Chart Pattern Secrets Newsletter

Issue 2

Welcome to the second issue of the Chart Pattern Secrets Newsletter.

We hope that you find it useful and are able to implement some of the ideas into your own trading methodology. Chart patterns can provide an interesting insight into potential price action and form an integral part of successful trading strategies.

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Look out in your inbox for the next issue of the Chart Pattern Secrets Newsletter. In it, we will discover the chart pattern **flags** and how **patience** is one of the most under-rated attribute a successful trader has.

Trends

Arguably, the cornerstone of technical analysis is the trend. A trend in technical analysis refers to a share moving in a clear distinct direction for a reasonable period of time. Shares very rarely move in the same direction day after day for weeks. Even shares that increase significantly over a month or so will have a few days in that month where the share price will fall. The underlying trend or direction is up, however.

When a share trends effectively, there will often be small movements against the overall direction. These small movements are often referred to as 'noise'. Unfortunately, noise can sometimes distract from the underlying trend. It is important to always stay focused on the trend, however.

One of the aims of trading is to buy shares at one price and then sell them later at a higher price. In order to do this, you should try to identify shares that have a high probability of going up. Those shares presently trending up are showing a tendency to head in the right direction and therefore are candidates for purchase.

Conversely, we can draw conclusions about shares that are trending down. If you want to buy shares and sell them at a higher price, buying shares that are showing a tendency to head down is not doing much to help you achieve your aim. This is why following the trend is one of the most important rules we can follow yet also one of the simplest.

How do you identify the trend? There are a number of various ways of identifying the trend including using moving averages and analysing the different points where the share price plotted on a chart appears to form peaks and troughs. Shares go up for one reason. There is more demand than supply for those shares. The buyers are being more aggressive and there is not enough selling pressure to hold them back. For a share to continue to go up and therefore trend up, there must be a continuous flow of new money, otherwise the trend will falter. The opposite is true for shares that go down.

When you think of the emotions behind people when they buy shares; it is normally of anticipation, some excitement and hope that the price will rise. It is generally positive thoughts. Similarly, think of the emotions associated with the decision to sell shares. It may be frustration, a lack of patience, however it is often fear and panic. It is normally not positive. There is the feeling that the odds are against you and that it is wise to get out from the situation and move on. Simply put, there is the anticipation that the share price is going to fall.

Finally, there is an interesting observation to be made about trends. You may often hear yourself say that a share is too expensive to purchase. You start to think that you have missed the boat; you have missed out on its run; you will get in too late if you buy now. These feelings are quite common but are not necessarily well founded, as shares can trend well for an extended period.

Self - confidence

Numerous character attributes are often listed as being important for an individual to achieve trading success. One often overlooked is self-confidence. Self-confidence is a measure of your belief in yourself, and has a number of consequences in trading should you lack it.

When starting out to trade, it is important that you objectively assess your level of self-confidence, as being successful requires you to trust and follow your trading plan. If you lack self-confidence, then you are not likely to trust and follow something you have developed, but worse than that, you may be influenced by someone else's opinion of a stock. Has anybody given you a red-hot tip about a stock before? What did you do? Did they also tell you when to sell it? How did it perform? In his book 'Reminiscences of a Stock Operator' (a fictionalised biography of one of the greatest market speculators, Jesse Livermore), Edwin Lefevre mentions how destructive tips can be to one's trading. This is coming from a book that was first published in 1923 and is one of the most highly regarded financial books ever written. Trust yourself and have confidence in your own trading plan.

When developing a trading plan, it is important that you develop all the steps yourself. By doing this, you will know and understand the logic behind each step in the approach. Should you conduct extensive backtesting, this will also provide you confidence in the approach when it comes to implementing the plan. This confidence will also provide you the discipline to follow the plan.

Furthermore, this confidence and discipline will be vital when it comes to trading the plan with real money. One way we can also increase our confidence is knowing that we have adopted sound risk management rules. A simple stop loss set when entering a trade should provide us the confidence to enter the trade in the first place. The stop loss prepares us for what potentially will be the worst outcome in the trade, notwithstanding the potential for far great loss.

Confidence is believing in yourself to do what needs to be done. It is a measure of your faith in your ability to do something. It is often suggested that successful people are not afraid to fail. In fact, a lot of successful people have failed along the way to success. However, they all have the ability to accept their failures and move on. They understand that failure is often a natural consequence of trying.

It is important that when you trade with a plan that you have developed, that you do so with a positive attitude and with confidence. As soon as you start to think about missing trades or thinking that the next trade is going to be a loss, it is probably time to review your trade or your own level of self-confidence.

Finally, one thing that will help with your confidence is your own knowledge and understanding of the markets, the products you are trading and various tools you use in your decision making. Competence yields confidence. If you are not competent at something, it is highly unlikely that you will be confident doing it.

Comments / Feedback:

Any comments on the contents of this publication or suggestions for future publications will be warmly welcomed. Please email to cpfinder@tradingxl.com.au, fax to +61 3 9870 1738 or phone us on +61 3 8802 0593.

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