TACTICAL INDICATOR CUP AND HANDLE PATTERN

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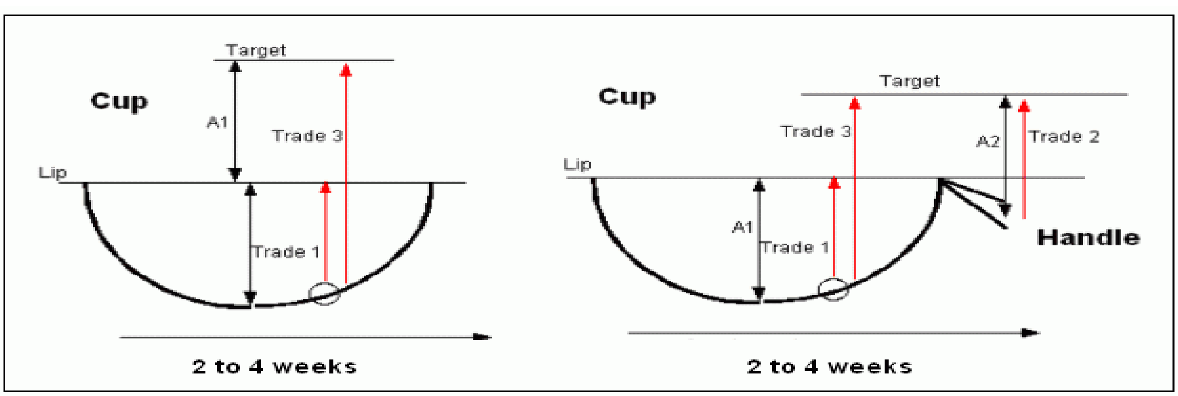
In recent weeks we have seen many new readers come on board and they have generated a demand for background notes on the indicators we mention in the newsletter and the essential tools of technical analysis. These summaries are designed to explain how various indicators are applied to trading opportunities. The notes include tactics and rules for using and applying or constructing each indicator. The notes finish with a summary of the advantages and disadvantages of each indicator. These notes describe the way we use these indicators in our trading and are designed as a short reference guide.

INDICATOR – CUP AND HANDLE PATTERN

This is a short term pattern that develops over 2 to 4 weeks. It may be a downtrend breakout, or occur within an existing uptrend. The cup is usually symmetrical but it may be asymmetrical. Symmetrical saucer curves are defined using a single curve tool. Use the GTE saucer tool. Asymmetrical saucers are defined using a combination of parabolic curve segments. Use the GTE parabolic tool.

APPLICATION

The cup offers similar trading opportunities to that of the saucer pattern. The projection targets are based on a breakout from the lip of the cup. Generally the cup pattern is sharper and deeper than the saucer. The combination cup and handle pattern is a stronger pattern. This applies to the pattern of price behaviour following a failed breakout at the end of a cup pattern. Prices move to the right of the cup line, and then decline. This pullback may also appear within a few days after a successful breakout above the lip of the cup. The decline is 'flag-like' and is defined with two parallel lines. Use the GTE Parallel line tool. This is the handle. Prices then break above the upper edge of the handle and the uptrend resumes. These are breakouts from short term patterns lasting 2 to 4 weeks so the achievement of target objectives is usually rapid. The target price is based on projecting the height of the cup above the upper edge of the handle at the point at which the new breakout occurs. Use the GTE Price Range tool to reposition and recalculate the price target.



TACTICS

- Trade from the base of the cup to the lip.
- Trade the breakout from the lip to the projected targets.
- Trade from the breakout above the upper edge of the handle. This pattern is not traded in anticipation of a breakout.
- Target is the height of the cup, projected from the point of the breakout from the handle pattern.
- Management of the handle breakout trade uses tight stop loss conditions as the breakout is often rapid.
- Best applied with price leverage

RULES

- The cup must be validly defined
- The handle is defined by a straight edge trend line, and most effectively by an upper and lower trend line.
- The height of the cup from the base to the lip is measured. This height is then projected upwards to set a breakout price target.
- On the day of the breakout, the stop loss is the lowest low in the handle pattern.
- On the day after the breakout, the stop loss is the value of the handle at the point of the breakout.
- On subsequent days the stop loss is volatility based. Count Back Line or 2xATR are useful methods.
- Loss of momentum signals the end of the trend. This may occur before targets are reached.

ADVANTAGES

- Reliable targets based on projecting the height of the cup from the point of breakout from the handle.
- Upside projection targets are reliable, particularly if they match existing resistance levels.
- Better returns due to the depth of the cup pattern

DISADVANTAGES

- Requires close trade management
- Handles can collapse rapidly.