

Implications of the Forex Market

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G'Day Trader,

During *real money trading* and *testing* we can discover many-many obvious regularities on the chart. It is very interesting because although they stick out a mile we can not realize them until we lose our money on them.

After I had the same situation many times I specified my *trading rules* to avoid them so I don't lose any more on them. Moreover, they put me in an advantageous situation as I can see the market movements from a different view now. Doing that it makes those fuzzy situations clearly understandable and tradable.

In the following articles I'll reveal 7 of my researches in detail, like these:

Thesis #1: What if the market is random after all (say makes unpredictable, random movements)?

Thesis #2: What if the 'regular' timeframes have a big trick to cheat you?

Thesis #3: What if the most popular M15 (15 minutes) chart is not the best timeframe to trade?

Thesis #4: What if the correlation is too strong?

Thesis #5: What if the more volatile is not really more volatile?

Thesis #6: What if the trend changing patterns don't change the trend most of times?

Thesis #7: What if the Technical Analysis is not the problem?

These notes apply to Forex market; they are very similar to the share market (or commodities) results, but obviously there are a couple of significant differences due to their trading hours, liquidity and volatility differences.

Thesis #1: What if the market is random after all (say makes unpredictable, random movements)?

According to a few but very serious theories *price movements* can not be calculated in short and middle term; but they are predictable for a longer time. Obviously, the term 'longer time' is always relative (we are talking about the World's fastest and biggest market: *Forex*) but all traders should understand and accept some important statistical facts:

The definition of '**market noise**' is well known by everyone. In practice it means an unpredictable (random) *price movement* which is totally incoherent with the *impulsive direction*; it reflects the *balance of buyers and sellers* in a moment; and that's the point: just in a moment. There is no relation with the main direction.

It's like when you go to ex. Surfers Paradise from the Elisabeth St, Brisbane CBD. It can be opposite way when you get out from your parking place or you can go at right angles to it when you turn to Edwards St. Those directions are just temporary (or I should say momentary) movements, and no one can predict the main direction from those movements.

But if we observed your movement on an hourly '*time frame*' that more likely would point towards your main direction (or very close to that).

Well, we have the same situation here, on the *Market*.

I am convinced that on *M15 (15 minute chart)* and/or below that we *trade* in the '*market noise*'. The chance for reaching your *Profit Target* or your *Stop Loss* is almost the same (for a long time and for a series of trades) and it's no more than fifty-fifty (based on *Risk Reward Ratio*= 1:1. It is easy to prove mathematically that if you want to go for more advantageous *Risk Reward Ratio*, say 1:2, you will have much worse chance for *winning trade*; you can not even maintain the 50-50% under those circumstances).

When you spot a pattern on *M5 (5 min chart)* you only catch the momentary movement; probably it's just like turning to Edwards St., or reversing out from the parking place.

If it was a losing trade you would be disappointed and would start not to trust that pattern. If it was a winning trade (it could be, remember: fifty-fifty) you would get more confident and would continue on. Most likely just until the first massive draw down when you would be disappointed again.

And hold on a minute here, please. Just because you had a winning trade it wouldn't prove that you are on the right track; one *winning trade* couldn't confirm your rights.

If you played *head and tail* (proven 50-50% 'strategy') and you would have 5 *winnings in row* (could happen, right?) it wouldn't confirm that it was a proven *lucrative strategy* for a long time (series of games). It shouldn't authorize you to raise your *capital* or rely on that '*strategy*' and base your *financial future* on that. Those cases give you false confidence and embolden you to take more risk for bigger loss – which comes sooner or later. It is not a prophecy – it is pure math and *probability theory*.

You can show me however many *price patterns*, *candlestick patterns* or any other *Technical Analysis signals* evolving on those *time frames* (M15 and below) and I can show you the same amount of counter-examples (which go to losing). I believe that you already saw them, yeah? Just probably couldn't understand why. That's why. That's fact.

My tested and proven opinion is that: H1 and D (1 hour and daily) charts provide the most reliable result (on Forex market) in the determination of the main trend more details later in Thesis #2).

On M15 and below one can reach long term success with applying only mathematical and/or Money Management strategies or with their combination.

Thesis #2: What if the 'regular' time frames have a big trick to cheat you?

We all know that *Forex Market* is an OTC market and being that it is not a centralized market. What it means for us is different *brokers*, different *platforms*, different time zones causes big differences on the charts, in time, in price (scale) and in their representation on the charts, as well, of course.

Obviously, the *M15* (15 min chart) and *H1* (1 hour chart) have to show the same pattern (almost the same: due to different brokers' *spreads*, the bid and ask charts look a little bit different; price just below the line here and just broke out there). It is not a big deal; it is easy to skip this issue.

But we have a really big concern with H3 and H4 charts (3 hours and 4 hours chart).

First, lots of *brokers* and their *trading platforms* support the *H3*, while others (say another half of them) prefer *H4* charts. It is very rare to find a broker which supports both. OK, -you could say- who cares, trade on the chart which you happen have. Moreover, you can easily download and apply a simple script in *MT4* to 'create' a *H3 chart* – no problem.

It could be true – but the whole story unfortunately points further: the more people trade the same direction at the same time (with the same signal?) the higher the *buying (or selling) pressure is*, so the higher the price movement is in that direction. We call that symptom '**self fulfilling prophecy**'.

If everybody recognized the same *buy signal* on *H3* chart and pressed the BUY button at the close of that *candlestick* at the same time then it would cause a high *buying pressure* and guess what: the price would increase and go to North. Unfortunately, 'the half of the World' couldn't even see this signal, because they don't even have *H3* chart to watch; they are staring at *H4* where the actual candlestick is still moving, hasn't close yet; or the *signal, pattern, break out, indicator cross* or whatever it is hasn't evolved yet.

Fact is fact: the *H3* and *H4* divide the traders (and their buying-selling power) on the charts.

The second concern is more significant: different *brokers* and their *trading platforms* works with different time zones (time gap). Because of this very reason *candlesticks* open and close at a different time.

Let's suppose that a *candlestick* on 3 hour chart opens at midnight at New York time and closes 3.00 AM, then the price movement at a London broker is going to be slipped away by 2 hours because their time gap can not be divided by 3 (5 hours). So, the same chart at London broker shows different *candlesticks* (with different open and close prices) which additionally close at different times. As a result, *self fulfilling prophecy* fails to come out and we have no chance to press the button at the same time on *H3* chart (or on *H4* it's doesn't matter now). Consequently we don't have a chance to get in the *break out* and we are just wondering why the price jumped out suddenly (in the middle of the candlestick). Well, that is why.

We have exactly the same with *D (daily chart)*.

Foreign Exchange market is open 5 x 24 hours all around the World.

One broker counts a day from New York midnight to midnight, the other one from London midnight to midnight and another from Sydney midnight to midnight. Those *daily candlesticks* on 3 different (time zones) *trading platforms* look different as their open price and closing price are never the same. Obviously they move in the same *price range* in the same main direction but they form different *patterns* and *signals (price patterns, candlestick patterns, break outs, indicator crosses etc...)*; the whole chart shows different picture in its detail.

Have a look at this:



Significant differences can be noticed in *daily candlesticks* with these two big brokers: **Oanda** (USA) and **Saxo** (EUR) *daily charts*. Compare the zoomed area #2, #3 and #4 candlesticks (#3 even has a different colour – different daily direction) or have a look at #7: it is a proper *Key Reversal pattern* on *Oanda* (upper one) while on *Saxo* it is still waiting for confirmation. Probably it is worth spending a couple of minutes to observe these charts – or even yours. You will find them very similar in many cases but there are many differences in evolving trading signals. Unfortunately, its going to be the same with observing a H3 or H4 charts, as well. You should watch other charts too to be able to interpret price movements and see what others trade, what the masses trade – as they make the price move.

The biggest issue on Forex market is the time gap.

H1 (1 hour chart) shows almost the same picture on all trading platforms; the other time frames come with significant differences in their formation. (obviously time frames below H1 – M30, M15, M5 – show the same picture but they are not reliable enough in the determination of main trends and signals – see Thesis #1.) I don't want to say that they are not suitable for Technical trading; I just want to say H1 gives us the most considerable signals.

Thesis #3: What if the most popular M15 (15 minutes) chart is not the best time frame to trade?

Those too, who have much bigger database than I have, claims that M15 (*15 minutes chart*) is the most commonly traded *time frame*. This is a statistical fact.

Unfortunately, this is a fact too, that approx. 90% of *traders* lose and only 10% win on the *Forex Market* (for longer term). If you are familiar with set theory you can easily come to the conclusion that the most of M15 *traders* are losing. That is another statistical fact.

I strongly believe that M15 movements (*time frame volatility*) are still in the market noise, say it's not certainly related to the main direction. I can support my opinion with the statistic of more than 7500 *trades* which well describes the reliability of M15 *trading signals*.

M15 Technical Trading signals reach the reliability which is sufficient enough for considerable trading only and exclusively when they coin side with the impulsive movement of the longer time frame.

Without a preliminary and thorough analysis of the longer *time frames* *M15 Technical Trading Signals* itselfs don't provide the reliability which is suitable for lucrative *trading series*.

Yes, I am still using M15 for *trading*, but not for *decision making*. I make my trade decision on a *longer time frame* and I use M15 only for timing the *entry point* (in direction of decision I made).

There is one more very negative feature of 15 minutes time frame, namely from psychological consideration: this *time frame* is short enough for sitting in front of your computer to watch your *trade* even 8-12 *candlesticks* long (8-12 x 15 minutes = 2-3 hours). On the other hand it is long enough to be affected emotionally by your trade. When the trade is 'under the water' (even if just temporarily) you are anxious about that; when it is in *positive balance* you get excited about not to turn against you.

Because of this very reason many traders experience high pressure and stress during their trades on M15 chart.

Managing the same kind of *trade* on *H1 (hourly chart)* or even on *H3 (3 hours chart)* looks easier because no *trader* can sit 8-12 *candlesticks* long on those *time frames* (8-12 hours or even one and half day). In this case most likely you just place your *trade* and check that regularly; most of its time you will be sleeping or working: price may hit your *Profit Target* or your *Stop Loss* by the time you wake up without having any stress.

M15 time frame is certainly not the most ‘confident’ time frame; for those who are susceptible to worry and/or to stress during trading, M15 time frame intensifies this effect. It could be a good idea to think about choosing a longer time frame to trade more confidently.

Thesis #4: What if the correlation is too strong?

During planning and executing your *trades* you should watch for *correlation* (and *opposite correlation*, as well) because they have very big effect on your *trading* results. In ideal case you should share your risk between 8-12 different and independent investments which have no or low correlation; that’s what we call *diversification* – it’s a very important part of *Risk Management*.

Unfortunately, in real life it is almost impossible on *Forex Market* as we have limited numbers of *currency pairs* to choose from and they are far from independent.

Currency pairs on *Forex Market* could have strong *correlation* – it is easy to see at the first sight: it is so obvious when we are talking about EURUSD and AUDUSD which are correlated on ‘USD leg’. For this very reason both of their movement strongly depend on USD’s strength (or even its weakness). Their *correlation*, of course, especially on different *time frames* -hourly or daily- depends on many other factor, as well: their actual *supply-demand*, their *high time zone*, their *news time*, etc.)

Statistical fact: nowadays, the most commonly and with the highest momentum traded currency pair, the ‘boss’, the ‘market indicator’ IS the EURUSD.

While EURUSD is in its narrowing phase (for example its in ‘Asian range’, when London, the World’s Financial Centre sleeps) and didn’t ‘provide’ direction, the other pairs are usually not able to break out or reach new highs or lows; they are just mainly sideways or their weak attempts are forced back.

In contrast, when EURUSD gets moving -even if its just temporarily or a *false break out*- it ‘sweeps along’ the other pairs. The movements of main pairs (the other 3 main -besides EURUSD: USDJPY, USDCHF and GBPUSD) strongly depend on EURUSD and the exotic pairs’, as well, even if there is no logic relation at the first blink.

The actual direction of the whole currency market is strongly influenced by EURUSD and its’ attraction and its’ repulsion. (each currency pairs’ have their own ‘personality’ of course, but they correlate with EURUSD to a certain extend most of time.)

Because of this reason similar *trading signals* could be find at the same time on different (currency pairs’) charts.

It could be very risky if -misinterpreting the *Money Management* rules- ones traded many of those signals (or even all) at the same time (could form on 4-5 different currency pairs at the same time, mostly in shorter time frames – on M5 or on M15). If they came out with winning they would give a heavenly feeling; but if they turned out with losing, which also could happen, they would cause a massive loss.

Unfortunately, we have the same issue with opposite correlation.

Obviously, the opposite correlating pairs move in opposite way so when the *trading signals* are coming, they are forming in opposite way.

At the first sight they look good as it seems to be a proper *diversification*: for example EURUSD long and USDCHF short. In real, if USD strengthened for some reason (news) EURUSD long would fall back causing loss; and USDCHF would break out up, causing another loss (opposite correlation on USD legs).

The opposite correlation comprehends the same risk as the straight correlation does.

One of the best solutions could be if, with a well-thought and properly applied *Money Management*, you shared the risk between the correlating or even between the opposite correlating *currency pairs* and you opened partial positions on each. Most of time it doesn't happen, because of greed, does it?

The 'perfect' solution could be if we could trade on non correlating currency pairs – but they only would be rare exotics with low liquidity, which wouldn't be suitable for regular *trading*.

Whether you like it or not, trading on Forex market is definitely not diversified trading; it is concentrated trading. One can reach diversified trading on Forex market with applying different (time frame) strategies (diversification in time: scalp, intraday, semi-swing, swing, carry, etc).

Thesis #5: What if the more volatile is not really more volatile?

I have heard that many times -mostly from beginner *traders*- he/she prefers *cable* (*GBPUSD* – instead of *EURUSD*) because *cable* is more *volatile* so he/she could make even 70-80 pip while only 40 on *EURUSD* with the same pattern. Unfortunately it is an unreal approach.

Obviously, if on the *currency pair*, which looks more *volatile*, a *Profit Target* of that certain pattern is 80 pips, then its *Stop Loss* order (example: *Risk Reward* = 1:1) will be at the same distance, say 80 pips. If we had a same pattern evolved on EURUSD and its *Profit Target* was only 40 pips away than its *Stop Loss* would be the same again, 40 pips. Keeping the same *Money Management* rules the profit is going to be exactly the same in both cases because on EURUSD we could double size the position having the same risk (lower *Stop Loss* distance allows bigger *position size* with the same risk). Measuring the ‘efficiency’ of the given *currency pair* is very difficult because it depends on many other factors (personality), but if we had to do it anyway (apart from reliability!) then it should be the proportion of its *volatility* (ex. ATR) and its *spread*.
Clearly: how big the expectable movement is and how much it costs.

If the expectable movement was high with relatively low cost, it could be a favourable *currency pair* (if the other factors, like the number of *trading signals* and their reliability is roughly the same). By the way it is not a big surprise that some brokers (example: Oanda) ‘price’ the spread based on the actual *liquidity* of the *currency pair* so it should not influence our decision to choose a *currency pair to trade* (a couple of ‘Genius’ sits at every broker who knows that and can complete a simple division even during news time 😊).

Briefly: choosing a currency pair to trade, we only need to watch for the parameters of strategy (numbers of signals, Risk Reward Ratio, reliability and biggest drawdown); the apparent volatility of that currency pair would not be relevant.

Thesis #6: What if the trend changing patterns don’t change the trend most of time?

The reliability of the *trend changing patterns* evolving on a shorter *time frame* (M1, M5, M15) is middling and untrustworthy. The reason behind that is to be found in the scale of their movement which still should be considered as *market noise* (we were already talking about it earlier).

The observation of a *previous trend* is essential in *trend changing patterns*; and many traders are satisfied with this: there is nice *trend changing pattern* with a full-screen filling *previous trend*, let’s jump into the *trade*.

The question still remains that if it was a *15 minutes time frame trend* or a much longer, even a *daily trend*. A *trend changing pattern* –even if it reaches its *Profit Target* – is only going to be a *counter trend*, or *dip* in the main – daily – trend but can not reverse that.

Unfortunately, they don’t reach their *Profit Target* most of the time, or they just hit the 161.8% of the distance and we can even feel lucky.

A questions arise in beginner *traders* that what it depends on, when it reaches the 161.8%, when the 200% and when it exceed far above that (yes, we are greedy, it would be awesome if the *trend changing pattern* – according to its name - reversed the trend and we could ‘travel’ with the newly formed trend, reaching multiple *Risk Reward Ratio*).

A trend changing pattern to fulfill its purpose should reverse the whole valid trend.

A *trend* formed on *daily chart* is most likely to be reversed by a signal observed on the *daily chart* (as well). *Trend changing patterns* evolved on a *shorter time frame* don't reverse the *long term trend*; they only cause a corrective movement in it. Obviously, they fail most of the time because it is just a small *correction* compared to the main *direction*.

So what does the effectiveness of a *short term trend changing pattern* depend on?

It is clear now: on the proportion of the distance of *Profit Target* of the actual pattern and the *long term trend* length.

If the *Profit Target* determines relatively low distance it can be reached, because it is still covered by the movement in *market noise* or just fit in the *corrective movement of the main trend* (maximum 19.1-25.00% of the last *impulsive movement* of the *long term trend*)

The reliability of those patterns which directions match with the long term trends are much higher. Those positions actually formed in the dip of the main trends in directions of the main trends (buy in the dip).

If one goes against the direction of the *long term trend* (eg. LONG) most likely gets in the market in direction of SHORT at the very bottom of the *dip*. Right after that the *corrective movement* ends and the *main trend* continues activating the *Stop Loss order* (I don't even want to think about if one has no *Stop Loss order* and the main trend goes AGAINST him/her).

I saw a ‘trader’ who lost his total assets in less than 10 days on less than 10 trades in case like this. 😞

Thesis #7: What if Technical Analysis is not the problem?

Everyone is capable to learn the science of *Technical Analysis*. I mean at least to a certain level.

Market participants have the same or very similar trading and preparing conditions. Free/or very cheap *trading tools, trading platforms, news, data feeds*, etc. widely available on the Internet.

Although, 90% of *traders* are still losing money.

Tons of educational/instructional materials available for free or for charge. They copy the materials and share them. They copy well developed *trading strategies* and share them; and still: 90% of traders are losing money. During trading they can use everything that can help: tutorials, books, videos, examples, *trading rooms*, skype, phone, cheat sheet, everything; and still: 90% of *traders* are losing money.

In contrast, if I close my eyes, don't even turn on my computer, don't even watch any chart for a week and I make a decision to buy or sell something I have 50% chance to be right and win (in case of having *Risk Reward Ratio* = 1:1).

Like playing Heads and Tails, right? Probably, I'll have 5 losing in a row or even 5 winning in a row. But out of 1000 'blind' trades I must I have to win around 500 and I have to lose around 500, that's for sure. (I will be in a slightly negative balance anyway because of the brokerage *-spread, commission-* as I have to pay for that both at winning and losing trades). It is mathematical fact.

The only question remains that – and I am very serious now: if one could be in 'slightly' negative balance, say in balance with 'blind' trading, then how come that the big mass of traders, who are supposedly 'educated' traders, who attended many seminars, webinars, who read a lot about trading, are in massive losing balance, moreover most of them are losing their assets in a couple of weeks or months.

We all know the answer; just hard to accept that, huh?

To become a *winning trader* you have to be better than the 90% on the *market*. Unfortunately, there is no 'mark' on your head which indicates that you are or have been a winner: you have to perform that again and again in every single trade, and it is hard. One or two winning trades can be pure luck; with your closed eyes you have 50% chance for that. **The problem is, if you open your eyes and you can watch the chart your thoughts are coming. Your thoughts arouse your feelings, your feelings lead to action and you are in a trade.** Based on your feelings.

It is a proven fact that, investors' mindset works totally different way than emotions. It is a human characteristic. All of us.

The first problem is in the education.

In the *profitable trading* there are no levels such as beginner level, intermediate level and advanced level. There is only a knowledge level which makes you able to lose and a knowledge level which makes you able to win. Between these two levels there is nothing but hard work, learning, practice, testing and developing.

On the *market* one needs the knowledge which makes one able to trade in a well organized and confident manner. When the knowledge of the Technical Analysis, as the ‘final product’ of a logical investor mindset, ‘overwrites’ the thoughts based on feelings and emotions, and as a result make an investor decision, which consistently meets the known, tested and proven trading rules.

It is an interesting paradox that traders lose serious thousands and millions in months because they only rely on free downloadable materials, gossips, tips and uncontrollable, copied, ‘stolen’, information from here and there. But in contrast of that huge loss they are not willing to pay for a good, proven recorded, well organized *curriculum, education, mentoring program*, etc.

The other problem is the personal *discipline* or I should say the lack of, therein. It is worthless to have proper knowledge and make *reasonable decisions* if the execution was failed. The reasons behind that can be found in *motivation, responsibility, commitment, discipline, sense of purpose, persistence*, the system of *goal settings* and many more.

Although this is my favourite topic and I developed many *methods, systems and rules* to create, apply and *monitor* this process successfully I don’t want to write about it in details here because it took another 100 pages and it is not my original topic now. Briefly: all of them, separately and one by one, as well, can be developed and applied without any limitations.

Anyway, fact is fact that more traders fail to execute their *trading plan* than develop a system. It is hard to work within certain rules and frames and it is hard to face the fact that it doesn’t matter how good you are or you will be you will certainly, and always have losing trades. Some people just can not handle that. As I mentioned above, the good news is that those skills (as well) can be developed without limitations.

Summarization

Those theses are my theses, my experiences. Based on my experience alone you can not trade successfully, you will need your own.

Do not accept them. Do not even argue with them. Just think about them.

Think them over, look for logical, rational explanations. Could you confirm them? Could you prove them?

Could you test them to confirm their existence or even the opposite?

You can only build your conviction and your confidence to trade based on your own experience. You can only trust and rely on your knowledge; all the other aspects are continuously changing on the markets.

My Links:



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Watch my Forex Trades on YouTube:

http://www.youtube.com/watch?v=YINzKjHT_wk

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