

Macro Patterns



Weight of Evidence

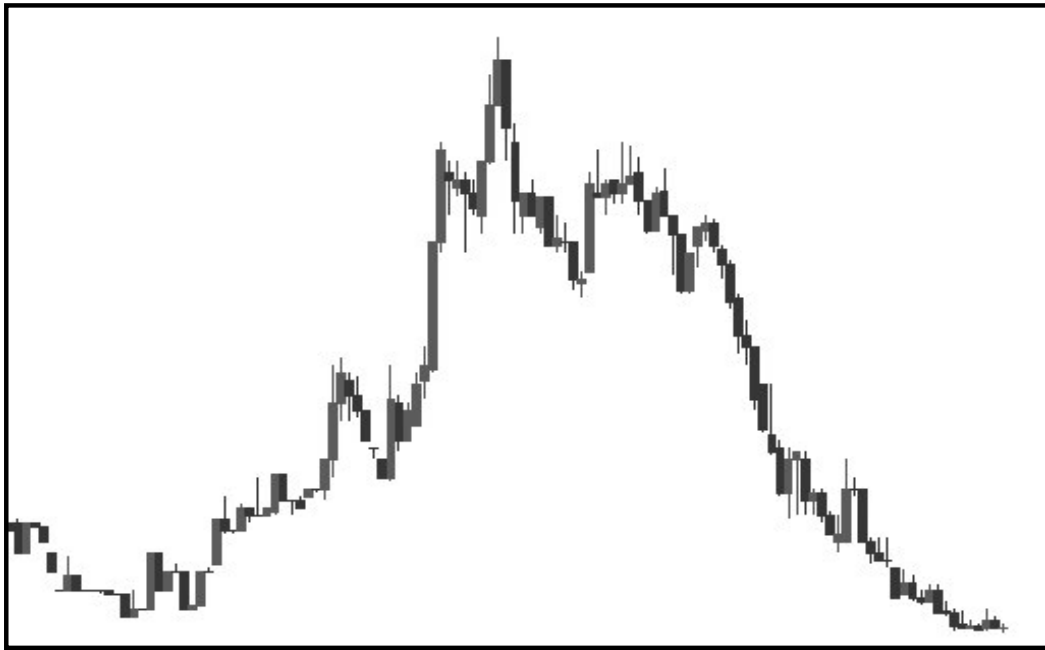
Weight of Evidence suggests that you should use at least one of the indicators from each 'family' in order to form an opinion about the share price's likely direction.

- The **Line** family
- The **Moving Average** family
- The **Momentum** family
- The **Volume** family
- The **Pattern** family

Develop a scientific process for analysing signals, and do not let your emotions dictate your trading habits. You need to define your signal in words so that another trader unfamiliar with your technique can duplicate your strategy. If it's not duplicatable, it's not a system. When several chart patterns and indicators point in the same direction, their signals are reinforced. If the weight of evidence of several indicators suggests that the share is uptrending, then the bulls have probably taken control of the market.

At the end of the notes in Appendix B, you will find a checklist that can help you understand the trend of the share, according to each of these 'families'. These help to form the 'set-up' conditions before entering a trade.

Share Stages



Stage 1: Base

This range trading activity occurs predominantly between horizontal support and resistance lines, located below the 30-week exponential moving average.

Stage 2: Uptrend

The share breaks above the resistance line established in Stage 1, and usually displays a decisive gap, or a dominant white candle on good relative volume levels.

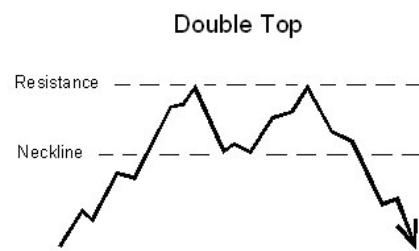
Stage 3: Top

The share forms a top, usually on heavy volume levels, and exceptionally positive media reports.

Stage 4: Downtrend

The share trades below the moving average and experiences a series of lower highs, and lower lows. Black candles out-number the white, and any level of support provided by a bottom reversal pattern is easily eradicated by bearish activity. The range of these black candles is often longer than the white candles. An uptick of the share price will often rise up to a previous level of support before continuing its downtrending activity.

Macro Patterns – Double Top/Bottom



- Top & Bottom Reversal
- Support or Resistance touched twice



- Confirmed when neckline broken

Description

Double top patterns form during an existing uptrend. They are characterised by a strong level of resistance that is touched on two separate occasions by subsequent price action. For each of the patterns discussed, the peaks or troughs may not necessarily be exactly symmetrical. Double Bottoms form during an existing downtrend, this pattern is characterised by a strong level of support that is touched on two separate occasions by the share price action.

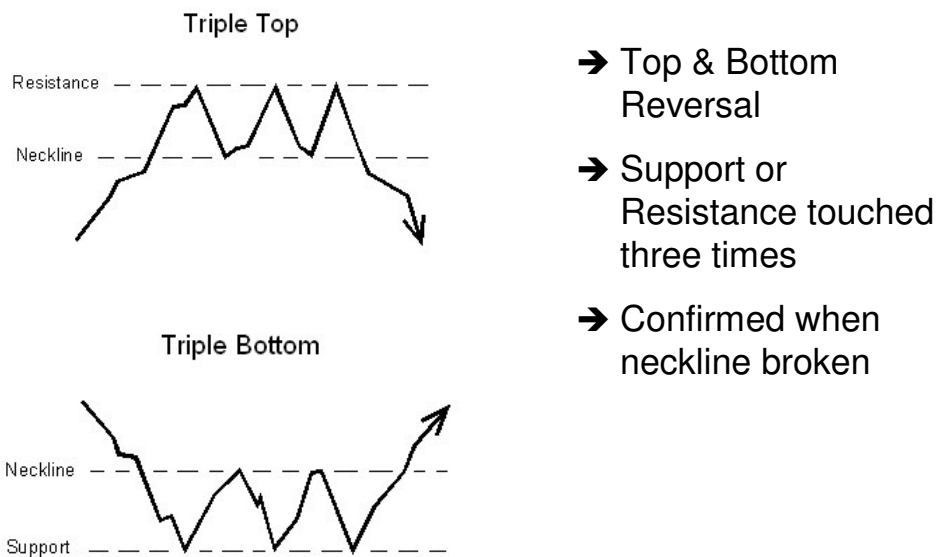
Location

Resistance or support is formed at the 'neckline'. When the share price closes above this level of resistance, particularly on heavy relative volume, for double bottoms or below the level of support for double tops, the pattern is confirmed. Trade in the direction of this break.

Psychology

The market has tried to continue the existing trend on two significant occasions. When the neckline fails, especially on heavy relative volume, the market sentiment reverses.

Triple Tops/Bottoms



Description

Triple top patterns form during an existing uptrend. They are characterised by a strong level of resistance that is touched on three separate occasions by subsequent price action. For each of the patterns discussed, the peaks or troughs may not necessarily be exactly symmetrical. Triple Bottoms form during an existing downtrend, this pattern is characterised by a strong level of support that is touched on three separate occasions by the share price action.

Location

Resistance or support is formed at the 'neckline'. When the share price closes above this level of resistance, particularly on heavy relative volume, for double bottoms or below the level of support for double tops, the pattern is confirmed. Trade in the direction of this break.

Psychology

See double top/bottom.

Example



Signal Failure

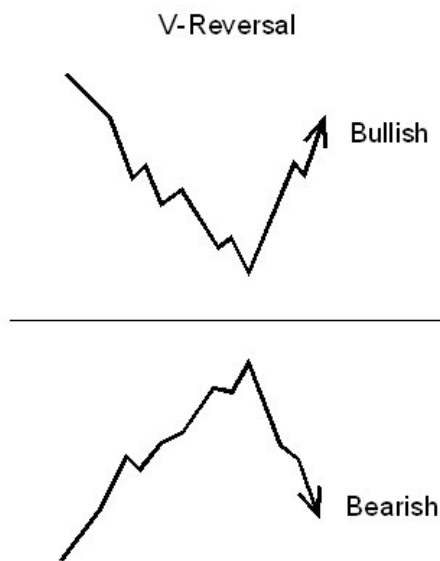
If a candlestick or macro pattern is not confirmed, this sends a powerful signal to the trader.



What happens when the signal we were expecting fails to materialise? In this situation most traders simply move on and look for another signal. This is a mistake, as the failure of a signal to eventuate is a powerful trigger. This reversal away from your expectation is known as a failed signal.

The failed signal is among the most powerful and reliable signals in technical analysis. By recognising these failed signals and acting appropriately, you can profit. This holds true whether you are using futures, shares, short selling, options or warrants as your instrument of choice.

Bullish & Bearish V-Reversals



- Top & Bottom Reversal
- Violent change of direction, typically on heavy relative volume
- A Bullish V-Reversal on low volume may be a dead cat bounce – so beware!

Description

The market violently and dramatically reverses its existing trend within a few periods. This is often accompanied by a significant increase in relative volume levels.

Location

This pattern is a top and a bottom reversal pattern. An increase in volume would assist in adding bullish confirmation. For a bearish V-Reversal, often there is no increase in volume required to provide a valid signal. The share can drop from a great height with just a few sellers initiating the downward slide.

Psychology

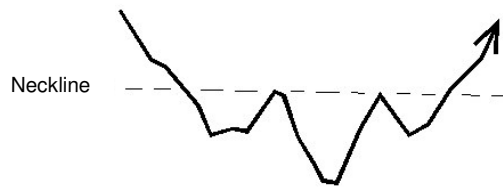
The market has violently altered its opinion of the value of the share, often initiated by a change in the fundamentals of the company. An immediate sell-off or rally is initiated usually on heavy volume.

Head & Shoulders

Head & Shoulders

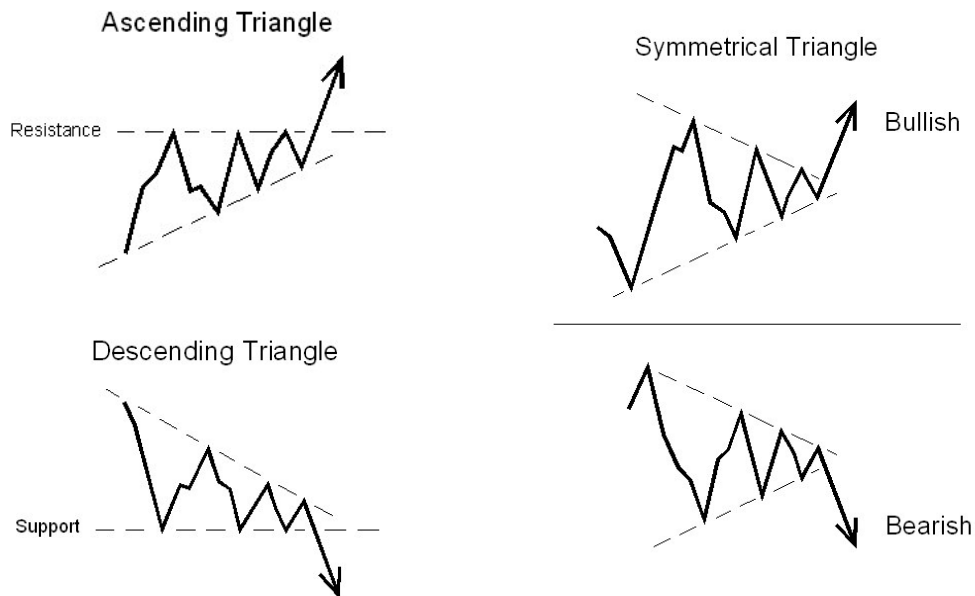


Inverse Head & Shoulders



The analysis of these patterns is the same as with triple top and bottom formations.

Triangles



Description

A **symmetrical triangle** is characterised by a convergence of an uptrend and downtrend line. An **ascending triangle** displays a series of higher lows, with a strong zone of resistance characterised by highs at the same price point. A **descending triangle** is the reverse formation to an ascending triangle. In this formation the bottom part of the triangle appears flat as bulls resist any attempt to push prices lower.

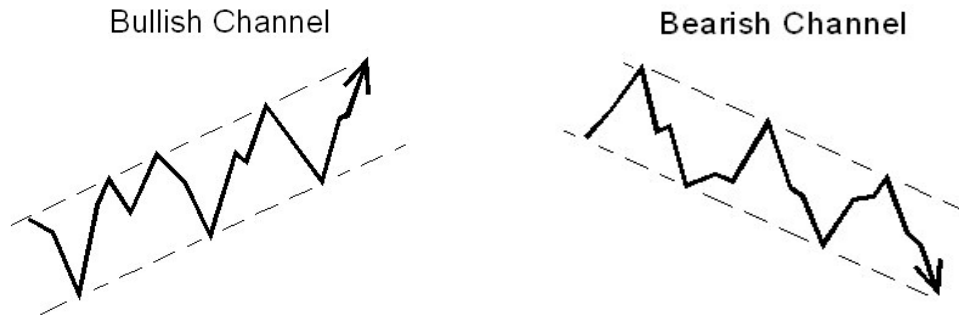
Location

Symmetrical triangles can form during up or downtrends. Ascending triangles usually form during a strong medium term uptrend with a breakout upward likely. Descending triangles usually form during a strong medium term downtrend with a breakout downward likely.

Psychology

Triangles suggest trader indecision. Traditionally price stalls and future direction is questioned. The triangle generally resolves itself in the direction of the primary trend. Trade in the direction of the breakout.

Channels



Description

Channels show share price action bouncing around between two support and resistance lines. A bullish channel is characterised by higher lows and higher highs. A bearish channel is characterised by lower highs and lower lows.

Location

Bullish channels help form an uptrend. Bearish channels help form a downtrend.

Psychology

During a trend, the market participants' perceptions about when a share is 'cheap' or 'expensive' come into play. When the share price is trading at an all-time high, the share is perceived to be expensive. This often inspires selling pressure.

When the share drops in price, it is then considered to be 'cheap', and new buyers enter the market. Existing buyers add to their current shareholding. This buying pressure drives the price upwards and an entry into a share at this time will allow you to harness the power of this bullish wave.

Appendix B – ‘Family’ Checklist

Line Family

Does the share display a series of progressively higher lows? If so, draw in a trend line below the share price action connecting two lows for a tentative uptrend line or three lows for a confirmed uptrend line. Start with a weekly chart and then examine the daily chart.

Is each level of resistance easily transcended, only to become a new level of support for future share price activity? (This is called change of polarity). Draw horizontal lines to depict areas of support and resistance.

Moving Average Family

On a weekly chart, are the share prices predominantly above the 30-week Exponential Moving Average (EMA)? This characteristic indicates an uptrend.

On a daily chart, are the share prices predominantly above the 30-day EMA? If they are, the share is trending up on a daily basis as well as on a weekly basis. If prices are above the 30-week EMA, yet below the 30-day EMA, the share is likely to be experiencing a counter trend reversal. Probability suggests that the share will ultimately continue it's uptrending behaviour in the near future.

Momentum Family

If the chart of the price action shows a series of higher highs and higher lows, there should be no sign of divergence with the momentum indicator, preferably on either the daily or the weekly chart, to confirm an uptrend. Are there any visible signs of divergence? If divergence is present, this suggests that the current prevailing trend is weakening and may be subject to a reversal.

Volume Family

Does volume expand on breakouts and contract on pullbacks? If so, this is a bullish sign. It means that traders are willing to pay higher and higher prices, yet when the share price decreases, they are reluctant to sell their shares.

Is the volume higher when white candles are present, in comparison to black candles?

Are volume spikes located predominantly above a short-term EMA applied to the volume chart in line with breakouts? (If you don't have the ability to run a moving average over the volume component of the chart, try drawing a horizontal line through roughly the middle of the volume. Then look to see where the spikes are located above and below the line. Spikes above the line indicate increased relative volume; spikes below the line indicate decreased relative volume levels.)

Do pullbacks in the share price action show the volume spikes drop below the short-term EMA (applied to the volume chart)?

Pattern Family

Is the share breaking upwards from a base formation pattern (Stage 1)?

Is the stock displaying continuously higher highs and higher lows, located above the 30-week EMA (Stage 2)?

Are there more white than black candles?

Are the white candles longer in length (ie. the range of the real-body) than the black candles?

Are there several candlestick tails pointing downward? This is a sign of buyer pressure. It indicates that the share price is likely to go upward in the following periods.

When there are candlestick tails pointing upward (indicating seller pressure), does the share price stall briefly, only to propel to prices above these tails on heavy volume?

On a weekly chart, when you stand back from the computer screen, (ignoring the name of the chart) and squint at it, is the predominant direction upwards?