Bulkowski’s Trading Quiz

What chart patterns can you find? A hint appears below and answers on the next page.

Hint. Look for the following chart patterns (If you find others, great!): Big M, 2 double tops, broadening pattern, wedge, triple bottom, pennant.
The earnings flag isn’t a flag at all but a pennant. Nevertheless, that’s what it’s called. Price has broken out upward from the pennant.

**Question 1:** Do you buy, short, or avoid trading this stock?

**Question 2:** If trading this one, what is the target price?

**Question 3:** If trading this one, what is the stop price?

The answers appear below and a chart on the next page.

**Answer 1:** Earnings flags are the best performing event pattern. Buy. Price must make a large intraday price swing or gap higher as shown here.

**Answer 2:** See my notebook

**Answer 3:** See my notebook on the next page.
Here's my notebook entry for the buy.

“Date: 5/19/04
Filled at: 43.989
Stop: 40.03, a loss of 9%. Placed 5/19/04
Upside target: 46 as per MMU from 36 to 42, then 40 projected upward
Mood (will trade work? Bought too soon?): pissed that GI trade was stopped out but confident of this one.
S&P direction over pattern lifetime: Downward for last 1.5 months
Future market direction (guess): Up. It's finding support at the last recent minor low. Market is nervous over oil price and inflation, rising interest rates looming.
Buy reason: Earnings flag and stock is moving higher as market is going down. Nice flat base at 38 and 41.”

I show the measured move up (MMU) pattern in red on the above chart. In theory, the second leg is supposed to copy the move of the first leg. The S&P chart appears on the next page.
The red line shows the downward price trend I spoke of. The green lines show underlying support. The top green line is just below the 38% Fibonacci retrace of the move from A to B, suggesting price might reverse and move up, as I wrote in my notebook.

More on the next page.
Here’s the price of oil. At the time I bought, you can see that it was on a steady climb since the September low.

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This is the flat base at 38 and 41 my notebook refers to.
This is what happened to the stock over the coming days. The red circles show the stop locations that my notebook entry details.

“5/26/04 Stop raised to 42.37
6/2/04 Stop raised to 43.73
6/16/04 Stop raised to 45.87
6/28/04 Stop raised to 46.73
7/1/04 Stop raised to 47.33
7/16/04 Stop raised to 48.43”

Most of the circles correspond to new highs in the stock. As price climbed, you can see that the circles became bunched. I grew more concerned the higher price climbed.

**Question:** Is it time to sell or hold on for additional gains? I show one answer on the next page.
Here’s my notebook entry for the exit.

“Date: 7/21/04
Filled at: 49.022
Mood (sell too soon?): Yes, at least intraday as price rebounded after I sold. In the short term, I see market weakness and weakness in this stock. It is struggling to get above 50 and stay there. I expect another decline then a retry at the top. 
Sell reason: The market is up 88 points and this is down 82 cents. All the other stocks in my portfolio are up today. That signals a trend change. The rate of change (ROC) oscillator has been trending down for months now (since April), diverging from price and I see momentum lessening. It may be that I want to protect my profits after two recent losses. Earnings are due in August 6. Yeah! I just logged in and the stock closed 2.64 lower! I got out just in time and the DJIA was down over 100.”

The next page shows the rate of change oscillator.
I made over 11% on the trade. Notice that even though the indicator signaled divergence (lower highs on the indicator but higher highs on the stock), I bought and made money.

The end.