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ANALYSIS MECHANISMS OF FINANCIAL MARKETS. FUNDAMENTAL ANALYSIS AND TECHNICAL ANALYSIS

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The financial market is a set of forms of trading in financial assets: foreign exchange, securities, loans, deposits, financial derivatives. The financial market includes the stock market (stock exchanges), the credit market (banks, investment and dealer companies, pension funds), capital markets (insurance, mortgage, interbank capital), and the world currency financial market. On the other hand, the financial market is a certain trading mechanism and a certain organized trading platform where various financial instruments are bought and sold.

A financial instrument is any standardized financial contract, or, for example, a stock or a bond. There are several types of financial markets. For example, the stock market is for trading stocks, or the foreign exchange market is for trading currencies. In any financial market, there are quotes (prices) that reflect the value of certain traded financial instruments. Quotes are constantly changing in accordance with the macro- and microeconomic factors acting on them. It is these changes in quotes that allow traders to make money by buying and selling traded contracts at a selected time.

The most interesting of the financial markets, the most accessible and the easiest to understand for many people is the foreign exchange market.

In order to find out what will happen to the currency tomorrow, or, in other words, to predict its value for a certain period of time in the future, you need to know and understand the basic methods of analyzing foreign exchange markets. At the moment, the main and confirmed by practical use of two methods are fundamental analysis and technical analysis.

Obviously, fluctuations in the value of currencies arise as a result of the impact of certain specific factors and these fluctuations have a certain specific form of their change, that is, they have a structure of fluctuations in value, or rather, fluctuations have a certain "picture" of price fluctuations.

So, the factors that affect the currency are studied by fundamental analysis, and the structure of price fluctuations is studied by technical analysis.

Fundamental analysis examines the factors that affect exchange rates. Fundamental analysis is the study of the influence of the politics and economics of countries on the exchange rates that interest us. Within the framework of fundamental analysis, various messages of monetary and financial events in the world, the phenomena of political and economic activity, both in individual countries and the world community as a whole, are studied. The study examines such factors that may have an impact on the development of the foreign exchange market. Fundamental analysis is an analysis of the above factors in order to predict the exchange rate.

Here information about the work of stock exchanges and large commercial banks, interest rates of central banks, the economic course of the government, possible changes in the political life of the country, as well as all kinds of rumours and expectations are important. All of the above is called fundamental factors, and you can learn about them from the news or various economic statistics.

Fundamental analysis is one of the most difficult and at the same time one of the key ones for forecasting in the foreign exchange market. It is much more difficult to carry out fundamental analysis than any other, since the same factors in different conditions have an unequal value on the market or can turn from the main ones into absolutely insignificant ones. In addition, fundamental analysis is very voluminous in terms of the processed information base, as it requires knowledge of economic theory. That is why fundamental analysis is difficult for many people or inaccessible because they do not have in-depth knowledge of the market economy.

Fundamental analysis makes it possible to identify both long-term and short-term changes in exchange rates. Example: one option, if there is news about an increase in inflation in the country. Inflation is the actual depreciation of the national currency (Zaitsev, Monetary Inflation…, 2016). After the release of such news, this news becomes a fact and the rate of the national currency in relation to other world currencies will fall within usually 1–3 hours. The second option, if we take in aggregate various factors and understand that all of them, in one way or another, have a negative character for the country's economy, then we can safely conclude that in the long term, and this is from a week or more, the rate of the national currency will also decline. In fundamental analysis, four types of fundamental factors are distinguished: 1) economic factors; 2) political factors; 3) rumours and expectations; 4) force majeure circumstances.

Technical analysis is the study of the price structure of the markets. But then you need to know how to understand and "see" this structure, how is it displayed? What is there in the market that responds to any changes or events related to the markets? Of course, this is the price of the product. In the case of the International Foreign Exchange Market, it is the value of one currency denominated in another. But the price at a particular point in time says little. But if we consider the price in different periods of time, then we will see a change in the history of prices, and this is the structure of the foreign exchange market, and these are the facts about how the price has changed over time. This is what gives us the ability to predict the price in the future. It is also necessary to determine how prices are formed in the foreign exchange market or the financial market in general? The price of a commodity is the value at which the buyer and the seller on the trading floor (financial market) agree on a deal, and this deal takes place. Based on this, we can say that the price reflects the balance between supply and demand at a certain moment. Moreover, the most important thing in this definition is that it is absolutely not important for a technical analyst, namely, it does not matter what caused this equilibrium and what factors influenced this equilibrium, it is only important how the price changed in comparison with the value that was fixed before.

For the greatest clarity, analysts and speculators use various charts when conducting technical analysis. This is the easiest, most affordable and most reliable way to compare prices over time. Thus, technical analysis is the study of price changes by studying charts in order to further predict future price changes. Types of charts:

a) Linear Chart. At a certain time interval, the price has its price, so we get points that are connected by lines and get a line chart.

b) Bar`s Charts. Bars represent not a single price display at a certain time interval, but several prices in this time interval. The bar fixes the highest price for a certain time interval (High price). The lowest point of the bar displays the lowest price for a certain time interval (Low price). The bar displays the Open price, it is the very first price fixed in the given time interval. The bar displays the Close price, it is the most recent price fixed in the given time frame.

The Line chart does not show if the price rose or fell within the time frame, but the line chart shows the change from previous prices. But the bar`s chart shows what happened within the interval. If the opening price is lower than the closing price, then within the time interval the prices grew, if on the contrary, then the prices within the time interval fell.

c) Candlesticks Chart. These charts display prices in the same way as the bar`s chart, but with a different symbol, which is named candlestick.

The founder of technical analysis is the famous Charles H. Dow, (1851–1902), the creator of the Dow Jones`s index and the company of the same name, which still exists and works in the field of financial markets. He laid out the basic ideas of technical analysis in the Wall Street Journal, published in the late 1890s. And after his death, the followers gathered together Dow's ideas, and technical analysis appeared on their basis.

Technical analysis has three postulates. Just as Euclidean`s geometry is based on axioms, so technical analysis is based on three postulates. These are postulates about price changes.

Postulate 1. Prices take into account everything. All factors, all events that are associated with the product or with the currency, will be displayed in the price. Such a mapping will take into account all factors in their mutual influence. This is what the postulate says in technical analysis.

In this postulate, in our opinion, there is a hidden error. We agree that “prices take into account everything,” however, money itself changes its value over time and, therefore, a change in the value of a commodity or currency in monetary prices does not always indicate an actual change in the value of a commodity or currency. Postulate 1 assumes that the value of money is unchanged and constant, but this is far from the case (Zaitsev, 2015; Zaitsev, Objective value…, 2016; Zaitsev, Obiektyvna vartist…, 2016; Zaitsev, 2017; Zaitsev et. al., 2017). It is advisable to supplement the postulates of technical analysis with the new postulate "zero". ***Postulate "zero"*** is formulated as follows: monetary units that participate in price indicators have their own internal exchange value, which is constantly changing.

Regarding postulate 2 (see below), there is no objection. However, one must understand that the price trends that are displayed on the charts are influenced by the intrinsic value of money as well.

Postulate 2. Price movement is subject to trends. A trend is a directional movement in price. The concept of trend is one of the fundamental concepts in technical analysis. It is necessary to learn that everything that happens on the market is subject to certain trends. The main purpose of charting and studying price charts is to identify these trends in the early stages of their development and trade according to their direction.

Postulate 3. History repeats itself. Trading in the foreign exchange market is mainly the psychology of its participants, and since the psychology of people does not change over the years, it can be assumed that the way the participants behaved in the past, so they will behave in the present or in the future.

Accordingly, the actions of the participants are reflected in the price, which means that certain price behaviour in the past will be repeated in the present and in the future.

Recently, there have been many publications of the following content: "Why technical analysis doesn't work" (Ken, 2017; Bailey, 2019) or "Debunking 8 myths about technical analysis" (Seth, 2020). Such publications talk about many problems of technical analysis, but nowhere and no one paid attention to the correctness of plotting price changes. Everyone thinks that when building a price chart, prices are taken at a given moment in time and is considered as another postulate that money does not change its intrinsic value over the course of its functioning. It is believed by tacit agreement that each of all monetary units that form prices show the same value as a year ago, as now, and a year in the future. But this is not the case. Monetary units change their value in every transaction in which they participate. We draw your attention to the fact that charts of price changes for technical analysis must be built taking into account the intrinsic value of money. Price charts constructed in this way will differ from existing price charts and, therefore, may show other trends compared to traditional charts.

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