P&F Vertical Counts


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Introduction

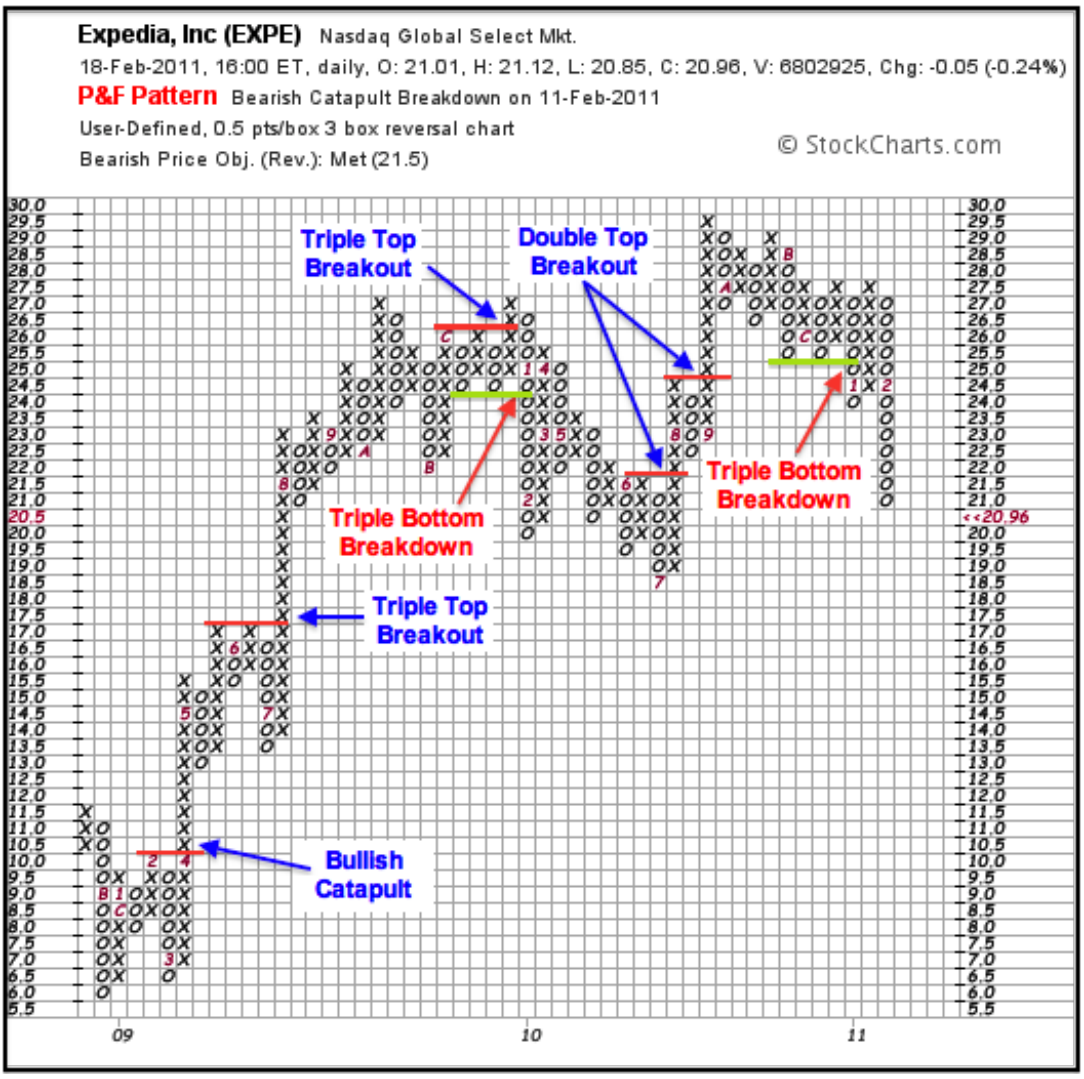
Point & Figure price objectives can be determined using the vertical count method. As its name implies, this method is based on the length of an important column. This can be the column that triggers a breakout or one that forges an important high or low. Once the column is complete, chartists can apply a simple formula to estimate an **Extension** and then apply this extension to the column high or low for a **Price Objective**. Keep in mind that these Price Objectives are rough estimates based on P&F charting techniques. There is no guarantee that prices will reach the objective.

Count Column

Chartists must first choose the column upon which to base the count, which we will call the **Count Column**. Because this column forms the basis for an upside or downside target, it should be of some importance. Namely, this column should signal some sort of reversal or continuation move with an upside breakout or a downside breakdown. Double Top Breakouts and Double Bottom Breakdowns are the most basic P&F signals required to establish a **Count Column**. The following signals can also be used to establish the **Count Column**.

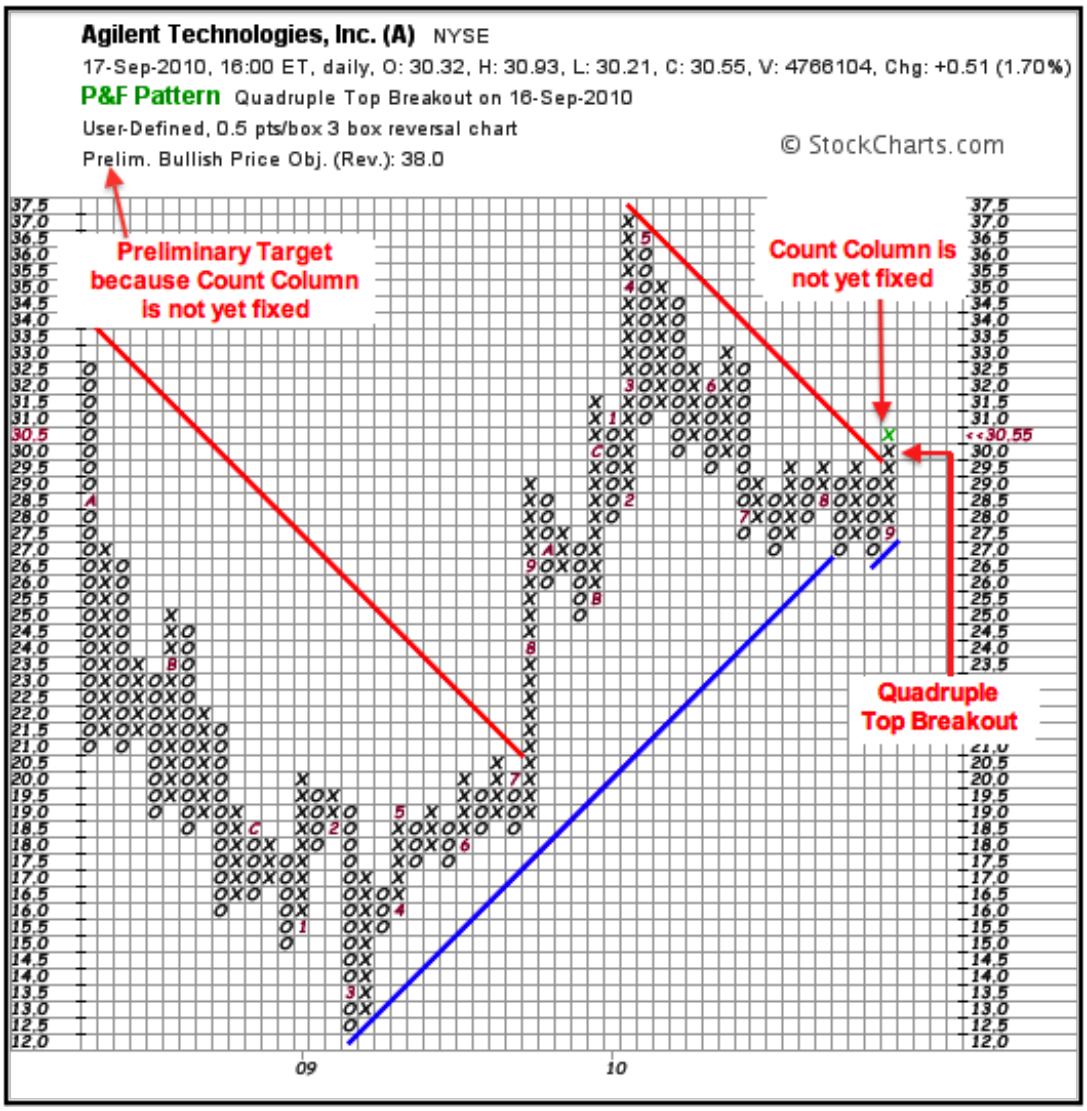
Bullish Breakouts: Ascending Triple Top, Bear Trap, Bearish Signal Reversal, Bullish Catapult, Bullish Triangle, Quadruple Top, Spread Triple Top, Triple Top

Bearish Breakdowns: Bearish Catapult, Bearish Triangle, Bull Trap, Bullish Signal Reversal, Descending Triple Bottom, Quadruple Bottom, Spread Triple Bottom, Triple Bottom



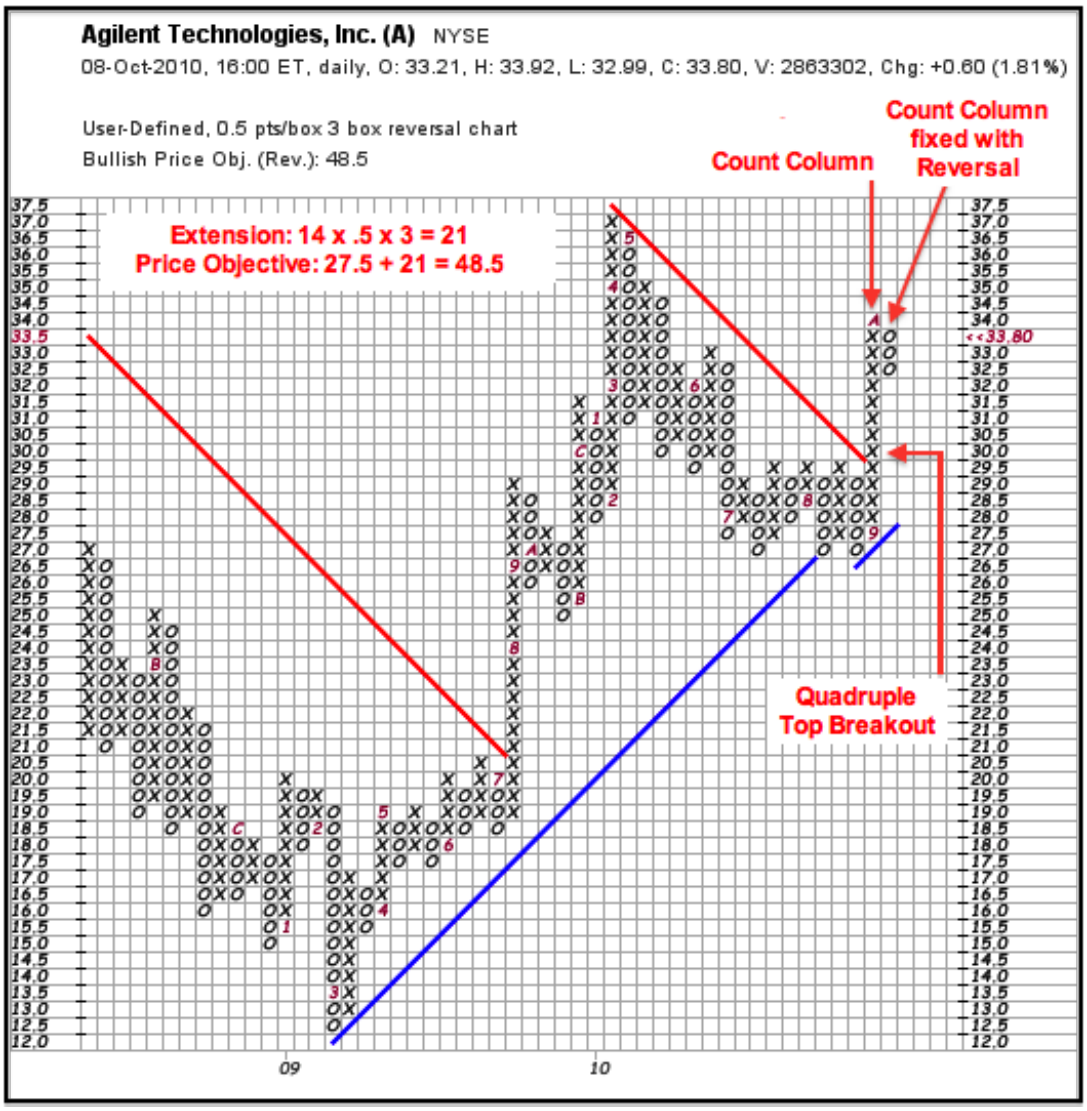
Count Column Completion

Once the **Count Column** is chosen, chartists must wait for this column to be completed to ensure a fixed or unchanging count. The number of filled boxes in a column is not fixed until there is a 3-box reversal. Keep in mind that a column of X's is subject to change until a 3-box reversal forms with three O's in a new column. Once this column is reversed, the number of boxes is fixed and we can then set the count in motion. Similarly, a falling column of O's is not complete until there is a 3-box reversal with three X's in the next column. Chartist can, however, make **preliminary** Column Counts based on the initial breakout. Keep in mind that these Price Objectives are subject to change until the **Count Column** is fixed with a 3-box reversal.

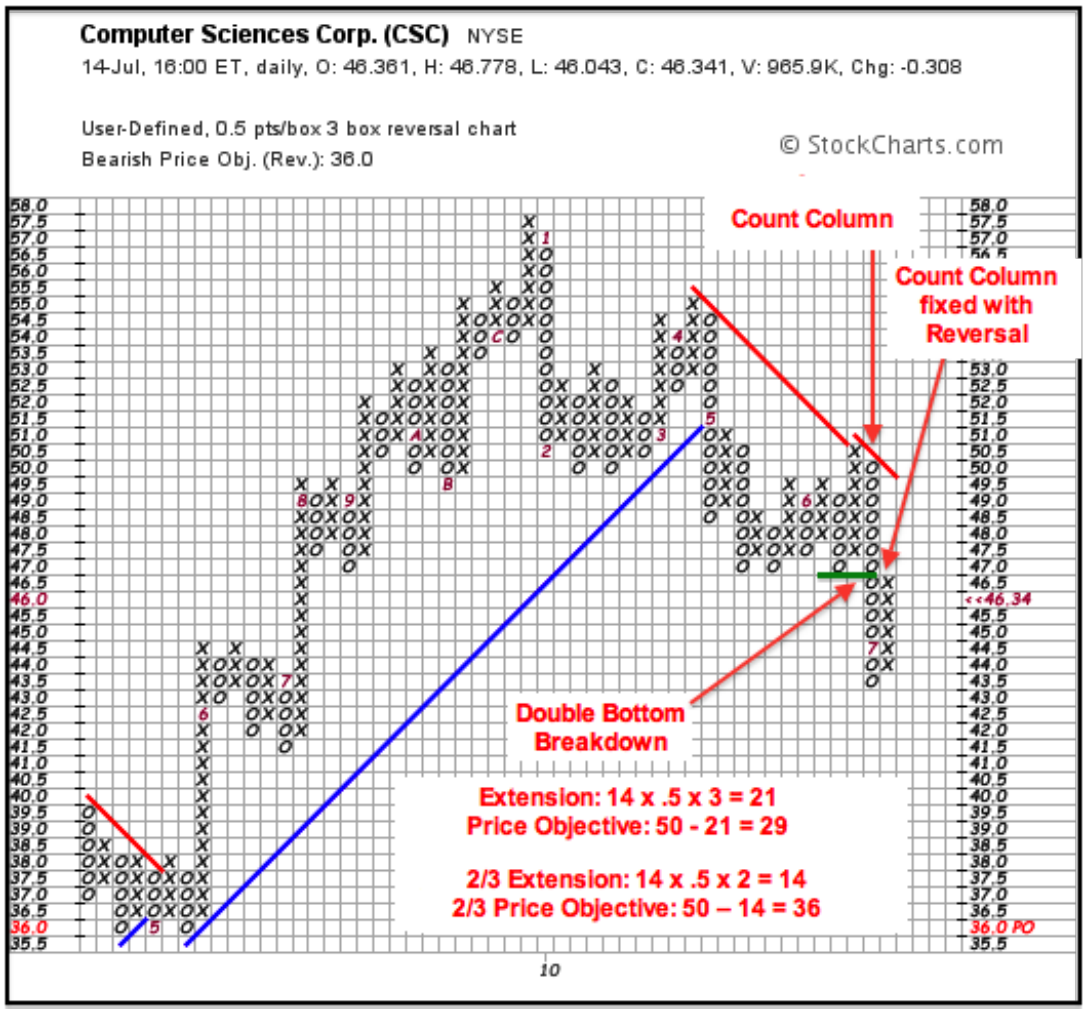


Price Objective

The next step is to count the number of X's or O's in the **Count Column**. This count is then multiplied by the box size and the reversal amount to define the **Extension**. For example, a column of 10 X's on 1 x 3 P&F chart would yield 30 (10 x 1 x 3 = 30). Remember, a 1 x 3 chart implies 1 point per box and 3-boxes for a reversal.



For bullish breakouts, the projected **Extension** (30) is added to the low of the **Count Column** to attain an upside target. On the chart above, the fixed **Count Column** measures 14 boxes. Each box is .50 and the reversal amount is 3. The total **Extension** is 21 (14 x .5 x 3 = 21). This amount is added to the low of the column for an upside target.



For bearish breakdowns, the total is subtracted from the high of the **Count Column** to attain a downside target. The chart above shows Computer Sciences with a Triple Bottom Breakdown to set the **Count Column**. Notice that this column became fixed at 14 columns when the stock rebounded back to 47 with a column of X's. The length multiplied by the box size (.50) and reversal amount (3) gives us the **Extension** (21). Subtracting this number from the high of the **Count Column** yields a downside Price Objective of 29. As noted in the alternatives below, Tom Dorsey advocates using 2/3 of the reversal amount for bearish Price Objectives, which yields a downside target of 36.

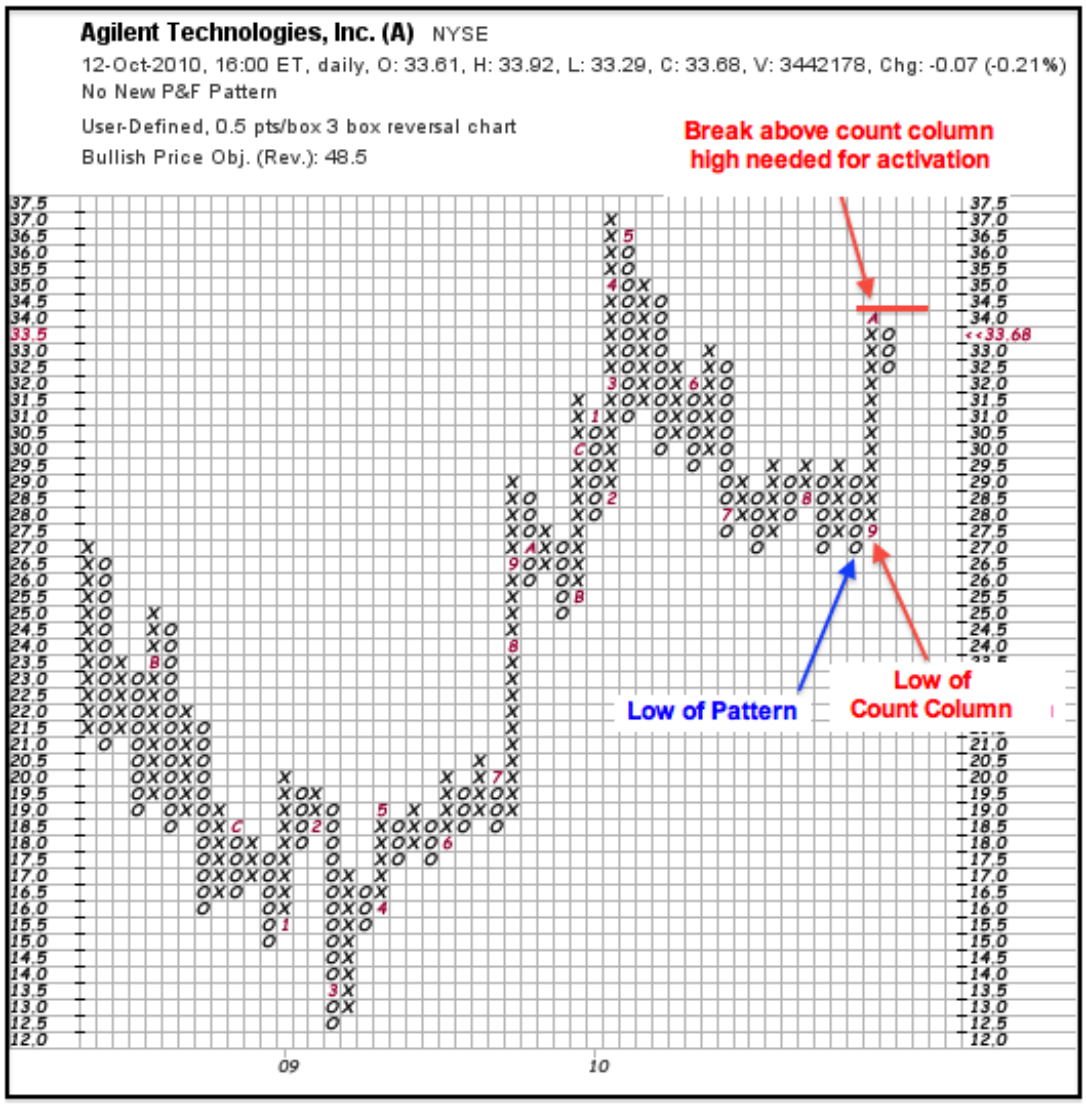
Counting Alternatives

Much has been written on P&F charting over the years. As with Dow Theory, it is unclear who exactly created Point & Figure charting and what the exact rules are. As such, there are different interpretations involving counting methods, the counting column, the projection point and the need for activation.

In his book, Point & Figure Charting, Tom Dorsey advocates a smaller multiplier for bearish Price Objectives. This may be based on the assumption that stocks have an upward bias over the long-term. Dorsey's method multiplies **Count Column** by the box size and then by 2/3 of the reversal amount, which would be 2 for a 3-box reversal chart. The total Extension is then subtracted from the value of the box at the top of the **Count Column**. The above example with Computer Sciences (CSC) shows the 2/3 **Extension**, which is used by StockCharts.com on bearish vertical counts for Price Objectives.

In his book, the Definitive Guide to Point & Figure, Jeremy du Plessis suggests establishing an activation point for vertical counts. Once the **Count Column** is completed, chartists should use the high of that column as the activation point for an Upside Extension. A break above this high activates the count, which in theory makes it valid. Conversely, the low of the Count Column becomes the activation point for a downside Extension.

du Plessis also suggests that vertical counts can be made from any vertical column that forges an important high/low or marks the first move from a significant peak/trough. This could be an exceptionally long column that is not part of a breakout, breakdown or reversal pattern. High-pole patterns could also be considered significant columns for a vertical count.



A.W. Cohen, an early pioneer in P&F charting, advocated starting a count from the high or low of the pattern. Tom Dorsey advocates applying the **Extension** to the high or low of the **Count Column**, which is the method used at StockCharts.com. The difference in these two techniques is often negligible because the difference between the high/low of the pattern and the high/low of the **Count Column** is usually just one box.

Sometimes the box size changes and this requires a counting adjustment. Instead of counting the number of boxes in a column and multiplying by the box size, chartists can simply subtract the column high from the column low. This sum can then be multiplied by the reversal or 2/3 the reversal amount to obtain the Extension estimate.

Combining With Trendlines

P&F charts can be displayed with or without trendlines. Rising (blue) trendlines are called Bullish Support Lines and falling (red) trendlines are called Bearish Resistance Lines. These lines provide a quick snapshot for the direction of the underlying trend. Many traders advocate trading in the direction of the underlying trend. This means taking bullish signals when the trend is up and prices are above the Bullish Support Line. Conversely, bearish signals are preferred when the trend is down and prices are below the Bearish Resistance Line. The chart below shows Agilent (AA) with these trendlines. Notice how the stock broke the Bearish Resistance Line and forged a Quadruple Top Breakout with the move above 30 in the last column of X's. This column is not yet fixed because we have yet to see a 3-box reversal. Price Objectives are preliminary until the column length is fixed.

Assessing Risk

Establishing a Price Objective only covers the reward part of the risk-reward equation. Chartists should also study the chart to assess risk. For bullish patterns and upside price objectives, a move below support or the pattern low would clearly negate a breakout. The box just below the pattern low often marks the worst-case level for a pattern failure. Similarly, a Double Bottom Breakdown or a contradictory P&F pattern would argue for a reassessment. For bearish patterns or downside price objectives, a move above resistance

or the pattern high would clearly negate a breakdown. The box just above the pattern high often marks the worst-case level for a pattern failure. Similarly, a Double Top Breakout or a contradictory P&F pattern would argue for a reassessment. There are sometimes failure clues before price hits the worst-case level. Chartists should employ other technical analysis techniques to measure risk and monitor the unfolding trend.

Conclusions

Price Objections based on a vertical count, horizontal count or any other count should be taken with a grain of salt. Consider these targets as broad guidelines. Securities will not always reach their targets. Some will even reverse course and trigger conflicting P&F signals before reaching their target. A P&F signal and a target are simply the starting point for analysis. Conditions change and chartists must regularly monitor the unfolding chart formation for evidence that would invalidate the original premise. It is also important to employ other technical analysis tools to confirm or refute a premise. For example, chartists can apply basic trend analysis on a bar chart or use bar chart based indicators to confirm the findings on the P&F chart.

Further Study

Dorsey's book starts with the basics of P&F charting and then proceeds to the key patterns. Dorsey keeps his P&F analysis simple and straightforward, much like the work of P&F pioneer A.W. Cohen. As a relative strength disciple, Dorsey devotes a complete chapter to relative strength concepts using P&F charts. These concepts are tied in with market indicators and sector rotation tools to provide investors with all they need to construct a portfolio. There is also a section on using P&F charts with ETFs.

The Definitive Guide to Point and Figure by Jeremy du Plessis lives up to its title and is required reading for the Chartered Market Technician exam. Chartists can learn about 1-box P&F patterns/counts, 3-box patterns/counts and various trading strategies. du Plessis also shows how to apply P&F charting techniques to other analysis tools, such as relative strength and Fibonacci retracements. Plenty of real-world examples are provided throughout the text.