Trend Direction

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A logical approach to time, price and pattern analysis provides three important pieces of information a trader should have before making a trading decision.

1. What is the trend direction of the market?
2. What could the market do to invalidate my opinion of the trend direction?
3. What could the market do to confirm the trend direction?

In the Dynamic Trading book and Dynamic Trader Weekly Report, we are constantly asking these questions – and providing the answers. Let's take a look at the current position of the S&P right up through the time this tutorial is prepared.

Time, Price and Pattern Position – Aug. 10

The assumption is the S&P made an important top on July 19 and the trend will be down into at least the second half of Sept., if not much later. The S&P trader's challenge is to now identify what the market could do to confirm or invalidate that assumption.

If the trend is not down and the decline from the July 19 high is only a correction, what would be the typical time and price projections for a corrective low?

Corrections very often unfold in an ABC pattern where the Wave-C is approximately 100% of the time and price range of the Wave-A. If the S&P were to decline beyond the 100% time and price projections, it would be a confirmation the decline was not just a minor correction but the early stages of a bear trend.

The chart below is 40-minute data of the Sept. 1999 S&P contract. On Aug. 5, the S&P made at least a short-term low at a critical juncture of projected time and price. The afternoon of Aug. 14 was the 100% Alternate Time Projection where W.C = 100% W.A in time. The recent low was made the morning of Aug. 5, just five bars later. The Aug. 5 low was 1292.0, just a few points below the 100% Alternate Price Projection at 1301.8 where W.C = 100% W.A.

Trend Direction

As of the Aug. 5 low, the S&P had reached the typical time and price projections for a Wave-C. We now have some very important information that can be used to make high-probability trading decisions.

If the Aug. 5 low is a Wave-3 low, the S&P should not trade above 1353.1, what is considered the Wave-A or 1 low. A Wave-4 should not trade into the range of Wave-1. If the S&P traded above 1353.1, it would be a signal Aug. 5 completed a Wave-C correction and the bull trend is still valid.

If the S&P continues to decline below the Aug. 5 low, it would be a signal that confirms the S&P is in the initial stages of a bear trend, not a minor correction. When a market exceeds the typical targets for a correction, the assumption should be it is in an impulse trend.

1. Trend Direction: The assumption is the trend is down and the S&P will continue much lower in the weeks ahead.

2. What would **invalidate** the Trend Direction? A trade above 1353.1 would be a signal the trend has not turned bearish as anticipated.

3. What would **confirm** the bear trend direction? A trade below the Aug. 5 low at 1292.0 signals the bear trend should continue.

Trading Strategies

Technical analysis is great. Unfortunately, many want-to-be traders never get beyond the technical analysis stage and often develop paralysis-of-analysis and never make a trading decision. What specific trading strategies would we use based on the simple analysis above?

1. As long as the S&P has not traded above 1353.1, all trades should be oriented to the short side in the direction of the main trend.
2. Look to sell on minor corrections above the Aug. 5 low and sell on trend confirmation signals if the S&P continues to decline below the Aug. 5 low at 1292.0.

The Dynamic Trading book teaches specific low-risk trend reversal and trend continuation trade-entry strategies.

You should be able to answer the three important questions – what is the trend direction, what will confirm and what will invalidate the trend direction – before you consider making a trade.