On the Profitability of Technical Analysis:

A case-study of Gold Market

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ABSTRACT

Technical analysis is the use of past price actions, to guide future trading decisions in asset markets. Technical Analysis attracts the attention of economists as its successes cast doubt upon the Efficient Market Hypothesis (EMH) which states that market prices instantaneously and fully reflect all relevant information and therefore, the prices follow a random walk. EMH holds that publicly available information, such as past prices, should not assist traders in earning unusually high returns.

Our study shows that the inefficiencies is present in the gold market during the studied period of last ten years and even after adjusting the transaction cost of bid-ask spread, one can consistently capture these abnormal returns. A total of 333,234 static filter rules were applied on gold market to test their profitability. These filters generate buying or selling signals based on given conditions. During this study 8.24% of filters outperformed the benchmark of passive buy-and-hold in long-term investment of ten years and 1.02% filters are those which consistently beat the market every year during the last ten years. So out of 333,234 filters, 3,397 beat the market every year. But to eliminate the crash risk and limit of risk exposure, we are more interested in filters having “Stop-Loss” limit of less than 17%. Out of 3,397 filters, 531 are of this type. Finally we end with 531 filters which are most consistent, stable and reliable, and also prove the inefficiency of gold market.

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TABLE OF CONTENTS

LIST OF FIGURES

LIST OF TABLES