Fibonacci Retracement levels are well known in the stock market. They are derived from the Fibonacci sequence, a series of numbers first observed by Leonardo of Pisa in the fifteenth century. These levels are made up of 6 percentage numbers or lines and are calculated based on the preferred trading period. Once the bottom and top of an uptrending stock are identified, the retracement levels between the highest price and the lowest price are calculated. Nowadays, this can be done with a simple click of the mouse. ChartNexus is a tool that offers free end of day data and allows for the drawing of Fibonacci Retracement levels effortlessly.

The most significant levels are 38.2%, 50% and 61.8%. Beginners should be aware that the lack of a comprehensive trading strategy or technical knowledge leaves them exposed to high risk. Experienced traders understand the behavior of the stock market well and know how to anticipate price movements. For example, some stocks may form a chart bottom before resuming the uptrend, while others may experience a strong bull trend.

In the current market conditions, ChartNexus can be an effective tool for identifying chart bottoms and the best time to enter the market. It helps traders to time their trades better and manage and minimize risk.
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make higher high and higher low. Fibonacci Retracement is used to identify the price level as it retraces to a higher low before testing the higher high. The first possible level of support for a retracement is usually the 38.2% line. The following figure below illustrates how the 38.2% line is effectively tested as support in the chart of China Energy.

In the figure above, China Energy began to pullback after forming a top from May 2007 to early June 2007. On 12th June 2007, the stock tested the 38.2% level and subsequently rebounded off the level. Again, from 24th to 25th June 2007, the stock tested the 38.2% level a second time and rebounded off it. 38.2% in this case served as a very strong support for China Energy.

The following figure shows Tech Oil & Gas rebounding after hitting the 61.8% line.

However, the 61.8% line is also known as the last line of defense for the stock price. A break below the 61.8% line usually means that the uptrend of the stock is negated. In Figure 3, Luzhou broke the 61.8% line on 1st March 2007 (in red) and the stock price went down further thereafter.

As observed from Figures 1 & 2, Fibonacci Retracement Levels offer very strong support or resistance to the price movement. In Figure 3, we can see that Luzhou’s stock prices were able to find good support at the 50.0% line from Oct 2006 to Jan 2007. However, in the month of March the 50.0% line turned from support to resistance, resisting Luzhou’s price from heading higher. Similarly in the month of April, Luzhou’s price found resistance at the 61.8% line and went into a downtrend shortly thereafter.

The Fibonacci Retracement levels can also be used in conjunction with other indicators to help in analyzing the stock chart. This is known as confluence of signals. The combination of other indicators further enhances and compliments the usage of Fibonacci Retracement levels thus resulting in higher probability of a successful trade. In this article, one of the popular indicators used by many traders, the 100-day moving average is used to analyze the stock chart of Tech Oil & Gas which is shown in Figure 4 below.

Figure 4 clearly shows that the prevailing trend of Tech Oil & Gas is an uptrend and that the price found support on the 100-day moving average from May 2007 to July 2007. The next observation is that the price was trading near the 61.8% Fibonacci Retracement level. While the 100-day moving average is supporting the price movement, Fibonacci Retracement is also providing support at the 61.8% level which is about the same price level as the moving average line. Hence the price is said to be very well supported because we have the confluence of two types of analysis, namely moving average and Fibonacci levels.

This article has highlighted the importance of understanding the stock market behavior in order to enhance one’s timing of the stock market. A powerful tool such as Fibonacci Retracement is widely used to identify possible support and resistance to the price movement. This helps experienced traders to buy low and sell high. In addition, the usage of the Fibonacci Retracement line together with the concept of support and resistance level and the confluence with the 100-day moving average helps to forecast the possible price movement and increases one’s confidence to take the trade. SI

Figure 3: Using Fibonacci Retracement lines as support and resistance level

Figure 4: Using Moving Average with Fibonacci Retracement level

Making money from the stock market has never been easy. If you have been seemingly buying high and selling low, ending up not making money in the stock market after years, why not start changing your approach and brush up on Technical Analysis. This two-day (16-hour) course will guide you through the basic to the more advanced concepts in technical analysis so that you will be armed with comprehensive trading strategies to identify the bullish and bearish signals in the market.

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