



# Brainy's Articles on Share Trading\*\*

## Breakouts introduction

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### Introduction

One of the best opportunities to capture a reasonable share price increase and eventually take some very good profits, is by spotting a new trend early, and in riding the trend. Sometimes a new trend will start with a price breakout above a line of resistance which might be apparent in a chart pattern like an Ascending Triangle, or below a long-term horizontal resistance line. A price breakout can be the starting point for a major price trend — the earlier we spot it and join it, the better.

This Article in Brainy's series on Share Trading and Investing (number ST-6130) introduces the notion of price breakouts, and shows a few realistic examples of past breakouts. By studying past breakouts and their characteristics we can be better prepared to spot future breakouts as they occur, and to understand their characteristics. A more detailed study of breakouts is included in Brainy's Article TA-3900, "**Breakouts — Case study details**".

On a price breakout it is possible for the share price to literally run away. So it is important with breakouts to avoid paying too much for a stock. In this regard, readers should also see Brainy's Article TA-5300, "**Avoid paying too much**".

### Breakouts — the basic psychology

Firstly, let's consider the underlying psychology that helps to explain why breakouts occur.

At any one point in time it is normal for the stock market participants who have an interest in a stock to have their own opinions about the "fair value" of the stock, and these opinions will fall into a range in share price. The participants rarely agree on just one price. Depending on the particular stock, and on many factors such as the latest news and announcements, this price range could be a small range, or it could be large. At some stage, if all of the interested sellers of the stock have finished selling, and if only buyers are left, then the share price will move higher. And conversely, if all the buyers have finished buying, then the share price will move lower. And it is possible that news or announcements can precipitate a move in share price.

### Breakout — definition

To best illustrate the principle of a breakout, refer to the accompanying sample price charts and brief descriptions here and below.

In the weekly chart of Aragon Resources (AAG) in Figure 1 at right, we can see that AAG was stuck below resistance at 14 cents for a 7-week period in February and March 2010. The big white candle in late March shows the price breaking out significantly above 14 cents, and a subsequent rise of about 70% over the following weeks.

The monthly chart of Amadeus Energy (AMU) in Figure 2 (below) shows this stock stuck below resistance in the 13 to 15 cents range for about 3 years, before breaking out above this level, and advancing 460% on this chart, but actually 800% by 2006.

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Figure 1: AAG Price breakout above resistance.

\*\* - The two words *trading* and *investing* are often used somewhat interchangeably.

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