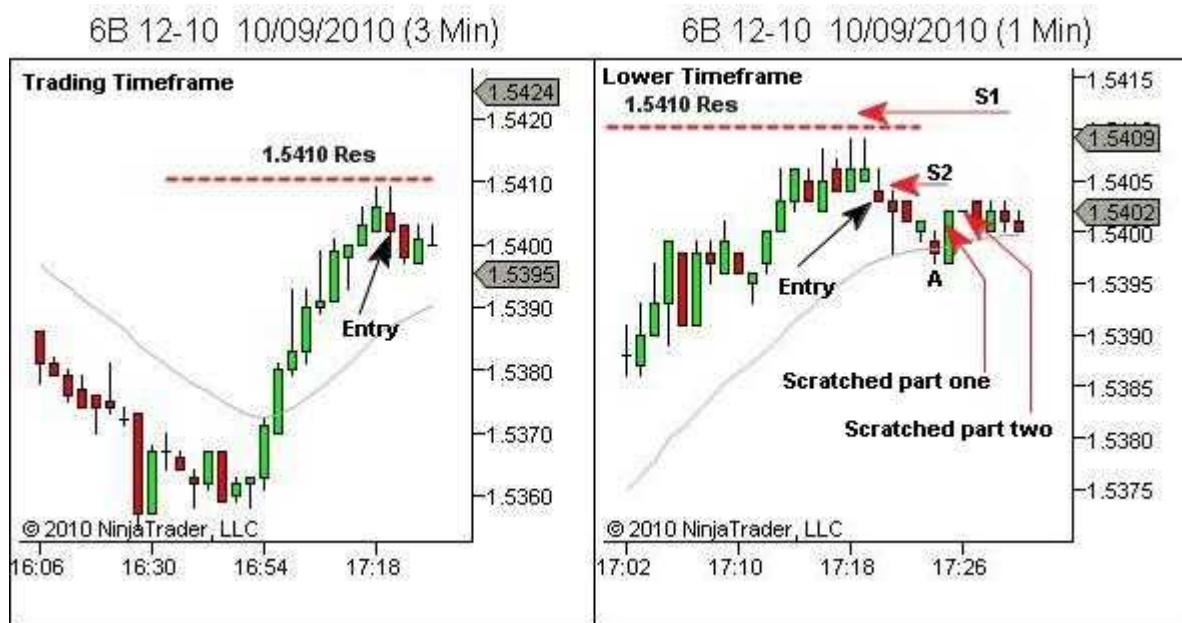


Figure 5.107 – Example 10 – Trade Scratched

Part two is held a little longer for reassessment. However I don't like this price action so scratch it within the next minute.

Part one scratched at 1.5401: 0 pips (less commission)

Part two scratched at 1.5403: -2 pips (less commission)

Let's look at the market analysis again, given the failure to push lower so far...

The original TST was treated cautiously, due to it occurring early in the session when direction has not yet been clearly defined. Testing the 1.5410 area of Asian session resistance, we expected either a quick and decisive reversal to lower prices, or a pause before continuing higher.

An entry was taken in order to profit if the first scenario occurred.

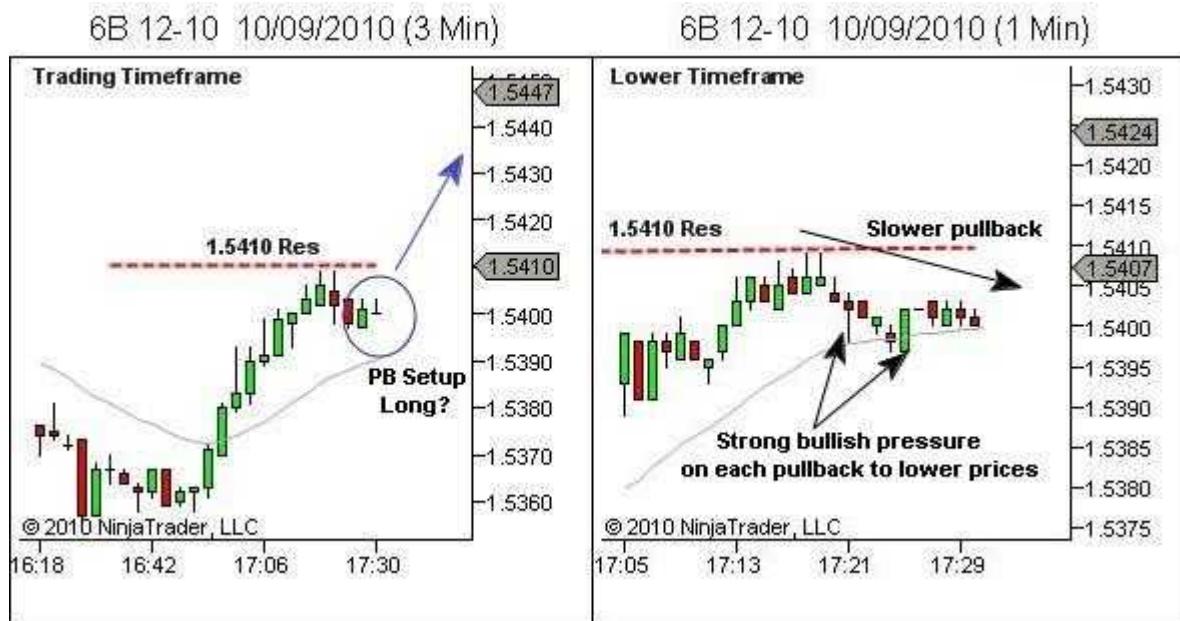


Figure 5.108 – Example 10 – Reassessment

The trade was scratched when (a) the pullback was slower than I liked, and (b) the lower timeframe action showed stronger bullish pressure entering the market whenever price reached new lows.

A failure to go down indicates stronger bullish pressure than anticipated, and a good possibility of continuation higher.

This would also offer a PB setup, which nicely demonstrates the way to enter a breakout, before the breakout occurs.

Should we take a PB entry long, and price does break out, I expect orderflow in this case will drive strongly to new highs. However, as always, price is watched closely following a breakout for potential breakout failure and/or breakout pullback opportunities.

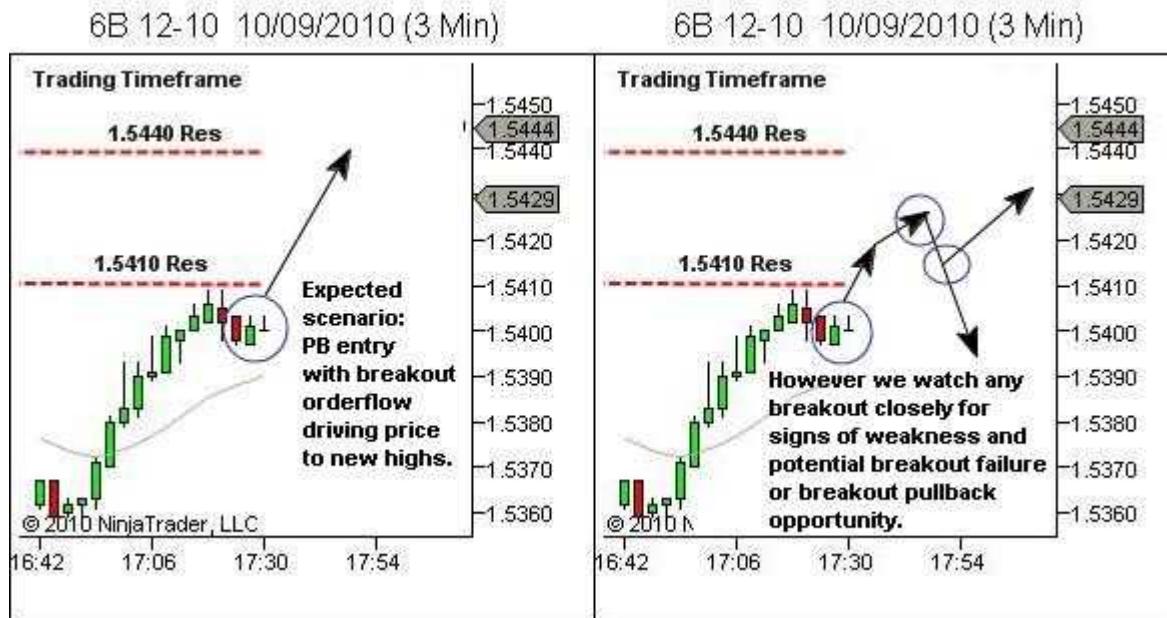


Figure 5.109 – Example 10 – Potential PB Opportunity – Entering Long Pre-Breakout

Step 1 – Trade Preparation

We now prepare for a potential PB opportunity, as shown below.

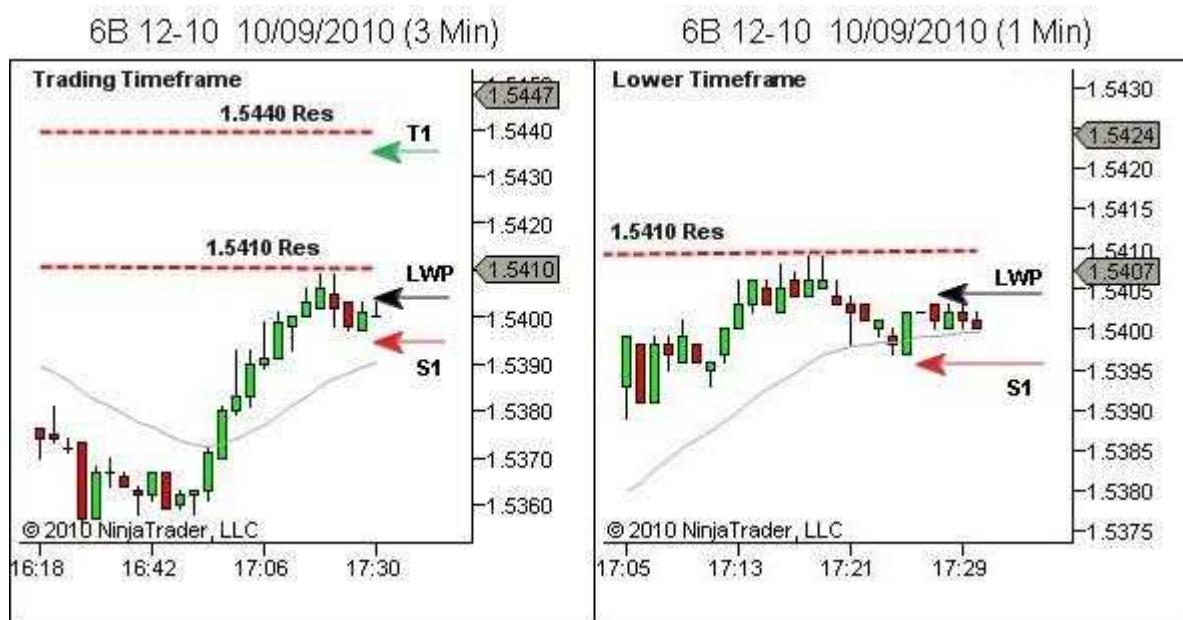


Figure 5.110 – Example 10 – Trade 2 Preparation

The stop S1 is placed below the pullback price action at 1.5396. If price hits this level then I'll exit and stand aside. After an attempt short and then another long, I'll need to step back from the market for a while and wait for clearer direction.

Target T1 is just below the 1.5440 resistance level, at 1.5435. Remember, I don't expect the previous 1.5410 swing high to offer much resistance – the scenario is for a pullback breaking to new highs.

T2 will be at 1.5464, just below the next resistance level (off the chart).

If price hits 1.5404, buy orders should be triggered sufficient to drive price to new highs. This will be our LWP.

A stop entry order is placed at 1.5404, and we watch for either the entry to trigger, or price to pull back further offering a lower entry (and requiring a possible reassessment of our analysis).

Step 2 - Trade Entry

Entry is triggered on the next candle.

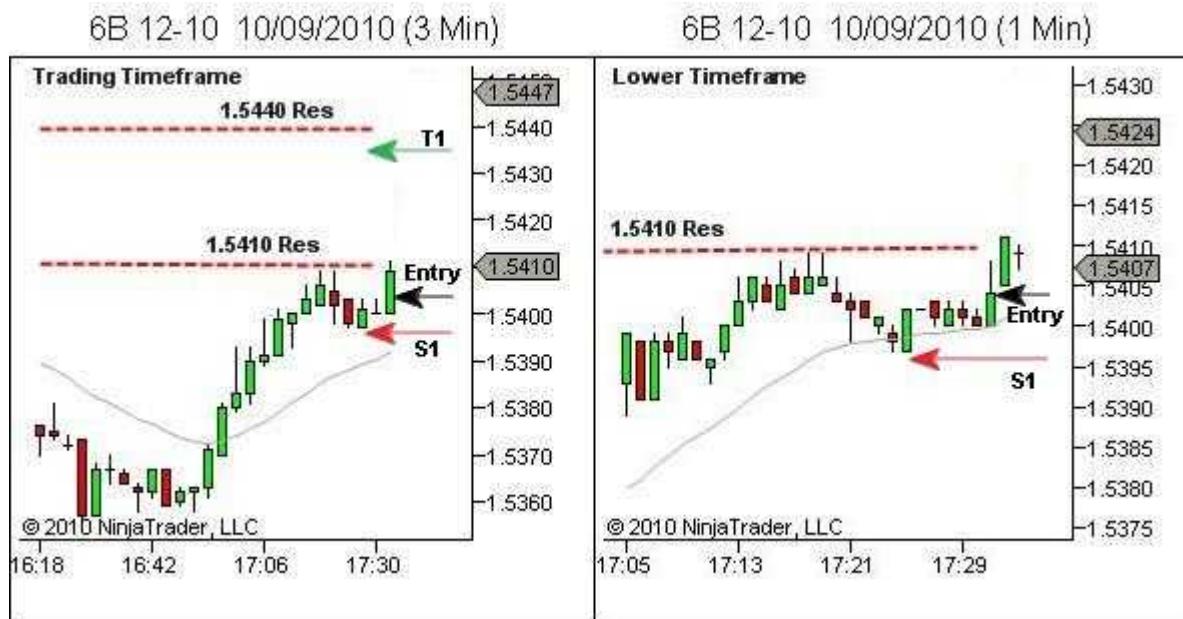


Figure 5.111 – Example 10 – Trade 2 Entry

Trade entry parameters:

Entry: 1.5404

S1: 1.5396 (risk 8 pips)

T1: 1.5435 (reward 31 pips) (4:1 R:R for part one)

T2: 1.5464 (reward 60 pips) (7:1 R:R for part two)

Step 3 – Trade Management & Exit

In figure 5.112 below, we see candle A triggering the entry, followed by candle B making the breakout to new highs.



Figure 5.112 – Example 10 – Trade 2 Management & Part One Exit

Trade management involves moving the part one stop behind significant candles, in order to avoid giving back profits.

On achieving the breakout, the stop is moved to breakeven (S2).

On the close of candle D, the stop is moved to S3.

On the close of candle E, the stop is moved to S4.

And as price approaches the target in candle F, the stop is tightened up below that candle to S5. T1 is achieved for 31 pips profit on part one.

For part two, I actually moved its stop to breakeven on the close of the one minute candle D (figure 5.112). This candle confirmed the breakout. If the breakout should fail, and I remain long (failing to recognise or react to the BOF opportunity), I do not want to be in this trade below breakeven.

Trade management beyond breakeven (S2) was managed in much the same way – trailing the stop below significant candles or price action features (swing lows). Refer to figure 5.113.

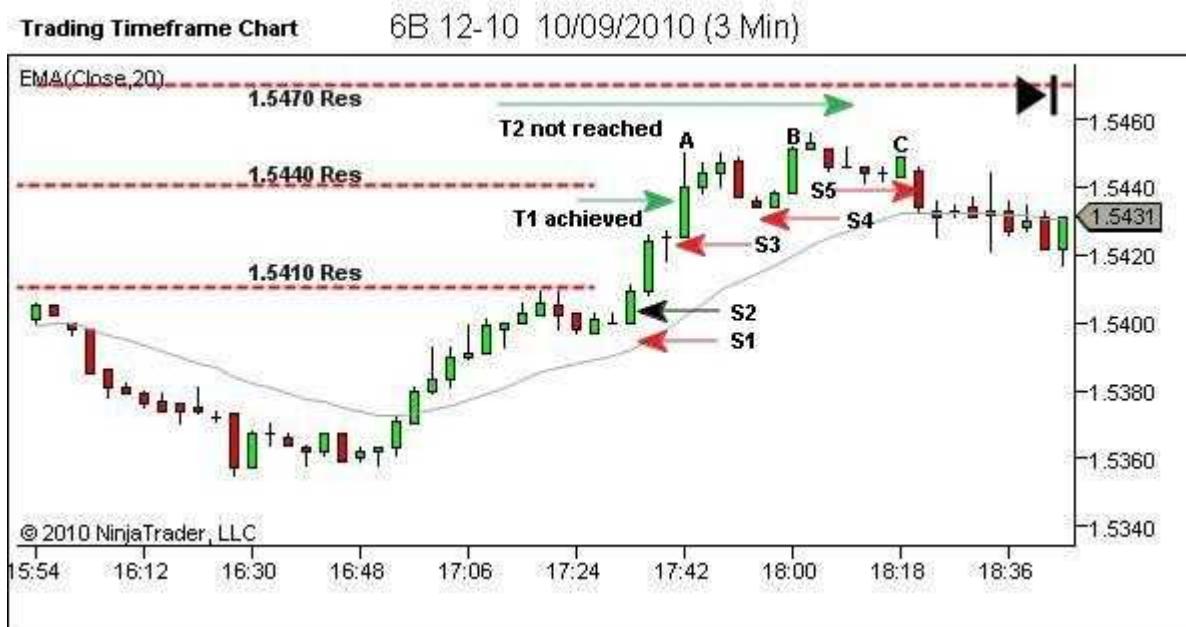


Figure 5.113 – Example 10 – Trade 2 Management & Part Two Exit

The stop was moved to S3 on close of candle A; S4 on the close of candle B and confirmation of the first pullback; and S5 on the close of candle C and confirmation of the second pullback.

As price clearly slowed through A to C, the exit was worked by moving the stop rather than pulling target T2 closer to price. This allowed control of risk while leaving the full profit potential available.

The exit was at S5, 1.5440.

Step 4 - Post-Trade

After reconfiguring our trading platform and confirming we are flat, our focus then returns to price in preparation for further setups.

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When time allows, we update our trade log and record any significant observations regarding market structure or price action, our trading process and our physical and psychological state.

Results:

Trade One:

- Part one: Scratched 0 (less commission)
- Part two: Scratched -2 (less commission)

Trade Two:

- Part one: Achieved T1 +31 (less commission)
- Part two: Achieved T2 +36 (less commission)

5.11 – Trade Example Summary Notes

The previous ten sample trades have obviously not shown all possible market scenarios – I'd love to be able to do that but it's just not possible.

They do however provide realistic examples of the analysis and trade process defined in chapters 3 and 4.

In writing a book such as this, the temptation naturally exists to provide example trades showing massive wins – every trade achieving T1, with T2 running to 50 or 100 pip exits. Every example would look like this...



Figure 5.114 – How Trading Systems are Usually Promoted

That's not reality though. Those trades are an exception, with the majority being scratched, small profit or small loss trades.

I've tried to avoid temptation, and provide more realistic trade examples.

At the moment you have an understanding of the processes I use to trade – at least at a conceptual level. Real learning is yet to come. Through implementation of the Volume Four and Five processes, you'll develop trading competence and confidence, as you *learn to trade*, and perhaps even adapt the strategy to suit your own psychological and personality needs.

More on that in Volumes Four and Five!

A final word on the examples... as mentioned throughout, commissions are to be taken out of the results. For those not familiar with the FX Futures markets, as used in the example, these commissions will typically be less than one pip per round turn (buy/sell). If trading spot forex, this cost will not apply. However you'll incur potentially greater cost through the fixed spread and the requirement to buy at the ASK and sell at the BID. We'll discuss that more in the next chapter, *Other Markets, Other Timeframes*.

Chapter Six – Other Markets, Other Timeframes

6.1 - Other Markets, Other Timeframes

The markets and timeframes discussed so far will not suit all traders.

Operating in the way I have presented the YTC Price Action Trader requires being present at the screen for at least half a session, if not a whole session, typically aiming for an average of around one trade per hour.

Not everyone is interested in this.

Some prefer longer timeframes. Some prefer shorter timeframes.

Likewise, not everyone will be interested in the markets that I enjoy trading (6B, YM, TF).

The good news is that the strategy can be adapted to any market and any timeframe, provided sufficient liquidity and sufficient price swing to allow profits much greater than costs.

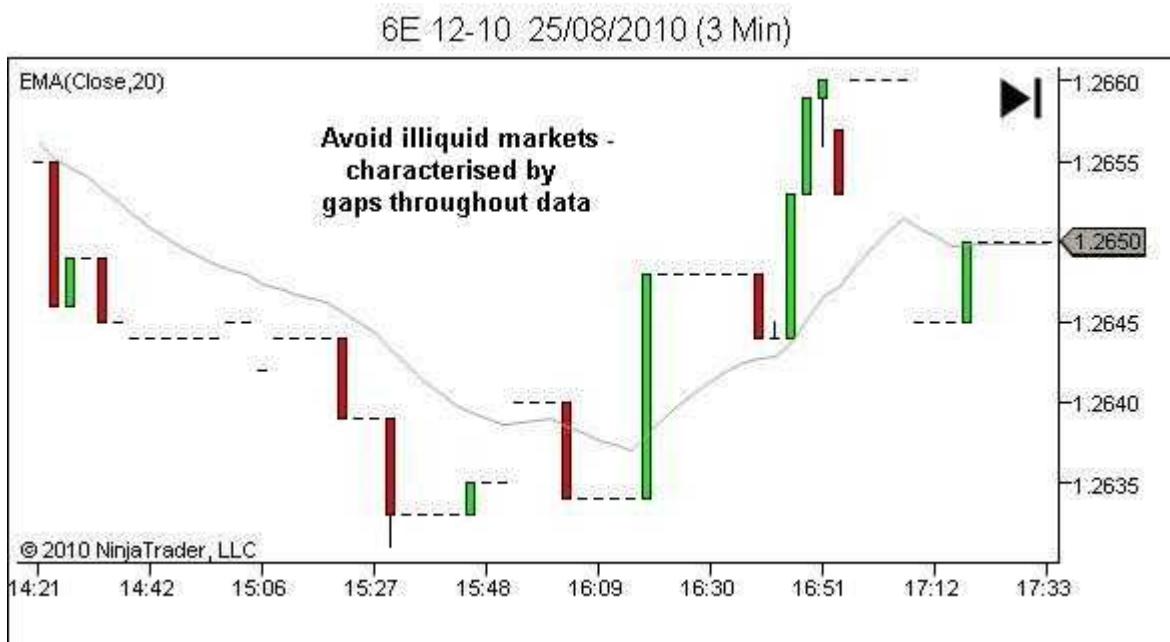


Figure 6.1 – Avoid Illiquid Markets

Avoid illiquid markets; easily spotted via charts which show many gaps throughout the data where trading has not occurred.

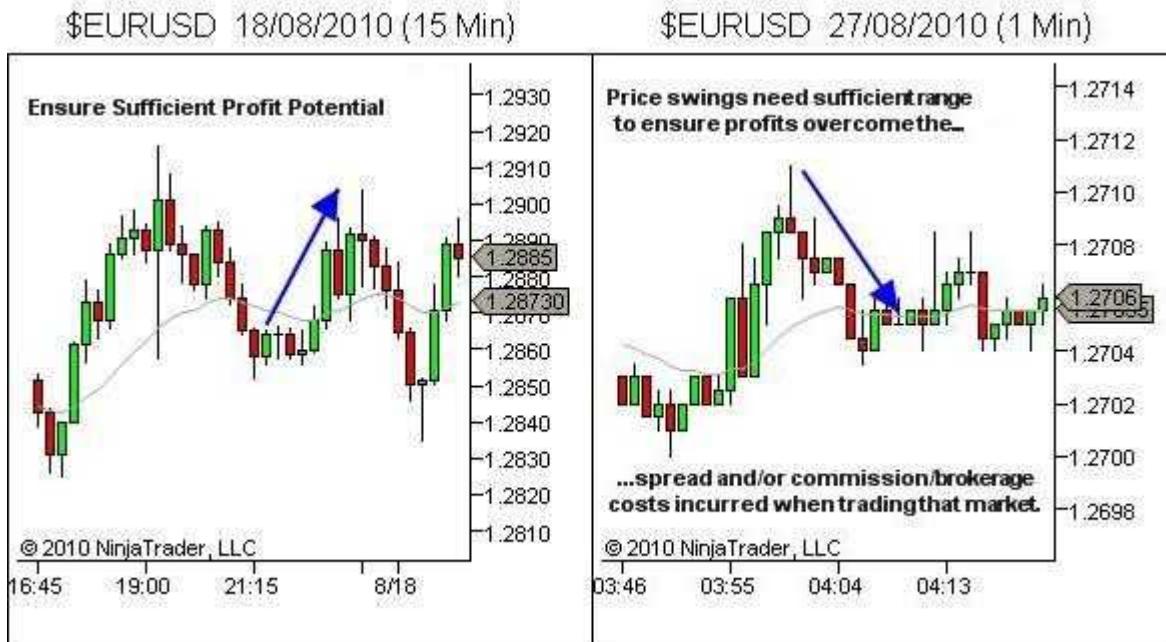


Figure 6.2 – Ensure Sufficient Profit Potential

Your *trading timeframe* chart also needs to provide sufficient profitability.

The 15 min EUR/USD chart on the left of figure 6.2 has average price swings in the vicinity of 30 pips, easily sufficient to ensure profit potential after taking the 2 pip spread into account.

The 1 min EUR/USD chart shown on the right hand side, provides average price swings of around 6 pips. With a 2 pip spread it'll take 2 pips of movement just to breakeven, leaving only 4 pips to achieve and take profits. This is not likely to be a long-term profitable business model.

The greater the cost of trading, the higher timeframe will be required to provide sufficient profit potential to overcome costs.

That being said, let's have a look at some examples of the strategy applied to forex, emini-futures and stocks.

6.2 – Examples - Forex

The examples used throughout this book have involved charts for 6B, the British Pound FX Futures market.

Given the explosion in popularity of the spot forex market over recent years, many of you will not be interested in FX Futures.

The good news though is that 6B charts are *essentially the same as GBP/USD*. This is demonstrated in the charts below, displaying 6B 3 min on the left and GBP/USD 3 min on the right (for the setup used back in Trade Example 1 of Chapter 5). Note the similarity.

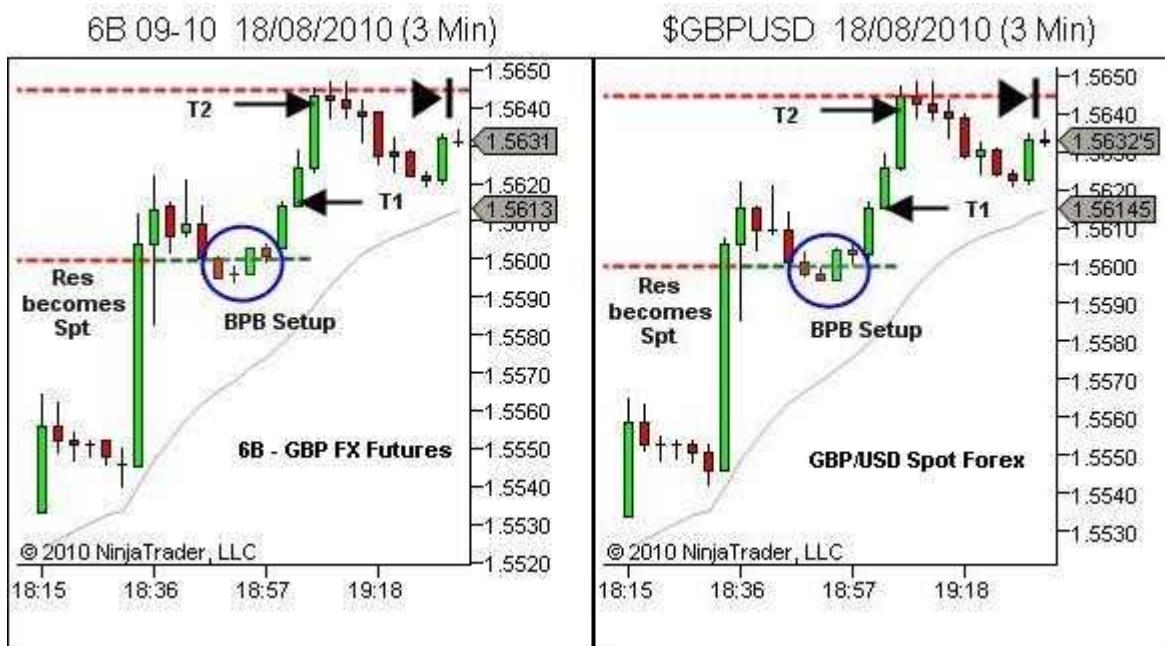


Figure 6.3 - FX Futures vs Spot Forex

Every 6B example used throughout this book could have been replaced with a GBP/USD chart; accepting that the spread would have become a factor in the trade selection and trade management (more on that in a moment).

In fact, up until mid-2009 I was trading this strategy with GBP/USD, using the 60/30 min chart for higher timeframe structure, 5 min chart for trading timeframe and the 1 min chart for lower timeframe. The following chart displays the same BPB setup using the 5 and 1 min timeframes.

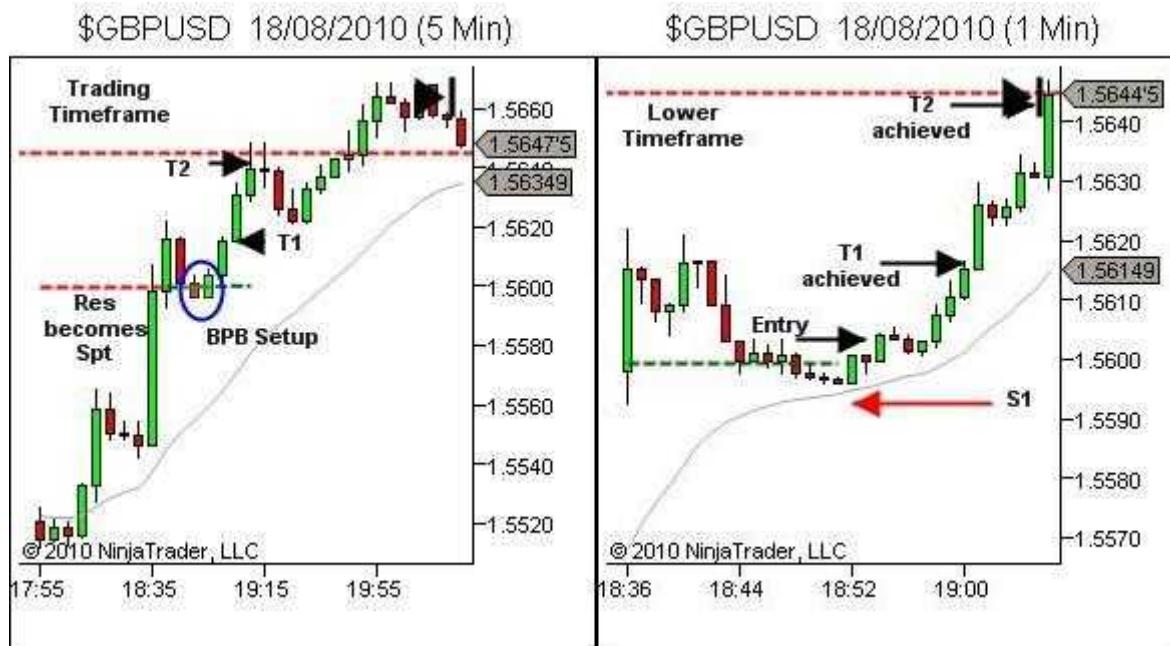


Figure 6.4 - GBP/USD – 5 & 1 Min Timeframes

Figure 6.5 below demonstrates slightly higher timeframes:

- Higher Timeframe: 60 min
- Trading Timeframe: 15 min
- Lower Timeframe: 5 min

Here we see the *trading timeframe* chart; a 15 min GBP/USD chart demonstrating five setups in the US forex session following release of the Existing Home Sales report (PB long with the trend; lower momentum TST of resistance; second PB long; second TST at resistance; and a PB short after change of trend).

Entry triggers would be taken from the 5 min timeframe.

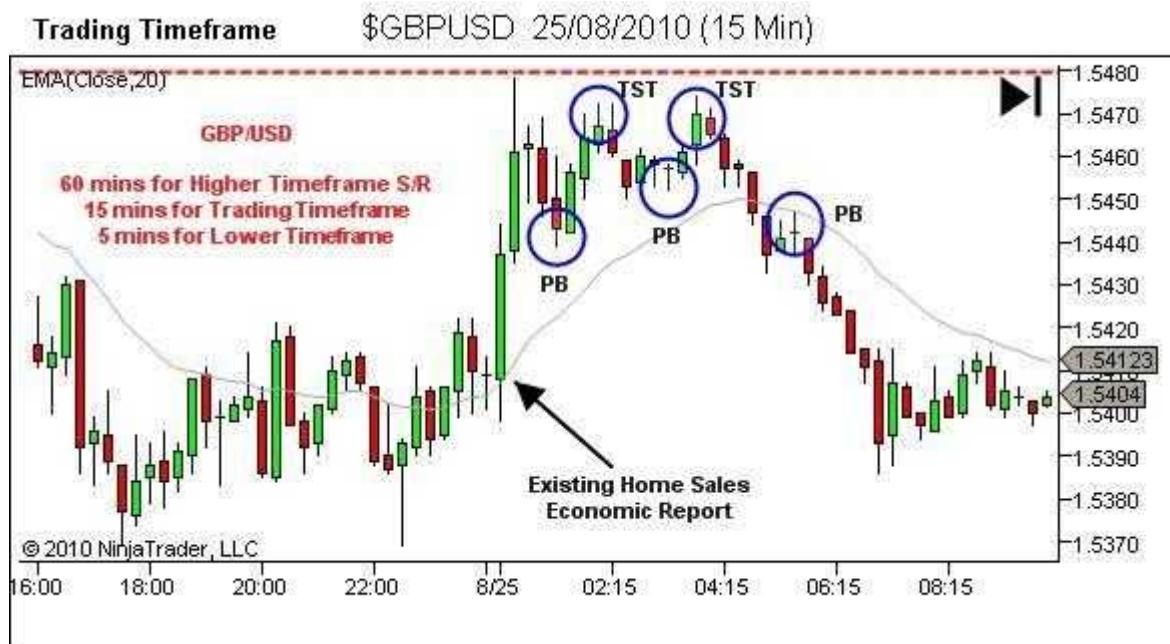


Figure 6.5 - GBP/USD – Trading Timeframe – 15 Min Chart

For those desiring larger timeframes, the following is a EUR/USD chart based on the following scenario:

- Higher Timeframe: Daily chart
- Trading Timeframe: 4 hour
- Lower Timeframe: 1 hour

The chart below demonstrates the *trading timeframe* (4 hours), showing a change to downtrend, with 3 pullback entries and one test of support.

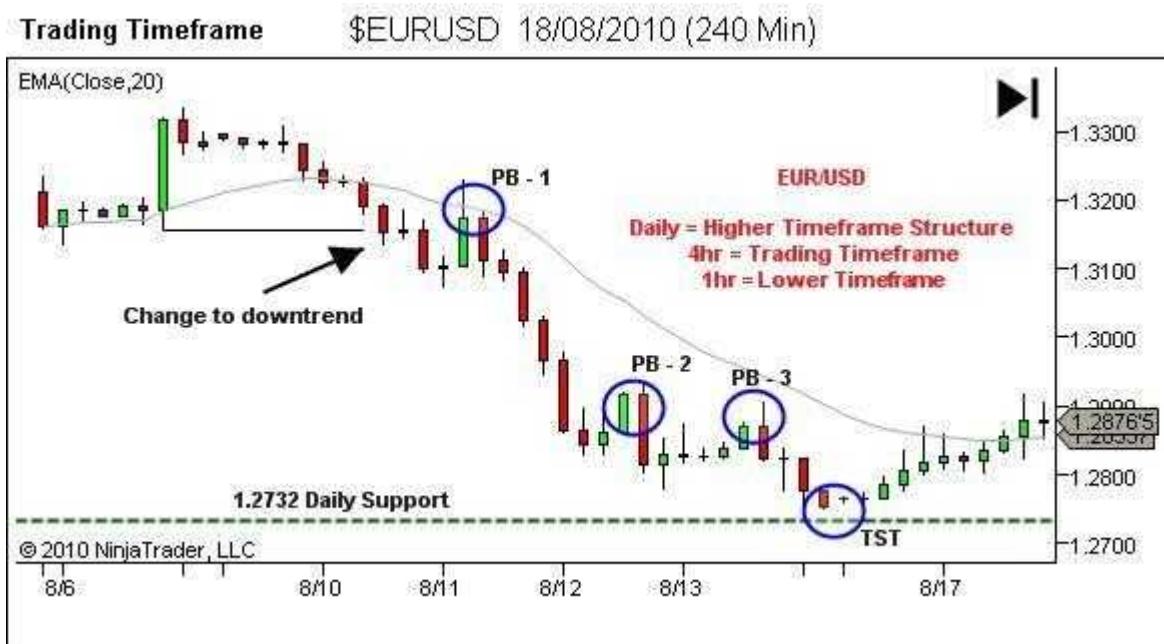


Figure 6.6 - EUR/USD –Trading Timeframe - 4 Hour Chart

As always, entry triggers are managed via the *lower timeframe*. In this case it's the 1 hour chart, as demonstrated in figures 6.7 and 6.8 below which reproduce our 4-hour setups PB-1, PB-2, PB-3 and TST.



Figure 6.7 - EUR/USD – Lower Timeframe - 1 Hour Chart (1 of 2)

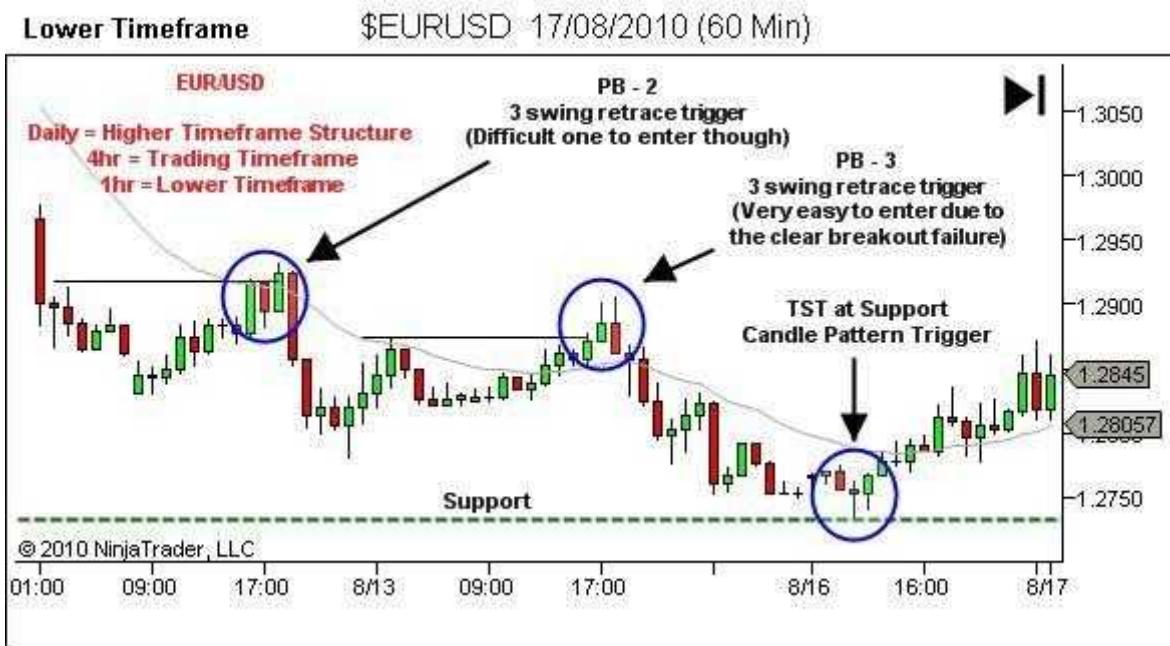


Figure 6.8 - EUR/USD – Lower Timeframe - 1 Hour Chart (2 of 2)

The following chart is based upon longer timeframes, likely suitable for those trying to fit their trading around a job.

- Higher Timeframe: Weekly chart
- Trading Timeframe: Daily chart
- Lower Timeframe: 4 hours

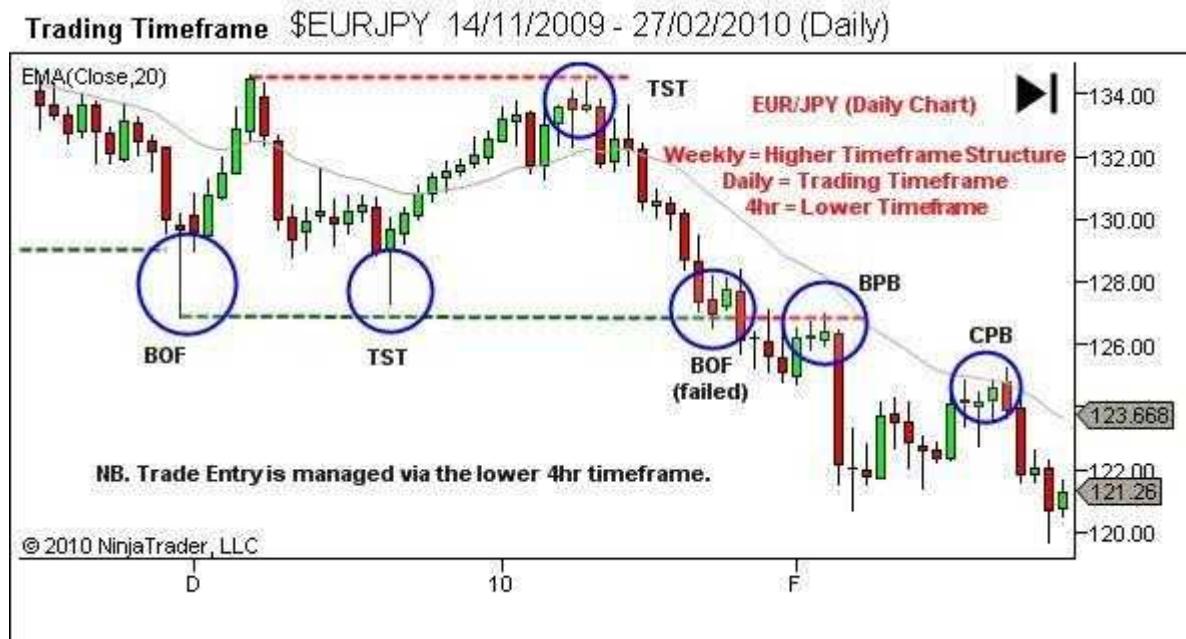


Figure 6.9 - EUR/JPY –Trading Timeframe - Daily Chart

This *trading* timeframe defines the trend and the setup areas. Entries would be timed off the 4 hour chart, assuming that suited your circumstances.

6.2.1 - Additional Forex Considerations

Spread

A further consideration for forex is the nature of the spread. Forex is widely advertised as being commission free, or having no costs. Nothing could be further from the truth. Your broker is not in the business of offering charity and helping you achieve trading success. They profit through offering retail spreads that are wider than the spreads they themselves pay.

In forex, you are limited to transacting at market prices – ie. you can only buy at the current ASK price and you can only sell at the current BID price.

This is in contrast to the FX Futures markets where you have greater flexibility through limit orders, and can (assuming filled by someone willing to take the opposite side of your trade) buy at the BID and sell at the ASK.

As such, forex traders start their trades at a disadvantage. Trading GBP/USD with a 3 pip spread for example, the market must move 3 pips before your trade gets to breakeven. Whereas that same 3 point movement in the FX Futures may have you at up to 3 points profit.

NOTE: This is not to say that FX Futures are necessarily better than Spot Forex. Each market has its advantages and disadvantages. It's beyond the scope of this book to discuss the pros and cons of each market. Carry out your own investigation in choosing your preferred market. However, in comparing FX Futures with Spot Forex, at very low timeframes, the reduced costs of FX Futures give it a clear advantage providing you can afford the larger position sizes. At higher timeframes, with greater profit potential in price swings, this fixed spread is less of a disadvantage.

In my own forex trading experience, I recommend absolutely no less than the 60/30, 5/3, 1 min timeframes in this market, and even then only for the pairs which offer a higher volatility to spread ratio. I've only traded GBP/USD on this short timeframe. I suspect EUR/JPY may offer sufficient movement as well (trial it if you're interested). (NB. Maximum GBP/USD spread of 3 pips).

All other pairs (in my opinion) do not have sufficiently large price swings to overcome spread costs on these lower timeframes. Higher timeframes will be required.

Which timeframes you choose will largely depend on your own personal circumstances and lifestyle. Higher timeframe examples have been shown in figures 6.5 to 6.9 above.

NOTE: This is also applicable to CFD traders, who also incur a fixed spread with the requirement to buy at the ASK and sell at the BID.

Number of Pairs to Trade

Your selection of timeframe will also impact the number of currency pairs you can trade.

I personally find that using the timeframes in this book (30/3/1) I can only focus on one instrument at a time. Others might be able to manage two. I would suggest no more than this, otherwise your focus will be spread too thin leading to potential lost opportunity and frustration.

You may of course wish to monitor a larger basket of currency pairs. Then select the one or two that you'll monitor during the current session, based upon some selection criteria which indicates a higher likelihood of your preferred environment (trending or ranging). The key point is though, that you only monitor one to two (maximum) during the session hours.

Higher timeframe traders, on the other hand, will have sufficient time to monitor a larger number of currency pairs.

Forex traders have only a small universe of available instruments, so may choose to limit their exposure to a basket comprising the majors and other higher liquidity pairs, such as GBP/USD, EUR/USD, USD/JPY, USD/CHF, AUD/USD, USD/CAD, GBP/JPY, EUR/JPY.

Session Opening

You'll need to consider how you manage session openings, when trading forex at major session open times (UK forex open, US forex open, Asian forex open).

The opening of a session can involve an increase in trading volume and potential change of sentiment and market direction.

I obviously have an assessment of trend, strength and weakness, and *future* trend direction, from the pre-session data. However I will be prepared to adjust my *future trend* premise, by treating session opens as if they were an S/R area that had just been broken.

Just like watching a broken S/R area for signs of strength or weakness, to give us a feel for a potential breakout failure and change of direction, or breakout pullback and continuation, I'm watching the initial few minutes of *new session* data to identify signs of strength and weakness. Future trend direction is likely to be in the direction of strength and against the direction of weakness.

Don't be in a hurry to trade though, until you have clearly established your bias for *future trend* direction. Sometimes it's immediately obvious. Other times the market can take a while for market sentiment to become clear.

News / Economic Releases

Lower timeframe forex markets are particularly susceptible to high volatility at times of regular news (economic) releases.

My current source of economic news events is listed on my Resources Page, <http://www.yourtradingcoach.com/Trading-Resources.html>, under the heading, Business Management.

You MUST be aware of the timings for release of these news events.

- My aim is to not initiate any trade just prior to a news release which is likely to move price (high or medium volatility), unless it's expected that the trade should be complete or showing significant profit, by the time the release occurs.
- If I have an open trade at the time of a regular news release, I will either close it out prior or tighten stops, as determined by my analysis.

Your number one priority is always risk management. These news releases pose significant risk if you're not aware of their timings.

6.3 – Examples – Emini Futures

The following charts demonstrate application of the YTC Price Action Trader strategy on various emini-futures charts, on a number of short daytrading timeframes.

First up, in figures 6.10 and 6.11 we see two examples of YM 3 min charts. This is the *trading timeframe*, based upon the same timeframes used throughout this book:

- Higher Timeframe: 30 min
- Trading Timeframe: 3 min
- Lower Timeframe: 1 min



Figure 6.10 - Emini Futures – YM Trading Timeframe - 3 Min Chart

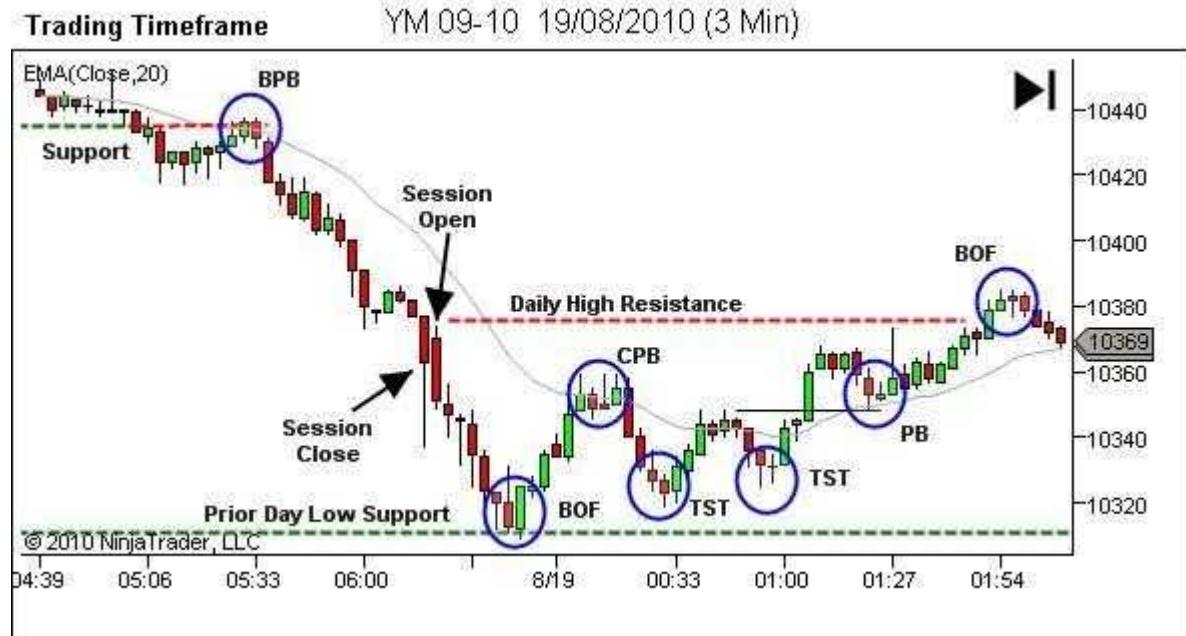


Figure 6.11 - Emini Futures – YM Trading Timeframe - 3 Min Chart

Figures 6.12 and 6.13 below demonstrate two examples of ES 5 min charts. This is the trading timeframe, based upon the following plan:

- Higher Timeframe: 30 min
- Trading Timeframe: 5 min
- Lower Timeframe: 1 min



Figure 6.12 - Emini Futures – Trading Timeframe – 5 Min Chart (1 of 2)

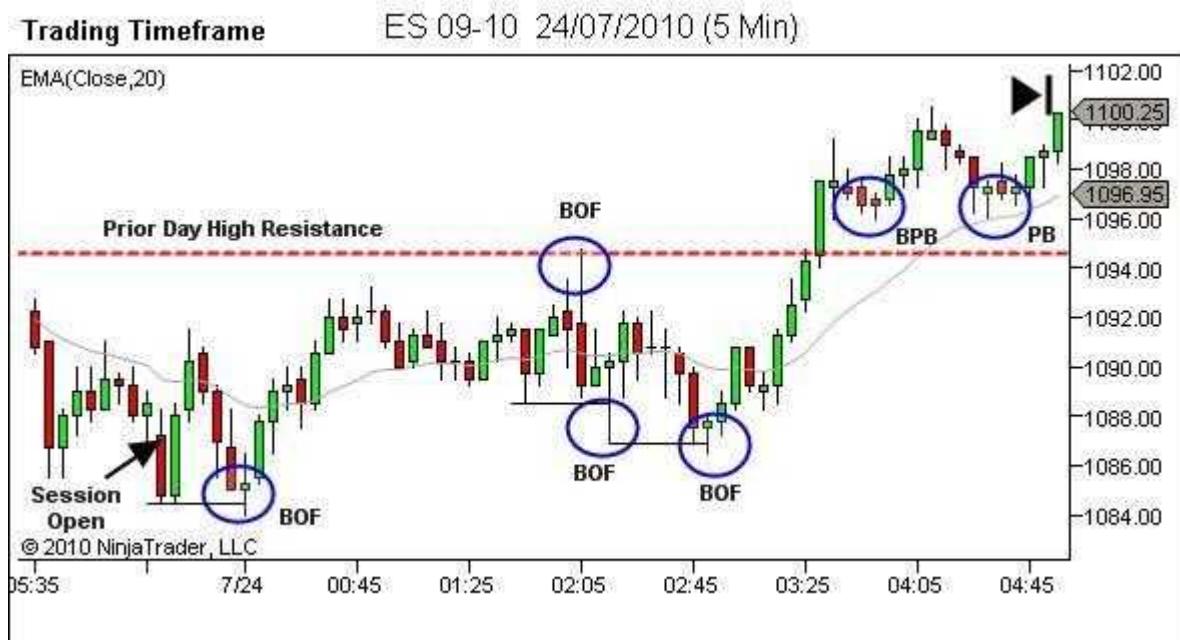


Figure 6.13 - Emini Futures – ES Trading Timeframe – 5 Min Chart (2 of 2)

The following chart is an example on the TF (emini Russell) using the same timeframes.



Figure 6.14 - Emini Futures – TF Trading Timeframe – 5 Min Chart

For those desiring a more intense trading session though, the emini futures markets offer the ability to trade even lower timeframes.

The following charts show the TF *trading & lower timeframe* charts based upon the following selection of timeframes:

- Higher Timeframe: 5 min
- Trading Timeframe: 1 min
- Lower Timeframe: 20 tick

Note that the *lower timeframe* chart shows the BOF and BPB setups from the *trading timeframe*.

(*The YTC Scalper supplementary ebook will outline additional considerations for trading at these lower timeframes, if this is something of interest to you.*)

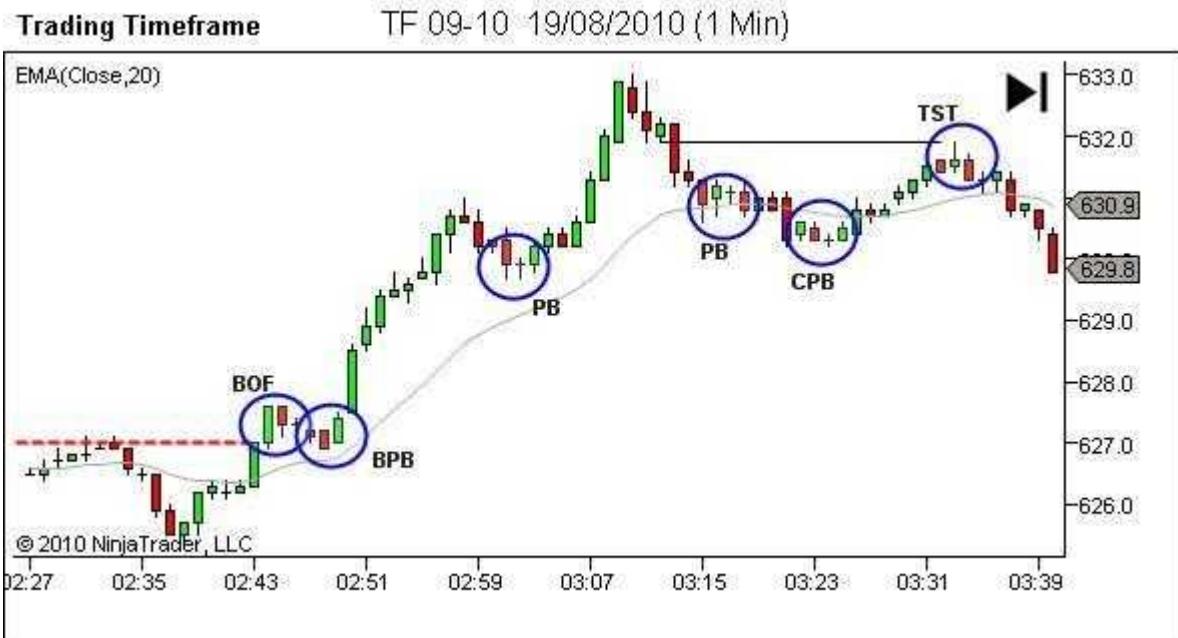


Figure 6.15 - Emini Futures – TF Trading Timeframe – 1 Min Chart

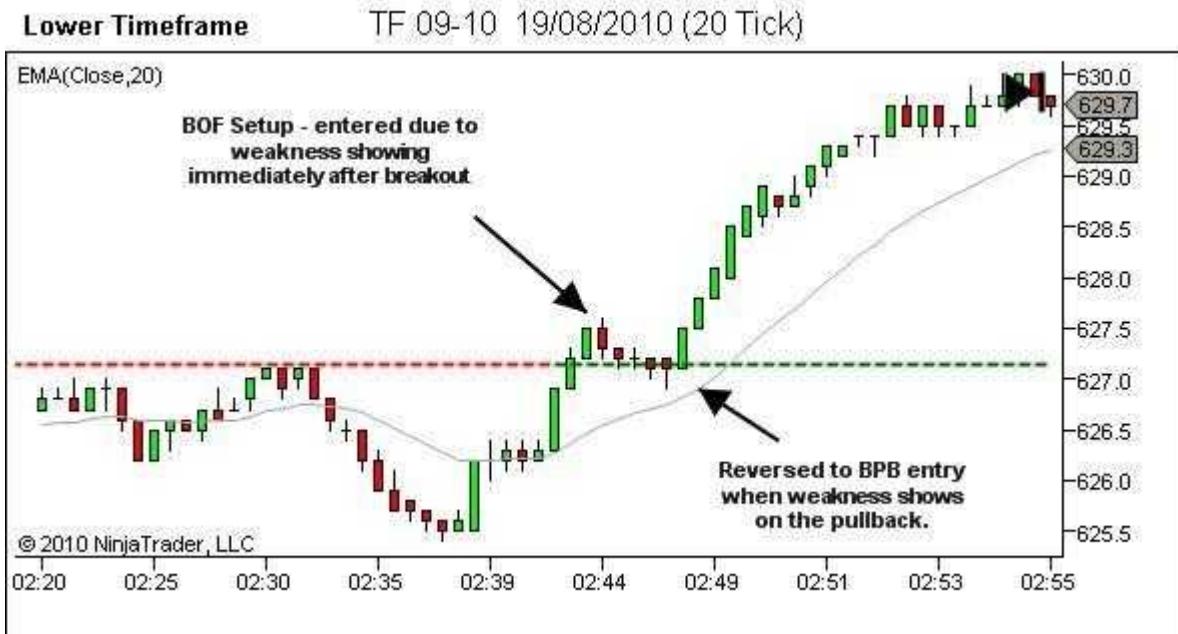


Figure 6.16 - Emini Futures – TF Lower Timeframe – 20 Tick Chart (showing BOF/BPB setups from figure 6.15)

6.3.1 - Additional Emini Futures Considerations

Session Opens

Like forex, you'll need to consider how you manage session openings.

I make my initial assessment of trend, strength and weakness, and *future trend* direction from the pre-session data. However I will be prepared to adjust my *future trend* premise, by treating the session open as if it were an S/R area that had just been broken.

Just like watching a broken S/R area for signs of strength or weakness, to give us a feel for a potential breakout failure and change of direction, or breakout pullback and continuation, I'm watching the initial few minutes of *new session* data to identify signs of strength and weakness. Future trend direction is likely to be in the direction of strength and against the direction of weakness.

Don't be in a hurry to trade though, until you have clearly established your bias for *future trend* direction. Sometimes it's immediately obvious. Other times the market can take a while for market sentiment to become clear.

Gap Opens

If you're daytrading emini futures, you'll need to consider how to manage gap openings, and how to establish a bias from the open – do you expect price to continue in the direction of the gap, or should you be searching for opportunity to fade the gap?

You probably won't be surprised to find that I don't have fixed rules. I prefer to consider each opening on its own merits.

However, here are a few pointers for how I manage gap openings in the emini's:

- The market structure is based firstly off the „session only“ chart, showing daily gaps. I then add S/R from significant overnight market data. Note that it must be a significant level or turning point.
- My pre-opening assessment of trend, strength and weakness and *future trend* direction are based upon the pre-session data.
- I then operate exactly as per any normal session open, adjusting my expectation for *future trend* direction based on my assessment of strength and weakness in the first few minutes of the trading session.

Fixed rules limit your ability to react to the current market environment. Treat each opening as unique and determine your analysis and future bias based on signs of strength and weakness.

Once again, don't be in a hurry to trade until you have clearly established your bias for *future trend* direction. Sometimes it's immediately obvious. Other times the market can take a while for market sentiment to become clear.

News / Economic Releases

As with forex, the lower timeframe emini futures markets are particularly susceptible to high volatility at times of regular news (economic) releases. While most reports are released during the overnight session, you will have some released from time to time during the US emini sessions, in particular at 10:00 ET.

Management is the same as discussed earlier in the forex section.

- My aim is to not initiate any trade just prior to a news release which is likely to move price, unless it's expected that the trade should be complete or showing significant profit, by the time the release occurs.
- If I have an open trade at the time of a regular news release, I will either close it out prior or tighten stops, as determined by my analysis.

Scalping

Additional considerations for scalping timeframes, as demonstrated above in figures 6.15 and 6.16, are beyond the scope of this book. If you're interested, they'll be covered in the supplement to this book, YTC Scalper.

Amongst the topics covered will be:

- Market selection
- Optimum trading times
- Abbreviated Analysis
- Market Internals
- Execution
- Missed entry
- And the many, many psychological problems encountered when decision time is limited.

6.4 – Example – Stocks & ETFs

With my usual trading platform not having an equities datafeed, we now feature charts courtesy of www.thinkorswim.com.

The first example is based upon daily trading of the SPY ETF, using the following timeframes:

- Higher Timeframe: Weekly
- Trading Timeframe: Daily
- Lower Timeframe: 1 hour

Market structure is taken from the weekly chart, as shown below. Note the circled areas, where price interacts with the S/R levels, which will be featured in the *trading timeframe* daily chart on the next page.



Figure 6.17 - SPY – Higher Timeframe - Weekly Chart



Figure 6.18 - SPY – Trading Timeframe - Daily Chart

The following example demonstrates WDC, traded via the same daily timeframe. Once again, lower timeframe triggers would be based off an intraday 1-hour chart, if your lifestyle allowed.



Figure 6.19 - WDC – Trading Timeframe - Daily Chart

The strategy is also applicable to daytrading of both stocks and ETFs.

The following three examples demonstrate *trading timeframe* charts for SPY, SBUX and OSX, using the following plan:

- Higher Timeframe: 1 hour
- Trading Timeframe: 5 min
- Lower Timeframe: 1 min



Figure 6.20 - SPY – Trading Timeframe – 5 Min Chart



Figure 6.21 - SBUX – Trading Timeframe – 5 Min Chart



Figure 6.22 - OSX – Trading Timeframe – 5 Min Chart

6.4.1 - Additional Stock & ETF Considerations

Gap Opens

Like emini futures, you'll need to consider how to manage gap openings and how to establish a bias from the open – do you expect price to continue in the direction of the gap, or should you be searching for opportunity to fade the gap?

As discussed earlier, I am hesitant to apply fixed rules to gaps, preferring to hold off on trading until I have clearly established a bias for *future trend* direction. Sometimes it's immediately obvious. Other times the market can take a while for market sentiment to become clear. Don't be in too much of a hurry.

The opening candles are monitored closely on the *lower timeframe* in order to identify signs of strength and weakness, and to therefore identify the likely future direction of price movement.

Trading Multiple Stocks & ETFs

As discussed in the Additional Forex Considerations, the greater the traded timeframe, the more opportunity we have to monitor additional instruments.

Unlike forex traders though, who are limited to a small universe of available currency pairs, stock traders have a much greater number of stocks from which to find their trade opportunities. You'll need to develop your own way of narrowing this down to a smaller basket of preferred stocks.

Having not traded stocks for many years it would be wrong of me to tell you how to do it. The fact is there is no right or wrong way to do this and you need to find your own way. There is a significant amount of information on the internet.

Remember though, opportunity comes through price movement. So, as an example, you may wish to conduct a market scan to find trending stocks that meet minimum volume requirements. Then visually narrow the selections down to a list of the best 20-30 which show smooth trending price action. This 20-30 will be your daily watchlist. Update the list each weekend, discarding those that no longer meet your requirements, or replacing the worst with better ones as they become available.

You may also wish to just outsource this whole process, choosing simply to trade based upon a basket of stocks selected by a favourite website (such as the Most Active lists at www.investors.com, www.stocktwits.com or www.bigmovingstock.com).

A further factor with multiple stocks on larger timeframes is the fact that you will likely have multiple positions on at once. You'll need to consider this from a money management perspective – how much total exposure will you allow at any one time. We'll consider this in a little more detail in Volume Four when we discuss risk and money management.

News Events

Like forex or emini-futures, stock trading will incur risk during the release of economic reports or news events related to that particular stock, sector or market. It's beyond the scope of this book to identify sources of fundamental news and events for stock trading. If you choose to trade the equities market, ensure you conduct research in order to identify the relevant fundamental events and to manage the risk appropriately.

6.5 - Conclusion

The YTC Price Action Trader strategy is applicable in any liquid market and timeframe.

Examples have been shown, applying the strategy to forex, emini-futures and stock/ETFs, in everything from the 1 min to daily *trading timeframes*.

We have also discussed additional considerations that apply uniquely to these markets.

This ends our discussion of strategy.

Volume Four will discuss the business aspects of trading and our documentation of a trading plan and procedures manual. Volume Five will then continue with a discussion of the process that must be undertaken in order to maximise learning (and therefore maximise the likelihood of you achieving consistent profitability).

PLEASE NOTE: The markets and timeframes chosen for your application of the YTC Price Action Trader strategy, should be determined by your own testing (largely trial and error) in order to best match your lifestyle requirements and your trading personality and psychology.

The combinations I'm showing here are not recommendations; rather they are demonstrations of the fact that these setups exist on all timeframes.

Www.ForexWinners.net

Resources

Trading Website: www.YourTradingCoach.com

YouTube Videos: <http://www.youtube.com/YourTradingCoach>

'Because You'd Rather Be Trading For A Living...'