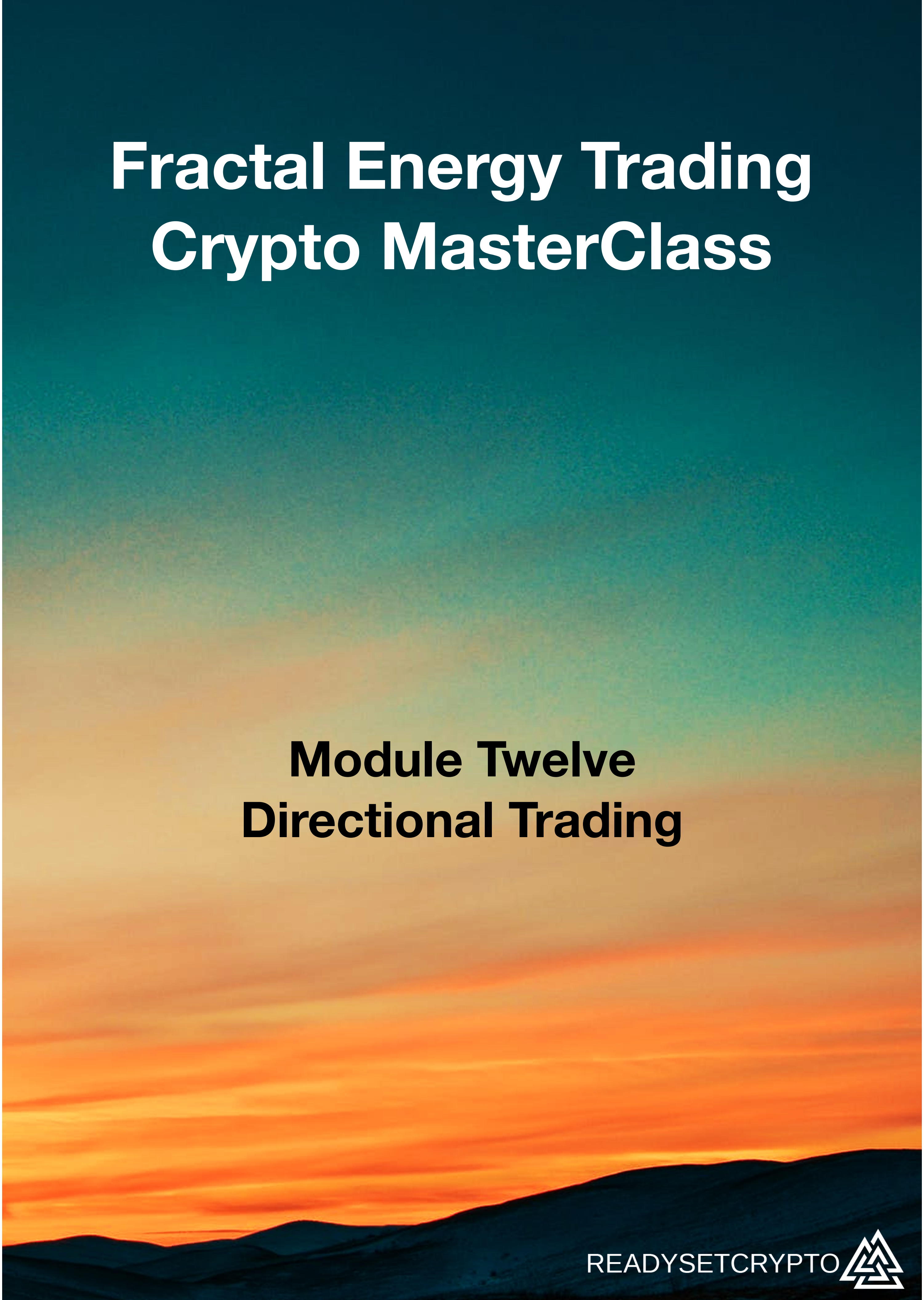

Fractal Energy Trading Crypto MasterClass

Module Twelve
Directional Trading

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By Doc Severson

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Introduction to Directional Trading

The concept of Directional Trading is fairly simple; you take a position long or short, and your goal is to have it gain value in the "direction" that you took the position.

- **Long** - This is most common, where you "buy low and sell high." You want the price to advance higher than your buy point, where you can sell it and reap the rewards.
- **Short** - Not as common, and typically only practiced by professionals and/or more advanced retail traders. You sell the asset to "open" and then buy it back to close the position. You want the price to drop after entry, where you can buy it back for a lower price.

Put another way, a long position is bullish, and a short position is bearish.

Don't be concerned if you've never encountered short positions, or your only exposure to short trades is the expression, "Don't sell yourself short."

We Will Only Cover Long Strategies

I think that learning to "short" the spot crypto market is a bad idea out of the gate for most retail crypto investors. Most Bear Markets are notoriously difficult to trade, and price action is much more linear during Bull markets. That means that it's more predictable, if there is such a thing. Perhaps it's that Bear markets and/or any type of corrective price action is much more "emotional" and thus more difficult to read.

In addition, there are ancillary reasons for not shorting the spot markets. Paying interest rates to "borrow" the token to short it, plus the ability to "borrow" might be limited with some coins, and is definitely not offered by all brokers in the space.

If you're going to take a bearish trade, do it with derivatives like futures or options, which for the most part are still very limited in scope with crypto.

We will only discuss "long" strategies in this program.

With that said, there are two types of long strategies/entries that I like to pursue with crypto trades: **Pullback** and **Breakout** entries.

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Pullback Entries

The context of a Pullback Entry is that 1) we have a strong Anchor trend to the upside, and 2) the Signal chart (usually Daily) timeframe executes a really strong pullback. The daily chart of BTC/USD shows one such pullback in Figure 1:

Figure 1

What makes this pullback notable? It's because the daily/signal chart has pulled back ***so hard*** against the major Anchor uptrend that it's gone into exhaustion. At this point it is highly probable that we'll see some type of counter-swing back higher to "relieve" the exhaustion on this hard drop…and don't forget that any "pop" higher will be in harmony with the larger Weekly/Anchor uptrend. (I have not included the weekly chart here for simplicity, please assume that it's an uptrend)

So do we just enter a long position once we see Pullback Exhaustion on the signal chart? That's "catching the falling knife," isn't it? There are two ways that we can do this:

- **Enter on Exhaustion** - The lower the better, especially once the Chop Index hits 25 or lower. This should produce a quick rebound at some point, even if it creates a lower high eventually.
- **Wait for Price Action reversal** - This method offers less edge, but is more sound. Wait for higher highs and higher lows to develop on the price of the signal chart, or perhaps even the intraday chart if you want slightly better edge. This is shown in Figure 2:

Figure 2

Note that you had to wait a couple of weeks for the full confirmation, but it was eventually worth it. A more aggressive "Enter on Exhaustion" entry would have gotten you in earlier, but to little benefit. The only advantage to that type of entry would be if the price ends up doing a full "v-bottom" which does occur.

The disadvantage of using this entry exclusively is that there are so few of them to use! I rarely see a chart pulling back to full exhaustion when it's in a primary uptrend. Most of the time the pullbacks are more limited in scope, limited to smaller timeframes, so a Slow Stochastic oscillator would be a better bet in that instance.

(I covered that method in my "Short-Term Trading Strategies" course)

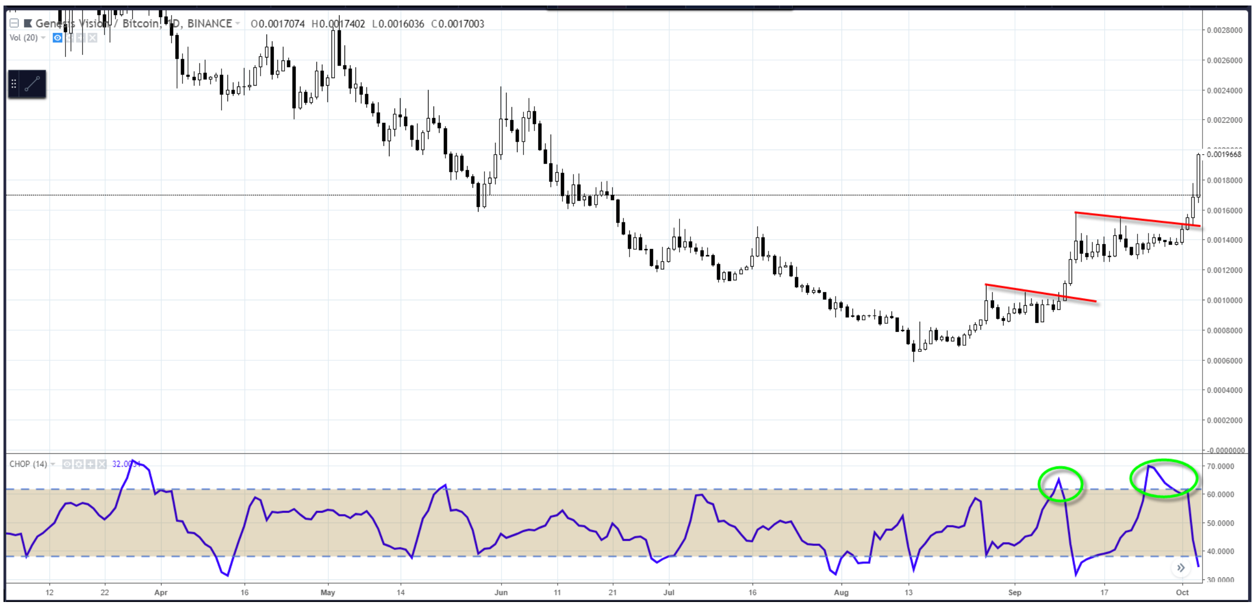
The next technique for directional entries I see ALL THE TIME and is the one that I use most often - the Breakout Entry.

Breakout Entries

I see Breakout Entries when a price chart is in the market character "Quiet/Trending." This means that it is almost stair-stepping higher in price, within the context of an Anchor trend higher. Range Contraction coils up the energy to a Breakout, and then it consolidates again before the next breakout.

Figure 3 shows a good example of a coin transitioning into this behavior:

Figure 3



You can see the high energy levels as shown by the green circles, and shortly thereafter you see the strong breakout higher. When should we enter these, after we identify the character and consolidation?

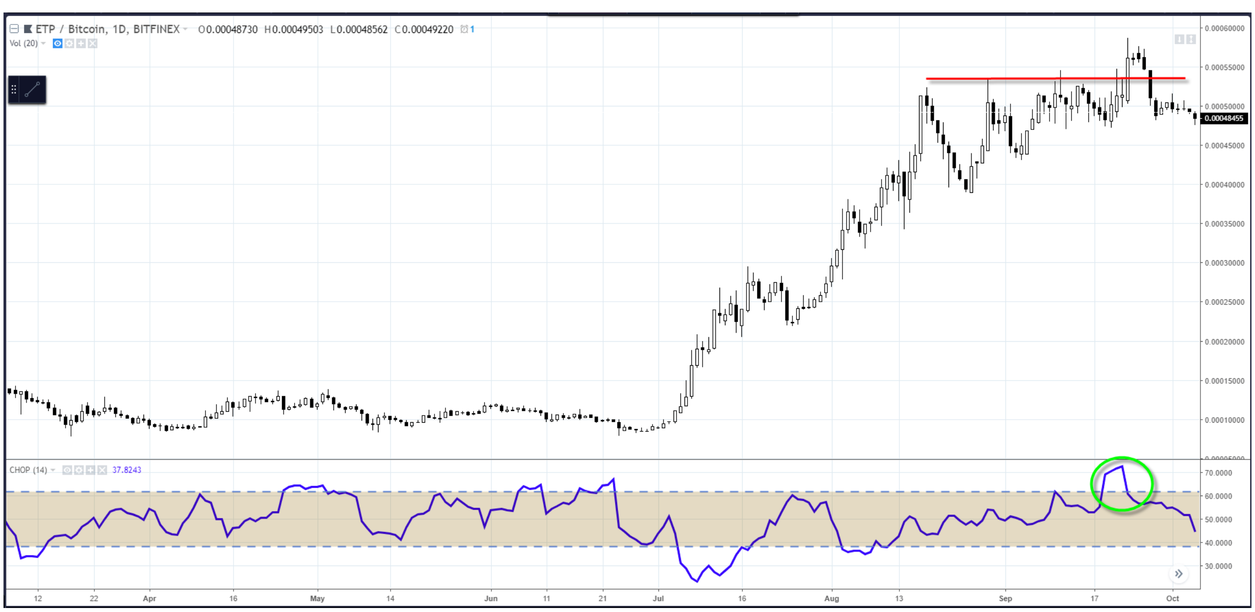
- **Enter In Pattern**- This is where we'll identify the behavior and the high energy level, typically above 61.8 Chop Index will not break long after that. We enter before the break.
- **Breakout Entry**- This method offers less edge, but is more sound. Wait for the trend line break (shown in red) to get a more "confirmed" entry. This is shown in Figure 4:

Figure 4

Note that the first consolidation triangle actually had the price break to the downside first! This is an example where waiting for the true break to the upside would have saved you from potential loss, as that would never have fired on the first pattern. The second pattern is more typical, with the correct breakout level identified.

Keep in mind that breakout entries can offer “false breaks” to the upside before being pulled back in, as in Figure 5:

Figure 5



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There is no way to avoid those, however coins in strong Anchor trends will typically break most reliably to the upside.

Choosing to enter either “mid-pattern” or “wait for the breakout” might depend on your own availability, temperament, or schedule. Many pattern breakouts occur in the middle of the night where I am, and as I wake up and see the notification, I have to evaluate if I’m too late. This is why entering mid-pattern can also be an effective method because some breakouts can occur on a whim and at the time when the least number of traders see it.

If I look for a breakout, normally I will place a “price alert” on the chart. You can also enter these positions based on “buy stops” to take you into the trade based on the price hitting a certain level, although you are then dealing (most of the time) with a market order.

Summary - Directional Trading

I really prefer that traders stay “long only” when dealing with spot crypto markets. It can be frustrating to watch a bear market and you might not have the ability to short the underlying coins, but there will be a flood of new derivative products soon that will allow you to trade risk-limited short positions much more effectively than just selling short the spot.

We talked about two different type of long entries based on price: 1) pullbacks, and 2) breakouts. If you see a market that offers LOTS of pullback entries in a trend, then you might want to consider using some form of oscillator. Yes, I know that I often disparage other studies, as you can still use just PRICE alone to enter on a shorter timeframe off of the pullback, but it can be difficult to read that reversal on the intraday chart.

This is why my favorite entry is the breakout from a consolidation.

Keep in mind that Bear Market Rallies might give you very few chances to make any gains in that swing; they will be short in length and very violent, so it’s imperative to get an aggressive entry. Rallies in Bull Markets offer much more potential.

Primary Bull markets are by definition much easier to trade bullish breakouts with, so be patient to wait for the right character to show!

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Homework and Next Steps

Please complete the following tasks before moving to the next module:

- [ ] Watch the associated video for this module.
- [ ] Look at your favorite coins, and see if they have offered any Breakout or Pullback entries over the past year.
- [ ] Do some Hard Right Edge price work to identify these entries and enter positions "on paper" to see how they would have worked out.

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