

FOREX INCOME BOSS

Presents



Chart Patterns

By Russ Horn

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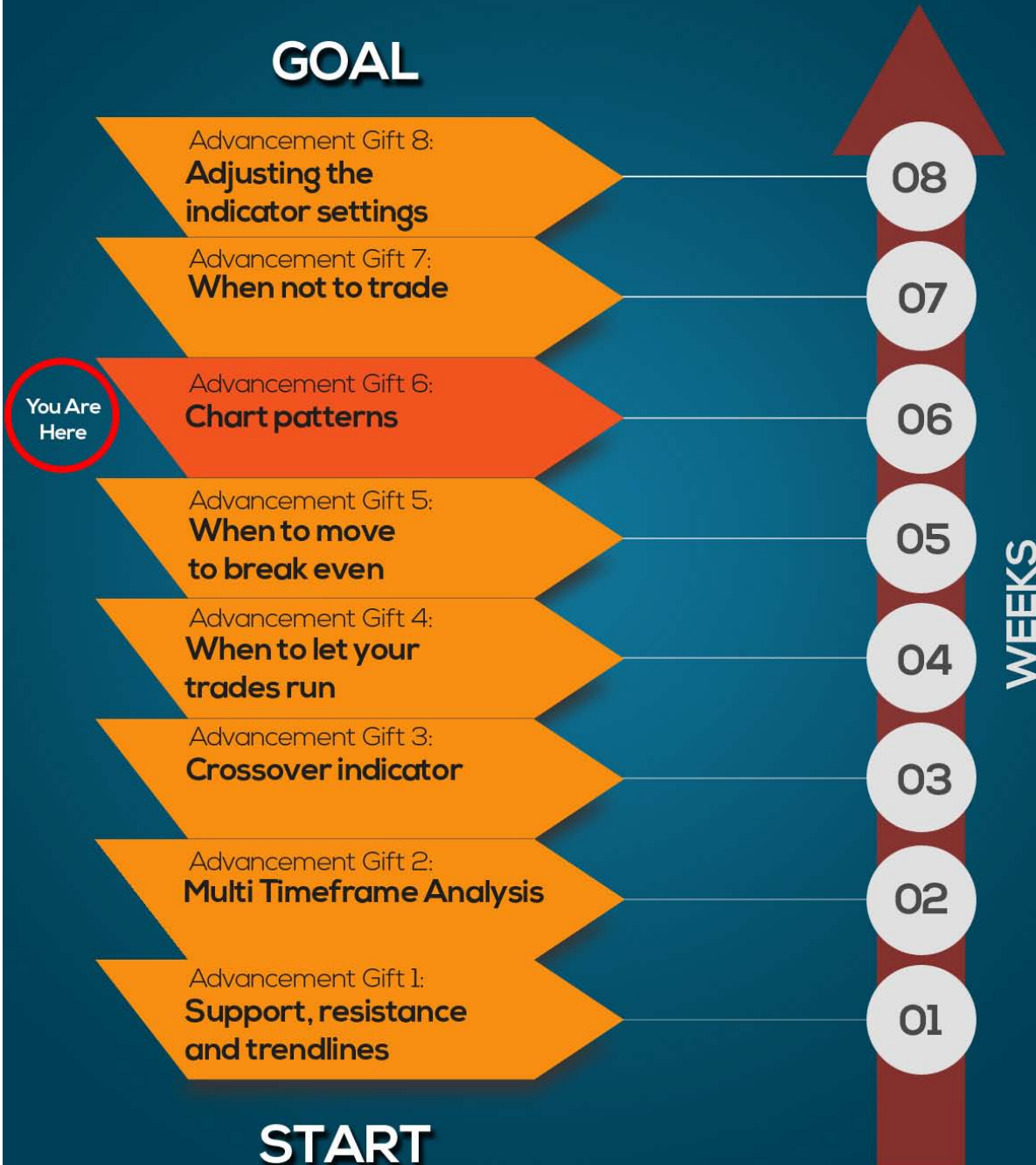
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FOREX INCOME BOSS

Advancement Gifts Roadmap

GOAL



1. Chart Patterns

What I will cover here are some of my favorite chart patterns that will deliver a higher-than-average probability of a successful trade. These patterns are reliable and many traders watch for these. Because of the number of traders waiting to trade these patterns, they have a kind of “self-fulfilling prophecy” thing going on. They are more likely to work out simply because the big money trades them too.

These patterns are important because when you see these patterns develop, you will have a better idea which way the market will breakout.

There are 4 trend following patterns, or “continuation” patterns, and there are 3 counter trend, or “reversal” patterns.

Trend following patterns:

1. Symmetrical Triangle / Pennant
2. Ascending/ Descending Triangle
3. Flag
4. Rectangle

Trend reversal patterns:

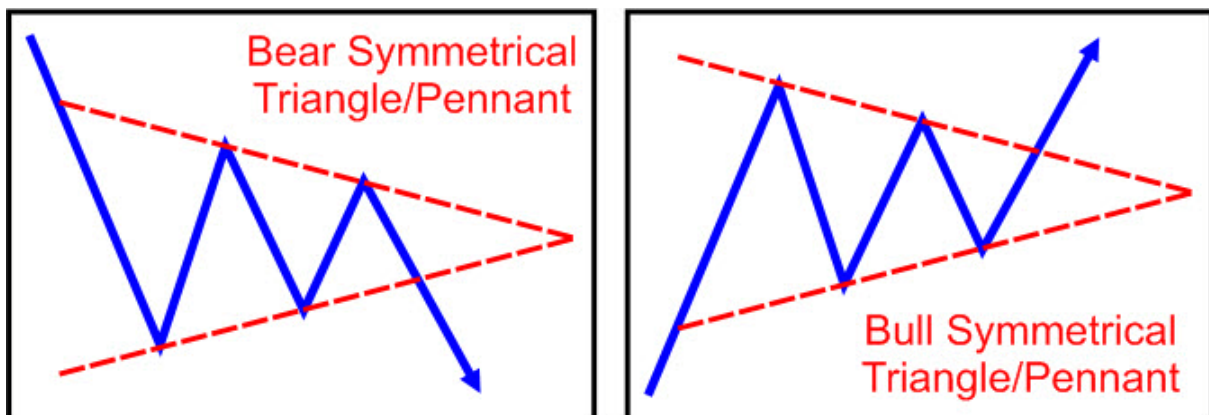
1. Wedge
2. Head and Shoulders
3. Double Top/Bottom

2. Continuation Patterns

The following chart patterns are patterns you will find in a trend. As the market takes a break from the big moves and rests a bit, you will find one of these patterns emerge. They are a good indication that the market hasn't finished its trend and the next trade you should be looking at will be with the recent trend direction.

Symmetrical Triangles and Pennants

These are essentially the same formation. As the market is pausing, you will find price retracting into a narrower and narrower configuration. The market squeezes itself from both the top and bottom. The Symmetrical Triangle and the Pennant show up just before the market takes off in its original direction.



You might be asking what then is the difference between a Symmetrical Triangle and a Pennant. The difference is slight and it's arguable at that.

With a Symmetrical Triangle, the market gently eases into the formation, while a Pennant comes after a very sharp and quick move by the market. This long, sharp, steep market move in front of the Pennant is called the "pole"

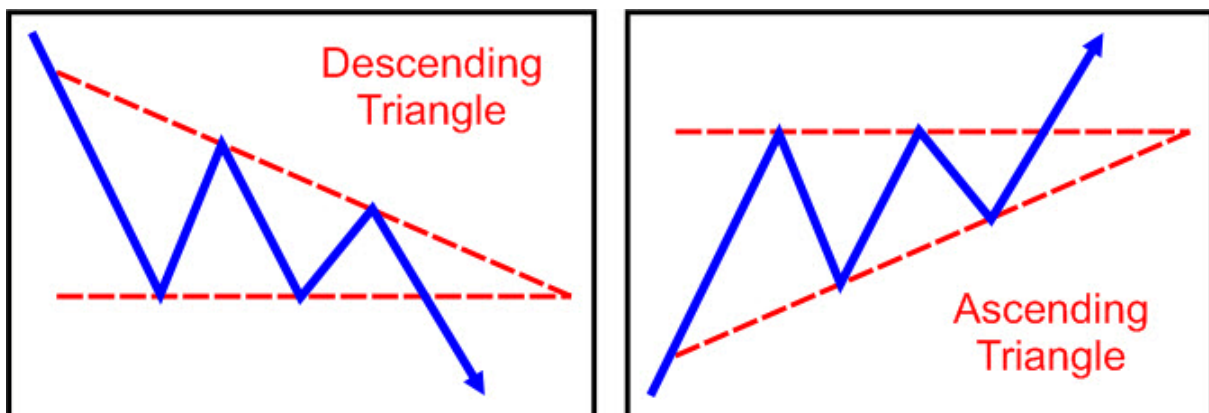


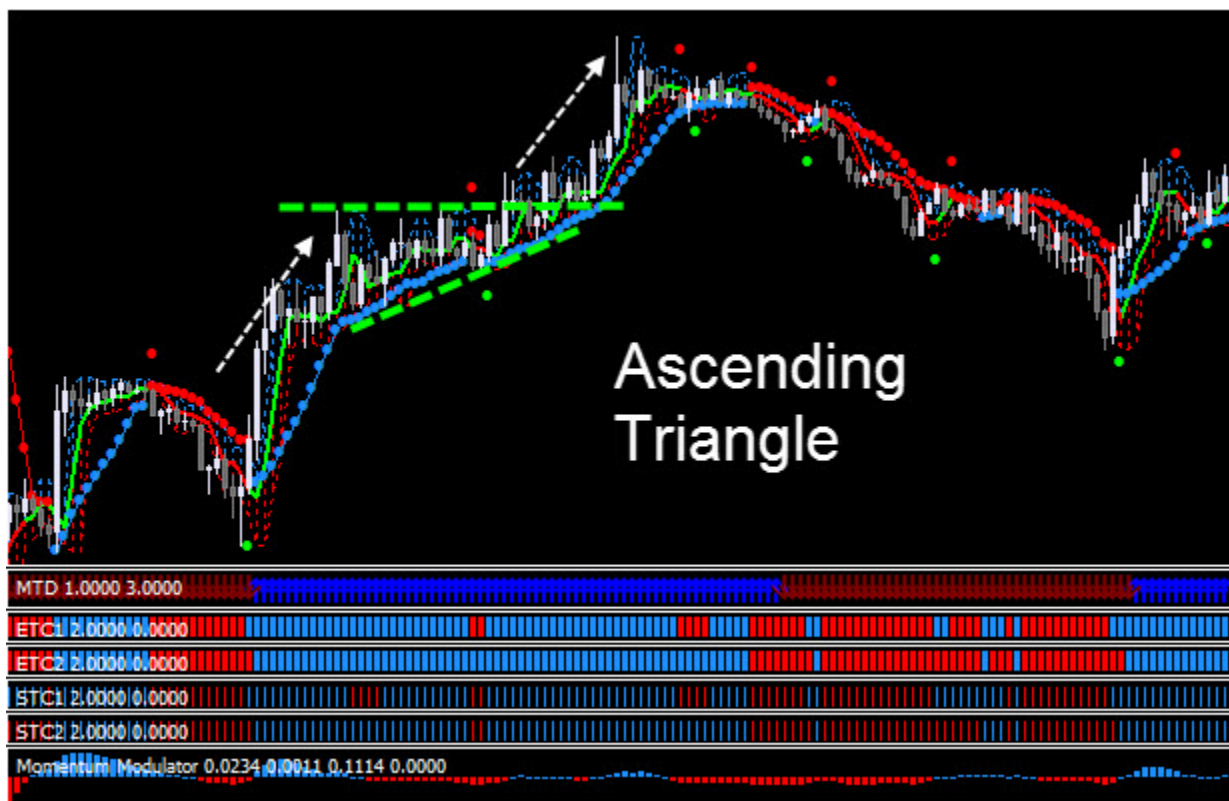
Ascending / Descending Triangles

This continuation pattern is similar to the Symmetrical Triangle, but in the case of the Ascending or Descending Triangle, the leading edge of the triangle is a flat line, a horizontal line of support or resistance.

In a Descending Triangle, price will drop in a bear trend and then take a breather. This resting phase will have price narrowing, but the lows it makes in the formation will be roughly the same while the highs will be getting progressively lower and lower. The psychology behind this formation is that the bears (sellers) are able to repeatedly push price to the same lows, but when the bulls (buyers) fight back, they can't make each push as high as the last. Eventually the bulls fail altogether and price is taken over by the bears.

The opposite is true for an Ascending Triangle. The formation comes off a rising market and then starts to form a series of equally high highs. The lows, however, are progressively higher and eventually the bulls take over completely.





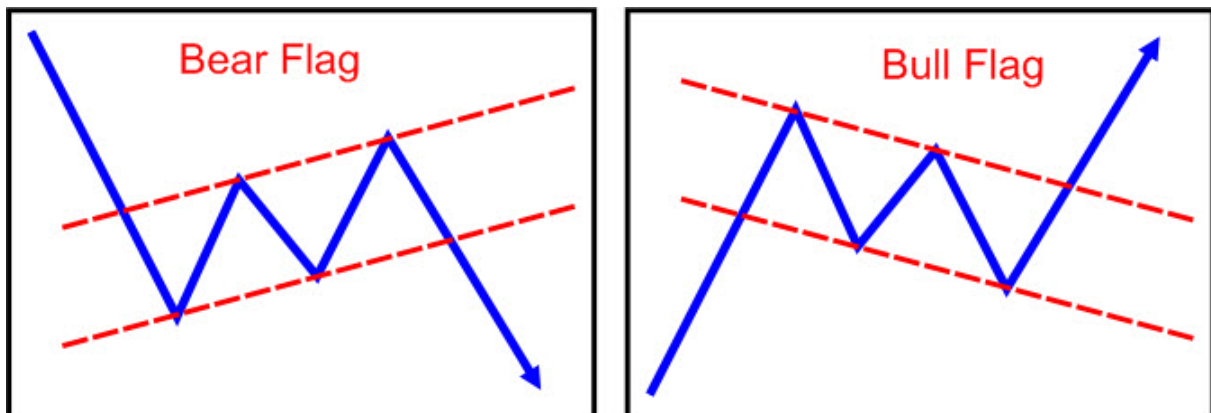
Flag

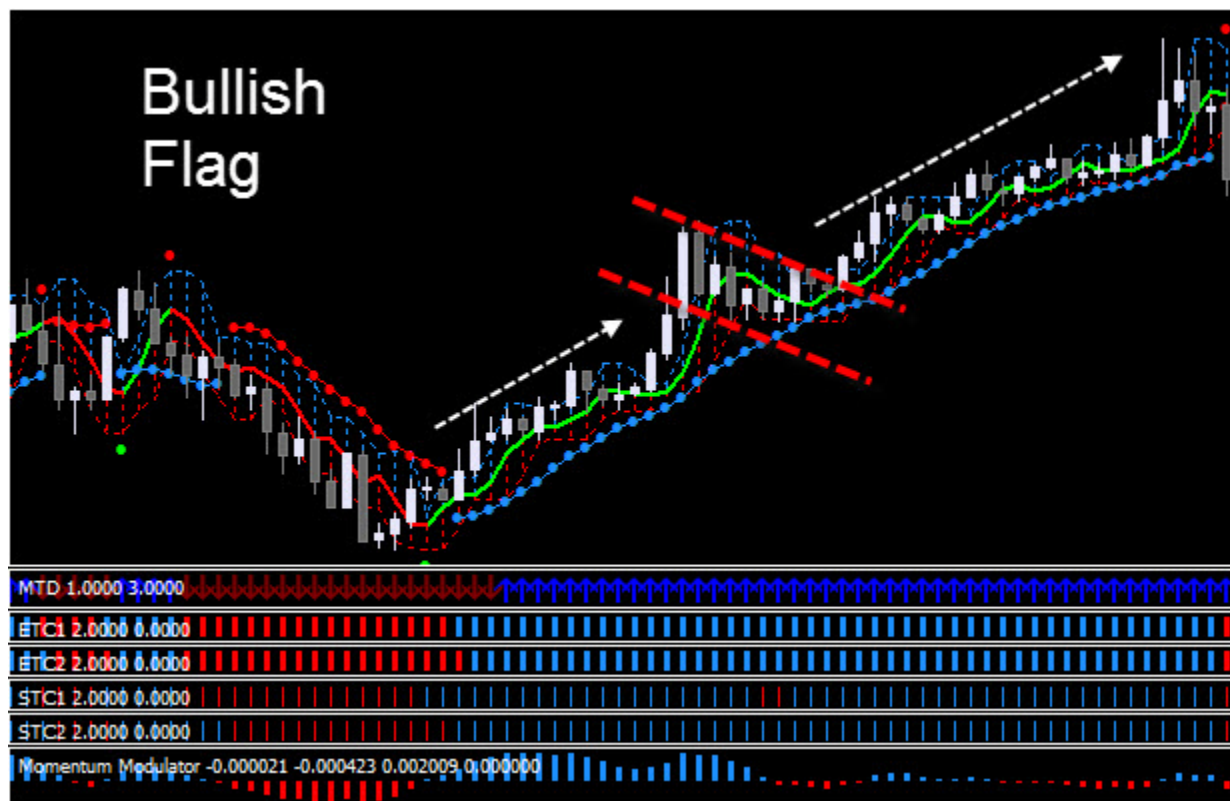
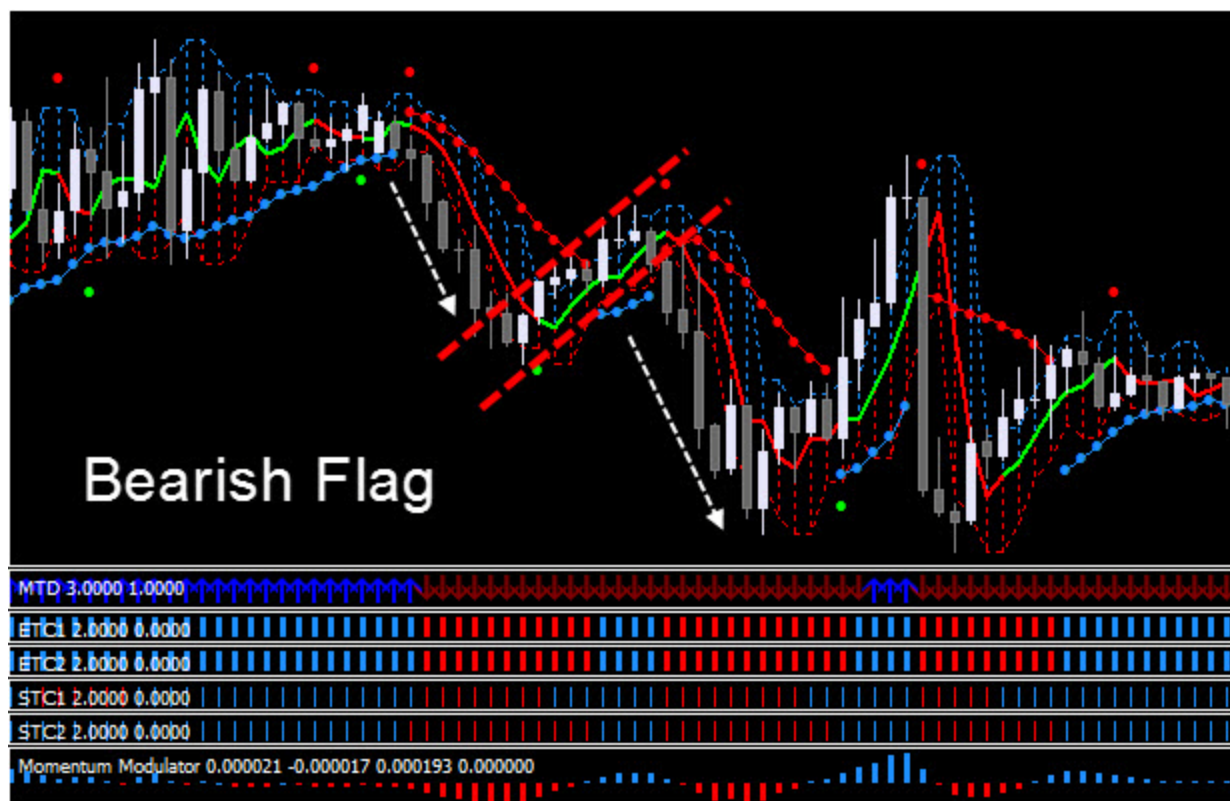
A Flag pattern is a take-a-break pattern as well. It starts off generally with a large quick move forming a fairly steep “pole”. Next comes the Flag formation as it gently moves up and down slightly against the initial move.

To be a true Flag, the formation takes place between two equally separated lines, a small support and resistance channel. The Bear Flag is formed as a slightly rising formation while a Bull Flag is a slightly falling formation.

After a large initial market move, there is a period of “covering”. That basically means traders who were in the initial large move are closing their positions. Some are closing their positions while others are opening new positions in the same direction as the initial move. This simultaneous buying and selling is like a tug-of-war between the bulls and the bears and the market doesn’t have the momentum to move in either way.

Once the open positions are covered, the remaining open positions and with the addition of the new positions will usually force price to take off in its initial direction.





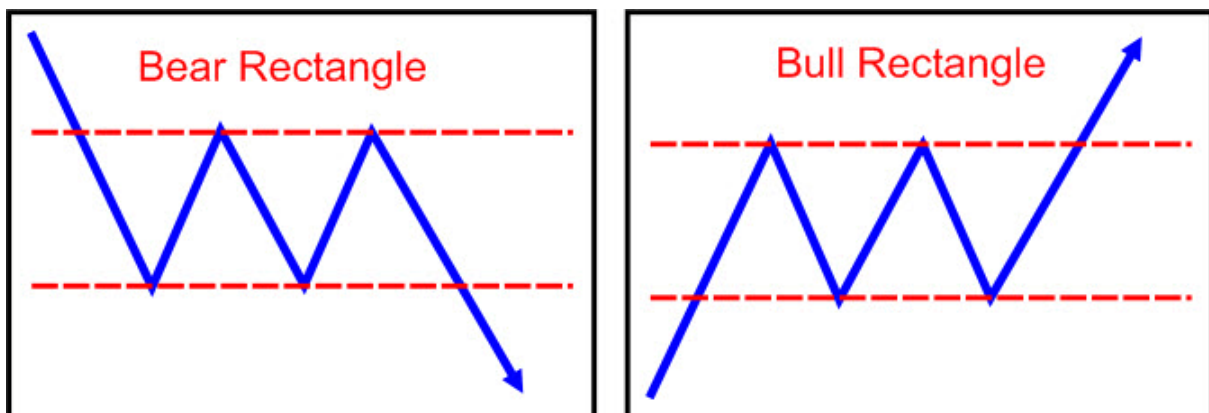
Rectangle

A rectangle is a fancy term for a range.

As price slows down after a bigger move, it will want to drift sideways for a bit. This drifting will have price floating up and down as regular business in the world influences price, but it's pretty stable.

A rectangle is price action that you can sandwich between two horizontal lines, support and resistance levels. You will find this after a big move, but also after the major market participants go to sleep on a smaller timeframe. Rectangles are periods of equilibrium, and others say it's a period of indecision. Either way it's a pause in the market that has a clearly defined high and low.

A Rectangle can be very narrow as in a consolidated market, or a little wider where there is actual price movement inside of it. This is the classic formation for a "breakout" type of trade.





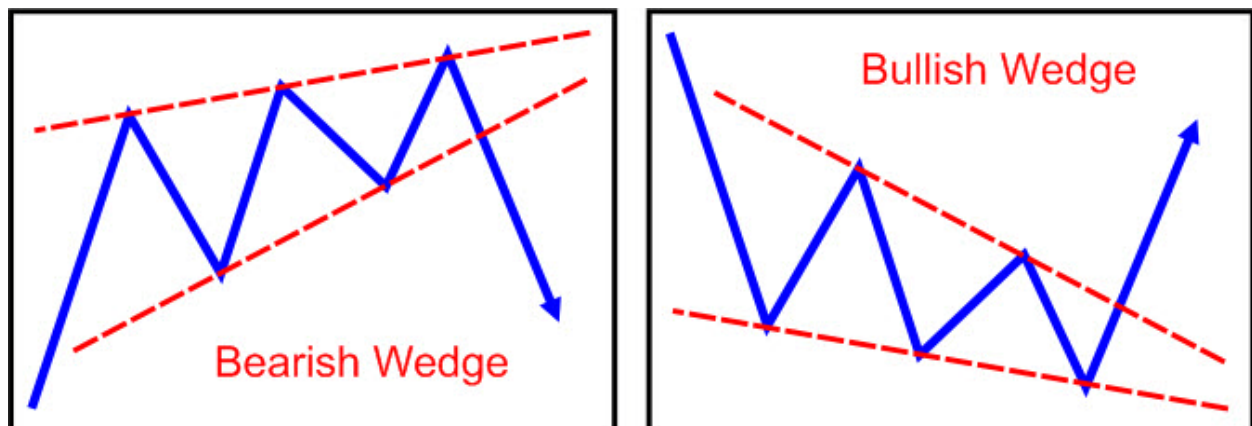
3. Reversal Patterns

Of course the market can't move in one direction all the time. It must change direction from time to time. Many small changes in direction are simply pullbacks, but there are also complete reversals. The trick is knowing the difference between the two. A pullback is difficult and usually unprofitable to trade, but there is good money in trading reversals. Knowing a couple of high probability chart patterns will help you decide when you would trade a reversal instead of leaving it alone as a minor correction.

Wedge

This is my favorite reversal pattern. It happens almost every time a decent reversal is about to happen, I watch for it with eagle eyes!

In a bullish reversal Wedge, price must be trending lower. At the bottom of the trend, the last couple of lows are very shallow, almost a kind of bottoming out. The first low is followed by a slightly lower low. The highs however are not as shallow, they keep falling more dramatically than the lows. The opposite is true of the bearish wedge. A topping out of price as price narrows, then the reversal happens.

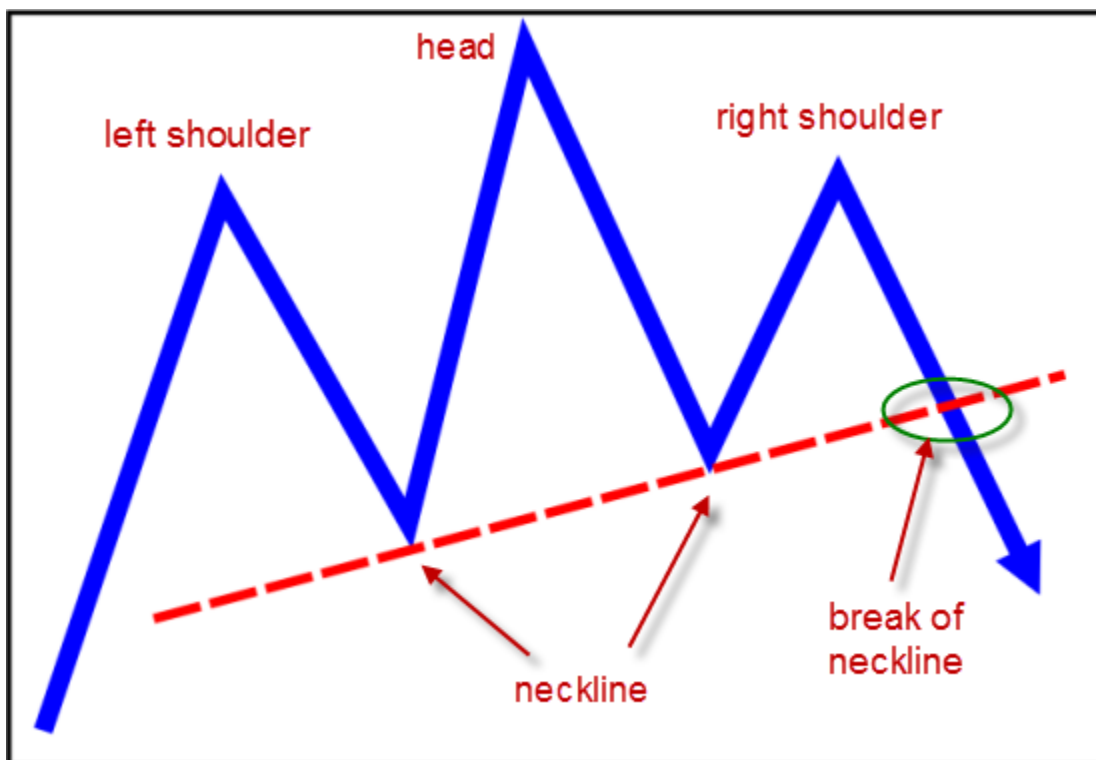




Head and Shoulders

The Head and Shoulders formation might be the single most popular chart pattern out there. It's fun to say and fun to trade. There are traders that look for this formation almost exclusively, and they do very well trading it.

The Head and Shoulders is what it sounds like. A bullish Head and Shoulders consists of a high being the left shoulder, followed by a higher high making the head. Finally there is another high that is lower than the head. This is the head and shoulders. The two lows formed by price on either side of the head is called the neckline. A trendline is drawn connecting them and when price breaks below, you have a short trade.

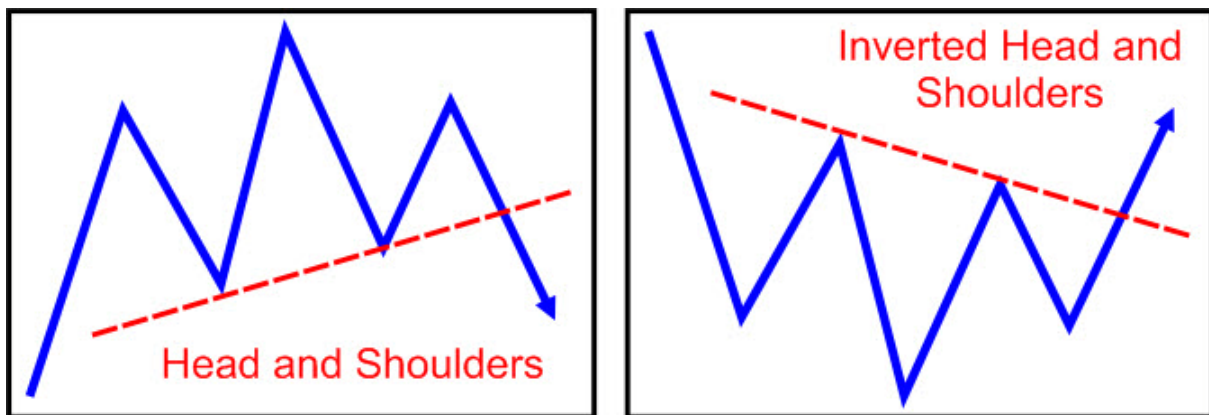


The theory behind the Head and Shoulders pattern follows the rule of a trend.

In an up-trend, you will find the market makes a series of higher highs and higher lows. In a down-trend, the market makes lower highs and lower lows, a kind of staircase looking pattern.

Head and Shoulders is a bearish pattern and it starts out with a higher high and a higher low. What follows is a lower high, this interrupts the pattern of an uptrend and is the beginning of a downtrend. The Head and Shoulders pattern assumes that the beginning of a new trend direction will have some follow-through.

The bullish version of the pattern is called the Inverted Head and Shoulders.



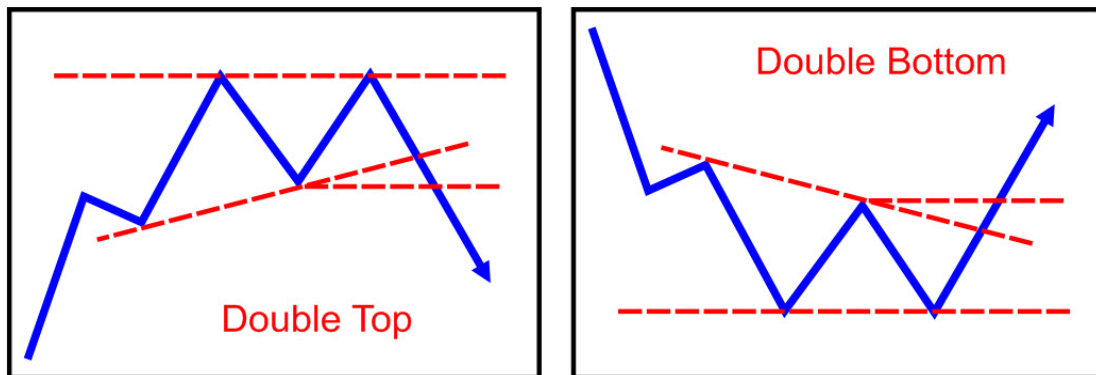


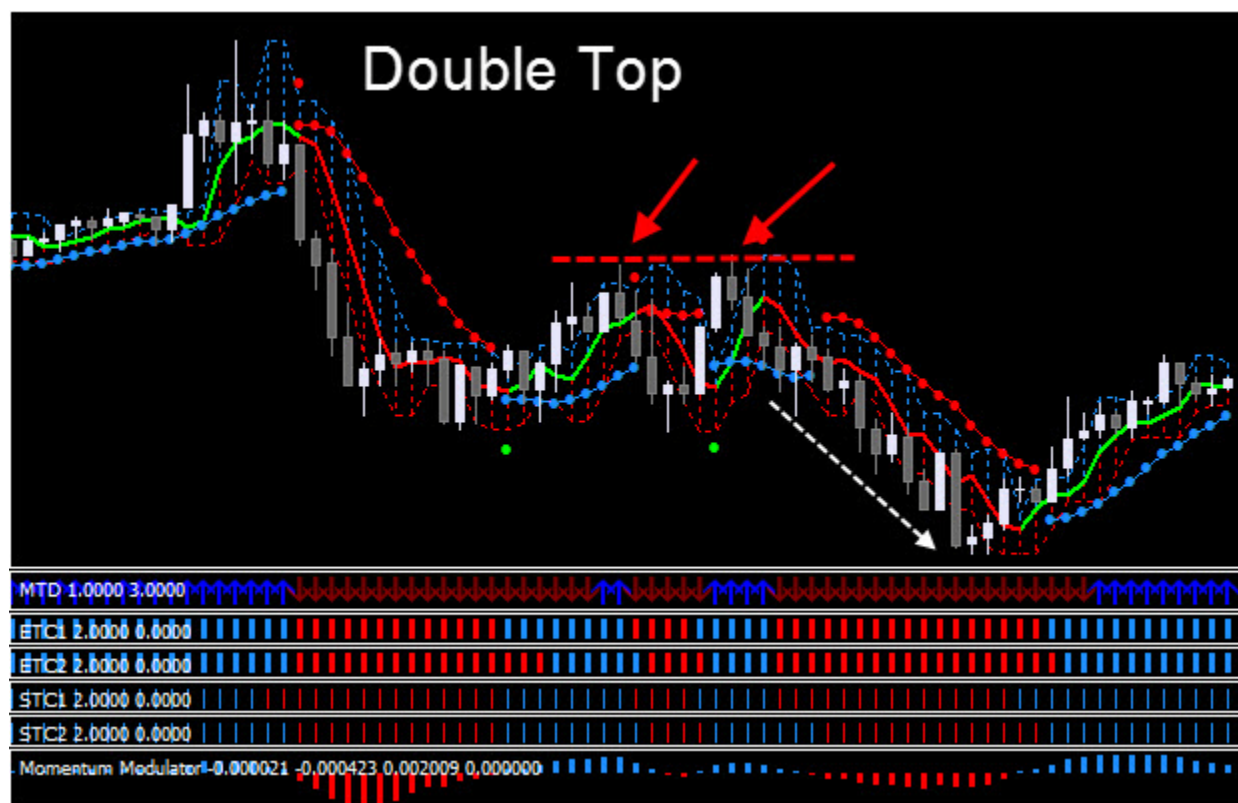
Double Top/Bottom

A double top or a double bottom is an attempt from the market to get past a certain price and be rejected from that price 2 times. This will generally lead to a movement in the opposite direction. Trades look for this formation and will act on its failure with a trade in the direction of the bounce.

The market makes a clear level of support or resistance, the price will be affected by this level but returns to it. A second rejection from this level of now established support or resistance provides a stronger bouncing opportunity.

There are several ways to trade a double bounce. A candle formation is one way to do it, getting a confirmation of the second rejection will have trades getting into a trade. A safer way to trade a double top/bottom is to draw levels of support and resistance, often being a level that the center between the bounces make. A quicker entry will occur when you can draw a trendline. An upward trendline on a double top and a downward trendline on a double bottom.

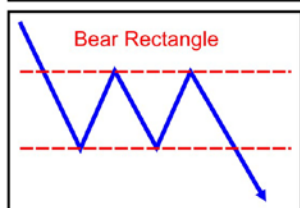
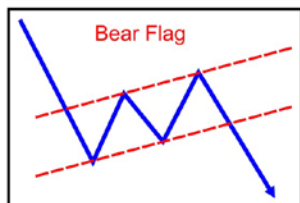
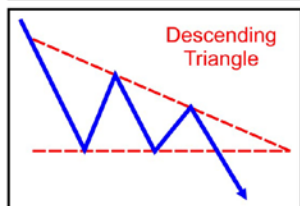
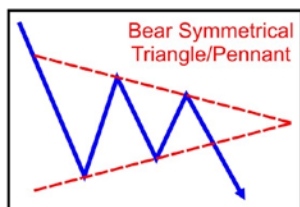




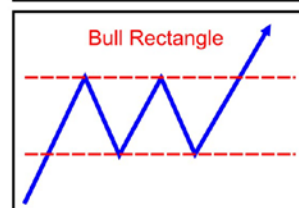
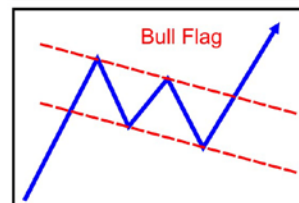
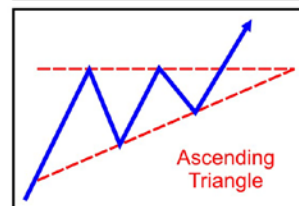
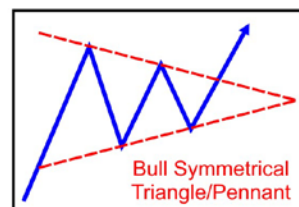
On the next page you will find the Quick Reference Guide to Chart Patterns that we discussed. You can print these out and keep them handy.

Quick Reference Guide to Chart Patterns

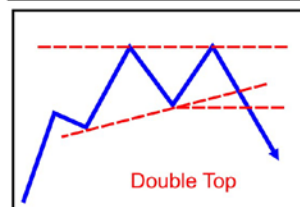
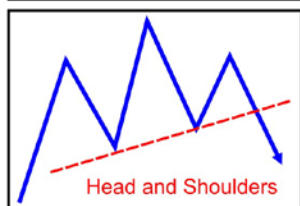
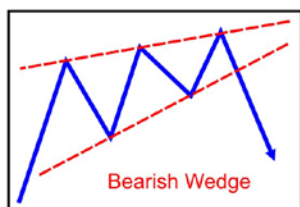
Bearish Continuation Patterns



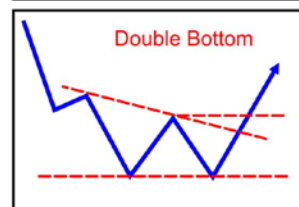
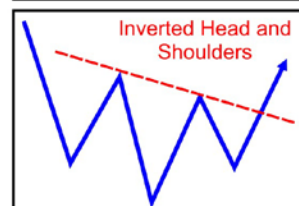
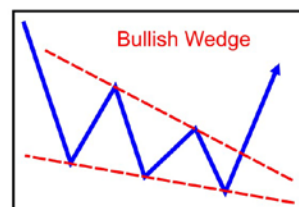
Bullish Continuation Patterns



Bearish Reversal Patterns



Bullish Reversal Patterns



4. Conclusion

Chart patterns are a great tool for further confirmation of a trade setup. You can trade them on their own, but if they line up with an FIB setup, you have a higher probability of a successful trade.

I am not in any way intending for these patterns to complicate the system. In fact, the opposite is the case. They will help you identify a possible continuation in the market or even a reversal.

Although chart patterns are not an integral part of the FIB system, it doesn't hurt to be better educated when it comes to your trading.

May all your dreams come true!

Russ Horn