The Out of Consensus View-Currency Outlook for 2011. First published in January 2011 edition of Forex Journal

The publisher of this illustrious tomb Mr Dickson Yap has kindly asked me to furnish a currency outlook for 2011. I relish this opportunity as I have strong views on the efficacy of long term forecasting in financial markets and indeed the whole idea of a question like "Currency Outlook for 2011". I am shortly approaching the second spoke on the Trine, or 66 years for the uninitiated. That long working life has been dedicated to the practice of the Law and a love affair with markets in roughly equal proportions. In that time I have gained some valuable insights, not only to trading but also the business of marketing markets. This out of consensus view may enlighten you to the reality versus the spin that so often conflicts you.

Qualifications

Let me buttress my views at inception by telling you something about my qualifications to write this article, and by telling you that we know more about currency markets than most. At the Danielcode we trade 16 forex pairs as well as a large number of US futures contracts with perhaps 70% or more of our trades coming from the forex complex. Since 12/01/09 we have had our trade signals monitored by an independent 3rd party and these are our results for the 12 month period under review:

> Cumulative Total: December 1, 2009 through November 30, 2010 (1 Year)
>
> Winners 857 86%
> Losers 144 14%
> Not Elected 651 39% of total signals issued
> Net S&R Winners 46 32% of losing trades

You are welcome to parse the monthly results at the Danielcode website www.thedanielcode.com .

In addition we have been running a Live Trade Room since 27 June 2010 where a significant group of our members watch our master trader Dave, place each of the trades from our proprietary T.03 PLUS signals, almost every trading day with due discussion of the appropriate stop loss, target and exit strategies. The sim account run by the Live Trade Room in real time and before a discerning audience has returned better than 40% in the 5 months to the 27th November, our last reporting date. Or 8% per month on 2% fully correlated risk per trade. This is the latest Trade Room report from Dave:

> "Time for the end-of-month results. My trading "month" ends on the 27th of each month so I am now done with the fifth month of trading in my Trade Room account. Here are the November 2010 results:
>
> Beginning Balance: $121,294.30
> Ending Balance: $141,070.17
> Net Return: 16.30%
> Sharpe Ratio: 4.06 (this is with five months of data now)
> Current Open Equity: $9,236.00
>
> The open equity is in NZD-USD (short at .7741) and DX (long at 78.68). If the Open Equity

was closed now the return for the month of December would be 6.55%. I'm hoping that we do much better than that in the next three weeks. If the Open Equity had been closed out before the end of my trading month the return would have been 23.92% for the month of November."

I caution you that a 'Sim' or simulated account is not the same thing as a live trading account, but our purpose here is to demonstrate in public and in real time the efficacy of the DC trade signals, and for this purpose alone, this methodology is adequate.

Having displayed a high level of accuracy in our trade program over the past 12 months, I trust that I have demonstrated sufficient knowledge of how markets work, that you may give due weight to my views on future market directions, and be suitably sceptical of others who seek fees in return for what is in essence an advanced form of gazing at chicken entrails or divination.

Witchdoctors

Strangely, the world is full of forecasters of financial markets. For Gnostics, those who know, long term forecasting is at best a joke and at worst a fraud. But it seems to be the raison d'être for a multiplicity of media outlets with talking heads clamouring to espouse their particular slant on future market direction. For most, these forecasts are mere puff, a little known legal term that is politely used as a euphemism for promoting the particular product that is being hawked. The success of this particular strategy runs in inverse proportion to the fear factor. Perma bulls are a dime a dozen but perma bears, particularly those threatening constant Armageddon are the ones who get the bikkies.

Worst among financial forecasters are economists, about whom, News Corp Chief, Rupert Murdoch presciently observed "Economists were invented to make Witchdoctors look good", or some such sentiment. For financial markets, economists and long term forecasters are a bane. But they, for reasons completely unfathomable to me, have become a staple on the celebrity circuit of talking heads and a must have for bankers' back room analysis. And we know how that has consistently played out. Wrong, wrong and wrong would be a mild consensus of any rational appraisal!

Unfortunately, the damage that these folks inflict is immense. Wrapped in cloaks of self importance and supported by a crowd of willing reporters, desperate to fill a daily column or report, the forecasters pronouncements, artfully handled by a PR company almost always attract prominence if not headlines. It is not deserved and any semblance of accuracy is entirely fortuitous, and today I want to open your eyes to how markets really work.

Crucial to any forward view of markets is the issue of timing. This has been a core problem for practitioners of the dismal science and witchdoctors alike. In fairness to economists, their observations on fundamentals may be quite correct but that is not of much value to traders and investors unless accompanied by a relevant time marker at which the projected condition will likely take effect. This they cannot do. Amusingly, one practitioner of the witchdoctor class of forecasting, wrote a much publicised book some years before the 2000 crash in Equity markets. The tales of doom eventually were fulfilled, but not before several major funds were savaged by attempting to short the NASDAQ as it roared into its 2000 top. The same book, presumably with some updates and amendments is still being held out as a gospel, and was resurrected with the 2008 Equities correction. Sadly, many believe this sort of aberrant fear mongering and hence missed most of the Equities rally from 03/2009. So we surmise that the old saw of even a broken clock being right twice a day is still apt.

What, you may ask is a discussion of Equity markets doing in a Forex article?

And the answer to that question is that all markets react to their time cycles in the same manner be it Forex, Equities, Grains or Gold. All are hostage to properly calculated time cycles which identify and extend each market's unique vibration.

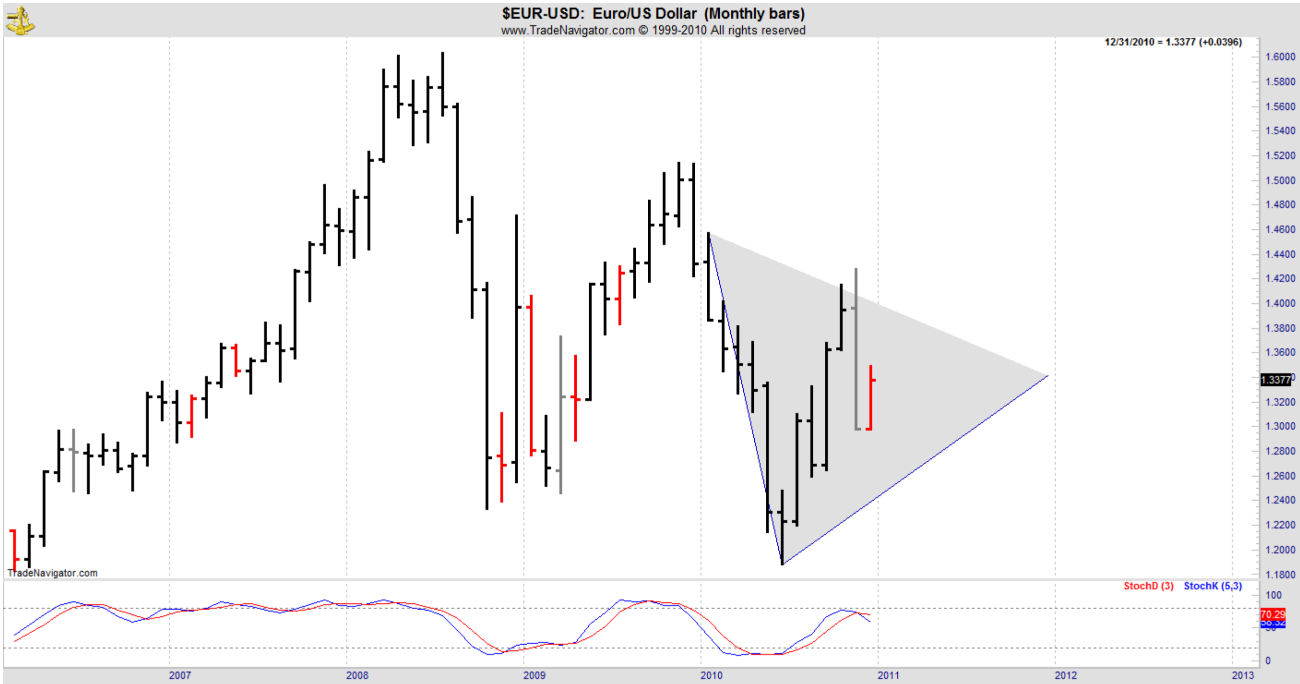
The father of the financial markets marketing cult, WD Gann, observed that all markets have their own unique time cycles or vibrations. He called this the Law of Vibrations, but sheltered further knowledge of this phenomenon with the caveat “You are not ready for this knowledge”. In fact, Gann, as an early disciple of the greatly lauded astrologer Sepharial was talking about Sepharial’s theory that market turns could be adduced from creating a birth chart or horoscope for individual markets. Interestingly, Sepharial and Gann in his quirky little book “Tunnel through the Air” had some success with this method of forecasting, particularly in the Cotton market, but that is not how market timing works.

If you are interested in the correct calculation of market time, you can read about it in my two ‘Master Class’ articles, available under the Articles tab at the Danielcode website, and I will show you how I used that methodology to correctly call major turns in significant markets in 2010.

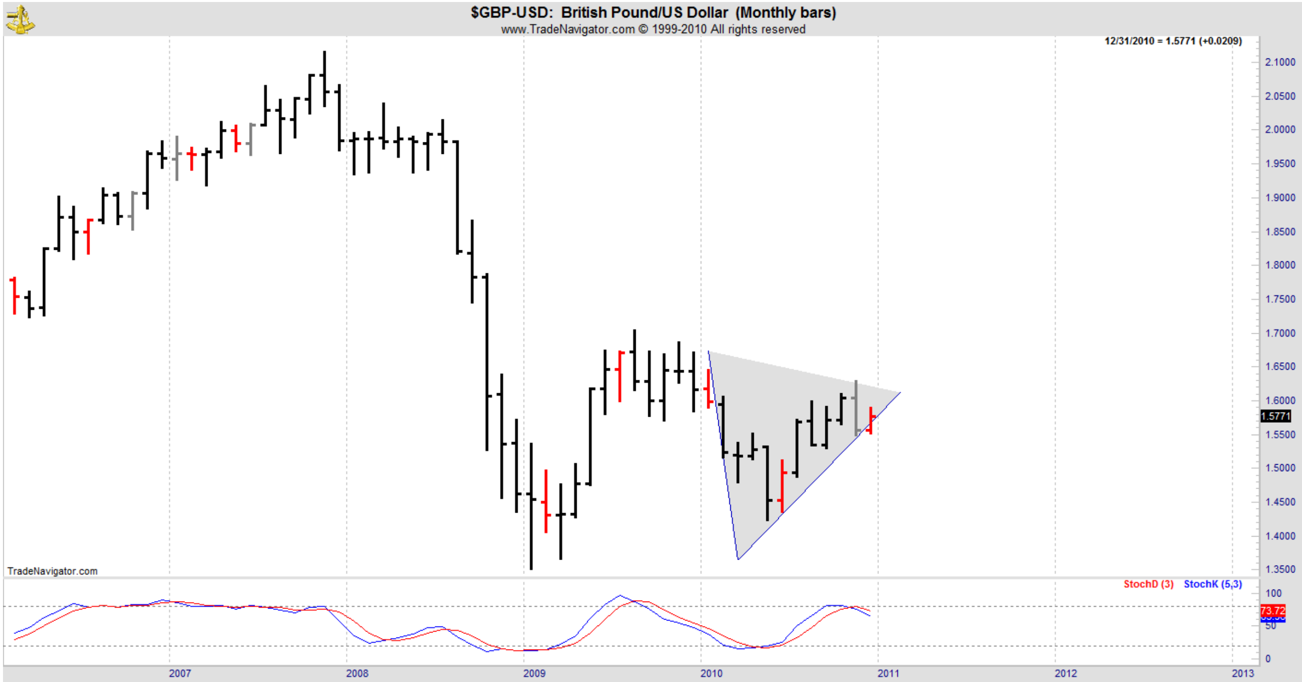
2010 Summary

To start with our prognostication of the future, we needs look at the past. In this case the immediate past in accordance with the law “Ecc 1:9 The thing that hath been, it *is that* which shall be; and that which is done *is* that which shall be done: and *there is* no new *thing* under the sun.”

This is the Euro-USD Forex pair with 2010 price action shaded:



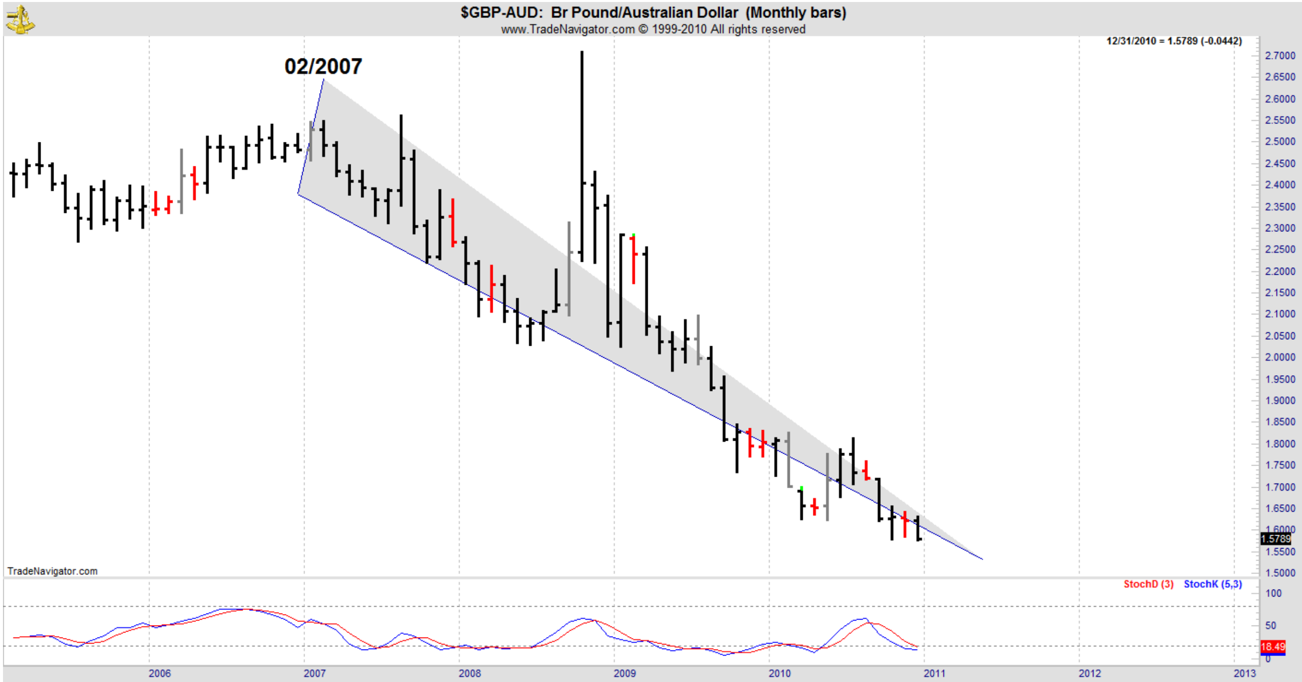
And the British Pound against USD:



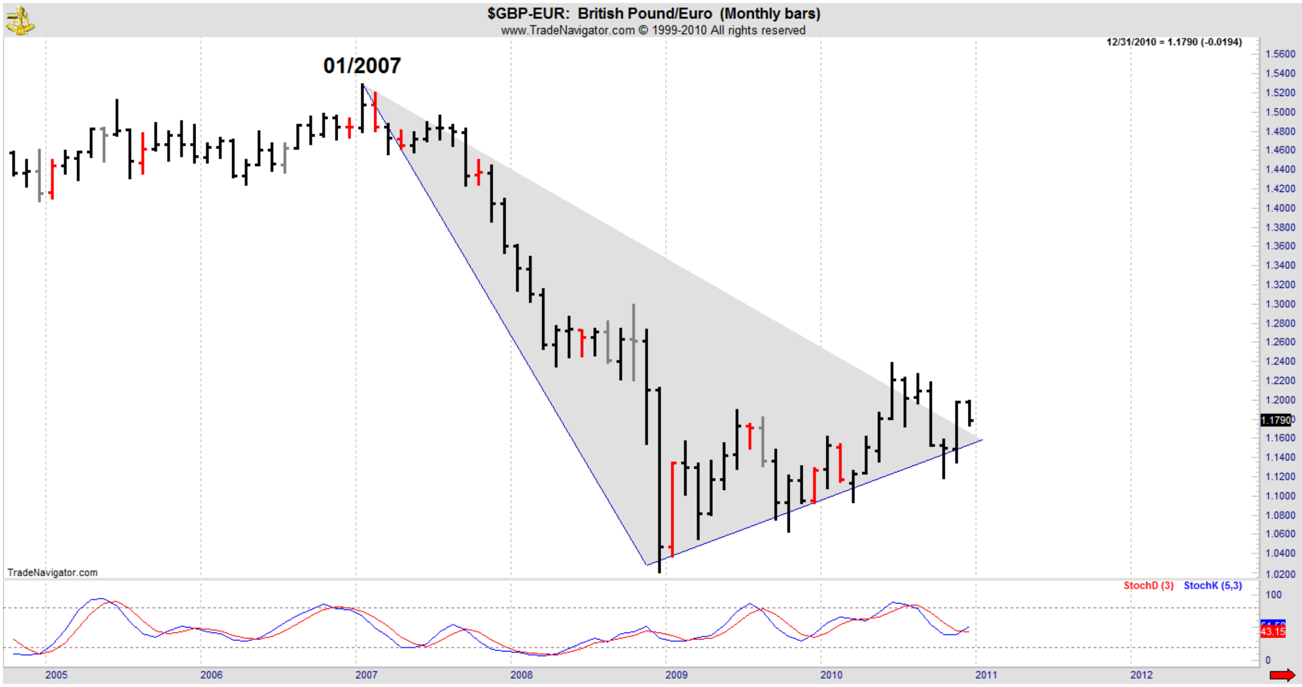
We can see from these charts that direction during 2010 was not linear. Indeed these pairs fulfilled my constant mantra "Markets fluctuate; sometimes violently". In contrast as the following chart shows, the major mercantile pair of EUR-USD enjoyed a 3 year period of great stability, optimism and linear price action from 2005 to 2008. So what changed and what is the likely outlook for the new year?

To some extent, free floating currencies act as the shock absorbers of modern economies. When economic and trade conditions change and those changes are not compensated for internally, currencies will demonstrate what politicians and the great unwashed public will not see, either through fear or apathy.

Our next chart demonstrates graphically what happens when a once great mercantile nation falls into the clutches of a History graduate from a minor Scottish University, masquerading as a knowledgeable financial engineer. This is the hapless Gordon Brown's legacy to UK Inc, which despite a new broom, in the form of the youthful and utterly inadequate incoming coalition partners, continues to see its currency debased against its significant trading partners, in this case Australia.



And much more importantly, although slightly less graphically, the similar fall from grace against its major trading partner, Europe.



Those of the witchdoctor class will point to this mechanism as an economic virtue. Currency devaluation by stealth or direct government policy, is supposed to benefit exports and make imports more expensive, thus enhancing the balance of trade. With a global supply chain, such is now only part of the story as input costs increase with devaluation to deny much of the supposed benefits. And why should this limited focus on exporters continue to be the linchpin of virtue. Savers and local investors are robbed by this process as their holdings too are devalued to create yet another underclass of serfs away from their home currency. It has been too soon forgotten that savings are the bedrock of capitalism. Savings, harnessed and judiciously employed en masse are the life blood of industry. Today's meagre minds suppose that all funding is debt. Indeed that is the dominant mode for our recent times. But Capitalism requires capital as its foundation stone and savings are the ultimate capital.

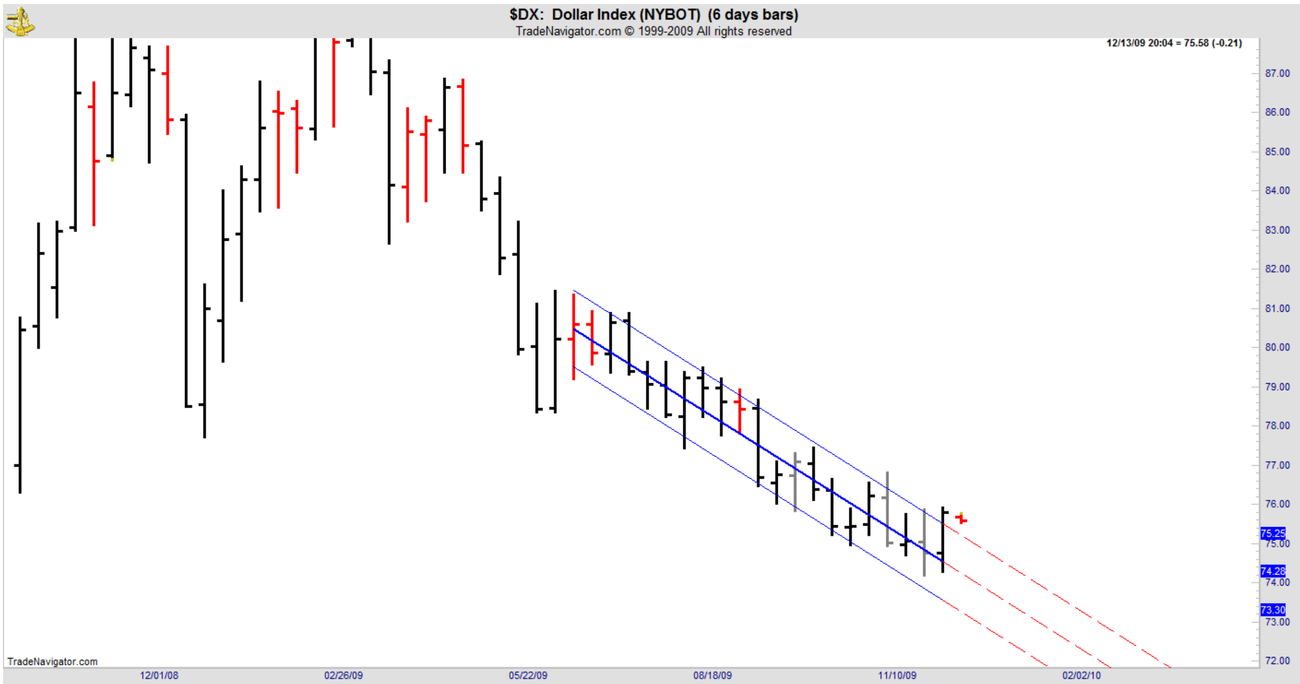
Consider therefore why manufacturers, service providers and their ilk are favoured by the economists appreciation of the virtue of devaluation. The answer for those of the myopic class is that the most obvious employers are always favoured by politicians, as the near term threat of the next election is always paramount. To clarify this important understanding, a quick scan of your favoured financial media will yield daily litanies; a chorus of cries from business that “Banks won’t lend”. Largely this is because the borrowers don’t have adequate collateral. Lending requires collateral. Capital requires hope!

And that dear readers is the crucial distinction underlying most of the Western world’s problem. Too much debt and too little capital is the very definition of insolvency. It is the creators of capital, the savers, who should be favoured, cosseted and treasured. Not the banks, the creators of debt. Witchdoctors indeed!

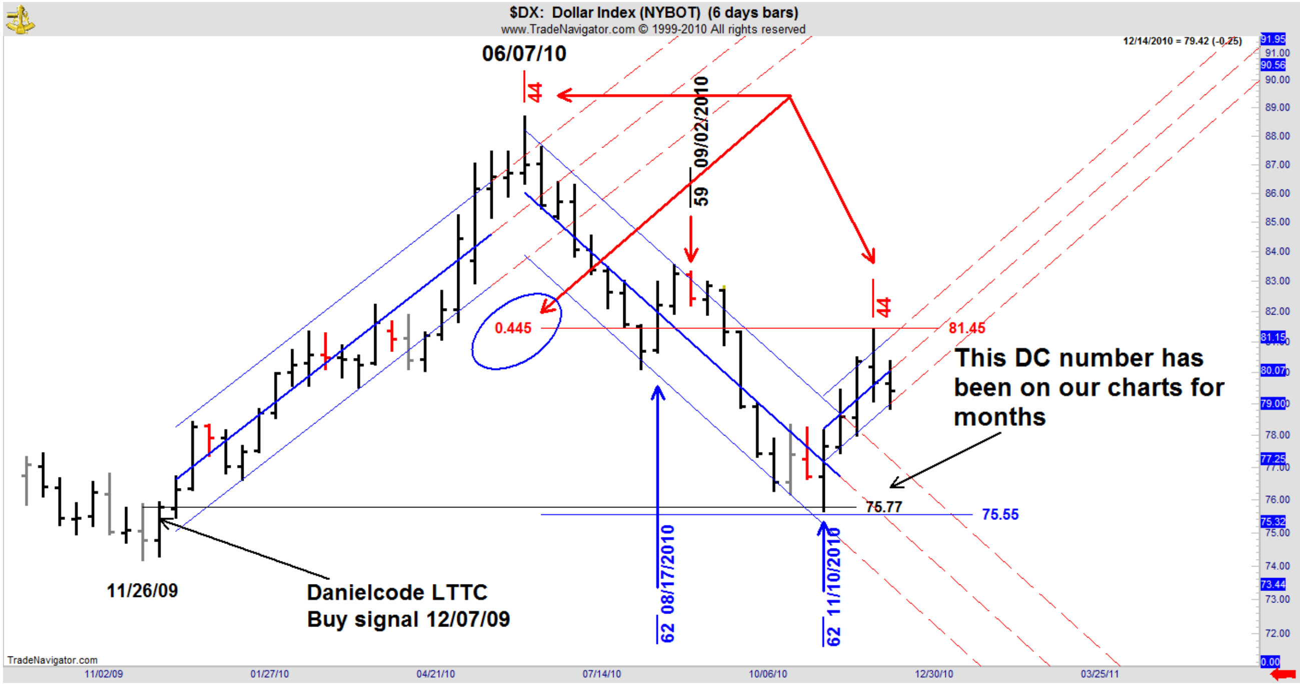
Parsing the Danielcode Time Cycles

If this article is to be of any real value to you, other than simply a quick read for the sake of entertainment, we must enter the realm of high probability events rather than the voodoo economics that I despise. This is the part where cautious and precise traders and investors can make some real money and profit from their patronage of Mr Yap’s august publication. Below is an extract and US Dollar Index chart from our 12/07/09 Long Term Trend Charts analysis:

“The bar ending 12/04 closed outside the regression channel. This is a buy setup signal on the 6 day time frame. A close on 12/14 above 75.94 will turn the trend up on this timeframe”

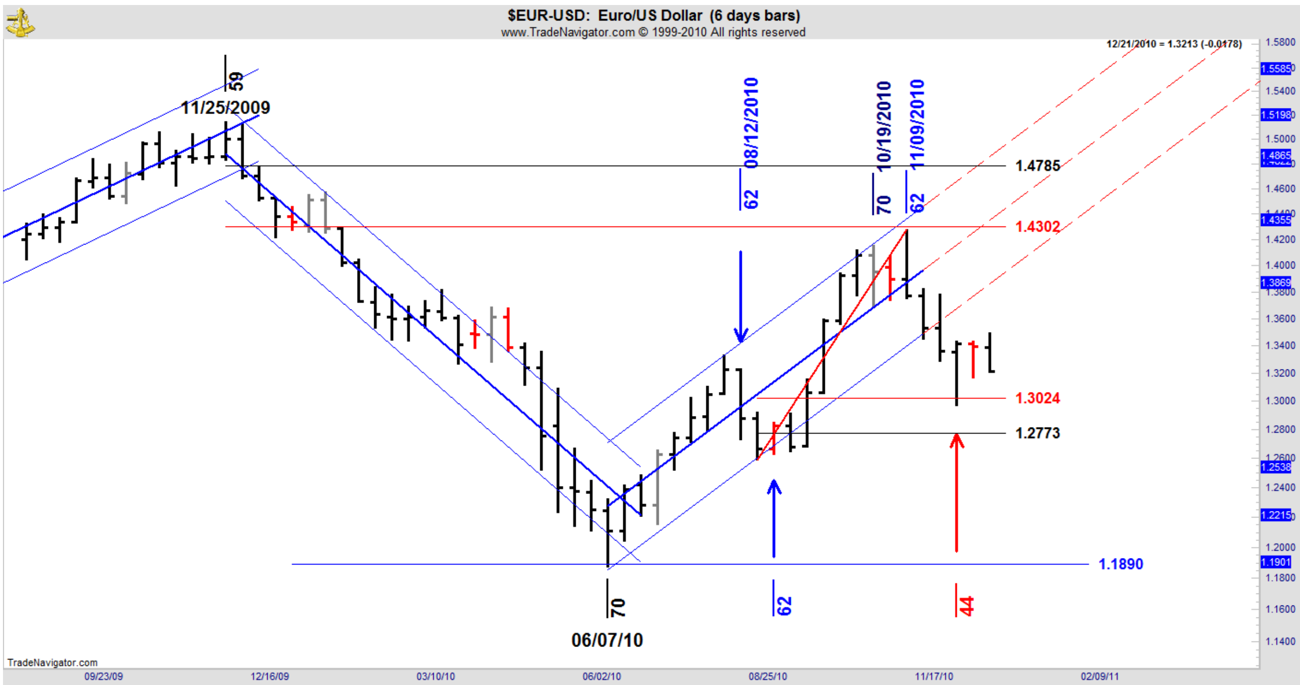


This is what happened: DX ran up from 75.79 to its closing high of 87.00, just as these Long Term Trend Charts forecast. That trade for swing traders was worth some part of $11,000 per one contract. From this fearsome looking chart you can see that DX made its top at the DC 44 week cycle before plunging to its final dénouement at the fateful DC Black line which as the chart says, was apparent to DC members as a high probability turning point, many months in advance!



A closer examination will reveal that all of the twists and turns in the DX adventures of 2010 were made at the DC time cycles. And these charts are free to all. You can see every week's chart archived under the "Trading Reports" tab at the Danielcode website.

Here is the DC timing chart for the important EUR-USD pair. Again, this chart is updated and published free to all on an (almost) weekly basis. The DC timing cycles and price targets that you see on these charts were known, weeks and sometimes months before the turns occurred. This is the immediacy and tyranny of time. Absent this vital feature, forecasts per se are useless. Just another opinion to be trumpeted if correct and quietly forgotten if wrong. And that's not forecasting. It is mere divination. And false divination at that!



Cast your minds back to midyear. Commentators and media were busy writing obituaries for the Euro in the confident expectation that its doom was nigh. And that's the danger of faux credibility mixed with sensationalism. DC time cycles identified the high probability turning points on both axis, time and price, well in advance, and you can too by learning this wholly unique and rational skill. .

If you have noticed that markets conform quite strictly to our proprietary regression channels, then you are already aware of what major currency markets will do in 2011, and we can sum that up succinctly:

1. Markets fluctuate; sometimes violently.

2. Once we have identified each market's unique vibration, we can create a true regression channel. Markets will observe that regression channel very precisely until there is a trend change.

3. All trend changes come at Danielcode time and price cycles. That is Daniel's Law of Markets. And it has ever been so. The corollary to Daniel's Law is that markets are sometimes predictable. That is why Danielcode traders enjoy an 86% strike rate.

Given the linearity of volatility, we can expect more frequent trend changes of major markets in 2011. On these time frames, volatility begets volatility. There will be trading opportunities aplenty in the coming year.

I invite you to visit us at www.thedanielcode.com . You will find a plethora of trading and market articles, PowerPoints and recorded webinars, the Long Term Trend and Timing Charts and much more. All of the above is free for your edification, and you will be most welcome.

Ecc 3:1 To every *thing there is* a season, and a time to every purpose under the heaven:

John Needham
www.thedanielcode.com
Sydney, Australia

16 December 2010