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!): 2 head-and-shoulders, wedge, three rising valleys, and a dead-cat bounce.
The rising wedge has an upward breakout, confirmed when price closes above the top trendline.

**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:** I don’t like wedges and the upward breakout is unusual. It’s a buy signal though.

**Answer 2:** Take the height of the wedge, multiply it by 58% (because that’s how often this measure rule works) and add it to the breakout price. The top of the wedge is at 10.43, low at 9.62 for a height of 81 cents. Multiply by 58% to get 47 cents and add it to the breakout price of 10.43 to get 10.90.

**Answer 3:** With low priced issues, they are more volatile and it’s more difficult to place a stop. I would probably use a volatility stop on this one. That places it at 9.75 or 6.8% below the current close. A vol stop is computed by finding the daily high-low range over the last month and averaging the values, multiplying by 2 and subtracting the result from the current low. It’s a way to prevent from being stopped out my normal price action.
The stock plummeted in a dead-cat bounce on a lower sales outlook. If you trade stocks long enough, you will probably run across a dead cat bounce. Even if you placed a stop below the bottom of the chart pattern, you would have lost more than that as price opened lower. On 7/28, the stock closed at 11.10 and it opened the following day at 9.25 before closing at 7.95, a close-to-close decline of 28%.

The end.