

**Technical Analysis:  
an antidote to human nature**

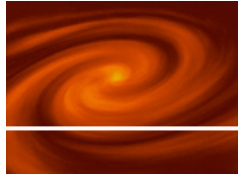
**ERM**

**15 March 2011**

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**United-ICAP**

**Walter J. Zimmermann Jr.**



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“Amass a store of wealth,  
and no one can protect it.”

Lao Tsu,  
Tao Te Ching  
verse 9

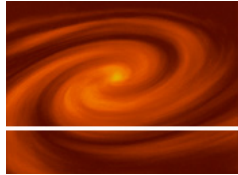
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## *Prices for Equities and Commodities...*



*are a Tug of War ...*



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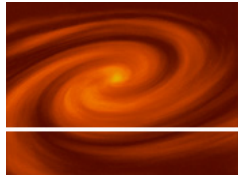
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***Prices for Equities and Commodities  
are a Tug of War Between***

***Fears  
of  
Deflation  
and a  
Bear Market  
Contraction***

**Market  
Price**

***Hopes  
for  
Re-flation  
and a  
Bull Market  
Expansion***



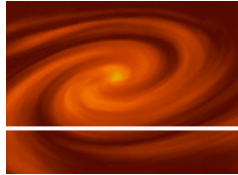
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**Inflation  
Hopes**

**The Market Price  
is a  
Consensus Opinion**

**Deflation  
Fears**



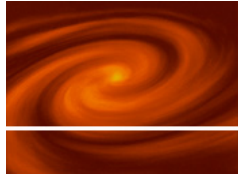
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**Prices Are Rising ...  
So Spending Now  
Saves Money**

**Inflation is a  
Consensus Opinion,  
a Collective Mood**

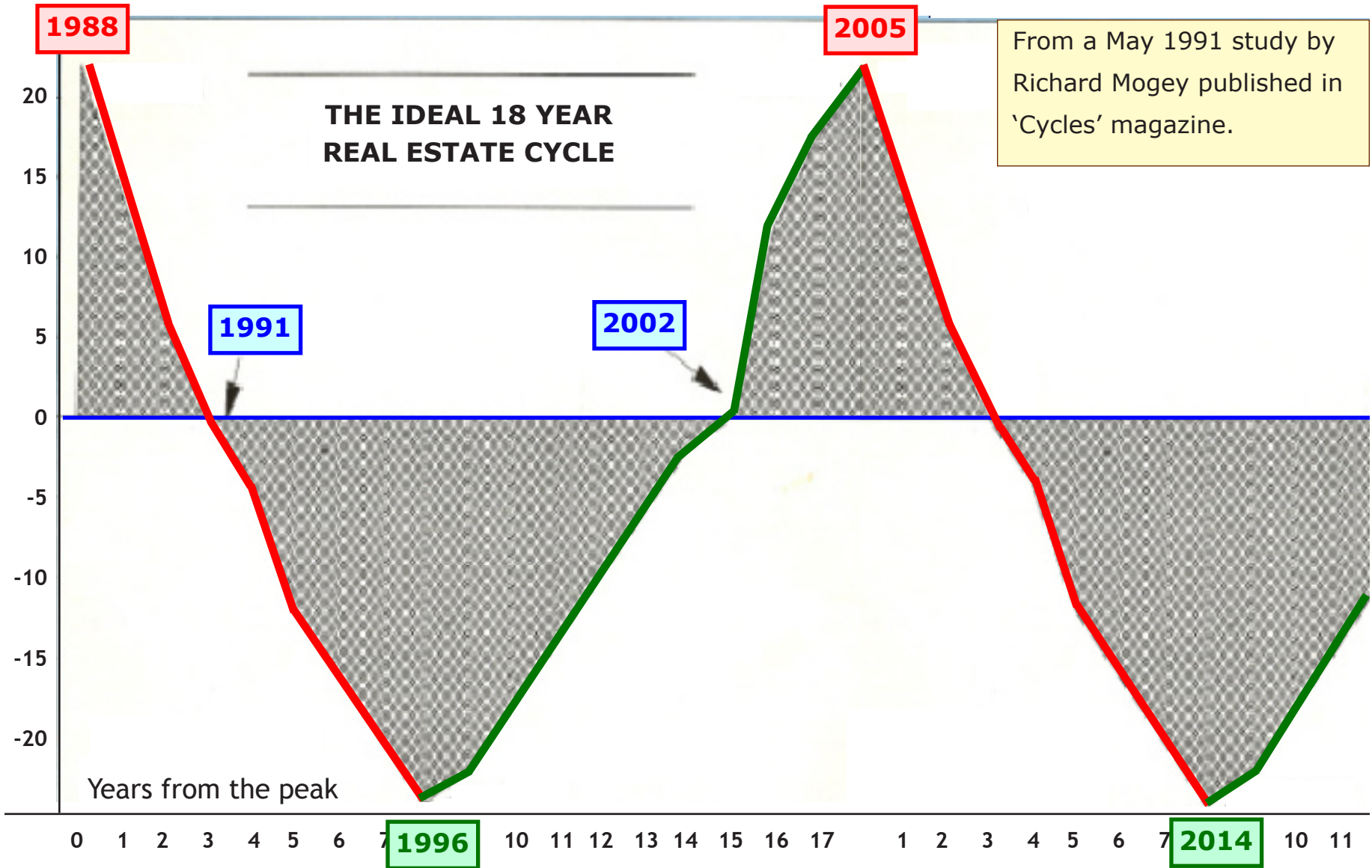


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**Deflation is a  
Consensus Opinion,  
a Collective Mood**

**Prices Are Falling...  
So Waiting to Spend  
Saves Money**

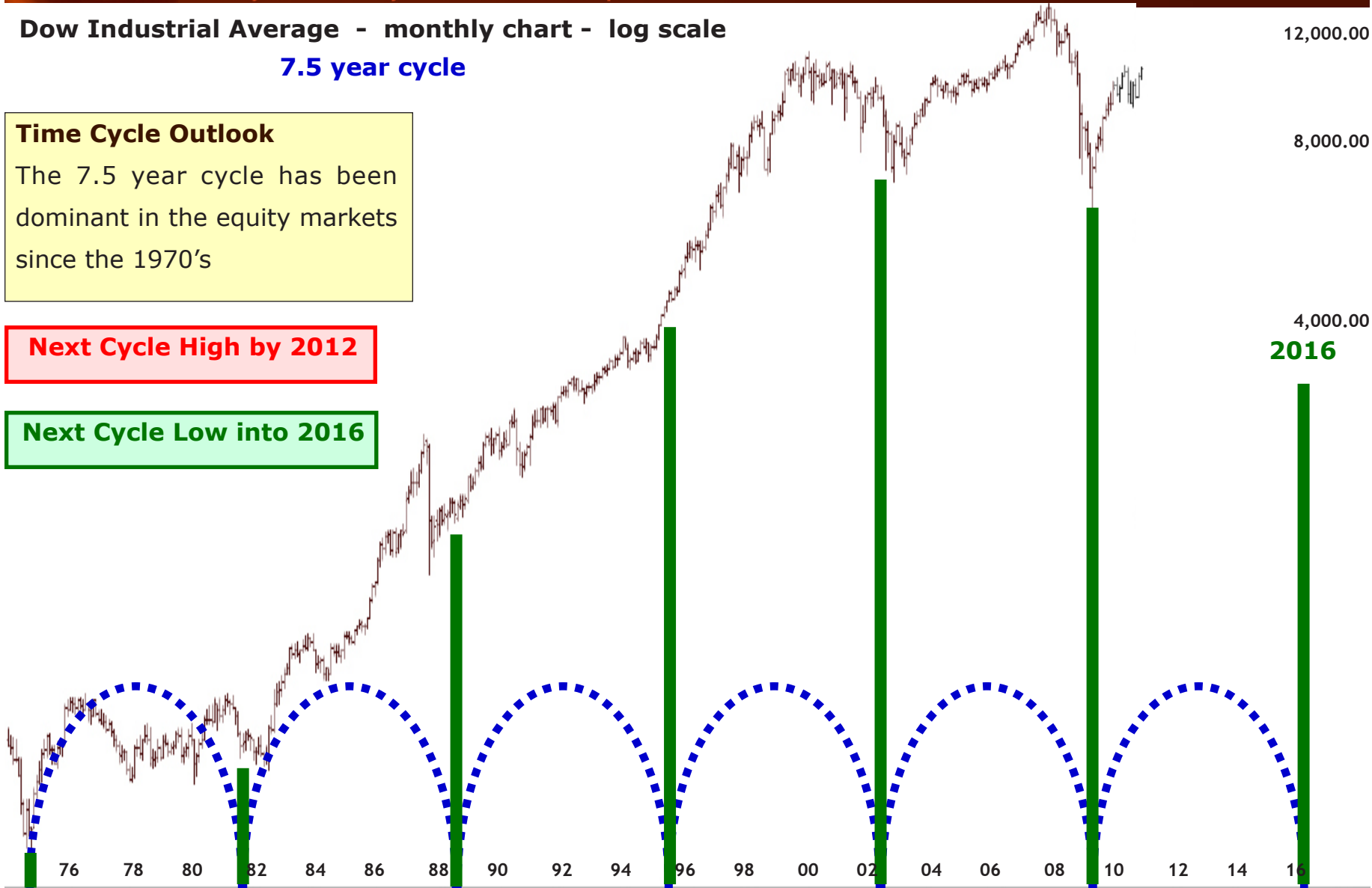


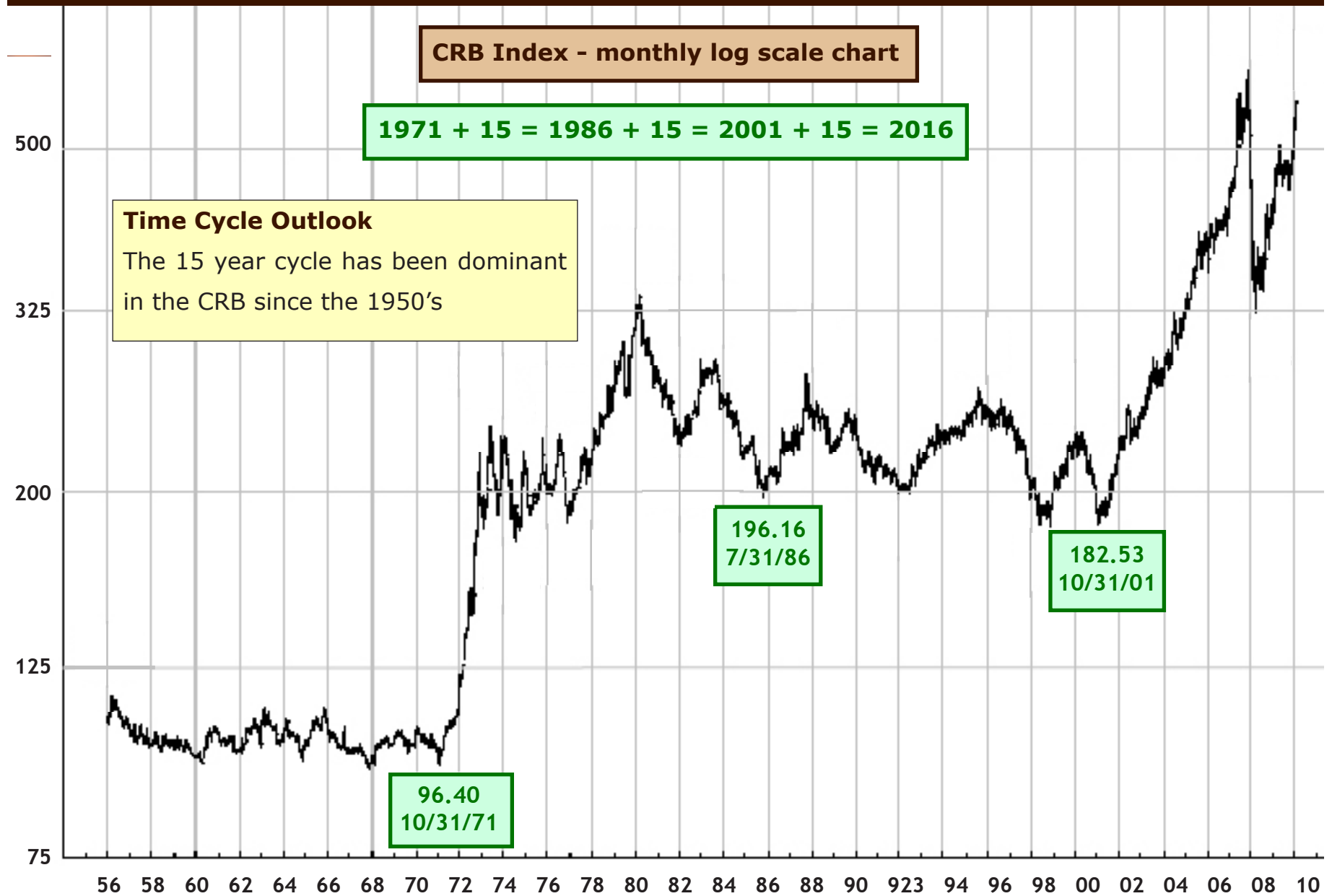
**Dow Industrial Average - monthly chart - log scale**  
**7.5 year cycle**

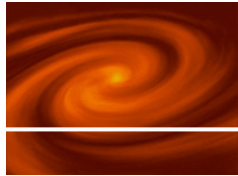
**Time Cycle Outlook**  
The 7.5 year cycle has been dominant in the equity markets since the 1970's

**Next Cycle High by 2012**

**Next Cycle Low into 2016**







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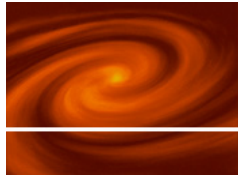
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***"You take the blue pill, the story ends, you awake in your bed and believe whatever you want to believe.***

***You take the red pill, you stay in Wonderland, and I show you how deep the rabbit-hole goes."***

***- Morpheus to Neo in 'The Matrix'***



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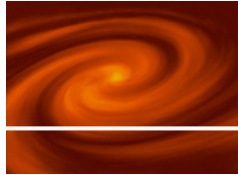
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### **Fundamental Analysis:**

**The price action is not relevant  
to predicting price trends**

### **Technical Analysis:**

**All one need know about supply  
and demand is in the price ac-**



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**Fundamental Analysis:  
Supply and Demand Matters  
“Efficient Market Hypothesis”**

**Technical Analysis:  
The Price Action Matters  
“Herding Behavior”**



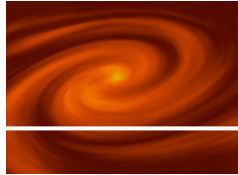
- Insects Swarm
- Fish Swim in Schools
- Birds Fly in Flocks
- Animals Migrate in Herds
- Financial Markets Trend

And all for the same reason.  
There is safety in numbers.

For hundreds of millions of years those who did not follow the herd became lunch for the predators. Their genes were not passed on. Herding was rewarded with survival.

Investment Herding Behavior:  
The market just rallied.  
Someone must know something.  
I had better buy.





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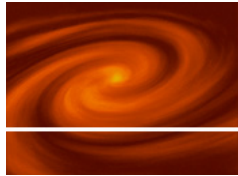
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### **Fundamental Analysis:**

**Investors buy after doing their own thoughtful and careful analysis**

### **Technical Analysis:**

**Investors buy after seeing others buy  
“Somebody must know something”**

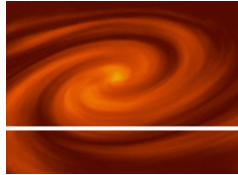


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**Fundamental Analysis:  
News Creates Price Trends**

**Technical Analysis:  
Price trends creates the news**

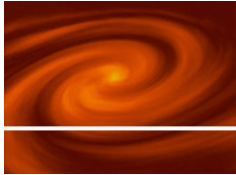


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**The trend changes with each new piece of news. There is no trend independent of the flow of the news.**

**The collective mood that creates price trends selects only the “news” that resonates with the collective mood.**



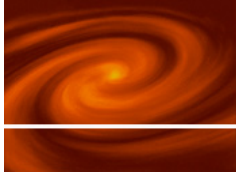
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**In presuming that the news creates the trend 'Fundamental Analysis' is confusing cause and effect.**

**The collective mood determines what is 'news,' so the content of 'news' is a sentiment indicator - a technical tool.**



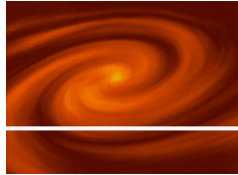
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**The market fundamentals are always the most bullish at the top. The news is always and only bullish at market peaks.**

**Markets peak when the bullish sentiment extreme exhausts the buying power of the market. Everyone will then be caught**



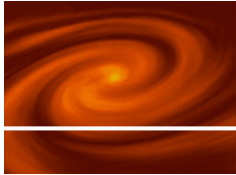
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**The market fundamentals are always the most bearish at the lows. The news is always and only bearish at the bottom.**

**Markets bottom when the bearish sentiment extreme exhausts the selling power of the market. Everyone will then be caught**

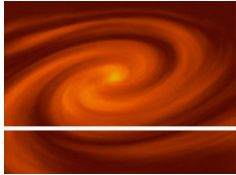


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**Markets peak as supply exceeds demand.  
Analysis justifies lower prices  
Prices are lowered to meet new appraisal.**

**Markets peak when the most bullish news  
so far fails to sustain the rally.  
Bulls lose confidence and liquidate.**



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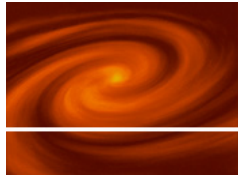
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**Markets bottom as demand exceeds supply.**

**Analysis justifies higher prices**

**Declines end when the most bearish news of the trend fails to sustain the fall.**

**Bears then lose confidence and liquidate.**

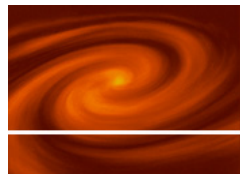


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**Deflation is a  
Financial Imbalance**

**Deflation is a  
Collective Mood**



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**'QE' to Reflate a  
Burst Credit Bubble**

**The Cure for Low Prices  
is Low Prices**



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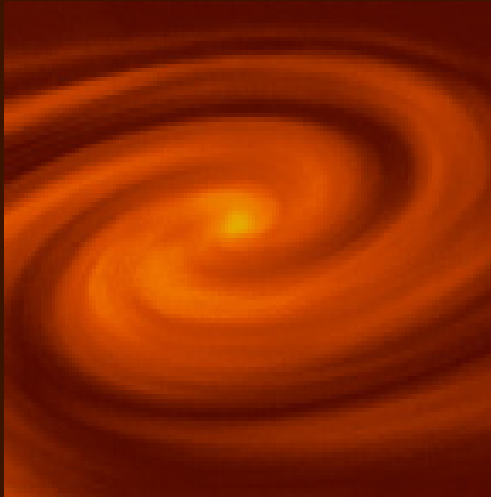
## Risk of Fundamental Analysis

**Do not see the turn coming so risk being the last buyer in an up trend and the last seller in a down**



## Risk of Technical Analysis

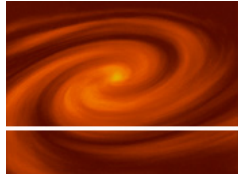
**See the turn coming well in advance so risk exiting the trend early**



## **Our Technical Tools:**

- **Candlesticks**
- **Sentiment indicators**
- **Momentum analysis**
- **Price chart pattern analysis**
- **Cycle analysis**



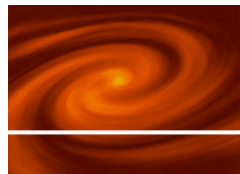


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**We have no use for the statistics and models of fundamental analysis.**

**We listen to what the price action is trying to tell us.**



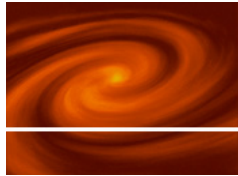
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**In a truly efficient market, prices would sit quietly waiting for news. Imagine a market on Spock's planet Vulcan.**

**However this is planet Earth. And the collective behavior of human beings displays herding behavior.**



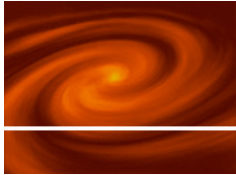
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**A fundamental analyst can never know what key factors are already discounted in the price.**

**Technical analysis studies the price action directly. So discounting is never an issue.**



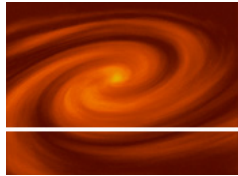
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**Fundamental analysis can be 100% correct about the supply - demand forecast but 100% wrong about the price outcome.**

**Prices are not driven by exogenous factors of supply and demand. Prices are driven by endogenous market forces.**



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## **FUNDAMENTAL ANALYSIS**

**Energy companies needs fundamental analysis to monitor supply and demand and technical analysis to manage price risk.**

## **TECHNICAL ANALYSIS**