The Bitcoin Roller Coaster Is Just Warming Up

Description

Bitcoin has been on a wild ride lately, and there's no reason to expect that to stop anytime soon. Year-to-date returns of over 1,500% have been generated for those that bought when the cryptocurrency was less than US$1,000. In just the past three months, the price of Bitcoin has nearly quadrupled.

However, since closing near US$19,000 more than a week ago, Bitcoin dropped to under US$14,000 on Christmas Day, which could have resulted in a nasty fall for those buying at the peak.

I don't refer to buying Bitcoin as an investment, because it isn't. Buying Bitcoin is purely speculative, and these wild swings in either direction do nothing to prove otherwise. What Bitcoin does is remind investors the dangers that can be prevalent when buying strictly for speculative purposes or trying to read and predict chart patterns.

Technical analysis can be useful, but don't rely on it

There are some technical indicators that you can use to help you spot a stock that is due for a recovery, like the Relative Strength Index (RSI), which is one I've found to be very useful.

Early in December, I'd mentioned that **Hudson's Bay Co.** (TSX:HBC) was oversold and could see a reversal, and the share price has risen more than 6% since then.

At the end of November, I'd also pointed out that **Just Energy Group Inc.** (TSX:JE)(NYSE:JE) and **Winpak Ltd.** (TSX:WPK) were oversold as well. Although Just Energy would go on to rise ~3%, Winpak ultimately declined further after initially seeing a bit of an improvement in its share price.

Using technical indicators like RSI can certainly help you assess a stock, but that shouldn't be the basis of your investment decisions.

With all the technology and tools available today, if technical analysis was really as successful as many would have you believe, Warren Buffett wouldn't still be one of the richest people alive.

Why investors shouldn’t ignore fundamentals

Fundamental analysis involves looking at a company’s financials, its competitive advantages, and overall position in the industry. This information is what will ultimately show where the company is headed in the long term.

It may not be an exciting way to evaluate stocks, because a stock with good fundamentals may still be an underperforming one. That doesn’t mean that the company is a bad one or that your analysis was wrong, but there may be industry or market conditions that are weighing down the share price.

In some cases, it may just be the result of a big investor reshuffling their portfolio. A big sell-off could trigger stop losses, and before you know it, the stock is in a free fall.

Bottom line

There are a lot of overvalued stocks both on the TSX and on the U.S. exchanges right now. It may seem like share prices will only keep going up, but the market has crashed before, and will again.

The danger with hype is that it can quickly turn into paranoia. A stock that seemed on an endless pursuit up in price could quickly see a significant sell-off; just ask investors of **Shopify Inc.** (TSX:SHOP)(NYSE:SHOP).

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