TSR TRADING SETUPS REVIEW

HOW TO TRADE WITH PRICE ACTION

STRATEGIES

GALEN WOODS

How to Trade with Price Action (Strategies)

Trading Setups, Rules & Examples

Galen Woods

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Introduction

This eBook contains a selection of articles I have written on Trading Setups Review. You can find out more about me by clicking here.

(All articles in this eBook are available for viewing online at http://www.tradingsetupsreview.com for free.)

In this Strategies Edition, I have selected the 10 most popular price action trading setups reviewed on Trading Setups Review. These strategies use price action patterns and minimal indicators. The last setup focuses on using volume to complement price action.

I hope you find this eBook a friendly companion for your offline learning, and I wish you all the best in your trading career.

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1. A Simple Inside Bar Day Trading Strategy Using YM Futures

To day trade successfully, we need a market that is volatile and liquid. S&P 500 E-mini (ES) and NASDAQ-100 E-mini (NQ) futures are popular day trading markets. Beyond them, the E-mini DOW (YM) futures contract is also a great choice. Among equity index futures, the trading volume of YM futures ranks right after ES and NQ futures.

Like ES and NQ, YM futures is also an electronically traded contract. Its underlying is the Dow Jones Industrial Index. For a one-point movement in the index, its value changes by $5.

If you are completely new to futures, you should spend some time browsing CME's website.

Read on for a simple inside bar day trading strategy with examples from the YM futures market.

1.1 Time-frame For Day Trading YM futures

The 5-minute time-frame is a common choice among day traders. But that is just a convention.

Instead, I use the Price Action Time-frame Index (PATI)* to find time-frames that are tradeable. It finds the smallest time-frame that is tradeable for a price action trader. As long as you are trading above the minimum tradeable time-frame (MTT)*, price action

analysis is possible. But note that the MTT changes over time as market price action changes.

For the YM futures market, its current MTT is the 4-minute time-frame. Trading using the MTT offers the highest number of trading setups. Hence, we will be using the 4-minute time-frame.

If you prefer fewer setups or longer intervals for ongoing analysis, increase your time-frame.

*The concepts of PATI and MTT are explained in my course - "Day Trading with Price Action".

1.2 Trading Rules - Simple Inside Bar Day Trading

These rules attempt to capture the first low-risk pullback in a new trend using an inside bar. We define the trend with the help of a 21-period simple moving average (SMA).

Bullish Inside Bar Trading Setup

1. From below the SMA, the market rises completely above it. A price bar must clear above the SMA.
2. Wait for the first bullish inside bar.
3. Place a buy stop order a tick above it.

(Why use a stop order to enter the market?)

Bearish Inside Bar Trading Setup

1. From above the SMA, the market falls completely below it. A price bar must clear below the SMA.
2. Wait for the first bearish inside bar.
3. Place a sell stop order a tick below it.

1.3 Simple Inside Bar Day Trading Examples

The charts below show the YM futures market using 4-minute candlesticks. The orange line is a 21-period SMA.

Winning Trade - YM Futures Bearish Inside Bar

YM Futures Inside Bar Example Winning

1. The market was above the SMA.
2. This bar went below the SMA and signaled a change in trend. We started looking out for bearish inside bars.
3. After YM pushed below the SMA, it did not prompt any significant bullish response. None of the candlesticks manage to test the SMA above it.
4. At the end of its third attempt to rise towards the SMA, a bearish inside bar formed. We sold a tick below it.

There are many options for exiting. As we expected the trend to continue, the most conservative target is at the last extreme low. (horizontal dotted line)

Even with this conservative target, this trading setup gave us a 2:1 reward-to-risk ratio. Hence, it was a setup of high positive expectancy.

Losing Trade - YM Futures Bullish Inside Bar

YM Futures Inside Bar Losing Example

The first bar on this chart is also the first bar of the session.

1. This session started below the SMA.
2. Within half an hour, YM managed to clear above the SMA.
3. The SMA rejected the first test by the market from above, giving hope to bullish sentiments.
4. However, as the market made a new session high, it started congesting. The candle bodies contracted and prices moved sideways.
5. Within this congestion, a bullish inside bar formed. We bought above this bar and got stopped out immediately.

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1.4 Review - Simple Inside Bar Day Trading Strategy

In an active market, using the right time-frame, inside bars offer great trading windows. It is a tool to control our risk and time our entries in a trending market.

While we used YM futures in this example, you can use this strategy in other liquid and volatile markets.

This trading strategy is simple as you only need a SMA and knowledge of inside bars. But there are two points to take note of when employing this trading strategy.

First, look for new trends. This is because retracement trades early in a trend has higher chance of success and more room for profit.

Second, avoid congestion areas. This is crucial for inside bar trading. This is because inside bars are often found in congestion patterns. The trick here is to distinguish between an inside bar in congestion and one that is not. You will suffer whipsaws if you assume that the trend will continue when the market is actually in congestion.

Look at the two examples again. In the winning example, YM was clearly drifting upwards and the top shadows were more prominent. It was not congesting. But in the losing example, the price bars were meandering sideways with both top and bottom shadows. It was definitely forming a congestion pattern. Hence, we should have avoided trading the bullish inside bar.

With regards to target placement, you should at least aim for the last extreme of the trend. When the momentum is clear, you can aim further. You can use support/resistance areas projected using past swing pivots and price thrusts. Another good option is the high or low of the last trading session.

Read: 10 Ways to Take Profit

In all, this YM futures strategy is a solid starting point for building your own simple trading method.

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2. Trading Consecutive Up/Down Days With Lower Risk

When a market closes up for consecutive days, traders get excited. They start speculating that the market cannot continue its upwards streak. Somehow, we are wired to think that what goes up must come down, and vice versa. (See: Gambler's Fallacy)

This is why consecutive up/down days form the basis of many stock scans and market strategy research. Traders want to find out if there is an edge in buying after consecutive down days or selling after consecutive up days.

- Buying after consecutive up/down days and selling after a week.
- Testing four days down and up.
- Building a heatmap of QQQ returns after consecutive up/-down days.

In these studies, they approached the trading idea as quantitative system traders. The results seem encouraging, but they are not conclusive of an actual trading edge. This is especially true for discretionary price action traders.

In this article, we will explore a price action trading strategy based on the same idea of consecutive up/down days. But we will focus on the market context of such consecutive up/down days.

2.1 Trading Rules - Consecutive Up/Down Days Low Risk Entry

Fading consecutive up/down days often means going against the market trend and momentum. It is a dangerous strategy, but it does not have to be.

In our low-risk variant, we focus on fading consecutive up/down days that go against the market structure of swings.

Long Entry After Consecutive Down Days

1. Four or more consecutive days down (close below open).
2. If the market has not breached the last swing low, buy a tick above the next bullish bar.

Short Entry After Consecutive Up Days

1. Four or more consecutive days up (close above open).
2. If the market has not breached the last swing high, buy a tick above the next bullish bar.

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2.2 Consecutive Up/Down Days Trading Examples

Winning Trade - Long Entry ROST Daily

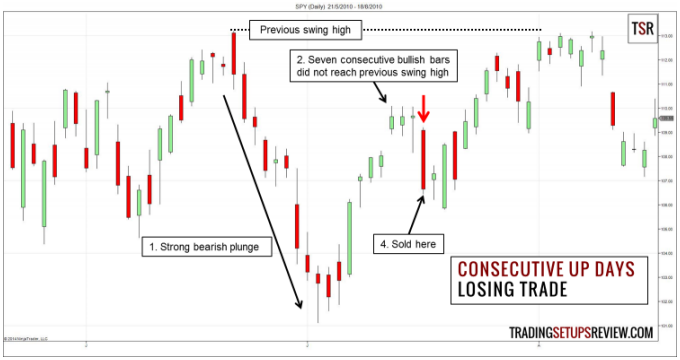
Consecutive Down Days Trading Winning Example

This is a daily chart of Ross Stores Inc. It shows an underachieving four-bar down thrust.

1. These four consecutive down days caught our attention. Is it a last-ditch attempt by the bears? Or is it the beginning of a powerful down trend?
2. The four-bar thrust did not even reach the previous swing low, hinting that the market was in the first scenario.
3. This bullish bar was our setup bar. We bought a tick above it.

The market continued to rise, opening with up gaps for the next four days.

Losing Trade - Short Entry SPY Daily



Consecutive Up Days Trading Losing Example

The chart above shows the daily bars of SPY, the S&P ETF. The price action in this chart is less straightforward.

1. There was a strong bearish plunge that was hard to ignore. It breached the last swing low so it was not a candidate setup under this trading strategy.
2. But after the bearish plunge, the market rose with seven consecutive bullish bars that did not hit the last swing high. That was in line with our trading rules.
3. We sold a tick below this bearish bar and was stopped out as the market continued to rise.

After the strong bearish plunge, the market rose sharply, forming a V-shaped reversal. Interpreting such V-shaped patterns is tricky. It shows strength in both directions and it is difficult to judge which side will emerge victorious.

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2.3 Review - Consecutive Up/Down Days Low Risk Entry

In most markets, there are many instances of consecutive up/down days. Most back-testing research trades them indiscriminately. Thus, they are going against the trend most of the time.

Using the market structure to filter consecutive up/down days is a simple method to make sure that we take only the low risk setups. This is akin to the improved three bar pullback trading strategy.

There will be fewer trading setups. However, it is a worthwhile sacrifice for better trading quality.

Other than the market context, you can also pay attention to the price thrust formed by the consecutive bars.

Are the consecutive bars making higher bar highs? Or lower bar lows? Do they exceed the previous bar by an increasing distance or a decreasing distance?

In my price action trading course, I discuss two price patterns derived from answering these questions. They are the Deceleration and Anti-climax patterns. They are useful patterns to look out for when you see consecutive up/down bars.

- The Deceleration pattern consists of consecutive up/down bars that weakens as they progress. The winning example above is also a bullish Deceleration setup.
- The Anti-climax pattern consists of consecutive up/down bars that are exhaustive. The losing example was in fact an Anti-climax pattern that was invalidated before the setup bar appeared.

To learn more about these price patterns, take a look at "Day Trading with Price Action".

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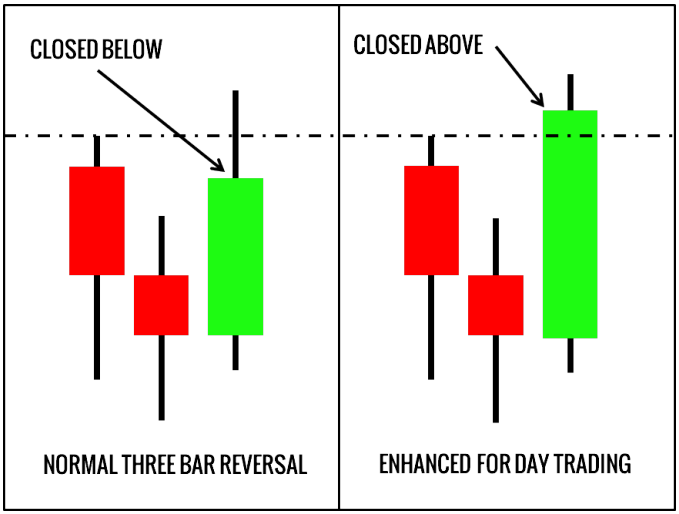
3. Three-Bar Reversal Pattern For Day Trading

Alton Hill from TradingSim, a day trading simulator, wrote about an enhanced three bar reversal pattern for day trading.

According to Alton Hill, three-bar reversals are too common in intraday time-frames. To select the best three-bar reversal patterns for day trading, he wants the third bar in the pattern to close above the highs of the first two bars.

The diagram below demonstrates the difference between the usual three-bar reversal pattern and Alton Hill's day trading version.



Three Bar Reversal Pattern For Day Trading

3.1 Trading Rules

Rules for Long

1. Bar 1 closes down
2. Low of Bar 2 is below low of Bar 1 (and Bar 3)
3. **Bar 3 closes above the high of both Bar 1 and Bar 2**
4. Buy at close of Bar 3

Rules for Short

1. Bar 1 closes up
2. High of Bar 2 is above high of Bar 1 (and Bar 3)
3. **Bar 3 closes below the low of both Bar 1 and Bar 2**
4. Sell at close of Bar 3

3.2 Trading Examples

Winning Trade

Three Bar Reversal Pattern Winning Trade

This a 5-minute chart of ES futures. It shows the regular session. I included part of the previous section to show the up trend that ended yesterday. After our entry, the prices drifted up for the rest of the session.

1. The previous session ended with a **strong bull trend**.
2. The three-bar reversal pattern was also the right shoulder of a **bullish head and shoulders formation**. (You might have noticed that the head of the formation was a regular three-bar reversal pattern. In this case, it gave a better entry than our enhanced pattern.)
3. The last bar of the pattern closed above the highs of the two previous bars. That was our signal to buy.

Losing Trade

Three Bar Reversal Pattern Losing Trade

This is a 5-minute chart of E-mini Dow contract. Despite a strong signal bar, the pattern failed immediately after entry.

1. Although prices were dropping consecutively for seven bars, the increasing **buying pressure** is obvious as the bars show long bottom tails (shadows).

2. Tails developed at the top of the bars during the pullback upwards. Tails on both top and bottom of the bars are giving us mixed signals, implying that **prices might be congesting soon**.
3. If we ignored the above warning signs and shorted the three-bar reversal pattern, it is difficult to find a worse entry point.

3.3 Review - Three-Bar Reversal Pattern For Day Trading

This modified three-bar reversal pattern is impressive. A simple rule has turned this commonplace pattern into a powerful setup.

In fact, this added rule is asking for confirmation of the pattern in advance. (Applying the technique of candle blending, if Bar 3 in a normal three bar reversal pattern has good follow-through in Bar 4, blending Bar 3 and Bar 4 would have resulted in this enhanced three-bar reversal pattern.)

You can easily combine this pattern with other indicators or price patterns to find high probability trade setups. The winning example is a great combination of a head and shoulders formation and a three bar reversal pattern.

However, due to the extra rule, the signal bar (Bar 3) tends to have a large range. As our stops are usually placed on the opposite end of the signal bar, the trade risk might be higher. We should either cut down our trade size or tighten the stop if possible. If you are unable to manage the risk, then skip the trade setup.

One last point to note is that if the middle bar of the pattern is an outside bar, be very careful. Outside bars often precede wild and unpredictable price action.

If you want to read more about three-bar patterns, you must take a look at our review of Johnan Prathap's Three Bar Inside Bar Pattern and Thomas Bulkowski's "Are Three Bar Patterns Reliable

for Stocks?" article in Technical Analysis of Stocks & Commodities magazine.

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4. NR7 Trading Strategy

The quiet period before the next explosive market move is like the calm before the storm. NR7 helps us to find the calm so that we can prepare and profit from the impending storm.

NR7 means narrow bar 7. It is a bar that has a smaller range than the six bars before it. It is a range contraction that precedes range expansion.

In our trading strategy, we add a simple trend rule to find low risk trend trades.

4.1 Trading Rules - NR7 Trading Strategy

Long Trading Strategy

1. Past 7 bars are completely above the 20-period EMA
2. Buy on break of high of NR7 bar

Short Trading Strategy

1. Past 7 bars are completely below the 20-period EMA
2. Sell on break of low of NR7 bar

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4.2 NR7 Trading Examples

Winning Trade - Bearish NR7

NR7 Trading Strategy Winning Trade

This is a 3-minute chart of CL futures on NYMEX. The orange line is the 20-period EMA. The NR7 bars have a yellow background.

1. Price swung down from above the EMA with eight consecutive bearish bars.
2. The seven bars that defined the NR7 bar were all below the EMA, showing that the bearish momentum held up. Although the NR7 bar closed higher than its open, it formed a micro triple top with the two bars before it. After the low of the NR7 bar broke, we went short.
3. Price came back up to test the break-even level of the trade. However, following a failed bull break-out of the doji NR7, prices plummeted.

The doji NR7 is also a great example to warn us against using NR7 to trade reversals without confirmation from other analysis.

Losing Trade - Bearish NR7

NR7 Trading Strategy Losing Trade

This is another 3-minute chart of CL futures. In this example, the NR7 trade experienced whipsaws.

1. The seven bars leading up to the NR7 bar were all below the EMA. Despite the four bullish bars in the retracement, price could not reach the EMA.
2. As price broke the low of the second NR7 bar, we went short. However, the consecutive NR7 bars was a hint of the tight congestion that followed.
3. Price hit our stop-loss at the high of the NR7 bar. It was a false break-out that reversed and continued the bear trend. Re-entry was a valid option as price stayed below the EMA throughout the retracement and our bearish outlook was not compromised.

4.3 Review - NR7 Trading Strategy

Toby Crabel studied the NR7 pattern together with the NR4/ID trading setup. Both patterns are popular trading tools found in many trading strategies.

(Read: Day Trading with Short Term Price Patterns and Opening Range Breakout)

In this NR7 trading strategy, we looked for markets with a strong trend and used NR7 as a low risk entry point to join the trend.

Do not follow the trading rules mechanically. Some NR7 bars appear at the high of a bull trend or the low of a bear trend. These setups are not the target of our trading strategy. Wait for a real pullback to enter.

Be very careful when you see multiple NR7 bars. Narrow range bars in proximity are a sign of price congestion in which NR7 patterns are less reliable.

Remember to follow the path of least resistance. The best NR7 bars occur when price is moving against the path of least resistance.

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5. A Simple and Effective Price Action Trading Setup

Observing price action is the simplest way to trade.

Yet, many price action trading setups are not simple at all, requiring interpretation of complex and subjective chart formations.

The worst part is that traders often memorize price action trading setups without understanding the concept behind them.

In this exclusive article, we will introduce a simple and effective price action trading setup - **Trend Bar Failure**.

5.1 Basic Definitions For Price Action Trading

Trend

In price action trading, higher highs and high lows show an upward trend. Lower highs and lower lows show a downward trend.

In our examples, for simplicity, we will be using the **slope of the 20-period EMA** as our trend filter.

You are free to use your own methods and discretion to find the trend. Some of the more popular trend tools are moving averages and the ADX indicator.

One tip for identifying trends: trends are obvious. When it is doubtful whether the market is trending, it is not trending.

Trend Bar

A trend bar is one that represents a trend on a smaller time-frame. It opens and closes on opposite ends of the bar.

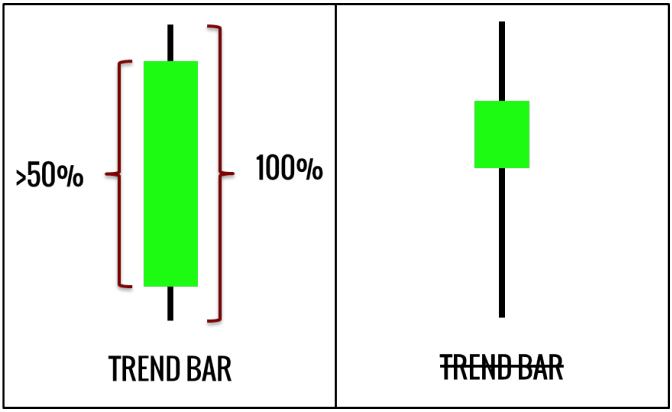
A bull trend bar opens near its low and closes near its high. A bear trend bar opens near its high and closes near its low.

What does a trend bar mean?

It means that traders have committed to one direction. Remember that in every bar, the number of contracts sold and bought are the same. The only reason for a bar to end up with a higher price is that the buyers were more aggressive than the sellers. The reverse is true for a bear trend bar.

How does a trend bar look like?

While we can identify trend bars subjectively depending on the market context, I prefer a more objective measure. A trend bar has a body that is greater than 50% of the entire bar range.



Trend Bar for Price Action Trading

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5.2 Trading Premise

These premises set the stage for this price action trading setup and explain its concept. The explanation below is for a bull trend. The reverse is true for a bear trend.

Trends tend to continue.

This is one of the principles of technical analysis. As trends tend to continue, our edge lies in following the trend.

Trend bars against trend hint at the entry of counter-trend traders.

In a bull trend, bear trend bars represent counter-trend traders trying to reverse the trend. The committed bearish traders are counter-trend traders.

The trend continues as counter-trend traders fail in their attempt to reverse the trend.

According to our first premise, the trend is more likely to continue than to reverse. Hence, it is likely that the counter-trend traders are wrong. The bearish trend bar is likely to fail without significant follow-through.

As the counter-trend traders realize that the bull trend is not reversing as they anticipated, they will cover their short positions and might even reverse to buying.

5.3 The Trend Bar Failure Trading Setup

Following the premises above, the entry for a trend continuation trade takes place when a trend bar against the trend fails.

If a **trend bar is not followed by another trend bar**, we should prepare ourselves for a Trend Bar Failure.

Rules for Long

1. 20-period EMA is sloping up (or if your trend assessment is bullish)
2. Bear trend bar
3. Low of bear trend bar broken (without forming a second bear trend bar)
4. Place a buy stop order above the high of the bar
5. Cancel order if not triggered within one bar

Rules for Short

1. 20-period EMA is sloping down (or if your trend assessment is bearish)
2. Bull trend bar
3. High of bull trend bar broken (without forming a second bull trend bar)
4. Place a sell stop order below the low of the bar
5. Cancel order if not triggered within one bar

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Trade Examples - ES Futures (5-Minute)

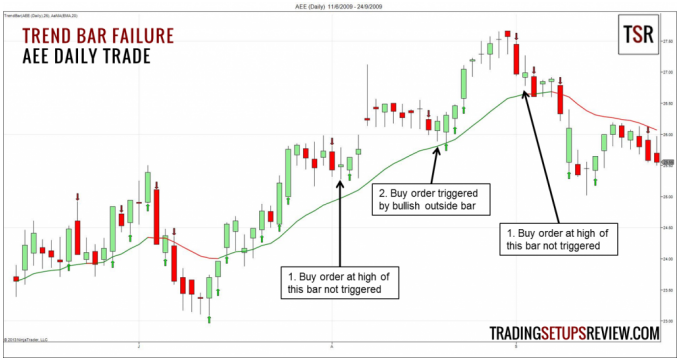
Trend Bar Failure ES Example

We have marked the trend bars in the charts. Bull trend bars with green arrows and bear trend bars with red arrows.

1. A strong bearish bar followed by a bullish reversal bar. It had good potential, but the buy order placed at the high of the bullish reversal bar was **not triggered**.
2. A bearish trend bar **tested the EMA without much follow-through**. The bull trend bar triggered the buy stop order, and led to a profitable trade.
3. This bear trend bar was also an **inside bar**. The two failure trades (failure of inside bar and trend bar) led to the 6 consecutive bull bars.
4. Although the bar after the marubozu was not a bear trend bar, its high was not broken and our buy order was **not triggered**.

We cancel orders if they are not triggered within one bar. This is because the best trades happen quickly like a knee jerk reaction. By cancelling orders that are not triggered swiftly, we are avoiding the second best trade and taking only the very best trades.

Trade Examples - Ameren Corp (Daily)



Trend Bar Failure AEE Example

You can use this price action trading setup for swing trading as well.

1. A doji broke the low of the bear trend bar. However, the buy order was **not triggered**.
2. An irresistible trade, with the an **outside bar** hitting our buy stop order after **testing the EMA**.
3. The strong bear trend bar had little follow-through, but the buy order was **not triggered**.

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Trade Example - EUR/USD (Weekly)

Trend Bar Failure EURUSD Example

Price action trading setups work well in the forex market.

1. The bear trend bar failed with a bull trend bar. This pattern is also known as the **pipe pattern**.
2. This trend bar failure was also an **inside bar failure**. However, the signal bar was a doji and not ideal.
3. The bear trend bar had limited follow-through. Although this trade was profitable, prices went sideways before resuming the trend. A more conservative trader would have exited during the **sideways congestion**.

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Trade Example - SPDR S&P 500 ETF (Monthly)

Trend Bar Failure SPY Example

This simple price action trading setup is robust enough for long-term analysis as well.

1. The bear trend was also an outside bar. This meant that the bears overwhelmed the bulls in that bar. However, the next bar was bullish reversal bar. This was good trade with a nice follow-through. However, it **might end up as a loss** if our targets were further.
2. Another nice **pipe pattern that tested the EMA**.

5.4 Conclusion

The Trend Bar Failure trading setup is extremely simple and versatile. It is the **ideal starting point for price action trading**.

The basic premise is the **trapping of counter-trend traders**. However, it manifests in different forms like inside bar failure and the pipe pattern.

As shown in the many examples above, you can use this price action trading setup in time-frames ranging from intraday trading to longer term monthly analysis.

The Trend Bar Failure is a price pattern from my trading course - "Day Trading with Price Action".

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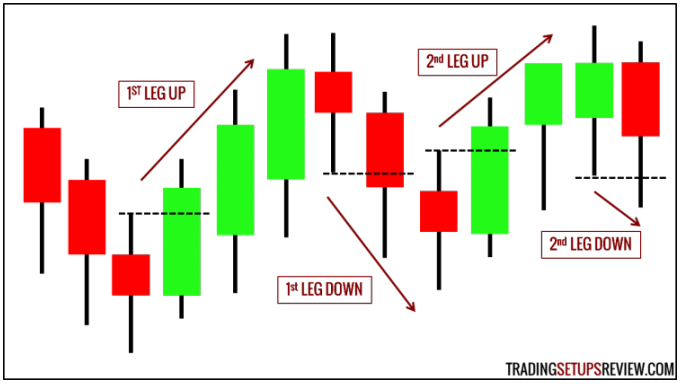
6. Two-legged Pullback to Moving Average (M2B, M2S)

Many price action traders claim that two-legged pullbacks are the most reliable trade setups. The variant we are reviewing today is from Al Brooks, who wrote three tomes on price action trading. These three books are not an easy read, but are extremely informative for price action traders.

In his books, he identified a two-legged pullback to the moving average as one of the best trade setups **when there is a strong trend**.

Before we start, let's have a basic explanation of counting legs. Any bar that goes higher than the previous bar starts a new leg up. Any bar that goes lower than the previous bar starts a new leg down.



Counting Legs Example

6.1 Trading Rules - Two-legged Pullback to MA

Long Trading Setup - M2B

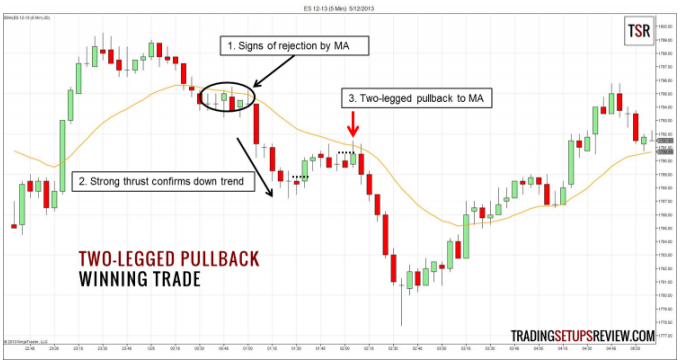
1. Strong up trend
2. Two-legged pullback down to 20-period EMA
3. Enter a tick above the bar that tested the 20-period EMA

Short Trading Setup - M2S

1. Strong down trend
2. Two-legged pullback up to 20-period EMA
3. Enter a tick below the bar that tested the 20-period EMA

6.2 Two-legged Pullback to MA Trade Examples

Winning Trade - M2S



Two-Legged Pullback Moving Average Winning Trade

This is 5-minute chart of ES futures contract, which is the main instrument Al Brooks trades. This trade is a beautiful example of a two-legged pullback trade.

1. After prices crossed below the EMA, it tried to crossed back but was clearly rejected.
2. The strong downwards thrust confirmed the down trend, which was what we needed before looking for continuation trades.
3. The two short dotted lines highlight the beginning of each leg up. This two-legged pullback looked good with the long top tails that showed as prices approached the EMA. The long top tails implied selling pressure.

Losing Trade - M2B

Two-Legged Pullback Moving Average Losing Trade

Another session of S&P E-mini futures showing 5-minute bars, which is Al Brook's recommendation as the sweet spot for day traders.

1. The day started with swings up and down without a clear direction. However, as prices made new lows, bottom tails emerged, showing buying pressure.

2. The up swing above the EMA seemed strong as there were eight consecutive bars with higher lows. However, there were three bear trend bars within the swing, which hinted at persistent bears.
3. Following a two-legged pullback to the EMA, we had a bullish reversal bar as our signal bar. We entered a tick above it but got stopped out after some sideways movement.

A key difference between the losing trade and the winning trade is how certain we were that the market was trending. In the winning trade example, we saw clear rejection from the EMA, which we did not see in the losing example.

6.3 Review - Two-legged Pullback to MA

Continuation trades work because the trend traps counter-trend traders. Two-legged pullbacks are more enticing to counter-trend traders and works better as a mousetrap for them.

Hence, in a trending market, the two-legged pullback to the moving average is a simple and high probability trading setup.

The key lies in finding trending markets. Pay attention to signs of a trending market and trade opportunities will present themselves. Very often, you can pay attention to the space between prices and the moving average for a sense of momentum. Two-legged pullbacks that follow strong momentum are better quality setups.

However, very strong trends tend to have single leg pullbacks. If you insist on waiting for two-legged pullbacks, then you must be ready to miss some trades in strong trends.

Also, with regards to counting legs of price movement, there are many nuances that we did not cover. Refer to Al Brooks' Trading Price Action Trends: Technical Analysis of Price Charts Bar by Bar for the Serious Trader (Wiley Trading) to learn more.

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7. Candlestick and Pivot Point Day Trading Strategy

What is the one trading rule that all candlestick experts agree on? Using candlesticks in isolation is not profitable. Hence, many candlestick trading strategies include other trading tools for confirmation.

John Person's candlestick trading approach uses pivot points for confirmation. In this review, we are using a simpler version of his trading strategy.

(Explore: Candlestick Trading Strategies)

7.1 Trading Tools

Pivot Points

Pivot points are price levels calculated using the high, low, and close of the last trading session. These price levels are potential areas of price exhaustion.

These are the formula for the common pivot points:

- Pivot Point (PP) = (High + Low + Close)/3
- 1st Support Level (S1) = (PP x 2) - High
- 2nd Support Level (S2) = PP - (High - Low)
- 1st Resistance Level (R1) = (PP x 2) - Low
- 2nd Resistance Level (R2) = PP + (High - Low)

Most charting software can plot the pivot levels automatically. If you need to draw them manually, you can use the online Pivot Point Calculator. It calculates up to the 4th support and resistance level.

High Close Doji

John Person devised his own candlestick trade triggers for his trading strategy. The bullish trigger is the high close doji.

Basically, wait for a doji. Then, look out for a candlestick to close above the high of that doji. That is our signal to buy.

Low Close Doji

The low close doji is the bearish version. Similarly, wait for a doji. But in this case, we are looking out for a candlestick that closes below the low of the doji to give us the sell signal.

7.2 Trading Rules - Candlestick and Pivot Point

Long Trading Strategy

1. Doji at a support level
2. Buy on close of high close doji

Short Trading Strategy

1. Doji at a resistance level
2. Sell on close of low close doji

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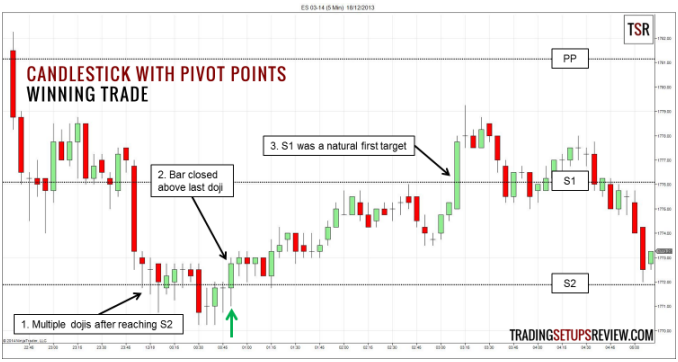
7.3 Candlestick and Pivot Point Trading Examples

Winning Trade - High Close Doji



Candlestick and Pivot Point Winning Trade

This chart shows a complete trading session of ES futures with 5-minute bars. Price started falling right after the market opened.

1. Prices found support at S2. The four dojis and three bullish bars tangling around S2 confirmed the support.
2. The bullish close above the last doji fired off a high close doji signal.
3. S1 was the natural first target.

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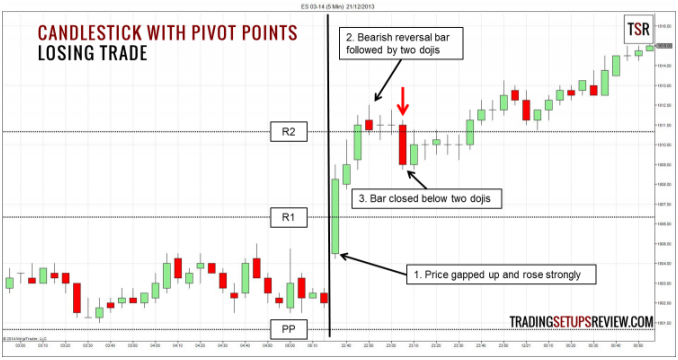
Losing Trade - Low Close Doji



Candlestick and Pivot Point Losing Trade

This is another 5-minute chart of ES futures. It shows part of the previous trading session. The solid vertical line separates the trading sessions.

1. Price gapped up and rose strongly through R1.
2. The ascent paused at R2 with a bearish reversal bar. However, it had little follow-through as shown by the two dojis.
3. This bar closed below the lows of the two dojis, setting up a low close doji. We sold into a losing trade as the upwards trend continued.

7.4 Review - Candlestick and Pivot Point

Trading candlestick patterns found around support and resistance levels is an effective trading strategy. In this particular variant, we used John Person's high close doji and low close doji with pivot point levels.

Dojis represent uncertainty. High close dojis and low close dojis are break-outs from uncertainty. Most break-outs fail.

To find high close dojis that perform better, look out for the following:

- Multiple dojis around pivot levels to confirm price exhaustion
- No strong bearish bars
- Failed low close doji

Apply the same logic for low close dojis.

When in doubt, it is always better to wait for more price action to unfold. This is because the best trades usually come after some congestion around the pivot levels.

Pivot points are popular day trading tools. However, they are not superior to other forms of support and resistance. Do not trade reversals with them indiscriminately.

The complete trading approach of John Person includes moving averages and the use of divergence for confluence. He also uses another trade trigger called jackhammer. To learn more, refer to his books:

- Candlestick and Pivot Point Trading Triggers: Setups for Stock, Forex, and Futures Markets (Wiley Trading)
- A Complete Guide to Technical Trading Tactics: How to Profit Using Pivot Points, Candlesticks & Other Indicators (Wiley Trading)

8. Trading The Engulfing Candlestick Pattern With Market Structure

If you have learnt how to trade candlesticks, you must know the engulfing candlestick pattern. Its striking name and visual makes it one of the most popular candlestick pattern.

Reference: Japanese Candlestick Charting Techniques

The engulfing candlestick pattern has two candlesticks. **The body of the second bar completely engulfs the body of the first bar.** It represents a total change of market sentiment.

An engulfing candlestick in the right context offers a high probability trading setup. Finding the best context with moving averages and oscillators are reliable trading methods.

Learn: Candlestick with RSI Trading Strategy

However, in this review, we will look at a simpler method that uses the concept of market structure to find point us in the right direction. Market structure refers to the relationship of swing highs and lows that lend structure to market trends.

8.1 Trading Rules - Engulfing Candlestick

Bullish Engulfing

1. Higher swing high and higher swing low
2. Buy with bullish engulfing candlestick pattern
3. High of pattern must stay below previous swing high

Bearish Engulfing

1. Lower swing high and lower swing low
2. Sell with bearish engulfing candlestick pattern
3. Low of pattern must stay above previous swing low

8.2 Engulfing Candlestick Trading Examples

Winning Trade - Bearish Engulfing

Engulfing Candlestick Trading Winning Trade

This is a daily chart of Allergan (AGN on NYSE). It shows a market plunge that erased months of gains.

1. The lower swing high and low confirmed the beginning of a downwards trend with the climatic bear bar.
2. Prices retraced up immediately after the drastic fall. The bull move stopped as a bearish engulfing candlestick emerged.
3. The bearish engulfing candlestick pattern formed on the mid-point (50% retracement) of the strong bear trend bar which provided resistance.

Losing Trade - Bearish Engulfing

Engulfing Candlestick Trading Losing Trade

This daily chart of Cardinal Health (CAH on NYSE) shows a bearish engulfing pattern that didn't follow-through.

1. Technically, there was a set of lower swing high and low.
2. However, in this case, the swings did not push out of the sideways movement of CAH. Hence, the lower high and low structure was not a reliable indicator of a downwards trend.
3. The bearish engulfing candlestick pattern led to a losing short trade, as prices broke out above the trading range.

8.3 Review - Engulfing Candlestick with Market Structure

Many trading strategies use engulfing candlestick patterns as a signal for major trend reversals. That is a low probability strategy. However, as we use engulfing patterns for continuation trades here, we have better odds.

Many candlestick traders wait for one more candlestick after the engulfing pattern as confirmation. For this trading strategy, you

should not wait for confirmation for most trading setups. Waiting for confirmation worsens our reward to risk ratio.

If you wait for confirmation, the trading setup is likely invalid due to trading rule 3. Basically, that rule keeps us away from taking trades that have poor reward to risk ratio.

Observing swing highs and lows is the simplest way to follow market trends. It builds on the market structure and does not need any trading indicator. While this approach gives some confusing signals during deeper pullbacks, its simplicity is still attractive. Regardless of your trading strategy, paying attention to the market structure will help you filter bad trades.

Read: Take Only The Best Trades

Congested markets might have many engulfing candlestick patterns with no follow-through. Be careful and avoid signals in sideways market. Look for clear swings to avoid congestion.

Hone your skills in reading the market structure. It is invaluable in any trading method.

9. Hikkake Trade Setup

Dan Chesler discussed this candlestick trading setup in the Active Trader Magazine in April 2004 ("Trading False Moves with the Hikkake pattern"). Hikkake means trap, trick or ensnare. This trade setup seeks to **profit from false breakouts**.

9.1 Trading Rules

Rules for Long Hikkake

1. An inside bar
2. The next bar has a lower high and lower low
3. Place buy order at the high of the original inside bar for the next three bars
4. Cancel order if not triggered after three bars

Rules for Short Hikkake

1. An inside bar
2. The next bar has a higher high and higher low
3. Place sell order at the low of the original inside bar for the next three bars
4. Cancel order if not triggered after three bars

9.2 Hikkake Trade Examples

Winning Trade - Hikkake Trade Setup

Hikkake Winning Trade

This is a daily chart of Cairn Energy listed on the London Stock Exchange. We had an inside bar, followed by a bar with a higher high and higher low, providing us with a Hikakke setup. We placed a sell order at the low of the inside bar. Two days later, price triggered the sell order and the stock went plummeting into profits.

This was an excellent trade as there was a **downwards trend** followed by a series of five bullish bars, which gave reasonable hope to the bulls. Hence, **bullish traders saw the inside bar as a low-risk entry** for a trend reversal upwards. Note that the inside bar had a good follow through, but not good enough to even test the bear trend bar three bars before.

When the Hikkake setup came along, price went south and stopped out the bulls. However, the hope for a reversal was strong and prices went back to test our entry price two bars later. When that test failed too, the downwards trend continued.

Losing Trade - Hikkake Trade Setup

Hikkake Losing Trade

This is a daily chart of International Power PLC. We saw a bearish inside bar followed by a bar with a higher high and higher low. We placed a sell order at the bottom of the inside bar. An outside bar triggered the sell order. Prices began to drift upwards after that and we lost the trade.

There were two main reasons not to take this trade. First, price **broke a bear trend line** (not drawn) before forming a higher low (six bars before the inside bar), hinting at a bullish context which was bad for shorts.

Next, for a short Hikkake to succeed, we have enough traders betting on a bullish breakout of the inside bar. However, as both the inside bar and the bar before it were bearish, traders were unlikely to bet on a bullish breakout. Moreover, it looked like a double top, which again deterred bullish traders. **Without bullish traders trapped**, this short Hikkake did not look good.

9.3 Review - Hikkake Trade Setup

This trade setup illustrates the concept of **trapped traders**. From whom do you think your profits come from? You always profit at other traders' loss. This is a fact of the market.

The inside bar has a smaller range and hence a smaller risk. This low-risk inside bar opportunity tempts many traders . The Hikkake pattern then sets up to enter when these traders have to exit with a loss. Understanding this concept of trapped trader will help you find the best Hikkake trading setups, which occurs when price has trapped many breakout hopefuls.

(Read: 4 Ways to Profit from Trapped Traders)

However, an inside bar is a **contraction in range** and may lead to a tight trading range where price action becomes rather unpredictable. This explains why this setup often fails with an outside bar, which shows strength in both directions. Remember, the context gives the edge.

(Learn: Using Candlestick Patterns with a Moving Average)

10. Capture High Profits with Low Volume Pullback Trading Strategy

Dow Theory relies on volume as a secondary indicator to confirm price action. Nonetheless, interpreting market volume has developed into a whole branch of technical analysis (volume spread analysis) and spurred many traders to create volume indicators. In this review, we will focus on trading low volume pullbacks in trends.

Like everything else in trading, absolute values are useless. Rather than "low", we actually mean "lower". We look at changes in volume.

When volume increases, traders are interested. When volume decreases, traders are not keen. The market does not move when traders are not interested. **So, the idea is to fade low volume moves**.

10.1 Trading Rules - Low Volume Pullback

Long Trading Setup

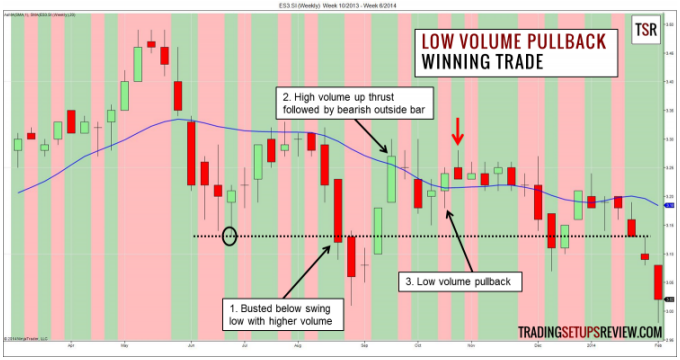
1. Price is above the 20-period simple moving average (SMA)
2. Price breaks above the last swing high with higher volume
3. Price falls with lower volume
4. Buy a tick above the next bullish bar

Short Trading Setup

1. Price is below the 20-period SMA
2. Price breaks below the last swing low with higher volume
3. Price rises with lower volume
4. Sell a tick below the next bearish bar

10.2 Low Volume Pullback Trading Examples

Winning Trade - Short Setup



Low Volume Pullback Trading Strategy - Winning Trade

This is a weekly chart of SPDR Straits Times Index ETF (ES3.SI on SGX). It seeks to replicate the performance of the STI which is the main gauge of Singapore's equity markets.

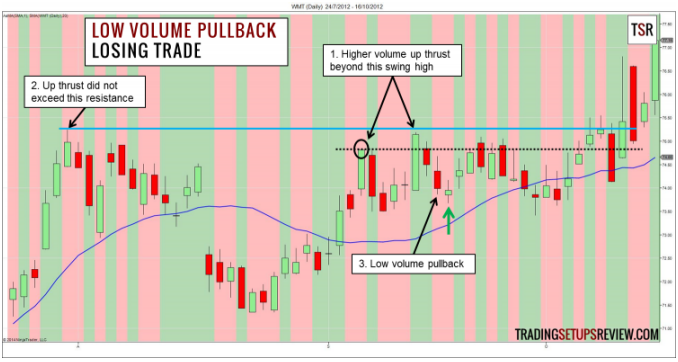
Volume overlays are great trading tools. They allow you to keep tabs on volume while you look at price action. They mitigate the risk of ignoring price action and focusing only on volume. In this case, green means higher volume than the previous bar, and red means lower volume.

Get the overlay here.

1. After moving up to test the SMA, price plunged down below the earlier swing low with higher volume (as shown by the green background). It confirmed that bearish momentum was still in place.
2. As prices pulled back up, it seemed as though we would not have a low volume trading setup. The pullback bars rose up sharply with higher volume. However, the bearish outside bar halted the up thrust and signaled the return of the bears.
3. Two bars later, we got an up bar with lower volume. It verified the lack of market interest in pushing prices higher. The next bar was a solid bearish reversal bar. We sold a tick below its low.

It took 15 weeks, but this trade proved profitable as the ETF fell to its earlier extreme low.

Losing Trade - Long Setup



Low Volume Pullback Trading Strategy - Losing Trade

This is a daily chart of Walmart.

1. Shortly after price moved above the SMA, it made a new high with higher volume.

2. However, if we extended our perspective, we would have noticed that price failed to rise above a key resistance that sent prices down below the SMA earlier. This failure made the picture less rosy.
3. We had a low volume pullback followed by a bullish reversal bar. We entered a tick above the reversal bar.

The trade's maximum profit potential is larger than the amount we risked. However, the trend did not resume until it moved below our signal bar to test our stop-loss level.

10.3 Review - Low Volume Pullback Trading Strategy

We used basic volume trading principles directly to create this simple low volume pullback trading strategy.

We looked for increasing volume during break-outs to confirm the market momentum. Then, we took advantage of low volume pullbacks to time when we enter the momentum.

(Like the idea of using volume to confirm trend break-outs? Check out the Yum Yum continuation pattern.)

This trading strategy is extremely useful for clarifying price action. When you can't tell what price is trying to do, volume might shed some light.

Paying attention to low volume pullbacks also improves other retracement trading strategies. Combine this low volume approach with the following setups.

- The Holy Grail
- Two-Legged Pullbacks
- 9/30 Trading Setup

If you want to pick up more ideas about using volume in trading, have fun with these.

- On-Balance Volume (OBV) Trading Strategy
- A Complete Guide To Volume Price Analysis
- Investing with Volume Analysis: Identify, Follow, and Profit from Trends

11. What's Next?

Strategies alone are useless. Profitable traders do not trade strategies. They trade the market. Understanding the price action concepts underlying the market is more important than learning all the trading strategies in the world.

To complement these trading strategies, here are some recommended options.

11.1 How to Trade with Price Action (eBooks)

You have just completed the Strategies Edition of this 3-book series.

The Kickstarter Edition gives a solid foundation with basic price action concepts and terms that will bring you a long way.

The Master Edition explains the more advanced concepts in price action trading with a focus on intraday trading.

Click here to download the 3-book "How to Trade with Price Action" series for free (or pay what you want).

11.2 How to Trade with Price Action (Online)

The "How to Trade with Price Action" eBooks are compilations of selected articles on Trading Setups Review and are updated periodically.

For our latest articles on price action trading, visit our website now.

11.3 Day Trading with Price Action Self-Study Course

Interested to learn the complete price action trading framework I use to trade? Take a look at my self-study course.

Click here to learn more.