

Research Paper



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PRICE RETRACEMENT IN LIQUIDLY TRADABLE STOCKS IN THE MARKET THE SIGNIFICANCE OF 50% PRICE RETRACEMENT LEVEL IN TRADING



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A large number of traders, especially day traders utilize *Fibonacci levels*[1] while trading. The most common Fibonacci levels are 23.6%, 38.2%, 50%, 61.8%, 78.6% and 100%. These levels will often prove to be *support*[2] or *resistance*[3], which provide the springboard for a security to continue in the direction of the primary trend. The Fibonacci level that has received the most notoriety is the 61.8% retracement level. While there are a number of *price retracement*[4] & *price extension*[5] levels including Fibonacci levels known by *professional traders*[6], the fifty percent level proves to be more significant. It is a natural trading intuition to buy a stock when it retraces half of its previous move. This basic trading principle is found in many trend following trading styles. This article will focus on *long positions*[7], but the same principles can be applied to *short selling*[8].

While there are a number of retracement & extension levels including Fibonacci levels known by professional traders, the fifty percent level proves to be more significant. Out of the 200 cases of retracement considered for this paper, 112 cases, had retracement level around 50 %. This is precisely 56 % of the sample size.

Identifying Reliable Fifty Percent Retracement Levels: Traders will often look for a fifty percent retracement of any move and think

that it is a great buying opportunity. There are a number of factors that go into identifying when a fifty percent retracement level has better than average shot of providing the necessary support to keep the trend intact. Below are a few basic tenets for identifying such support.

Range of Recent Swing Points: The most recent *swing high*[9] and *swing lows*[10] must have a significant distance between them. This will ensure that traders are not getting into a *choppy trend*[11], where price will penetrate any and every Fibonacci level. This also provides with a safety net that when the *security* resumes the *primary trend*[12], there is ample room between the 50% and 61.8% retracement levels. Also, even if the security is only able to *double top*[13], it will ensure a hefty gain.

Decreased Volume on test of Fifty Percent Retracement Level: When the security is pulling back to the fifty percent retracement level, the *volume*[14] should begin to drop off. This implies that the selling pressure has subsided and that the primary trend is ready to resume. Many traders want to buy the test of the 61.8% retracement, but stocks that are able to hold their 50% retracement level are more *bullish*[15] as the security had a smaller retracement. The NIFTY chart indicates 13th July 2009 as the bottom with 3rd August 2009 as the top. 50 % retracement level is 4333.50



against the actual 4342 on 19th August 2009. Out of the 200 cases of retracement considered for this paper, 112 cases, had retracement level around 50%. This is precisely 56% of the sample size.

Identify other Areas of Support The 50% retracement level has even more significance when

it coincides with another form of support. These forms of support can come in the form of *trendlines*[16], *gaps*[17], *moving averages*[18] or *previous tops*[19] or *previous bottoms*[20]. The confluence of multiple support levels increases the odds that the security will resume its primary trend.

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