

GF Markets Academy

Fibonacci Retracements



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What is Fibonacci Retracements Trading

- Fibonacci Retracement is a method of technical analysis for determining support and resistance levels.
- It is named after the Fibonacci sequence of numbers, whose ratios provide price levels to which markets tend to retrace a portion of a move, before a trend continues in the original direction.



What are Fibonacci Retracement Levels

- Fib retracement levels are horizontal lines that indicate support and resistance in a trend.
- The Fibonacci retracement levels are 23.6%, 38.2%, 61.8%, and 78.6% and show how much of a prior move the price has retraced.



Support level

Consider the support level as a floor that when the price passes above it or breaks it becomes the new resistance level. Likewise, consider the resistance level as the ceiling where the price is trying to breakthrough. When it does break through it becomes the new support level and vice versa.

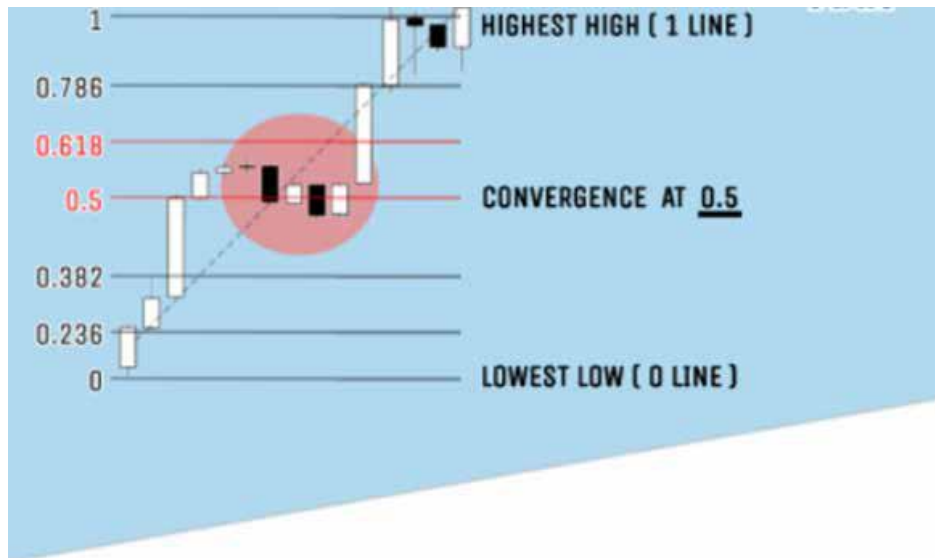


Importance of Fibonacci Retracement Levels

Fib retracement levels can be used for quite a few things. It can be used for identifying a stop-loss order, an entry price or to set price targets. For instance, when a trader sees a stock moving up and the price increases, it retraces to 61.8%. Once it moved up to this level it will move up again. Since the bounce occurred on an uptrend on the Fib retracement levels, the trader confirms a buy position. The trader might also decide to place a stop-loss order at 61.8%. If the price goes below the level, it means that the rally failed.



How to Place Fibonacci Retracement Levels



FIBONACCI RETRACEMENT LEVEL - BUY

I STRECH FIBONACCI FROM LOWEST LOW TO HIGHEST HIGH

II KEEP AN EYE ON MOST IMPORTANT LEVELS : 0.5, 0.618

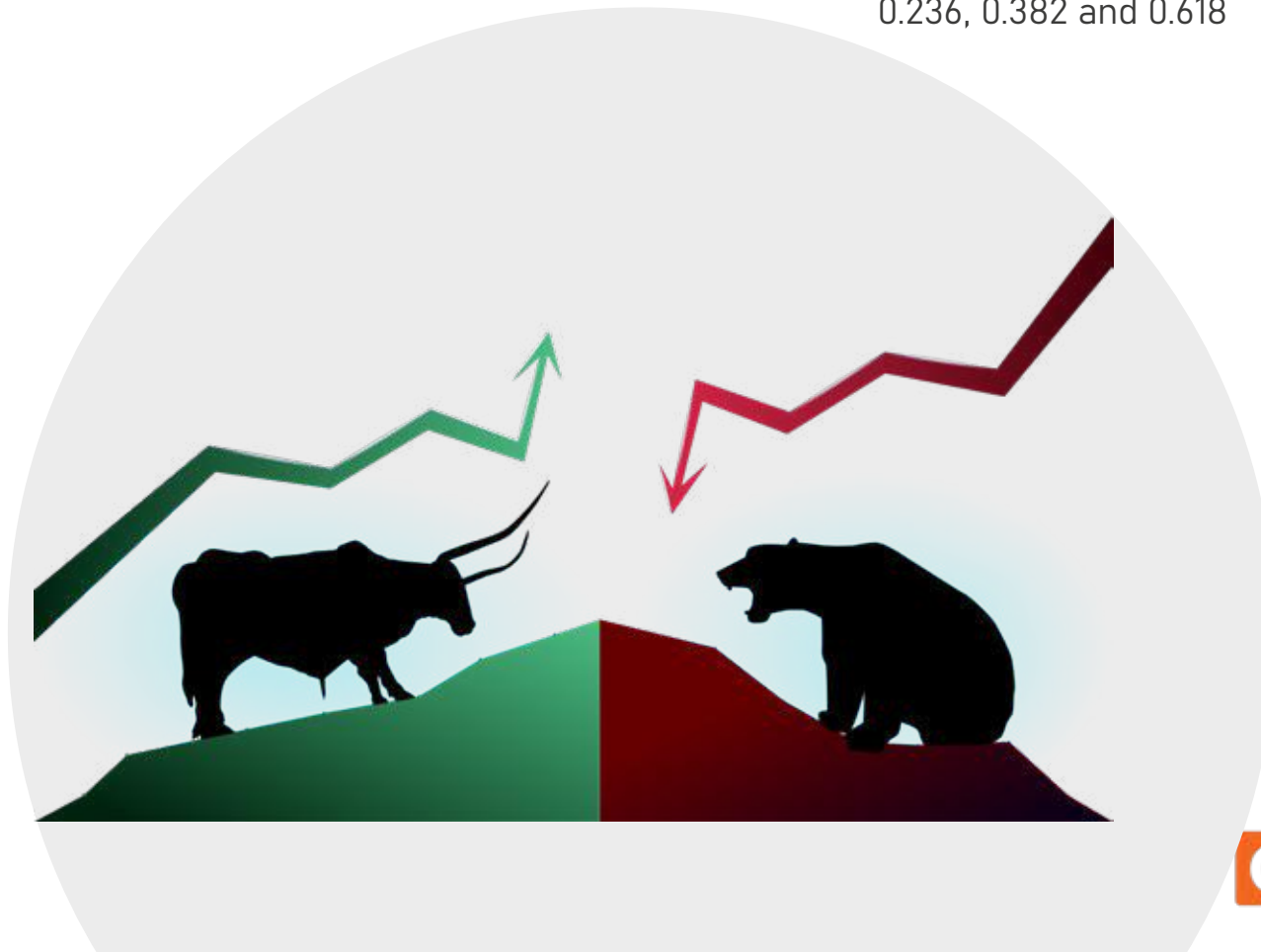
III CONVERGENCE MOST LIKELY TO APPEAR ON 0.5 OR 0.618

In an Uptrend

- Step 1:** Identify the direction of a market
- Step 2:** Attach the Fib retracement tool on the bottom and drag it to the right all the way to the top
- Step 3:** Monitor three possible support levels: 0.236, 0.382 and 0.618

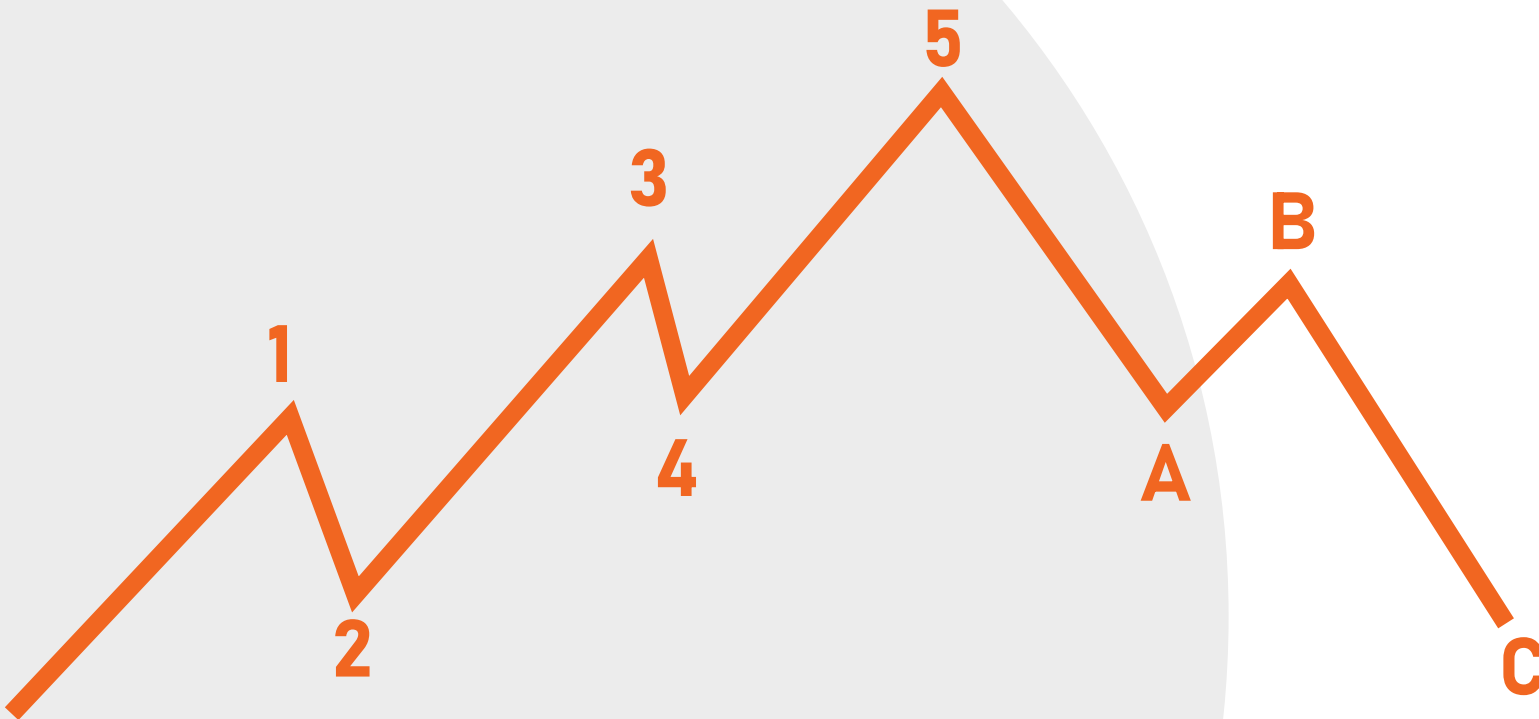
In a Downturn

- Step 1:** Identify the direction of a market
- Step 2:** Attach the Fib retracement tool on the top and drag it to the right, all the way to the bottom
- Step 3:** Monitor three possible resistance levels: 0.236, 0.382 and 0.618



Fibonacci Retracement

Fib retracement levels occur in other technical analysis ways. For example, Elliot Wave Theory (we will learn about it in another e-book) patterns. Fib levels are static numbers that do not change, unlike moving average. The static numbers allow easy and fast identification. This helps traders to act as soon as the price target is reached whether it is a reversal or a breakout.



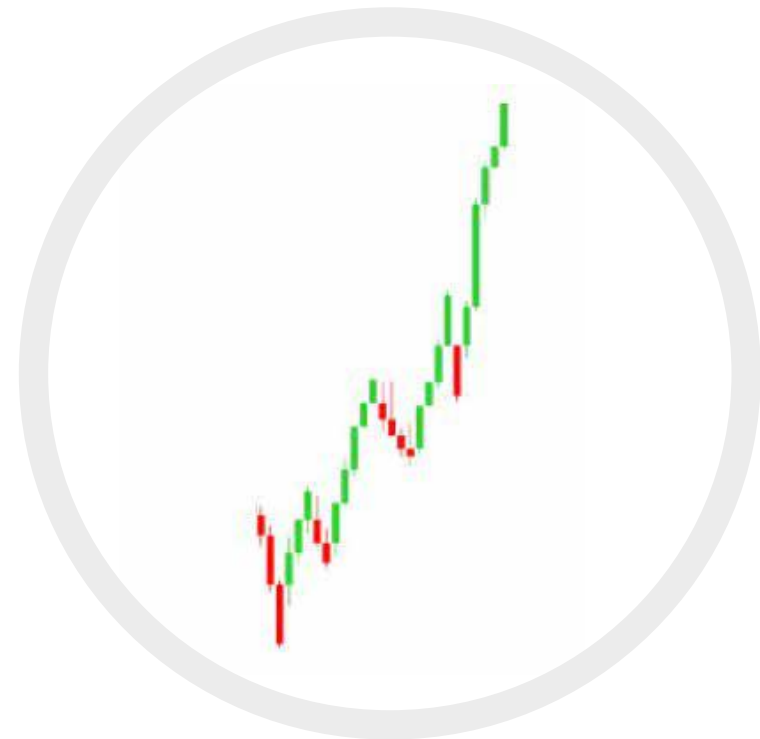
Reversal

A reversal is a change in the price direction of an asset. A reversal can occur to the upside or downside. Following an uptrend, a reversal would be to the downside. Following a downtrend, a reversal would be to the upside.



Break Out

A breakout is when an asset's price is moving outside a defined support or resistance level with increased volume. A breakout trader enters a long position after the stock price breaks above resistance or enters a short position after the stock breaks below support.



Limitations of Fibonacci Retracement Levels



Just like any other technical tool or indicator used for helping traders, fib retracement levels also carry limitations. Support and resistance levels are useful and many times successful. However, they do not indicate if the price will continue in the same direction or reverse. This is why, other indicators are used along with it such as the price starting to bounce off the level. Another issue, is that it is difficult for traders to understand which retracement level is a useful one at the given time. Traders can not know 100% at which level the price might have a reversal.



Fibonacci Extensions

- Fib extensions can be used to establish profit targets or estimate up to which level the price will go. Extension levels are also possible areas of a trend reversal.
- Common Fibonacci extension levels are 61.8%, 100%, 161.8%, 200%, and 261.8%



How to calculate Fibonacci Extensions?

- Unlike Fibonacci Retracements, Fibonacci Extensions don't have a formula. When traders apply this tool on a chart, they choose three points.
- First point is the start of the price movement.
- The second point is where the price will end.
- The last point is the end of the retracement against the move.



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What do Fibonacci Extensions tell you?

- If the price breaks through one extension level, it may continue moving toward the next. That said, Fibonacci extensions are areas of possible interest. The price may not stop or reverse right at the level, but the area around it may be important. For example, the price may move just past the 1.618 level, or pull up just shy of it, before changing directions.
- In a long position on a stock where a new high occurs, the trader can use the Fibonacci extension levels to identify where the stock may go. The same is true for a short position. Fibonacci extension levels are used by traders to understand profit targets.

Retracements

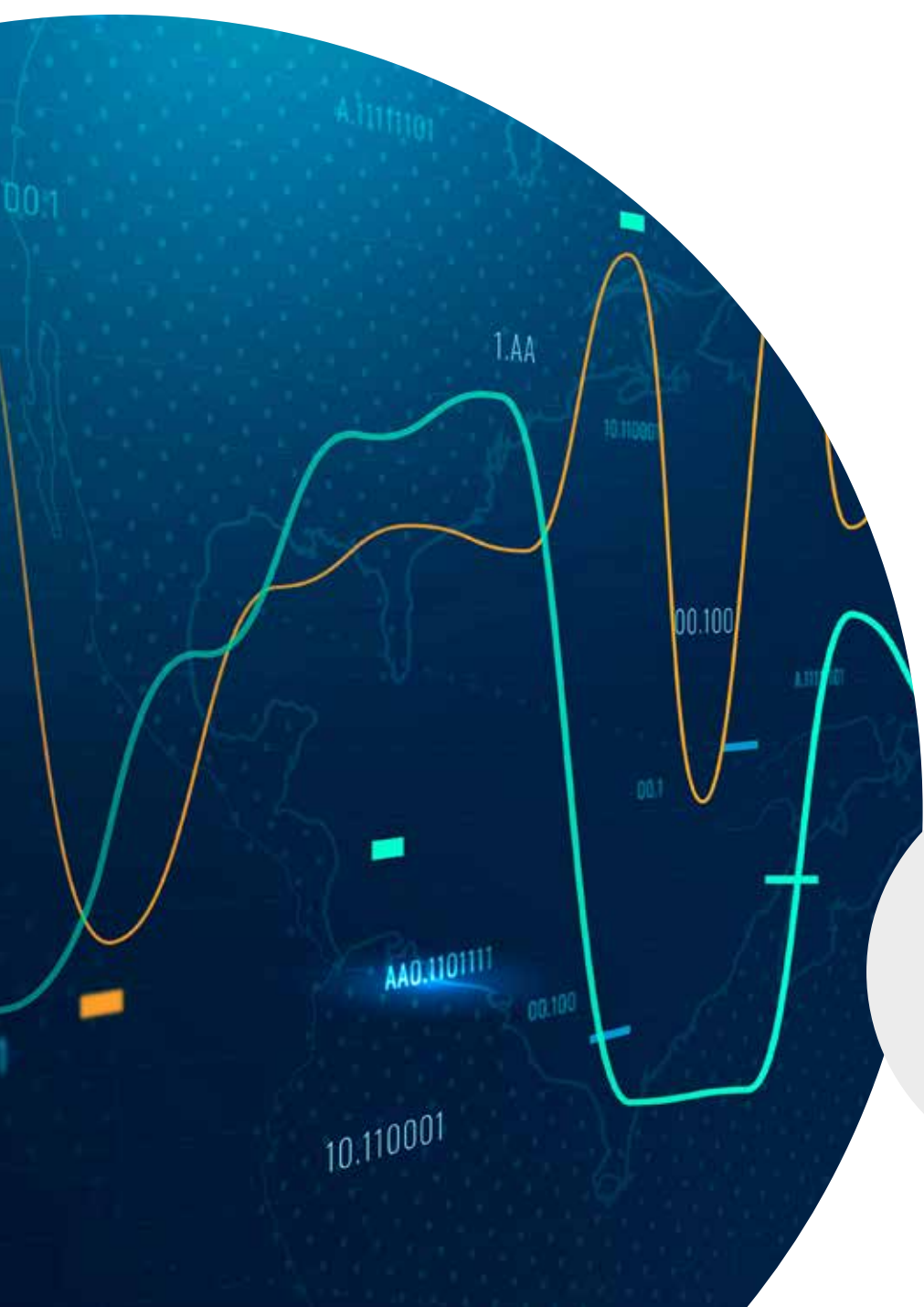
Fibonacci Retracement levels are used to identify how long the retracement could be. It measures the pullbacks in an uptrend or a downtrend.



Extensions

Extensions are used to identify how far the price of an asset will go after the retracements. This can be described as the measurement of the impulsive waves (Elliott Theory) of the direction.





Limitations of Fibonacci Extensions

- Fibonacci extensions are not meant to be the sole determinant of whether to buy or sell a stock. Investors should use fib extensions along with other indicators. Candlestick patterns are especially informative when trying to determine whether to enter a long or short position and for how long.
- The price could at any given time reverse due to news releases, or unexpected events in the market.



Sum Up

- Fibonacci Tools can be used to draw support and resistance lines, stop-loss and profit targets as well as uptrends and downtrends in the market.
- It is very important to use them in conjunction with other indicators for a more reliable reading and not on their own.

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