G91-1056 Support and Resistance Areas, and Will the Market Give Us a Second Chance?

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NebGuide

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Support and Resistance Areas, and Will the Market Give Us a Second Chance?

This is the sixth of nine NebGuides designed to aid producers in starting to use technical analysis in their marketing plan.

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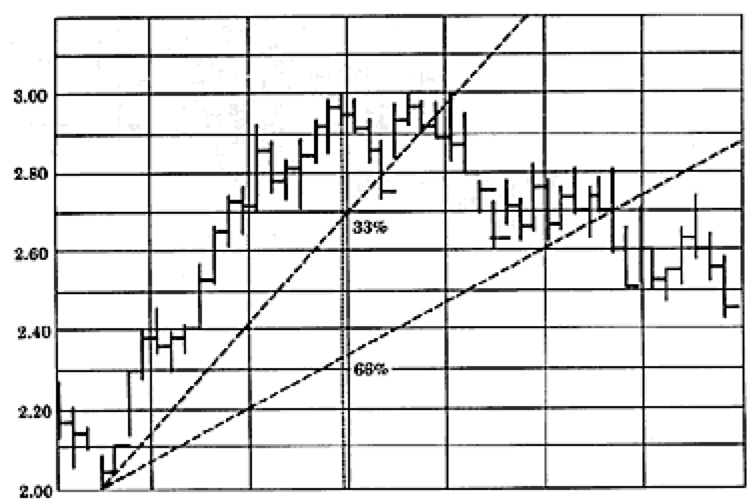
Among the most frustrating aspects of marketing are missed opportunities for good prices. These occur because producers becoming overly optimistic. This optimism stems from the belief that a bull market will keep going up.

Ultimately, the market ***does*** change direction -- it does so many times before the producer has priced his crop. This NebGuide examines where to draw additional support and resistance lines beyond the support and resistance trend lines explained in the second NebGuide in this series. Some "will the market give me another chance" possibilities also are explored.



No market moves straight up or straight down (see *Figure 1*). Even in a strong bull market, the market retrenches or takes a breather. When this happens, the market often breaks through the up trend line.

Figure 1.

The producer will not know if this simply is a breather before another up move, or the time to bail out. Speed resistance lines can be an important tool for answering this question. In our illustration, the market moves from $2 to $3 following the up trend line before falling through the line.

The critical questions to ask are:

- is the market all over or just taking a breather?
- if it is taking a breather, how far is it likely to fall before recovering?

The mathematical procedure is to measure the move, up to $1 in this case. Multiply that by 33 percent, or 33 cents in the example. Subtract this amount, 33 cents, from the high, $3 Place a dot representing 33 cents directly below the high and draw a line from the starting point of the move through the 33 percent dot on the graph. Draw in a 66 percent line. These new lines will become either support or resistance lines.

If the market falls down to the 33 percent line and does not close below the line for two consecutive days, the odds are the market will go back upward, using the 33 percent line as the new trend line or support line. This gives the producer a chance for higher prices.

If the market ***does not*** reach new highs, the 33 percent line generally will give producers a second chance to approach the previous highs. If the market, as shown in the illustration, falls through the 33 percent line, the 33 percent line then becomes an upper resistance line and the percent line becomes the lower support line. Since markets generally list both support and resistance lines, the odds are high the market will move downward to test the support levels on the 66 percent line. If it closes below the 66 percent line, a major down trend has been confirmed.

Usually, at this point, most producers are saying, "why didn't I do something?"

What are the odds the market will give producers another chance to recover at least part of what they missed? Since markets rarely continue on a straight downward movement, there is some chance to recover.

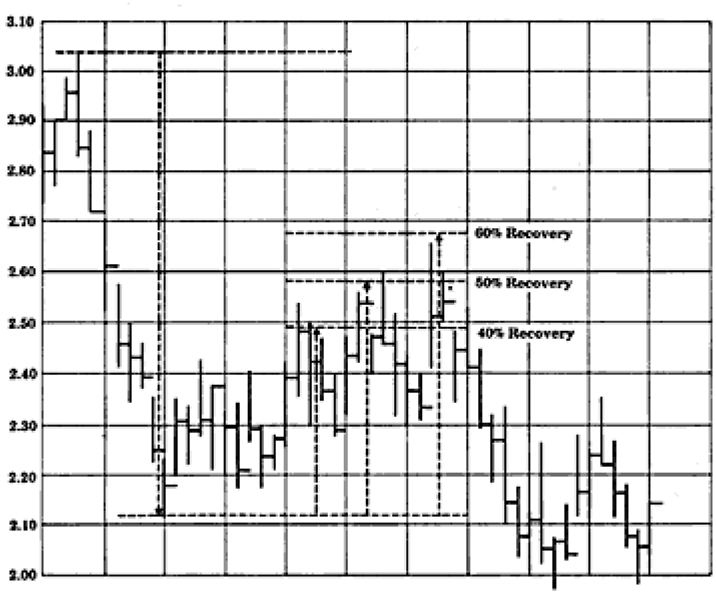


Figure 2.

After a major downward move producers, along with the rest of the world, feel markets will go even lower. ***Historically, markets retrace some territory of a lost move.*** The odds indicate that after a major down move, prices will recover 40 percent of what was lost 60 percent of the time.

For example, (see *Figure 2*) if the market fell $1, it would recover 40 percent of that $1 fall 60 percent of the time. To continue the odds, 50 percent of a price move will be recovered 50 percent of the time. In the example, 50 percent of the time producers could expect the market to come back $.50.

Consequently, there is a 1/3 chance the market would recover 60 percent of what was lost ($.65 in the example) when the market fell apart.

Watch the market closely when following a procedure.

If, for instance, the market explodes through the 40 percent line with vigor and enthusiasm, the odds are in its favor to reach the next level. But, if the market has a hard time getting through the 40 percent line and is in a minor sideways trend, the odds decrease that the market will recover to the next level.

Conclusion

Producers can use trend lines as indicators of how far the market will fall. After the fall, trend lines can be used to estimate either recovery or continued downward movement. Predicting resistance and support lines gives producers a barometer to gauge the market.

Markets generally stall out in a major down trend and give producers a second chance to recoup some of the lost opportunity. To accomplish this, producers must watch the market carefully during retrenchment and not let hopes and wishes override solid marketing strategy.

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