WHAT IS TECHNICAL ANALYSIS?

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It is possible that what is now called technical analysis, or market analysis, is the oldest form of financial analysis in the world. Several centuries ago in the corn markets of England and the rice markets of Japan traders developed a method of recording transactions that would enable them to see at a glance how much people had been paying for the product. With the help of that information they were able to assess where supply and demand were in balance and thus see better what price they should agree for their future transactions. The form that this monitoring took was a series of markings on the page at different levels to represent prices as they rose and fell. The result was something very close to a modern "point and figure" chart, one of the best tools technical analysis have at their disposal.

Those who invest or trade in financial markets know that the only way to make money is to get a higher price when you sell than you paid when you bought. It sounds simple but it isn't or there would be more millionaires. In recent years a great deal of attention has been paid to fundamental analysis, that is the attempt to estimate the value of a currency, a share or an entire equity or bond market based on profitability, management or economic strength, and future prospects. The assumption of this approach is that value is the sole determinant of price. In fact price and perceived value are rarely in equilibrium. Prices are set by supply and demand, and they represent all that is known, feared, and hoped for by the market as a whole and its individual participants. Despite the now discredited random walk theory that posited the impossibility of predicting future prices due to their supposed random action, prices actually move in widely acknowledged trends. Where fundamental analysis focuses on value, technical analysis concerns itself with price, volume of transactions and individual/group psychology. Part of this discipline involves the charting of historic prices for all markets and individual items; part is concerned with the statistical analysis of price and volume time series and part with the examination of the current emotional state of the relevant market in its continuous battle between fear and greed.

Analysing price charts includes identifying short, medium and long-term trends, pinpointing future potential trouble areas where consolidation shows that supply and demand have been evenly balanced in the past and calculating price targets. Successful chart reading is greatly enhanced by the use of computer-based statistical analysis which creates oscillating indicators showing overbought/oversold conditions, the pace and direction of momentum and the relative performance of one item against another or against the market. These indicators measure how fast, how often, how many, how much and so on and give a measurement of the heat and speed of the market, as well as identifying the best and worst constituents at the time. As a result, even for the convinced fundamentalists, performance can be enhanced by deciding *when* it is desirable to buy or sell items that have been identified as attractive or dangerous in terms of value.

One of the many attractions of technical analysis is that its methodology can be applied almost identically in any market anywhere. The same techniques can be applied to currencies, commodities, bonds, interest rates and equities. They work as well in Japan as in Europe, in developed or developing markets. Data availability and reliability are the only obstacles to a universal application of methods and techniques. Success in the market, however, has another more insidious obstacle to overcome. Crowd behaviour, as shown in panics and periods of euphoria, can distort not only perceptions of a realistic valuation for markets, but also realistic price levels, given all the information being offered by price time series analysis. All forms of analysis rely heavily on historical data, but normal expectations based on past events can be confounded when market hysteria occurs. Even worse than this is personal mental and emotional weakness when it comes to making investment decisions. The study of mass and individual market behaviour and psychology is a branch of technical analysis, though as with so much of the methodology of technical analysis, there are some signs of poaching from the quantitative analysts in this area.

Bar charts, point and figure charts, candle charts, swing charts, volatility, momentum or relative analysis, Elliott waves, Gann angles and levels, an understanding of normal or extravagant behaviour - they are all tools available with a study of technical analysis and they should all lead to better investment profits given consistent and intelligent application.