Head & Shoulders

Article

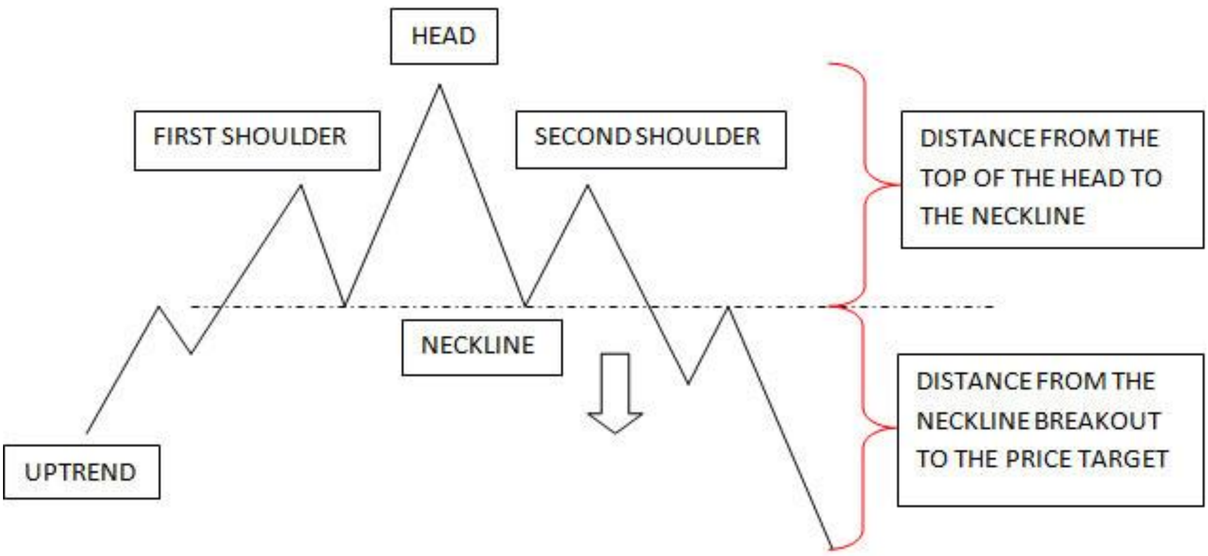
The Head and Shoulders pattern is regarded as the most reliable and well known trend reversal pattern. It consists of three well defined consecutive rallies, (two shoulders and one head) that occur at the end of an uptrend. All 3 rallies stop at the support line which is called the Neckline and connects the last 2 lows of the pattern. The two shoulders are usually of the same or similar length while the third peak (the head) is higher than the other two peaks.

The confirmed completion of the pattern occurs when two factors are filled: (a) there is a breakout of the neckline with the price moving below it and (b) the price closes below the neckline. It often happens that following the breakout, the price comes back to test the neckline again signalling to investors that this previous support is now a confirmed resistance. This test of the neckline is known as a throwback. However, there should be a degree of caution in cases where the price after the breakout moves considerably above the neckline again. This indicates that it might have been a false head and shoulders pattern and that the uptrend will most likely continue.

The same principles and characteristics apply to a Reverse Head and Shoulders pattern which occurs at the bottom of a downtrend instead.

Price Target: Following the breakout, the price target is approximately equal in amplitude to the distance between the top of the head and the neckline, and it is measured from the point at which the neckline is broken. Keep in mind that this is the minimum price target as prices can many times move well beyond that price objective.

Definition Chart Explaining Head & Shoulders



Real Time Chart that Includes Head & Shoulder

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