BASIC TECHNICAL ANALYSIS EBOOK

This e-book goes deeper in studying all the specific features of the technical analysis. From price patterns to different types of trends, these are the most common terms related to this school of analysis of the market. Keep reading to find out why technical analysis is still the focus of the investors' attention.

What is Technical Analysis

Technical analysis is a trading discipline that evaluates trading and investment opportunities by analyzing the statistical trends about the trading activity. This type of analysis focuses on the patterns of price movements, trading signals and other charting tools to determine the strengths and weaknesses of an asset.

What is so special about it? Well, it can be applied to any security - stocks, futures, commodities, currencies, and many others. However, it is most useful for commodities and forex markets, where traders focus on the short-term price movements.

Technical analysis attempts to forecast the price movement of any virtually tradable instrument that is subject to the influence of supply and demand. It is most commonly used to track the movement of the prices, but some apply it to other factors, such as volume or open interest figures.

Price Patterns

In technical analysis, the price patterns are signaling the transition between the rising and the falling trends. When a price pattern signals a change in the trend direction, it is a reversal pattern. When the trend continues in the same direction after a brief pause, it is known as the continuation pattern.

Reversal Patterns

These patterns are a sign of periods during which the bulls or the bears are reaching the end of their trending life. These reversals can happen on both market tops and bottoms. If they are on the market tops, those are known as the distribution patterns. On the other hand, if they happen on the market bottoms those are
accumulation patterns.

Continuation Patterns

These patterns are formed when there is a pause in the prevailing trend. For example, when the bulls are catching their breath during the uptrend, or the bears are relaxing during a downtrend. And while that pattern is forming, there is no way to know if the trend will continue or reverse. In this case, technical analysts recommend assuming the trend will continue, until proven otherwise.

Technical analysis works based on three main assumptions:

1. The market discounts everything

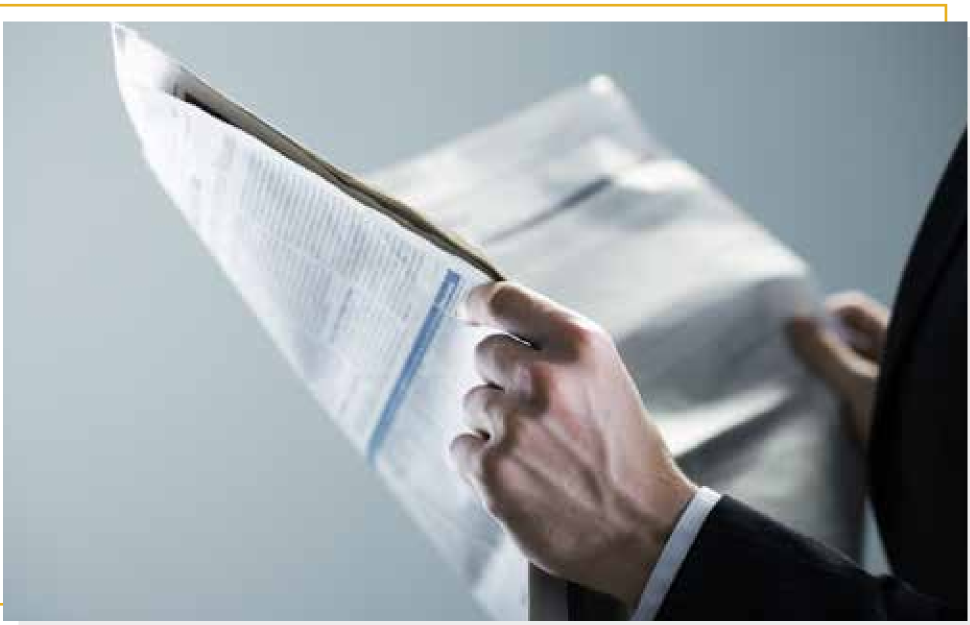
In other words, this analysis considers that majority of important things to know about a stock are already a part of it, so the deeper studying of it is not necessary. That's why this type of analysis is considered as simplifying - it rather focuses on the patterns than on a detailed study of something that is already seen and well-known.

2. Price moves in trends

This analysis is based on trends. It depends on them greatly, since they form patterns which are essential for its future studies. The focus is the short-term movements. In addition, the main principle is that the stock price will more likely stay the same than reverse drastically.

3. History repeats itself

A big part of the technical analysis is focused on the previous price movements on the market. In addition, the analysts believe that history helps to control emotions and reactions, thus contributing to better understanding of the market psychology.



Types of Trends

A trend is a general direction the market can take during a certain period of time. Trends can be both upward - when they are related to the bullish market, or downward - related to the bearish market. There is no specific amount of time during which something needs to sustain to become a trend. However, the longer it last, the more notable it is.

Trends are analyzed, too, just as the markets are. That process is used to predict the future movements and trends, how will they develop and how will they affect the market. And though this analysis applies a lot of data, that still doesn't guarantee the accuracy of the results.

These are the 3 common types of trends on the market:

Uptrend

The uptrend, or the upward trend, as it is otherwise known, is the price movement of a financial asset in the upward direction. It refers to a peak higher than the one that happened earlier in the trend.

What does it mean for the investors? Well first, it gives them the opportunity to profit from rising asset prices. Then, they can use the information about it to predict the reversal. It's quite simple when you look at it like that - when a price starts making lower swings, it means that a downtrend could be underway.

Downtrend

A downtrend happens when the price of an asset is lower for a longer period of time. It is the opposite of an uptrend. Typically, the investors aim to avoid downtrends since they decrease the value of an investment. A downtrend can last from a few minutes to a few years, so detecting it on time is quite important. When a downtrend is underway, the investors should avoid taking long positions.On the other hand, short sellers aim to take advantage of these times to earn a quick profit. They do so by borrowing and then immediately selling shares, under the agreement they will repurchase them in the future.

Sideways/Horizontal Trend

The sideways trend is a horizontal price movement that occurs when supply and demand are close to being equal. This usually happens during a long period of consolidation before the price continues to follow the existing trend, or before a new one is formed.

This type of trend is a result of the price traveling between strong levels of support and resistance. An important indicator of this trend is volume, which remains mostly flat by balancing both bulls and bears.

Support and Resistance

Support and resistance are two of the most often discussed attributes of the technical analysis. The terms are used to refer to price levels on charts that tend to act as barriers. If that happens, they are preventing the price of an asset to be pushed towards a certain direction.

The Importance of Support and Resistance

Support is a price level where a downtrend is expected to pause due to a concentration of demand. As the price drops, the level of demand goes up, and that's how the support line is formed. On the other hand, resistance is created when there is a sell-off due to increased prices.

This support line is quite important because it provides potential entry and exit points. When a price reaches this point of support or resistance, there are two possible options. Either it will bounce back, or it will continue in the same direction until the next support and resistance occur.

Key Facts About Support and Resistance

Technical analysis uses support and resistance levels to identify price points on a chart. This way, they can determine the probabilities for a pause, a reversal, or a prevailing trend. The key in this area is market psychology since the traders and the investors remember the past experiences and react accordingly.

Round Numbers

One of the most common features of support and resistance is that an asset's price has a difficult time moving beyond the round price level. That's why many inexperienced traders tend to buy or sell when that happens. Also, this is the reason why most target prices and stop orders by retail investors or large investment banks are at a round price.

Role Reversal

This is one of the most interesting phenomena that could happen with support and resistance. Namely, the price of the underlying asset breaks out and goes beyond the support and resistance levels. What happens next is, the expected role of support is switched with the resistance, assuming its new position.