CQG'S TRADEFLOW™ CHARTS:

A REVOLUTIONARY WAY TO SEE & TRADE THE MARKET

by Thom Hartle

CQG's new charting service, TradeFlow™, tracks the inside market of electronically traded futures contracts, gauges the level of volume of executed trades and displays the aggressor's - the buyers or the sellers by colour coding the bars. TradeFlow charts place floor-trading visibility on the desktop.

To see the value of this innovative tool, recall that today's popular charting styles, such as the classic bar chart, candlestick chart, point & figure and the simple tick chart, all have one element in common: they use just the last price for plotting. The fact is, just observing the last price for a trade is, without question, a limitation. Why? Consider this: does the last price reveal what traders are actually doing? For example, if the inside market is rising, are traders continuing to be aggressive and paying the ask price, which should cause higher prices, or are they starting to back away at higher levels, which will lead to a retracement. Can you see whether traders are hitting bids or lifting offers on any of the above listed charts? No, but traders using CQG's innovative TradeFlow charts can, and that may give them an edge.

First, TradeFlow charts display the movement of the inside market. TradeFlow charts use the best bid and ask for the low and the high. Second, the TradeFlow bar is colour coded to show the percentage of volume executed at the ask price (green) versus at the bid price (red). If 500 contracts traded during one TradeFlow bar and 400 were up at the ask price (buying) and 100 at the bid price (selling), the bar would be 80 percent green and 20 percent red. You instantly know that traders were aggressively buying relative to the sellers. Finally, the width and brightness of the colour is based on the total volume of executed trades during the formation of the bar. Wide and brightly coloured TradeFlow bars indicate heavy activity. Narrow bars indicate low activity. Therefore, TradeFlow bars give floor trading visibility because you see whether other traders are buying or selling and by how much.

Figure 1. TradeFlow Bars and TradeFlow Volume. TradeFlow bars are colour coded on a split basis. The green portion is the percentage of volume of trades at the ask price (buying). The red portion indicates the percentage of volume of trades into the bid price (selling). TradeFlow Volume separates the actual number of contracts traded at the ask (green histogram bars) versus the bid (red histogram bars).

TRADEFLOW CHART AND THE TRADEFLOW VOLUME STUDY

Figure 1 shows the TradeFlow chart along with the TradeFlow Volume study for the June DAX Index futures contract. The TradeFlow Volume study displays the actual number of contracts traded at the ask price as a green histogram bar and at the bid as a red histogram bar for each TradeFlow bar. We'll walk through both in Figure 1 and show the unique information available to traders using TradeFlow.

In Figure 1, bar A to bar B is a rally accompanied with steady buying as indicated by the TradeFlow Volume histogram bars being approximately the same height until the completion of TradeFlow bar B. Notice the histogram bar directly below bar B is slightly lower than its predecessor. At that point in the rally, fewer traders were willing to pay up at the ask price then the previous bar. Also, the red histogram bars, which represent trades into the bid or selling, were beginning to edge lower at bar B, also indicating that there was some light selling beginning to appear.

Following bar B, the inside market traced out a trading range with narrow TradeFlow bars indicating low activity. Buyers bid the market up to resistance at 6073.50 and then traders hit bids causing the entire TradeFlow bar to turn red (bar C). This led to a retest of support at 6072.00 bid and traders again stepped up as indicated by the nearly all green TradeFlow bar, bar D. The next three TradeFlow bars are narrow, but entirely green, indicating that despite the low volume, traders were lifting offers. This is quiet accumulation going on. Then, buyers jumped in during bar E, the volume expanded, traders only lifted offers and the market broke through the resistance. We know this because the entire bar is green and wide.

The inside market climbs to 6075.00 bid and offered at 6075.50 (bar F). Bar F is entirely red, indicating traders only hit bids at this price level. We were warned that the market was running out of buyers by the declining green TradeFlow Volume histogram bars just before bar F. But, TradeFlow bar F is narrow, which means the volume is light, and therefore indicates that despite being all red and a sign of selling, the low volume did not necessarily imply a top. The inside market trades sideways for two more bars and on the second TradeFlow bar the buyers again appear as indicated by the high percentage of green colouring in the TradeFlow bar.

"THE TRADEFLOW VOLUME STUDY DISPLAYS THE ACTUAL NUMBER OF CONTRACTS TRADED AT THE ASK PRICE AS A GREEN HISTOGRAM BAR AND AT THE BID AS A RED HISTOGRAM BAR FOR EACH TRADEFLOW BAR."

The market advances up to an asking price of 6076.50 (bar G). But, this level brings in some selling and the TradeFlow bar is almost entirely all red. Also, the red TradeFlow Volume histogram bar directly below it extends more below the zero line then the previous red histogram bars, indicating a pick up in selling pressure. Following bar G the inside market is hit by bids. Traders aggressively hit bids leading to wide TradeFlow bars, with deeper red TradeFlow Volume histogram bars. Any buying (traders lifting offers) was weaker than during the previous rally as indicated by the low green TradeFlow Volume histogram bars. Finally at bar H, the inside market was neutral as the TradeFlow bar is nearly 50 percent green and red.

TRADEFLOW ON BALANCE VOLUME STUDY

CQG's TradeFlow method includes a version of the 'on balance volume' (OBV) study. The classic OBV study is a running sum of final bar volume where if the close of one bar is higher than the previous bar's close the entire bar's volume is added to the OBV line. If the bar closes down from the previous close then the volume is subtracted. This version fails to differentiate between true buying and selling. The CQG TradeFlow On Balance Volume study uses the net difference between buying and selling for the running sum. In other words, if traders bought 500 contracts and sold 100 contracts, the TradeFlow On Balance Volume line would climb by 400 contracts no matter what the last price was. This is an accurate indication of what traders are actually doing.

Figures 2 and 3 show how the TradeFlow On Balance Volume study can aid the trader reading the price action.

In Figure 2, the inside market first dropped to 6074.50 bid and then moved into a trading range tracing as high as 6076.50 offered and retesting the 6074.50 bid three times. During this trading range the TradeFlow On Balance Volume line was showing a slight upward bias or that, on balance, there was slightly more buying than selling. At point C, as the market was testing resistance, the TradeFlow On Balance Volume line started to move just above the previous peak readings, signaling buyers were beginning to come into the market.

Figure 3 takes up the action following the rally after point C.

In Figure 3, as the inside market climbed to TradeFlow bar A, the TradeFlow Volume study was warning of an end of the advance by the green histogram bars flashing lower readings indicating buyers were being less aggressive. At this point the TradeFlow On Balance Volume line traced out a peak at point A in the study. Next, the inside market made a new high, point B

Figure 2. TradeFlow Charts and TradeFlow On Balance Volume Study. As the inside market was moving back and forth between 6074.50 and 6076.50 the TradeFlow On Balance Volume line was slowly edging up (point A to B).

Figure 3. TradeFlow Charts and TradeFlow On Balance Volume Study. Watching for divergence between the TradeFlow bars and TradeFlow On Balance Volume study can give a good reading on whether buyers or sellers are dominating the trading action.

and the associated TradeFlow On Balance Volume reading was at a lower value than the previous reading. In other words, buyers were less aggressive on this drive to make a new high than on the previous drive. In addition, at point B when the inside market was 6079.00 bid and offered at 6079.50, traders only hit bids as indicated by the all red TradeFlow bar. Sellers were even more aggressive in the second red TradeFlow bar at point B, as the bar was all red and wider than the previous bar.

The inside market then dropped down and support was established at 6077.50 bid (point C), the inside market traded sideways and then made a new low down to 6076.50 bid (point D). There are two things to notice: when the market traded to 6076.50 bid (TradeFlow bar D) the volume of trading was very light and nearly 100 percent buying. The lower bid ask pair did not draw out sellers and the TradeFlow On Balance Volume reading was at a higher reading at point D than the reading at point C. This indicated that sellers were not the aggressors, that there was buying going on, and a rally followed.

SUMMARY

Other charting styles fail to give you the information provided by the TradeFlow chart and two studies, TradeFlow Volume and TradeFlow On Balance Volume. This innovative charting style gives back to traders in the electronically traded futures markets the same edge pit-traders had when the world had to enter into their domain to trade.

For more information about TradeFlow charts and other features about CQG as a solution for traders, please visit www.cqg.com.