



Trading Between the Lines: Pattern Recognition and Visualization of Markets

By Elaine Knuth



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Insights into a pattern-based method of trading that can increase the likelihood of profitable outcomes

While most books on chart patterns, or pattern recognition, offer detailed discussion and analysis of one type of pattern, the fact is that a single pattern may not be very helpful for trading, since it often does not give a complete picture of the market.

What sets *Trading Between the Lines* apart from other books in this area is author Elaine Knuth's identification of sets of patterns that give a complete analysis of the market. In it, she identifies more complex chart patterns, often several patterns combined over multiple time frames, and skillfully examines these sets of patterns called "constellations" in relation to one another. These constellations turn sets of individual patterns into a more manageable set of patterns, where the relationship between them can lead to tactical trading opportunities.

- Shows how to apply complex patterns to specific trades and identify opportunities as well entry and exit points
- Markets covered include commodities, equities, and indexes
- Presents an effective trading approach based on real market cycles-as opposed to computer simulations-that are found in active markets

Moving beyond the simple identification of basic patterns to identifying pattern constellations, this reliable resource will give you a better view of what is really going on in the market and help you profit from the opportunities you uncover.

Q&A with Author Elaine Knuth

How can a trader improve his/her ability to recognize patterns and visualize where the market might be going?

It is the old adage, experience is the best teacher. Years of market observation has been my teacher. Every day I update data on all markets – even those I am not actively following. I first run an automated a computer scan on capturing patterns built on some of the ideas in the book. While I am doing this, I also visually scan the end of day action of each market before opening. I go through

about 70 charts, spending about a minute or two on each one. This gives a daily feel for what is going on in a market. If I see something interesting, I also then spend more analysis time on that market. Then if any of the automated scans also pick up something, I also take a closer look at those markets. This may sound simple, and rather dull, but if you enjoy the markets it is as interesting as reading a good article or report in the morning.

While going through each market I ask myself:

- Is it range bound?
- Is it in a trend acceleration phase?
- Is it creeping along with very low volatility?
- Or do I even know what is going on at first glance? If not, why not?

Let's say we have a market in a strong and accelerating trend phase, breaking out to ever new highs over the past weeks. Then on the daily scans, we detect that momentum is now weakening against still rising prices. This can be important information.

So once we decide to take a trade and go short, for example, the next logical question is what do we expect from the trade? Or ask where might the market be going?

That is not quite the right question. As traders we are not in the forecasting business. We do not know where the market will go, but instead we build a trading scenario(s) around the current price action and price history.

So with this daily pattern presented and possible trade opportunity, we then take a look at the weekly price history. And ask, for example:

- What was the price range before the most recent breakout to new weekly highs?
- Did this breakout level also act as support, bringing in more buying?
- What drove the buying then?
- What is the collective market motivation for selling now?

In summary, the trigger on this example was the daily action; and the actual trade entry on the intraday price pattern. (Identifying support and resistance or pivot points on the daily session.) The visualization of possible targets -- where the market might be going -- and overall market condition is built on the weekly price history. So I work with patterns in multiple time frames to plan out the entire trade and trade management.

How do the Valley of the Kings and the Place of Truth differ from classical trend continuation patterns?

Classical trend continuation patterns such as ascending or descending triangles, pennants, bull or bear flags are generally more specific to shorter term price action. These patterns are often excellent trade set ups for swing trading strategies. Of these classical trend continuation patterns, the so-called "cup and handle," however, shares some features of the Valley of the Kings in that part of the cup and handle (bottom of the cup) is characterized by a basin or trading range. In our discussion of the Valley of the Kings, we we consider the market

sentiment and logic behind the basin or extended valley.

Also, and unlike the narrow range of the cup basin, our Valley of the Kings presents us with a wide price range, including little price volatility often over relatively long periods of time. Additionally, and important to remember, is that the Valley of the Kings (like other pattern constellations described in the book) is not a trade set up, but instead a state of the market where the trader can seek his or her own set up within this very large unfolding pattern.

Finally, specific to the Valley of the Kings, is that it is a bull trend continuation pattern. Completion of this pattern is often marked by a breakaway daily pattern, such as a breakaway gap to the upside.

Can you discuss the thinking behind two other patterns you discuss in the book: the Quiet Before the Storm and the Lightning Bolt?

I was thinking about market patterns that might express themselves before a “surprise” when markets suddenly head south or take off to the upside. Would there be anything in price action alone to tip us off beforehand? And reviewing maybe hundreds of episodes where a market had big and sudden move, there was, indeed, often a series of conditions that repeated itself before market storm events or where a storm event pattern (as in the Lightning Bolt) had high predictive value. So that is what I’ve discussed here, putting it into weather metaphors to give it a concept and natural logic instead of simple and dry descriptions of market patterns. And I think it worked.

When thinking about what is called “Quiet Before the Storm” we have low price volatility. This is obvious. But there was often something more concrete than just low or even extremely low volatility: a series of identifiable price patterns leading up to and resulting in a big and often rapid sell off. A part of this storm pattern, for example, is when the classic bull ascending wedge pattern fails and all are taken by surprise. (But if you read the book, you will see why this is neither a real failure nor a bull ascending wedge pattern as often mistaken to be.) The exact pattern and conditions behind this “failure” are described as the “Quiet before the Storm.” And like in nature, there are specific atmospheric conditions (read market conditions) that lead up to this before any sudden cloudburst.

The weather metaphor of the “Lightening Bolt” to describe the price pattern behind a market that suddenly and unexpectedly takes off to the upside worked on many levels. Often there is little or no warning, but after this pattern has hit, we know a massive change is underway. So unlike all other patterns we discuss in the book, the lightening bolt is the only one that is not one for anticipatory trade set up, but a reactive trade. And identifying this particular pattern has tremendously helped me trade market situations that come unnatural for me. I have weakness that I like to be early into a trade and not to jump onto a trade one a market has taken off. Of course under some conditions, such as the Lightening Bolt, that is the time to take the trade, reactive or not.

What advice would you give traders looking to incorporate price pattern analysis into their decision making process?

Keep it in perspective and understand exactly what pattern analysis is and is not.

With pattern recognition and visualization tools (that can help us detect even more discreet market behavior) we can determine – to a relatively high degree – the overall state of a market and classify a market condition. Once we have that established, we know (or think we know) the beast we are dealing with. Then, and perhaps by incorporating additional tools of TA, such as momentum or volatility indicators, a market condition and our exact trading approach can be determined. Yet my honest advice is to incorporate price derivative indicators as “diagnostics” and not for absolute trading rules.

Regardless of the level of trading experience, examine markets for patterns that you think have some predictive reliability and where a trading method that fits your style can be incorporated. This exercise to discover and define your own patterns and trading strategies around them will teach you a great deal about price analysis.

If you are a short term swing trader holding trades only a few days at the most, and concentrate on strategies around those patterns and with intra-day price data, understand what the unfolding pattern is over the longer time scales. The intra-day pattern you might be trading is the granular of a much larger price pattern. And if you do not know what is going on in the larger time scale, you see only the single trees in the forest you are venturing into. Eventhough you might only be trading the short term price action, understanding the larger price dynamic will keep you out of trades that appear to be a breakout, for example, but are nothing more than short price volatility.

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Editorial Review

From the Inside Flap

Praise for Trading Between the Lines

"It's refreshing to see an investment book focused on answering the key questions: What's going on in the market? And where might prices be going next? In *Trading Between the Lines*, Elaine Knuth considers the very essence of market dynamics, psychology, and the price patterns associated with a range of conditions and situations. These thoughts are then developed effectively in her book into a colorful lexicon of market environments and potentially powerful trading strategies." —Adam Sorab, Head of Technical Research, CQS LLP, UK

"*Trading Between the Lines* offers readers important insights about the manner in which market patterns reflect differences in perception and human emotion across the trading population. Elaine Knuth makes wonderful use of intuition to communicate the core ideas underlying technical analysis." —Hersh Shefrin, Mario Belotti Professor of Finance, Santa Clara University

"Elaine explains bubbles, reversals, crashes, and how to take advantage of them with subtle common sense. She reminds us that prices and markets are a matter of human relationships, and not farfetched mathematics." —Valérie Gastaldy, Commercial Director, DayByDay, Paris, France

"As a market practitioner for more than 30 years, I have evolved from seeking an indicator to forecast the market to understanding that forecasting is best left to the analysts, and that it is better to make money than to be right. My compliments to Elaine; she has put her money on the line and learned from the hardest teacher in the world—the market. She shares many of these lessons in this book. I particularly liked the idea of creating market scenarios. Once a trader creates a scenario and understands what to do under various conditions, then he or she is never taken by surprise." —James Stewart, Vice President and Director, Capital Markets Division, Raiffeisen Bank SA

From the Back Cover

Financial markets, whether you're talking about equities or commodities, are an ordered system of exchange, where participants are driven by individual responses to information. Within this arena, price, and the patterns emerging from a series of prices, give us instruction—they are our guide.

Nobody understands this better than Elaine Knuth—Principal Partner of Davenport Advisors, LLC—and now, with *Trading Between the Lines*, she shares her extensive insights on the integral role price and pattern play in successfully analyzing, and trading, today's markets.

Unlike other books in this field, which focus on a series of single patterns in isolation, this reliable guide details a series of more complex patterns—often several patterns combined over multiple time frames—and skillfully examines these sets of patterns called "constellations" in relation to one another. Along the way, it will help you discover how conceptualizing price behavior can allow you to recognize price pattern structures with predictive character and build effective trading tactics.

Engaging and informative, *Trading Between the Lines* puts this discipline in perspective as it: Examines specific reversal pattern constellations to the upside as well as the downside Covers continuation patterns and strategies—the Valley of Kings and the Place of Truth—that will allow a low-risk entry strategy for an existing and well-established trend Explores patterns—the Quiet Before the Storm and Lightning Bolt—that signal unexpected moves Brings together many of the pattern constellations and concepts into a universal pattern set called Adam and Eve Addresses the issues of risk and trade management as they pertain to trading pattern recognition methods

When making a trade, you're speculating on a future change in condition. With the pattern recognition and visualization methods found in *Trading Between the Lines*, you'll learn how to create strategies that can fit your risk appetite and exploit changes, or future price events, in many markets.

About the Author

ELAINE KNUTH is the Principal Partner of Davenport Advisors, LLC. Prior to this, she was the managing director at AQX Securities, advisor to the board of AQ Advisors in Zurich, and the managing partner of the Zurich Commodity Trading Advisory, Stewart Capital Management. Prior to starting her career in financial markets, Knuth worked as a journalist for a wide variety of publications, including *Investor's World*, *Forbes*, and the *Journal of European Business*. She is a member of both the Swiss Association of Market Technicians (SAMT) and the American Association of Professional Technical Analysts (AAPTA). Knuth was president of the International Federation of Technical Analysts (IFTA) from 2007 to 2010.

Users Review

From reader reviews:

Louise Wax:

The feeling that you get from *Trading Between the Lines: Pattern Recognition and Visualization of Markets* could be the more deep you searching the information that hide in the words the more you get enthusiastic about reading it. It does not mean that this book is hard to understand but *Trading Between the Lines: Pattern Recognition and Visualization of Markets* giving you thrill feeling of reading. The copy writer conveys their point in a number of way that can be understood by anyone who read this because the author of this reserve is well-known enough. This particular book also makes your own personal vocabulary increase well. Making it easy to understand then can go with you, both in printed or e-book style are available. We advise you for having this *Trading Between the Lines: Pattern Recognition and Visualization of Markets* instantly.

Andrew Parker:

The book with title *Trading Between the Lines: Pattern Recognition and Visualization of Markets* possesses a lot of information that you can find out it. You can get a lot of benefit after read this book. That book exist new information the information that exist in this reserve represented the condition of the world today. That is important to you to understand how the improvement of the world. That book will bring you with new era of the syndication. You can read the e-book on your smart phone, so you can read this anywhere you want.

Eva Ammons:

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David Mandujano:

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