In This Issue

The Many Faces of Technical Analysis

With the holiday season finally over, it's time to focus on the year ahead. Ring in the new; ring out the old and let's move forward. Before relegating 1992 to the far recesses of our memories, let's reflect on some important topics discussed in this journal over the year. Now is the time to capture what wisdom we can from the past and carry it with us into the future. What better time to examine our goals and sharpen our technical/fundamental focus?

For nearly three years, this newsletter has introduced trading topics and ideas that have solicited heavy praise from readers. Over the same period, the length of time the average CSI customer stays with the service has increased by more than 50%. We are gratified to hear that our comments are part of the reason CSI subscribers are finding success and limiting failures in the markets. Unlike many newsletters that give specific trading recommendations, this journal attempts to educate and encourage independent thought. My focus is to help investors make their own decisions, not to make decisions for investors. This thrust keeps last year's topics timely for the future and makes them worth a second look as we begin 1993.

Technical analysis combines the three interactive, compatible elements. They are market data, mathematical manipulation, and market form or signature. Each of these three elements must be managed effectively to achieve an overall successful result.

Market Data:
Market data must exhibit stochastic stationarity to survive the rigors of mathematical manipulation. We have gone to great lengths in the past to explain how one can reduce raw market data into stable, stochastic stationary series. Data on stocks that trade with reasonable market volume are thought to possess the stationary characteristics desired. However, raw commodity data with its inherent birth-death process is not stationary. This data is therefore greatly lacking as a means of fostering reliable predictive results from any analytical viewpoint. Perhaps this is the major reason that futures market traders are thought to fare much worse than their stock market counterparts.

Many data vendors offer blended commodity files for analysis, but CSI's Perpetual Contract® data is the closest to stationary as any alternative we have seen. Perpetual Contract data exhibits a time-weighted average of prices a constant period forward. The contract birth-death process is essentially removed, producing a series that is smoothed, but representative of the active trading period for the commodity. The resulting series approaches a stationary form, which is suitable for predictive use.
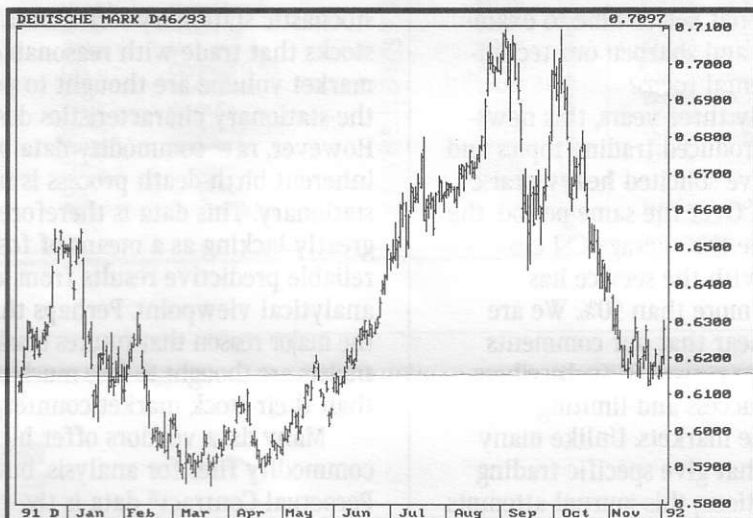
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The two charts below demonstrate the significant difference between raw data (top) and stationary Perpetual Contract data (bottom).

Mathematical Manipulation:

The mathematical analysis methodology must be statistically sound and the trading method must consume a minimum of parametric control. It is often not enough to merely capture raw market data, apply certain conventional tools and expect a lasting, profitable result. Tool kit software packages offering a variety of technical studies can be a blessing or a bane

to investors. Unfortunately, traders who are avid users of tool kits and other single-market methods are likely to be heavy losers in the long run.

Tool kits are available from many sources. CSI offers a study package with 24 technical indicators, and many others are compatible with the CSI update service. Such packages give a good feel for the potential of technical analysis, but the risk may exceed the reward. If you discover a potentially winning procedure with a tool kit, please be careful to evaluate your performance by removing inevitable hindsight bias from the results. CSI's Trader's Money Manager™ helps remove the mystery of future performance from a proposed systematic trading approach. Too many market players ignore the mandatory evaluation step before exposing themselves to uncertain market forces.

When focusing on technical considerations, the methods used will often reveal your chances of achieving longer term success. Single-market tool kit studies exist at the less capable end of the performance scale. Multi-market methods, where many related markets are used to predict a given single market, exist at the highly capable end of the scale.

Methods in the intermarket area involve multiple linear correlation, neural networks, indexing and spread trading to name a few. Differential filtering methods and differential smoothing are worthy sophisticated methods that are typically (but not necessarily) applied to single-market analysis. These are valuable aids that may be near the center of the performance scale.

In addition, portfolio selection and weighting are important technical requirements every serious trader must consider before committing market funds. The days of investing in one market or one single market group are

TMM Versus Optimal f
A study of contrasts

The money management techniques used by CSI's Traders Money Manager (TMM) program are often confused with those used in Ralph Vince's Optimal f theory. Both TMM and Mr. Vince's innovative Optimal f calculations deal with managing risk through adjusting contract exposure. To clarify the important differences in these two analytical methods, we offer the following:

1. TMM uses Monte Carlo simulation to tell you whether your trading approach is worthy of investment and, if so, how you should pace your market exposure. Simulations can offer many benefits, but they tend to increase computing time significantly. Optimal f is a deterministic calculation that deals with pacing the size of your investment.

2. TMM degrades input statistics on profit and loss by parameter count and sample size to remove hindsight bias. The input can represent either actual experience or simulated performance. Optimal f does not degrade, but assumes your actual or simulated record is representative of future performance.

3. TMM assesses the sufficiency of capital requirements to reach a given goal in advance of any further actual trading. Optimal f does not have a facility to determine the probability of remaining solvent and is not goal oriented.

4. TMM deals with the exact distributional form of degraded input and makes no assumptions about whether input is distributed in any general way when assessing market exposure. Optimal f uses a geometric average of profits and losses. It introduces a maximum overall loss as a key factor in producing an estimate of a non-integral number of contracts to trade.

5. TMM computes the number of integral contracts to hold at any given moment as a function of both the probability of remaining solvent and whether increasing market exposure will increase your worth. Optimal f computes fractional changes in market exposure which the user must interpret and convert into real life integral contracts.

6. TMM will compute your expected annualized percentage return on investment with and without money management. TMM will also compute your dollar capital requirement to reach a given dollar goal for all levels of success probability up to 99.99%. Return on investment and success probability are not factors in the Optimal f calculation.

TSPE & TMM Version 2.1 Ready For Release

Over the past several months, the CSI programming staff has been working on an upgrade of two of our most innovative products. The Trading System Performance Evaluator™ (TSPE) and Trader's Money Manager (TMM) programs have matured into formidable tools that will better certify your market timing methods and manage your capital resources. Enhancements include the introduction of improved mathematics, better computing precision and additional display facilities. The manual has been expanded to include a tutorial and a friendly overview of the product, explaining in simple, concise language how you can benefit from the program.

The enhancements of TSPE and TMM versions 2.1 make them worth considering anew. All of the above capability is available at no increase in price. TMM is priced at $499. The capital analysis functions of TSPE can be broken out separately for only $199. Upgrades for previous purchasers are available at no charge. Please use the product summary order form on page 5 or call CSI marketing if you wish to order either of these products. ✦

John Sweeney, Technical Editor of Stocks & Commodities Magazine said of TMM, "Bob Pelletier won't get rich selling this product, but he will certainly gain a great deal of respect for offering it." John was right about not getting rich, but that was not our objective. Our objective in offering TMM is to keep our customers from becoming poor by buying trading systems that don't work or taking advise that doesn't produce. The extensive time and effort spent assembling these products, in our opinion, was absolutely necessary to validate trading schemes before real money was placed on the line.

Ask Customer Service

Last month this column discussed the important year-end file maintenance required for updating continuous contracts into 1993. This topic takes on a new importance for those users who did not heed our warning before 1993 began. For the sake of those of you who somehow missed the file-extension deadline, this month's column addresses what to do if you didn't prepare continuous files for 1993.

Q. *Help! All of a sudden my Perpetual Contract and stock files are not updating when I call for data. The data listing says NOFL, which means there are no files for these contracts, but I updated them just last week.*

A. The problem is that you are trying to update files that ended December 31, 1992 with 1993 data. There is simply no more room in the files. This situation can occur when using QuickTrieve® version 4.0 or earlier, or when users of later versions say (N)o to autocreation of new files during updates.

This problem can exist for any continuous data file, including stocks, indexes, cash, nearest futures and Perpetual Contract data. QuickTrieve's Move/Split a Data File (Move a contract file on version 3.1) will help you extend your files.

The file extension process is much easier with QuickTrieve 4.01 or later than with previous versions. These later releases can autocreate all necessary files in a single run. They can also automatically create new data directories when the limit of 120 files is reached.

To begin, select <H> from the QuickManager® Menu. A list of your files will be displayed. Press the letter designator of each continuous file ending in 1992. When finished, press <F3>*.

You will be asked if you want to create files for all items or just those not existing on your target path. Say All. You will be shown each selected file and will be asked if you want to change the beginning or ending date of each. Answer Yes. Change the ending year for each item to 93. You may substitute 94 or 95 as desired to avoid doing this next year, but be aware that this practice tends to waste disk space.

When finished, check your new files to see that the data was transferred properly. If the new files are

O.K., you'll probably want to delete the original files using <B> Delete data file from disk.

You'll need to re-collect any missing days from 1993 to update your files. Your CSI bill will show an extra-access surcharge if you retrieve more than 26 days in a billing cycle.

*The <F3> feature is included in version 4 series QuickTrieve only. Users of prior releases must move each file individually as directed through screen prompts.

Q. *I collected and distributed my daily updates, and all the data went into files. When I tried to plot my updated data, some of the graphs ended with December 31. Where are my 1993 prices?*

A. If you look a little more closely, you'll probably find that the files with the missing data are continuous, ending in 1992. You'll also find a new set of files for the same series ending in 1993. You must be using Quicktrieve 4.01 or higher with file autocreation to experience this scenario.

If you try to plot your new files, you'll find that they hold only the updates you have collected since January 4th - not very useful.

We recommend combining your 1993 data with past data using the procedure described above. After transferring your 1992 data into your new, larger file, you'll need to transfer your 1993 data there as well. After checking for proper transfer, delete the short 1993 files.

Q. *I created new, longer QuickTrieve-format files to hold my stock data for another year, but I'm wondering if my CompuTrac-format files need similar attention. There doesn't seem to be a problem with them. Do CompuTrac data files require extra maintenance?*

A. No. CompuTrac-format files are self perpetuating. The annual extension process only applies to continuous QuickTrieve-format files. ✦

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gone forever. Statistical diversification, as opposed to subjective product diversification is a mandatory requirement for any trader. Trading several statistically diverse markets at one time with perhaps different analytical approaches may be the missing key to success that will make your market exposure less prone to risk.

Market Form or Signature

Each market has its own form or signature that must be understood before investing. This signature should be fully evident in the input data so that the precious and rare lessons of the past are visible to the analytical method. The signature can be found by studying vast quantities of past history. If a model offers only an abbreviated view of history, the movements of the past that triggered

jumps or drops in price may not be present. You need an extensive history of these movements to benefit from their future recurrence.

Any model that is limited to a view of six months of history when three decades are available, for example, is not doing the job for you. Anyone who ignores history's lessons is destined to repeat the failures of the past.

Market losses are considered by some to be tuition payments to opposing market players that help to teach the rules. It doesn't have to be this way, however. Learning the rules can be largely accomplished by paying attention to what is required before taking on trading risk. ✦

Bob Pelletier

> *"Anyone who ignores history's lessons is destined to repeat the failures of the past."*

CSI Software Product Summary

❏ **QuickTrieve®/QuickManager®** - To retrieve, manage & edit data; includes Alert Calendar: Unrestricted use $99, Daily data user $39 and 4.04 Upgrade $25

❏ **QuickPlot®/QuickStudy®** - Charting & analysis software (requires QT/QM) $156 Currently on sale @ $99

❏ **Trade Data Manager™** - Macintosh downloader & accounting program; includes 1st month of updates $99

❏ **Trader's Money Manager™** - Introductory price $499 (a $200 savings)

❏ **Trading System Performance Evaluator™** - Computes your system's capital requirements $199

❏ **TraDe$k™** - Traders' complete accounting system-(price varies with number of accounts) Starting @ $399/Unrestricted use $299/Daily data user or 12-month lease starting @ $22/Mo.

❏ **Seasonal Index Value Pack** - Three years of history for 33 popular commodities $444

❏ **Daily Updates** - Starting at $12 per month

❏ **CSI News Journal** - Aug. 1990 to present $35/Yr. or $5/Reprint

❏ **CSI Mailing List** - $200/1,000 names (CSI users omitted)

| ☐ CHECK | ☐ MASTERCARD | ☐ VISA |

AMOUNT ENCLOSED $ _____

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☐ 5¼" DISK   ☐ 3½" DISK   01/93

All prices subject to change without notice.