

Kaufman Uses Multiple Trading Methods, Cites Market 'Noise'

By Jim Wyckoff

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(Note: I wrote this story a few years back, when I was a journalist with FWN.)

Many traders attempt to find the single-most "robust" trading strategy possible by looking for one set of rules which works for all markets. Such systems don't take into account the fact that markets can change quickly and dramatically due to a news event, according to Perry Kaufman.

"There are times when a market is volatile, or moves unusually, and you need to take different strategies to trading," said Kaufman, a market strategist, author and director of research for the consulting firm Kaufman, Diamond & Yeong, based in Wells River, Vt. He was speaking at the Technical Analysis Group (TAG XVIII) traders conference, held here late last week and sponsored by Dow Jones Telerate.

"Price shocks"--a government economic report or other major news event--can quickly turn a quiet, sideways market into a volatile and highly discretionary one, he said. A trading system that works in a sideways market will likely not work well in a volatile one.

Kaufman focused on what he terms "market noise," which is the unpredictable movement of a market. He said more active markets have more market noise, and are therefore harder to trade.

The formula for measuring "market noise" is as follows, according to Kaufman: Change in price divided by the sum of each price movement over a period of time.

More market noise means it takes longer for a trader to identify a trend in a market, said Kaufman. He said the S&P 500 futures are very "noisy," and therefore need a longer time for a trend to develop. Conversely, Eurodollars have less noise, so traders can jump on a price trend in a shorter period of time.

Very long timeframes make market noise less significant, said Kaufman. For short-term trading, noise is more important than the trend, he said.

"Short-term (price movement) is mostly noise and long-term is mostly trend," said Kaufman.

"If a market has high noise, you should not trade with a trend-following system," he said.

Kaufman ranked the world's markets by their "noise" factor--keeping in mind his proposition that less noisy markets are easier to trade.

Brazil has the least market noise because it's an emerging marketplace, said Kaufman. There's less participation in emerging markets. Thus, "you can trade trend-following systems and faster moving averages" in those markets, he said.

Indonesia, Turkey, Malaysia and South Africa are among the other less noisy world markets, he said.

The U.S. markets are the noisiest, most active markets, and hardest to trade, said Kaufman. France, Japan, Germany and U.K. markets are close behind.