

# Quick Overview

MY METHODOLOGY CAN BE BROKEN UP INTO  
A NUMBER OF STEPS AND ARE GOVERNED BY RULES.

**Rule 1:** Use the daily, weekly, and monthly timeframes

**Rule 2:** Hold on to trades for 1-100+ days.

**Rule 3:** Only use price to determine decisions. Ignore the news.

**Step 1:** Assess the phase or trend of the market  
within the scientific timeframes.

**Step 2:** Assess the patterns within the phase, or  
within the governing pattern.

**Step 3:** Assess the potential for momentum with  
an insurance bar (daily or weekly).

**Step 4:** Let the market confirm that momentum  
with a resting order.



## Rule 1

# Use the daily, weekly, and monthly time frames

Studies show that once a reversal happens, price tends to keep moving for up to a year.



Gutierrez and Kelley (2008) discovered that price tends to keep moving, for up to one year, after even a small reversal.



First, return autocorrelations are negative over very short horizons, positive over intermediate horizons, and become negative again over long horizons.



In a study by Friesen et al. (2009)



Therefore, using daily, weekly, and monthly timeframes gives you a much better chance.

## Rule 2

# Hold on to trades for 1-100+ days

Day trading doesn't work. Anyone who argues otherwise needs to show you some scientific proof.



I have never been a fan of shorter time frames. They simply don't work. Getting in and out of trades with a small stop loss is a recipe for disaster.

Chague et al. (2019) proved this. They found that it is "virtually impossible" for day traders to make money in the long run.

Basically, they came to the same conclusions as studies published decades before. Like Barber et al. (2009).

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Barber, B. M., Lee, Y., Liu, Y., & Odean, T. (2009). Just how much do individual investors lose by trading?

Chague, Fernando and De-Losso, Rodrigo and Giovannetti, Bruno, Day Trading for a Living? (November 21, 2019). Available at SSRN: <https://ssrn.com/abstract=3423101>

## Rule 3

# Only use price to determine decisions. Ignore the news.

Although there is some evidence that news trading works. You need to have a team of analysts to interpret every article, report, and speech that comes out.

Gutierrez and Kelley (2008) also discovered the following phenomenon.

“ Our findings extend to weekly price movements with and without public news. In addition, there is no relation between news uncertainty and the momentum in 1-week returns. ”

In other words... when it comes to momentum (how much price moves) the uncertainty that news brings about doesn't effect the price direction longer timeframes.

Therefore, there is no need to factor in the news. It is distracting and will stress you out, which is the downfall of most news traders. Again, studies dating back decades agree with this statement (Oberlechner et al, 2005).

# The three rules: my conclusion



These 3 rules will add an additional edge to your trading. All three have scientific backing. I only cited a VERY small sample of research. Each of those papers show at between 10-50 other studies backing up their claims. That's over 150 scientific studies.

These 3 rules will also reduce the stress of sitting in front of your screen all day and spending hours looking out for news reports. That alone makes them worth adopting.

# **My Trading Methodology & The Science Behind It**



# Step

## Assess the phase or trend of the market within the scientific timeframes.



This step feeds into rule #1.

There are 5 possible phases in the market:  
Up, Down, Sideways, Reversing-up, and  
Reversing-down.

In order to assess the phase or the  
condition of the market, we need to  
establish which direction the market is  
going now.

Gutierrez and Kelley, 2008 demonstrated  
that the market can continue is an  
uptrend for up to 1 year after a reversal.

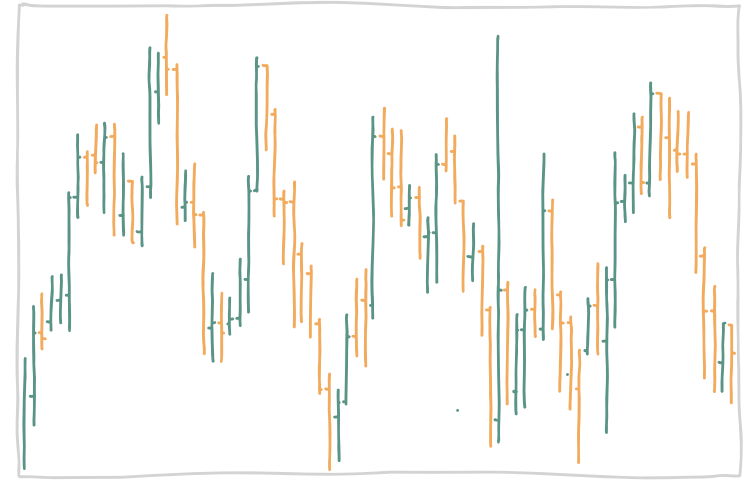
1. Up



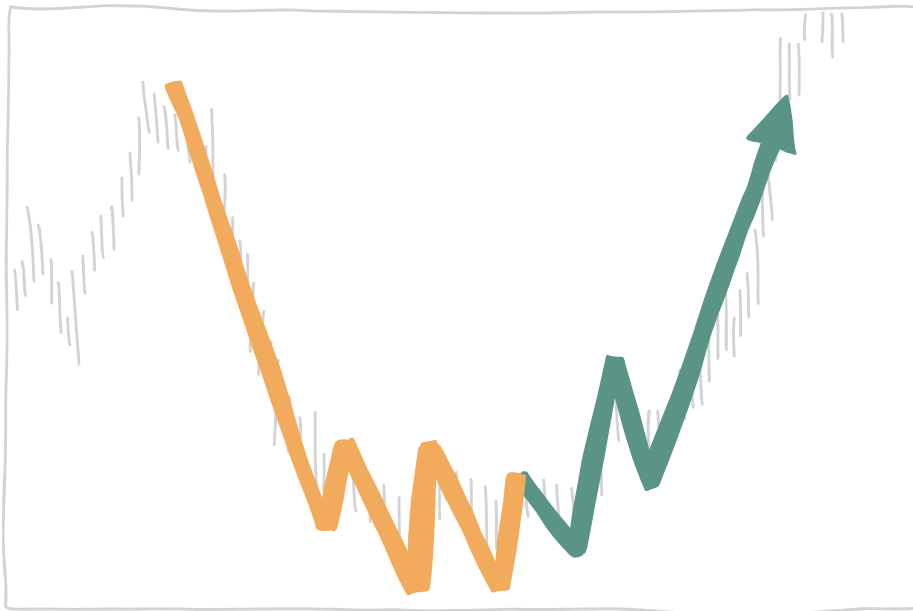
2. Down



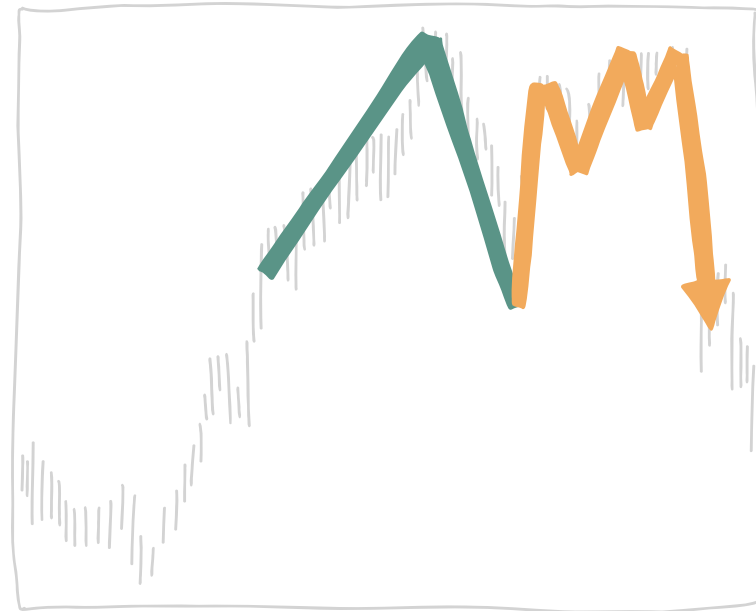
3. Sideways



4. Turning from **down** to up



5. Turning from up to **down**





## Step 2

# Assess the patterns within the phase, or within the governing pattern.

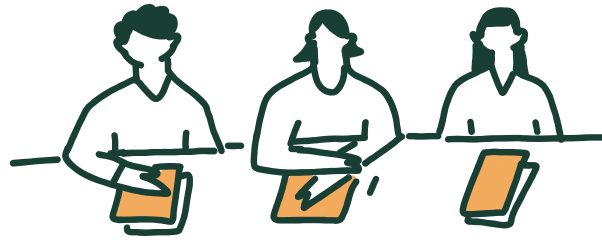
If a market is in phase 4 or phase 5, then a reversal must have happened. This reversal becomes the governing pattern. If the reversal is heading up, then you are more likely to make a profitable trade if you take it in the direction of the phase (Friesen et al. 2009).

The patterns that happen within that phase will confirm the direction of the market, and when price is ready to break out, you'll have momentum on your side. Foltice & Langer (2015) studied how momentum effected returns. According to them:

“ We find that the strategy can indeed work for individual investors with initial investment amounts of \$5,000.” ”



When it comes to the patterns themselves, there are lots of studies that show proof they work. A small list of scientific studies has been provided on the next page.



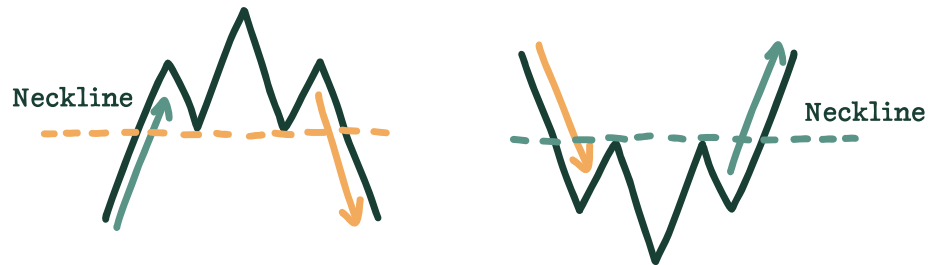
- Folnce, B. & Langer, T. (2015) Profitable momentum trading strategies for individual investors. *Financial Markets and Portfolio Management*, 29(2), 85-113.
- Friesen, Geoffrey C.; Weller, Paul; and Dunham, Lee, "Price Trends and Patterns in Technical Analysis: A Theoretical and Empirical Examination" (2009). Finance Department Faculty Publications. 11
- Gunierrez and Kelley, 2008 — R. Gunierrez Jr. and E. Kelley, The long-lasting momentum in weekly returns, *Journal of Finance* 63 (2008)
- Leuthold, R.M. (1972) Random walk and price trends: the live cattle futures market. *Journal of Finance* 27: 879-889.
- Smidt, S. (1965a) A test of serial independence of price changes in soybean futures. *Food Research Institute Studies* 5: 117-136. Smidt, S. (1965b) *Amateur Speculators*. Ithaca, NY: Graduate School of Business and Public Administration, Cornell University. Stevenson, R.A. and Bear, R.M. (1970) Commodity futures: trends or random walks? *Journal of Finance* 25: 65-81.
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- Dooley, M.P. and Shafer, J.R. (1983) Analysis of short-run exchange rate behavior: March 1973 to November 1981. In D. Bigman and T. Taya (eds) *Exchange Rate and Trade Instability: Causes, Consequences, and Remedies* (pp. 43-69). Cambridge, MA: Ballinger.
- Irwin, S.H. and Uhrig, J.W. (1984) Do technical analysts have holes in their shoes? *Review of Research in Futures Markets* 3: 264-277.
- Sweeny, R.J. (1986) Beating the foreign exchange market. *Journal of Finance* 41: 163-182.
- Taylor, S.J. (1986) *Modelling Financial Time Series*. Chichester: Wiley.
- Federico Garzarelli, Matthieu Cristelli, Gabriele Pompa, Andrea Zaccaria & Luciano Pietronero, 2014, Memory effects in stock price dynamics: evidences of technical trading, *Journal of Scientific Reports* volume 4, Article number: 4487 (2014)
- Park, C.-H. & Irwin, S. H. What Do We Know About the Profitability of Technical Analysis? *J. Econ. Surv.* 21, 786-826 (2007)

# Step **2** Visual

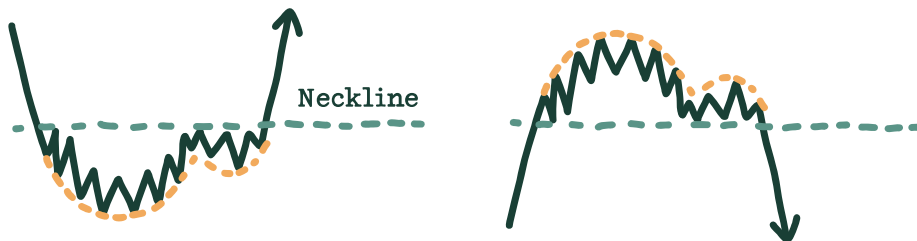
## 1. The Double Top or Bottom



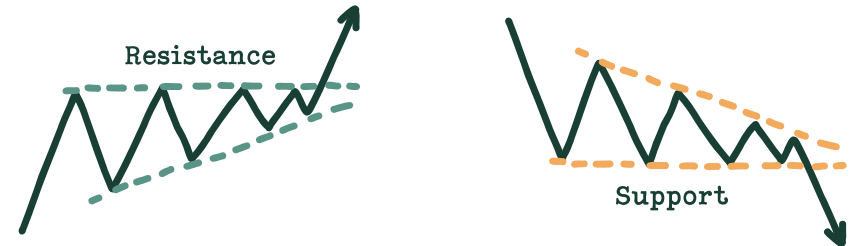
## 2. Head & Shoulders + Inverted Head & Shoulders



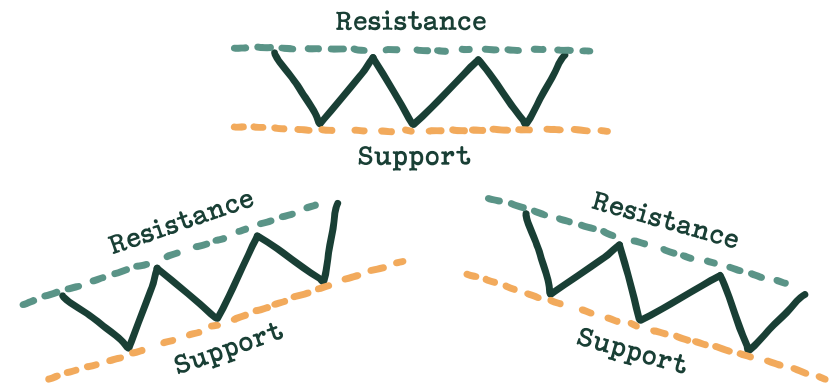
## 3. Cup & Handle + Inverted Cup & Handle



## 4. Ascending & Descending Triangle



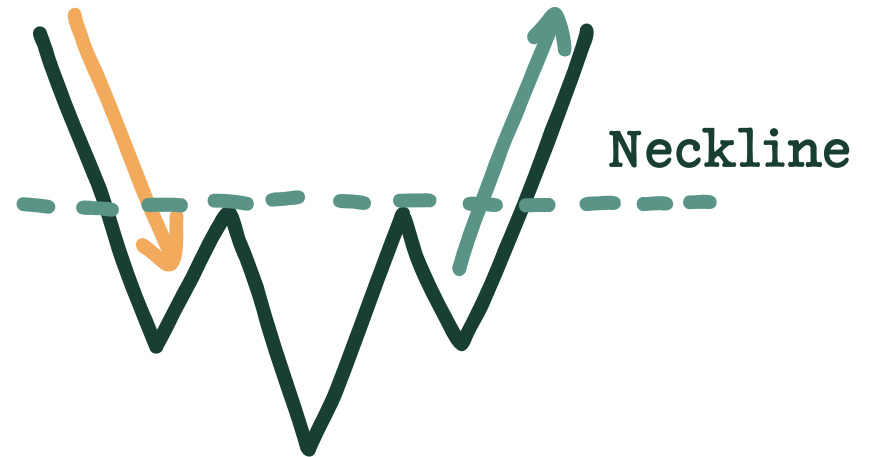
## 5. Channels



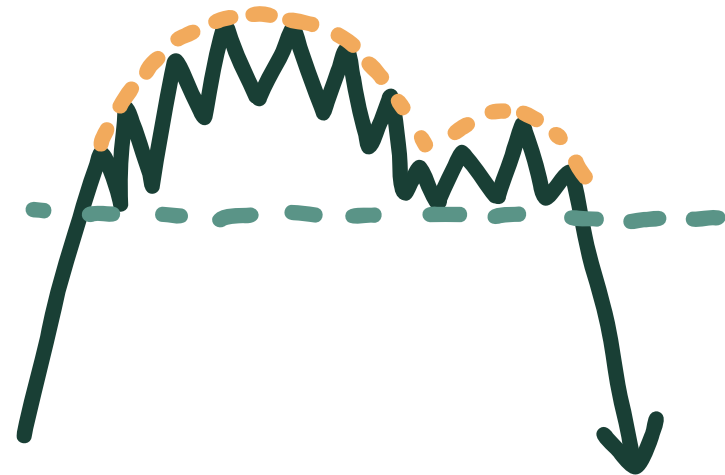
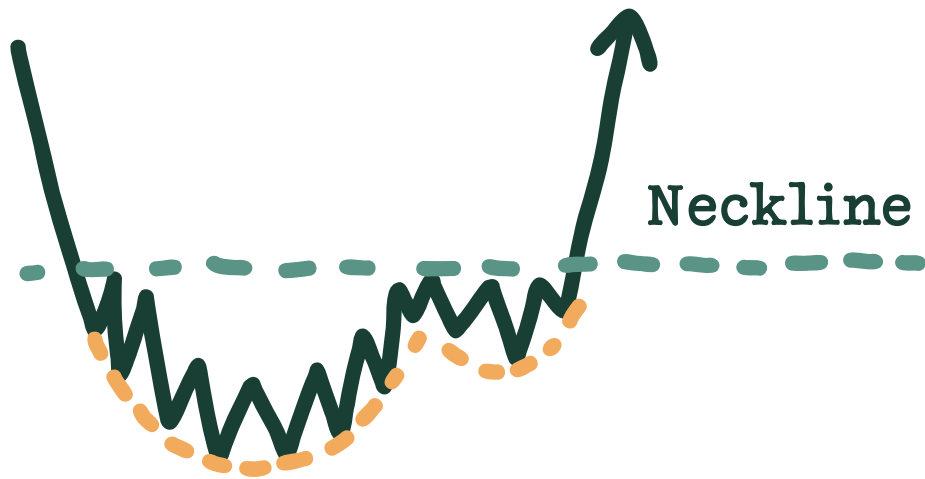
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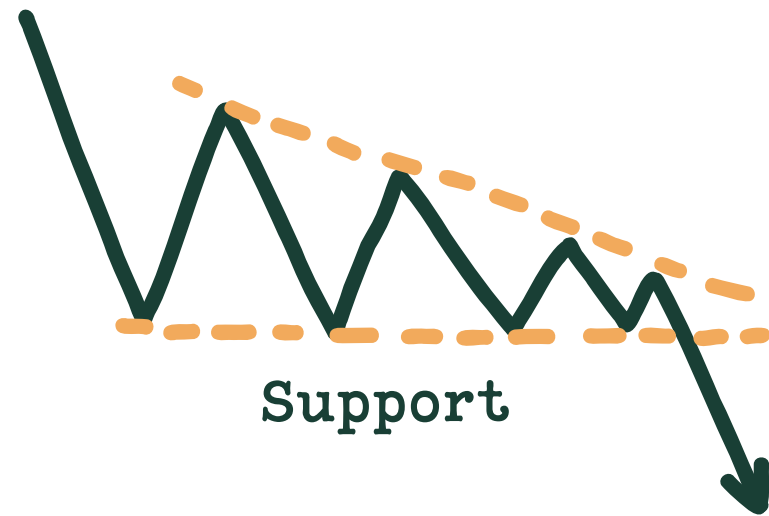
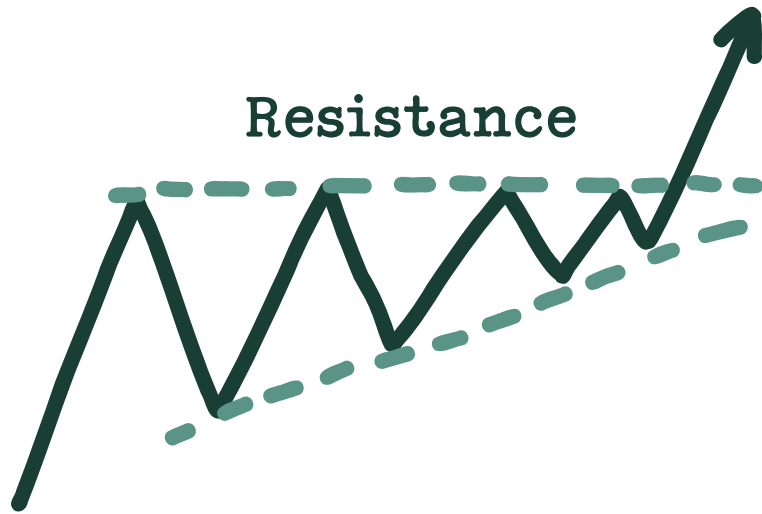
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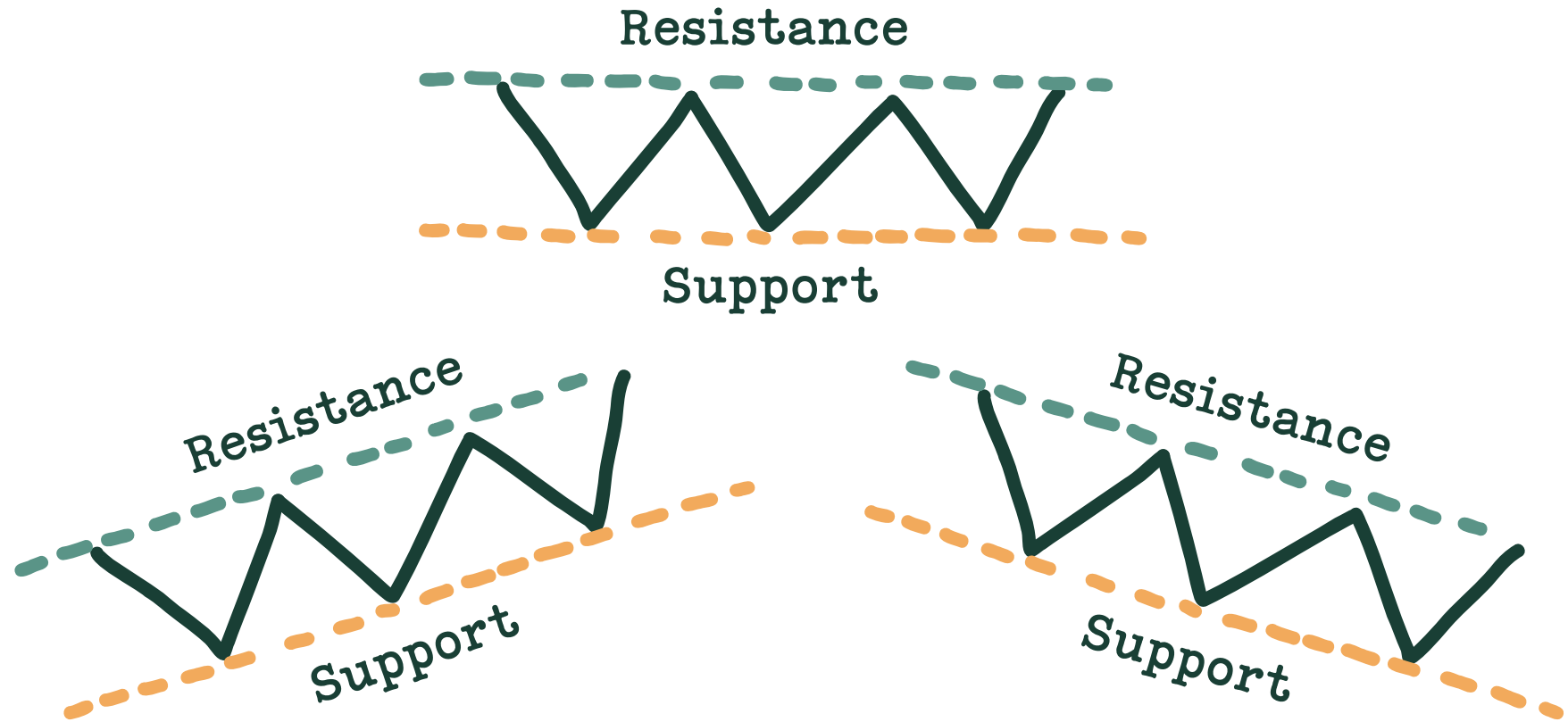
### 3. Cup & Handle + Inverted Cup & Handle



## 4. Ascending & Descending Triangle



## 5. Channels





# Step 3

## Assess the potential for momentum with an insurance bar (daily or weekly).

One of the final steps in my methodology is the insurance day bar. I will assess whether or not the momentum is ready to explode based on the close of the bar, relative to the high and low.

A study by Dunis et al. (2011) found that:

“Open and close chart prices generate a significant  $\alpha$  and their returns cannot be solely explained by the factors derived from Fama and French (1993).”



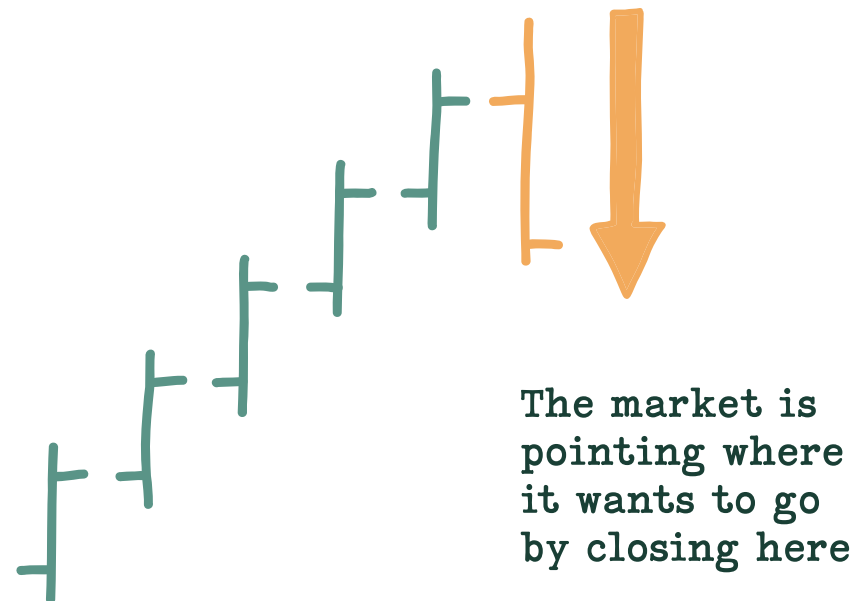
In other words, by using the open, high, low, and close of the bar to determine your entry, you can generate significantly higher profits using technical analysis “which cannot be explained by market factors.”

One year later, Ślepaczuk et al. (2012) released a study showing how Forex and Futures markets are especially well suited to this type of trading.

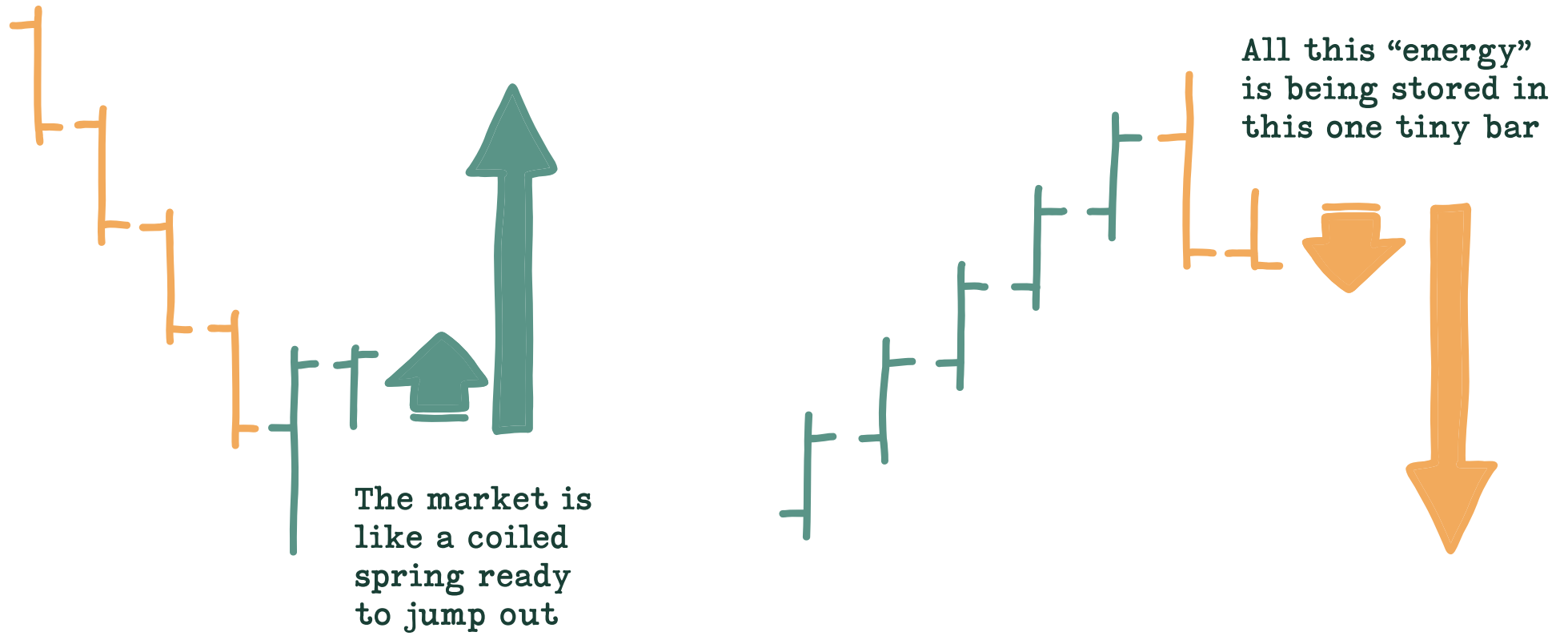
Dunis, C., Laws, J. & Rudy, J. J (2011) Profitable mean reversion after large price drops: A story of day and night in the S&P 500, 400 MidCap and 600 SmallCap Indices. *Journal of Asset Management*, August 2011, Volume 12, Issue 3, pp 185-202

Robert Ślepaczuk, Grzegorz Zakrzewski, Paweł Sakowski (2012), Investment strategies beating the market. What can we squeeze from the market? *University of Warsaw - Faculty of Economic Sciences*, No. 4/2012 (70)

# 1. Key reversal



## 2. Inside Day Bar



# Step 4

## Let the market confirm that momentum with a resting order.



The best way to confirm that your decision is correct, is to let the market confirm it. Besides making intuitive sense, there is an incredible amount of scientific evidence to back this up.

Grundy (2001) and Hirshleifer (1998) all document how profit increases when market momentum is automatically confirmed with a limit order.

The latter study has been confirmed and cited hundreds of times. For example Shantha et al. (2019), Brasiano et al (2017), and Alti et al. (2019).

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ALTI, AYDOĞAN & TITMAN, SHERIDAN. (2019). A Dynamic Model of Characteristic-Based Return Predictability. *The Journal of Finance*. 10.1111/jofi.12839.

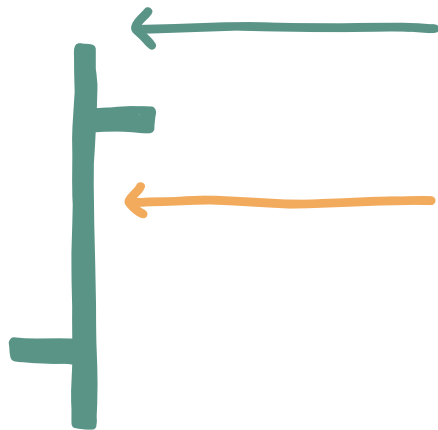
Brasiano, Redik & Hanafi, Mamduh. (2017). Does Momentum a Domestic Phenomenon? A Case from Indonesian Capital Market.

Grundy Bruce D. (2001) Understanding the nature and risks and the sources of rewards to momentum investing. *Review of Financial Studies* 14(1):29- 78 · March 2001.

Hirshleifer, David & Daniel, Kent & Subrahmanyam, Avanidhar. (1998). Investor Psychology and Security Market Under- and Over-Reactions. *Journal of Finance*. 53. 1839-1885. 10.1111/0022-1082.00077.

Shantha & Ram, Vedantam. (2019). Influence of news on rational decision making by financial market investors. *Investment Management and Financial Innovations*. 16. 142-156. 10.21511/imfi.16(3).2019.14.

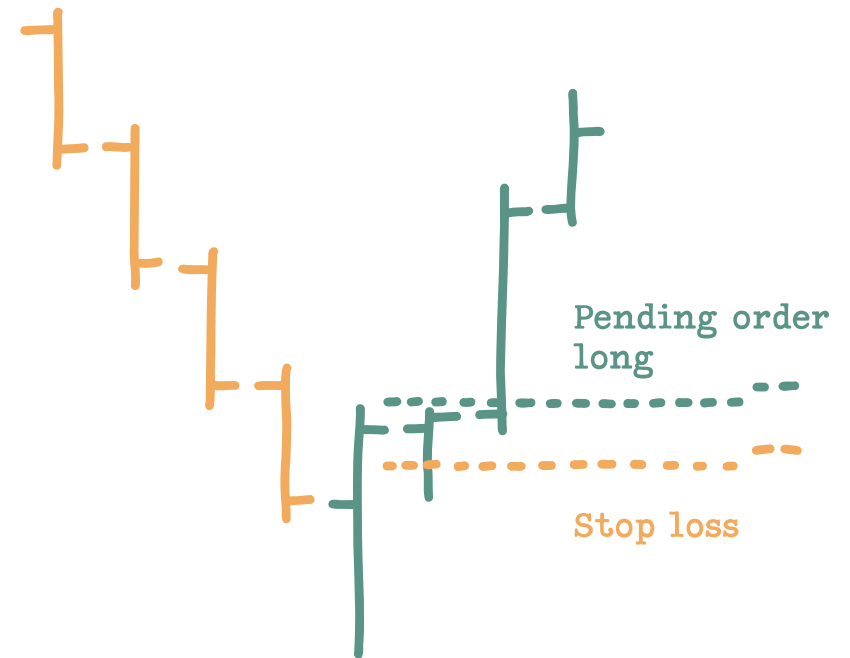
# If price breaks below the low of the insurance bar ... then we enter a pending order long



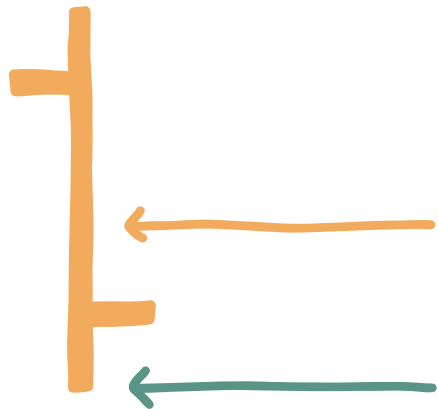
We will "BUY" when price reaches 2-4 pips above the high of the previous day. This is known as a "BUY-Stop Order".

We will place a Stop Loss 20-30 pips below the close of the previous day.

This will automatically close the trade and protect your account balance.

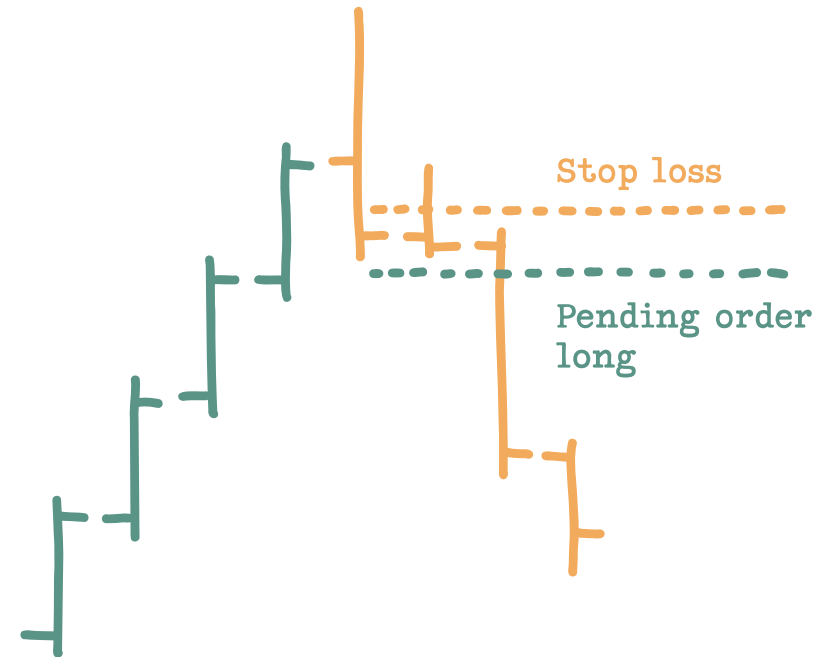


# If price breaks below the low of the insurance bar ... then we enter a pending order short

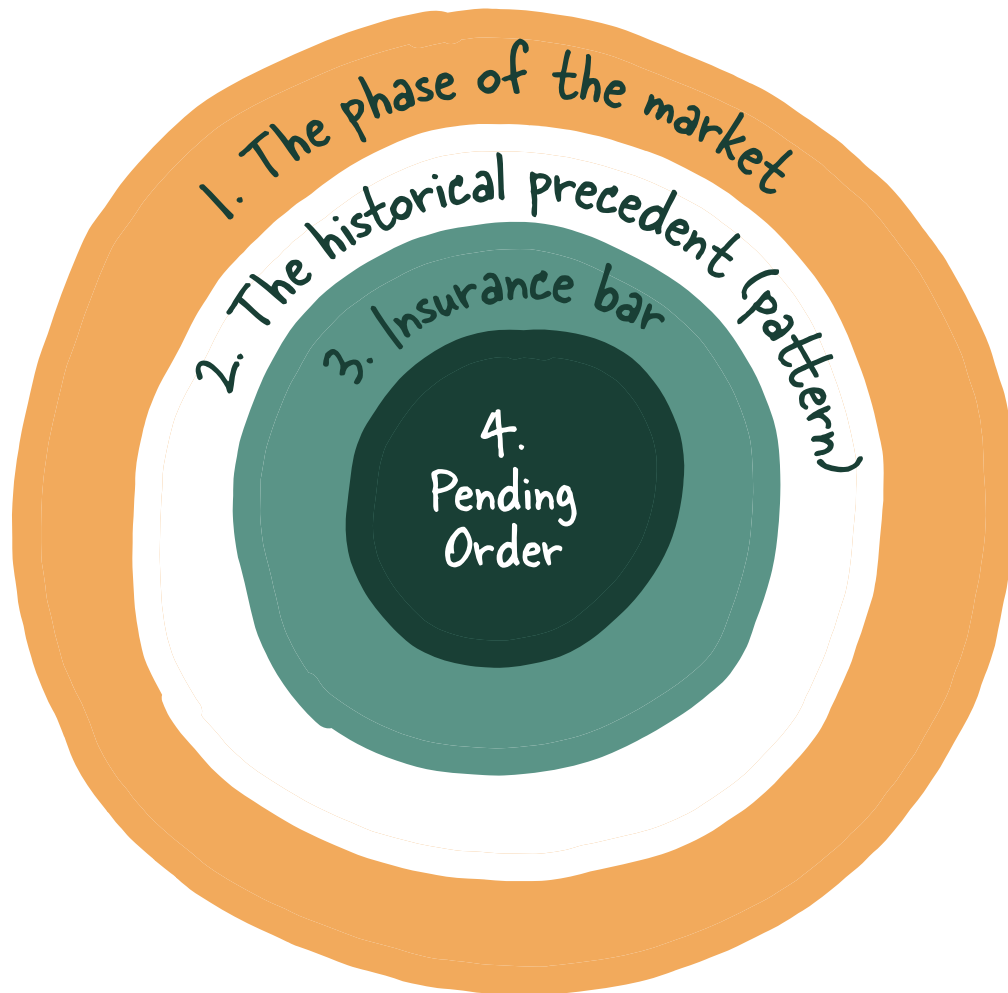


We will place our Stop Loss 20-30 pips above the close of the previous day. This will automatically close the trade and protect your account balance.

We will "SELL" when price reaches 2-4 pips below the low of the previous day. This is known as a "SELL-Stop Order".



# The Pattern Trader Methodology



Every single step within this methodology has scientific backing of some sort.

By layering each one on top of each other we're able to increase our edge in the market.

# Do this: YOUR TASK



1. Print this document.



2. Look at it before you take every trade.



3. Make sure you've followed all the steps and rules.



4. Join me on the workshop where I'll walk you through everything.