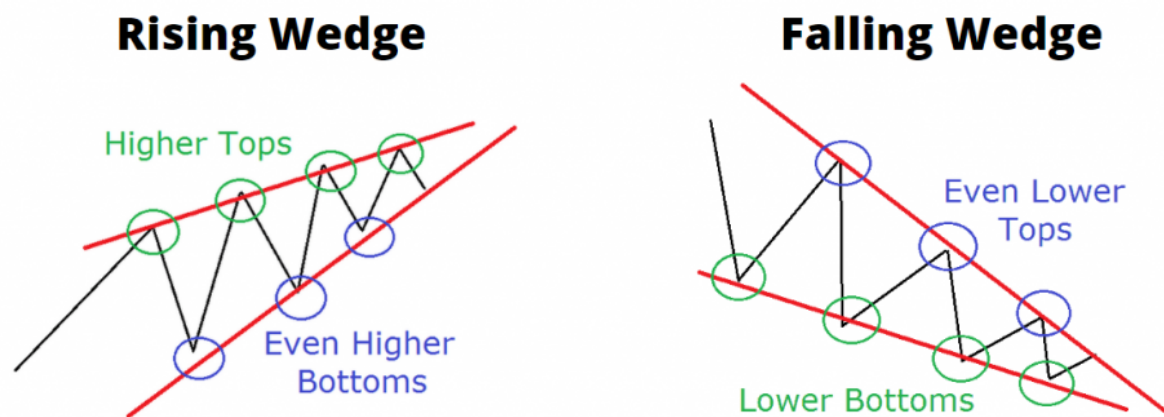


Rising and Falling Wedge Patterns: How to Trade Them

How To Trade Wedges



TradingSim
#1 MARKET REPLAY PLATFORM

Rising and falling wedges are a [technical chart pattern](#) used to predict trend continuations and trend reversals. In many cases, when the market is [trending](#), a wedge will develop on the chart. This wedge could be either rising or falling. Wedges can also appear at the end of a bullish or bearish trend. Thus, a wedge on the chart could have continuation or reversal characteristics depending on the trend direction and wedge type.

In this post, we'll uncover a few of the simplest ways to spot these patterns. Likewise, will give you the best way to predict the breakout and trade them.

What do rising and falling wedge patterns look like?

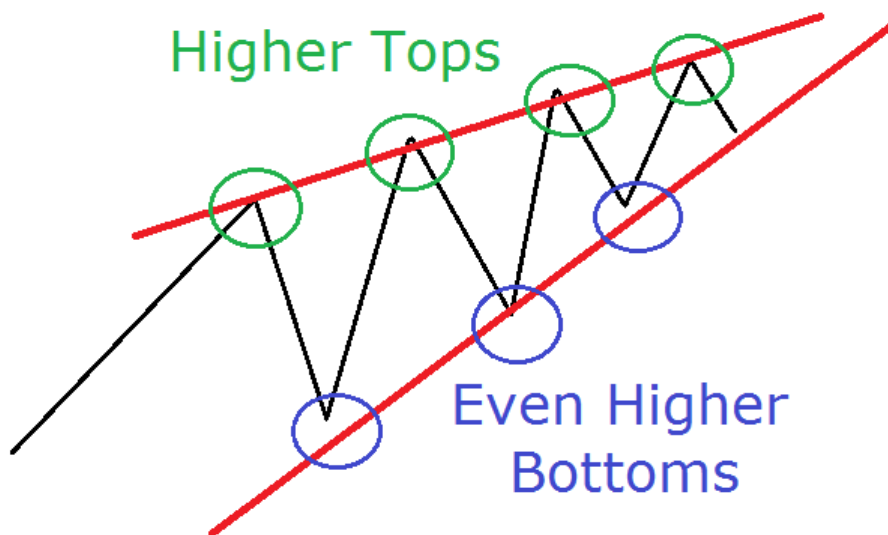
Although many newbie traders confuse wedges with triangles,

rising and falling wedge patterns are easily distinguishable from other chart patterns.

Rising Wedge

The rising wedge pattern develops when price records higher tops and even higher bottoms. Therefore, the wedge is like an ascending corridor, where the walls are narrowing until the lines finally connect at an apex.

The below image illustrates the rising wedge pattern formation:

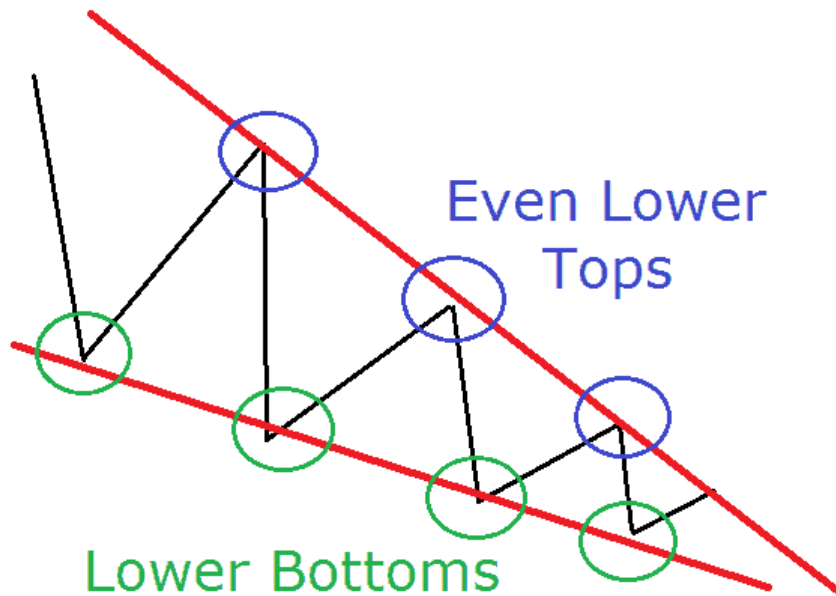


Rising Wedge

Note that the rising wedge pattern formation only signifies the *potential* for a bearish move. Depending on the previous market direction, this bearish movement could be either a trend continuation or a [reversal](#). In other words, during a rising wedge pattern, price is likely to break through the figure's lower level.

Falling Wedge

A falling wedge pattern is an exact mirror image of the rising wedge. A falling wedge pattern develops on the chart when there are lower bottoms and even lower tops:



Falling Wedge

As you can see, the bottoms are decreasing, but the tops are decreasing at a faster pace.

Opposite to rising wedge patterns, falling wedge patterns provide a bullish signal, which implies the price is likely to break through the upper line of the formation.

Predicting the potential breakout direction of the rising and falling wedge patterns

Again, rising and falling wedge patterns could result in a continuation or reversal. It all depends on the direction of the primary trend.

You may be thinking, “But how is it possible for a pattern to have two very different outcomes?”

The answer to this question lies within the events leading up to the formation of the wedge.

Trend Continuation

During a trend continuation, the wedge plays the role of a correction pattern on the chart. For example, imagine you have a bullish trend and suddenly a falling wedge pattern develops on the chart. **In this case, the wedge represents a correction.** Thus, we expect a price breakout from the wedge to the upside.

The same applies for rising wedge patterns. The difference is that rising wedge patterns should appear in the context of a bearish trend in order to signal a trend continuation. Ultimately, the price action will break to the downside.

Trend Continuation Chart Example

Take a quick look at the image below, which shows how wedges behave during a bullish market:



Rising and falling wedge continuation patterns

As you can see from this 10-minute chart of GM, it is in a strong uptrend, which is tested a total of 9-times.

There are two falling and two rising wedge patterns on the

chart.

As previously stated, during an uptrend, falling wedge patterns can indicate a potential increase, while rising wedge patterns can signal a potential decrease. **Notice that the two falling wedge patterns on the image develop after a price increase and they play the role of trend correction.**

Conversely, the two rising wedge patterns develop after a price increase as well, so they represent the exhaustion of the previous bullish move. As you see, after the two increases, the tops of the two rising wedge patterns look like a trend slowdown.

During a downtrend, we have the exact same scenario – price is likely to increase after a falling wedge pattern and price is likely to decrease after a rising wedge pattern. However, since the equity is moving downwards, our rising wedge pattern implies trend continuation and the falling wedge pattern – trend reversal. This is when the two types of wedges switch their roles. Yet, their behavior and potential remains the same.

Here is an example for your consideration:



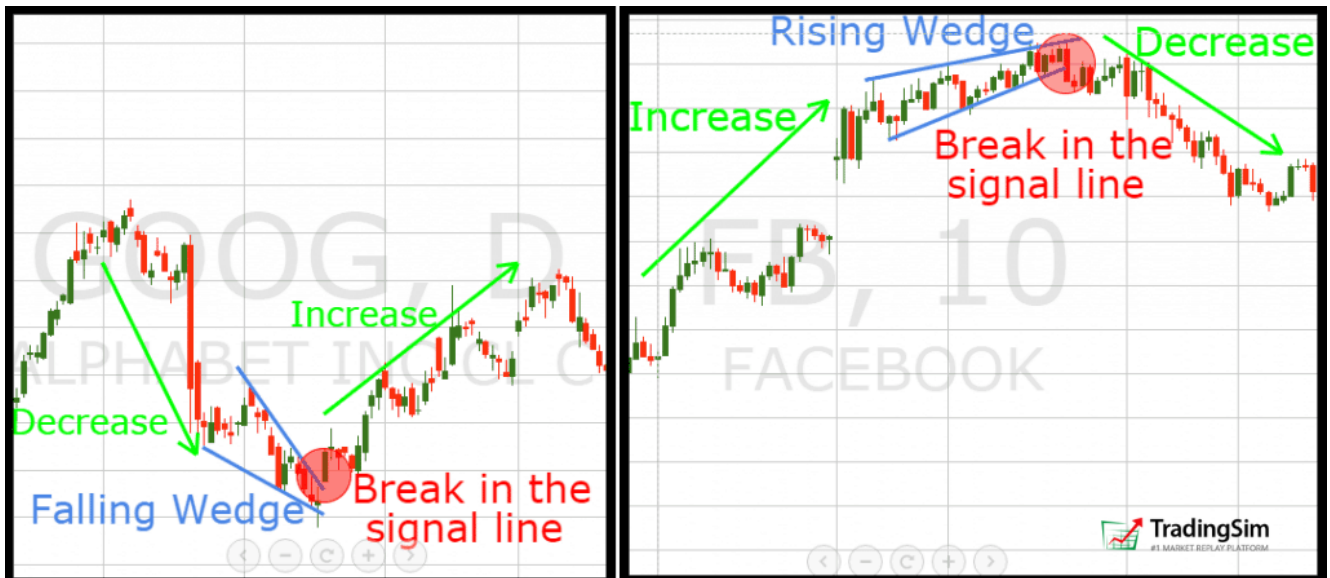
Rising wedges in a downtrend

Trend Reversal

In different cases, wedges play the role of a trend reversal pattern. In order to identify a trend reversal, you will want to look for trends that are experiencing a slowdown in the primary trend. This slowdown can often terminate with the development of a wedge pattern.

The best way to think about this is by imagining effort versus result. Before a trend changes, the effort to push the stock any higher or lower becomes thwarted. Thus you have a series of higher highs in an ascending wedge, but those highs are waning.

Trend Reversal Chart Example



Wedge Trend Reversal Pattern

Above is daily chart of Google and a 10-minute chart of Facebook showing the exact trigger for entering a position.

Note in these cases, the falling and the rising wedge patterns have a reversal characteristic. This is because in both cases the formations are in the direction of the trend, representing moves on their last leg.

How to trade rising and falling wedge patterns?

Every wedge has a signal line. Depending on the wedge type, the signal line is either the upper or the lower line of the pattern.

For example, if you have a rising wedge, the signal line is the lower level, which connects the bottoms of the wedge. If you have a falling wedge, the signal line is the upper level, which connects the formation's tops.

When you see a break in the signal line, you should enter the market in the direction of the break. For example, when you have a rising wedge, the signal line is the lower level of the figure. When you see the price of the equity breaking the wedge's lower level, you should go short. At the same time,

when you get a falling wedge, you should enter the market whenever the price breaks the upper level of the formation.

Where should you place your stop loss?

When trading a wedge, [stop loss orders](#) should be placed right above a rising wedge, or below a falling wedge. You do not want to make your stops too tightly as the price action will often violate one of the trend lines before rebounding swiftly. You will want to see a real break of significance to know you need to exit your position.

When should you take profits?

The potential price target of a wedge is equal to its size.

This means that if we have a rising wedge, we expect the market to drop an amount equal to the formation's size. If we have a falling wedge, the equity is expected to increase with the size of the formation.

Below you will see an image showing how to trade a rising and a falling wedge:



Wedge Trading Example

This is the 5-minute chart of JP Morgan. There are two wedges on the chart – a red rising wedge and a blue falling wedge. We enter these wedges with a short and a long position

respectively.

The overall JPM movement is bullish and the two wedges show a price cycle during a bullish trend:

- Price bounces from a trend
- Price starts hesitating and closes a rising wedge
- The wedge is broken and the price decreases into a falling wedge
- Price touches the trend and the falling wedge is broken in a bullish direction
- New bullish movement appears

The blue arrows next to the wedges show the size of each edge and the potential of each position. The green areas on the chart show the move we catch with our positions. The red areas show the amount we are willing to cover with our stop loss order.

In both cases, we enter the market after the wedges break through their respective trend lines.

These two positions would have generated a total profit of 80 cents per share by JPM.

How to practice rising and falling wedge patterns

The best place to practice any strategy is in a market simulator. We suggest flipping through as many charts of the more liquid names in the market. Get out your trend line tools and see how many rising and falling wedges you can spot. Draw them, and then make note of the price action on the breakout or breakdown.

While you do this, analyze the bigger picture context. For example, is the stock in an uptrend or downtrend? What do higher time frames like the 15m, 1hour, or daily chart look

like? Also, what does volume look like during the pattern?

Many times, you may find that volume recedes during bearish continuation wedges, while it may increase in bearish reversal wedges.

Over time you should develop a large subset of simulated trades to know your probabilities and criteria for success before you put real money to work.

We hope this helps, and here's a quick summary in parting:

- Wedges are technical analysis chart patterns.
- Wedges could be rising and falling.
- Rising wedge patterns usually imply an impending decrease in price.
- Falling wedge patterns usually imply an impending increase in price.
- Wedges could be trend confirming or trend reversing depending on the previous price movement.
- We should enter the market with the break through the signal line of the wedge.
- Stop loss orders should be placed above the rising wedge and below the falling wedges.
- We should aim for a target of a minimum amount equal to the size of the wedge.
- Even if the wedge is successfully completed, we should not close our position if the equity is still trending in our favor.