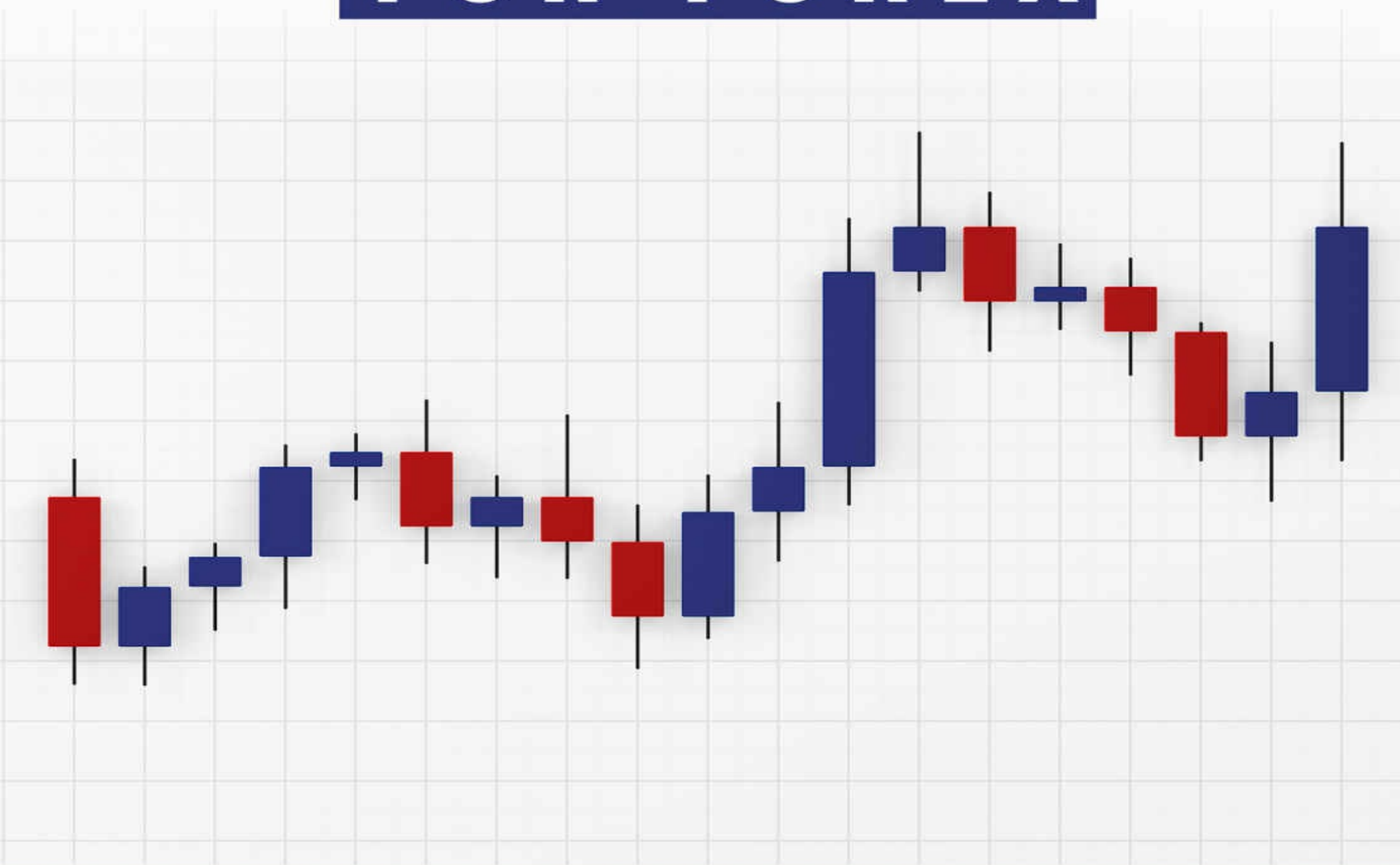
PRACTICAL PIN BAR TRADING

FOR FOREX



KC THORPE

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Practical Pin Bar Trading: Forex

Introduction:

In this e-book you will find the information necessary to educate yourself on how to trade Pin Bars in the Forex markets.

You will learn:

- The anatomy of a Pin Bar and why it forms.
- How to identify Pin Bars
- Pin Bar market context
- How to trade Pin Bars using “confluence”
- 3 types of trade entries
- 4 types of stop loss placements
- 3 types of take profit levels
- How to create a trading checklist

So without any further delay let’s gets straight to it!

Basics:

I thought I should spend some time covering the basics information and skills that I believe are required for getting the most out of the material contained in this e-book.

Understanding of the Forex Market

Firstly, there are thousands of books and websites that can provide you with information regarding what Forex is and how it works. Information such as a detailed history, descriptions of major market participants, and the mechanisms that drive price in the Forex market have all been covered by many other trading educators (I suggest looking at www.babypips.com or Currency Trading for Dummies if you are a beginner). This book is focussed on Pin Bars and how to trade them, not providing a detailed Forex trading course.

How to Place Orders

It is assumed that you are well versed in the use of Stop & Limit orders and how to attach stop loss and take profit levels to your orders in the trading software that you use. If you do not understand these terms then you should research them before reading this book (for example see Types of Orders on www.babypips.com).

Technical Analysis

There will be references to various Technical Analysis methods within the text and example carts provided in this material, at the very least it is assumed that you are familiar with the techniques in the list below prior to reading this book.

- Exponential Moving Averages
- Support & Resistance Lines
- Trend lines
- Fibonacci Retracements
- Candlesticks & charts

Bars / Candlesticks

Steve Nison brought candlesticks to the Western markets about 20 years ago and traders have been using them ever since. Numerous texts and websites are dedicated to candlesticks and there formations and with the exception of the Pin Bar, candlesticks and their anatomy will not be covered in this text.

Money Management

Money Management techniques can make or break your trading account. Principles such as risk to reward ratios, positive expectancy, drawdown, expected win / loss streaks and maximum percentage risked per trade should all be understood by the reader. If you wish to know more about this then read Van Tharps' "Trade your way to Financial Freedom".

Moving On...

One other thing to note is that most (if not all) of the information contained in this e-book can be found on the internet or in other publications (books, trading courses & DVDs) and as such I am not bringing anything new to the table as far as the Pin Bar is concerned. But, in writing this material I have tried to condense all of the knowledge I have gained from countless hours reading, trading and talking to other traders into one short book so that you (the reader) have an honest account of how to trade a very profitable setup without having to go through years of searching like I have.

So, now that we have gotten that out of the way let's get right into what a Pin Bar looks like and methods for trading it.

Pin Bar Anatomy.

So, what is a Pin Bar, and what does it look like? The term Pin Bar is derived from what Martin Pring used to call a Pinocchio Bar in his seminal book "Technical Analysis Explained". The premise behind the Pin Bar is that price is lying to you, and this is why Pring devised the name "Pinocchio" (after the fictional character who's nose grew every time he told a lie).

Why is price lying to you? Because when a Pin Bar is forming it provides you with a sense that price is making a sustained move in a certain direction (up or down) and that a breakout may be occurring, the problem with this move is that it is based on emotion and excitement and it doesn't last long before price retraces back to it's original level (or very close to it).

As Pring describes it, the forming of a Pin Bar is like two people having an argument that gets more and more heated with their voices getting louder and louder, and then at some point they realise they have gone too far and have been a bit silly, eventually they end up saying sorry and go back to the level in the relationship that they were before the argument occurred.

Note: Pin Bars show a time in the market when participants were a little emotional and price needed to come back to a more stable level.

Profiting from Pin Bar formations is as much about good judgement as it is sound trading analysis. Not every Pin Bar forms in the same way or at the price you want it to and there is always a degree of decision making or "discretion" that needs to be employed when trading Pin Bars.

Pin Bars are known to be part of "price action" trading and generally very few technical indicators are used when trading with them in this manner. This is because the behaviour of current price action is the major determining factor when trading, not technical indicators. Most indicators are derived from a series of previous prices and lag the current price action, but indicators can be useful when combined with price action to provide you more confidence when trading (known as "confluence").

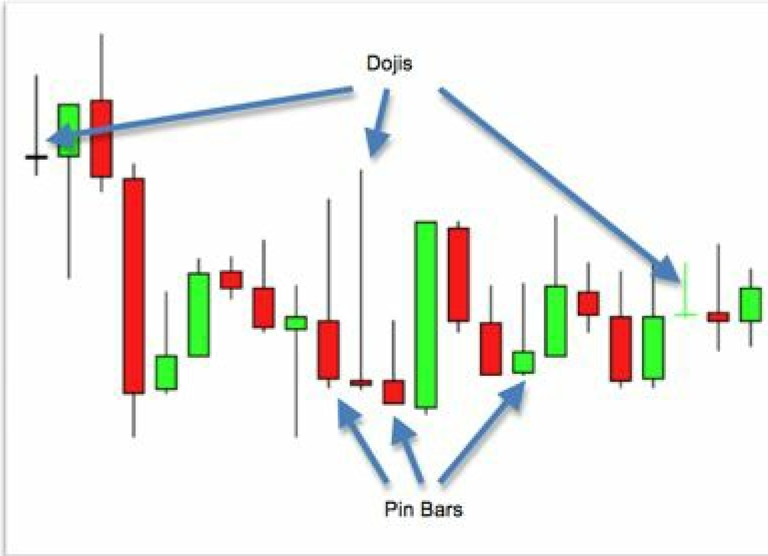
Form:

So, what makes a Pin Bar? Generally it is accepted that a Pin Bar is comprised of most of the following points:

- The "wick" (or tail) should be at least 2 - 3 times the length of the body.
- The body should be completely contained within the previous days range.
- The body should be present towards either the upper or lower extreme of the Pin Bar.
- The wick should stand out when compared to surrounding bars.

As they say "pictures speak a thousand words" and as such I will try to back up most of the material in this book with chart examples. So, some of the first things to look for are whether the body of the Pin Bar has formed inside the previous days trading range and the length of the wick when compared to the body.

Below are a few charts that show the difference between a Pin Bar and other single bar formations such as dojis. Pin Bars are different from dojis and as such they are traded differently (not covered in this book). Dojis are a sign of indecision in the market (because the close is very near to the open) and are a warning to exercise caution as the current trend may be over soon. Traders need to be aware of the difference between dojis and Pin Bars.



Points to note

- Generally Pin Bar signals are only relevant for the next 4 - 5 bars. So, if you watch the daily charts and a pin bar forms it will make most of its impact on future price moves within 4 - 5 days of its creation. This is because Pin Bars are short duration setups / formations (when compared to a head and shoulders formation) and because of this it makes sense that they will normally only affect the outcome of the bars immediately in the future.
- Pin Bars should not be traded in solidarity. There are many factors that influence whether or not you should trade a Pin Bar and for that reason you should not take a trade solely based on the fact that a Pin Bar has formed.

- Not all Pin Bars are created equally and again the choice whether or not to trade a Pin Bar should include the quality of the Pin Bars formation (read on for further clarification).

The best way to learn about Pin Bars is to open up some charts and try and find some for yourself. Once you have found a selection of Pin Bars, try and figure out whether or not they are good or bad Pin Bars with respect to their form and the candles that precede them.

Significance:

Now that you have scanned your charts and found some examples of Pin Bars there is another thing that you have to take into account. Is the Pin Bar significant? In other words, does the Pin Bar stand out form the previous bars / candlesticks?

There is a degree of discretion that has to be employed when deciding whether or not a Pin Bar is significant but one simple rule of thumb to follow is that the wick of the Pin Bar should be as large or larger than the previous days trading range.

Some traders and trading educators will claim that the bigger the Pin Bar the better, but my experience has shown that if the Pin Bar wick is more than 4 times larger than the average trading range of the preceding bars then it will most likely become a continuation pattern rather than a reversal pattern. When presented with a massive Pin Bar my advice is to stay on the sidelines and wait for a better opportunity to present itself as you have to risk too much capital in hopes of being profitable.

Context:

To be able to trade Pin Bars effectively you need to be able to gauge the direction of the trend and trade with it. The problem is defining whether or not a market is trending could be a book in itself, and traders employ many different methods for determining whether or not the market is trending. The list below is a few methods traders use to gauge the strength and direction of a trend:

- Moving Averages
- Trend Lines
- Average Directional Index
- Trader discretion

Most traders use a combination of these (rather than just one) to judge whether or not they are looking at a "bull" or "bear" market, but the reality of trading is that markets rarely go up or down in a straight line and more often than not spend most of their time in a trading range. You can never know in advance whether or not price will breakout of a range or continue trending but you can put the odds in your favour by utilising sound technical analysis and trading techniques as outlined in this e-book.

It has been said many times before that "the trend is your friend" and until you master the art of trading you should always be looking to trade with the trend. Nial Fuller from Learn To Trade the Market claims that 70% of counter trend moves fail, and this is a good enough reason for me to go with the flow rather than against it.

The best types of Pin Bar setups form when there has been a sustained moved (either up or down) and price retraces to an area of "value" or "interest". These areas can be support / resistance, trend lines, moving averages or large round numbers (all explained later).

Ideally a Pin Bar should close in favour of the prevailing trend, for example if the trend is up then the Pin Bar should have the close higher than the open **and** should be a bullish Pin Bar. The opposite applies for a down trend.

Pin Bars that are in heavy traffic or choppy, range bound markets should not be traded. The reason for this is that there is no clear trend and there are too many areas of interest for price to stall at.

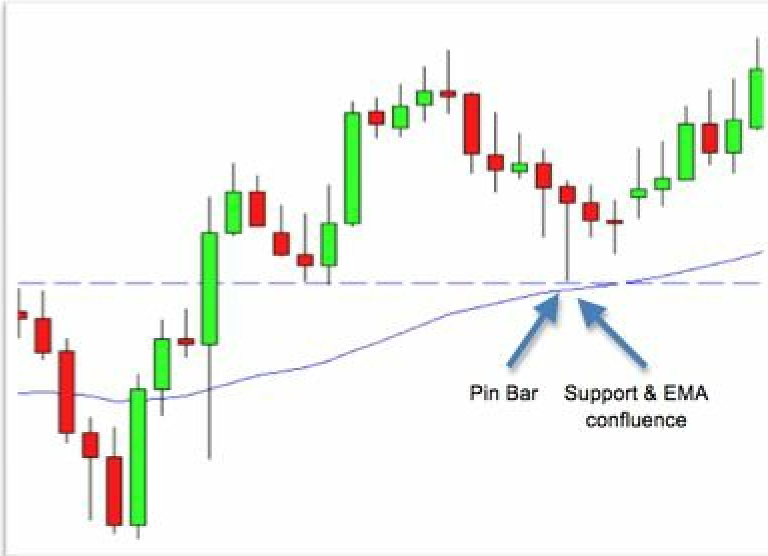
Pin Bars with high potential for profit generally form in space, which in simple terms can mean they form on the retrace to a trend line or some other level like 38.2, 50 or 61.8 Fibonacci retracement levels. The reason that you should look for Pin Bars that are created in "space" is because usually the potential levels for taking profit are a fair distance away from the Pin Bar, which means more profit in your pocket if the trade is successful.

Confluence:

As I have said previously Pin Bars should only be traded when they form in areas of "value" or "interest" and the more of these areas of interest that converge together near where the Pin Bar has formed the more significant the Pin Bar signal becomes, this is known as "confluence".

Support / Resistance (S/R):

One of the first things you should look for when you open a chart are areas of [support or resistance](). This is a very basic but very powerful tool in technical analysis and people have made money trading systems based purely off S/R levels. I prefer to use S/R levels in conjunction with other forms of technical analysis to increase my chances of success (i.e: confluence).



One universal truth of S/R levels is that old support becomes new resistance and vice versa and price tends to flip flop around these areas.

Large Round Numbers (LRN):

One thing that most trading educators fail to focus on is Large Round Numbers. The human brain finds it easier to remember and deal with large round numbers such as 1.0000 or 1.2000 rather than 1.0148 or 1.2234. For this reason large round numbers are levels that price action signals such as Pin Bars tend to form.

The significance of Large Round Numbers should not be underestimated in the Forex market. It is a well known fact that the psychology of market participants is a major driving factor of price in Forex. Fear, greed and hope all play a major role in peoples decisions when they trade and using round numbers simplifies their decision making process. Be on the lookout when price is near a round number, these levels become like magnets for Pin Bars.

Moving Averages (MA):

Moving averages come in two forms: the Simple Moving Average (SMA) or the Exponential Moving Average (EMA). Most traders use EMAs these days as they give more weight to recent price action and therefore react more quickly to recent events than SMAs do.

As well as being used to gauge the trend direction and strength, MAs can be used as dynamic levels of support and resistance. In some cases price can be seen to bounce off certain EMA values almost religiously during retraces in trending markets.

The only problem with EMAs is that everybody uses different period values depending on the time frame and markets they are trading. My advice is to pick two periods and stick with them, as once you get some experience under your belt you will start to learn how they behave in different market conditions and be comfortable with using them when trading. Some popular values of moving average periods are listed below:

8, 21, 50, 65, 150, 200 and 365.

Most professional traders that are looking at the daily or weekly time frame use the 50 and 200 day moving averages, but the choice is completely up to you.

Fibonacci Retracements (FIB):

If you have ever read anything about Forex trading undoubtedly you have come across Fibonacci Retracements. The 38.2, 50 and 61.8 retracement levels are the most important to watch out for when trading Pin Bars. I would not suggest trading a Pin Bar just because it formed at one of these FIB levels, try and find some more "confluence" such as an MA that is close to price or a significant S/R level to combine the FIB level with.

A lot of people ask why Fibonacci levels work in the Forex markets and the real answer is that no one knows, but they do have significance. I suspect the reason is that so many traders look for price action to appear at these values and it becomes a self fulfilling prophecy.

Trend lines (TL):

Trend Lines can be useful in trading to gauge trend direction or when you think a trend may have exhausted itself and is about to turn the other way. But there is another way to trade with them, especially if you are using Pin Bars. If the prevailing trend has been in place for some time and then retraces, sometimes you can draw a trend line and wait for price to retrace back to it and if you are lucky a Pin Bar may form right on the trend line.

As stated earlier, these can be the best types of Pin Bars to trade as you are not only trading in the direction of the trend, but normally your risk to reward ratio is substantial. In other words Pin Bars that form near retracements to Trend Lines or Fibonnacci Levels are usually created with "space" around them, which means there are generally fewer areas of interest nearby to get in the way of making some big profits.

A word of caution when using Trend Lines, the steeper the line the more likely that it will be broken by price and the less significant it becomes. This happens because if there is a period of consolidation followed by a sharp move in price the sudden jump (and subsequent trend line) is less likely to be sustained and the trend may break down. This is one of the biggest reasons most trading educators teach S/R and gloss over Trend Lines. The other major reason is because Trend lines are very subjective, everybody tends to draw trend lines in different ways.

Trend lines can also be used to form channels and these can be very useful in the Forex market. Price can be seen to respect channels and trend lines frequently, but remember they are not as reliable as horizontal support and resistance lines.

Sometimes trend lines can be broken and then price will retrace to them and they will change from being a support trend line to a resistance trend line. Just because a trend has been completed does not mean that the trend line is no longer valid.

Pivots (PP):

A vast majority of professional traders use Pivot Points in their arsenal of technical analysis tools. They are derived from averaging the high, low and close prices of the previous time period and as such are dynamic S/R levels. The reason why a lot of professionals use Pivot Points is that they are completely objective (unlike trend lines), this means everybody calculates them using the same formulas and the same set of prices, therefore everyone should be watching the same price levels, and like FIB levels they become a self-fulfilling prophecy. Pivot Points can be combined with any other technical indicator to provide confluence and are a great tool to use when trading Pin Bars.

Confluence Examples:


Pros:
Sustained up-trend
Pull back to 21 EMA & S/R Level
Bullish Pin Bar
Pin Bar


Pros:
Up-trend
Pull back to 50 EMA &
Fib 50% Level &
S/R Level
Cons:
Bearish Pin Bar in up-trend
S/R
Pin Bar


Pros:
Down-trend
Pull back to 50 EMA &
Fib 50% Level &
S/R Level
Pin Bar
Cons:
Bullish Pin Bar in down-trend


Pin Bar
1.2350
Pros:
Down-trend
Pull back to 21 EMA &
LRN &
Trend line
Bearish Pin Bar in Down Trend


Daily Pivot
Pros:
Overall down-trend
Pull back to Pivot &
Fib 78.6% Level
Cons:
Bullish Pin Bar in down-trend

Putting it all together:

Before we cover how to trade Pin Bars there is something that you need to know when it comes to placing orders. If you are an inexperienced trader you should **NEVER** place an order for “Market Execution”. Read that again, because I can't say it any more simply than that. The reason for this is that an order placed at market price is usually done out of excitement (not logic) and most likely does not conform to your trading plan (if you even have one).

Novice traders normally place Market Orders because they log onto their trading platform and see that a great Pin Bar has just formed, they become excited thinking about profits and are blinded to areas that may be hazardous to price (known as confirmation bias). Typically once the order has been placed, the beginner immediately sees the error of their ways, but its too late, the trade has most likely gone against them.

Sometimes you can get lucky and these trades work out for you, but why take the risk? If you are trading on daily (or higher) time frames, there should be no real need to place orders at market price and you should be trading according to a well thought out plan not by emotion.

Ok, now that we have all of the boring stuff out of the way, let's move on to how to trade Pin Bars.

Entries

Everybody always focuses on the Entry setup when presented with a new trading system. No doubt, you probably skimmed through this book when you first purchased it to look for this section. It has been proven time and time again that you can have the best entry point in the world but if you don't have a plan for where or when to exit then your entry is worthless.

That being said, a poor entry point will definitely not help you either, but it is important to realise that where you enter a trade is only a small portion of a trading system / plan and you should never enter a trade without knowing where or under what conditions you will exit. As Steve Nison says "there is always a price that says you are wrong" and this is known as your stop loss. Before entering any trade always make sure that you know your risk to reward ratio and your take profit and stop loss levels.

There are a few methods for trading Pin Bars and below is a summary of the three main methods traders use:

Method 1: High Risk - Enter at Market on next bar open

If you are an experienced trader and are supremely confident that the Pin bar setup that has formed is going to take off and result in quick profits then you can enter on the open of the next bar / candlestick. This trade will most likely be in the form of a Market Order and your stop should be place above the high / low of the pin bar (which depending on the size of the Pin Bar means you may have to risk a lot of capital).

Method 2: Medium / High Risk - Enter On Stop when Pin Bar High / Low is breached

It can be seen from many of the examples in this book that Pin Bars do not always form perfectly and can have wicks on both sides of the body, one small and one large. We can use the small wick to our advantage by allowing price to build some momentum in the direction of the small wick before the order is triggered. Unlike Method 1 this method confirms that price is moving in the desired direction before initiating the trade. If you place your On Stop order a small distance (2 - 3 pips) beyond the high or low of the Pin Bar then price has to move in the direction of profits before the trade is placed.

I would suggest that you should only take a trade using methods 1 or 2 if your calculated risk to reward ratio is 1:3 or greater. Simply stated, this means you should only trade if you stand to make $150 for every $50 risked.

Method 3: Low Risk - Enter on 50% Pin Bar retrace

History shows that price has a tendency to retrace a portion of the range of the Pin Bar in a lot of markets. The conservative trader can benefit from this phenomenon by entering a Limit order to buy or sell when price retraces roughly 50% of the Pin Bar range after the Pin Bar has been completed. I say roughly because this is not an exact science and you have to take into account market conditions and areas of interest to gauge what level you think price may retrace to.

One thing to be aware of with this method is that most of the time price does not retrace a percentage of the Pin Bar, more often than not price just takes off and keeps going. This can leave you high and dry and missing out on potential profits, but remember, there will always be another Pin Bar setup in the future that you can profit from, and price could have just as easily gone the other way and produced a losing trade.

Regardless of the method you use when you are looking to enter a trade on a Pin Bar setup you should be looking for reasons not to trade rather than day dreaming about all the cash you are going to make and not seeing the obvious levels of interest in price that may cause you to lose money.

In practical terms this means that you should only take the best Pin Bar setups (i.e: ones with lots of confluence), and in the real world this can mean that you only trade 3-5 times a month. For some people this does not provide enough trades and they need more action (read: drama) so they trade on lower time frames, but it can be argued that overtrading is a major factor in novice traders blowing up their accounts. In my opinion it is better to wait for the market to create one perfect 'A' grade setup than to trade twenty 'C' grade setups.

Stops:

Some traders find it hard to think about attaching a stop loss level to their trade. The simple fact is that no one likes to be wrong and if your stop loss gets hit it can be a massive blow to your confidence (not to mention your trading capital). Some people don't like stops because they feel that it creates doubt in your mind about whether or not you will win the trade.

Rest assured the market does not care about your doubts, fears, hopes or dreams and will do exactly what it wants whether you attach a stop to your order or not. Nobody can predict the future and every trade setup is a unique moment in the market, no other trade will be exactly the same, therefore you may as well place a stop and cover your bases in case your prediction about where price is going is wrong. (If you want some good reading on this subject try Mark Douglas' book Trading in the Zone).

Method 1: Very High Risk - Stop level at Pin Bar Open / Close

This is an extremely risky place to set your stop level and should not be attempted by the faint of heart. Sometimes the trade will just take off towards profits and you can get lucky, but more often than not you will be stopped out for a loss. The reason for this is if you place your stop near the Open / Close of the Pin Bar there is a chance you will get whipsawed by intraday market gyrations and your stop will be taken out.

Method 2: High Risk - Stop level at nearest point of interest inside the Pin Bar range.

Sometimes a Pin Bar may form right on or near a LRN (or other area of interest such as S/R or TLs) that has been significant in the past and you may wish to place your stop 2 - 3 pips beyond that level to limit the amount of capital you have to risk. This method can also be very hazardous to your trading account as the big players in the market sometimes gun for the interest levels to shake out the small time traders who place their stops near them (because they can't afford too risk much), so be vary wary of using this method.

Method 3: Medium Risk - Stop level at 50% of Pin Bar range.

Risk of being stopped out can be reduced by placing your stop somewhere around the 50% range of the Pin Bar, this allows price a little more room to move but still be prepared to be stopped out for a loss often when using this method.

Method 4: Low Risk - Stop level beyond Pin Bar high / low

The simplest and most likely method that you will profit from is to place your stop a certain distance (maybe 2-3 pips) beyond the high / low of the Pin Bar. Depending on the size of the Pin Bar this may mean you have to decrease your lot size in order to gain the desired amount of capital risked according to your trading plan, but it is worth it in the long run.

One last thing to note that can be the difference between success and failure as a trader is the ability to bring your stop to break even as soon as you can. The mechanics of doing this are at the discretion of the trader but I normally move my stop to break even (covering the spread) once the trade has moved 2 or more pips in my favour. This is born out of experience and getting comfortable as a trader and the level you choose may be completely different.

Note: a trade that stops out at breakeven is not a loser, it is a winner!

Taking Profits:

Taking profit is one of the most important things to do as a trader. How many times have you seen a profitable trade turn into a loser because you didn't take profit? It hurts doesn’t it? This is one of the worst habits a trader can develop but it is easy to remedy if you use the techniques outlined below.

Not every trade will be a winner, but you can increase your chances of success if you have a plan and stick to it. At times, the methods described below will cause you to miss out on some profits, but any profit in your account is better than a loss and there will always be another chance to make money.

As with entries and stop losses there are a few methods for taking profit when trading with Pin Bars.

Method 1 (TP1): Low Risk - TP at nearest SR level inside the previous bars range

If the bar that precedes the Pin Bar (also known as the left eye) is fairly large then the first profit target can be an area of interest level that is within the trading range of that candle.

Method 2: Medium Risk - TP at previous bars low or high

Your second profit target should be the low or high of the bar / candle that precedes the Pin Bar. This is pretty easy to judge and you should be shooting for a minimum risk to reward of 1: 1.5 with this method.

Method 3 (TP3): High Risk - at nearest interest level outside the previous bars range

The third way to take profit is to locate the nearest interest level beyond the previous candles range and set your stop at that level.

Partial Profit:

Advanced traders can manage their profits by taking partial profit at some of these levels. It is not uncommon for professional traders to take 50% profit when they reach TP1, then a further 25% - 50% at TP2 or TP3. Some traders like to let their profits run once they have reached TP1 and taken some profit, but only do this if you have moved your stop to break even or beyond. The amount of profit you take and at what level is completely up to you if you choose to utilise this method.

Trailing Stops:

You can use trailing stops to lock in profit if you need to leave a trade unattended (say overnight). Trailing stops are a good way to create piece of mind when you are fearful that the market could turn against you or if you can't watch over your trade for a prolonged period of time. It is a good idea to have an understanding of how volatile the market is when doing this as you do not want to get stopped out prematurely from ordinary market gyrations.

So, what's the Plan?

Now that you have been armed with all that information you need a plan of action to maintain consistency in your trading and sustain profits. Below is a table outlining an example checklist / plan to use when trading Pin Bars.

Details			Tick
	Date:		
	Time:		
	Currency Pair:		
Trend			
	Up		
	Down		
	Sideways	Ranging (trade carefully)	
		Choppy (don't trade)	
Pin Bar			
	Wick Length: (2 – 3 x body)		
	Significant: (2 – 3 x previous range)		
	Same direction as trend		
	Body Inside previous bars range		
Confluence			
	Moving Average		
	Support / Resistance		
	Trend Line		
	Fibonnacci Retracement		
	Pivot Point		
	Large Round Number		
Trade			
	Buy (long)	Price:	
	Sell (short)	Price:	
	Entry	Next Bar Open (market order)	
		High / Low of Pin Bar (on-stop)	
		50% retrace of Pin Bar (limit)	
	Stop Loss	Price:	
		Beyond Pin Bar High Low	
		50% of Pin Bar Range	
		Area of interest inside Pin Bar Range	
		Open of Pin Bar	
	Exit	TP1 (nearest area of interest inside previous bar range) Price:	
		TP2 (previous bar high / low) Price:	
		TP3 (nearest area of interest outside of previous bars range) Price:	
	TP1 Risk to Reward > 2.0		

Once you have been through the checklist and have decided that you want to trade the setup, re-read the checklist and give it a second thought. A wise person once said "you should be looking for reasons NOT to trade, instead of reasons you should trade", this is good advice to a point because you will never get the perfect setup and at some stage you have to get your toes into the water. My advice is if you follow the checklist and you are satisfied with the risk then test the market with a small trade, if it goes your way then you can put on additional positions as necessary.

One last thing to note is that traders should always consider keeping a trading journal.

Your journal can be used in addition to the checklist and should log all of the relevant details concerning each trade like ongoing win percentage, equity in your trading account and even your mental state when entering the trade. It can be useful to attach screen shots at the time of the trade entry and exit to the journal for graphically tracking the best types of setups. Journals like this are an excellent way to track your progress, analyse where you may be going wrong or find areas of improvement in your trading strategy.

Conclusion:

So there you have it folks, my attempt at trying to produce a practical e-book for trading Pin Bars with plenty of example charts to provide clarification of the important points. I hope you have found it beneficial and not a massive waste of time and money like so many other e-books out there. If you have any questions or feedback try visiting my blog at www.theloungetrader.com or send me an email at kct@theloungetrader.com.

Happy Trading!

K.C Thorpe