INTEGRATED PITCHFORK ANALYSIS

Basic to Intermediate Level

Dr. Mircea Dologa

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Contents

Dedication

This book is dedicated to

Richard W. Schabacker, a giant of Technical Analysis, who devoted his entire life to pioneering research of the financial markets. His books, published in 1930 and 1932, still reflect the quintessence of modern charting analysis – price movements with their patterns and volume – and are so relevant today it seems that both works have just been written. This giant has not only paved the way for the 21st century trader but also provided an astonishing wealth of charting information which modern market technicians would do well to use!

Apprentice traders today, who are so eager to gather and assimilate trading information.

Cassandra and Kim-Tracy, my beloved daughters, probably the youngest apprentice traders around; they are 14 and 18 years old.

About the Author

Dr Mircea Dologa began his investment and trading career in the pharmaceutical and real estate industries in 1987. Once he passed the Series 7 and Series 3 exams, he realized the scarcity of the true 'know how' tools in financial literature and seminars. As a Commodity Trading Advisor (CTA), he founded a new teaching concept, mainly based on practical aspects of trading, for both newcomers and experienced traders. He is an international contributor to trading magazines in the USA (*Technical Analysis of Stocks & Commodities*, *Futures*); the United Kingdom (*The Technical Analyst*); Germany (*Traders* - English- and German-language editions); Australia (*Your Trading Edge*) and Asia (*The Trader's Journal*).

After reading hundreds of trading books and attending numerous seminars, the same question kept popping up: Where is the meat? Most of the time. . . it wasn't there!

The author's main thought during the two years of planning, conceiving and writing this book was how to revealing the practical aspects of trading. The key topic, continuously present in his mind, is described below.

This *Integrated Pitchfork Analysis* workbook is a way of bringing risk control to the trader using this technique. Risk control is the only factor that counts when building consistency – the same principle applies in any entrepreneurial activity. Risk dominance will be always present because of the trader's professional life. He knows that, of all businesses, trading is the only one that imposes planned losses. Risk management is the only element which will enable him 'to be or not to be' a consistent trader. The main idea throughout the book is: 'How to build consistency', and for that you have to religiously respect the saying: 'You make money, if you don't lose money'. The author sincerely hopes that he has accomplished this hard task of teaching and implementing trading consistency, but will let you, the trader, be the sole judge!

Dr Mircea Dologa attended New York University and Cooper Union School of Engineering and Science in New York and graduated from the latter with a B.S. in Theoretical Physics. He obtained his Doctorate in Medicine from the School of Medicine in Paris. After graduation and internship at the Mount Sinai Hospital in New York City and Xavier Bichat Hospital in Paris, he worked in the medical field of gastroenterology, and also took MBA courses in finance and business management at the University of South Carolina in Columbia and the French School of Business and Finance (HEC Paris France). After holding the position of Medical Director and later General Manager in a French pharmaceutical company, in 1992 he decided to focus exclusively on his investments and since then he has devoted his activity to financial markets. He lives with his wife and two daughters in Paris, France.

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Founder of www.pitchforktrader.com

Acknowledgements

I can never thank enough my wife, Felicia. Without her continuous support, patience and dedication I could have started writing, but certainly never have finished. As with trading, writing demands tremendous peace of mind. . . and she was always there. . . year after year!

Thanks too, to the Wiley Finance Publishing team, which has detected in *Integrated Pitchfork Analysis* an original trading topic worth publishing. The Chichester team has done a tremendous job to help me with the manuscript: Caitlin Cornish, the very efficient Finance Publisher; Aimée Dibbens, Caitlin's assistant, was worth her weight in gold in promptly answering any questions I might have; Lori Boulton and Louise Holden, the marketing team, have been indispensable in their advice about the book's launching; and Rachael Wilkie, the English expert who has initiated me into the science of editing, showing me elegant rephrasing indispensable to the wellbeing of our readers.

The assistance of Pamela van Giessen – the US Editorial Director – was for me very valuable when it came to harmonizing communication across the ocean.

Last but not least, I would like to thank Johannes Petrus Joubert, my student who has become an efficient trader in South Africa. Besides other human and trading qualities, his talent in proofreading has really made the publication of this book possible.

As all authors already know, the making of a book takes almost as long as writing it. . . no detail is to be forgotten!

Would I do it again? Yes, I would!

Introduction

Human nature tends to see what it expects to see . . . (Anon)

Common sense compels us to acquire a consistent technique that gives us the confidence to learn how to trade. This will not come without 'sweat and tears' but, as the Eastern sage says: 'What first brings pleasure, in the end gives only pain, but what at first causes pain, ends up in great pleasure.'

Trading should not be too difficult if you build on a solid foundation . . . just watch the basics!

Integrated Pitchfork Analysis is a coursebook focusing on the branch of Technical Analysis which uses the Andrews' pitchfork trading technique. The process begins with the underlying theory (basic and intermediate knowledge) and then, step by step, the practical aspects about the low-risk high-probability trade from its inception until its termination are covered. The emphasis is on the trade's management and money management. No prior knowledge of trading is required.

The course is divided into two parts. Volume I focuses on developing the basic knowledge of the pitchfork's morphology (study and description of a defined structure: definition, form, inflexion, derivation, and compounding) and its dynamic principles. It is indispensable to have this knowledge before using the more advanced concepts. Volumes II and III (in preparation) will focus on developing the multiple integrative methods that will greatly improve the chances of the trader being consistently successful.

Any professional trader will freely admit that it is vital to master just one main technique at a time. Once the learning process is accomplished, he can then apply his own rules and perceptions to help him become a trading force. Because each trader behaves slightly differently, he will use different methods to make decisions about entering a trade, exiting, stop losses, trail stops or projecting profit targets.

PUSH THE LIMITS OF YOUR LEARNING CURVE

The trading learning curve is like that of any other discipline. A neurosurgeon, an engineer or a teacher are continuously faced with new problems which are similar but not exactly identical to those previously encountered. In order to acquire consistently positive results, these professionals must repeatedly analyze problems from their past which will help them with those of the present. Would you allow your child to have surgery performed by an intern, or would you rather it was performed by the chief surgeon? No physician would dare to operate alone after just a couple of weeks, months or even five years of learning the surgical techniques!

We cannot emphasize enough that chart interpretation and the wisdom of technical market behaviour cannot be learned overnight. This being said, we shouldn't be surprised that many of the 'wannabe' traders lose money and disappear after a couple of months. The richer the storehouse of experience, the more efficient the problem analysis will be. As a consequence, the consistency will improve and the trading results will ameliorate. However, most novice traders jump the gun and start trading after only a couple of months, if not weeks. Their thinking probably goes along the lines of, 'Even a stopped clock is right . . . twice a day!'

OMISSION AND INACTION

I couldn't proceed further with this process of imparting trading knowledge without mentioning the work of Jonathan Baron (http://www.sas.upenn.edu/~baron/), a 61-year-old psychology professor at the University of Pennsylvania. He has dedicated many years of his life to the study of judgement and decision-making, which he has described in wonderful detail in his latest book, *Thinking and Deciding*.

Knowing at least a bit about the omission phenomenon, coupled with inaction and decision-making processes, will greatly enhance our trading performance (see Chapter 19). Now, please don't get me wrong! My book is not about psychology even if, as a physician, I consider it is as important as food and shelter in the development of modern civilisation. This book is about short-term trading or, more specifically, about the pragmatic aspects of integrated pitchfork trading which will assist the novice trader in achieving a consistent performance.

NEVER AGAIN THE SNAKE OIL . . .

If the trader does not take the right approach to learning, not only could it cost him his shirt but he could be eliminated before he has had a chance to start making any money. After reading this book, common sense will dictate that you practise all the rules in order to get the most out of the charts.

- If you are a beginner, go to the web references listed below (we illustrate Dow Jones Cash Index and German Dax Cash Index URLs), and you'll find free delayed access for most of the securities:
  - http://www.futuresource.com/charts/charts.jsp?s=DJY
  - http://www.futuresource.com/charts/charts.jsp?s=DAXY
  - http://www.prorealtime.com
- We recommend the Advanced GET Charting, which is one of the most efficient, ergonomic and prolific charting tools available to the trader. We have been using it for years. You can take a 30-day free trial and see if the tool fits with your everyday practice: http://www.esignal.com
- Draw as many pitchforks as you can, especially in the pre-open. Become familiar with the intricacies of the pitchforks, rectangles, failures, and so on.

- Follow the charts during the day, simulating scenarios. Let the market come to you. Assess your post-market work and see if your judgements were good and, if not, why they failed.
- Discern whether there is some kind of correctable error in your judgement, a mistake in understanding the learning curve topics, or a sudden unexpected market condition.

More often than not, the novice traders do not focus on risk and money management as an essential part of their trading practice. This is due to greed and also to a poor understanding of the learning curve. As a first trading approach, their goal is to be right more than 50% of the time. However, trading is a business which is different to any other type of business. It is the only one where losing money is part of the way of life. The trader must understand the vital importance of the difference between losing tiny bits on average and consistently winning. Once you have learned how to lose these tiny bits, then and only then will you really start making money!

WHY A BOOK ON INTEGRATED PITCHFORK ANALYSIS?

As mentioned above, common sense encourages us to acquire a consistent technique that will give us confidence. Once you have decided to enter the highly competitive field of trading, you will quickly realize that this immense field can never be totally mastered. But one question arises: 'Do we really need to know all these topics?' The answer is, of course, 'No!'

The essence of becoming a consistently-successful trader is to understand the overall context of the market, and specialize in one of the techniques that works for various markets in any kind of tendency: trending or non-trending. In your quest for the 'Holy Grail' technique, you should be aware that by learning and cruising along with the 'smart money' people, you will acquire an inexhaustible edge.

As we have previously stated (at www.pitchforktrader.com):

> *. . . You should realize that in 2005 a large portion of the Chicago Mercantile Exchange (CME) floor traders and Chicago Board of Trade (CBOT) floor traders specialized in practising the pitchfork technique. They rely on it as part of their trading arsenal, in an off-floor environment. Our colleague, Timothy Morge, from www.medianline.com, conducted these professional and high quality exchange-sponsored seminars. We have for him, the deepest admiration and gratitude. We consider him, not only a master trader, but also a great teacher that has massively contributed to the development of the hyper-specialized field of pitchfork analysis, originated more than three quarters of a century ago and then continued by the late Dr. Alan H. Andrews, since the early 1960s.*
>
> *So . . . sit down and think for a moment . . . if these people having the opulence of the smart money, who are using the best trading techniques that money can buy, are learning the pitchfork technique, what does it mean? Do they know something that the novices or the non-consistent traders ignore? The answer is a big 'Yes'.*
>
> *They are convinced that the pitchfork technique should belong to their trading arsenal, because they have seen it at work . . . and it works. It is one of the best ways to consistency . . . so they adopted it. While the crowd is still far behind . . .*

As we all know, the market price evolves in a *time–price* virtual space. In order to be consistent, both parameters should be taken into consideration. More often than not, traders do not apply time—price related techniques, using only price-related ones. It is also true to say that there are not many techniques around capable of using the time—price intricacy.

The potential technique should be tested, valued and reliable for both the trending market and for the sideways market.

The last, and probably the most important, parameters in choosing the most symbiotic and consistent technique are its sensitiveness and its feature applicability towards an ergonomic and profitable employment of risk control and money management.

Vocabulary Warning: We would like to warn the novice trader about some aspects of employing the right trading words. Most of the charting programs, which plot the ratios, are not limited to Fibonacci ratio applications only. When the Fibonacci ratio icon is clicked, the program calculates and plots whatever the value of ratio is entered, without any concern abut who invented it. Therefore we will follow the same procedure and use only the words Fibs or Fibonacci (ratios), whatever the name of the inventor. For accuracy's sake, the possible choices are listed below:

- Fibonacci ratios: 0.146, 0.236, 0.382, 0.500, 0.618, 0.786, 0.886, 1.000, 1.618, 2.618, 4.25 and 6.85.
- Dow ratios: 0.333 and 0.666; also their halves.
- Gann ratios: 0.25, 0.50, 0.75 and 1.00; also their halves and eighths.

EPISTEMOLOGY . . . ALWAYS HAS THE LAST WORD!

Even if you are lucky and have discovered the most consistent and symbiotic technique, there remains the problem of assimilating and practising it.

Epistemology is the science of learning, building knowledge from the basement, and understanding its limits and its validity. We will try to make full use of it throughout the entire book.

The method of building knowledge blocks (modules) is used in all the books in such a way that the information is assimilated very easily, and then it is put together for immediate memory retention and applicability. The methodology used to explain the concepts is simplified in such a way that the novice can quickly understand it without any prior knowledge.

The intermediate level trader might want to skip the beginning chapters (see Contents), advancing directly to the more complex topics.

CONCLUSION

After several years of hard work, I have decided to share our research with trading colleagues, at a very reasonable price compared with other trading techniques available on the market. My educational background and professional ethics do not allow me to publish unreliable or inconsistent information. I know the affection that an author has for his or her work, but in my case I have tried to do my best, as objectively as possible, in the name of advancing the science of technical analysis.

I firmly believe that Integrated Pitchfork Analysis is one of the most reliable and consistent techniques. It harmoniously respects and is guided by the four principles listed below:

- The edge of learning and practicing along with the 'smart money' techniques.
- Learning to navigate in the time—price virtual space of the contextual market, enclosing the local market flow.

- The diversified efficiency in the various trending and sideways markets.
- And finally, the ergonomic and profitable trading efficiency in synergy with risk control.

Dr Mircea Dologa, MD, CTA
November, 2008
Paris, France
mircdologa@yahoo.com
Founder of www.pitchforktrader.com

Please read below the current disclaimer that the Federal Trade Commission (FTC) has proposed must be prominently displayed by anyone offering an investment course to the public.

Disclaimer

The purpose of this material is to provide you with a very powerful trading technique, named 'Integrated Pitchfork Analysis', a valuable tool in the financial markets. The text, the chart examples, or any part of this material are not to be taken as 'investment advice'. They are purely and strictly for educational purposes. Ultimately, you are responsible for all of your investment decisions. The data used in this material is believed to be from reliable sources but cannot be guaranteed.

There is no guarantee that this tool will continue to work in the future. 'Past performance is not indicative of future results'. You should understand that there is considerable risk of loss in the stock, futures or options markets. Neither the author, nor anyone else involved in the production of this material, will be liable for any loss, damage or liability directly or indirectly caused by the usage of this material.

Prelude

HOMEWORK FOR THE READER: SPOTTING AND MANAGING A TRADE

0.1 Homework Instructions

In order to evaluate the reader's knowledge in comparison with that of the book's presentation we will assign in this section some homework for the reader, using the first three charts (Figs 0.1, 0.2 and 0.3). Your learning task is to study them carefully and try to find the best low-risk high-probability trading opportunity.

Figure 0.1 Homework chart: market under observation (Courtesy of www.pitchforktrader.com)

Figure 0.2 Homework chart: market under observation (cont.) (Courtesy of www.pitchforktrader.com)

Figure 0.3 Entire trade chart, including unmarked entry and exit (Courtesy of www.pitchforktrader.com)

Do it in writing and take your time to study this example. Use only your trading experience as a guide. If you encounter difficulties, it means that this book is for you and that you will improve your knowledge after you have read and assimilated the information in this book.

Very few people are at ease in front of a naked chart. So do not blame yourself for anything . . . just study it. It takes what it takes!

After the three assignment charts, we will present in detail which trade will represent the best low-risk high-probability opportunity. Please do not be tempted to jump the gun and go straight to the chart solution. It will not be in your interest!

We wish you good luck!

Do not go to the next page, unless you have finished the homework!

0.2 Homework Solutions

Figures 0.4–0.10 offer a concise presentation of the homework and reveal the logical mechanisms of spotting and managing a low-risk high-probability trade. The synopsis table and the new lessons from the trade's execution, located at the end of this chapter, complete the assignment.

Figure 0.4 will help you implement your valuable chart markings:

– down-sloping trend line;
– labelling of the most current move (ABC swing);
– applying Fibonacci tools to monitor the activity of the local market.

All these start to take away the emptiness and incomprehension of the naked chart and begin the development of a competitive edge.

Figure 0.4 Implementing chart markings (Courtesy of www.pitchforktrader.com)

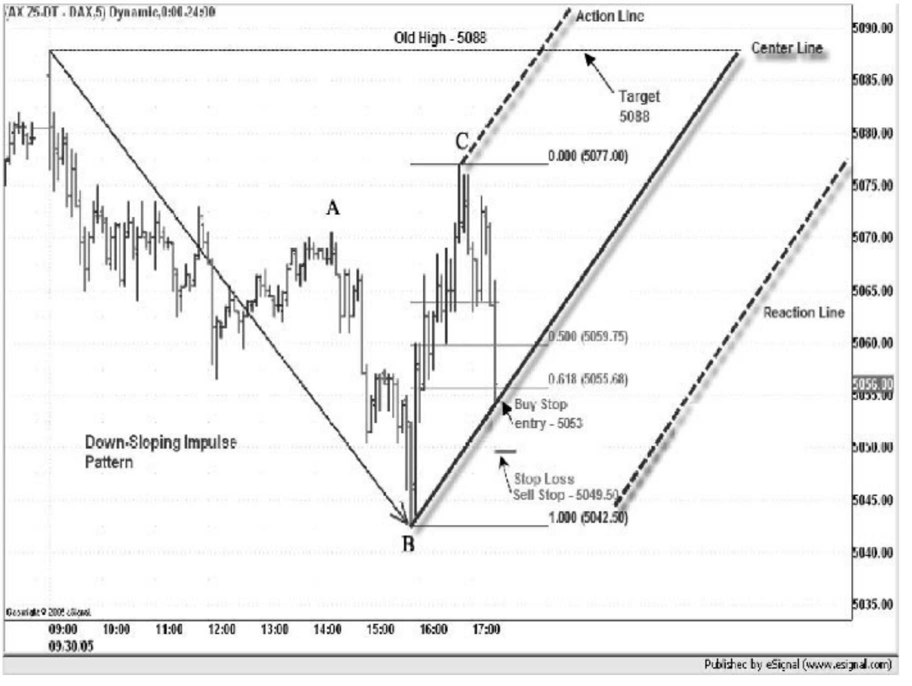

Figure 0.5 Local market movement (Courtesy of www.pitchforktrader.com)

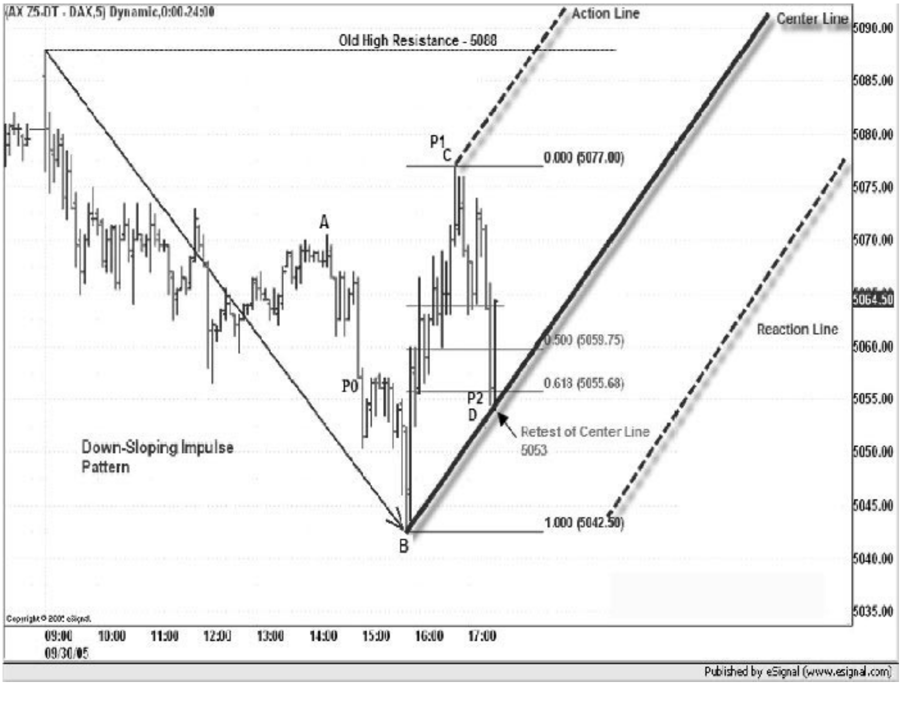

Figure 0.6 A retest starts the trade (Courtesy of www.pitchforktrader.com)

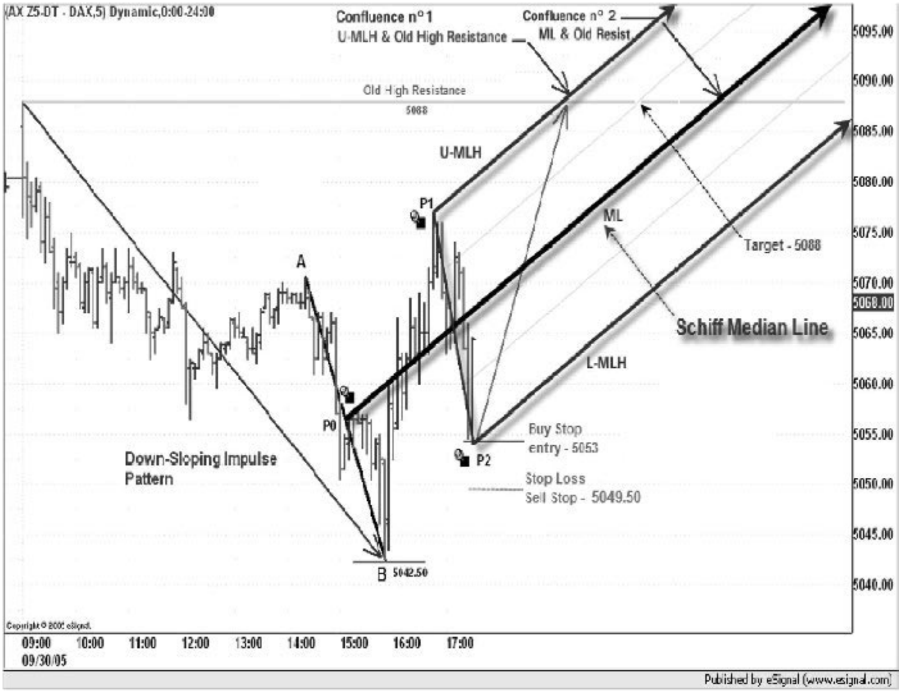

Figure 0.7 Replacing the A&R Lines with a Schiff median line (Courtesy of www.pitchforktrader.com)

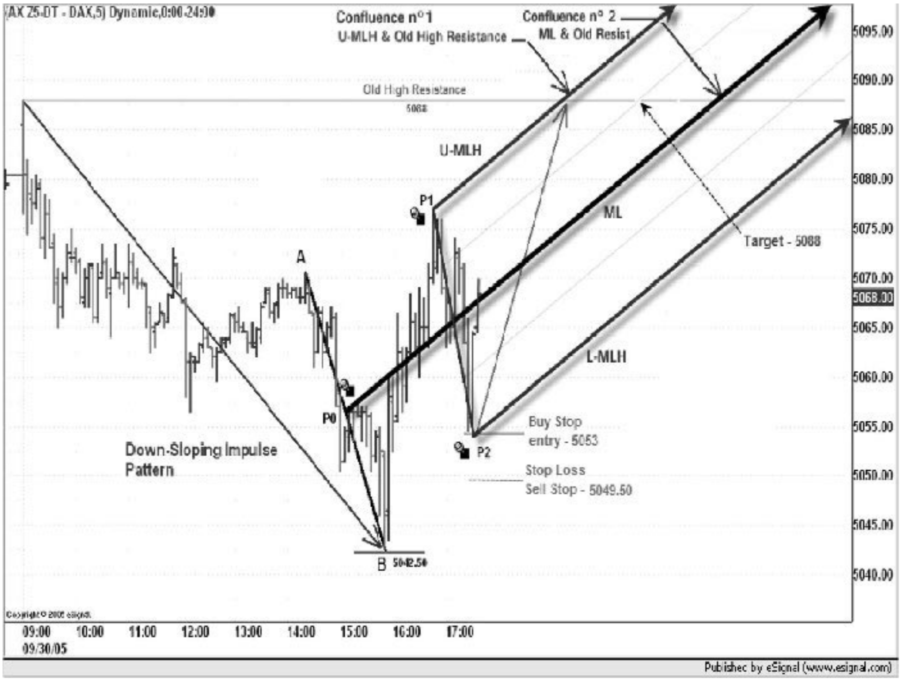

Figure 0.8 Schiff median line trade (Courtesy of www.pitchforktrader.com)

Figure 0.9 Schiff median line trade (cont.) (Courtesy of www.pitchforktrader.com)

Figure 0.10 Reaching the logical profit objective (Courtesy of www.pitchforktrader.com)

The corrective moves of the local market (Fig. 0.5) should encourage you to do the following:

- Construct the Action and ReAction Lines. This approach is dictated by the attainment of the 61.8% Fibonacci ratio retracement level and the absence of an efficient traditional pitchfork set-up (anchor and P1–P2 swing).
- Consider the eventuality of a test-and-retest trade applied to the Center Line.
- Implement the three-pawn technique: prearranged entry, initial stop loss an target.
- Decide on the most optimal money management strategy: R/R ratio, degree of the trade's probability, number of trading units and number of contracts per unit.

A retest of the Center Line starts the trade (Fig. 0.6), once the entry order has been executed.

Next (Fig. 0.7), replace the A&R Line with a more efficient contextual structure, the Schiff median line. Thus we can visualize and manage the trade better at this stage of its development and at this market price level.

Be ready to follow the rules: discipline and patience. The automatic control mode (refer to the Three Pawn Technique) of the trade will bring you to either the target or to the planned stop loss (Fig. 0.8). The dice have already been thrown . . .! You cannot lose more than the already-planned and psychologically-accepted amount.

Follow closely the hard-earned money through the trailing process, break-even set-up (right after the market advanced one ATR move), trails nos1 and 2, both snugged under the last low of the swing (Fig. 0.9).

The logical profit objective has been attained and the trade terminated (Fig. 0.10). None of the four trailing stops were used. Proceed to the conclusion of the trade, including the trader's journal (refer to Table 0.1: Trade Synopsis Table below).

Table 0.1 Trade synopsis table

Trade Synopsis Table

Test and Retest of the *Center Line* Technique

1	Spotting the Trade	**Test-and-Retest of the Center Line**
2	Finding the Optimal Set-up	**5-min time frame chart**
3	Time Frame Alignment	**Upper Time Frame aligned upwards**
4	Three Pawn Technique *(long trade)*	**Entry - *buy stop* - 5053** **Stop Loss - *sell stop* - 5049.50** **Logical Profit Objective - *sell stop* - 5088** **Money Management:** Risk - 3.5 pts Reward - 35 pts R/R ratio - 10
5	Profit & Loss Statement	Trading units - 3 Break-even - 5053 Trailing stops - 4 Exit - targeted out 5088 P/L - 105 pts/contract (3x35) - 2625 euros ($3333) Time spent in trade - from day's afternoon until the next day's morning
6	Trader's Journal	**New lessons out of this trade:** Energy building rectangles Trailing relay locations Secret revelation of the Market Direction

Figure 0.11 Formation of a narrow consolidation (Courtesy of www.pitchforktrader.com)

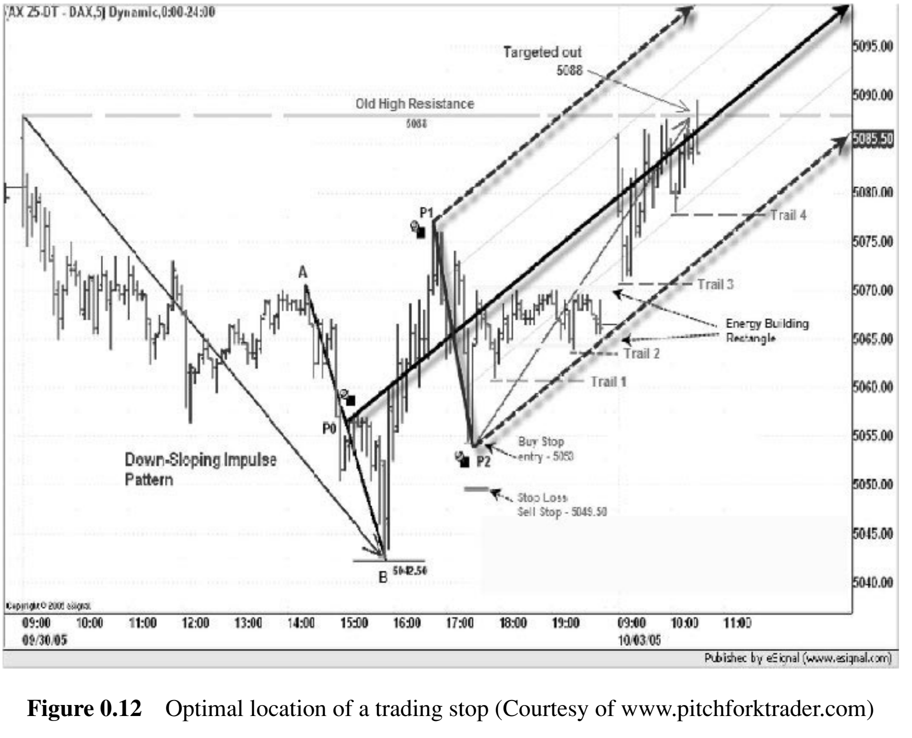

Figure 0.12 Optimal location of a trading stop (Courtesy of www.pitchforktrader.com)

Figure 0.13 Revealing the future direction of the market flow (Courtesy of www.pitchforktrader.com)

0.3 Trader's Journal: New Lessons out of This Trade

As always, don't neglect the importance of writing down your thoughts for later use!

Detect any energy-building rectangles that could be the foundation of a future trend. Observe carefully in Fig. 0.11 the formation over several hours of a narrow consolidation. The lower boundary is often used as the trailing stop's most trusted location. Whatever the case will be, be prepared for a next day exploding momentum.

The outburst of restored energy within the rectangle projects the market price to several times its initial height (Fig. 0.12). The trusted location of the trailing stop is once more confirmed: the upper/lower boundaries of the energy-building rectangle, right under the low of the up-swings.

The up-sloping trend line located between trail nos 1 and 2 (Fig. 0.13) is worth a thousand words. It will reveal the future direction of the encapsulated market flow energy and offer the trader a hidden competitive edge.