Chart Pattern Secrets Newsletter

Issue 6

Welcome to the latest issue of the Chart Pattern Secrets Newsletter.

We hope that you find it useful and are able to implement some of the ideas into your own trading methodology. Chart patterns can provide an interesting insight into potential price action and form an integral part of successful trading strategies.

Contents:

This issue contains the following:

Next Issue:

Look out in your inbox for the next issue of the Chart Pattern Secrets Newsletter. In it, we will discover **pennants** and more **common trading mistakes** that so many traders make.

cpFinder - Chart Pattern Software

Introducing cpFinder (*chart pattern finder*) - an exciting new stock charting program that you can use on all of your favorite commodities, futures, forex, and stock market data (MetaStock data format) to scan for highly profitable trading opportunities. **cpFinder** is one of only a few software packages available on the market today, that allows you to scan for occurrences of these common patterns:

- ✓ Ascending Triangles
- ✓ Symmetrical Triangles
- ✓ Descending Triangles
- ✓ Head-and-shoulders Up
- ✓ Head-and-shoulders Down
- ✓ Double Top
- ✓ Triple Top
- ✓ Support
- ✓ Gaps

- ✓ Up Trends
- ✓ Down Trends
- ✓ Pennants
- ✓ Flags
- ✓ Wedges
- ✓ Double Bottom
- ✓ Triple Bottom
- ✓ Resistance

Free Trial Available: ***Try before you Buy !!*** For more information on the product or the free 14 day fully functional trial, please visit www.cpfinder.com and click on 'Free Trial'.

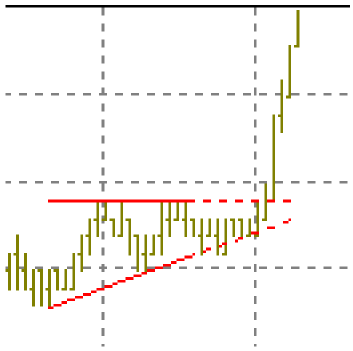
Triangles

A triangle in a chart is created when the distance between a security's highs and lows are decreasing. There are a number of different types of triangles including symmetrical, ascending and descending.

A symmetrical triangle occurs when both the highs and lows are moving towards each other, i.e. a security is achieving lower highs and higher lows. It can occur in either an up or down trend and is normally a continuation pattern. A continuation pattern occurs when the security continues to move in the same direction after the pattern as it was before the pattern formed. Having said that, occasionally, a symmetrical triangle can be a reversal pattern but in either case this will only be confirmed once the security breaks out from the triangle as shown in the chart.

Ascending triangles occur when a security is achieving higher lows, however the highs are remaining mainly at the same level due to resistance. Similarly, an ascending triangle can occur in both an up or down trend. The fact that the lows are increasing provides some indication that the demand for the security is increasing as the buyers are placing greater pressure on the sellers as the support rises.

Chances are that the security will break up from an ascending triangle as shown in the chart below.



Descending triangles occur when a security is achieving lower highs, however the lows are remaining mainly at the same level due to support. Similarly, a descending triangle can occur in both an up or down trend. The fact that the highs are decreasing provides some indication that the supply for the security is increasing as the sellers are placing greater pressure on the buyers as the resistance rises. Chances are that the security will break down from a descending triangle as shown in the chart below.

The point at which the two lines meet in the charts is often called the apex and if the break does not occur before meeting the apex, the pattern will most likely fail. If a trade is initiated on a break from a triangle, a suitable stop could be placed on the other side of the triangle.

Dow Theory

Dow Theory is the composite work of Charles Dow, William Hamilton, and Robert Rhea. Dow Theory was based on analysing the general swings in the market, with the aim of identifying the general trends. A lot of this work underpins modern technical analysis studies.

There are a number of basic principles of Dow Theory. These include 'the average discounts everything', 'the market has three movements', 'both averages must confirm for a trend to be valid' and 'volume provides additional evidence'.

The 'averages discount everything' is well explained by Rhea in his book 'The Dow Theory', reprinted by Fraser Publishing Company, Vermont in 1932, which states:

"The fluctuations of the daily closing prices of the Dow Jones rail and industrial averages afford a composite index of all the hopes, disappointments and knowledge of everyone who knows anything of financial matters and for that reason the effects of coming events (excluding acts of God) are always properly anticipated in their movement. The averages quickly appraise such calamities as fires and earthquakes."

The market has three movements, which are the primary trend, the secondary reaction, and the daily fluctuation. The primary trend is the overall movement of the market over an extended period of time from anywhere between less than a year to several years. The average of a primary movement is more than two years although there is no method of forecasting this.

The main factor in a primary bull trend is the demand created by investment and speculative buying caused by improving business conditions and increased speculative activity.

The primary bear trend is created by the supply caused by a variety of economic bad news and does not end until prices have discounted the worst of what could be expected to occur.

The second type of movement is the secondary reaction. This is a decline in a bull market and a rally in a bear market. On average, these movements will last from several weeks out to several months. It has been observed that in a bull market, prices can decline between 33% and 66% of the price change since the last secondary reaction. Similarly, prices can climb between 33% and 66% of the price change since the last secondary reaction in a bear market.

The third type of movement is the daily fluctuation which was considered unimportant by Dow, Hamilton and Rhea. Furthermore, Dow believed that the daily fluctuations had no influence in determining the overall trend and could almost be misleading. He was concerned mainly with identifying the primary and secondary movements only.

Interestingly, despite Dow's opinion of the unimportance of the daily fluctuation, many present day traders consider daily fluctuations in their analysis and trade short term. Notwithstanding that, many could probably benefit from considering trends of a greater time period even if only trading short term.

Comments / Feedback:

Any comments on the contents of this publication or suggestions for future publications will be warmly welcomed. Please email to cpfinder@tradingxl.com.au, fax to +61 3 9870 1738 or phone us on +61 3 8802 0593.

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