P&F Trendlines [ChartSchool]

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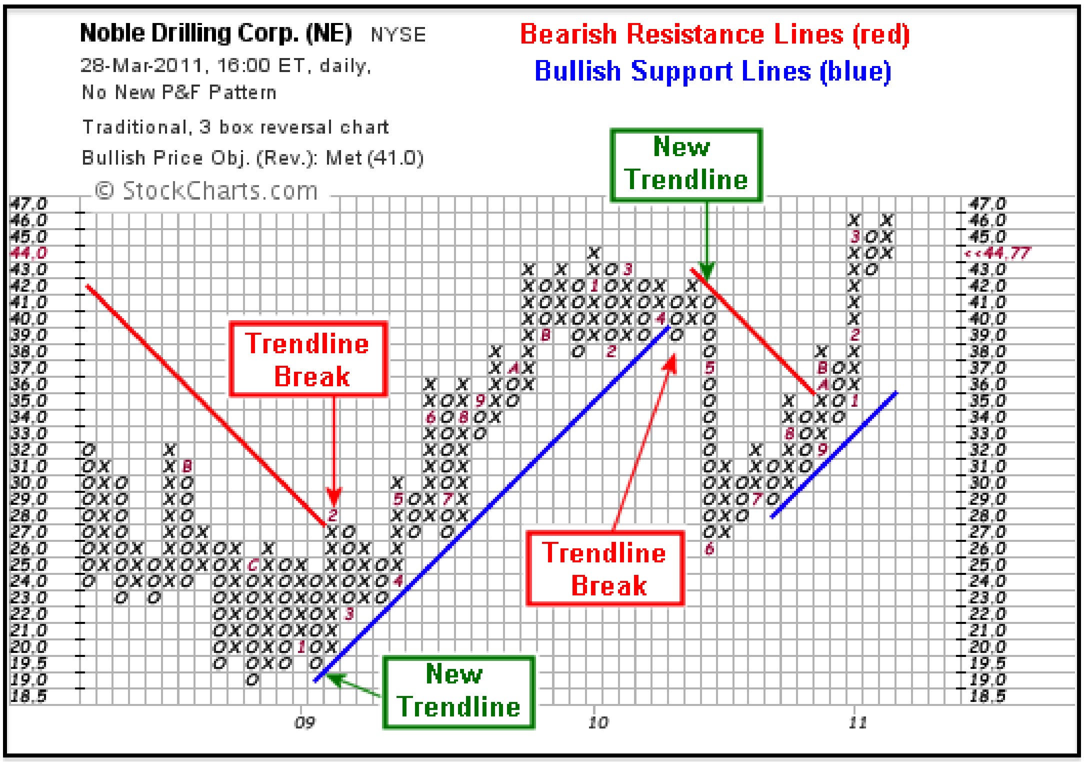
P&F Trendlines

Introduction

Trendlines on 3-box Reversal P&F charts are drawn at 45 degrees up and 135 degrees down. An ascending trendline is called a Bullish Support Line and a descending trendline is called a Bearish Resistance Line. Because these lines are drawn at specific angles, they represent a specific rate of ascent or descent. Chartists can use P&F trendlines to define the overall trend and look for signals in the direction of that trend.

Changing Trendlines

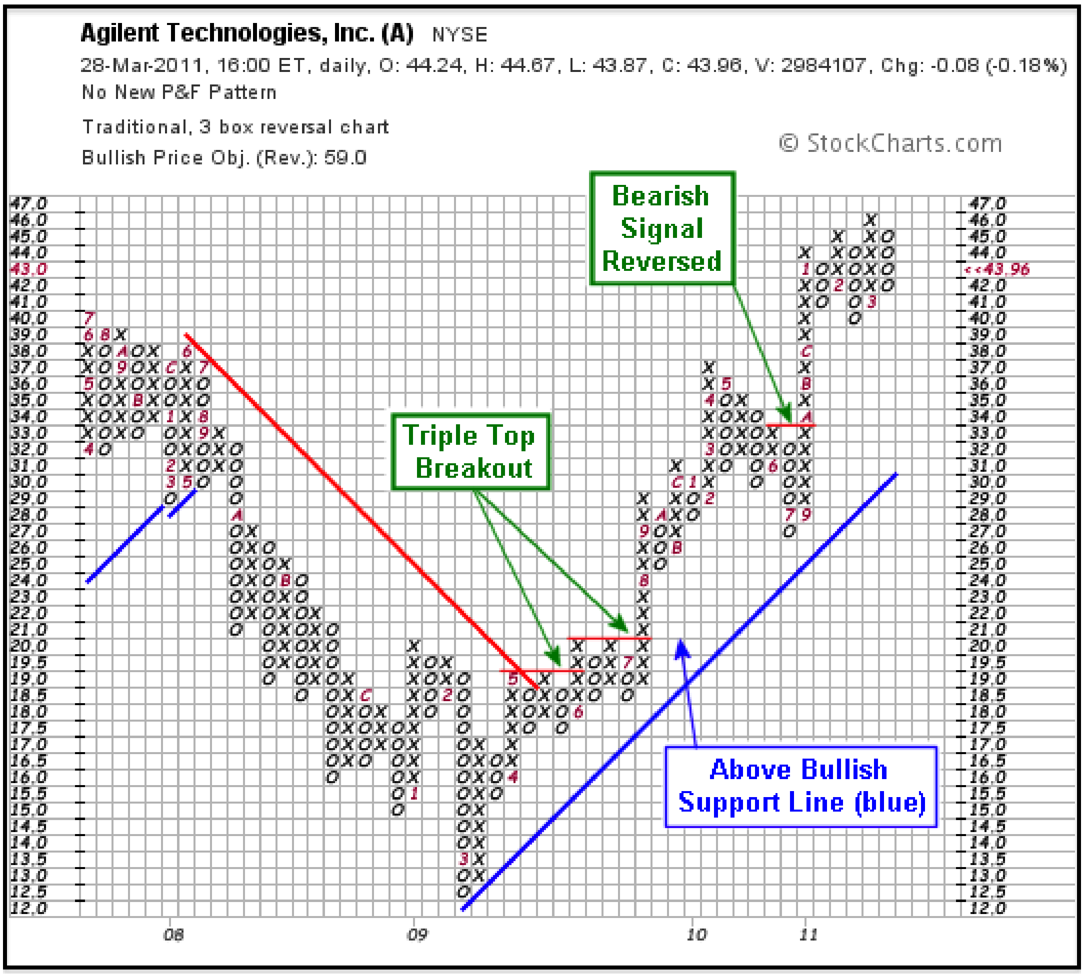
There is always a Bullish Support Line or Bearish Resistance Line present. After a break above the Bearish Resistance Line, a Bullish Support Line will be drawn from an important low. Extending up at a 45-degree angle, this line will remain in force until broken. Once broken, the Bullish Support Line will cease and a new Bearish Resistance Line will be drawn from an important high near the break. Extending down at a 135-degree angle, this line will remain in force until broken.



The chart above shows Noble Drilling (NE) with four trendlines. The Bearish Resistance Line extended through 2008 and was broken in early 2009 (red 2). At this point, the Bearish Resistance Line ended and a Bullish Support Line was drawn from the low. This line extended the rest of the year and was broken in April 2010 (between red 4 and red 5). A new Bearish Resistance Line was then drawn from the high and remained until the October 2010 break (red A).

Bullish Support Line

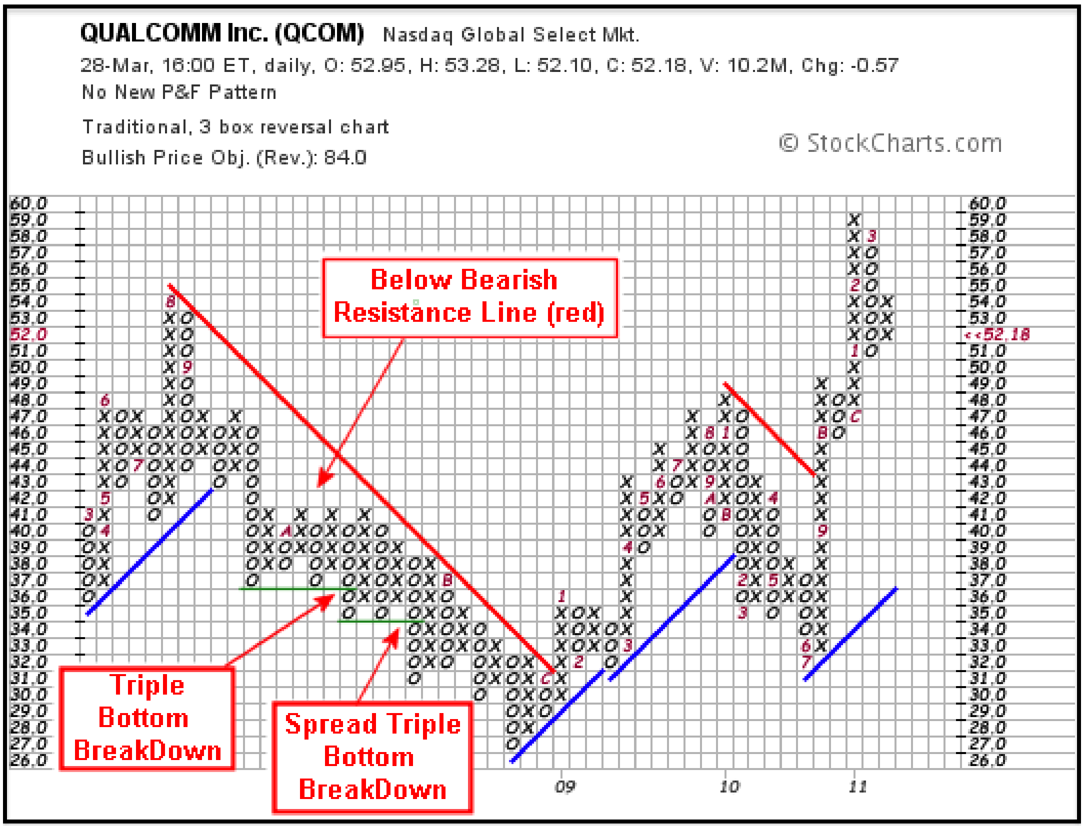
In general, an uptrend is present when prices are above the Bullish Support Line. This line extends up at a 45-degree angle to ensure a certain rate of ascent. Sideways price action or a slower rate of ascent will lead to a trendline break. According to P&F theory, bullish signals should be taken when above this trendline and bearish signals should be ignored. This is trading in the direction of the bigger trend.



The chart above shows Agilent (A) with a blue Bullish Support Line. There were at least three bullish signals above this trendline. There were two Triple Top Breakouts in 2009 and then a Bearish Signal Reversed Breakout at end of 2010. The red "A" on the chart marks the Double Top Breakout that confirms the Bearish Signal Reversed pattern. This red "A" also marks the month of October.

Bearish Resistance Line

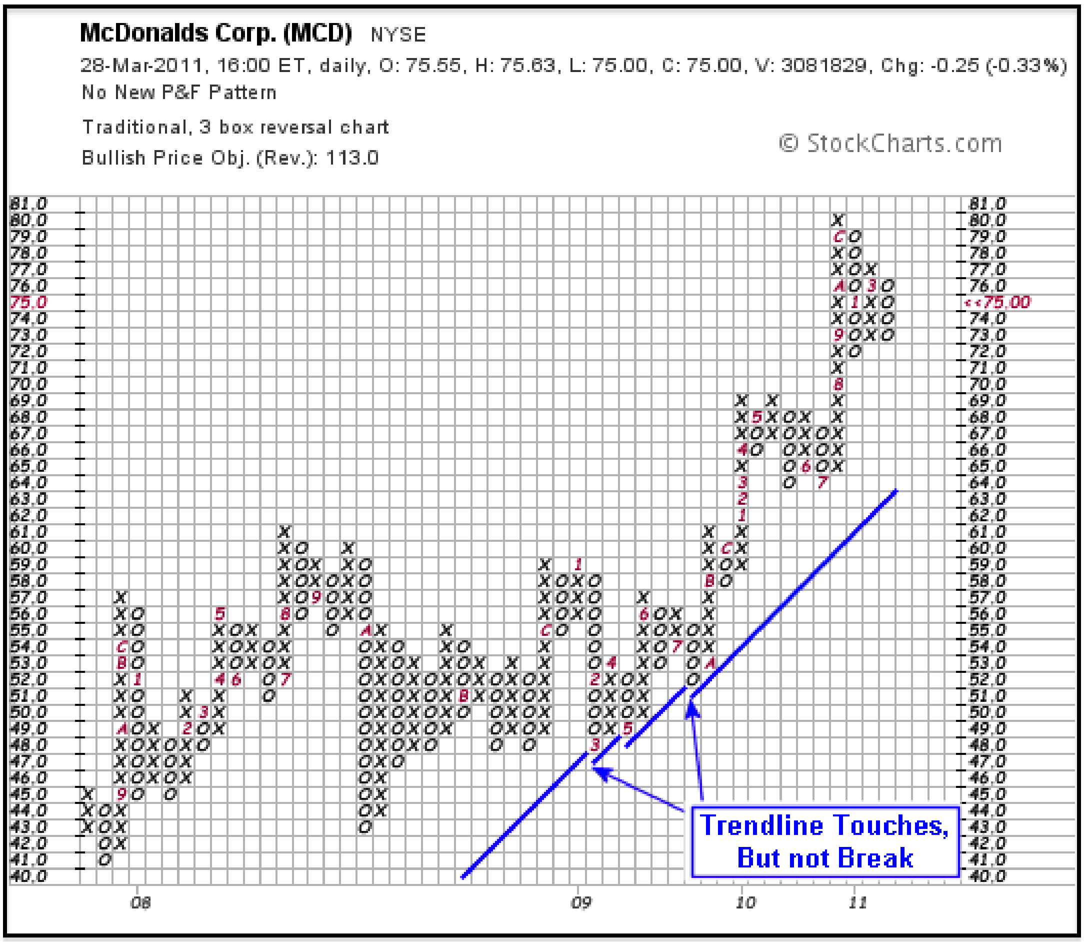
A downtrend is present when prices remain below the Bearish Resistance Line. This line extends down at a 135-degree angle, which is just a 45-degree angle turned upside down (180 - 45 = 135). This angle requires a certain rate of descent. Sideways price action or a slower decline would lead to a trendline break. According to P&F theory, bearish signals are preferred when below the Bearish Resistance Line. Bullish signals should be ignored or used to take profits on short positions.



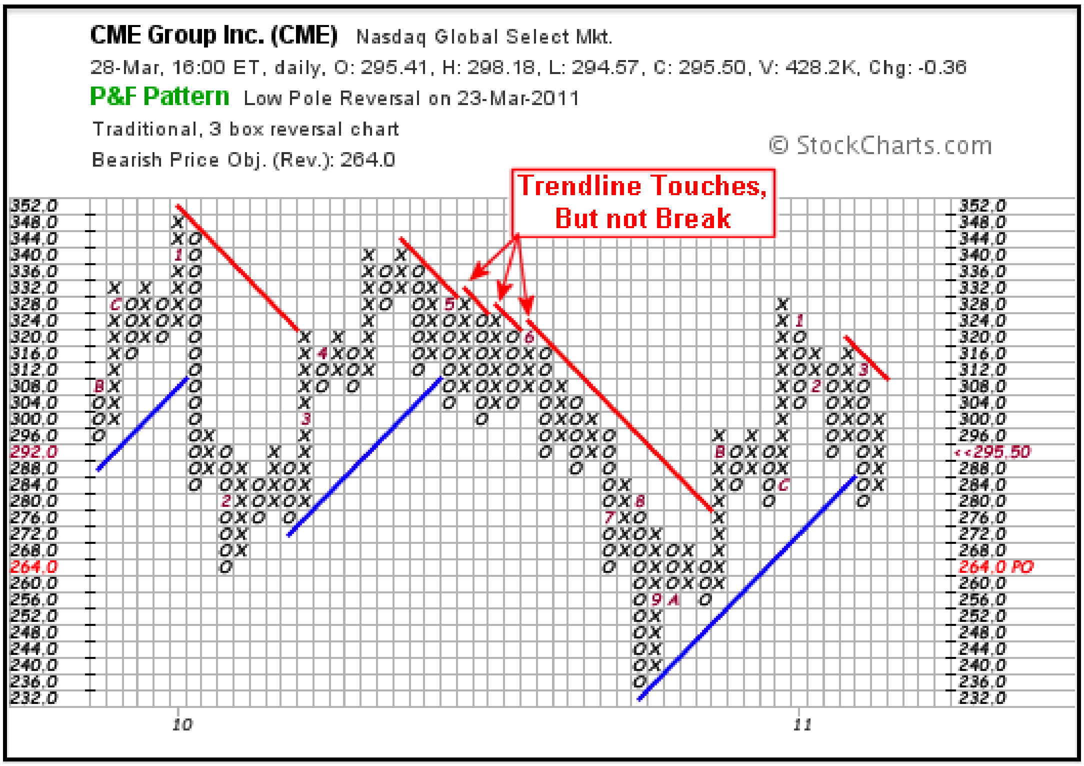
The chart above shows Qualcom (QCOM) with a Bearish Resistance Line in the latter part of 2008. Well after this line was established, the stock forged a Spread Triple Bottom Breakdown and a Triple Top Breakdown in October. The red “A” marks the beginning of October and the red “B” marks the beginning of November.

Trendline Adjustments

It ain't broken until it's broken. There are times when an O-Column declines right to the trendline and reverses back up. Technically, this is not a trendline break. However, a new trendline is required to reflect this test. The chart below shows McDonalds (MCD) touching trendlines three times in 2009. A red 3, a red 5 and an O printed in the boxes that coincided with the trendlines. Because these trendlines were not broken, the line shifted down one box to reflect an adjusted rate-of-ascent.

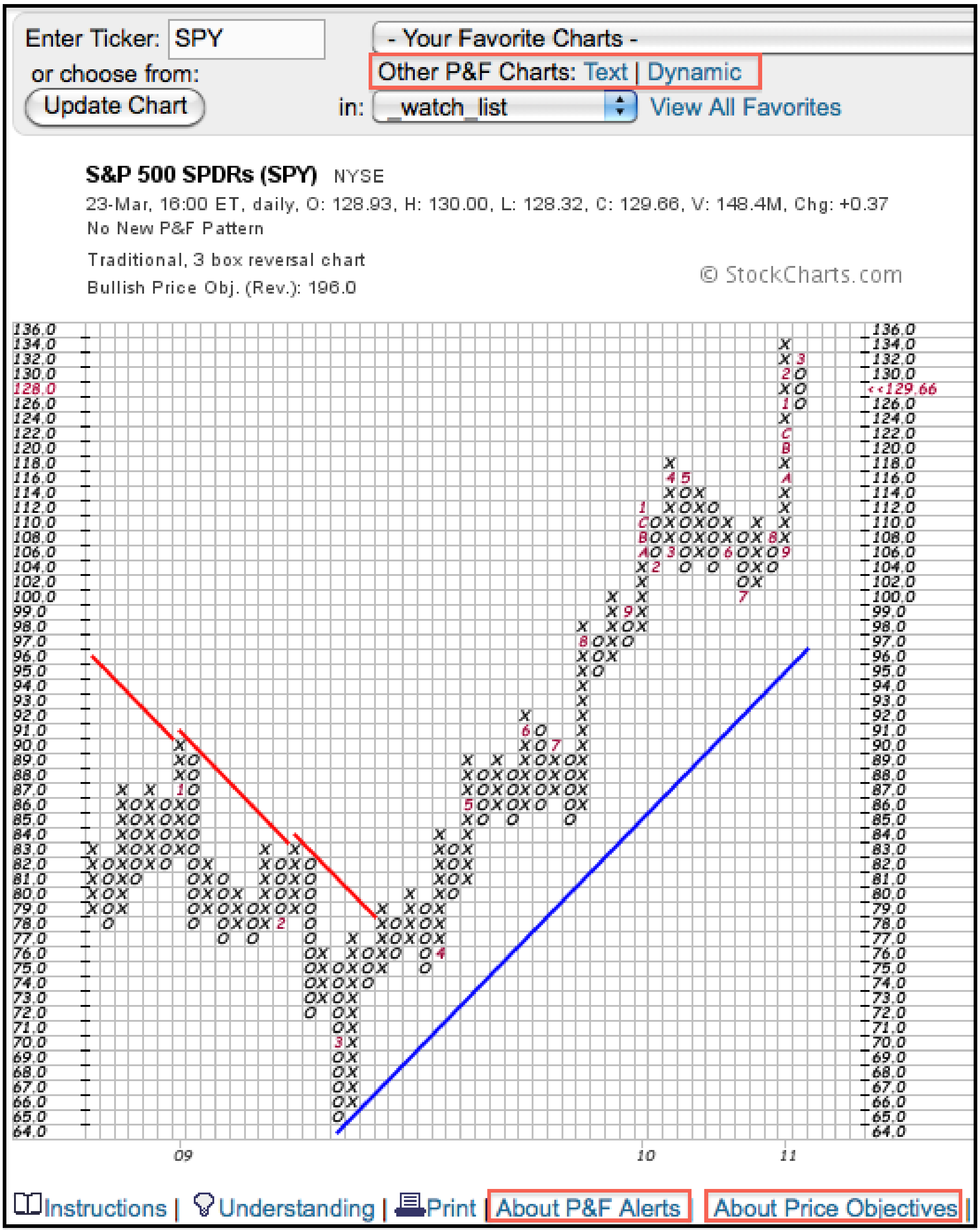


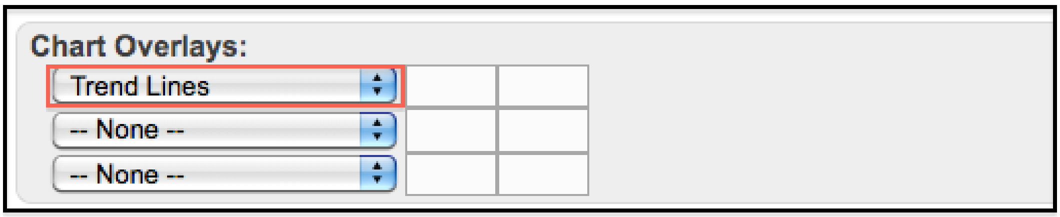
The same holds for Bearish Resistance Lines. Sometimes an advance extends to the same box as the Bearish Resistance Line, but does not break this trendline. After the subsequent downturn, a new Bearish Resistance Line is added based on this new reaction high. The chart below shows CME Group (CME) hitting the Bearish Resistance Line a few times in the middle of 2010. Despite challenging these trendlines, there was never an actual breakout. After the reversal back down, a new trendline was drawn one square higher.



Creating P&F Trendlines

You can add P&F Trendlines to any P&F chart using the “Trend Lines” overlay in the Overlays dropdown on our P&F Chart Workbench.





Conclusions

Trendlines drawn on 3-box Reversal P&F charts are more objective than trendlines drawn on bar or line charts. Chartists can use this objectivity to establish a trend biased based on the trendline displayed. A bullish bias is present when the current trendline is a Bullish

Support Line. A bearish bias is present with a Bearish Resistance Line. Daily P&F charts cover a fairly long timeframe. Chartists can use the daily P&F chart to establish a big trend bias and then turn to 30-minute P&F charts to look for signals in harmony with that trend.