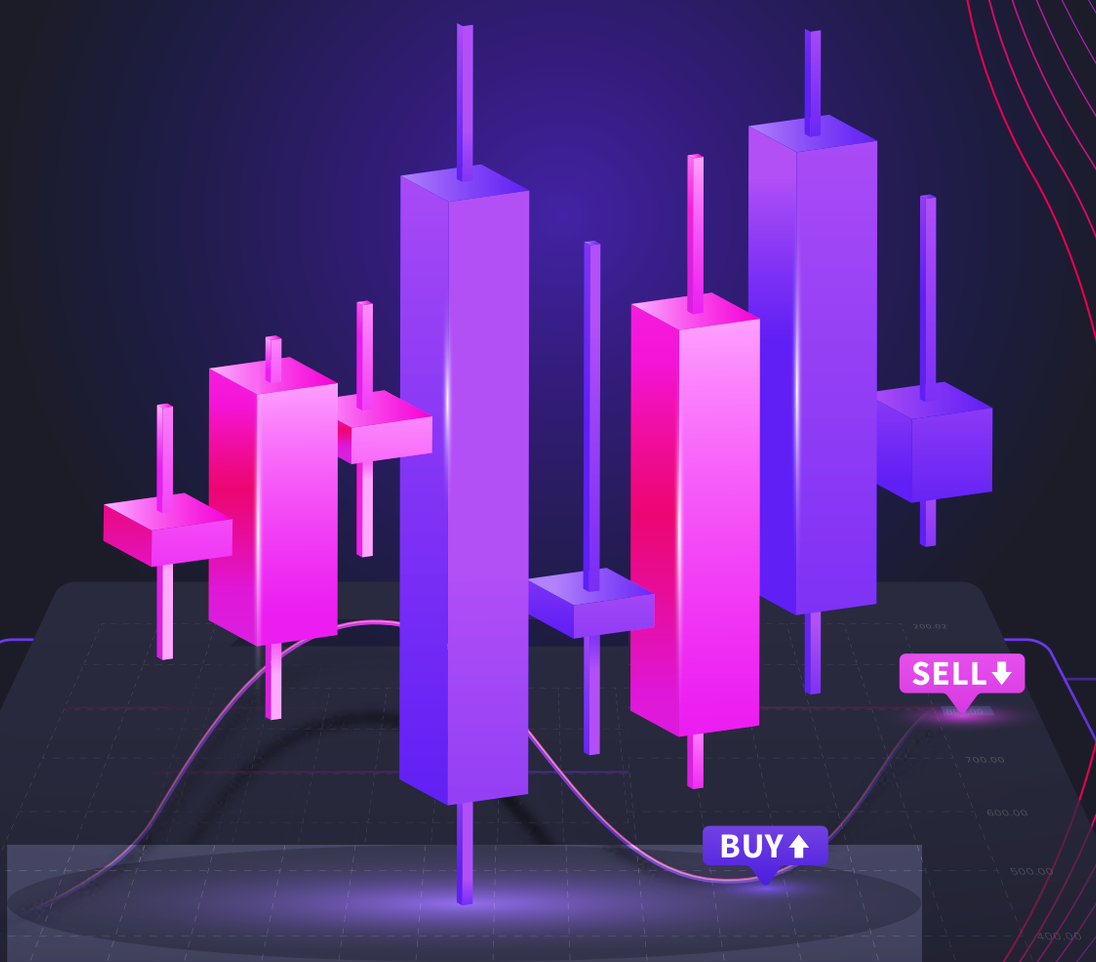
inveslo
YOUR GATEWAY TO TRADING

Basics of

Technical Analysis



Written By
Inveslo Analysis Team

Contents

		Page
1	Introduction	3
3	The Different Types of Charts	4
3.1	Line charts	5
3.2	Bar charts	6
3.3	Candlestick charts	8
4	Supports and resistances	10
5	Significance of support and resistance levels	12
6	Trend lines	14
7	Basis of reversal chart patterns	17
8	Popular bearish reversal patterns	18
9	Popular bullish reversal patterns	22
10	Popular continuation patterns	26

Introduction

According to the definition of technical analysis, it is a tool or a method used to identify a security's probable future price trend at the earliest stages based on the data collected in the market.

The theory behind the validity of technical analysis is the notion that the collective actions - buying and selling - of all the participants in the market accurately reflect all the relevant information pertaining to a traded security so that they continue to assign a fair market value to the securities, regardless of what the security's actual price is.

There is no way to predict a precise market response to all relevant information about a particular market or stock, even if that information was available. In a world with so many factors interacting, it is easy to overlook important ones in favour of those considered to be the "flavour of the day." Except for shocking news such as natural disasters or acts of God, the technical analyst believes that all relevant market information is reflected (or discounted) in the price.

However, these factors are quickly discounted. The financial markets have trends, momentum, and patterns that repeat over time, not precisely in the same way but similarly. Self-similar charts show the same fractal structure (a fractal is a tiny pattern; self-similar charts are made up of smaller versions of the same pattern), whether in stocks, commodities, currencies, or bonds. Rather than reflecting fundamental factors, charts reflect the mood of the crowd. It can therefore be said that technical analysis is the study of human mass psychology. Consequently, it is also referred to as behavioural finance.

3 The Different Types of Charts

When you analyze the forex market, you will likely come across charts with several lines and indicators. They may seem overwhelming at first. But there is nothing to worry about. The use of charts allows us to communicate information quickly and understand the market better. In Forex analysis, there are several kinds of charts. Depending on your trading style or the type of analysis you are doing, you might find that one chart may be better for your needs than another.

In general, there are three types of charts:

Line Chart

Bar Chart

Candlestick Chart

Let's take a closer look at each of them in greater detail.

6 Trend lines

During the previous lesson, you learned that support and resistance are the areas where the price has been unable to break through. So how can you predict which direction the price will most likely move?

To determine the market's direction, we use trendlines in technical analysis. The first step toward making a successful trade is identifying the trend. The problem is that markets do not move in a straight line but change in a zigzag pattern as they make tops and bottoms.

Market direction

The direction of price movement can be identified by drawing trendlines over pivot points of high price movements and under low price moments. The pivot points of high prices are known as market tops, and the turning points of low prices are known as market bottoms. If you follow this strategy, you will figure out the direction in which the price is moving and the pace at which it changes. Furthermore, it is also possible to detect additional levels of support and resistance within the pattern itself.

7 Basis of reversal chart patterns

What are chart patterns?

Chart patterns are the most commonly used type of technical analysis. Pattern recognition is one of the most popular methods used for price action analysis. It is easy to find dozens of them across a chart.

Whenever a market hits a significant support or resistance zone, it might either bounce off or break through that level.

Because markets are unpredictable, it is not always possible to predict the next move correctly. However, one of the good things about technical analysis is that chart patterns tend to repeat themselves. So, it is possible to gather clues about what the price will do next if you recognize these patterns and notice when they emerge.

Patterns in charts are the result of human behaviour. When a pattern is formed over time, showing areas of resistance and support. There is a tendency for similar patterns to reappear as they are usually caused by the same behaviour and factors, and these factors have the same effects. This allows traders to predict the price movements of the currency pair with greater accuracy.

However, it should be noted that these patterns are by no means foolproof and should only be used as a guide to a market's future direction.

Types of chart pattern

There are two broad categories of chart patterns. Reversal and continuation patterns and both types can be found across any time frame.

Reversal patterns are those that signal a trend may be about to reverse.

Continuation patterns are those that demonstrate a consolidation or pause during a trend.

In the following lessons, we will examine reversal and continuation patterns in greater detail.