

[Lesson #1 -- An Introduction to Technical Analysis and Swing Trading](#)

Hello, my name is Dr. Melvin Pasternak. Over the last several decades I have used technical analysis to make short-term equity trades virtually every single day. And thanks to my persistent study of this topic along with a unique trading approach I have developed over the years, many of these trades have turned out to be highly profitable.

Throughout the years I have always strived to make education a top priority in my life. And through positions as both a college professor and a trading seminar instructor, I've had the good fortune of being able to teach technical analysis to thousands of investors throughout my career. However, I've always had a burning desire to bring my educational ideas and unique trading insights to a much larger audience. So when well-known financial publisher StreetAuthority, LLC came to me in 2002 and told me I could reach tens of thousands of additional investors each and every week by publishing my own equity-trading newsletter, I jumped at the opportunity.

In each of my weekly [StreetAuthority Swing Trader](#) newsletters, my aim is twofold. First, I always share an analysis of at least two or three specific stocks that I believe will make you money in the near term. And second, I strive to give you a very strong grounding in the technical analysis methods I use so that you can dramatically increase your own batting average when you spot potential opportunities.

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[\(1.\) MORE ABOUT MY BACKGROUND](#)

I was born in 1944. I bought my first stock in 1961 -- IBM -- when one summer during college I worked as a runner on the floor of the New York Stock Exchange. I noticed it kept going up and up and I hated to see the ship leave port without me. My attitude has not changed much since.

In the late-1970s I became fascinated with what I call "classical" technical analysis -- support and resistance, price patterns such as triangles or rectangles -- and studied this subject diligently.

I subscribed to chart books by earth mail -- grateful to have them even if they were two weeks late. In the early 1980s I discovered financial television. Nightly I would watch FNN (forerunner of CNBC -- Ron Insana had hair back then) and would write down in long columns the advancing and declining issues, up and down volume, new highs and lows, etc...

At about this same time, armed with a thick pad of graph paper, I began hand charting the S&P 500 daily. In those days, when I shared my hobby of technical analysis, I always brought along my own "Monster chart," my hand-created chart of the S&P. It regularly grew to be about twenty feet long before it had to be delimbed so I could carry it in an attaché case. But much like an octopus, its tentacles always seemed to grow right back.

God bless whoever created stock market software! In the early 1990s I started using Metastock and integrated many of its funny-sounding tools -- stochastics, moving average convergence/divergence, the parabolic stop and reverse -- into price pattern analysis. At the same time I began teaching technical analysis courses at leading discount broker T.D. Waterhouse and then at the college level. Since that time I have taught literally thousands of people both the basics and the more advanced, intricate details of technical analysis. In the process, I have helped make most of them better traders. Through both this trading course and my weekly StreetAuthority Swing Trader newsletter, I sincerely hope to do the same for you.

Over the years, I have made thousands and thousands of trades and have large stacks of brokerage receipts in my basement to prove it. During the last year of the great bull market I increased my account size by ***several hundred percent and turned a profit on over 80% of my picks***. Through dozens of market-related interviews on radio, T.V. and the newspaper, I suspect my guidance has helped make at least a few people wealthier.

Once I managed to hold a stock (GE) for three years! But I hate to see profits erode, so I am by nature a short-term (or swing) trader. Very occasionally, when the opportunity presents itself, I will enter and exit a position on the same trading day. However, as you'll quickly find by following my picks in my weekly StreetAuthority Swing Trader newsletter, most of my trades generally last from several days to several weeks.

Academically, I hold both a Ph.D. and an MBA. I have given business writing seminars to a number major corporations -- including such well-known names as Shell and Chevron -- and love to write myself. But my true passion lies with the stock market. When I teach, in person, or in writing, I try to be clear, simple and direct.

(2.) AN INTRODUCTION TO TECHNICAL ANALYSIS

The underlying theme behind both this trading course and my weekly newsletter is that ***the better you are at technical analysis, the more money you will make swing trading***.

Let's start with the basics...

Technical analysis is the science and art of interpreting a stock chart. It is based on the belief that all of the market's hopes, fears and decisions are already expressed in this chart. Decode the chart's message and predict whether a stock will go up or down. Make a correct prediction and be rewarded by making money.

Technical analysis is all about spotting a stock's trend and making sure that you are on the correct side of that trend. As a swing trader, I try to identify and ride a given trend for a period of several days to several weeks. Just as important, I also attempt to identify changes in trend as soon as they begin to take shape.

When it comes to my own trading, I regularly apply more than 40 essential tools of technical analysis. Most important are the often-overlooked basics -- trends and trendlines, support and resistance levels, volume analysis. I search for chart patterns -- rectangles, triangles, inverted heads and shoulders. I focus on "gaps," pay meticulous attention to the subtle messages of candlesticks, and integrate early warning indicators such as the MACD histogram or stochastics. As more and more technical tools

start to give you the same message, the more likely your analysis is to be correct and the more likely you are to be rewarded with a swing trading profit.

Technical analysis is not perfect though. Some market climates are very easy to make money in -- others are far trickier. Let me be very upfront about this point at the outset. Technical analysis can only increase the *probability* that you will make correct trading decisions. It is not a perfect science, and I have yet to meet a perfect technician. ***The stock chart is an ever-evolving message -- one that needs continuous interpretation and reinterpretation.***

That said, the more adept you can become in the application of technical analysis principles, the more money you will be able to make swing trading. One of the core missions of my weekly StreetAuthority Swing Trader newsletter is to share this knowledge in a clear, simple way so that when you analyze your own trading opportunities you will have an effective set of decision-making tools.

(3.) WHAT IS SWING TRADING?

Financial success in the stock market can be achieved in any time frame. It all goes back to following the trend of the time frame you are trading or investing in. (I will more fully explain that important point in the next installment of this trading course.)

Warren Buffett's style of buying great stocks and holding them for life may seem out of tune with a bear market; yet, who is to quarrel with his success? If you had put \$10,000 into Berkshire Hathaway (BRKa) in 1965, then your investment would have grown in thirty some-odd years to about \$65,000,000! And that result includes the crash of 1987 and a Dow well off its Y2K bull market peak. Even Jesse Livermore, who is widely regarded as a master trader, argued that in a bull market you "buy right and sit tight."

For some, however, this one-decision approach to building stock market wealth is not their chosen path. They are short-term traders.

A scalper may enter the market for seconds, arbitraging the difference between the bid and ask price. His near cousin is the day trader. But that description implies often undue longevity. Most day traders I know take a position for perhaps 15 minutes to one hour. They aim for many quick, small percentage gains. They may trade five, six, ten, or even upwards of twenty or more times a day. Some are wealthy, but most just end up making their brokerage firms rich.

A cardinal rule of day trading is to not hold a position overnight; however, some day traders will violate this dictum late in the day by looking for "overnighters" -- attractive stocks that have risen and have the capacity to pop on the next day's open.

A swing trader will generally remain in the market for several days to several weeks. The swing trader's goal is to quickly spot an upside or downside trend reversal, to go long or short the stock, and to in turn ride this trend until it reverses. He or she will often suffer through several minor trend corrections along the way, but will always stay focused on capturing the overall "swing" of the stock. Below I will present you with a brief example of this swing trading approach by taking a closer look at a chart of Silicon Image (SIMG). In doing so, I will identify several profitable swing trading opportunities in that historical chart and will explain how you could have earned tremendous profits

on this stock by applying technical analysis. But first, I'd like to examine what it takes to be a successful swing trader...

(4.) ARE YOU A SWING TRADER?

Swing traders come in many shapes and sizes. But from talking to thousands of traders over the years, I believe these are some of their most important qualities.

First, they are fascinated by the market. They often rise early, tune into the pre-market S&P futures and log onto their favorite financial website. At work, they are irresistibly drawn to check quotes on their favorite stocks and to see how the market is doing.

Next, they are fascinated by trading. Many see it as a game -- a chess match played between them and the market. When mastered, they know full well that this game can have very great financial rewards.

Most swing traders are aware of technical analysis, examine charts and may casually talk about MACD or a head and shoulders pattern. But many, I have become aware, still need to learn the fine points and sometimes even review the basics.

Finally, a swing trader has learned, often by bitter experience, the fallacy of applying buy and hold strategies in the wrong kind of markets. They believe in capturing profits. On the other hand, they have also learned patience. Losses should be cut short but profits let run until there is a clear technical signal to sell -- not merely "the stock has gone up 11% since I purchased it."

(5.) IT'S ALL IN THE CHART -- A BRIEF EXAMPLE OF HOW YOU CAN PROFIT THROUGH SWING TRADING

The historical 10-month daily chart of Silicon Image (SIMG) below provides us with a beautiful illustration of the enormous profits that one can earn through swing trading. This chart is in candlestick form (an essential tool for swing traders), uses bollinger bands, and presents the following indicators: rate of change, MACD, MACD histogram, price relative to the S&P 500, commodity channel index (CCI), full stochastics and RSI. (Note: If you're a beginning trader and you're unfamiliar with some of these terms, don't be alarmed. I'm going to cover these terms and other important topics in greater depth in my upcoming trading lessons, so please stay with me here!)



During this 10-month historical time frame I counted four very profitable swing trades. For the sake of this example, I have labeled them ST (Swing Trade) A-D on the chart above. Depending on your

specific entry and exit points, all four of these trades could have yielded gains of 50% to 100% in as few as 30 trading days!

Now I'd like to discuss **ONE** of these trades with you in detail to show you what a great swing trade setup looks like and how this newsletter will help you spot profitable opportunities. I have labeled this swing trade "C," and it took place starting at the beginning of October.

At SIMG's October, you'll note a very significant candlestick -- it looks like a cross and its bottom part, or "shadow," is outside the Bollinger band. It is called a one-legged doji, and it is a very powerful signal. At the time, this candle indicated that supply and demand were coming into balance after a long downtrend. The bulls were now as powerful as the bears. This shift in supply and demand was then confirmed by the next candlestick, the white one, which clearly showed that the bulls were now in charge.

Now let's look at some of the other information on the chart. Cast your eye down to price relative to \$SPX (the S&P 500). Notice how after a long period of underperforming the S&P, the pattern changed to the positive. The S&P had already started to rally by then in late-2002, but SIMG was now stronger than a rising market!

The indicators below \$SPX were all telling me the same story as well. Note the "Buy" to indicate a positive MACD crossover, CCI signal, and bounces from oversold levels in both the stochastics and RSI. All of these signals were unambiguous when I was examining this trade (not just in retrospect), and all were screaming, "I, SIMG, want to be bought."

But perhaps you were cautious in early October. Or maybe you were not following the stock closely. Although you might have missed out on SIMG's first leg up, you didn't completely "miss the boat" on this trade. As it turns out, the stock was still setting up for another great trading opportunity. In the beginning of November a signal showed up that was so powerful it implored to be taken. At that time SIMG broke through \$4.63 -- a resistance level that had turned the stock back twice before.

Even more important, you could have recognized that an "inverted head and shoulders pattern" had formed. At that time, the measuring principle would have told you that the new target for SIMG was now well over \$7. You could not let that plane leave the airport without you!

Let's say you bought at \$4.65 and sold at the break of the trendline, another very clear signal that occurred in mid-November (I have labeled this on the chart). With the stock at \$6.95 at that point, you would have managed to pocket a 49.5% return on this trade in just about 20 trading days!

I will not review all of the reasons why there was then a clear set up to go short at point "D." But if you recognized the signals, then the profit potential on the way down was equally as great.

(SIDE NOTE: Notice that I have avoided choosing best-case entry and exit points. Why? Because this is a real-life example. As it turns out, I didn't catch these extremes when trading this stock. However, ***I did trade SIMG for a tidy profit in the real world in a manner very similar to the one I just described, and I have the trading slips to prove it.***)

The example above might seem pretty straightforward, but admittedly: hindsight is 20/20. Trading SIMG in real time will always prove much more of a challenge. In addition, there are a number of risk factors involved with swing trading. The stock market is full of mine fields for the unwary. There are currents and countercurrents. If you enter a trade at the wrong time, then you can get stopped out even if you are right on the overall direction. Unexpected events can turn trends on a dime. Your technical analysis can be partial or incorrect. The list goes on and on...

However, the good news is that you don't have to navigate through these treacherous waters alone. Through a subscription to my newsletter -- the [StreetAuthority Swing Trader](#) -- you can gain access to my experience and guidance on a weekly basis.

(6.) HOW CAN THE STREETAUTHORITY SWING TRADER HELP YOU?

I can be of service to you in two ways. First, each week I will pick between two and five specific stocks to trade long or short. I will do this in conjunction with detailed analysis of the technical trends of the overall market and will attempt to spot key reversal junctions in both the broader averages and the individual stocks.

My years of experience in technical analysis will be dedicated to helping you pinpoint opportunities that have the potential to produce dramatic swing trading gains (similar to what you've already seen in the SIMG example above).

Second, I will teach you all I know about technical analysis. Was there anything new to you, anything you would benefit from learning, in the analysis of SIMG above? If so, then I'm pleased to have presented you with some compelling material. If not, then keep in mind that I will go into much greater depth than this in both my upcoming trading lessons and in my weekly email newsletter. So even if you're already an advanced or expert trader, I can almost guarantee you that you'll learn something new (or at least hone your existing skills) by reading the StreetAuthority Swing Trader.

Momentum divergence. Trendlines and resistance. Inverted head and shoulders patterns and the measuring principle. The long-legged doji candlestick. The function of bollinger bands. CCI or stochastics. How to put all these ideas together into a cohesive whole and come to a clear trading decision. I will cover all of these topics, as well as hundreds of others.

My commitment is to not only provide profitable trading ideas week in and week out, but also to teach my subscribers to improve their technical analysis skills in a clear, logical and systematic way.

(7.) WHERE DO WE GO FROM HERE?

Please take out a pen and paper. Complete the following statement: An uptrend is a _____ of _____ peaks and _____s.

If this concept is not already on the tip of your tongue, then it should be. In the next installment of this swing trading course I plan to start with the most basic and important concept of technical analysis -- the trend. I will show you how to spot the trend, lay out a clear, simple way to draw accurate trendlines, give you a very clear method of when to sell based on the trend, cover trend-following principles of moving averages to spot profitable trends, and much, much more.

Even if you have never subscribed to an investment newsletter and have no intention of doing so now, you can at least take advantage of this free offer to learn by reading the next installment of my in-depth swing-trading course. Trust me, the trendline is a simple, but incredibly powerful tool. Most traders I've met do not use trendlines accurately or frequently enough.

From there, I will cover many more essential concepts for successful swing trading in the remaining installments of this course. You will learn about support and resistance, price pattern analysis, buying the breakout, what volume characteristics to look for, and much, much more. I'll also share with you my personal, detailed methodology for making successful swing trades. Best of all, this course is entirely free, so you have absolutely nothing to lose! And by following my weekly newsletter and paying close attention to my individual stock picks, you might even be able to profit from my advice.

Thanks again for reading my swing trading course, and good trading in the weeks ahead!

And, oh, I almost forgot, "an uptrend is a series of rising peaks and rising valleys."



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