No trading system is bullet-proof. The list of factors that can impact a stock’s share price is long and growing … from investor sentiment to economic growth to management comments, pretty much anything can drive share prices higher or lower on a given day.

But, if you look for the edge or advantage, you’ll be able to uncover stocks with the most potential to outperform over the longer term.

To discover this advantage, we stress the importance of owning **Trifecta Stocks**. These are stocks that pass our rigorous quantitative, fundamental and technical analysis.

For the sake of clarity, we’re going to focus just on technical analysis in this special report. (Be sure to check out our other reports for a more in-depth look at quantitative and fundamental analysis.)

You could say that technical analysis is an art (visual) and a science (statistical). That’s because technical analysis uses various tools and techniques that display consistent patterns over time—both visually and statistically.

Given this, our ‘trader’s toolbox’ is filled with indicators that are superb predictors of chart patterns. So let’s take a closer look at four of these indicators that **Trifecta Stocks** uses every day to evaluate a stock’s potential.

**Momentum Indicators**

As you can gather from its name, momentum indicators help determine the direction of a stock’s share price. Are there more forces supporting shares move higher? Or are there more forces pushing shares lower?

To answer these questions, we favor **Moving Average Convergence/Divergence (MACD)**.

MACD basically measures the difference between moving averages, which is why it’s an indicator of strength (or weakness) of a trend. It focuses on the trajectory of change in a stock’s price trend, and is based on the exponential moving average (EMA)—which keeps up with the real ebb and flow of the market.
So when using MACD, we look for crossovers or crossunders of the zero line. (The settings are default at 12, 26 and 9.) To explain further, consider the chart of BP PLC (BP) below.

The blue line represents the difference between BP’s 26-day EMA and 12-day EMA. If share prices have been moving higher in the last 12 days compared with movement in the last 26 days, shares have positive momentum. The black area represents this momentum. And when blue line crosses above the red line, the 9-day EMA, it also represents a move higher and a good buying opportunity.¹

Looking at the chart, you can see that BP shares started gaining momentum at the end of April when the blue line crossed over the red line and then pushed above the zero line.

It’s also important to note that MACD measures relative strength, which compares price performance to that of an index like the S&P 500. If we are bullish on a stock, we look for higher lows, higher highs and strong levels. But if we are bearish on a stock, we look for lower lows and deep lower levels.

Typically, we focus on a timeframe of 14 periods, or roughly three weeks—enough time to evaluate the short-term trend.

Looking at BP once again, you can see in the chart below that in July shares were consistently producing higher lows and higher highs—a sure sign of relative strength compared with the S&P 500. But then you can also see when shares faltered at the end of July and started posting lower lows.

Williams %R

To determine if a stock is overbought (trading near its high) or oversold (trading near its low), we turn this oscillator, Williams %R.

Williams %R takes a stock’s current closing price in relation to the high and low over a particular number of days. Typically, a 10-day trading period is used.

What’s unique about the Williams %R is the reverse of the common 0 to 100 scale found in most oscillators. So -100 is the lowest low, while 0 is the highest high of the day range you’re considering. That means readings of -80 to -100 is considered oversold, and reading of -20 to 0 is overbought.

To explain further, consider a recent 10-day chart for C.H. Robinson Worldwide (CHRW). As you can see in the chart below, the red circles represent when CHRW’s shares were in overbought territory (-20 to 0), and the green circles show when shares were oversold (-80 to -100).
As you can probably gather from the CHRW chart, the Williams %R is often used as an indicator of when to buy or sell a stock—if the stock is oversold, buy; if the stock is overbought, sell. But at Trifecta Stocks, we’re trend players so we use it differently.

We look for embedded characteristics. For example, if the indicator is stuck in overbought or oversold territory and it stays there while the stock moves in the direction of the trend. Intuitively, it makes sense to ride out a trend for as long as it plays out.

**Bollinger Bands**

One of the best ways to spot and ride price trends is using **Bollinger Bands**.

This indicator draws bands above and below a stock’s share price on a chart. Typically, a 20-period moving average is the middle band, while the upper and lower bands are each two standard deviations from the middle band.²

Most of a stock’s price is contained within in the bands. In fact, we look for the stock to stay within the Bollinger bands 95% of the time if we use the normal two standard deviations.

Now, as I mentioned, Bollinger Bands help us spot price trends. Comparing the price level with a moving average gives a gauge of where the stock lies in terms of future direction. The 20-period moving average is normal, a month’s worth of action. But on the rare 5% occasion that the stock price pierces the upper or lower Bollinger band, a reversal is usually at hand.

So when there is an upper Bollinger break, we look to buy. When there’s a lower Bollinger break, we should sell. And when the bands narrow, a big move is imminent (coiled spring effect). These potential events are what you want to watch for.

Just consider the six-month chart for **Avis Budget Group (CAR)** below …

As you can see, the red circles indicate when share prices pierced through the top and bottom bands. And as expected, there was a reversal in the stock’s trend. The green arrow, on the other hand, shows a narrowing of the bands—and the big move was a shot higher.

**Volume**

The final technical indicator we want to discuss is **volume**.

We believe strong volume is a sign of institutional sponsorship or distribution. Since institutions such as hedge funds, mutual funds, pensions and trusts account for 80% of the market action, it makes sense to follow this lead.

Let’s face it: No institution will tell you when they are buying or selling, but a stock’s absolute volume tells us so much.

We look for large and unusual sizes of volume on the daily chart to help us determine whether the setup is good or not. Since we are trend followers, a breakout on big volume is bullish while a breakdown on high volume is generally bearish.
Again, let's take a closer look and consider the one-year chart of **Ford (F):**

What you'll discover is that Ford had some pretty huge volume days on a breakout in share price at the end of December 2012—and that turned out to be the start of a sizeable uptrend for the stock.

**Conclusion**

As you can see technical indicators can reveal a lot of different information—from the momentum of a stock, to the oversold or overbought condition of a stock, to institutional interest in a stock. All of which, investors use for buy and sell signals.

Remember, though, not all buy or sell signals are genuine.

A stock price crossing its 20-day moving average or a share price touching the upper Bollinger Band could be a temporary blip. Because the very next minute, the price could reverse sharply ... and relying on one indicator over a short time frame could result in a big loss.

That's why at **Trifecta Stocks,** we always consider more than one technical indicator over different timeframes.

I encourage you to do the same. First, extend the technical analysis we discussed in this report to each of the stocks in your portfolio—or to any stocks you are considering to buy.
For each stock, use your favorite charting software. For each of the four technical indicators, plot a chart in the recommended time frames. Determine if there are any buy or sell opportunities—and then repeat for the next three trading days or until you feel comfortable trading real money.

But as I mentioned, no technical indicator is perfect. That’s why at Trifecta Stocks, we combine analysis of all four technical signals to confirm the market move—and then put our stocks through rigorous fundamental and technical analysis, too.

Before we ever make a recommendation, a stock must pass our rigorous technical, fundamental and quantitative analysis. Then it is deemed a Trifecta Stock—and worthy of your hard-earned dollars.