

Welcome to the first lecture of the price action trading volume 3. The lectures in this new volume are going to follow more or less the same format of the volume 2. I will take a market scenario and strip it down to its smallest components so you can learn how the attention to detail can make all the difference in professional price action analysis. It's important also that you remember that the instrument and the timeframe we analyze it's not relevant. As I showed many time in the past already, price action functions in the exact same way in all financial instruments and all timeframes.

In this first lecture we are going to start a little bit slower in a sense by not focusing too much on the context of what's happening in the market, but we are going to focus more on the linework and how different tools correlate in a non-obvious manner. Price action traders must remember that their edge lies in the ability to see context and lines that most of the market cannot see. Everybody can see the obvious horizontal support and resistance line, but the lines you learned in the price action trading course volume 1 are completely outside the realm of analysis of most of the participants in the market. Seeing these lines is not easy of course, but knowing about their existence is half of the work done already.

There is a lot to be said also about the feeling of trading in the zone as it is usually referred to in the industry. If you are a price action trader with some experience under your belt, you must have noticed already that there is a point in the analysis where things begin to make a lot of sense, which is something that certainly doesn't happen when you open a chart and everything seems like a chaotic mess. This state where everything begins to make sense in the chart is a natural consequence of creating a professional analysis by counting major and minor highs and lows, and starting with the simplest forms of context, and then building the analysis from there. Just like a skyscraper begins with a solid foundation.

Without further ado, let's begin the analysis of this lecture, starting by observing four points in this chart. We have a high followed by two lows, and then another high in what we would call a major running flow in the fractal flow jargon. Lows number 2 and 3 are referred to in the technical analysis industry as double bottoms, which is something that tells you absolutely nothing new. It's just a description of what's already there. This is where our problem starts because alternating highs and lows like we have displayed here in this chart represent an opportunity to draw a pitchfork.

The possibility of drawing a pitchfork implies that we must choose the axes of the pitchfork exactly, and in this case, it's not clear where we should place the b-axis of a pitchfork that has its a-axis in high number 1, and its c-axis in high number 4. In other words, we need to choose between lows number 2 and 3 to draw a b-axis, and this choice matters of course because the angle of the pitchfork is going to change depending on our choice, and that by itself will produce a significant difference in the future of the analysis.

Let's first analyze what happens when we draw the b-axis of the pitchfork in low number 2. We can tell immediately that the centerline of the pitchfork acts as a barrier for price in the large price vector down of the running flow. Here is where the attention to detail begins to make a difference in terms of precision. Somewhere after the major high number 4, the frequency of the market in relation to the pitchfork has shifted, and we can clearly see that by the space between price and the upper line of the fork, and more obviously, when price reaches the centerline without respecting it exactly or creating what's called an overshoot.

If you are a student of the price action trading course volume 1, you may have an idea of where I'm going with this. The way we have to solve this problem we are analyzing is by using the principle of frequency shifting to catch this change in frequency in real time, and

hopefully increase the accuracy of the analysis. In this case, it's very straight forward because the space between price and the upper line of the fork already gives us a clue of how the frequency shift can happen.

If you notice carefully, before price touches the centerline for the first time, there is a minor flow developing for the downside. The upper limits of that minor flow are the first sign of where the frequency really is. Right after that, price dives down to the centerline creating an overshoot, and then it comes back up to create a high that has a series of wick expansions. This situation shows that there is some sort of barrier in that level because buyers are trying to hit it higher, but the unusually large wicks imply that sellers are not letting the buyers hit price higher.

If we observe the limit of the minor flow before this wick expansion, and the wick expansion itself, it's not difficult to see that they follow more or less the same angle as the upper pitchfork line. If we shift the fork down to these extremes we are talking about, we will see that the rest of price action is completely captured by the upper half of the pitchfork with a decent accuracy. This frequency adjustment also happens to catch one high with the tail of the pitchfork. This is the sort of detail that adds to the subtlety of the linework and enables the trader to trust a line more easily.

Now let's analyze the exact same linework, but this time the b-axis of the pitchfork will be placed in the low number 3. Even though the pitchfork is almost the same, the relationship between price and the fork lines changes because now we are not talking about a frequency shift per se, but we are talking about a contraction in volatility. Notice that the pitchfork catches the angle of the major vector down, but it fails to catch its edges. However, it fails to catch its edges in a suspiciously symmetrical way. In more technical terms, we have undershoots in both sides of the pitchfork.

Using the perspective from physics, if we imagine that price is a particle that follows a Brownian motion, which is the standard consensus in finance, we can see that the volatility of the third major vector down was lower than the volatility projected by the pitchfork. The great thing about the pitchfork is that beyond giving us a projection of future volatility, it also gives us goal posts to measure if this future volatility is going to be as expected or not. The failure of the projection is also good information as you can see in this example.

A pitchfork can also be correct about the angle, but wrong about the range of volatility, which is exactly what's happening in here. If we take the fork angle and try to find the frequency along the lows in the final moments of the third major vector down, we'll see that the angle of the fork catches those frequencies with an astounding precision. The conclusion about this whole example is interesting. It tells us that a pitchfork is a versatile tool, and it can show us different ways of pointing to the same thing. When you're trying to decide which low you are going to place the b-axis, your answer should be predicated on how much further evidence you can find about how well the pitchfork in question is able to touch on the current frequency of the market.

Thinking about price in the frame of physics can be useful sometimes because that enables us to grasp a little better what the goal of a pitchfork is. In other words, a pitchfork is a tool to project the future angle and range of volatility of the market based on the recent past. It takes advantage of the short-term memory window that the market appears to display and uses that to create a window to the imminent future. Remember also that a failure in this projection can sometimes be useful. Bad information is still information at the end of the day in this case.