Indicators

Topic 7

What Does a Technical indicator offer?

- Technical analysts use indicators to look into a different perspective from which stock prices can be analyzed. Technical indicators provide unique outlook on the strength and direction of the underlying price action for a given timeframe.

Why use indicators?

- **Technical Indicators broadly serve three functions:**
- to alert, to confirm and to predict.
- Indicator acts as an alert to study price action, sometimes it also gives a signal to watch for a break of support.
- A large positive divergence can act as an alert to watch for a resistance breakout. Indicators can be used to confirm other technical analysis tools.
- Some investors and traders use indicators to predict the direction of future prices.
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Tips for using indicators

- Technical Indicators that can be used to assist you in selection of stocks and in tracking the right entry and exit points. But it doesn't mean that traders should ignore the price action of a stock and focus solely on the indicator.

- They are derivatives and not direct reflections of the price action.

- While applying the indicators, the analyst should consider: What is the indicator saying about the price action of a security? Is the price action getting stronger? Is it getting weaker?

- It would be a futile exercise to cover more than five indicators.

Types of indicators

- Indicators can broadly be divided into two types "LEADING" and "LAGGING".

Leading indicators

- Leading indicators are designed to lead price movements.
- Benefits of leading indicators are early signaling for entry and exit, generating more signals and allow more opportunities to trade.
- Some of the wellmore popular leading indicators include Commodity Channel Index (CCI), Momentum, Relative Strength Index (RSI), Stochastic Oscillator and Williams %R.

Lagging Indicators

- Lagging Indicators are the indicators that would follow a trend rather then predicting a reversal.
- A lagging indicator follows an event.
- These indicators work well when prices move in relatively long trends.
- They don't warn you of upcoming changes in prices, they simply tell you what prices are doing (i.e., rising or falling) so that you can invest accordingly.
- These trend following indicators makes you buy and sell late and, in exchange for missing the early opportunities, they greatly reduce your risk by keeping you on the right side of the market.
- Moving averages and the MACD are examples of trend following, or "lagging," indicators.

Thank you