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Breakout Trading is the most underrated trading technique in the trading community!

Every trader (intraday, swing, positional, or scalper) should know how to differentiate between a genuine breakout and a false breakout.

Do you know why?

Read this thread!

(1/N)



It’s important to understand two herds that exist in the market:

1. Smart Money &

2. Dumb Money

‘Smart Money’ refers to big sharks who have money & information power who give direction & momentum.

‘Dumb Money’ refers to retail traders who often try to make quick money.

(2/N)

You should know one secret now.

Participation from smart money creates a "genuine breakout."

And the absence of smart money participation results in a "false breakout."

Hence, it is always a good idea to follow smart money (by knowing real or false breakout)

(3/N)

What is Breakout?

As per Investopedia

“A breakout is a stock price moving outside a defined support or resistance level with increased volume. A breakout trader enters a long position after the stock price breaks above resistance.”

(4/N)



The price broke the resistance trend line with high volumes in this image.

Similarly, few recognize it as a breakdown if the price breaks the support trend line.

To keep it simple, we will focus only on the breakout.

(5/N)



What is False Breakout?

As per Investopedia -

“A failed break occurs when a price moves through an identified level of support or resistance but does not have enough momentum to maintain its direction.”

(6/N)



But this definition of Breakout Trading doesn't hold good in many cases:

Look at some examples:

Example 1 - HDFC

(7/N)



Example 2 - Rain Industries



Example 3 - Kotak Mahindra Bank

(8/N)



Then how to Differentiate a "Real Breakout" from a "False Breakout"?

We need 4 parameters:

1) A Big Breakout Candle

2) Quick Time (the price shouldn't move in small candles after breakout)

3) Absence of Selling

4) Good Volume

(9/N)

1) A Big Breakout Candle

The breakout candle should be big as compared to the previous candle before the breakout.

It indicates the presence of "smart money"

(10/N)



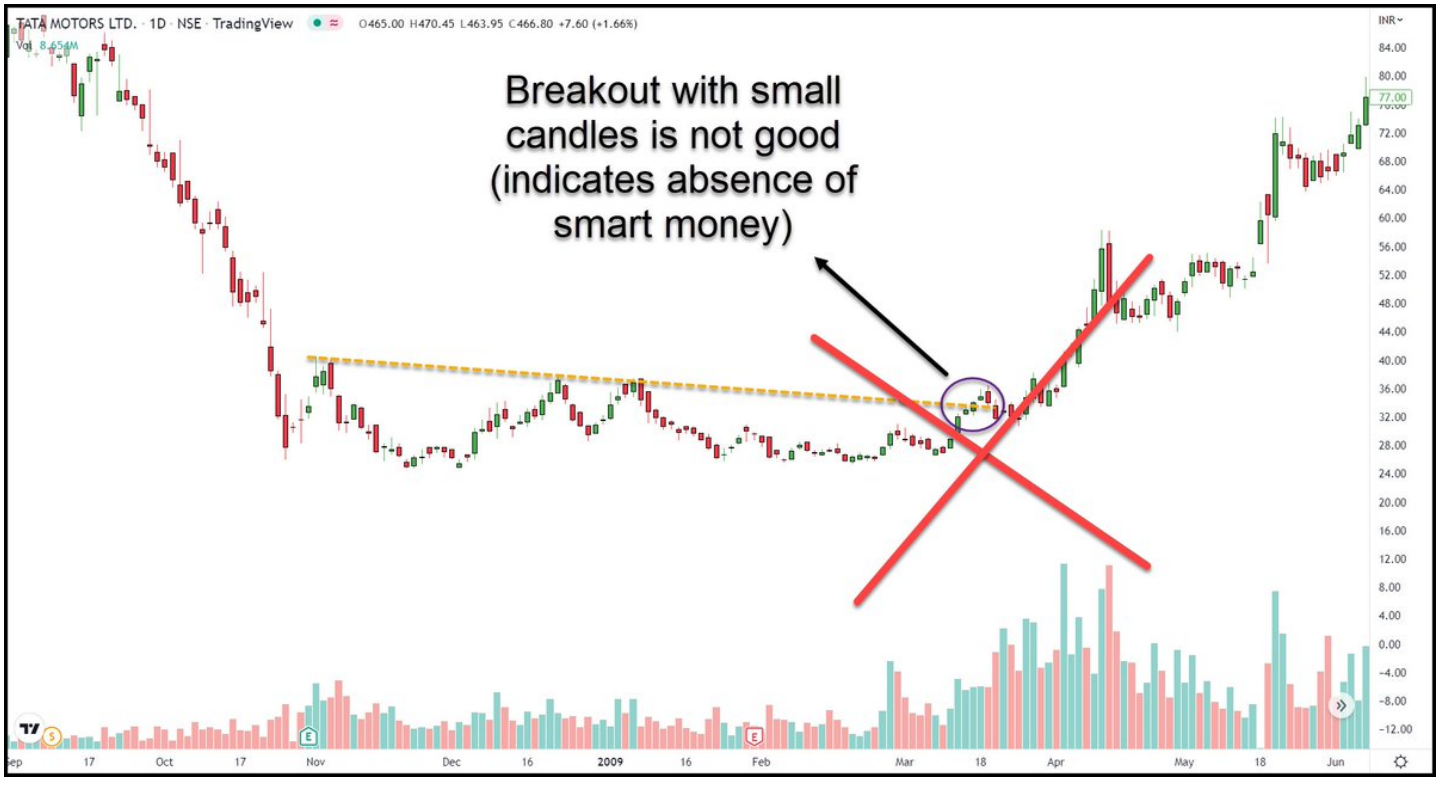
2 - Quick Time

A breakout should come in one quick candle (previous step).

It indicates the absence of "smart money"

A breakout with a couple of small candles is not good (as shown below)

(11/N)

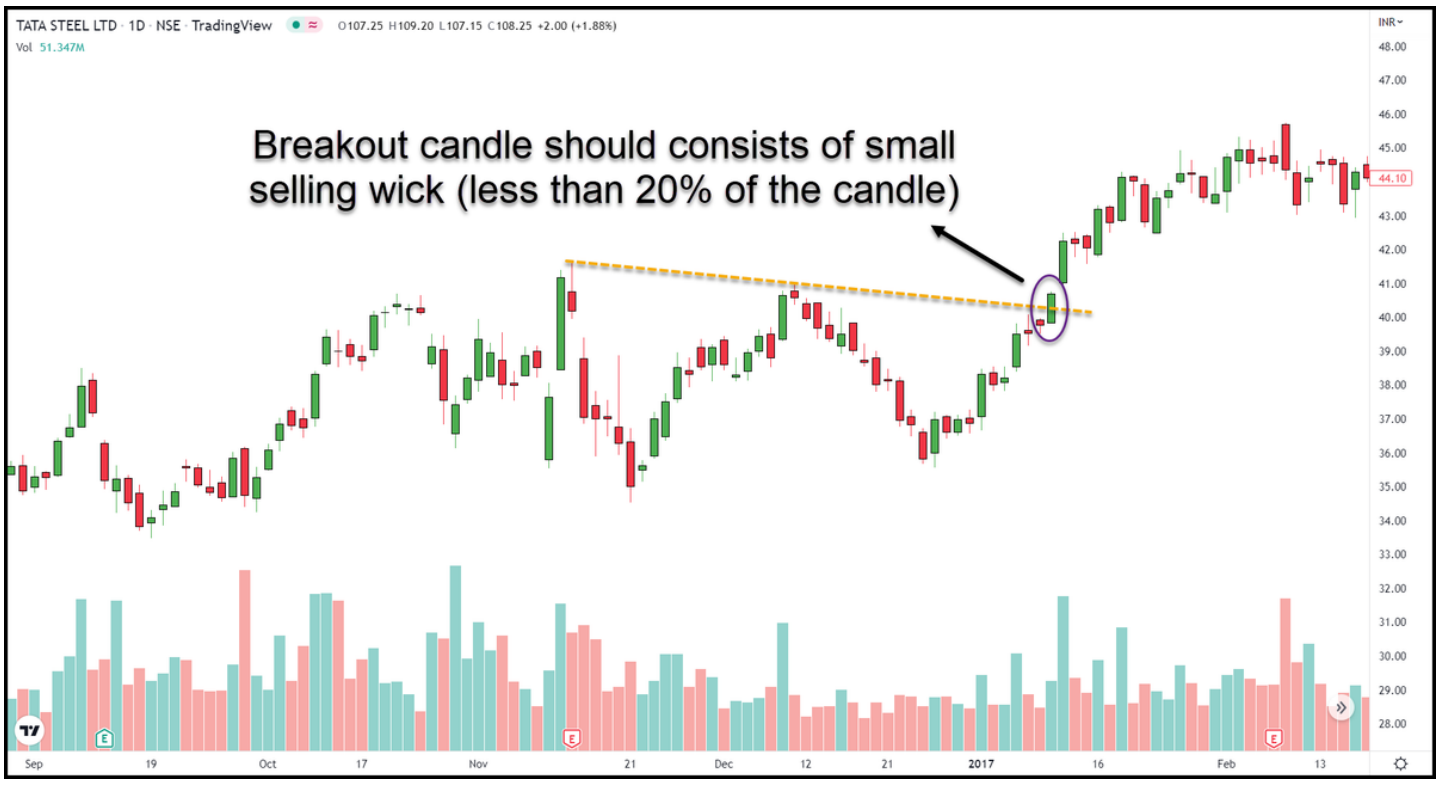


3 - Absence of Selling

Breakout candle should have no selling wick or the selling wick should be less than 20% of the breakout candle.

It indicates smart money is keen to carry the position!

(12/N)



4 - Good Volume

Good volume indicates the presence of smart money.

(13/N)



Below are some examples which satisfy all these conditions:

Example 1



Example 2



Example 3

These charts displayed these four characteristics at the time of breakout, and hence, the price showed a good move on the upside later.

There is a high probability of a good upside move if a chart displays all these characteristics during the breakout

(14/N)



Trade Management

As a trader, before entering any trade, you should know the bare minimum below 4 aspects:

- Entry
- Stop-Loss
- Profit Booking Level
- Risk per Trade

(15/N)



That's a wrap!

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