Price breakouts

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These four stocks are a good example of share-price breakouts in action.

By Robert Brain, ATAA

The June edition of *ASX Investor Update* looked at share price trends through charts and the capital-protecting stop-loss approach. This month we examine chart breakouts that can often be anticipated and reflect the changing sentiment of investors and traders.

At any point in time it is normal for market participants who have an interest in a share to have their own opinions about its "fair value", and these opinions will fall into a range in the share price.

Depending on the share and factors such as the latest news and announcements, this price range could be small or large. At some stage, if all of the interested sellers have finished selling and only buyers are left, the price will move higher as buyers compete with each other.

Two common types of price breakout include those that:

- Follow a period of price consolidation.
- Follow a period of narrowing price variation within a chart pattern, such as a Symmetrical Triangle.

These breakouts occur because the opinions of fair value by buyers and sellers change rapidly. These situations are best explained by the examples below. **More information on breakouts**.

1. Lynas Corporation (LYC)

During February to May 2010, Lynas Corporation traded mostly within a narrow range between 45 cents and about 57 cents. To see the actual range in price each day we need to look at the accompanying candlestick chart covering the period late March to mid-July. **A larger version of the chart is available**.

Towards the right-hand end of the chart we can see the price has broken above the trading range. It went on to rise about 360 per cent over the following 44 weeks. If only we all could have spotted this at the time.

Note that the price rose in April to about 57 cents. The solid red line indicates this level as an approximate zone of resistance, above which there were no buyers prepared to pay more at the time. In May, the price fell to within about 45 cents to 47 cents twice, except for the single-spike low on May 5. The green line at 45 cents indicates the bottom of a zone of likely price support, where some buyers step in to buy up the perceived cheap shares. Throughout May the price tried to rise above about 54 cents twice, but retreated both times with no buyers present.

When the price fluctuates in this manner between an upper and lower level, it suggests buyers and sellers have been in some disagreement about the actual value of the shares. When the price rises to a level that is perceived to be too high, sellers take profits and overwhelm the market participants, resulting in the price falling. But when the price falls too far, buyers step in and overwhelm the sellers, outbidding each other and forcing the price higher.

In this case, in late June there must have been a change in opinions because there are three consecutive white candles on June 16-18 pushing above the recent resistance of about 54 cents, followed by four days where three of the candles have no candle body. These are called Doji candles and indicate indecision about whether the price should rise or fall.

Then there is a big white bullish candle (with no tails) on June 25 accompanied by higher volume; relatively higher than in recent days. The price then fell to the old resistance level of about 54 cents, which has now become a support level to hold the price up. After several days the price moved higher on July 9 with much higher volume, which indicates a strong level of support from buyers to outbid each other higher. The rest is history - up 360 per cent in 44 weeks.

Lynas Corp (LYC) - March to July 2010

Source: © July 2012, **Robert Brain**

2. Resolute Mining (RSG)

Resolute Mining traded back and forth between about 64 cents and 85 cents over the three months from mid-March to June 2009. **The big-picture daily chart is available**. before falling to a low of 51.5 cents in early July. From there the price again swung up and down in a wide range until September; except that on each swing-low the low price was higher and higher than the previous low prices.

The share price of Resolute Mining in the accompanying daily candlestick chart (**a larger version is available**) shows that from mid-September 2009, for three weeks the price traded within a narrowing range. The boundaries of this price range can be shown on the chart with the straight line segments as indicated. The upper red lines and the lower green line in this example roughly form a triangle-shaped pattern, and volumes were in the range of about 1-6 million shares a day (the bar chart in the lower portion of the diagram).

In the last days of this triangle pattern the buyers were less and less convinced of the merits of higher prices, with volumes dropping. But the candle on October 6 has an upper tail (or wick) which is testing higher price movements, followed by a Spinning Top candle the next day with significantly higher volume. The higher volume indicates a much higher level of interest with buyers outbidding each other and forcing the price higher.

The tall white candle on October 8 also has high volume, indicating continued interest in the shares and a lack of supply (sellers), with the potential buyers bidding higher and higher. The price went on to rise 80 per cent over the following eight weeks.

Resolute Mining (RSG) - daily chart, September to October 2009

Source: © July 2012, Robert Brain

3. Murchison Metals (MMX)

A weekly price chart of Murchison Metals (**available online**) shows the share price reached a high of $3.12 in April 2010, then steadily fell to a low of 23.5 cents 18 months later in October 2011 - that's quite a fall. Anyone who held these shares in that period would have lost a lot of their investment capital (about

93 per cent). In hindsight it might have been wise to implement a stop-loss technique.

After the low in October 2011 (see chart below) the share price jumped in mid-November and crept up to a ceiling price of 48.5 cents. This is a line of resistance, shown on the chart with the red horizontal line. It seems that no one has been prepared to pay more than 48.5 cents in the past few months - pending company takeover offers are one possible cause for this chart effect. Every time the price has moved up towards this level, it has slipped away again. This indicates an excess of supply of the shares and a willingness to sell and pocket the cash.

Interestingly, there is one recent volume spike on this chart in late June with a very small candle, actually a Doji candle with the week's closing price the same as the opening. This indicates a lot of buying interest at this price, with many sellers keen to sell, but no interest in moving the share price, and for a whole week. The higher volume weeks (and higher volume days on a daily chart) can indicate quiet accumulation of the shares by professionals and larger investors such as fund managers.

The fact that the price has stayed within a very narrow range of about 3-4 cents for several months is a good warning that a price consolidation like this is not a guarantee of a quick price breakout. There might eventually be a shortage of sellers, resulting in the price running higher; but it is difficult to tell if, and when, it might occur. When the price breaks above the 48.5 cent level and stays above it for a few days, we might have confidence that a new uptrend may be under way.

Murchison Metals (MMX) - a weekly candle chart, Dec 2011 to July 2012

Source: © July 2012, [Robert Brain]()

4. Stockland (SGP)

The weekly candlestick price chart of Stockland from early 2011 shows a continually narrowing range of price (**[a larger version is available online]()**).

The price fell sharply over five months from $3.90 in March to almost $2.50 in August. Since then it has rallied sharply a couple of times (indicated by the dotted green lines) and subsequently fallen again. But each time it has risen, it has been to lower prices than previously, and when it has fallen it has been to higher prices than previously.

This price action is a reflection of the views of the market participants, all the investors and traders in the shares. Remember that at any one point in time it is normal for market participants to have opinions about fair value and that falls, into a price range, small or large.

In the accompanying chart the upper price boundary (the downward sloping red line) indicates the market participants have lower and lower opinions of a fair value price, while the lower price boundary (the upward sloping green line) indicates they have higher and higher views about fair value.

If we draw straight lines on the chart above and below the price action, one result is the Symmetrical Triangle chart pattern shown here. A pattern such as this often ends with one of two scenarios. The price can break strongly to either the upside or the downside, before reaching the right-hand tip (the apex) of the triangle. The alternate, but less likely, scenario is the price might continue to trade in a narrowing range until the tip of the triangle, then simply keep trading sideways with no breakout at all. Astute investors and traders need to keep an eye out for either of these outcomes.

Stockland (SGP) - a weekly chart, 2011-2012

Source: © July 2012, [Robert Brain]

About the author

Robert Brain is a share trader and sharemarket analyst, and runs **Brainy's Share Market Toolbox** web-based business supporting investors and traders. He is a national director of the Australian Technical Analysts Association (ATAA) and vice-president of the Melbourne ATAA Chapter. Robert uses the **Australian BullCharts** charting software platform.

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