1991

G91-1052 Determining Market Trends

Lynn H. Lutgen
University of Nebraska - Lincoln

G91-1052-A

Published by Cooperative Extension, Institute of Agriculture and Natural Resources, University of Nebraska-Lincoln

Determining Market Trends

This is the second of nine NebGuides discussing basics of technical market analysis and benefits of following market trends to aid decision-making.

Lynn H. Lutgen, Extension Agricultural Economist - Marketing

- Drawing the Uptrend Line
- Drawing the Downtrend Line
- Conclusions

Most livestock and crop producers are not "day traders" -- participants in the market on a daily basis -- nor should they be. A typical producer may enter the market only a few times in a marketing year, or only once, as when selling the crop at harvest.

Because producers are not day traders, market trends are one of the most valuable tools, or indicators, that can be obtained from correctly executed charts.

Trends determine the direction the market might take for an extended period of time. A trend usually continues until some major economic force enters the market, causing a change in direction.

For example, if the United States has huge surplus stocks of corn, producers can expect a sideways (horizontal) price trend until either a severe drought or a dramatic increase in world demand lowers the surplus. Either of these developments, or a combination of the two, would cause the market to move from a sideways trend to an uptrend.

You can get a feel of the direction the market is taking by simply listening to market news on the radio. But charts provide a visual display of price movement that gives you, as a farm business operator or owner, a much better understanding of market trends. This is similar in principle to a road map, which shows specific twists and turns in the road, instead of just the general direction the traveler is going.

The three basic trend lines -- sideways, uptrends and downtrends -- also are classified as to the time frame of trend patterns, because markets never move continuously in a smooth pattern. There are short-term, intermediate and long-term trends.

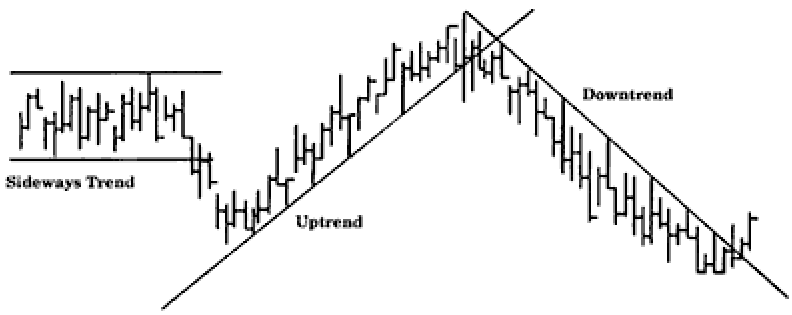
An example of trends within trends would be a short-term downtrend within a long-term uptrend in the market. A short-term trend generally is defined as lasting less than 20 days; an intermediate trend from

one month to a maximum of six months; a long-term trend continues six months or more.

Producers can plot trend lines on either a daily or weekly market chart. It's an individual decision on how much information is needed to fit the marketing needs of a particular enterprise, and how much time can be spent in charting.

The sideways trend is usually the longest running trend in the grain market. This is generally due to the presence of large surpluses, accompanied by a steady demand pattern that does not lower the surplus level at a significant rate. Based on fundamental factors, intermediate and long term sideways trends normally appear at the bottom, or close to the bottom, of a trading range.

Here's an example of market price fluctuations over a sustained period of time, with sideways, uptrend and downtrend lines (*Figure 1*).



Note that when drawing a sideways trend, two lines must be drawn (over the top and along the bottom), versus only one line -- at the bottom and top, respectively -- for up or down trends. The top line is drawn across as many highs as possible and the bottom line is drawn across as many lows as possible.

These lines become support and resistance lines challenged when the market breaks out of a sideways trend. At this time the market generally makes a significant move, either up or down through these lines.

Sideways trends can be frustrating for producers, especially because they occur at the bottom of the market. Sellers are always waiting for uptrend lines while buyers are holding out for downtrend lines.

Drawing the Uptrend Line

Draw the line along the bottoms of the market movement, connecting as many points as possible. The basic uptrend line serves two important functions:

- it shows the steepness of the upward direction;
- it is an indicator of how high prices might go, as long as the line is not broken.

The uptrend line is also a support line because it is drawn at the close of rallies. This is important: **If the market closes two days in a row below the line or if the market is breaking through the support, the market can be expected to reverse its course.**

Caution: the market may not immediately run into a downward trend because rising markets generally have one last gasp at trying to continue upward before switching to a downtrend.

Drawing the Downtrend Line

As shown in the example, draw the line along the tops of rallies and connect as many points as possible. Because the market has difficulty penetrating this top line, it becomes a resistance line. **Expect a change in market direction if the market closes above the downtrend two days in a row.**

Note: Downtrend lines often turn into sideways trend lines.

Conclusions

It is important to draw in both long-term and short-term trend lines. Knowing the direction prices are moving is one of the first steps in achieving a successful marketing plan. Trend lines give a strong indication of what can be expected in the future.

File G1052 under: FARM MANAGEMENT
K-25, Marketing
Issued December 1991; 6,000 printed.

Issued in furtherance of Cooperative Extension work, Acts of May 8 and June 30, 1914, in cooperation with the U.S. Department of Agriculture. Elbert C. Dickey, Director of Cooperative Extension, University of Nebraska, Institute of Agriculture and Natural Resources.