



The Daily Breakout Strategy

How to Trade Breakouts in Forex

It is always the same question for traders of all experience-levels in Forex: Which strategy achieves the most profit and which trading system will save the account in the forex market? We cannot promise the Holy Grail, because it simply does not exist in trading. But there is a helpful strategy that achieves high profits in volatile market phases: the breakout strategy.



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Maite Krausse has been interested in the stock markets since taking her degree in business administration. Today she is a professional day trader and is specialised on forex. Her husband and Maite offer professional support to traders – finding daily trading signals, analysis and tips.

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» Simple Approach – Huge Effect

Breakouts are best used with the majors, the five major currency pairs. We use the volatile trading times of the European and American trading session (8 am until 10 pm Central European Time) to cover the fundamental events.

The price range that the price shall “break” is formed from 12 am to 8 am CET and offers the trader the basic



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trading approach for the following day at 8 am. This range is valid for the particular day – you'll define it again on the next day and therefore this strategy is useful for day traders.

The highs until 8 am are the upper border and the resistance level and the lows are the support levels. If the price exceeds the high or undercuts the low, the buy order above the high or the sell order below the low is executed. The trader does not need to watch the chart the whole time – we enter pending orders at 8 am for the buy and sell entries.

As soon as a buy or sell order is executed the trade is managed all day – we use a 1:2 risk-reward ratio on quiet days and a risk-reward ratio of 1:4 on economically important days, for example a Fed decision regarding interest rates.

We do not risk more than one or two per cent of trading capital per trade – in contrast to four or eight per cent of profit possibility. Trade management is simple with an automatic trailing stop of 15 to 25 pips.

Entries

We observe the price range between 12 am to 8 am CET in the 15-minute chart. During this time we determine the highs and lows. We enter two to five pips above the high or two to five pips below the low.

Furthermore, we look at support and resistance levels in the hourly chart. We determine sell orders above resistance and sell orders below support.

Exits

Greed is one of the cardinal sins in trading. But every trader knows the

feeling of a trade in profit and you want to achieve even more pips. This is a very human feeling and therefore you need a strong trading plan with fixed take-profit rules. We calculate it based on the RRR and we follow it strictly.

For example, we can determine the stop-loss (SL) at 20 to 30 pips. The take profit (TP) is determined at 40 to 100 pips, depending on market fluctuation. We choose a smaller TP in quiet market phases and a higher TP on days of interest rate decisions and other big events.

If a trade is stopped out with a loss, we can re-enter on the same day, again with a pending order.

The breakout strategy is now clearly determined and that helps the psyche of the trader – cancelling out greed and fear. You should always follow your entry and exit rules and you should accept false breakouts or huge profits after your TP.

F1) EUR/USD on 22nd August, 2014, 30-Minute Chart



You see the circles of the entry levels (green for long, red for short). The price range is defined by the high at 1.3289 and the low at 1.3273. The long entry would be at about 1.3294, but it is within the resistance area at 1.33 and therefore we would place the buy order above 1.33. The same goes for the support level. The short entry would be at 1.3268 – you could choose the round number 1.327. The short trade would have been profitable. The EUR/USD decreased about 50 pips from 1.327 within one hour.

Source: www.tradesignalonline.com

F2) False Breakout EUR/USD on 26th August, 2014, 30-Minute-Chart



An example for a fakeout in the EUR/USD. As the entries are valid until 9 pm, we could have compensated the lost pips on the short side during the US trading session.

Source: www.tradesignalonline.com

and you define the new entries on the following day.

Breakouts and Fakeouts

Every strategy has its ups and downs. The breakout strategy works well during trend phases and volatile markets, but there are more false breakouts, so-called fakeouts, during sideways phases.

Therefore it is important to limit losses and secure profits by using trailing stops. If a trade is stopped out with a loss, we can re-enter a second time, if the signal appears again. Of course we again limit our risk to one to two per cent of our trading account.

There are days where you think there are only fakeouts and then it is wise to stop trading or to minimise the risk further. Because one thing

is sure: The market never reacts the same, but the next profitable phase will arrive!

Daily Breakouts with the Highest Profits

The highest profit probability is usually coincident with price developments influenced by fundamental events. Therefore it is helpful to take a look at the economic calendar, because the biggest moves often occur on surprises and new information on the economic situation of a country and its currency.

Especially interesting are Fed decisions regarding the interest rates and protocols. You can raise your TP to 100 or more pips on such days.

The market includes speculation and news in the monetary policy of important currencies in advance. Therefore, it is very important to get an overview of the current economic and political situation and you should always take a look at the higher time frame like the 4-hour or daily chart to recognise primary trends.

Trading Times

After you defined the entries as well as TP and SL trading starts at about 8.30 am CET. The entries including SL, TP and trailing stops are entered in the system of your broker and are valid until 9 pm. Then the orders are cancelled

F3) Head-and-Shoulder Formation GBP/USD, Hourly Chart



The inverse head-and-shoulder formation predicted a long breakout with an entry above the neckline.

Source: www.tradesignalonline.com

This way you can increase the hit rate in the direction of the trend. A glance at the chart of the past week confirms the enormous downtrend-potential – due to political crisis and speculation about the interest rate policy of the Fed. You can also enter swing trades of several days in strong trend phases – but always trail the stop and take profits!

Evaluation and Help

Not every breakout offers the same profit possibility and you should be able to evaluate the better possibilities and the valuable entries. The professional trader uses tools to help with the decision.

For example breakouts from symmetrical patterns, like increasing or decreasing triangles, double top/bottom- and head-and-shoulder formations. If the price formed such a pattern you should be alert and you should plan your entries based on these patterns. The intensity of such

Moving Average Convergence Divergence (MACD)

Gerald Appel developed the indicator that is very well known in trading. It calculates two lines. The faster line (MACD-line) is the difference between the exponentially smoothed moving average based on the closes, most of the time over a period of twelve and 26 days. The slower line (signal line) is the exponentially smoothed 9-period average of the MACD-line. Most investors trade buy and sell signals at the cross of these two lines. The difference between the lines can be displayed in the MACD-histogram.

breakouts is often stronger if a pattern formed on a higher timeframe (for example on the daily or 4-hour chart).

Another way to identify breakout chances is to recognise certain candle patterns on the daily chart. For example the inside-bar candle is a very popular

Preview of the next Issue

COVERSTORY



The Sorrows of Young Trader

You probably heard about some great success stories of traders that doubled or tripled their accounts in no time, or even became Market Wizards. But what about the path of getting there? What about the path of becoming good enough? Today Maite Krausse of MaimarFx.com will tell a fiction backstory. A backstory that's happening way more often, but which is rarely if ever told.

PEOPLE



Interview Jens Rabe

In the current November issue, we're publishing a cover story about options trading written by Jens Rabe of r2fag.com. Marko Graenitz went to interview him in his trading room. Stay tuned for some insights to how he managed to shift his career from selling insurance to professionally writing options for a living.

The December issue of TRADERS' will be published on **27th November 2014**.

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F4) Inside Bar Daily Chart EUR/USD



The long entry above the high of the inside bar would have achieved 50 pips and the short entry below the low of the inside-bar would have achieved over 100 pips. The inside bar started a downtrend that still goes strong.

Source: www.tradesignalonline.com

pattern for predicting a breakout in trend direction or as a reversal. An inside-bar formation is confirmed, if the following daily candle with the contrary colour (day 2) has its high and low within the range of the prior daily candle (day 1). The entry on day 3 is above/below the high/low of the second daily candle.

There are countless other methods for rating the strength of a breakout, for example based on the RSI (Relative Strength Index) or MACD (Moving Average Convergence Divergence). If the MACD-histogram is small and has short bars, the momentum is low and the breakout may not have much strength. If the MACD-histogram is large it induces a strong momentum and therefore the probability of a strong breakout is high.

It is important to focus on strong price developments and to ignore small details. The trader has to follow his rules and must not try to predict the price. Because one day the market acts logically for the disciplined trader, but on the next day it may react totally illogically.

Conclusion

Trading breakouts is a strategy that many traders use and it delivers good results for swing trading as well as day trading. The best results are achieved during volatile market phases or strong trends – indecision of market participants most of the time results in a low hit rate.

If you can identify breakouts, there is a good possibility of getting high-quality entries and to swim with the “big fishes”. The trader will not miss a trade and he will achieve good profits in big trends and strong movements. «

Strategy Snapshot

Strategy Name:	Daily breakout strategy
Strategy Type:	Trend following
Time Frame:	Day trading
Setup:	Definition of the price range 12 am to 8 am 2-5 pips above/below the high/low entry with pending orders for the following day. Entry based on support/resistance levels. Trades that are stopped out can be re-entered
Entry:	Long 2-5 pips above the high, Short: 2-5 pips below the low
Stop-Loss:	20-30 pips
Take Profit:	40-100 pips
Trailing Stop:	15-25 pips
Risk Management:	Risk per trade: 1-2% of the trading capital
Average Number of Signals:	1-3 trades per day per currency