# THE GMMA – TREND BREAKOUT TRADING

By Daryl Guppy

Many new readers have asked about the GMMA, how it is constructed and how it is used for trading. I developed the GMMA in 1994 and have used and refined its application over the past 20 years. It is a robust and reliable analysis indicator widely used in equity, currency and commodity markets. The GMMA can be applied in any time frame – daily charts, 1 minute charts, 1 hour charts etc. It tracks the psychological behavior of market participants. In FX markets, we use a Super Guppy to track the volatility clustering and identify trend change points. We include these notes for new readers. ED.

Identifying a trend breakout is the most straightforward application of the GMMA and it works well with "V' shaped trend changes. It was not about taking the lag out of the moving average calculation. It is about validating a prior trend break signal by examining the relationship between price and value. Once the initial trend break signal is validated by the GMMA the trader is able to enter a breakout trade with a higher level of confidence.
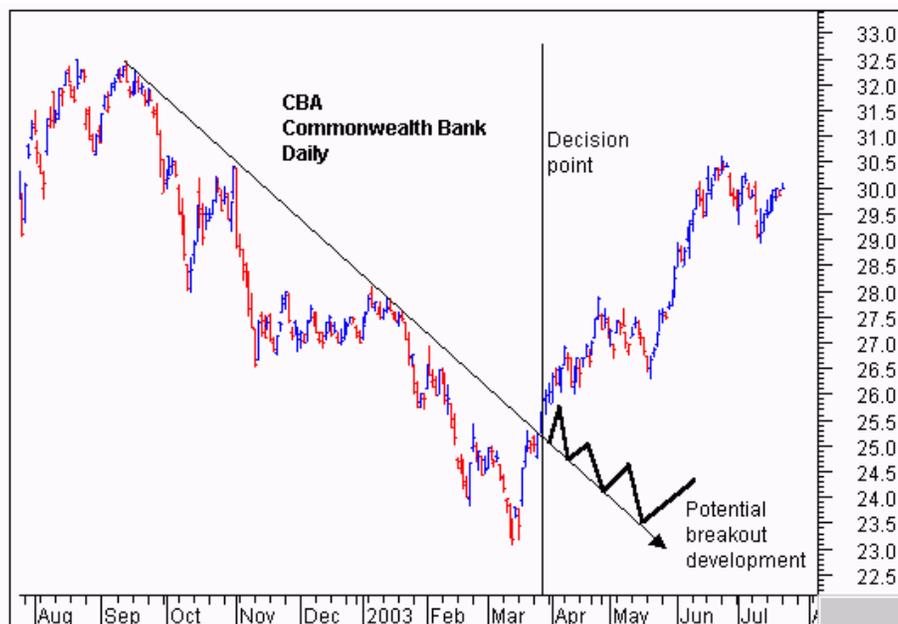
The CBA chart shows the classic application of the GMMA. We start with the breakout above the straight edge trend line. The vertical line shows the decision point on the day of the breakout. We need to be sure that this breakout is for real and likely to continue upwards. After several months in a downtrend the initial breakout sometimes fails and develops as shown by the thick black line. This signals a change in the nature of the trend line from a resistance function prior to the breakout to a support function after the breakout.

The GMMA is used to assess the probability that the trend break shown by the straight edge trend line is genuine. We start by observing the activity of the short term group. This tells us how traders are thinking. In area A we see a

compression of the averages. This suggests that traders have reached an agreement on price and value. The price of CBA has been driven so low that many traders now believe it is worth more than the current traded price. The only way they can take advantage of this 'cheap' price is to buy stock. Unfortunately many other short term traders have reached the same conclusion. They also want to buy at this price. A bidding war erupts. Traders who believe they are missing out on the opportunity outbid their competitors to ensure they get a position in the stock at favorable prices.
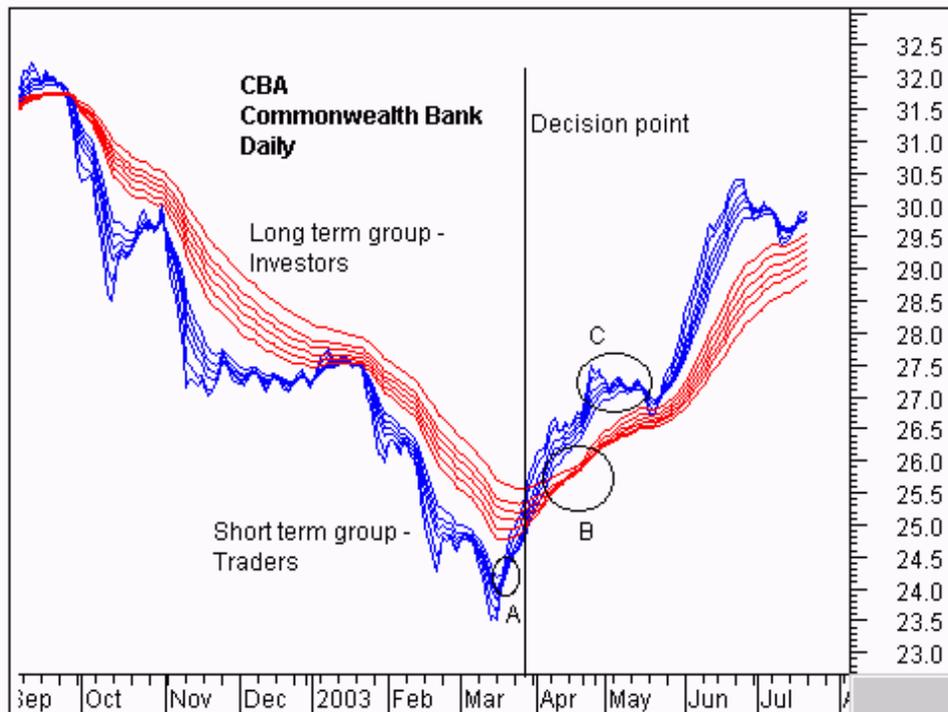
The compression of these averages shows agreement about price and value. The expansion of the group shows that traders are excited about the future prospects of increased value even though prices are still rising. These traders buy in anticipation of a trend change. They are probing for a trend change.

We use the straight edge trend line to signal an increased probability of a trend change. When this signal is generated we observe this change in direction and separation in the short term group of averages. We know traders believe this stock has a future. We want confirmation that the long term investors are also buying this confidence.

The long term group of averages, at the decision point, is showing signs of compression and the beginning of a change in direction. Notice how quickly the compression starts and the decisive change in direction. This is despite the longest average of 60 days which we would normally expect to lag well behind any trend change. This compression in the long term group is evidence of the synchronicity relationship that makes the GMMA so useful.

This compression and change in direction tells us that there is an increased probability that the change in trend direction is for real – it is sustainable. This encourages us to buy the stock soon after the decision point shown.

The GMMA picks up a seismic shift in the markets sentiment as it happens, even though we are using a 60 day moving average.. Later we will look at how this indicator is used to develop reliable advance signals of this change. This compression and eventual crossover within the long term group takes place in area B. The trend change is confirmed. The agreement amongst investors about price and value cannot last. Where there is agreement some people see opportunity. There are many investors who will have missed out on joining the trend change prior to area B. Now the change is confirmed they want to get part of the action. Generally investors move larger funds than traders. Their activity in the market has a larger impact.

The latecomers can only buy stock if they outbid their competitors. The stronger the initial trend, the more pressure there is to get an early position. This increased bidding supports the trend. This is shown by the way the long term group continue to move up, and by the way the long term group of averages separates. The wider the spread the more powerful the underlying trend.

Even the traders retain faith in this tend change. The sell off that takes place in area C is not very strong. The group of short term averages dips towards the long term group and then bounces away quickly. The long term group of averages show that investors take this opportunity to buy stock at temporarily wakened prices. Although the long term group falters out at this point, the degree of separation remains relatively constant and this confirms the strength of the emerging trend.

The temporary collapse of the short term group comes after a 12% appreciation in price. Short term traders exit the trade taking short term profits at this level of return and this is reflected by the compression and collapse of the short term group of averages. As long term investors step into the market and buy CBA at these weakened prices, traders sense that the trend is well supported. Their activity takes off, and the short term group of averages rebounds, separates, and then run parallel to the long term group as the trend continues.

The GMMA identifies a significant change in the markets opinion about CBA. The compression of the short term and long term groups validates the trend break signal generated by a close above the straight edge trend line. Using this basic application of the GMMA, the trader has the confidence necessary to buy CBA at, or just after the decision points shown on the chart extract.

Next week we look at using the GMMA to join a trend safely.