



CSI Technical Journal
December 2004
Volume XXII, Number 12

In This Issue

- ?? Holiday Schedule
- ?? Prediction or Coincidence?
Successful Trading Systems
Require Logical Conclusions
- ?? Tech Talk
- ?? New One-Button Update Partners
- ?? Breaking News
Additions to the Commodity Database

Holiday Schedule

CSI will be closed for voice communication on Friday, December 24 for the Christmas holiday and will close at 6 p.m. on Friday, December 31 for New Year's Eve. The CSI host computer will be accessible without interruption throughout the holidays and data will be available for the many markets that remain open on these days. All of us at CSI send our very best wishes for a joyous holiday and a prosperous new year.

###

Prediction or Coincidence? Successful Trading Systems Require Logical Conclusions

The recent U.S. national election brought up an interesting statistical coincidence that had held true for 64 years. From 1936 through 2000, the success or failure of the NFL Redskins football team on the Sunday before Tuesday's presidential election seemed to predict the next president of the United States. If the Redskins won, the incumbent's party retained the White House. If the Redskins lost, the incumbent's party

lost. Every time. Although there had been a perfect correlation for the last 17 presidential contests, the 2004 election proved this “predictor” to be flawed.

With the Redskins’ loss to the Green Bay Packers on Sunday and corroborating exit polls on Tuesday, many an American voter began to wonder if the predictor would, indeed, extend its streak to 70 years. Cut to November 3rd: President Bush was settling in for another term in Washington, not packing for Crawford, Texas. For the first time in the history of the Washington Redskins, they failed to predict the winner. Astonishing!

What happened to the predictor? The same thing that happens to trading systems that are based on coincidence, curve fitting or crystal ball gazing rather than sound scientific, mathematic or economic principles. They are *non sequiturs*, relying on the fallacy in logic where the conclusion *does not follow* the premise. There is no underlying principle to support the premise that the result of a football game will predict the result of an election. The two are totally unrelated, but still there is the fact that the predictor was right for 17 consecutive presidential elections. The inevitable failure came because it wasn’t based on science, but superstition or coincidence; it was illogical.

We bring this up to our readers because the failure of the Redskins to predict the election aptly demonstrates a seemingly flawless, but baseless indicator at work. As we can see by the victory of the incumbent despite the Redskins’ loss, what consistently worked in the past for such unrelated events should not be relied upon to predict the future. It is important for analysts to avoid making the same mistake.

Valid technical indicators must be based on sound concepts. A good place to start might be the well-understood connection between price and volume: When price moves on strong volume, more traders join in and, more likely than not, their sheer numbers will carry the momentum of the move into the following trading session. Therefore the premise that a strongly supported price trend is likely to continue is based on an observable tendency than can be explained by trading psychology. This isn’t rocket science — just a hypothesis that can be confirmed by analysis and logic, and harnessed by technical trading systems. Nevertheless, this is a single relationship and not enough substance to be the solid basis of a trading system.

A more comprehensive study might evaluate and seek to profit from substantive or causal relationships that can be explained through fundamental and econometric data. To do this, causality must be established in a statistical or econometric sense. Cutting-edge analysts apply the tenets of modern portfolio theory through the use of neural networks, statistical correlation methods and diversification through negatively correlated markets. Various third-party technical trading systems that are fueled with CSI data have been successful with this type of far-reaching technology. CSI engineers are also studying such an approach.

Our website has an invaluable mixture of studies that carefully pair off markets according to their correlation with other markets over a variable number of decades. These allow you to view the correlation coefficients of all markets with all other markets

to help you understand how they perform. These studies are available on the CSI website for everyone to try.

CSI's extensive Unfair Advantage® (UA) database of world market data and comprehensive fundamental information provides analysts with everything needed to make daily investment decisions. Traders find the UA database to be incomparable and its uses diverse. For example, CSI's Commitments of Traders data, supplied by the U.S. Department of Agriculture through Steve Briese's Bullish Review, offers fundamental data on small, large, and commercial traders' interests. These are a great source of wisdom for serious traders. They let you see what the big boys are doing; why not have a look?

For analysis from another perspective, one customer uses CSI information to forecast market behavior based on conditional leading events. He looks at prerequisite econometric events drawn from CSI data reserves such as the daily movement of interest rates, gold prices, energy product prices, unemployment trends and numerous other substantive factors that might precede a given market's movement. Observed correlations are analyzed for valid economic explanations. Validated relationships that appear to be predictive lead to buy or sell signals. Based on user feedback and the demand for esoteric series, I imagine that CSI subscribers are involved in many different types of original analysis work.

Surprisingly, there are still services around that base their entire existence on studies and systems that observe a single market wherein the only underlying tenet is that price is expected to determine price. There is often no further consideration of any other substantive independent material to back up the trading algorithm. Such systems offer a zero-sum game, made worse by the cost of commission and slippage. If this sounds familiar, reconsider your approach and favor substance over promise. Explore corroborating methods that factor in multiple independent events before you risk your capital.

Whatever trading system you might come to rely on for market prediction, please remember to test it for repeatability and reliability through Unfair Advantage's Trading System Performance Evaluator™ (TSPE). This little gem that is part of every Unfair Advantage system reviews the complete track record of your actual or proposed trading system for a particular market and calculates the probability of reaching a stated goal using that system. Key factors include the starting capital, number of parameters (too many can lead to curve fitting) and sample size, which helps TSPE correct for bias.

It is not insignificant that, if the Redskins election predictor were a trading system, TSPE would have deemed it unsuitable because of its relatively small sample size. Although the predictive indicator held for a whopping 64 years, there were only 17 samples in the form of election results. CSI recommends at least thirty events to assure statistical reliability.

Sample size notwithstanding, TSPE makes a key basic assumption that the events leading to repeatable performance are substantively related with causal effect. You must be prepared to judge the difference between causality and coincidence. If you can attest to this important requirement, you may have discovered a truly predictable winner.

Whatever your party affiliation and whether the outcome of the election brought you joy or dejection, the financial markets will continue to reward without bias those who take the time to understand the processes at work. Maybe that great equalizer will help bring Americans back together after the electoral strife. Successful traders will be the ones who apply the most appropriate risk-reward ratio, who study the markets from multiple angles and who use trading systems based on sound principles. If we learn nothing more from the election of 2004, let it be not to rely on superstition, coincidences or (most especially) not non sequiturs. Despite all the hubbub about Redskins and Packers, in the end, the former Texas Ranger won.

Unfair Advantage Features:

Costing little more than a dollar a day, the Unfair Advantage database includes world futures, futures options, derived market seasonality, world stocks and a vastly comprehensive collection of fundamental facts on employment, wages, lending rates, government archives and reports, etc... Most exchange-derived series reach back to the first day of trading.

Bullish Review:

For more information on The Bullish Review and Steve Briese's investment insights, visit www.INSIDERCapital.com.

Tech Talk

Each month in this column the CSI Technical Support Staff addresses issues of interest to many CSI subscribers. This month they discuss handling changes associated with the new Windows XP Service Pack 2, Unfair Advantage's new "Add Blank Records," "Enlarge Price Range" and "Redownload" features, and an unusual "low" price for Korean Gov't Bonds.

Q. Ever since I upgraded my computer with the new XP Service Pack 2, strange notices have been appearing on my screen. One is a "File Open Security Warning" that appears when I start Unfair Advantage and the other messages refer to popups. What should I do about these?

A. The message “The publisher could not be verified. Do you want to run this software?” comes from Microsoft and reflects our status as a non-Microsoft-affiliated software producer. Don’t worry; we’re in good company.

The Microsoft Help system advises that if you know a file doesn’t contain a virus, if you know and trust the publisher and if you know what the program will do on your computer, then you may safely run the program. Unfair Advantage passes these tests. We suggest that before clicking [Run] to launch Unfair Advantage, you uncheck the box next to “Always ask before opening this file.” This will prevent the message from displaying on future uses of the software.

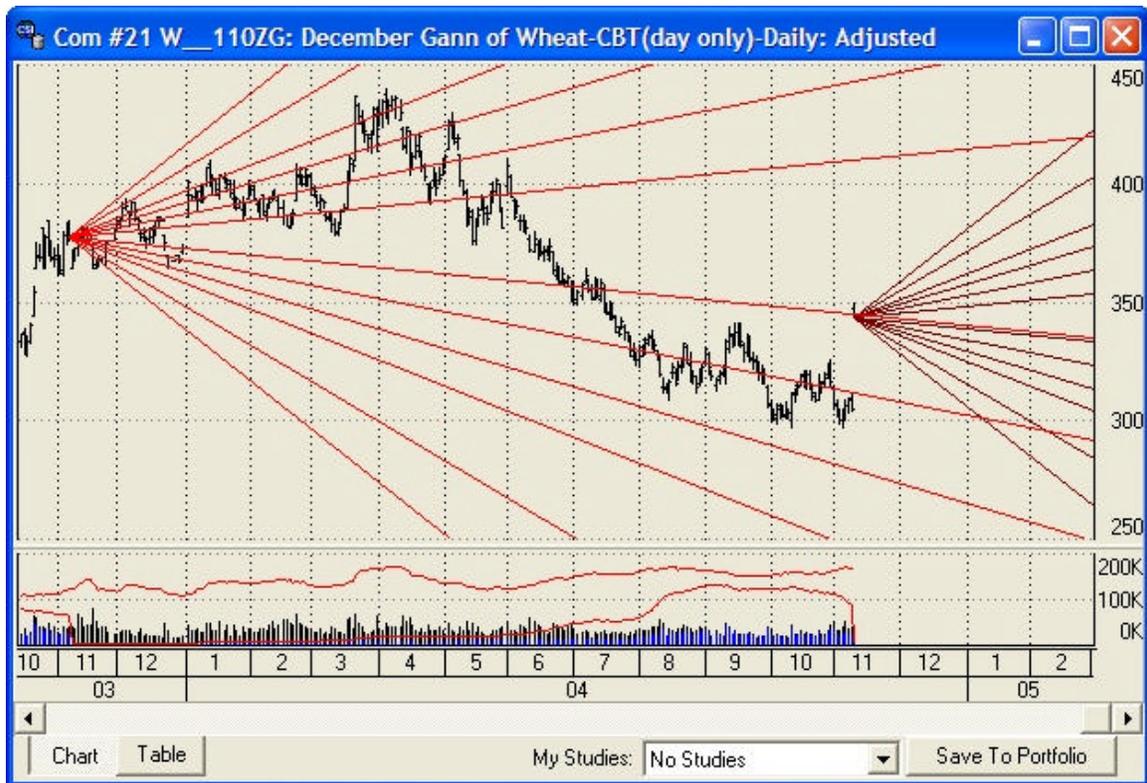
The popup blocker reflects Windows’ improved ability to protect you from unwanted advertisements. However, if you want to use any of our web-based services, you’ll need to allow some popups. This applies to the features in the online newspaper as well as to intraday quotes accessed through SnapQuote and Position Manager. You must wait until a popup is being blocked before you can allow it. When this happens, click the banner/bar at the top of your screen that says “Popup Blocked.” The resulting menu will give you the option of allowing popups from the respective site temporarily or permanently. We recommend permanently allowing them for CSI and associated websites.

Q. I would very much like to be able to add spaces to the right, above, and below my Unfair Advantage charts to provide room for my thoughts and forward-looking indicators. Will you please add this feature?

A. Good suggestion. Thank you. We have enhanced UA version 2.8.2 to accommodate your requests. To add space to the right, make a chart and then click your right mouse button. Select “Add Blank Records” from the resulting menu. UA will ask you to choose a future date to add. For example, if you want a pad of two months forward from December 6th, you would enter 20050206. UA will immediately redraw the chart with the specified buffer as “holidays.” You can remove these additions by again right-clicking your mouse and choosing “Remove Trailing Holidays.”

To add space above or below the chart, click your right mouse button and select “Enlarge Price Range” from the menu. This will bring up a dialog where you can enter a maximum and/or minimum scale value. Enter the desired upper and lower limits, and then click [OK]. UA will redraw the chart using the new, expanded charting range. To change or remove this expansion, reselect “Enlarge Price Range” and either enter new prices or delete the entries. Click [OK] to accept. Alternately, you can remove your changes by clicking your right mouse button and selecting “Clear Enlarged Price Range.”

Those who do not have version 2.8.2 can add days through the “Edit Database” mode of Unfair Advantage. This is done by creating a chart and then clicking the “Table” tab to display a table of your price series. Click any cell within the table and then right-click your mouse. From the resulting menu, select “Add a Day,” and then click “Holiday” to identify the addition as a non-trading day.



[Insert Graphic: GannFan1.jpg.

Caption: Gann Fans extend into blank areas added below and to the right of price data.]

Q. Should I click the “Redownload” checkbox on Unfair Advantage’s Download/Distribution Selection screen?

A. Unfair Advantage is designed to download and distribute a repeat of the last day that was successfully updated along with a complete set of all available current-day data. As we have said many times before, this redundancy confirms an impeccable database by assuring that any late arrivals and corrections are included. For normal daily and even intraday updates, we strongly recommend that you use the Redownload feature. (Leave the checkbox checked.) In rare instances, a CSI technical support representative may ask you to change this temporarily. Unless you have a specific reason to do otherwise, please leave the “Redownload” checkbox checked.

Q. My data for the December 2004 contract of the three-year Korean Gov’t Bond (KTB) appears to be in error. The low is way outside the normal range and another quote vendor has supplied a more reasonable price. Please correct this in the CSI database.

A. As we do whenever a data point appears questionable and whenever a customer requests verification, we contacted the exchange (KOFEX) to find out if that unusual low price was quoted in error. They confirmed that it was not. This was an actual trade. The correct data set is: Open = 112.50, High = 112.55, Low = 110.01 and Close = 112.30.

While the low price isn't an error, it is certainly an anomaly. Because of this, we added it to our list of "unreasonable" trades that are automatically overridden in charts and export files. Anyone who does NOT want their database to be affected by changes such as this should go to Unfair Advantage's Preferences screen and click "General UA Behavior 1." Check the box (click it) next to the second entry, which is "Include unreasonable, but real, trades." Please note that additions to this file are very few and far between. They usually involve overseas trades, so it is likely that subscribers to CSI's North American Futures database wouldn't notice any differences at all.

For changes that are not universally applied, you may manually edit values in Unfair Advantage's exception file. This will allow your preferred values to override any value in the official CSI database. It will also allow you to disregard your changes as desired. Here's how:

- 1) Create a UA chart of the series to be changed. Be sure you select actual contract or stock data, not an adjusted or detrended series.
- 2) Once the chart displays, click the "Table" tab at the bottom of the screen.
- 3) Scroll through the table data to find the date you want to edit.
- 4) Double-click on the desired cell. A cursor will display, allowing you to manually change the entry. Type your preferred value, keeping in mind that UA will also remember the old value.
- 5) Press [Enter] to accept your change. The entire table row for the edited day will change color to alert you that you are not viewing original prices.
- 6) To assure that this edit will show in your charts, tables and export files, go to Unfair Advantage's "Preferences" screen and click "General UA Behavior 1." If the checkbox beside "Ignore User Supplied Prices" is checked, then click it. If it is unchecked, leave it alone. This entry must be unchecked for your edits to show. Click [OK] to save your changes. You can undo your edits by either checking this box at any time or by removing the entry from the exception file through the editor.

See "Editing the Database" in the Data Resources chapter of the Unfair Advantage manual for more information on this and similar features.

New One-Button Update Partners

We promised to keep you apprised of new analysis products that support one-button updates from CSI, so here's the latest. We are pleased to announce that two additional companies have taken this important step for their customers:

- ?? MTPredictor(TM) software for Risk/Reward trading with Elliott Wave now offers one-button compatibility with Unfair Advantage for seamless data retrieval. For

information about MTPredictor and its developer Steve Griffiths, please visit the MTPredictor Ltd. website at www.mtpredictor.com.

?? Great Inspirations Software also supports one-button updates with the release of their new Stock Market Magic trading software that is based on a new artificial intelligence technology called Neuro-Genetic Time Folding. Visit www.gisor.com for more information.

Both of these analysis programs now include prompts to launch and run Unfair Advantage in the background through a single button or menu selection. Data retrieval and file maintenance are handled automatically. From there, analysis is just a few keystrokes away. This allows our mutual customers the convenience of a one-stop data retrieval/analysis service, but with the benefits of CSI's unmatched data quality and reliability.

MTPredictor and Great Inspiration Software join Vantage Point (www.traderstech.com) and Delta Society (www.deltasociety.com) in providing specialized features for enhanced compatibility with CSI.

If you would like the makers of your third-party analysis program to offer one-button CSI compatibility, please let them know. CSI will provide support for any necessary programming changes at no charge and will announce their achievement in this Journal. Thank you for your help in spreading the word.

Breaking News: New Additions to the Commodity Database

These arrived too late for inclusion in the printed version of the CSI Technical Journal, so they will be included in the January edition.

Name:	CBOE China Index		
CSI Number:	948	Symbol:	CX
Exchange:	CBOE Futures Exchange (CFE)		
Contract size:	\$100 X Index Value	Unit of Measure:	Points
Delivery months:	1-12	First date:	20041116
Conversion factor:	+2	CSI point value:	\$1
Minimum tick:	5 CSI points (\$5)	Newspaper/CSI ex.:	285.15/28515
Trading Hours:	08:30 - 15:15	Max. months forward:	12

Name:	CBOE S&P 500 3 Month Variance		
CSI Number:	949	Symbol:	VT
Exchange:	CBOE Futures Exchange (CFE)		
Contract size:	\$50 X Index Value	Unit of Measure:	Points
Delivery months:	3,6,9,12	First date:	20041116
Conversion factor:	+2	CSI point value:	\$0.5

Minimum tick:	50 CSI points (\$25)	Newspaper/CSI ex.:	159.00/15900
Trading Hours:	08:30 - 15:15	Max. months forward:	12

Name:	Polish Zloty		
CSI Number:	950	Symbol:	PLZ
Exchange:	Chicago Mercantile Exchange (CME)		
Contract size:	500,000 Zloty	Unit of Measure:	Points
Delivery months:	3,6,9,12	First date:	20041116
Conversion factor:	+5	CSI point value:	\$5
Minimum tick:	2 CSI points (\$10)	Newspaper/CSI ex.:	.30294/30294
Trading Hours:	17:00 - 16:00	Max. months forward:	18
Note: Combined Globex + RTH Session.			

Name:	Euro/Polish Zloty		
CSI Number:	951	Symbol:	EPL
Exchange:	Chicago Mercantile Exchange (CME)		
Contract size:	500,000 Zloty	Unit of Measure:	Points
Delivery months:	3,6,9,12	First date:	20041116
Conversion factor:	+5	CSI point value:	EUR 5
Minimum tick:	2 CSI points (EUR 10)	Newspaper/CSI ex.:	.23406/23406
Trading Hours:	17:00 - 16:00	Max. months forward:	18
Note: Combined Globex + RTH Session.			

Name:	Yield Rates		
CSI Number:	774	Symbol:	UYR
Exchange:	U.S. Government	Conversion factor:	+2
Contract size:	Variable	Unit of Measure:	Points
Delivery months:	N/A	First date:	20041116
Yield rates are supplied as a list of perpetual delivery months as follows:			
Treasury Yield Curve Rates:		CSI Delivery Month Code	
1 month		39	
3 months		40	
6 months		41	
1 year		42	
2 years		43	
3 years		44	
5 years		45	
7 years		46	
10 years		47	
20 years		48	
Required Net Yield Rates (90 day):			
5 year balloon		49	

7 year balloon	50
15 year	51
20 year	52
30 year	53
FMNA Posted Yields (90 day):	
10 year	55
15 year	56
20 year	57
30 year	58

###