

Moving Averages

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Moving Averages

- Simple Moving Average
 - Calculation
 - Strengths and Weaknesses
 - Lagging Indicator
 - Trend following tool
 - Nasty “Chop” in sideways markets
 - MA Cross-overs
 - Optimisation
 - Death Cross/Golden Cross
- Exponential and Weighted Averages
- Applying averages to other data sets like Volume
- Moving Average Envelopes
- Bollinger Bands
 - As an “overbought/oversold” tool in trendless markets...
 - ...and the dangers involved in this approach!
 - As a breakout and volatility tool
- Donchian Channels
 - “Turtle” system

Moving Averages

- A moving average is the basic trend following and trend confirming tool.
- They show the average value of the data for the period for which you are viewing.
- A 3 day moving average of price shows the average price over the last 3 days, a 14 day average shows the average price over the last 14 days and so on.
- Moving averages are called as such because they are calculated on an ongoing basis and hence tend to move in line with underlying price action.

Moving Averages

- It is important to understand the methodology behind moving averages, as with any indicator, in order to properly use them and also to know their strengths and limitations.
- There are many forms of moving averages the main type being the simple moving average.



Moving Averages

- This is simply an average of price over a certain number of days.
- It is calculated as follows:
- $(\text{Price 1} + \text{Price 2} + \text{Price 3}) / \text{Number of Days}$
- **Example:**
- $(10 + 11 + 12) / 3 = 11$
- As a new day is added so the first day in the calculation drops off.

Moving Averages

- Therefore after when we close the next day at \$13 the calculation would continue like this:

$$(11 + 12 + 13) / 3 = 12$$

- The old “day 1” value of \$10 is no longer used in the equation as we have a new day’s value to use. This is why averages are called 'moving'.



Moving Averages

- Strengths and weaknesses:



Moving Averages

- Strengths and weaknesses:



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