LESSON 4: STOCHASTIC OSCILLATOR

Forex Training Summary and Quiz

Stochastic Oscillator in Forex

Stochastic Oscillators were developed in the late 1950s by George C. Lane and are used to help predict the future direction of an exchange rate.

The Oscillator scale ranges from 0 to 100.

When calculating the strength of a trend, the Stochastic Oscillator defines and *uptrend* as the period of time when rates remain equal to or higher than the previous close, while a *downtrend* is the period of time when rates remain equal to or lower than the previous close.

The Full Stochastic consists of two stochastic lines - %K and %D where:

%K tracks the current rate for the currency pair

%D is a moving average based on the %K line - the fact that it is an average of %K means that it will produce a "smoothed out" version of %K

The %K line is commonly referred to as the Fast Stochastic as it moves with changes in the spot rate while the %D line - which is a moving average of the %K line - reacts more slowly to rate changes. For this reason, it is often referred to as the Slow Stochastic.

Crossovers occur when the %K line intersects the %D line. When %K crosses over %D, the spot rate is increasing and this is viewed as a *buy* signal. When %K crosses under %D, the spot rate is falling and this is interpreted as a *sell* signal.

Divergence refers to the gap between %K and %D - an *increasing* divergence is a signal that a rate reversal is likely as the %K stochastic is moving at a faster rate than the %D Stochastic.

Overbought / Oversold - when the %K Stochastic moves above 80 on the Oscillator scale, the currency pair is considered *overbought* and a rate reversal to a decrease is likely. When the %K Stochastic moves below the 20 level, it is considered a sign that the currency pair is *oversold* and a rate reversal to an increase in expected.

Putting It All Together

1. The Stochastic Oscillator provides feedback on _________.

market volatility

potential future market direction

the crossing point of the slow moving average

historical prices

2. The %K line is known as the _________.

exchange rate

liquidity rate

stochastic slow

stochastic fast

3. The %D line is known as the _________.

exchange rate

liquidity rate

stochastic slow

stochastic fast

4. When the %K line crosses over and moves above the %D line, this is a _________.

buy signal

sell signal

indication of market uncertainty

sign that volatility is increasing

5. When the %K line crosses over and moves under the %D line, this is a _________.

buy signal

sell signal

indication of market uncertainty

sign that volatility is increasing

6. When the %K line climbs to 80 or higher in the Stochastic scale, the currency is said to be _________.

overbought

volatility

oversold

oscillating

7. When the %K line falls to 20 or lower in the Stochastic scale, the currency is said to be _________.

overbought

diverging

oversold

retracing

Score 7/7

Reset Quiz SUBMIT QUIZ

START LESSON 5

Please refer to our more detailed Risk Warning, and NFA's FOREX INVESTOR ALERT.