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There is a substantial risk of loss associated with trading Derivatives . Losses can and will occur. My methods will not ensure profits

Sunday, March 10, 2013

Inefficient Indicators

Do Technical Indicators Work?

When I started trading, like any other beginner, I thought the indicators are the holy grail of trading. I was using a bunch of them in my charts and was paying more attention to these rather than on price and volume. Later, I learned that these indicators are doing more harm than good in my trading, and started paying more attention to price action

All the indicators are derivatives of price and volume data and these derivatives could be effective comparison tools. Where we need to select a trading vehicle from a probable list, some of these tools could be useful. If we are focusing on a single instrument like Nifty Futures these are worthless.

Many Indicators are lagging in nature. There are countless moving averages and these are all arrived at averaging the past values. I don't find any reason to believe these levels to work. Of course some widely followed averages like 50SMA and 200SMA may attract some order flow not because of the magical nature but as a self fulfilling prophecy

Another set of indicators measure the rate of change or acceleration. These are called leading indicators. Traders look for the divergence of such indicators. The basic assumption is trend decelerate before reversal. This assumption is faulty and price move can accelerate further without market reversing. You will be told to get price action confirmation before trading such divergences. Why price action alone is not sufficient?

Some indicators like MACD combines both lagging and leading indicators. These are all secondary derivatives and fail to avoid the basic shortcomings of primary derivatives.

There are another set of indicators which are belief based. This includes Fibs, Gann, floor pivots and many other mystical variations. If you are using them, "Let your Beliefs Save You!"

Now a days Indicator Bashing has become very fashionable. These people claim they are trading pure price action. If you look closely you can see they are trying to trade some candle patterns without any respect for the location.

There are countless methods to trade the Markets profitably. You can save a lot of time and effort by applying a simple test. Look at the defined Market Structure, the framework within which price is supposed to move. Find out whether the Market is respecting these levels repeatedly and these levels are actionable. Throw it out, if it is not.

Posted by [SMART Trader](#) at 3:24 PM



5 comments:

[Vishal](#) [March 10, 2013 at 4:53 PM](#)

Hi ST sir,
Happy shivraathri to you and your family., :)
Nice article as always.,

[Reply](#)



[SMART Trader](#) [March 10, 2013 at 9:51 PM](#)

Vishal

Thank you and same to you

ST

[Reply](#)

[Anurag](#) [March 11, 2013 at 9:20 PM](#)

Do Technical Indicators Work?

Had this question been asked 8-10 months back, i would have said 'YES' they do. Look at this example, look at that example...look here the indicator clearly says buy/sell and see how much profit I would have made.

Indicators are nothing without the location. Market structure has to be defined/followed. But, almost all the available information promotes these indicators like holy grail and everyone falls for them (except few books) And the experience that follows, damages trading psychology so badly that in most cases it becomes almost impossible to be undone.

Unlearning is very difficult.
Structured learning is as important as market structure.

As always, super article ST sir, spot on.

Reply

Anonymous March 16, 2013 at 6:59 PM

While downplaying indicator bashing you have indulged in it yourself to some extent.
You ask why price action by itself is not sufficient? Well, there are so many types of price actions (you are only using ten diff names) . Combining a divergence signal will point us towards which of the price actions are the significant ones. That is the value being conveyed. I don't see why you felt the need to denigrate it?
Subtler nuances of indicator readings can be helpful to spot shifts in price action. After all the alphabet soup that you have is also doing something similar?

I found your sincerely of purpose in price analysis refreshing so was wondering why you needed to bash anything else. Gann, fibi, Elliot etc are all forms price action trading, at the end of it.

A broader mindset in markets is always an advantage.

NC

Reply



SMART Trader March 16, 2013 at 9:56 PM

NC

There are million ways to trade the Markets. This blog is about the way I trade. Naturally I have to write about what I find useful and what I think useless in my trading journey. My trading is evolving and I may use some indicators in future, if I find them useful.

The subject had been discussed to death in many forums. There is no point indulging in intellectual masturbation any more.

ST

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