BASICS OF FOREX

Welcome to Forex

The Foreign Currency Exchange Market (also called FOREX or FX) is the largest and most active marketplace in the world. It is the largest not only by volume (more than two trillion dollars per day) but also the most active market because of its 24 hour non-stop schedule. Most of the trading takes place through an electronic brokering system known as the interbank data center. At any given time, in some part of the world; foreign exchange is being traded

A few years ago, foreign exchange trading was limited to banks and other large financial institutions. Now in this electronic age, any person can perform online trading with a personal computer and the Internet. Almost all banks, hedge funds, pensions, and mutual funds are involved in foreign exchange trading. Money can earned regardless if a currency is gaining or losing its value.

Currencies are always quoted as a combination of pairs. The four major pairs traded are

· EUR/USD : Euro to the USA Dollar
· USD/JPY : USA Dollar to the Yen
· GBP/USD : English Pound to the USA Dollar
· CHF/USD : Swiss Franc to the USA Dollar

Pairs without reference to the American dollar like EUR/JPY, EUR/GBP, GBP/JPY and so on are called "Cross pairs." Other than the major pairs and cross pairs; some minor pair combinations like AUD/USD, USD/CAD can also be traded to give the trader or investor freedom to speculate in whichever currency he/she chooses.

Besides Volume and Liquidity, Forex (FX) offers more to Traders and Investors:
· 24 Hours trading
· Commission free trading (Broker earning only from spread)
· Sell before you buy (Short Selling)
· Margin Trading with leverage up to 200:1
· Hold a position for unlimited time

Risk Warning

Forex Trading is considered a "High Risk / High Reward" business. Your investments in forex trading are exposed to high risks and should be traded only with risk capital. There is no system which can guarantee profits in trading any foreign exchange, commodity, index, currency or any other speculation

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Forex Basics

Assuming that you all are familiar to stock market, I will start with a comparison to stocks.

Both stocks and forex are considered as high risk/high returns business. Unlike stock markets which are different for different countries, forex is one single market and daily turnover of the market is approximately USD 3 trillion! Market is open from Monday to Friday and its a 24 hours market.

Everybody needs foreign exchange...whether you are an exporter or importer or a tourist...If a UK company has to takeover an Australian company they will have to sell pound and buy Australian dollar which may make Pound weaker against AUD. If you are an exporter you repatriate your funds from other countries in euro or dollar or any other currency and convert it into your local currency. This is one of the reasons why yen becomes strong against dollar before their annual book closing. Japan has a trade surplus against US. (exports>imports)

Almost all the hedge funds, mutual funds, pension funds or any investment companies and individual investors trade in forex and take advantage of the currency movements. Simple logic is buy low sell high. short selling is possible here. In stocks you may short sell ...and buy back on the same day before the market closing and may make some profits or loss. you will not be allowed to carry forward your trade for next day. (it is possible in some countries or with some brokers) but in forex you can sell euros against dollars (u need not have euros) and close the deal (buy euro against dollar) after 15 days or a month and take your profits. So whichever side market moves you can make money. You need not worry if euro crash or yen crash or any other currency crashes.

There is only one reason for a person to loose in forex. I call it as KK's hope and fear theory. When the market goes against him he will keep the position hoping that market will bounce back. when the market is in his favour he will have a fear that market may bounce back and he will loose the profits. HOPE lets him keep a loosing position till he looses 99% of the account and due to fear he will grab small profits and miss out the big profits. There is only 1 factor which makes forex riskier than stocks. In stocks a person is generally allowed to buy 4 times more than his deposit value. That is with USD 100 your broker may allow you to buy stocks worth USD 400. But in forex you can buy USD 10,000 worth currency for a deposit of USD 100 and people who become greedy tend to buy more and loose the account. That is where your money management skills come into picture.

You don't have to be a technical analyst and economics expert to trade in forex. I know at least a dozen chartered accountants who have lost money in stock market. All you need to learn is some money management, risk management and emotional management skills.

let's get into trading basics now.

In forex currencies are bought in lots which is normally USD 100,000. Few American companies recently introduced mini forex where you can buy small lots of USD 10,000. As a beginner I suggest you to go for mini forex trading. With a deposit of USD 5,000 the broker will allow you to buy currencies worth USD 500,000. But to be on the safe side lets keep USD 1,000 per lot. (1lot = USD 10,000)

Lets concentrate only on major currencies.
4 major currency pairs are
euro/usd
usd/yen
pound/usd
usd/swiss frank

currencies are always quoted in pairs. buying euro/dollar means buying euro and selling dollar. selling dollar/yen means seling dollar against yen. if dollar/yen goes up it is dollar which becomes stronger against yen. if euro/dollar goes down, it is euro which is becoming weaker. It always the first currency against 2nd currency

you buy 1 euro/usd at 1.2200 and sell at 1.2201
we say you made 1 pip profit (1 pip is also called as 1 point)
when u buy 1 lot, this profit becomes 1 dollar in mini trade

dollar/yen is at 105.50 now
say you expect this pair to go down
you sell 1 lot at 105.50
(here u r selling dollar and buying yen)
you take profits at 105.40
you made 10 pips profits
this amounts to a profit of 10 yen (approx 8 dollar)

If you understand this theory, you are now ready to start demo trade

If you visit the link 'forex brokers worldwide' in my site you will see different websites

of forex brokers. Fx Solution is one of the major forex broker and one of few companies which offer mini forex trade.

To begin with, lets go for a demo trade with them. when you decide to go for a real trade you may open account with any of the licensed forex broker.

Download the trading station from here and install the software

Register for a demo trading and they will give you your login name and password. using this login name and password you can log on to their server and start watching real time currency prices and even trading them.

The first window gives you the currency price. click on the price and buy a currency. if u r seeing euro price as 1.2240/45 it means you get 1.2245 for buying and 1.2240 for selling. if you think euro will go down from here click on the selling price and sell 1 lot.

When u sell, your open position window shows the details like time of purchase/sold, quantity, current price, current loss/profit etc.

You may click on the blank space below stop and leave a price which will be your stop loss price. for example if u leave the price as 1.2270, the maximum loss you make in this trade is 30 dollars. this is how you limit your losses. you may click on blank space below limit and mention the price where you want to take profits. just do some trades to get acqauinted to the software. do not worry about profit or loss now.

Goto http://www.forexveda.com/charts.html. Watch the charts and take your own decisions and do some trades to get acquinted to the software. u may see 1 hour chart for short term trades (short term = 1 min to few hours)
or day charts for medium term trades (1 day to few days) to get acquinted to the software do day trading and go for short trades.

You can leave a limit order buy clicking on entry. for example if the currency is at 1.1750 and u want to sell at 1.2280 and u have no time to sit and watch the market, you may just click on entry and select the currency, quantity and price and click on ok. the moment the price reaches the level it will be bought or sold at the specified price.

Forex Lesson 2

Hope you have gone through the forex basics and understood how the forex trading

works. In this lesson I will be introducing you to some trading strategies and economic data releases which have immediate affect on the market.

As I have said in forexbasics, forex trading is about descipline, money management and risk management. One need not be an economist to predict the forex market. One need not keep watching market through out the day (and night) to trade in forex market. You need not be a technical analyst or fundamental analyst to make money in forex. All you need is a right strategy and descipline to follow the starategy. Make your own rules, but don't break it.

How Important are news and economic data releases?
Lot of people trade based on news and economic data releases. The news and data have only a temporary effect in the market. On september 11th dollar crashed after the terror strike. It crashed next day too. But in following days, dollar gained strength and made new highs. During Kosovo war, when euro was crashing against dollar, all gave reasons to kosovo war. When the war got over, euro gained few pips and later continued its downward trend. When some ministers in japan give statement favouring weaker yen, you will see a sudden spike in Dollar/yen. After few hours you can notice that it will come back to where it was earlier. There are lot of data releases from USA at 13:30 GMT. you may notice that a dollar supportive news may just push dollar up and little later market is back where it was trading before the data release.

If you observe the market reaction during data releases for few days, you will be able to understand when to protect your profits and when to open positions. If you notice that dollar has been weakening throughout the asia and european sessions, a negative data may not pull the dollar much down but a positive data will give a quick correction. and after a while it will be back at where it was.

You can actually ignore the news and facts. It is advisable to move trailing stops just before data release to protect profits.

Trailing stop

If you buy something at 40 and the market is trading at 90 just before data, its better to place a stop at 80 so that if there is a sudden fall u may exit at 80 with 30 pips profits. and when the market comes back to 40 to 50 you may buy back.

Strategies

I use 2 different startegies depending on the market.
1) Trade in medium term direction with large stop loss.
For example euro is in upward direction. u may keep buying euro at lower and take profits and buy back. if euro falls more after you buy, you may buy more at lower keeping stops for all at much lower level. Incase of a currency changing medium term direction, ou may end up loosing a big amount. But, that doesnt happen too often. by the time it happens, you may have recovered part of the losses by making many trades at lower levels. This strategy is advisable for accounts with large equities.

2) Keep small loss and big profit targets
Here you will be trading only if you find the RRR attractive. RRR means risk to reward ratio. here you will enter market only when there is more room for profits and less for risks. You may have position something like this. Buy at 1.2230 stop loss at 1.2130 and target 1.2430. In this trade you are risking 100 pips for a profit of 200 pips. You can even trade for less pips. For example buy dollar/yen at 108.60 stop loss at 108.20 and target 109.10 Here you are taking 40 pips risk for a 50 pips profits

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The End