The winner takes it all

Looking for a straightforward way to make money, even when the markets are quiet? Binary betting could be the answer, and the key to success is discipline, as Larry Levy explains

Binary betting is a simple and alluring way of betting on markets. Meet the criteria of the bet and you can almost double your money. Fail to do so and you lose your stake. It offers clear opportunities where conventional spread betting fails. For example, since markets often spend their time moving sideways, the Range Bet or No Touch Bet offers a way to make money from lack of movement or volatility in a market. All you have to do to win is to find a market with a high statistical probability of going nowhere and you could double your stake by placing a binary bet.

With Double Up or Double Down bets, you can bet that a share, index or currency is likely to go up or down, and if it does so by more than just one tick then again you can double your stake.

The downside, however, is that many people have an inconsistent strategy (or none at all) when it comes to trading. Often trading is impulsive in nature. Although binary betting companies usually skew a 'double or quits' bet slightly in their favour (for example risk £50 to make £45), they also profit because of the statistical fact that traders on average lose more than 50% of the time. Most people lose in the end because a consistent winning strategy is not pursued.

If an account begins to show consistent winnings, the spread or binary betting company can always start to hedge the bets in the underlying market, perhaps even betting on trades being a winner by over-hedging. But for the 70%-plus of trades that lose money, they are simply turning the cash in those client accounts into profits through the clients' inability to understand the instrument on offer. Brokers call it 'turning capital into commission'.

Trading statistical probability

Statistical probability is one way to win using binary bets, more so than in normal trading. Success is dependent on smart money management, finding a set of good probabilities and consistent and thorough execution.

They say that if you want to tame a wild animal you must first understand the nature of the beast. The first step to winning is to find a set of circumstances in which there is a high statistical chance of winning. In one sense this task is simpler than with conventional back-testing, as there is no requirement to measure point gains and losses, as is the case with normal trading and spread betting. All you have to register for the strategy is a simple 'win' or 'lose'.

Let's say that, ideally, you find a system or set of circumstances that wins 80%-plus of the time. The challenge then turns to effective and rigorous application of that system.

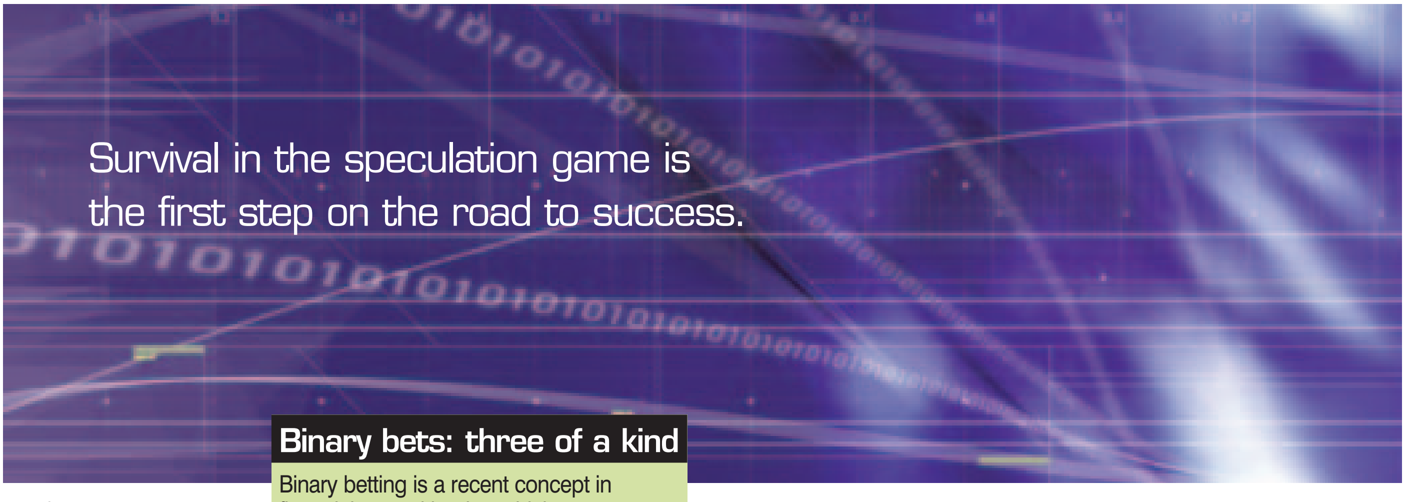
This can be more difficult than it appears, as many people are betting as a punt or a fancy, treating the trade as a one-off win or lose rather than implementing a well thought out strategy statistically designed to win by taking every trade.

Even a system that wins 80 times out of 100 can have six or seven losers (or more) in succession. And remember, just because a system wins 80% of the time based on back-testing does not necessarily mean that it will do so in the future.

Say for example an account starts with a balance of £250. Greed means that many traders, being human, will risk say £50 to win £45 (a typical house skew). Doing this increases your chances of total failure dramatically, even given a system that wins 80% of the time.

You should plan on the possibility of an opening string of losers – say 20 in a row – and *still* have the chance of account recovery. So, if the opening balance is £250, the maximum bet should be 1/20th of this amount and the risk should be no more than £10 per bet.

After five net wins the account stake should have gone up to £300, and you can afford to increase your bet to say £15. Another seven net wins and your account stands at just over £400 and you can increase your bet size to £20. Another 11 net wins and you are at £600 and the stake goes to £30. ➤



Binary bets: three of a kind

Binary betting is a recent concept in financial spread betting which operates across hundreds of financial markets. A binary bet always scores either 100 or 0 and you can 'buy' or 'sell' at any time. While the different markets can differ from broker to broker, there are three different types:

Standard: betting on the FTSE closing up for the day.

One Touch: if a market touches or goes through a certain level, then the bet is automatically settled at 100.

Range bets: a price is quoted on whether a market will close higher or lower than a certain level.

If at any stage you enter a sustained losing streak, break points must be designed to reduce the stake until the account is again large enough to increase it. Survival in the speculation game is the ➤ first step on the road to success. Taking care of the risk of ruin first is crucial.

Pyramiding – the compounding principle of increasing your bets with increased balances and trading the system consistently – is crucial to turning a small account balance into a large one.

It is best not to try and turn a large fortune into a small one by rushing in enthusiastically only to limp away with huge losses. It is, however, very important to establish discipline and consistency in your trading with real money, then scale up.

It's just as easy to place a binary bet for £5,000 as it is for £5 but it's the perfection of the method and the discipline that is important. By starting small, you are not subjecting your base capital to the high risk of failure from an early lack of discipline.

Designing a winning system

There are two main factors to consider when designing a system for financial binary bets: direction (or lack of it) and time. Time, an often-overlooked factor, is crucial because a market has to be in a defined range at a defined future point.

Most technical analysis techniques revolve around attempting to predict direction, so there is plenty of material to work with in directional analysis.

The difference between using these tools to maximize points gain (normal trading) and what directional binary betting is all about is simply looking at the probability over time that the market moves even a point in the direction that wins the bet. The extent of the move is largely irrelevant, except in a target bet.

Moving averages, cycles, oscillators and many other indicators can be used to statistically test direction over different set time periods resulting from the signals generated.

A simple example could be a moving average crossover system where the market was still lower or higher a set period of time later. If this system is found to work in a high percentage of tests, especially on multiple markets, it could be applied for profitable binary betting using the money management techniques outlined above.

Non-directional

A Range or No Touch Bet relies on the market either staying within a set range or not reaching a particular price between two set time points. A number of market situations could lead a market to move within a narrow range. Here are some circumstances in which this often happens:

❶ A very large move in an equity market will often then lead to anything from a few hours to a few days of sideways movement. A recent dramatic example was the victory rally in the Dow. The market was rapidly marked up in an historical buying panic, reaching a new and higher valuation very quickly, often in the space of one or two days. The market then moved sideways for several days in a consolidation phase. Often an index will have a sideways day after a dramatic move the previous day.

❷ Equity and currency markets will frequently stagnate in front of or around holidays in other markets or even at certain times of day. For example, US markets frequently have a Monday holiday on days when European equity markets are still open, and often traders will sit on the sidelines marking time during such periods.

❸ On an intra-day basis, indices and currencies often stagnate before key figures or announcements come out. A regular event, such as the US Federal Open Markets Committee (FOMC) meeting, often results in hours of waiting as markets come to a virtual standstill prior to an announcement.

Instead of watching paint dry and going stir crazy in front of the screen, one could make some money on a bet based on the market going nowhere.

Daily or intraday

Trading either time-frame is possible using binary betting. It's simply a question of establishing which signals are most reliable.

The advantage of intra-day data is that perhaps signals can be generated more frequently – satisfying the lust for action and rapid account growth.

The caveat however, is that intra-day patterns often tend to display less certainty than longer-term ones. Another advantage of daily trading is that analysis can be performed once or twice a day, rather than having to watch the screen all day long.

Choice of instrument

A range of leading UK, US and other equities and indices are available to the binary bet trader, as well as a range of currencies and commodities. Choose the instruments that you can most reliably predict statistically.

An advantage of following a wider range of instruments, using some kind of scanning system, is that you have a wider possible choice of trading opportunities.

As a final tip, only take the best trades – not the ones that almost but don't fully fit the criteria. You owe yourself nothing less. And if you miss a trade, always remember – the markets will still be there tomorrow. ■