

Technical Analysis IV: Identify the Market Trend

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Three Phases of Major Trends

A trend represents a general direction of the market. Dow Theory asserts that major trends have three distinct phases: accumulation, public participation and distribution.

The accumulation phase represents the first part of the trend in which those who are well-informed buy or sell. In other words, if the well-informed recognize that

the recent downtrend is soon coming to an end, they would buy, and vice versa.

The public participation phase involves the masses following the major trend. This occurs as prices begin to accelerate rapidly and there is news supporting the trend.

The final distribution phase occurs as the news highly favors the current trend and speculative volume and public participation increase even further. At this point, the well-informed investors who

accumulated when the market was at its peak (trough) begin to sell (buy) before other investors begin to follow suit.

A Trend Is Assumed to Be in Effect Until It Gives Definite Signals That It Has Reversed

This is a major theory that essentially mirrors the physical law stating that an object in motion tends to continue in motion until some external force causes it to change direction. Relating that principle to price trends, a strong trend will tend to continue in its current direction unless there is a price reversal indication, as per technical or even fundamental analysis. The later articles will focus on learning to spot reversals in the market and how traders can place orders to take advantage of such reversals.