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GF Markets Academy

Technical Analysis
For Beginners

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Introduction

Technical Analysis is using historic price movements, and market statistics to predict the future price. Traders believe that all available information are reflecting in the chart of an asset. Technical analysis tools include Moving averages, Fibonacci retracement levels, candlestick formations and other.

Chapter 1

Support and Resistance

- In a bull market or in an uptrend the support is the floor, and the resistance is the ceiling.
- When the price moves up to a higher high than before it creates a new resistance.
- Resistance is a signal, that a lot of traders will be selling at that point.

- The opposite is true during a downtrend or a bear market.
- When the price moves down to a lower lows than before it creates a new support.

Important entries and exits form support and resistance levels:

Trade the “Bounce”

- Buy when the price falls towards support.
- Sell when the price rises towards resistance.

Trade the “Break”

- Buy when the price breaks up through resistance.
- Sell when the price breaks down through support.

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Be aware of

- Sometimes it might look that the support or resistance level was broken. However, it might not be true because the market was just testing it to see how strong it is.

- The picture on the right resembles a test.

Following the trends

- Most experienced traders follow the trends and take trading opportunities in the direction the trend goes. Assume that you are holding a position in a stock for two months and you are expecting the value of the shares to increase.

- Let's imagine that you notice that the price fails to get above $177.50 several times over several months, even though it has gotten very close to moving above that level. In this case, traders would call the price level near $177.50 a level of resistance. This is something you will notice with practice and consistency.

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Chapter 2

Indicators

01 Moving Averages (SMA,EMA)

02 Oscillator

03 Moving Average Convergence Divergence (MACD)

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Moving average

- The moving average (MA) is a technical analysis tool that analysts and traders use to determine the price direction of a trend. It takes into consideration the average price by dividing the price of a specific period of time by the total price. The MA is calculated constantly in order to include the latest price fluctuations.

- Moreover, the MA is referred to as the lagging indicator because it marks the price movement of an underlying asset to produce a signal or show the direction of a given trend.

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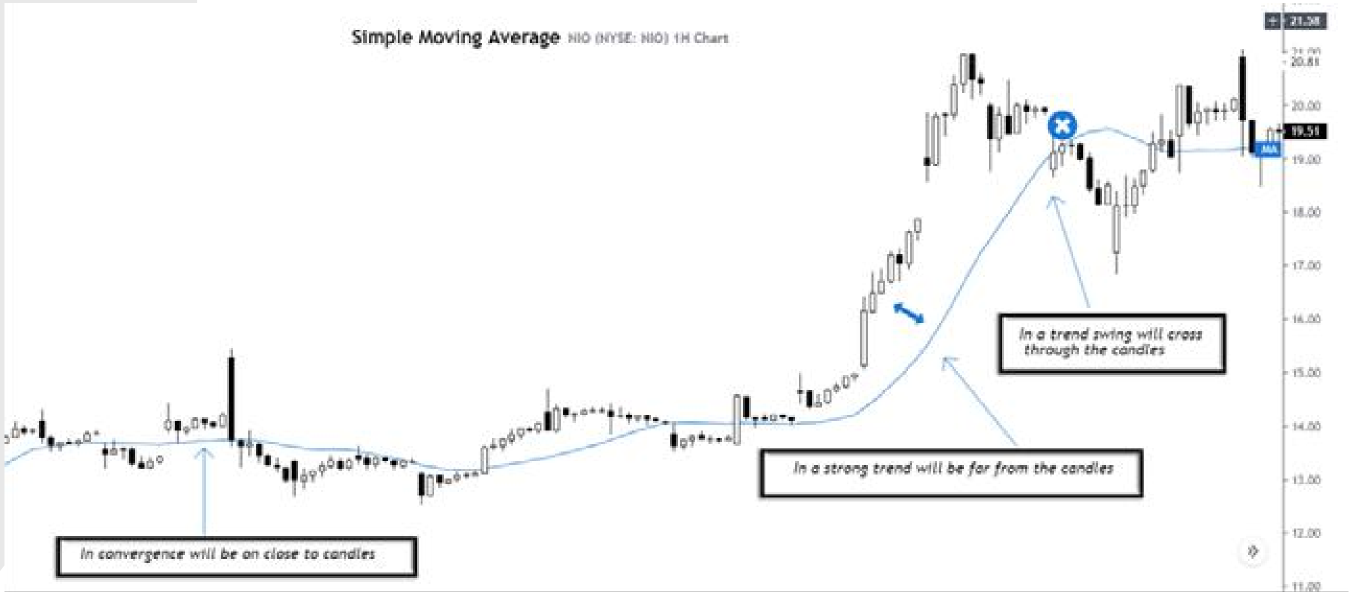
Simple Moving Average

- This is the most straightforward of the moving averages and is considering the recent data of price and divides them by the total data prices of an asset to find the average. Traders use it to identify potential entries or exits in the market. An SMA is a back looking tool and can be applied to past prices for a given period.

- The SMA helps to identify resistance and support levels or buy or sell signals in the market.



Exponential Moving Average

This is the most straightforward of the moving averages and is considering the recent data of price and divides them by the total data prices of an asset to find the average. Traders use it to identify potential entries or exits in the market. An SMA is a back looking tool and can be applied to past prices for a given period.

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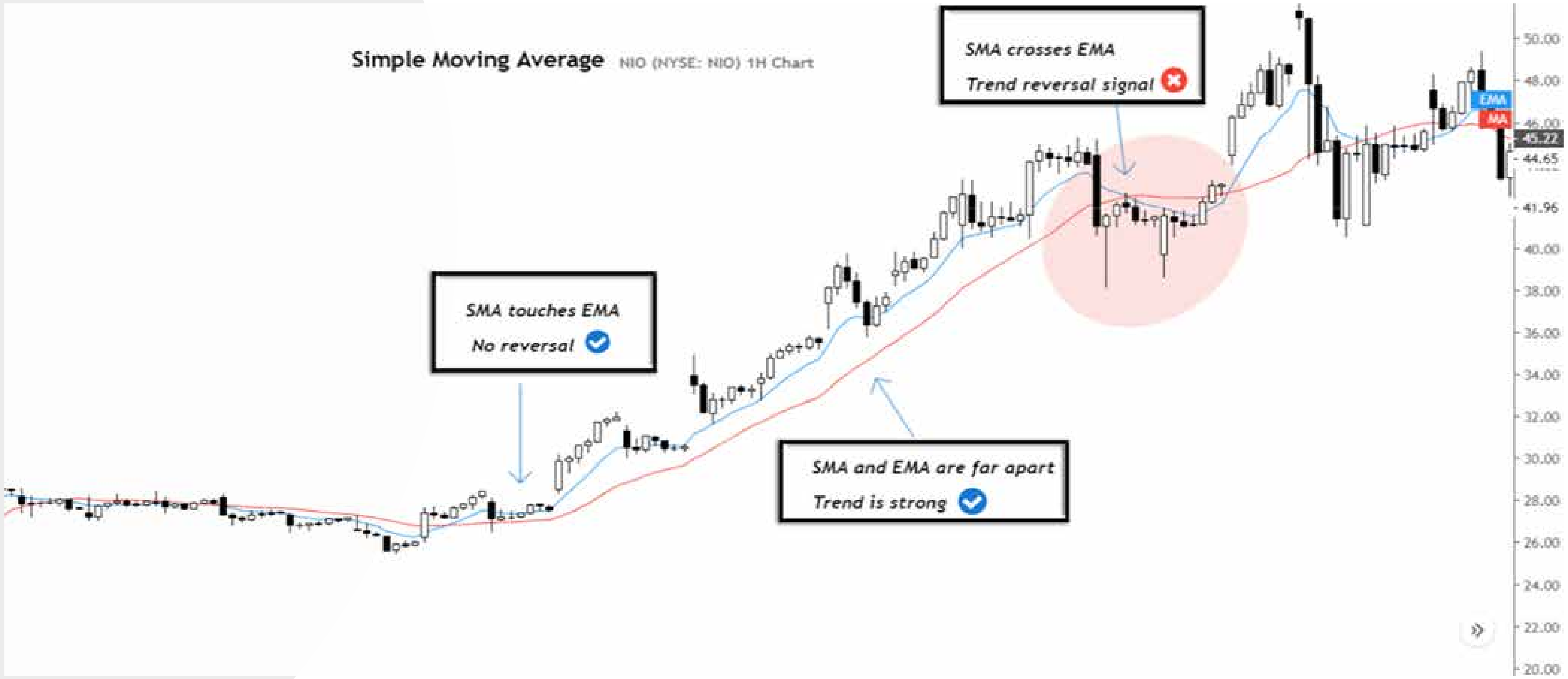

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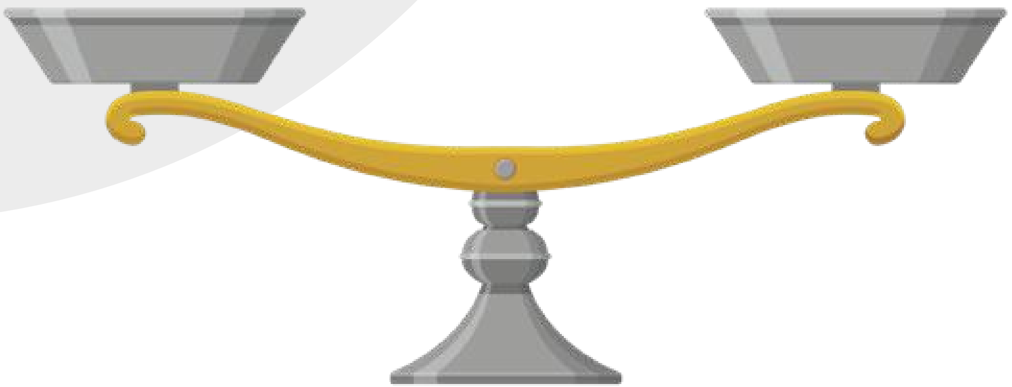
SMA or EMA?

The question is always which MA to use when trading. One of the differences, as has been said, is that the EMA gives weight to recent prices. The EMA is moving faster than the SMA, it will change direction faster, following the trend of recent prices. On the other hand, the SMA will need more time to recognize the changing trend.

However, this means that the EMA will be more outspoken in giving the wrong signals that may occur. It will show them too early, and the possibility of error occurs much faster. Thus, while the EMA immediately follows the reversal of the trend, the SMA moves more slowly. It means that the SMA lasts longer in the game, and this is significant, especially when there is a short-term unpredictable price movement.

In summary, EMA will react on time to trend changes but also a greater possibility of errors. SMA shows the changes much slower but less inaccurate signals during instability.



Three Trading Strategies with MA

01 The first one is called the "crossover" and is one of the main MA strategies. The first type is the price crossover. This is when a price crosses above or below a MA to indicate a potential change signal in the price trend.

02 The second one is called the "golden cross". It is identified when you use two moving averages to the chart. For example, one longer and one shorter. When the shorter MA crosses ABOVE the longer MA it indicates a buy signal.

03 The third one is called the "death cross". Again, when you use two MAs on the same chart one longer and one shorter. When the shorter MA crosses BELOW the longer MA it indicates a sell signal.

Stochastic Oscillator

The stochastic oscillator shows a comparison between the closing price of a stock and a series of prices of that same stock over time. It is an indicator that tends to oscillate around the average price level. The reason for this is a whole range of stock prices that affect it. Traders use it to determine signals that indicate overbought and oversold positions. Its characteristic is a high level of prediction of whether it is time to buy or sell and has high accuracy. It uses a range of values from 0 to 100.

Stochastic Oscillator

When observing the graph, you can notice the K line moves faster than the D line. The investor watches the lines move. In doing so, one should observe how the price and the D line move and monitor their changes. In other words, whether they move into overbought or oversold zones. If they are moving in the overbought zone (above 80), the trader should consider selling. If they are moving in the oversold zone (a level below 20), he should consider buying.

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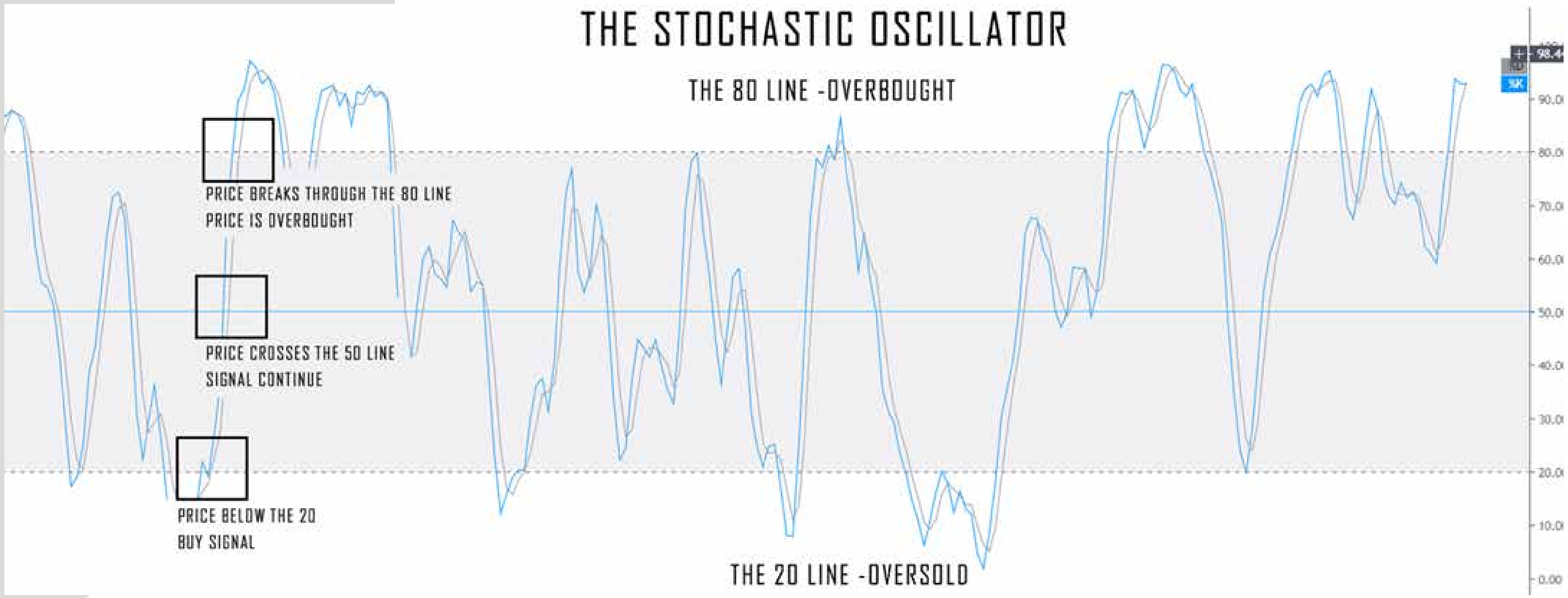
Stochastic Oscillator

One of the disadvantages of this oscillator is the possibility of false signals. It is the case when the share price does not follow the movement of the indicator. More precisely, the indicator gives a different signal from the price movement. It can especially happen during unstable market conditions. The way to overcome this is to take into account the price trend. It is then a confirmation of the signal given by the indicator, in other words, when the price trend is aligned and in the same direction as the signals.



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Moving Average Convergence Divergence

It is a technical tool developed in the '70s by Gerard Appel. His aim was to compare two exponential moving averages to chart momentum by measuring the relationship between them. Today It is one of the most effective and simplest momentum indicators available and used by analysts and traders.

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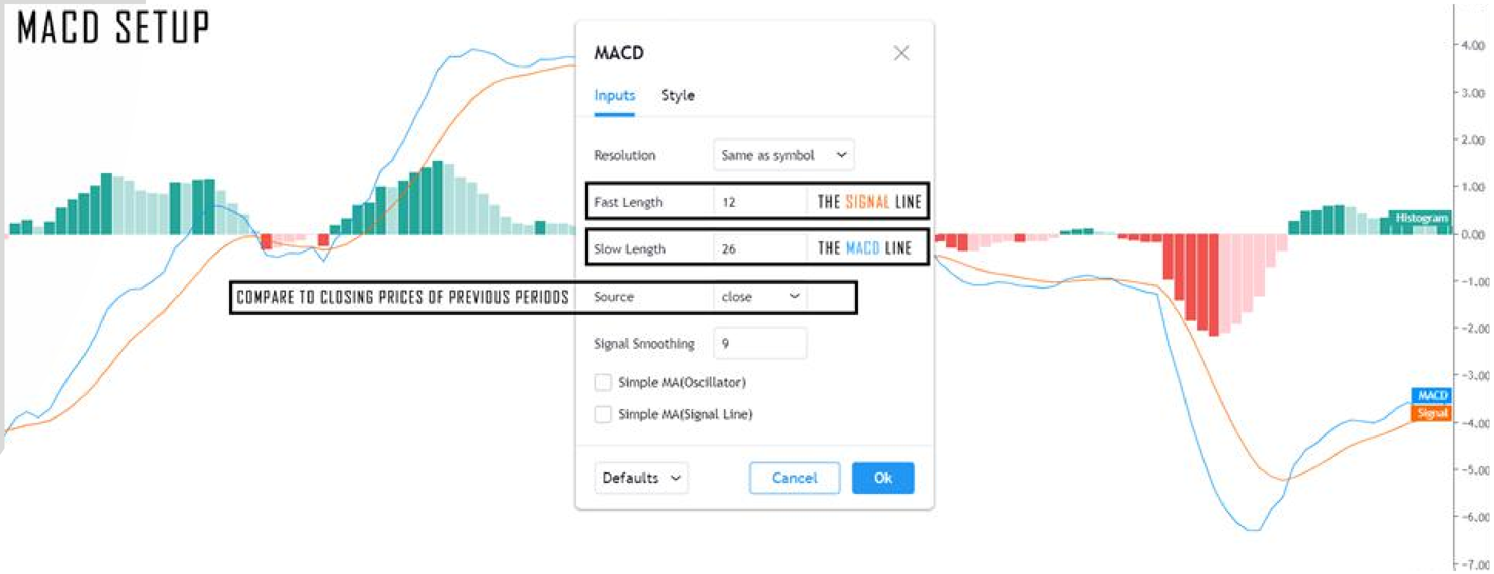
MACD Setup

The MACD indicator is consisting of two moving averages(lines), the MACD and the signal line. It is used by traders and analysts to spot buy and sell signals in an asset. In addition, it can determine whether a stock price is considered to be overbought (expensive) or oversold (cheap).   The one line needs to be longer and the other one shorter in order for the MACD to subtract the longer from the shorter one. Is worth noting that both lines are exponential moving averages lines. The shorter EMA is always converging toward or diverge away from the longer EMA.



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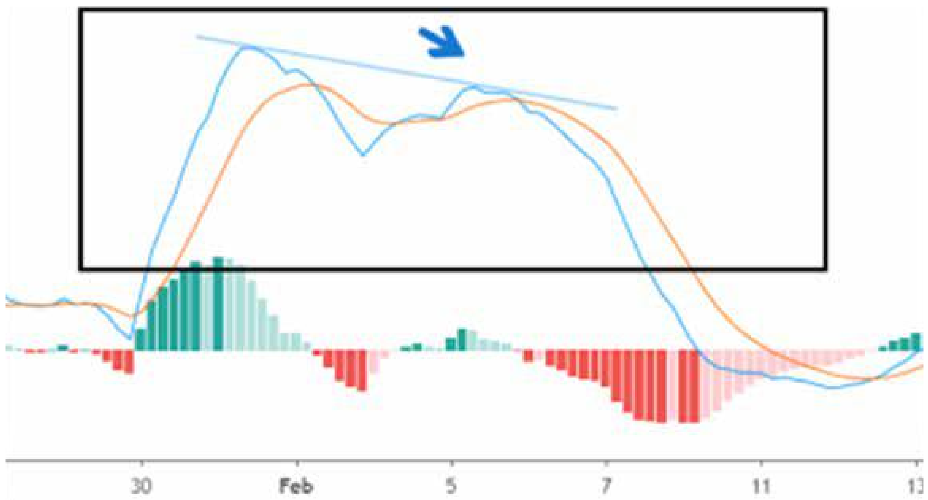
What is Divergence?

When the MACD is in a position so that the prices formed are different from the corresponding lowest and highest prices, it is a matter of divergence.

Bullish Divergence

When the MACD makes two rising lows that correspond to two falling lows, then it is bullish divergence. That would be a relevant bullish signal in the case of a long-term trend that is still positive. It is considered a reliable technique.

Bullish Divergence

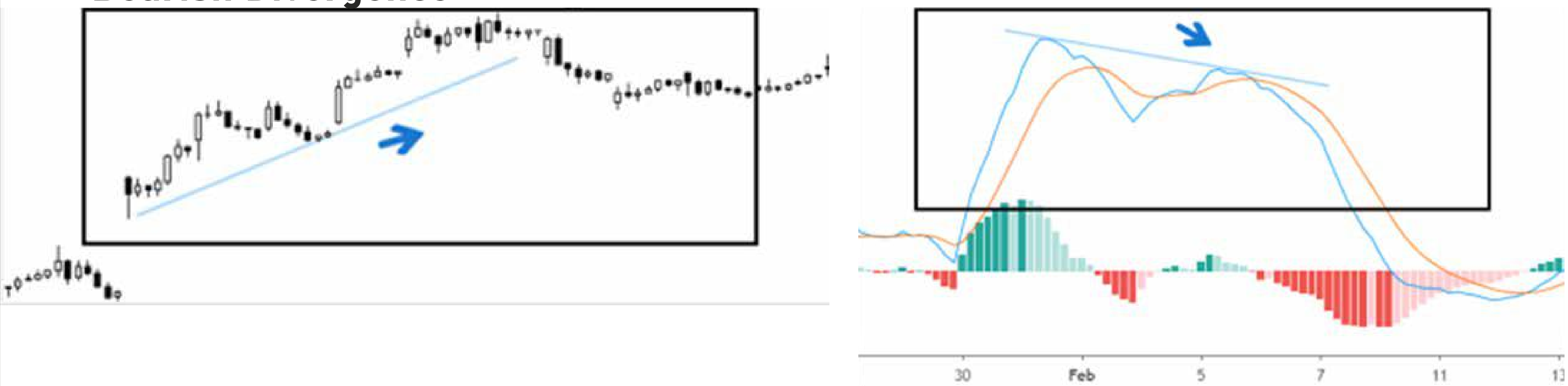


Bearish Divergence

Again, on the contrary, when MACD makes two falling highs that correspond to two rising highs, it is, you quessed it, a bearish divergence.

This divergence that occurs during the long-term bearish movement is a reliable confirmation that the bearish trend will continue.

Bearish Divergence



Understanding of Extremes

01 When the MACD line is far way below the zero line let's say in a very negative point, the MACD translates that the price of the security is oversold/very cheap. This will suggest a buy signal since investors and traders are always looking to buy oversold securities that can potentially reach a higher price than the current.

02 On the other hand, when the MACD line is well above the zero line in a very positive spot, the MACD line translates that the price of the security is relatively overbought/ very expensive. When this happens, it suggests a sell signal since investors and traders find the price more expensive than it should be.

03 Now assume that both the MACD line and the signal line are sitting on the zero-line suggesting the security is expensive. Compared to the extreme cases we saw above; this is not a situation where the security is extremely overbought.

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Limitation

- As most of the technical tools used for chart analysis, the MACD indicator should not be used alone. Instead, it should be used in combination with other indicators or technical tools to form a more accurate and not confusing market opinion and therefore investment decision. Can it go wrong?
- The weakness of this indicator is false signals, as well as insufficiently reliable signals. Signals of a possible reversal may occur, but not a real one. It is the so-called false positive.

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Always Trade Smart

GF Markets is created by traders with years in the industry. Our mission is to provide an accessible and intuitive way for traders of all levels to invest.

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