TECHNICAL ANALYSIS
PLAIN AND SIMPLE

CHARTING THE MARKETS IN YOUR LANGUAGE

THIRD EDITION

MICHAEL N. KAHN

TECHNICAL ANALYSIS PLAIN AND SIMPLE, THIRD EDITION

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This book is dedicated to my father,
Arthur M. Kahn, who would have
loved to see it in print.

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As with just about all books ever written, the author did not complete his work alone. This book is no exception.

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He has been a regular guest on the *Nightly Business Report* on PBS, has appeared on CNBC, and was the editor of the Market Technicians Association newsletter, *Technically Speaking*. His first book, *Real World Technical Analysis*, was published in January 1998, by Bridge/Commodity Research Bureau Publishing.

Prior to writing technical commentary, Mr. Kahn was a Senior Product Manager for Knight-Ridder Financial before that company was merged into Bridge. He was responsible for the marketing design of several of the firm’s charting software platforms and launched technical analysis coverage for Knight-Ridder Financial News. He was also a coeditor of the *Tradecenter Market Letter*.

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PREFACE

Technical analysis is one of the oldest market disciplines, yet the majority of the investment and academic communities consider it, at best, a minor supplement to their own work. At worst, it is disparaged as tea-leaf reading or simply a self-fulfilling prophecy. Look at these two phrases. They suggest that the technical analyst divines the market from some mystical process. This could not be further from the truth.

Consider the fundamental analyst. This person relies on company reports, conversations with company insiders, and macro-economic research in relevant business sectors. All this is indispensable when determining if a company is viable and predicting how its business will fare in the future.

Now consider the source of all the raw data. Much of it is projection and conjecture. How can you rely solely on such raw data when earnings reports and other industrywide data will be subject to revisions?

Technical analysis looks at actual trades in which bulls and bears have put their money where their collective mouths are. There is no revision of data. There is no ambiguity. There is no mystical divining of the future. All market and stock selection is based on current, not past, price performance, the predictable behavior of market participants, and the dynamics between markets over time.

Trends exist. Information is slowly disseminated to the public in an imperfect manner, and as the public acts on the information, the markets move. They continue to move until either the last group has acted or an outside influence, such as news, ends the trend. Sounds a lot like physics, does it not? A body in motion tends to remain in motion.

Look at another aspect of the analysis. Behavior is a key component of the analysis. When similar market conditions occur, market participants react in similar ways. This is how the patterns and measurements within technical analysis are created.

For example, the market holds fairly steady as buyers and sellers adjust their portfolios to meet their specific investment criteria. A stock might trade from 50 to 52 for weeks in this way. Is the stock good? Is the company good? You do not know. All you know is that bulls and bears consider the stock to be fairly valued within a small range. A body at rest tends to stay at rest—physics again.

Now somebody comes into the market to buy a large block of stock. Why? Technical analysis does not know but more important, it does not care. All it needs to know is that money has flowed into the market and increased demand for the stock. Demand? That is straight from basic economics. If demand rises, the price must rise to induce sufficient supply (sellers) to come into the market and restore equilibrium. This does not sound very mystical, does it?

So, now that demand has increased, market activity picks up to provide supply. It also changes in character as people try to decipher what is happening. Here are the familiar concepts of fear and greed, both key determinants of human behavior. Some participants think that something has changed and the stock is now undervalued. It could be a new product or simply a decrease in the company's raw material inputs. Perhaps it is foreign capital coming into the stock. Or a shortage of the stock itself. Whatever the reason, some market participants know something, or think they know something, about improved prospects for the company and they buy. The market breaks out of the trading range, and as it does, more market participants act. The size and scope of their actions is often similar to the size and scope of their actions at other occasions in which the market has broken out of similar ranges. It can be measured and projected.

Technical analysis has an unfortunate name. Perhaps "price action analysis" or "supply, demand, and reaction analysis" might be better. In 1998, great strides were made between market technicians and the academic community in the emerging field of behavioral finance. Now there is a possible name to use.

One aspect of the technical discipline is explaining the difference between valuations and actual market prices. If a stock is worth 75 on paper based on discounted cash flows, projected growth, and overall economic conditions, why is it trading at 90? The difference is in the market's perceptions of the stock. People have pushed the stock up past its theoretical value. Technical analysis is perfectly suited to handle this. Because people's perceptions can change quickly, it is also perfectly suited to reacting equally as quickly. This type of reaction speed is impossible using fundamental analysis alone.

Do you scrap your fundamentals and rely exclusively on technicals? Absolutely not! Although there are scores of money managers and traders that are 100 percent technical and making a lot of money, you, the reader, are not interested in making technical analysis your sole investment discipline just yet. You are reading this book because you are seriously interested in enhancing your returns, not searching for a completely new method. Perhaps one day you will make that switch, but that is beyond the scope of this book.

At this stage, charts give you a clear picture of what your fundamental research is saying. Remember that the fundamentals describe the company. Technicals describe how the stock performs. You are buying stock, not companies.

But why does this book need a third edition? If technical analysis is not subject to revision, then its concepts should have near-permanent shelf life. Unfortunately, the markets are ever–evolving, and analysts are always learning new things about how it operates. After all, wasn't the world considered to be flat at one point by the best minds of the time? Or that leeches healed disease? You get the point. As the markets change, so, too, must the analysis.

Between the first and second editions, most of us experienced our first live bear market for stocks. Between the second and third editions, we experienced a near breakdown of both the financial markets and the usefulness of our analytical tools. This edition incorporates everything new I have learned about the markets and how to analyze them. It is likely not going to be the last edition because the markets will not stop changing. Remember the old saw, "Whenever you find the key to the market, they change the locks."

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ABOUT THIS BOOK

Imagine that you speak only Mandarin and you want to read Shakespeare. Somebody has to translate it into your language. That is why this book was written. It will present technical analysis to you in your language and in the order that makes sense to you. You will go through the analytical process, calling on the tools as you need them, not as they might be organized in a textbook.

My career has been entirely within the financial services industry, yet in most of my positions, I have served in the role as translator. I translated the research department's output into ideas for the sales force. I organized the trader's inventory into a solution for the brokerage customer. I spoke with customers and translated their needs into specifications to give to programmers, and then translated the result back into learning aids for the sales force. This book is a logical extension of that. I hope to translate an often misunderstood, yet valuable, analytical discipline into simple tools any investor can put to immediate use. All of this can and will happen without compromising the quality of the analysis.

Core Themes

Making Money, Not Correct Market Forecasts

You need to be humble because the market is a lot bigger than you. You cannot tell the market what to do, even if it is "wrong" by all measures. It can hold a "losing" position a lot longer than you or even your country's central bank can. What you want to do is listen to the market. It will tell you where it is going, so you can jump on for the ride.

With technical analysis, the worst case is a bad trade from a false breakout. Humility allows you to acknowledge your error immediately and cut your losses.

At its best, technical analysis will never let you miss a big move. That does not include the unusual situations of legal changes, buyouts, or natural disasters. However, if a market is going to have a sustained move either down or up, technical analysis will get you out or keep you in, respectively. It probably will not be at the very beginning or the very end, but you will capture the bulk of the move and get out before giving back a significant portion of your profits.

What Makes a Stock Look Good?

A rising tide raises most boats.

To be trite, a stock that is going to go up is the one that looks good. Why state it like this? The answer is that you should not be interested in only flashy glamour stocks or common household names. You need to look for stocks where demand exceeds supply, where the so-called smart money has been placed in the early stages of their individual bull markets. Stocks that are already moving higher with increasing public interest are ideal candidates. These are all evident on price charts with supporting indicators.

Notice that there is no mention of companies with solid fundamentals. Strong balance sheets and good earnings growth make for good companies. On paper, this suggests a certain price range over time.

In the real world, valuations are only one component of stock prices. Investor perceptions of value, based on supply and demand, economics, politics, pop culture, and fear and greed, make up the difference between fundamental valuation and market price. Price can be higher or lower than valuation. Technical analysis seeks to follow price trends, not paper valuations.

What makes a stock look good? Find at least three of the following, and chances are, you will pick a winner:

- A rising price trend as more and more investors jump aboard.
- Rising volume as investors become more aggressive in their purchases.
- Strong, but not excessive, price momentum. Anything higher indicates that supply and demand are out of synch.

- A strong sector. If the sector is doing well, there is likely to be enough business for all the stocks in it.
- Strong market. A rising tide raises most boats.
- Supportive environment. Low input prices, high output prices, low cost of doing business, and favorable supply and demand in the industry.

All of this information is available on the charts. Supportive environment sounds like fundamental analysis, and it is to a degree. Technicians call this *intermarket analysis*. For example, an electric utility has high energy input costs and is often saddled with a good deal of debt. A bear market in oil and gas combined with a rally in the bond market (declining interest rates) suggests favorable conditions for the stock.

Choosing the Right Tools

Technical analysis offers a vast array of tools for every type of analytical task. There are charts that display prices in time frames ranging from trade-by-trade to daily to monthly and longer. They can show market cycles, phases of fear and greed, and projected targets.

Indicators are available to measure price momentum, volume distribution, and market breadth. There are even methods in popular use to measure sentiment and how perceptions change. For the purposes of this book, you will stick to the basics and use those tools available to the individual investor.

Flexible Analysis for the Real World

Allow yourself to *hear* what the market is telling you and be able to listen to it, no matter what you may have thought beforehand. *See* patterns develop. *Feel* the changing tides of investor sentiment. If you need further sensory reinforcement, *smell* your profits and *taste* success.

Strict interpretation of technical rules is, of course, the best way to learn the topic. But this book will focus more on the spirit of the law instead.

This will allow you to take the concepts as you need them, rather than follow a textbook outline.

What This Book Is About

This book was designed to do three things: enhance your returns, help you avoid bad trades, and get you to think in terms of probabilities.

Enhancing Your Returns

Even this early, it is important to repeat the point that at this stage in your investment career, technical analysis will not and should not replace other methods. You should focus on enhancing your other decision-making processes to increase the likelihood of success. You will expand your set of investment decision-making tools and learn to select the right tool for the job.

The following chapters also take the mystery out of technical analysis. The entity called "the market" is really made of the collective actions of human beings. It can therefore be analyzed with tools that measure crowd behavior and the imperfect dissemination of information. Sounds hard? It is not. A chart with supporting indicators can do this with relative ease.

Finally, there is a visual (sensory) component to the numbers (earnings, sales, etc.). In the investment world, a picture really is worth a thousand words.

Avoiding Bad Trades

If enhancing your returns deals with buying the best stocks, then avoiding bad trades is just another way to express that thought. Technical analysis can quickly show you situations where the stock has drifted too far away from its fundamental value and is therefore not presenting a good opportunity. It can also tell you that a stock is not healthy when it fails to react to what should have been good news (higher earnings, new product, better business environment). If the stock does not rally on good news, it may mean that the bulls are exhausted. They may have already bought their share and therefore do not demand any more.

Probabilities

Technical analysis is about probabilities and escapes. People probably react in similar fashion to similar situations, but it is not guaranteed. Proper analysis will give you the probability of a correct buy or sell decision, as well as tell you right away when you have made a mistake.

Even if your analysis and decision were absolutely correct, the world changes. When it does, the technical condition of the stock or market changes. The charts will alert you that you need to reevaluate your positions.

What This Book Is Not About

Do not worry that you might read about sophisticated analysis and therefore think like a short-term trader at the stock exchange. Treatment of each subject is kept deliberately light.

You will not have to wade through a discourse on how the market works or how to manage your personal finances. It is assumed that you already know this. This book is not concerned with why you are investing, other than to make money.

Finally, there will be no discussion of earnings, sales, revenues, debt, weather, harvests, or other fundamental data other than to mention that fundamentals do drive the stock price in the long term. Respect them, but do not use them directly in the stock-picking decision.

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HOW TO GET THE MOST FROM THIS BOOK

This book is aimed at serious individual investors seeking to augment their current stock-picking abilities. It is also of value to the professional investor or trader in any market (stock, bond, currency, or commodity) who has not yet used technical analysis and is seeking additional tools for decision making. Whether you are investing alone or as part of an investment club, this book will explain the basics of chart reading, market timing, and even some money management.

Read the first section to get an overall feel for what technical analysis is all about. Then, take one chapter at a time and see how it applies to what you are already doing. Examine some of your past trades that worked out well to see if the technical condition present was favorable. Next, look at some of your past trades that did not work out, to see if technical analysis could have kept you away from them or at least told you quickly, before too much money was lost, that they had gone bad.

Do not rely exclusively on what you learn here. Technical analysis is both an art and a science in that it can be rigorously tested but it still depends on the experience of the analyst to set parameters of precision and risk tolerance. Use the concepts presented here to augment your current analysis. There will be time later to study the topic in detail. For now, your job is to increase your investment returns right away.

You Don't Have to Abandon the Fundamentals

One thing you need to remember is that we will be focusing on supplementing your current stock selection discipline. You will not have to give up your broker's advice, advisory services, or favorite hot tips. Rather, you will learn how to evaluate these recommendations to see if they are technically sound, and therefore be able to determine if the time is right for the investment. You will also be able to track your current portfolio to find advance warnings of impending reversal. In other words, you will be able to keep more of your profits because you will be able to sell quickly and with more confidence.

If your broker calls with a new recommendation, consider delaying a purchase when the chart looks bad. The market is telling you something that has not yet appeared in the fundamentals. Remember that if nobody is buying the stock, no matter what the fundamentals say, it will not go up. Also, markets can trade far away from their underlying fundamental values, and technical analysis will tell you when that is happening. In the stock market, a company may be very profitable and a leader in a growing industry, but its stock may have traded to unrealistic levels. The company is great. The stock is not.

Technical Analysis Is Portable

We may talk a lot about stocks but almost everything here is relevant in the bond, currency, and commodity markets. Chart patterns and trends are valid in all markets. Some instructors actually take well-known indices, multiply their values by a constant, and then turn the chart upside down when they present it to their classes. The analysis is nearly identical to the unaltered chart.

Yes, it is true that markets act somewhat differently at tops than they do at bottoms. It is also true that each market and individual stock has its own "personality." However, for our purposes in basic analysis, the nuances and subtleties can be ignored.

Daily charts are used where each unit summarizes the trading activity of a single day. Almost everything you will learn is valid in all time frames. Daily charts are great for 3–9 month analysis. Longer time horizons require weekly or monthly charts where each chart unit summarizes a week or month, respectively, of trading data. If you are a short-term trader, charts in the hourly or minute times frames are needed. However, learning to day trade is not why you are reading this book.

Finally, because technical tools work in most markets, you can cover more ground than a fundamental analyst. That means you will be able to analyze a technology company, food retailer, and a bank with equal ease. You will even be able to chart interest rates and oil prices to help with your stock selection.

You may be less detailed, but you are not using only one analytical method. Your goal is profits, not analytical expertise. Let the business media interview the expert. You are here to make money.

1

REQUIRED BACKGROUND

As much as it would be good to jump right into learning technical analysis, it is still a good idea to understand some broad concepts.

The Past

"Those who cannot remember the past are condemned to repeat it."
George Santayana

Historical Data

When investment professionals as a group make their decisions, they often analyze such fundamental information as economics, politics, and demographics. They look back to the past to forecast what may happen in the future. This does not mean that they are consulting a magic oracle but rather, they are employing technical analysis of the markets. This discipline relies on generous amounts of historical price data that is both accurate and readily available to their computer applications.

Technical analysis is based on human behavior, but it is not a study in psychology. Investors and speculators react the same way to the same types of events again and again, and this is reflected in the ebb and flow of prices. If one charts this activity over time, patterns in the price action emerge. Some of these patterns comprise standard technical analysis, while others are created by analysts based on their own observations

> Investors and speculators react the same way to the same types of events.

and calculations. Historical data are required in both cases to test theories and fine tune their parameters.

When currency traders, for example, are deciding whether or not to buy yen, they may look at a chart of yen prices for the past year to determine if the recent rally has ended. This graphical representation makes it a quick study. By expanding the chart to cover more years, they can quickly find other occasions when the yen rose quickly and what happened just after it did.

History Repeats

Technical price patterns are often followed by similar reactions. For example, if prices were rising and then start to trade in a small range, the characteristics (shape and size) of the range can be used to determine how far the market will move once the pattern is ended. This is not just a guess, but a highly likely condition (reaction by humans) based on thousands of similar occurrences in the past. The more historical data the investor has available, the more historical observations can be made and the more likely the investor will make a correct buy or sell decision.

The biggest advantage to using a historical database in making these decisions is that it gives the trader or analyst perspective. A sharp price increase in one commodity today may be taken as a bullish sign until it is viewed as part of a longer chart that has been declining for the past six months. In that light, the rally in a commodity may well be an opportunity to unload it rather than load up on it.

One of the biggest criticisms is that technical analysis is a self-fulfilling prophecy. Wearing a “making money, not forecasts” hat sounds like a good deal for those who get in early. Stepping back from the profits for a moment, it should be conceded that the criticism is true in some cases.

One definition of a technical breakout says that a market that moves above the top of a technical pattern should be bought. Short-term traders who see this buy, and the market moves higher due to increased demand.

This works well on the initial breakout as new buyers are drawn in. However, unless there are more technical factors supporting the move, the rally will fail. In this case, the prophecy will not come true. For a sustained rally, there must be increasing demand and increasing participation from the public (individual or institutional). True breakouts are usually presaged by changes in the underlying technical condition, have certain confirming characteristics at the breakout, and are followed by improving technical indications.

Although this undermines the self-fulfilling prophecy argument, rallies, chart patterns, and breakouts can all be measured and followed because people do repeat their actions. A triangle pattern in today's market is formed for many of the same reasons that it was formed before. A breakout now will probably create the same result.

History repeats itself in the same way that snowflakes look alike. From a distance, they look the same. When put under the microscope, however, the differences become apparent. In the markets, human participants tend to do similar things given similar circumstances. For example, if a rally stalls and a triangle pattern forms on the charts, buyers and sellers become increasingly uncertain about what to do. They buy and sell with less confidence as they wait for some outside influence to spark the next move, higher or lower. The fact that there are at least five different variations of triangles tells us that these periods of increasing uncertainty are not exactly alike.

What does a budding technician make of all this? Following the basic rules of market behavior will be profitable most of the time, and we must be nimble enough to react when events deviate from the expected.

This summarizes the similarity of market actions without locking us into strict definitions. People tend to do similar things given similar conditions. We learn from our mistakes. However, there are always new people entering the market who have not yet had their lessons.

Repetition and Rhyming

Are no two snowflakes exactly alike? Does lightning ever strike twice? Does a bull market last the same time and move the same distance?

It was Mark Twain who said, "History does not repeat itself. But it does rhyme." No matter how much today's market may look like a previous market, you cannot be 100% sure it will continue to react in the same way. It may go up, but not as fast. It may pause to rest in a quiet trading range, or it may pause to rest in a volatile trading range.

With so many variables that can affect the market, the difference between having 80 and 90% of them in line probably does not matter to a bottom-line decision of buy, sell, or hold. It might affect the course or amount of the rally, but not the decision to buy or sell.

Technical Market Theory

Most people want to know a little about how the car works so they know how to drive it and when to take it in for service. Technical market theory encompasses a large body of work, rigorous testing, and decades of experience. At this stage, it is similar to the car in that the basics need an explanation. Becoming expert takes rather longer.

As technical investors, we are chart readers. The key is to think of a chart in psychological, not graphic, terms. In other words, support is the level at which the aggressive selling of the bears has waned sufficiently to be offset by the rising aggressiveness of buying by the bulls. Resistance is the level at which the aggressive buying of the bulls has waned sufficiently to be offset by the rising aggressiveness of selling by the bears.

The Basics of Technical Analysis

Chart patterns represent the behavior of the masses. They are built from actual transactions, so in effect, they represent how the pool of investors, traders, speculators, and hedgers have put their money where their collective mouths were over time.

Because the composition of the pool stays relatively stable over time and investors react the same way time and time again when presented with the same circumstances, chart patterns can be used to measure the likelihood of similar resolutions to current market conditions in the future.

Not all players have access to the same information at the same time.

Since not all players have access to the same information at the same time and they do not react at the same speed when they do get it, markets present opportunity. If everyone knew about a new product announcement from the Widget Company at the same time and they reacted the same way, the stock would only trade at the market maker's bid-ask spread until the news came out. It would then jump completely to the next level, where it would trade perfectly flatly until the next news development. Trends represent the slow dissemination and assimilation of news.

Because the market really consists of the mass of human will, it is prone to excessive swings from optimism to pessimism and back again. Technical analysis helps to measure these swings.

Humans Again—Market Psychology

This emerging field of analysis is beyond the scope of this book. However, a few of the basic concepts can be learned that directly apply to analyzing a stock or market, as well as a few that are indirectly indicated in the charts.

Perceptions

It is worth reiterating that a stock's price often does not match its fundamental value. Current market price can and does deviate from the (forgive the jargon) capital asset price model and discounted value of future cash flows. In a marketplace where humans, not computers, determine prices, it is not what it is worth; it is what people think it is worth.

How else can the phenomenon of Internet stocks be explained? In 1998 and 1999, these stocks tripled after their initial public offerings when they had no profits and unreliable revenues. And the 1987 crash? How can the fundamental value of the entire stock market be cut by almost one-third in one day when there was little change elsewhere in the outside world?

Leading into the crash, people were ignoring such important factors as soaring interest rates and the prevalence of a “buy anything” mentality. When reality caught up with perceptions, prices tumbled.

To rephrase this, the stock market or any other market never reflects calculated true value. It reflects people’s perception of the value; what people think it is worth.

The Crowd Versus the Individual

People like to believe that they are independent thinkers and that rational analysis and logic often prevail. They also might be modest enough to admit that other people have valid, and even superior, opinions.

When those same, rationally thinking people are part of a crowd, they tend to conform to the crowd. It is uncomfortable to maintain a minority opinion, even when the individual’s analysis is sound. As part of a crowd, humility is lost, as everyone begins to think that they (the crowd) are 100% right. There is no room for contrary opinion. Facts not confirming the mass opinion are ignored.

In the previous section, the 1987 crash was used as an example. The crowd wanted to buy stocks and the market went up. The rare dissenter was called a “doomsayer,” even though the evidence for a crash was in place.

The same condition is in effect at market bottoms. The crowd sees nothing but bad news and the market continues to fall. Changing conditions are ignored as they were in 1982, even as the dawn of the greatest bull market of all time was at hand.

Technical analysts have the tools to follow the changing tide. Confidence in their analysis provides the conviction to act as an individual, against the crowd, if necessary.

Myths and Truths

A few of the myths surrounding technical analysis have been covered: the self-fulfilling prophecy, basing future price activity on past performance, and reading tea leaves. There can be some truth to self-fulfilling prophecy. After a stock breaks higher from a chart pattern, new buyers are drawn in. They push the price higher and that, in turn, draws in still more buyers.

The problem with this explanation is that it unknowingly merges short- and long-term analysis with a one-time action (breakout) into one story. Short-term analysis would have told short-term traders to buy before the breakout. If technical conditions continue to improve after the breakout, then long-term analysis would confirm it with improved momentum (prices move convincingly) and higher volume (more shares change hands, suggesting broader public participation). Investor sentiment would improve as the changes in fundamental data filtered down to all investors.

The past-performance issue is another of the critics' favorites. How can past performance determine the future? The "random walk" theory of markets says that if prices are random, then nothing can predict them. But prices are not random. Prices are based on calculated value modified higher or lower by human perceptions of value. Calculated value changes in predictable ways based on the economy and the individual company. Perceived value also changes in predictable ways.

It cannot be calculated how perceptions will change, but they can be measured based on current buying and selling in the market. Buying and selling leave measurable footprints on the charts, and because humans tend to do similar things given similar circumstances, it can be forecasted what the market, as the sum of all humans participating, will do next.

It is not the past action of stocks that is used to predict the future. Rather, it is the form and extent of current trading and the time-tested knowledge of what people have done after similar patterns in the past that determine supply and demand. This allows prices to be forecast.

The Pillars of Technical Analysis

There are four main areas of technical analysis that analysts can objectively measure and use in trading systems. They are as follows:

- Price
- Volume
- Time
- Sentiment

There are indicators and analyses in each of these areas, and Chapter 23, "Sometimes Being Wrong Is Good," outlines many of the more popular ones. For the purposes of introducing these concepts in this chapter, it will be sufficient to give them a general treatment.

Price is the most important of these areas; we measure profits and losses in price differences between buys and sells. It deservedly gets the most focus by analysts and academics alike, but if all four can be employed together, the odds of making successful decisions can be dramatically increased.

Volume includes such concepts as accumulation and distribution, market breadth, open interest, and trade count. Time includes cycles, seasonality, and relationships between patterns and trends from a duration point of view. Finally, sentiment is a more subjective area that seeks to determine solely if the masses—i.e., the consensus of investors—is tipped too far in one direction. At that point, it pays to consider positioning against the crowd. Such indicators as cocktail party chatter and options premiums play roles here, and there will be more on each aspect later in various places in this book.

For Fundamentalists

"The biggest mistake that a fundamental analyst makes is thinking that a stock and a company are the same thing. The biggest mistake a technician makes is thinking that a stock and a company are different."
—Phil Roth, chief technical market analyst, Miller Tabak & Co. LLC

Even the most ardent believer in fundamental analysis could benefit from technical analysis. Technical analysis helps to time purchases and sales of securities. When a company receives glowing fundamental reports, its stock may not be good to buy. It may have already run up on the news or anticipation of the news. It may have been caught in a frenzy of activity that was unrelated to the fundamentals. Internet stocks in 1998 were a good example of this.

Technical analysis helps to determine if the price of the stock has moved to an extreme. Price in the market can and does become decoupled from the fundamentals.

Even a fundamental analyst in technical denial uses some technical information, such as 52-week price range and earnings history. The former represents a crude measure of past performance. The latter is actually the trend in earnings.

To recap, this book is not about getting you to abandon your fundamentals. It is about enhancing your analysis with charts. This author is a full-fledged technician, but you do not have to be.

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