Fibonacci Tool Basic

This guide is meant to help understand the basics of the fib tool and represent how they are placed on the chart.

First there is nothing magical or no secret set of numbers as to the reasons that fibs are used in trading. It is simply a measuring tool, if you need magic or psychic help trading you need to call the 1900 numbers to get the next direction of the markets, better yet just flip a coin.

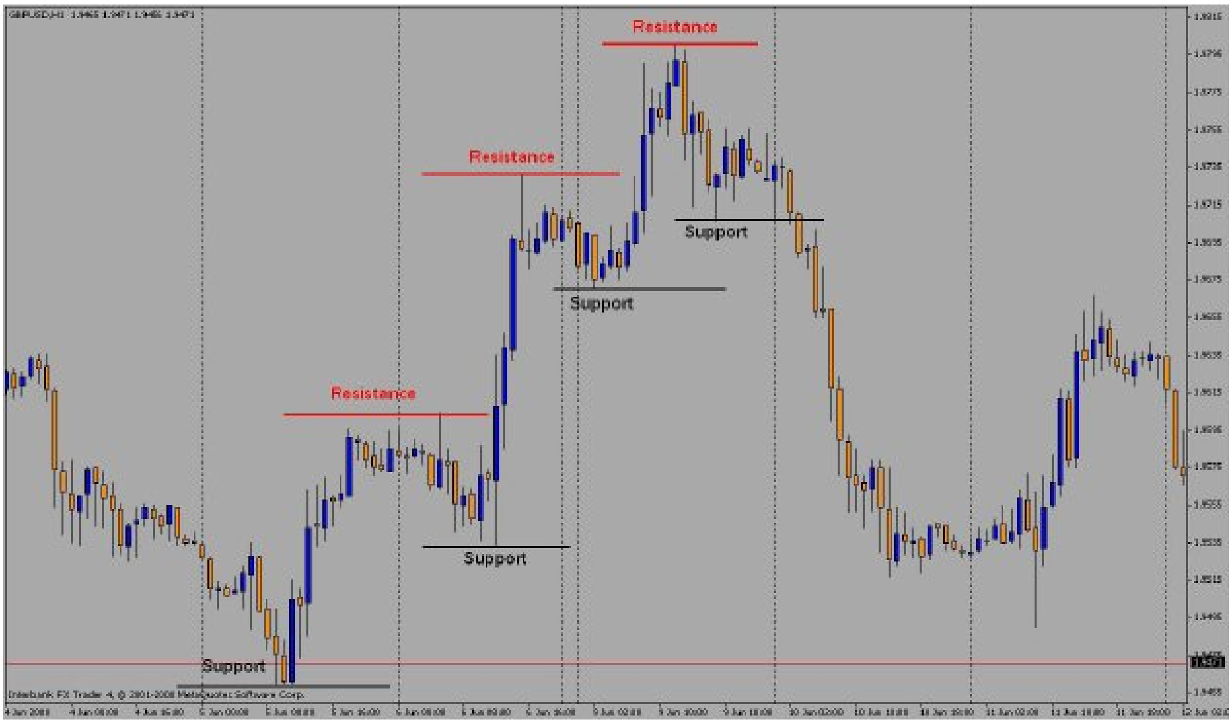
Two points you need to understand;

1. The market moves from economic conditions and is displayed in economic indicators that you see reported as the news. This sets the market in its motion. Not always will you see a pair going in the direction it should from day to day news announcements for the simple fact something is trumping it or it is not significant enough to change the current sentiment.

2. Indicators, fib tools, candlestick formations do not move the market they are merely showing you entry and exit points. Most of the time new traders have so many indicators from so many different systems or methods that they

have a confused situation, its evident in the questions you see asked on the forums here.

Me personally I trade based off support and resistance. If you don't know what support and resistance is it's the areas on the chart you see price reversing its direction at. Support is what forms below price; Resistance is what forms above price.



I use Fibonacci as a guide to trade support and resistance. The fib tool is drawn from a resistance point to a support point. I have renamed the levels of the fib tool to suit the job I want the tool to accomplish.

The fib tool is a representation of support and resistance as viewed from a horizontal plane, perfect for my style of trading. The point of renaming the levels is that no matter if you draw the tool by starting at the top and pulling to the bottom or the bottom and pulling to the top the levels will be in the same place and by renaming the levels of the tool you can always draw from the high point (resistance) to the low point (support).

The normal levels of the fib tool are not actually Fibonacci numbers but derivatives of the Fibonacci numbers, there are the most common numbers used 0, 23.6, 38.2, 50, 61.8, 76.4, and 100. Then there are the extensions 138.2, 161.8. Nothing magic about them other than the fact these levels have proven to be used over time and still are.

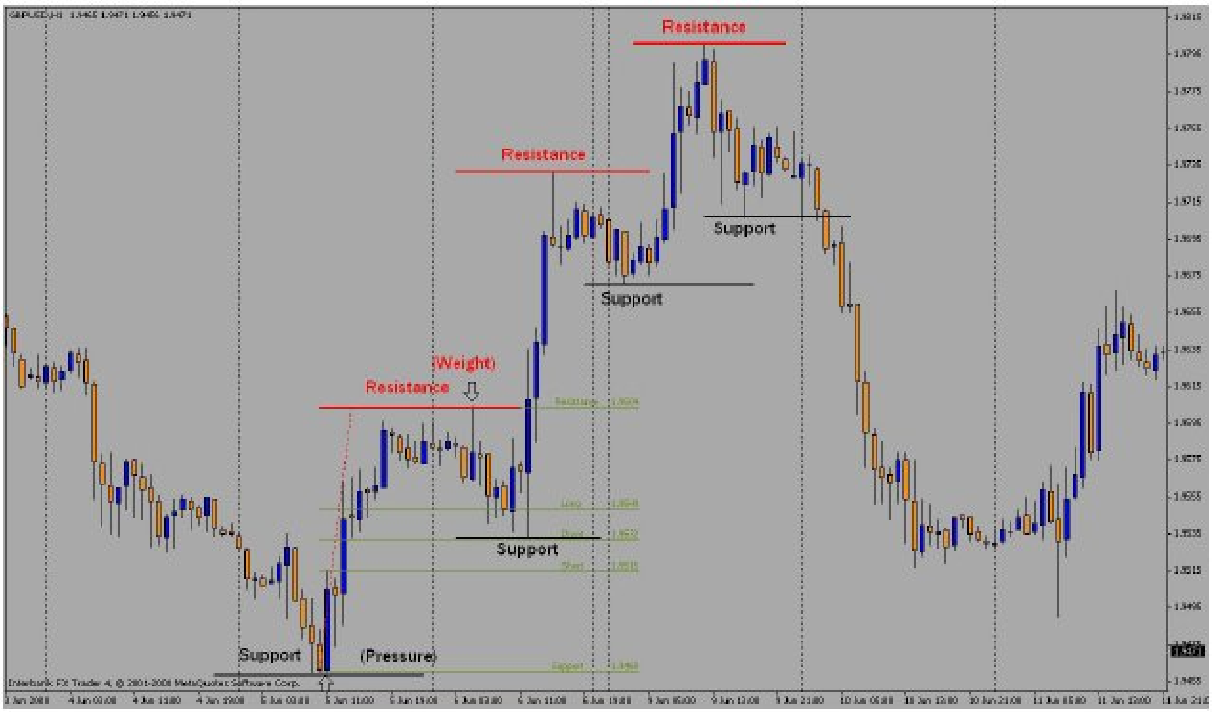
Me personally I do not use all the numbers since they serve no purpose for what I use them for. I don't use the 23.6 or the 76.4. Also leaving the description in the form of a number can be confusing if you are always pulling from high to low because leaving the numbers and pulling from low to high the numbers will be backwards.

Renaming them to represent what I want the tool to show me long and short solves this as well. A better way to describe the fib tool is more of a balance measurement between a long and a short condition. I've used this analogy before and its if you imagine the playground seesaw and how it works by when more weight is applied to one side it tends to tip into the direction with the more weight on it, now applying pressure from the other side it will try and tip to the other side and if enough pressure is applied it will tip over to the other side and reverse.

The fib tool is just a representation of this simple concept in the sense that if more bullish pressure is applied the pair will tend to tip into a bullish condition, if enough bearish weight can be applied in the opposite direction to the bullish pressure it will attempt to tip in the bearish direction from the weight over coming the pressure.

The balance point always being the 5o fib level (renamed Pivot). If you remember once the seesaw was almost in balance or almost tipped to the other side it always required that extra oomph to push it on over to the other side, without the extra oomph it fell back to the direction it was in. That extra oomph is what the Long and short levels represents once it gets past the oomph part it would reverse and go to the other side.

Now with this fresh in your mind we will apply this concept to the support and resistance chart posted earlier. First chart here shows we place the fib tool by starting at the resistance point and pulling down to the support point, so we can see the balance points between long and short (fibs inner levels Long, Pivot, Short). This is the optimum place we want price to go after each movement it makes, ideal conditions are a movement then a retracement, a movement then a retracement.



The highlighted area is where we want price to go in an ideal condition. This chart shows the inner levels where we want to make our entries from.

What happens in this instance is the ideal condition, price visits the inner levels. We have an indication of a bullish move from the price we are measuring so we would be expecting price to bounce.

A bounce is when price is above the inner levels fall to them and bounces off like a ball….hence bounce. A bounce is not when price is below the levels goes up test them and then falls again that's a rejection…just like when a center in a basketball game rejects an opponent from dunking in the basket, he rejects the opponents shot.

But we want to look at this in weight and pressure, weight makes it go down … pressure makes it go up. In this example weight was applied to the pressure from the buying, but once we reached the balance point enough pressure is reapplied and overcomes the weight again and we get the bounce, this is your entry once you get use to recognizing this.

There is no certain way or method to enter here you just simply need experience trading the market and over time it will become natural because there are so many things that affect its movement fundamentally you have to be aware of. It's called learning the market you're trading. I get a lot of what if this or this or this happens.

There is no way to answer this because there are too many reasons why to enter and why not to enter that we could go on and on for days on end trying to describe all the condition you will face as a trader. Safest entry in my opinion is a break or a candle opening past the levels but even this is not perfect and you have to be able to read what's going on to decide your entry…once again experience as a trader and knowing the market your trading. I can’t teach you to trade only show you the tools I use and how I use them.

Now that enough pressure has been applied and it overcomes the weight price will resume the direction it was in. up.

Now we get to the extensions, the 138.2 and the 161.8. When we are in a trending market you will see this more often and that's price reaching the extensions. Initially I would recommend taking profits out at T1, unless price clearly blows through T1 and then target T2. T1 is the 138.2 and T2 is the 161.8 level.

This next chart shows the Target ranges or points, taking profits out here is the smart move and don't worry about what happens after this. You've made a good profit and its time to just watch so you can get ready to set up again from this move.

Trying to get ever single pip is a big mistake. There's nothing magical about the extensions either, to understand the concept think of being in a retail business. You want to buy at a wholesale price then sell at a retail price. To apply this to this fib tool the inner levels of the tool 38.2, 50, 61.8 are where price becomes a bargain into the trending price. The extensions 138.2 and 161.8 are the point where price meets the retail value, but in the world of forex this works in both directions.