

Cash FX Traders: Learn to Use the FX Futures Markets to Give You an Edge!

At the recent Forex Trading Expo held in Las Vegas, I was one of five panelists in a two-hour session called “Meet the FX Pros.” The idea behind the session was that the five of us were all very experienced, professional FX traders with varied backgrounds, and that would allow the audience to get varied opinions about how to trade cash FX and FX futures, what tools to use, what time frames are best, and what currencies offer the “best” trading opportunities on a regular basis. In short, the people would be able to ask five different professional traders with very different backgrounds and trading styles anything they had on their mind.

About half way through the session, someone asked me what currency pairs I daytrade, and more important, what time frame do I look at when daytrading? I told them that my current favorites were the euro FX/US dollar, the Japanese yen/US dollar, the Canadian dollar/US dollar, and the Canadian dollar/Japanese yen pairs. For time frames, I told them something that really made the audience pause: I generally chart the FX futures markets using eight- or 13-tick range bars, and then I put my position on in either the cash FX or the CME futures markets, depending on net entry price (the lowest spread). When I said this, hands shot up all over the room because many people had no idea what a range bar is, and they certainly didn’t know why I would chart the FX futures and then execute my position in the cash FX market. If I was going to take a position in the cash FX market, why didn’t I simply use the cash FX market data for my intraday charting?

Before I could answer that question, one of the other professional traders to my left jumped in and pointed out that when you chart cash FX, there is no “gold standard,” meaning that there is no one consolidated feed. And worse, in many ways, cash FX is unregulated. For example, if you look at daily highs, lows, and closes from the top five cash FX brokerage shop feeds, they will generally have completely different highs and lows for the day.

On the electronically traded FX futures, the CME records and transmits *each* trade as it occurs, and along with each trade, actual trade volume is transmitted at the same time. The trades are transmitted in order, and the data feed shows the true progression of each trade as it happens—in order, with attached volume, and in real time. In comparison, there are more than fifteen different cash FX feeds that I can name, none of which transmit each trade with attached real time volume, and even if they did, none of these cash FX brokers that provide cash FX data feeds are larger than the CME, nor do they provide a feed that consolidates all of the cash FX market’s prices. That means these data feeds are “polling” the market price “X” number of times a second and sending out snapshots of price. For some charting methods, this is more than adequate, but there are some really powerful tools available for you to use that take a feed that transmits each trade as it occurs, with volume attached, in real time.

This means that cash FX traders generally overlook charting methods like range bars, volume-based bars, and any studies that are based on real-time volume. But I quickly pointed out that there was no reason to not use these very powerful charting tools. Most importantly, don’t just push the button on your charting package that says “range bars” and put up range bars on your cash FX data feed data. The data coming from the cash FX data feeds do not carry enough statistical information (because they are taking snapshots or “polling”), and they do not have statistically significant real-time volume attached to each of the prices they transmit. On the CME FX futures data feeds, your charting package gets every trade that occurs—in order—and each trade transmitted has the actual volume of that trade.

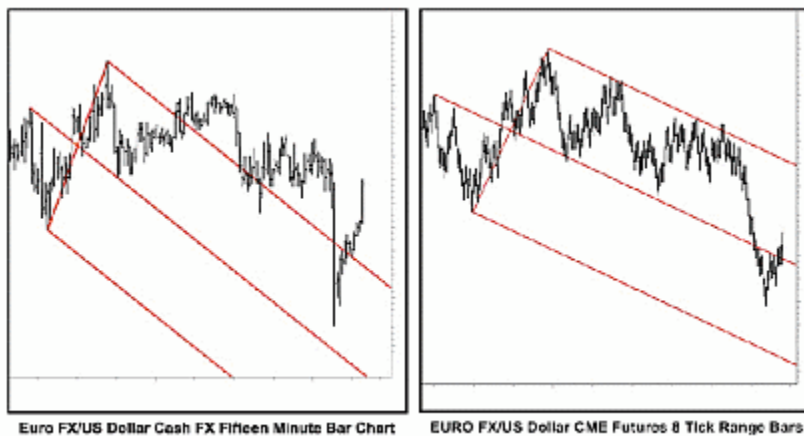
Some cash FX traders will say, “So what? My charts look just fine!” and to them, I say if what you are doing is

working, by all means, don't let my suggestions change your method. But if you want to see some powerful tools that can truly give you an edge on the rest of the market, start looking at some of these non-time-based charting methods.

For example, let's just focus on eight-tick range bars, one of my favorite charting methods when I intraday trade currencies, whether on the CME or in the cash FX market. An eight-tick range bar has a high that is eight ticks above the low of the bar. When price makes a high that is above that eight-tick range, or a low that is below that eight-tick range, a new bar is started. This method takes time out of the equation. Why is that important? Everyone that trades knows that markets get busy, then quiet; then busy again; then they get quiet again. When you use time-based bars, your charting program puts out a new bar every "X" minutes, even if nothing is happening. When you use non-time-based bars, a new bar is only started when there is a reason to start a new bar. In range-based bars, price has broken out of the bar's maximum range. In volume-based bars, price has traded "X" number of contracts, and when price hits the number of contracts you have set for the size of each bar, it then starts a new volume-based bar with the next trade.

By taking time out of the chart, you can often take the drifting or skewing that happens in sideways markets. In active markets, you'll see more bars, and each will better represent the market's activity. In quiet markets, you'll see fewer bars, and no "false signal" bars that were printed just because "X" number of minutes went by.

Still confused? Let me show you a picture of a 15-minute cash FX market chart right next to an eight-tick range bar chart of the CME futures. The same amount of time has gone by, and I used the same pivots to draw the lines on the chart, but look what taking time out of the chart does for me:



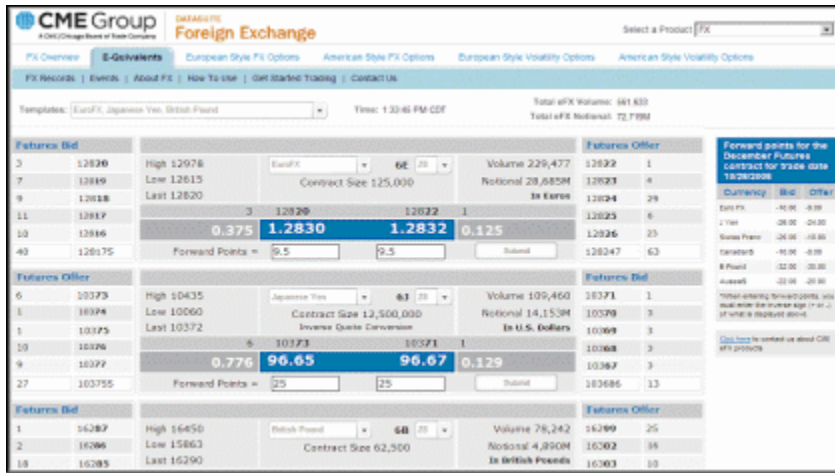
The difference between the two is striking, yet as I stated earlier, both charts start and stop at the same times, and the highs and lows for the pivots used when drawing the Median Line are exactly the same on both charts. The difference between these two charts is simple: By taking time out of the equation, price isn't skewed as it moves to the right on the chart. That means the probable path of price is much clearer, especially in intraday markets that have periods where the market speeds up and then slows down. But to use this type of bar, you need a data feed that pushes out true real-time volume and shows each trade as it occurs in real time—and at the moment, only the CME electronic data feed does that.

Does that mean cash FX traders should continue to not use these powerful charting techniques? Of course not! All we need is a little sleight of hand, and an interesting page available to all of us from the CME, and all of us who trade cash FX can quickly learn to chart using the CME FX futures and then trade in the cash FX markets (or we can choose to execute in the CME FX futures if the entry price is better).

Here's a great page that all cash FX traders should have bookmarked:

<http://equivalentswdc.cme.com:443/index.html>

And you'll know you have found the right page if it looks like this:



From this page, it's very easy to see just what cash FX price translates to in the CME FX futures. This page gives you the "Forward Points," or Swap Points, that represent the difference between trading in the cash FX market, which has a two day settlement, and the CME FX futures market, which has a fixed settlement based on the contract month you are trading.

So the plan is simple: You set up a futures chart right next to your cash chart and you are able to use non-time-based charts like range bars by charting them on the CME FX futures contracts. Then, when you see an entry set up you like, you convert the CME FX futures price back into the cash FX equivalent price. Then you can choose which market you want to take your position in!

Here's one more tool to make it easier:

	A	B	C	D	E	F	G
1							
2	Euro FX/US Dollar Cash and Futures Equivalent Prices						
3							
4		Enter the 'Center' of the Range:		1.2830			
5							
6		Enter the Forward Points:		9.5			
7							
8		Cash FX Price		CME Futures Price			
9							
10		1.2955		12965			
11		1.2950		12960			
12		1.2945		12955			
13		1.2940		12950			
14		1.2935		12945			
15		1.2930		12940			
16		1.2925		12935			
17		1.2920		12930			
18		1.2915		12925			
19		1.2910		12920			
20		1.2905		12915			
21		1.2900		12910			
22		1.2895		12905			
23		1.2890		12900			
24		1.2885		12895			
25		1.2880		12890			
26		1.2875		12885			
27		1.2870		12880			
28		1.2865		12875			
29		1.2860		12870			
30		1.2855		12865			
31		1.2850		12860			
32		1.2845		12855			
33		1.2840		12850			
34		1.2835		12845			
35		1.2830		12840			
36		1.2825		12835			

This is an image of a “cheat sheet” I keep on my computer. At the start of each morning, I go to the CME Equivalents page, get the forward points, plug them into each currency pairs’ sheet, and then I have a sheet in front of me that tells me that when the CME euro FX/US dollar futures are trading at 128.65, it’s trading at 1.2855 in the cash FX market. And this “cheat sheet” is even more important in the currency futures that are traded as inverses of the cash FX market, like the Japanese yen/US dollar FX futures. This sheet automatically adds or subtracts the forward points for you and then does the correct inverse calculation, so you’ll be able to see that 98.30 in the cash FX market equals 102.00 in the CME Japanese yen/US dollar futures.

If you trade cash FX, don’t miss out on these very powerful techniques! Get a bit creative, do a little homework, and get the edge that some of us already use to trade both the cash FX and FX futures markets.

If you’d like a copy of my Excel spreadsheet that does the simple calculations for you, drop me a line and I’ll be glad to send you a copy.

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