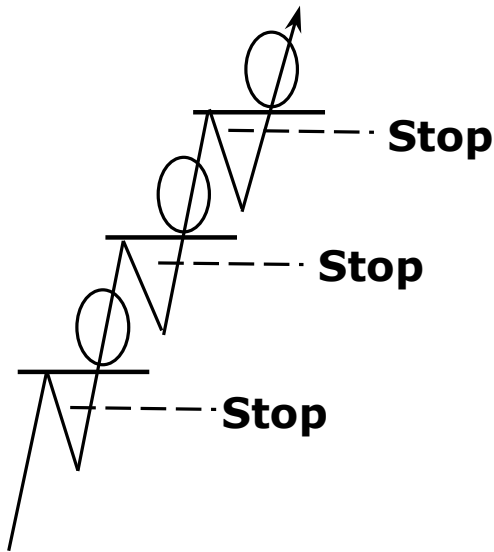


# Trading Strategies

## Breakout & Retracement Trades



## Breakout Trades

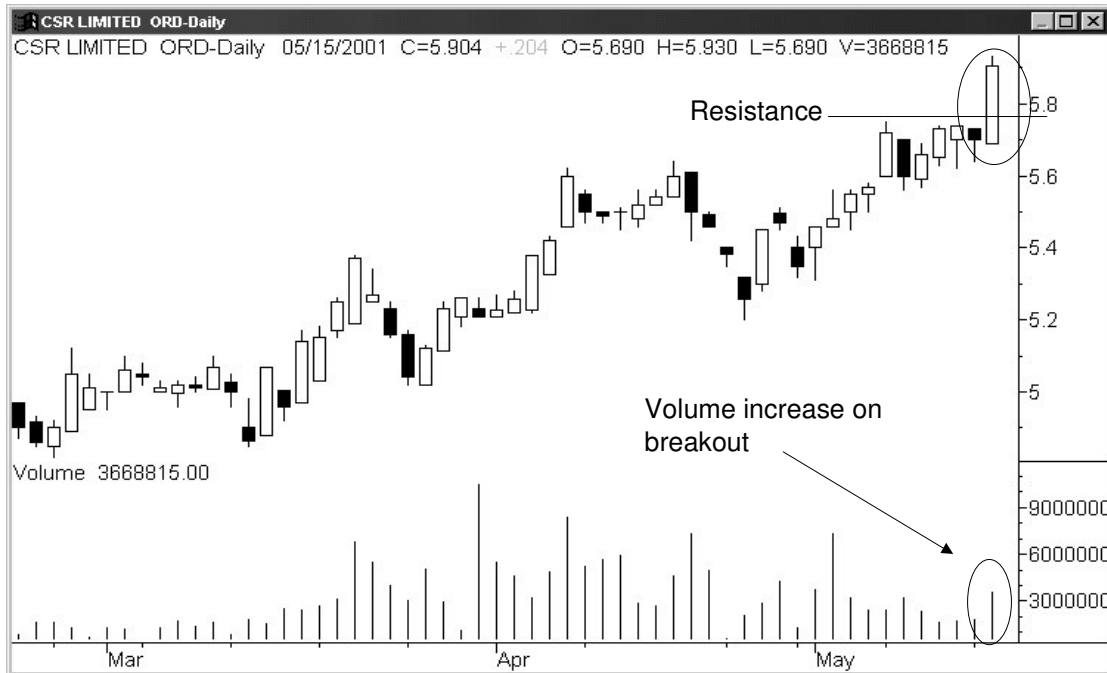


- During an existing uptrend, share price action consolidates between a significant support & resistance line
- A breakout exceeds resistance on heavy relative volume which acts as a buy signal
- Set a pattern based stop just under resistance line

The longer the consolidation period, the more dramatic and enduring the ultimate breakout is likely to be. I am more likely to enter a position if there is little overhead resistance close to my entry price. If the trend is to remain intact, it is unlikely that the share price will collapse back to within its previous trading range. Should the prices bearishly penetrate the previous level of breakout, my stop loss will generally be triggered and I will exit the trade immediately.

This is a common pattern within Stage 1, as the share breaks out and moves into Stage 2. It is also common as periods of consolidation within an existing Stage 2. This is one of my favourite buy signals, especially when the support/resistance lines occur along psychologically significant price points eg. \$2.00 and \$3.00 etc.

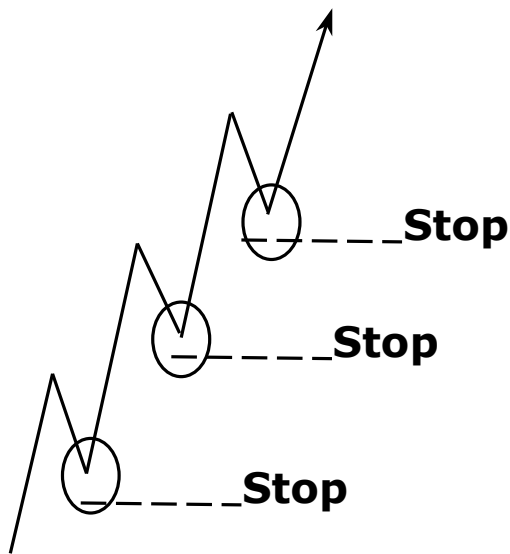
## Breakout Trade Example



I entered a position in CSR at the end of the day, on completion of the white candle formation. It is up to you whether you enter on the basis of the white candle itself, or whether you await confirmation to trigger your entry. Let's have a look at the result of the trade...



## Retracement Trade



- While the share is in an existing medium term uptrend, buy on bottom reversal pattern
- Set pattern based stops just under lowest point of bottom reversal pattern

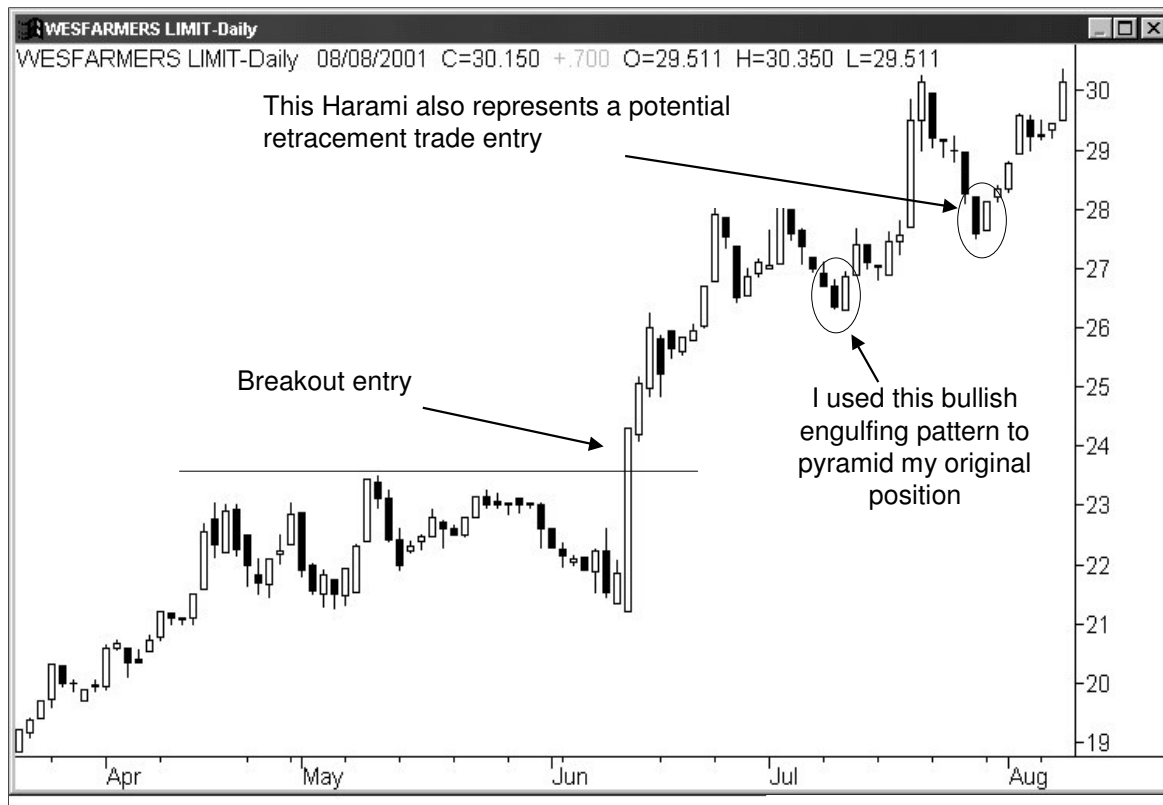
Entry can be made with a high degree of probability if there is a confirmed bottom candlestick reversal pattern. Common patterns include hammers, piercing patterns, bullish engulfing patterns and a new pattern that will be discussed later in this publication; an inverted piercing pattern.

Retracement trades may require confirmation to ensure the effectiveness of the bottom reversal candlesticks pattern before purchasing the share. If the closing price of the share has punctured a level of support or an uptrend line, prior to producing a bottom reversal, this has a different implication compared to if the reversal was apparent above a support line. I do not enter a trade based on a bottom reversal pattern if support, the moving average or the trendline has been broken. The weight of evidence in this situation would suggest that the share has commenced a downtrend.

## Retracement Example



Let's review an actual example of a retracement trade that I used in order to pyramid an existing holding. Have a look at the Wesfarmers daily chart above and see if you can circle a breakout entry, as well as a subsequent retracement pyramid point. Resist the temptation to look directly at the answer, until you've had a chance to really analyse the chart.



The breakout entry is shown where the white candle penetrates an existing resistance level, during a medium term uptrend. The retracement trade examples can be seen as temporary pullbacks during an existing medium term uptrend. Entry can be guided using a bottom candlestick reversal pattern such as the Bullish Engulfing pattern, or the subsequent Harami.

## *Ideal Set-Up Conditions – Uptrend*

- Share in an existing **uptrend**
- Share is breaking out from a **base** formation within a hot sector
- Preferably when the overall market is **bullish**
- Several **technical indicators** that have provided bullish signals eg. rising momentum indicator, rising moving average, upward sloping trend line
- Share moving into **Stage 2**, or currently in Stage 2

A **Set-up** is a set of general conditions that would suggest the share is uptrending or downtrending. A **Trigger** is the exact pattern, indicator or signal that would force you to buy or sell a share/option.

## *Ideal Set-Up Conditions – Downtrend*

- Share in an existing **downtrend**
- Share is breaking down from a **top** formation within a cold sector
- Preferably when the overall market is **bearish**
- Several **technical indicators** that have provided bearish signals eg. falling momentum indicator, falling moving average, downward sloping trend line
- Share moving into or currently in **Stage 4**



## *Ideal Trigger Conditions – Uptrend*

- ✓ A break upwards past a resistance level, initiated with a green candle, on heavy relative volume, (ie a breakout trade)
- ✓ A bottom reversal within an existing uptrend (ie a retracement trade)
- ✓ A gap upwards in combination with the above 2 conditions
- ✓ A top reversal pattern that fails

Depending on the system that you plan to implement, your entry signals into a long position for example, based on the uptrend set-ups and triggers, may prompt you to open a position. However, your downtrend observations may not be the only trigger for you to sell your shares.

Once a share is in a fully-fledged downtrend, you may have given back too much profit or suffered a large depletion of your trading equity. Other exit methods may avoid these consequences. There are a variety of other methods that may trigger your exit decision prior to a downtrend being in place. Often actual exit signals have more to do with capital preservation than trend reversal.

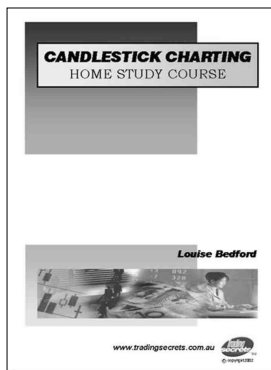


For more information on breakout and retracement trades, as well as stop losses and successful trading methods, refer to **Charting Secrets**, by Louise Bedford.

This book is available at all good bookstores, or online at [www.tradinggame.com.au](http://www.tradinggame.com.au).

## *Ideal Trigger Conditions – Downtrend*

- ✓ A break downwards past a support level, initiated with a red candle, especially if it is on heavy relative volume, (ie a breakout trade)
- ✓ A top reversal pattern within an existing downtrend (ie a retracement trade)
- ✓ A gap downwards in combination with the above 2 conditions
- ✓ A bottom reversal pattern that fails



For more information on how to trade effectively with Candlesticks, you can order **The Candlestick Charting Home Study Course** from [www.tradinggame.com.au](http://www.tradinggame.com.au)

It comes with a free 12 months of Trading Game Forum membership so you can ask trading questions and receive responses from Louise Bedford, Chris Tate and other experienced traders.