I’m guessing you don’t like trading breakouts…

…because you’re afraid the breakout might fail, right?

It’s a sucky feeling to go long on a breakout, only to watch it reverse and hit your stops. Ouch.

But have you ever thought, what if the breakout trade is a winner, what’s your reward?

Well… you can ride massive trends in the markets. You can catch favourable risk to reward trades. You can be profitable on your trade right from the start (with no turning back).

Can you see the power of trading breakouts?

I sure hope so!

Because here’s what you’ll learn in today’s post…

- What is breakout trading and the benefits of it
- The biggest mistakes to avoid when trading breakouts
- How to find high probability breakout trades
- How to enter your breakout trades
- How to set your stop loss for breakout trades

Are you ready?

Then let’s begin…

What is breakout trading and the benefits of it

A breakout occurs when price trades beyond:

1. Swing high or low
2. Support or Resistance

Here are some examples…

The benefits of breakout trading

There are several benefits to trading breakouts. For example…

- **Momentum is with you** – Trading breakouts allow you to enter your trade with momentum at your back
- **Catch big trends** – If you were to trade pullbacks, sometimes it may never come. But with breakouts, you never have to worry about missing another move in the markets

You're probably wondering:

"Rayner, if trading breakout is such a profitable method, why don't most traders do it?"

Because of these 2 words… false breakouts.

But here’s the thing:

False breakouts are simply the cost of doing business.

And it doesn’t matter which trading method you use, there will be losers along the way.

Whether you’re trading pullbacks, reversals, Support & Resistance etc.

If you can overcome this mental “barrier” of yours, you’ll get to see the power of trading breakouts.

Imagine catching moves like these…

But first… let me share with you how not to trade breakouts.

The biggest mistakes to avoid when trading breakouts

Here’s the deal:

Not all breakouts are created equal.

There are times when it’s worth trading a breakout, and times where the reward is not worth the risk.

Now you’re probably wondering:

When should I avoid trading breakouts?

- Don’t trade breakouts when the market is far from Support/Resistance (S/R)
- Don’t trade breakouts without buildup

Let me explain…

Don’t trade breakouts when the market is far from Support or Resistance (S/R)

Trading breakouts when the market has moved far away from S/R is never a good idea.

Why?

Because you don’t have a logical level to place your stop loss. Even if you do, it usually results in a poor risk to reward profile.

Pro Tip:

If it seems you’re “chasing” a breakout, then it’s usually a bad trade.

Don’t trade breakouts without buildup

I get this question a lot…

Rayner, what do you mean by buildup?

To put it simply, buildup means consolidation.

So… if you see the market has moved a long distance towards a key level (without buildup), chances are it will fail.

Here’s an example:

You’re probably wondering…

Why is this so?

Here’s an explanation:

Traders in profit will exit their positions at the nearest swing high (to protect their profits).

And traders looking to short will do so at the swing high.

After all… they want to sell high, right?

So here’s what happens…

You get a double dose of selling pressure. From traders exiting their long trades, and traders looking to short the markets.

With so much selling pressure at the same area, chances are, the breakout would fail.

Make sense?

How to find high probability breakout trades

Wouldn't it be great, if you know which breakout trades have higher odds of success?

Well… you could. And I'm going to show you how…

Based on my experience, these are the best times to trade breakout:

1. When the market is trending strongly
2. When there's no Support/Resistance nearby
3. When the market is forming buildup at Support and Resistance area
4. When there are higher lows into Resistance or lower highs into Support

Let me explain…

1. When the market is trending strongly

I'm sure you can agree with me on this…

If the market is trending strongly, you're unlikely to catch the trend on a pullback.

You've probably experienced this yourself and know the pullback just doesn't come.

So, what can you do?

Well… you can trade the breakout, right?

Here's what I mean…

You can get long when price trades above the swing high, and place your stops below the “respected” moving average (in this case, it’s the 20 EMA).

Pro Tip:

When the market is trending strongly (with little to no pullbacks), look to trade the breakout instead.

2. When there’s no Support/Resistance nearby

Think about this:

If you’re short the market, where would buyers come in?

If you’re long the market, where would sellers come in?

Support and Resistance, right?

Thus, the best breakout trades occur when you’ve got no “opposing force” against you (or it’s far away).

Imagine:

If you want to go short when the market is trading at all-time highs.

Where will you short?

There’s no resistance, swing high, or pivot high you can rely on. This makes it difficult to trade against the trend.

Thus, my favorite breakout trades are the ones trading at all-time highs/lows.

Because there is little “opposing force” against the dominant trend.

Those who attempt will cut their losses and fuel further price advance.

3. When the market is forming buildup at Support and Resistance area

This is another of my favorite when trading breakouts.

It's an advanced concept, but I'll break it down so you can understand.

If you remember:

I said avoid trading breakouts without buildup.

Now the question is…

Why do you want to trade breakouts with buildup?

Here's why:

A buildup would attract stops in the market as traders place their stop-loss beyond the highs/lows of the consolidation.

It could be to protect their existing positions or to trade the breakout in either direction.

So, when the market breaks out of consolidation, you get a double dose of pressure.

And it's caused by traders looking to protect their positions and traders looking to trade the breakout.

An example:

4. When there are higher lows into Resistance or lower highs into Support

Higher lows into Resistance is a sign of strength by the buyers and there's a good chance the market will break out higher.

Why?

Because if there were strong selling pressure at resistance, the price should have fallen quickly.

The fact it didn't tell you that buyers are willing to buy at higher prices and thus forming higher lows into Resistance.

Visually, it looks like an ascending triangle.

Here's an example:

And when you get lower highs into Support, it's a sign of strength by the sellers.

Because if there were strong buying pressure at Support, the price should have risen quickly.

The fact it didn't tell you that sellers are willing to sell at lower prices and thus forming lower highs.

Visually, it looks like a descending triangle.

An example:

Does it make sense?

Good.

Because in the next section, you'll learn how to enter and exit your breakout trades…

How to enter your breakout trades

So, you've learned what a breakout is, the mistakes you should avoid when trading breakouts, and how to identify high probability breakout setups.

Now you're probably thinking…

Rayner, how do I enter my breakout trades?

Well, there are usually 2 ways you can trade a breakout.

Either you wait for a candle close, or you use a stop order.

You wait for a candle close:

- It's easier to execute the trade psychologically as the candle has closed in your favor
- You may get a poorer risk-to-reward (as the market has already moved in your favor)

You trade breakout using a stop order:

- It's harder to execute the trade psychologically because there are no signs of "confirmation"
- You usually get a better risk-to-reward (as you're entering near the breakout level)

Now the question is, do you wait for a candle close, or not?

Truth be told, there's no right or wrong to either approach.

How to set your stop loss for breakout trades

Okay, so now you're thinking…

Rayner, I know how to enter my breakout trades.

But what about stops, how do I set my stop loss?

Well, I have a simple rule you can follow.

Your stop loss should be at a location where if triggered, will invalidate your trading idea.

So if I'm longing a breakout, I'll set my stop loss (1 ATR) below the lows of the buildup.

And if I'm shorting a breakdown, I'll set my stop loss (1 ATR) above the highs of the buildup.

Here's an example:

Summary

- Trading breakout allows you to trade with momentum, cut your losers fast, and catch big trends,
- Don't "chase" breakouts or trade breakouts without buildup
- It's ideal to trade breakouts when 1) the market is trending strongly 2) there's no Support/Resistance nearby 3) there is buildup 4) you get higher lows into Resistance (or lower highs into Support)
- You can enter a breakout after the candle closes or using a stop order
- You can set your stop loss 1 ATR away from structure when trading breakout