Technical Analysis for the Fundamental Investor Script

Some guidelines on using technical analysis
- Technical analysis takes finesse and practice, it's more of an art and a science
- The interpretation of the technical analysis can also vary stock by stock
  - For example, some stocks may be highly cyclic, some not—this can affect how you apply the analysis
- There is much, much more to technical analysis than we'll go over today, this is merely an introduction
- As always, this webinar is for demonstration purposes only, and nothing presented is recommendation to buy or sell a stock.

Chart Patterns
- These are recognizable chart patterns within a price chart that can confirm a trend or signal trend reversal
- There are hundreds of these, we won't go over them today

Moving Averages
- Moving averages are used to find:
  - Trends – it smoothes out fluctuations and makes it easier to see if the stock is going up, down, or sideways; helpful if the stock has volatility
  - Trend-reversals – by crossovers between a shorter and longer average
    - Bullish crossover: shorter-term average crosses above the longer-term average
    - Bearish crossover: shorter-term averages crosses below the longer-term average
  - Support and resistance levels – when the price crosses the moving average
- The Simple Moving Average (SMA) shows the average closing price over the last *n*-days
  - You can adjust the time periods or add a third time period
- *Example: FB (1-year time period) with SMA*
  - Bullish crossover August 8th—trend picking up
  - 50-day SMA as resistance from January 27-29
- The Exponential Moving Average (EMA) is similar to SMA but more sensitive to the more recent price changes

Bollinger Bands
- Bollinger Bands measure the overbought and oversold conditions of the market in order to predict future price movement
  - If the price is toward the top of the band, it's overbought—could take a downturn
  - If the price is toward the bottom, it's oversold—could taken an upturn
  - The price can quickly correct it if gets outside the band

- Because the width of the band uses standard deviation, which is a measure of volatility, the bands widen during period of high volatility
    o A narrowing of the bands can signal an imminent increase in volatility
- *Example: ACE*

Moving Average Convergence Divergence

- MACD is a momentum indicator that's meant to spot subtle changes in the trend of a stock
- The MACD line itself (blue) is the 26-day EMA subtracted from the 12-day EMA and is plotted against the 9-day EMA "signal" line (green); the signal line subtracted from the MACD is the "divergence" (the green histogram)
    o When there are crossovers it's a signal to buy or sell:
        ▪ When the divergence goes positive, it's bullish
        ▪ When the divergence goes negative, it's bearish
        ▪ Bullish signals are considered stronger when above the zero-line
        ▪ Bearish signals are considered stronger when they are below the zero line
- *Example: WYNN*
    o Bearish crossover on March 10-11—the MACD picked up on this very quickly
    o MACD can be used to interpret the sideways trend

Relative Strength Index (RSI) and Money Flow Index (MFI)

- The RSI and the MFI are oscillators: they fall in a bounded range, from 0 to 100
    o Like all technicals, they try to predict where the stock price is heading by finding short-term overbought and oversold conditions of a security; they also can help confirm a trend or predict a trend reversal
- The MFI incorporates volume into its calculation, so it helps tell if there is too much or too little volume associated with a move
- General guidelines for the RSI:
    o If it's at 70 or above, it's overbought→ the price could go down
    o If it's at 30 or below, it's oversold→ the price could go up
    o For the MFI, these values are 80 and 20, respectively
        ▪ If the RSI/MFI cross these thresholds, the price can experience a quick correction
- *Example: XL – price correction*
    o When the RSI/MFI spiked, the stock generally took a downturn
- *Example: TWX – divergence*
    o Recently, the price is rising but the RSI/MFI are headed down, could signal a reverse in the current uptrend

Volume

- This is the daily trading volume of the stock which is very important for technical analysis—mouseover the bar for the exact date and volume

- o It's used to confirm trends and chart patterns, or to predict trend reversals (through divergence)
- Trend confirmation: volume moving with the trend signals a stronger trend
- *Example: BMA – trend confirmation*
    - o Beginning of chart shows volume ramping up with the price
- *Example: NRG – divergence*
    - o Recently the stock price is rising but the volume is falling—this is divergence and could signal a trend reversal

Volume by Price

- Volume by Price is used to find support and resistance levels for a stock
- Each bar represents a price range, the length of the bar indicates how much trading occurred in that price range—mouseover the different sections for a tooltip
    - o The green portion shows the amount of trading when the price moved hirer
    - o The red portion shows the amount of trading when the price moved lower
    - o The longest bar can be used to spot possible support and resistance levels
- Note that these bars change depending on the time period selected
    - o Because they depend on data from the whole time period, you can only use it to analyze the data towards the end of the time period
- *Example: AIG – demonstrate length of bars*
- *Example: WLP – demonstrate support*
    - o The longest bar looks likes a support
    - o Add in Volume and Candlesticks and you can see the volume spiked on January 30th as it hit the support and rallied

Scrolling Through Technicals

- With the table and the chart linked, it's easy to scroll through the technicals of stocks in the table
    - o You could do this each day, or several times a day, to find the ideal time to enter in a position for a stock you've been watching
- Premium users can save a chart "shortcut" with any technicals they like in order to easily access them

Screening on Technicals

- The Momentum Screener (in the Library) incorporate technicals: Bollinger Bands, Simple Moving Average, Range
- You can create a new screener
    - o Look in the "Technical Indicators" folder
    - o You can run your screener on any population of stocks in Stock Rover (for example, the S&P 500)
        - ▪ Add any promising stocks to Technical Watchlist
        - ▪ Create a note (premium) with your thoughts

Create Fantasy Portfolio to Test Technical Methods

- Copy an existing portfolio (with history) and either go back in the past and alter trades to see how you would've done if you'd timed your entries and exits better
  - o Or going forth just try out some technical methods with this portfolio to see how you do!