

The application of the three different moving averages provides an objective way to qualify short-term, intermediate, and long-term trends in any time frame as well as provide you a solid method for reentering positions, which are running powerfully in one direction. It is for these reasons I use these particular moving averages.

TREND REVERSAL INDEX

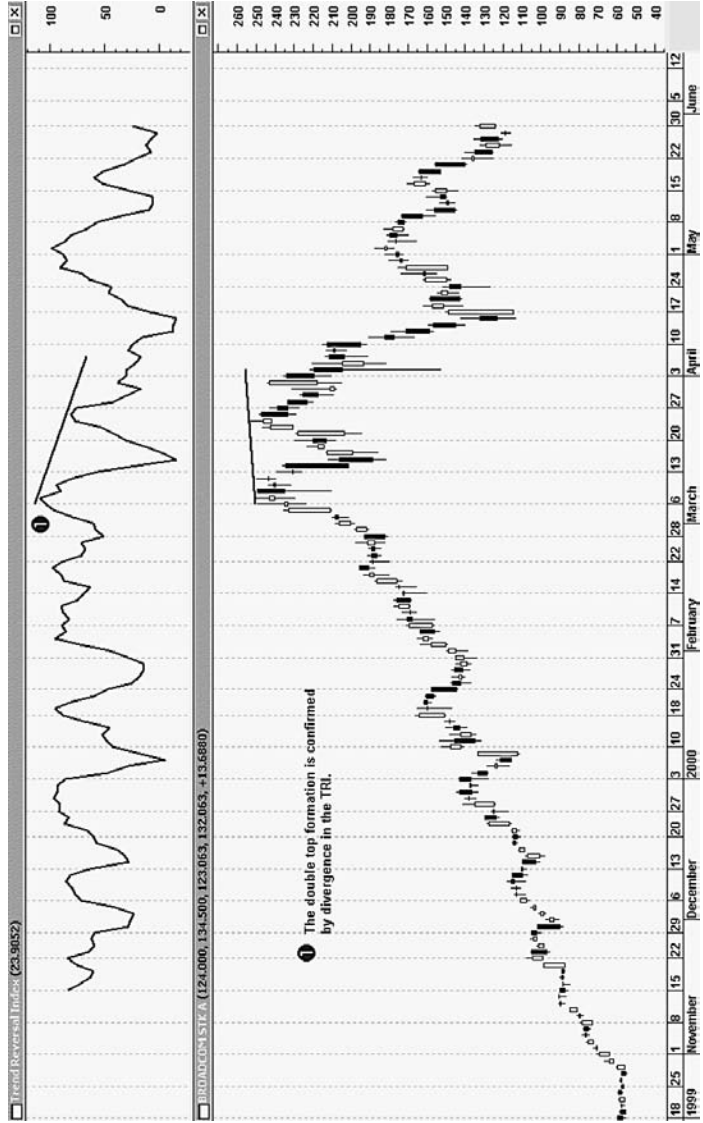
Over the course of this chapter, different indicators will be described, which accomplish a number of tasks, including determining relative overbought and oversold levels with a Detrended Oscillator; trend strength with a Vertical/Horizontal Filter; and 5-, 15-, and 39-period moving average to determine the different trends.

Perhaps the most powerful of all the ancillary indicators I use is the *Trend Reversal Index (TRI)*. The TRI shows divergence between the price of the underlying security and the investment vehicle itself. There are many divergence players out there; however the TRI was developed after numerous parameters were experimented with and tested; finally a 13-period RSI with a shorter 3-period RSI was incorporated. The creation of the TRI indicator would not have been possible without the help of the collective efforts of my trading team and numerous traders with whom I have worked over the years. Appendix C contains the custom formula for using the TRI in MetaStock. This section will illustrate the importance of the TRI in being able to confirm a reversal of trend, coupled with the arrival at a major inflection point in the market, as well as other tools in the One Shot – One Kill Method. The ability of the TRI to predict reversals in trend serves as a good confirmation tool. Once you have enough experience using it, you should become adept at spotting reversals without it.

Chart 2.3 shows how Broadcom is making a higher high while the TRI is making a lower high. This divergence between the price and the index is a very powerful indication that the recent runup in price does not carry with it the same degree of thrust as the first runup. If this second runup meets with resist-

CHART 2.3

The Trend Reversal Index (TRI) is a tool that can tip off reversals at key price levels. Broadcom attempts to retest its former highs, and the TRI shows us a significantly weaker level behind the respective move. This bearish divergence, when coupled with other indicators, is a good indication of a potential reversal.



ance at a key level (what's known as a *Fibonacci level of resistance*; see Chapter 4), and creates a divergence, there stands a very good possibility the trend will reverse. As you will see in Chapter 4, many different resistance points exist. However, having the TRI can act as the equalizer in attempting to ascertain which areas stand a better chance of serving as resistance.

The next example in Chart 2.4 shows a huge TRI buy signal generated when the market pulled back to an area of proven support. The Nasdaq 100 made a lower low, but the TRI made a higher low, causing the bullish divergence, which was quickly followed by a powerful rally. Many traders use divergences as a means of entering into positions. Traders look for divergence in stochastic, RSI, and oscillators as a means of spotting a weakening trend. It has been my experience that the TRI serves as a better filter than most of those conventional indicators.

Like any indicator in the One Shot – One Kill Method, the TRI is much more powerful when used with a combination of other indicators. For this reason, don't fall in love with one indicator, as using the TRI will tip you off to reversals in trend but the 15-period MA and Fibonacci Friends (I'll explain this term in Chapter 4) offer the means of entering the position.

TREND LINES AND TREND CHANNELS

Trend lines and *trend channels* are simple yet effective ways to not only gauge potential support or resistance but also to set profit objectives and even spot reversals. Being that the underlying premise of my method is to sell rallies in declining markets and buy weakness in climbing markets, trend lines and trend channels are another complimentary component in this effort. It is for these reasons that trend channels and trend lines are included as one of the indicators.

Much of the explanation that you will read in this book on trend lines was accomplished through a collaborative effort with one of my good friends and colleagues, Paul Ierna, a professional trader and hedge fund manager. It is important to keep in mind when looking at trend lines that it is the buyers who are in control of where the trend line is drawn in most cases. This doesn't