

How to follow Fibonacci ratio dynamic approach with volatility in intraday stock or commodity trading ?

This is the most successful way to make money in intraday trade. Just spend 1 hour to read and prepare your own excel sheet and try this method. Also back test it to realise the success of this method.

You can access a much advance tool developed using the same concept from the following link <http://www.smartfinancein.com/volatility-trade-calculator.php>

Most of the stock, commodity, currency traders around the globe has already experienced the power of Fibonacci ratio in deciding the trade. However I feel to put few words on its traditional way of practice while deriving a trade decision. Fibonacci ratio uses starts with the retracement principle and ends with parallel projection, growth projection, expansion, Fibonacci fan line and Fibonacci arc. Looking back in to the retracement principle we know it is of two type **a. growth retracement b. decay retracement**. Whenever the price of any asset fall from a high or retrace back from a climb or retrace back after recording an high it is called as decay retracement and vice versa. Let us see an example say nifty future after attending 5623 on 08th September 2010 has started falling down to 5580 this action of nifty future is known as **decay retracement**. Similarly say nifty future after attending 5580 on 08th September 2010 has started going up to 5608 this action of nifty future is known as **growth retracement**.

From the above discussion we have concluded that raise in price from a low or fall in price from a high is known as retracement. One thing is sure in both the cases of retracement is that the price action is getting set from a particular price point. This is called your prior trend. While applying the Fibonacci principle in price forecasting we need the prior trend. In other words in the previous time period what was the high and low. Let us take an example: say on 8th September 2010 at 11:30 a.m. I have identified the high and low of the nifty future as 5608 and 5580. This is known as the prior trend high and low.

In Fibonacci method trade practice we used to take the prior trend price and calculate the different resistance and support and decide the trade in 0.618 retracement level. This approach of Fibonacci application is known as the static approach. Why it is called static approach of analysis? Since the price point considered for the study is already happened. To make the Fibonacci retracement work dynamically and most effectively we need a **dynamic price point**. The dynamic price point is nothing but a high and low which has not happened in the chart and which is yet to happen in future. The 2nd property of the **dynamic price point** is it must be derived from a probability estimate. One such estimate which was neglected for years together by the traders community has the power to generate the dynamic price point is known as **“volatility”**. Volatility is the standard deviation of the price change as per the definition. Volatility can be calculated from the past closing or last traded price of the stock. Below mentioned are the steps I need to take to derive a trade decision based on the dynamic price point applied on Fibonacci principle.

- a. I will calculate the daily volatility from the past 10 day's last traded price data.

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- b. I will calculate the dynamic price point which is the expected high or low for the current day.
- c. I will use the last trade price of the previous day as the initial price point and expected high and low price point as the final point of the probability move.
- d. Then I will use the Fibonacci method on them and use the 0.382 price point as the trend estimation point.

In the above case I am assuming the trend is continuous and it will follow the same line during the day also. However in many days the price tends to open higher or lower which is known as the gap action. This too also called gap up or gap down opening days. If this gap is below my trend estimation point then I will not worry much. However if it happen to be above or below my trend estimate point hen it is a case of worry and this condition is alone sufficient to say that the current days volatility has gone up. In this case it is better if I will change the last record of my experiment with the opening price. This once correction will make the entire concept more dynamic and more user friendly.

Let me put an example to validate the dynamic Fibonacci ratio with the concept of volatility.

A	B	C	D		
Date	Price-sbi	Ln(current/previous)	(Ln(current/previous)) ²		
18-May-10	2280.35				
19-May-10	2208	-0.032241812	0.001039534		
20-May-10	2275	0.029892924	0.000893587		
21-May-10	2278	0.001317813	1.73663E-06		
24-May-10	2225.9	-0.023136537	0.000535299		
25-May-10	2160.1	-0.030006811	0.000900409		
26-May-10	2172	0.005493885	3.01828E-05		
27-May-10	2236	0.029040153	0.00084333		
28-May-10	2234.05	-0.000872474	7.6121E-07		
31-May-10	2263	0.012875285	0.000165773		
		-0.000848619	0.000490068		
	variance	0.000489348			
	volatility	2.212121169	daily volatility		
		50.06030204	Expected Daily return		
	daily return	2212.939698	Expected daily low		
		2313.060302	Expected daily high		
	31st close	2263			
	buy signal	2282.123035	31st close +0.382* expected daily return		
	sell signal	2243.876965	31st close -0.382* expected daily return		
	Open	High	Low	Close	LTP
01-Jun-10	2251.1	2276	2202.1	2207.45	2207.45

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The above table explains the detail dynamic approach of the Fibonacci concept. Let us have a look on it.

I have taken the **last traded price** of past 10 trading session of state bank of India. I have calculated the absolute return using the LN () function. Hence LN (19th may 2010 price/18th may 2010 price) will give the absolute return for the 19th may 2010. Similarly I have calculated the absolute return for all remaining days. Then I have taken the square absolute return or the second multiple of the absolute return in the second column “**D**”. After this step I will calculate the average **of absolute return** and **square absolute return**. Once this process is completed then I will calculate the variance by using the following formula.

$$\text{Variance} = \text{square absolute return average} - (\text{absolute return average})^2$$

$$\text{Daily volatility} = \text{square root of variance} = \sqrt{\text{variance}}.$$

All the above process we have done to calculate the daily volatility from its past 10 trading day's data.

In our example we have got the daily volatility as **2.21**. This says the stock has the probability of risk 2.21 % or it can swing 2.21 % in intraday basis from the mean point of 2263 (i.e. closing price of the last trading day of our observation).

Hence 2.21% of 2263= 2263* 2.21%=50.06. So we can conclude the next trading day which fall on 1st June 2010, the stock has the chance to touch 2263+50=2313.06 in upside or it has the chance to touch 2263-50.06=2212.94.

Now we got 2 dynamic price points which has not occurred in the price time chart and has the great possibility to occur in future. Considering above two price points one as swing high and other as swing low and initial price point as 2263 we will derive the trend now.

2263+0.382*50.06=2282.12 (this price will set the Fibonacci growth retracement and it has the chance to move to 1.618 retracement level).

2263-0.382*50.06=2243.88 (this price will set the Fibonacci decay retracement and it has the chance to move to 1.618 retracement level.)

Hence we can use the 2282.12 as a trend confirmation point for the up trend and buy for the target of 2313.06 and 2243.88 as the trend confirmation point for the down trend and sell for a target of 2212.94.

Between the trend identification and final target 0.5, 0.618, 0.786, 1, 1.272, 1.618 Fibonacci ratios must be used to derive the intermediate targets.

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Above dynamic approach of the Fibonacci method will hold good if the gap up or gap down opening in the next day happens in the range between **2282.12 and 2243.88**. Slight deviation till maximum 1% above or below this trend identification point will not bother me a lot and I can initiate the trade. However if the gap up or gap down opening will be more then this threshold price points then I will change the 31st date price point with the opening price point. This will take care of the volatility raise or fall condition and this will give me the new dynamic Fibonacci price points. Some time also I will achieve the final target points after initiating the trade. If I will think beyond or “what next beyond this final target points?” then I can change the 31st may or the last data record of my experiment with the final target point and get the new dynamic price points. To validate the success of this method I have given the 1st June 2010 OHLC date for your reference in the same table. You can view more examples from [my video webinar recording by following this link](#).

With smaller data set and using the various other methods like gann, Fibonacci and Elliot principle we have developed a comprehensive calculator using the volatility. This will help you in deriving the intraday trade decision. However the paid version of the tool will help you in option trade and short term investment decision also. [Access the wonderful free tool](#) To take intraday trade decision.

Future event or happening is not scaled by any tool till date however the rational approach of estimating the future happening will yield greater success as compared to the other approach.