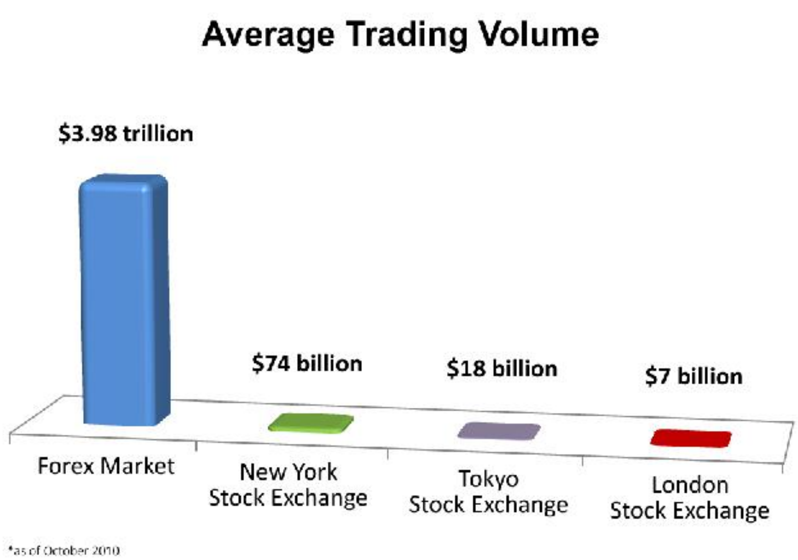
What is the Forex?

If you've ever traveled to another country, you most likely had to find a currency exchange booth at the airport, and then exchange the money you have into the currency of the country you are visiting.

When you do this, you have just participated in the Forex market! You've exchanged one currency for another.

The foreign exchange market, also known as "Forex" or "FX," is the largest financial market in the world. Compared to the measly $70+ billion a day volume of the New York Stock Exchange (The largest stock market in the world), the foreign exchange market is huge with its $4 TRILLION a day trade volume. It is the largest LEGAL market in the world.

Below is a graph of the average daily trading volume for the Forex market, New York Stock Exchange, Tokyo Stock Exchange, and London Stock Exchange:



That huge $4 trillion number covers the entire global foreign exchange market, BUT retail traders (that's us) trade the spot market and that's about $1.49 trillion of which about 319 Million dollars a day is traded by retail traders like yourself. With that much trading occurring, certainly there are some opportunities for the average guy to participate.

What do We Trade in the Forex?

We trade **MONEY –** lots of it**.** In the stock market we trade a piece of paper that represents a share of a company stock. But in the Forex we trade the money: YEN, British Pounds, Dollars, Swiss Francs etc.

To get your head wrapped around this concept you can equate buying a currency as buying a share in a particular country, similar to buying stocks of a company. The price of the currency is a direct reflection of what the market thinks about the current and future health of the United Kingdom economy. And this is compared to its counterpart in the Forex.

When you buy, say, the Japanese yen, you are basically buying a "share" in the Japanese economy. You are *betting* that the Japanese economy is doing well, and will even get better as time goes. Once you sell those "shares" back to the market, hopefully, you will end up with a profit.

Generally speaking, the exchange rate of a currency versus other currencies is a reflection of the condition of that country's economy, compared to other countries' economies.

Major Currencies

Symbol	**Country**	**Currency**	**Nickname**
USD	United States	Dollar	Buck
EUR	Euro zone members	Euro	Fiber
JPY	Japan	Yen	Yen
GBP	Great Britain	Pound	Cable
CHF	Switzerland	Franc	Swissy
CAD	Canada	Dollar	Loonie
AUD	Australia	Dollar	Aussie
NZD	New Zealand	Dollar	Kiwi

Currency symbols always have three letters, where the first two letters identify the name of the country and the third letter identifies the name of that country's currency.

Take NZD for instance. NZ stands for New Zealand, while D stands for dollar.

The currencies shown in the above chart are called the majors because they are the most widely traded ones.

Currencies Are Traded in Pairs

Forex trading is the simultaneous buying of one currency and selling another. Currencies are traded through a broker or dealer, and are traded in pairs; for example the euro and the U.S. dollar (EUR/USD) or the British pound and the Japanese yen (GBP/JPY).

When you trade in the Forex market, you buy or sell in currency pairs.

Major Currency Pairs

The currency pairs listed below are considered the "majors". These pairs all contain the U.S. dollar (USD) on one side and are the most frequently traded. The majors are the most liquid and widely traded currency pairs in the world.

Pair	Countries	FX Geek Speak
EUR/USD	Euro zone / United States	"euro dollar"
USD/JPY	United States / Japan	"dollar yen"
GBP/USD	United Kingdom / United States	"pound dollar"
USD/CHF	United States/ Switzerland	"dollar swissy"
USD/CAD	United States / Canada	"dollar loonie"
AUD/USD	Australia / United States	"aussie dollar"
NZD/USD	New Zealand / United States	"kiwi dollar"

Major Cross-Currency Pairs or Minor Currency Pairs

Currency pairs that don't contain the U.S. dollar (USD) are known as cross-currency pairs or simply as the "crosses." Major crosses are also known as "minors." The most actively traded crosses are derived from the three major non-USD currencies: EUR, JPY, and GBP.

Euro Crosses

Pair	Countries	FX Geek Speak
EUR/CHF	Euro zone / Switzerland	"euro swissy"
EUR/GBP	Euro zone / United Kingdom	"euro pound"
EUR/CAD	Euro zone / Canada	"euro loonie"
EUR/AUD	Euro zone / Australia	"euro aussie"
EUR/NZD	Euro zone / New Zealand	"euro kiwi"

Yen Crosses

Pair	Countries	FX Geek Speak
EUR/JPY	Euro zone / Japan	"euro yen" or "yuppy"
GBP/JPY	United Kingdom / Japan	"pound yen" or "guppy"
CHF/JPY	Switzerland / Japan	"swissy yen"
CAD/JPY	Canada / Japan	"loonie yen"
AUD/JPY	Australia / Japan	"aussie yen"
NZD/JPY	New Zealand / Japan	"kiwi yen"

Pound Crosses

Pair	Countries	FX Geek Speak
GBP/CHF	United Kingdom / Switzerland	"pound swissy"
GBP/AUD	United Kingdom / Australia	"pound aussie"
GBP/CAD	United Kingdom / Canada	"pound loonie"
GBP/NZD	United Kingdom / New Zealand	"pound kiwi"

Other Crosses

Pair	Countries	FX Geek Speak
AUD/CHF	Australia / Switzerland	"aussie swissy"
AUD/CAD	Australia / Canada	"aussie loonie"
AUD/NZD	Australia / New Zealand	"aussie kiwi"

CAD/CHF	Canada / Switzerland	"loonie swissy"
NZD/CHF	New Zealand / Switzerland	"kiwi swissy"
NZD/CAD	New Zealand / Canada	"kiwi loonie"

Exotic Pairs

Exotic pairs are made up of one major currency paired with the currency of an emerging economy, such as Brazil, Mexico, or Hungary. The chart below contains a few examples of exotic currency pairs. Depending on your Forex broker, you may see the following exotic pairs so it's good to know what they are. Keep in mind that these pairs aren't as heavily traded as the "majors" or "crosses," so the transaction costs associated with trading these pairs are usually bigger.

Pair	Countries	FX Geek Speak
USD/HKD	United States / Hong Kong	
USD/SGD	United States / Singapore	
USD/ZAR	United States / South Africa	"dollar rand"
USD/THB	United States / Thailand	"dollar baht"
USD/MXN	United States / Mexico	"dollar peso"
USD/DKK	United States / Denmark	"dollar krone"
USD/SEK	United States / Sweden	
USD/NOK	United States / Norway	

It isn't unusual to see spreads that are two or three times bigger than that of EUR/USD or USD/JPY. So if you want to trade exotics pairs, remember to factor this in your decision.

Forex Market Size and Forex Liquidity

SIZE MATTERS! Unlike other financial markets like the New York Stock Exchange, the Forex spot market has neither a physical location nor a central exchange.

The Forex market is considered an Over-the-Counter (OTC), or "Interbank", market due to the fact that the entire market is run electronically, within a network of banks, continuously over a 24-hour period.

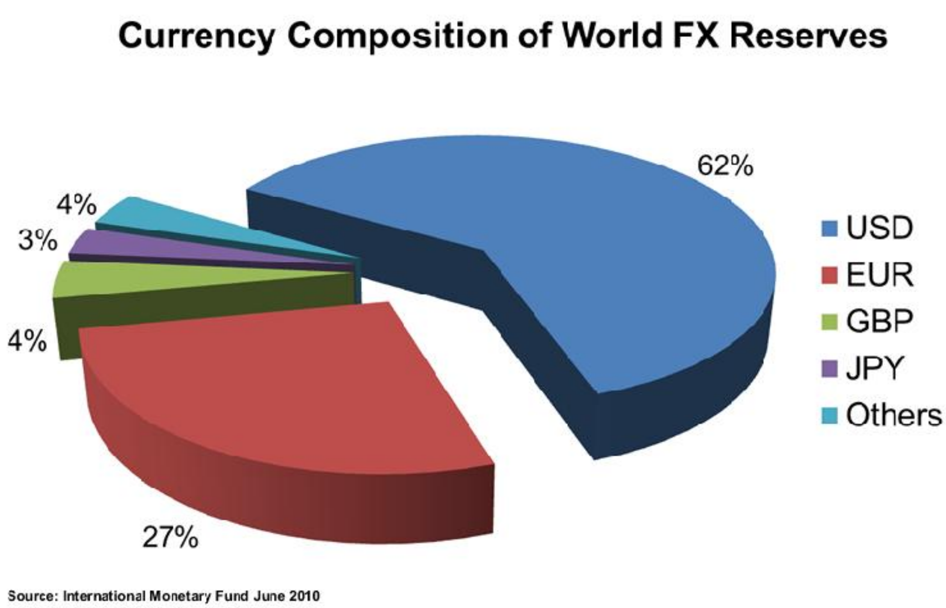
There is NO central location like Wall Street so the spot Forex market is spread all over the globe. The Forex OTC market is by far the biggest and most popular financial market in the world, traded globally by a large number of individuals, banks and organizations.

In the OTC market, participants determine who they want to trade with depending on trading conditions, attractiveness of prices, and reputation of the trading counterpart.

The chart below shows the most actively traded currencies.

The Dollar is King of the Forex

You've probably noticed how often we keep mentioning the U.S. dollar (USD). If the USD is one half of every major currency pair, and the majors comprise 75% of all trades, then it's a must to pay attention to the U.S. dollar. The USD is king!



In fact, according to the International Monetary Fund (IMF), the U.S. dollar comprises almost 62% of the world's official foreign exchange reserves! Because almost every investor, business, and central bank own it, they pay attention to the U.S. dollar.

There are also other significant reasons why the U.S. dollar plays a central role in the Forex market:

- The United States economy is the LARGEST economy in the world.
- The U.S. dollar is the reserve currency of the world.
- The United States has the largest and most liquid financial markets in the world.
- The United States has a super stable political system.
- The United States is the world's sole military superpower.
- The U.S. dollar is the medium of exchange for many cross-border transactions. For example, oil is priced in U.S. dollars. So if Mexico wants to buy oil from Saudi Arabia, it can only be bought with U.S. dollar. If Mexico doesn't have any dollars, it has to sell its pesos first and buy U.S. dollars.

Speculation is what drives the Forex

One important thing to note about the Forex market is that while commercial and financial transactions are part of trading volume, most currency trading is based on speculation. That is the trading of one currency against another hoping to profit from the fluctuation of that price.

So the vast majority of trading volume comes from traders that buy and sell based on intraday price movements. The trading volume brought about by speculators is estimated to be more than 90%! Should you decide to become a Forex Trader you will be one of these speculators.

The amount of buying and selling volume happening at any given time - is extremely high which means there is lots of liquidity. This makes it very easy for anyone to buy and sell currencies.

From the perspective of an investor, liquidity is very important because it determines how easily price can change over a given time period. A liquid market environment like Forex enables huge trading volumes to happen with very little effect on price, or price action.

While the Forex market is relatively very liquid, the market depth could change depending on the currency pair and time of day. As a general rule you want to trade when there is the highest amount of liquidity (or market participation) and that is the first 2 to 2 ½ hours of each session.

Different Ways to Trade the Forex

Because Forex is such a big market , traders can use a number of different ways to invest or speculate in currencies. Among these, the most popular ones are Forex spot, futures, options, and exchange-traded funds (or ETFs).

Spot Market

In the spot market, currencies are traded immediately or "on the spot," using the current market price. What makes this market unique is its simplicity, liquidity, tight spreads, and round-the-clock operations. The ability to participate in this market is available to the average person since accounts can be opened with as little as a $250. Aside from that, most brokers usually provide charts, news, and research for free.

Futures

Futures are contracts to buy or sell a certain asset at a specified price on a future date (That's why they're called futures!). Forex futures were created by the Chicago Mercantile Exchange (CME) back in 1972. Since futures contracts are standardized and traded through a centralized exchange, the market is very transparent and well-regulated.

Options

An "option" is a financial instrument that gives the buyer the right or the option, but not the obligation, to buy or sell an asset at a specified price on the option's expiration date. If a trader "sold" an option, then he or she would be obliged to buy or sell an asset at a specific price at the expiration date.

Just like futures, options are also traded on an exchange, such as the Chicago Board Options Exchange, the International Securities Exchange, or the Philadelphia Stock Exchange. However, the disadvantage in trading Forex options is that market hours are limited for certain options and the liquidity is not nearly as great as the futures or spot market.

Exchange-traded Funds

Exchange-traded funds or ETFs are a new hybrid of the Forex world.

An ETF could contain a set of stocks combined with some currencies, allowing the trader to diversify with different assets. These are created by financial institutions and can be traded like stocks through an exchange. Like Forex options, the limitation in trading ETFs is that the market isn't open 24 hours. Also, since ETFs contain stocks, these are subject to trading commissions and other transaction costs.

You can also buy and sell ETF's like Silver (SLV) and Gold (GLD) and participate in owning a fund that has nothing but these metals as the basis for its existence. With the exception of a small % of the value of the ETF assigned to Administration, the value of the share is based on the value of the commodity each day. In the Spot Forex, we can trade Silver (XAG) or Gold (XAU) similar to a currency trade since these precious metals are bought and sold using US dollars.

Many traders use great charts to do their analysis and then take positions in ETF's.

The Advantages of Trading the Forex

There are many benefits and advantages of trading Forex. Here are just a few reasons why so many people are choosing this market:

No commissions

No clearing fees, no exchange fees, no government fees, no brokerage fees. Most retail brokers are compensated for their services through something called the "bid-ask spread".

No middlemen

Spot currency trading eliminates the middlemen and allows you to trade directly with the market responsible for the pricing on a particular currency pair.

No fixed lot size

In the futures markets, lot or contract sizes are determined by the exchanges. A standard-size contract for silver futures is 5,000 ounces. In spot Forex, you determine your own lot, or position size. This allows traders to participate with accounts as small as $250.

Low transaction costs

The retail transaction cost (the bid/ask spread) is typically less than 0.1% under normal market conditions. At larger dealers, the spread could be as low as 0.07%. Of course this depends on your leverage and you will learn about that a little later in this report.

A 24-hour market

There is no waiting for the opening bell. From the Monday morning opening in Australia to the afternoon close in New York, the Forex market never sleeps. This is awesome for those who want to trade on a part-time basis, because you can choose when you want to trade: morning, noon, night, during breakfast, or even on your mobile phone using a broker app.

No one can corner the market

The foreign exchange market is so huge and has so many participants that no single entity (not even a central bank) can control the market price for an extended period of time.

Leverage

In Forex trading, a small deposit can control a much larger total contract value. Leverage gives the trader the ability to make nice profits, and at the same time keep risk capital to a minimum.

For example, a Forex broker may offer 50-to-1 leverage (it is 100-to-one or higher outside the USA), which means that a $50 dollar margin deposit would enable a trader to buy or sell $2,500 worth of currencies. Similarly, with $500 dollars, one could trade with $25,000 dollars and so on. You pocket the gains on $25,000 not the $500 you used to control that amount. However, leverage can be a double-edged sword. You accept the loss on $25,000 not the $500 you used to control that amount.

Without proper risk management, this high degree of leverage can lead to large losses as well as gains.

High Liquidity.

Because the Forex market is so enormous, it is also extremely liquid. This means that under normal market conditions, with a click of a mouse you can instantaneously buy and sell at will as there will usually be someone in the market willing to take the other side of your trade. You are never "stuck" in a trade. You can even set your online trading platform to automatically close your position once your desired profit level (a limit order) has been reached, and/or close a trade if a trade is going against you (a stop loss order). Additionally, you can use a trailing stop that moves with the currency to protect any gains.

Low Barriers to Entry

You would think that getting started as a currency trader would cost a ton of money. The fact is, when compared to trading stocks, options or futures, it doesn't. Online Forex brokers offer "mini" and "micro" trading accounts, some with a minimum account deposit of $250.

We're not saying you should open an account with the bare minimum, but it does make Forex trading much more accessible to the average individual who doesn't have a lot of start-up trading capital.

Free Practice Software!

Most online Forex brokers offer free "demo" accounts to practice trading and build your skills, along with real-time Forex news and charting services.

You can practice and then get a FREE charting software package demo from ProAct Traders to start your learning journey.

Demo accounts allow a novice trader to hone their trading skills with "play money" before opening a live trading account and risking real money.

But why trade the Forex and not the more traditional markets?

Forex vs. Stocks

There are approximately 4,500 stocks listed on the New York Stock exchange. Another 3,500 are listed on the NASDAQ. Which one will you trade? Do you have the time to stay on top of so many companies?

In spot currency trading, there are dozens of currencies traded, but the majority of market players trade the four major pairs. These four pairs are much easier to keep an eye on than thousands of stocks?

Here are a few more advantages:

24-Hour Market

The Forex market is a seamless 24-hour market. Most brokers are open from Sunday at 4:00 pm EST until Friday at 4:00 pm EST, with customer service usually available 24/7 and support staff who speaks your language. With the ability to trade during the U.S., Asian, and European market hours, you can create your own trading schedule.

Minimal or No Commissions

Most Forex brokers charge no commission or additional transactions fees to trade currencies online or over the phone. Combined with the tight, consistent, and fully transparent spread, Forex trading costs are lower than those of any other market. Most brokers are compensated for their services through the bid/ask spread.

Instant Execution of Market Orders

Your trades are instantly executed under normal market conditions. Under these conditions, usually the price shown when you execute your market order is the price you get. You're able to execute directly off real-time up to the second streaming prices.

Keep in mind that many brokers only guarantee stop, limit, and entry orders under normal market conditions. Trading during a major fundamental announcement or during a time of intense conflict (like a war breaks out etc.) the broker will not be able to guarantee your stops or orders. Fills are instantaneous most of the time, but under extraordinarily volatile market conditions, order execution may experience delays.

Short-Selling without an Uptick

Unlike the equity market, there is no restriction on short selling in the currency market. Trading opportunities exist in the currency market regardless of whether a trader is long or short, or whichever way the market is moving. Since currency trading always involves buying one currency and selling another, there is no structural bias to the market. So you always have equal access to trade in a rising or falling market.

No Middlemen

Centralized exchanges provide many advantages to the trader. However, one of the problems with any centralized exchange is the involvement of middlemen. Any party located in between the trader and the buyer or seller of the security or instrument traded will cost them money. The cost can be either in time or in fees.

Spot currency trading, on the other hand, is decentralized, which means quotes can vary from different currency dealers. Competition between them is so fierce that you are almost always assured that you get the best deals. Forex traders get quicker access and cheaper costs.

Buy/Sell programs do not control the market.

The stock market is very susceptible to large fund buying and selling.

In spot trading, the massive size of the Forex market makes the likelihood of any one fund or bank controlling a particular currency very small. Banks, hedge funds, governments, retail currency conversion houses, and large net worth individuals are just some of the participants in the spot currency markets where the liquidity is unprecedented.

Analysts and brokerage firms are less likely to influence the market

IPOs are big business for both the companies going public and the brokerage houses. Relationships are mutually beneficial and analysts work for the brokerage houses that need the companies as clients. That catch-22 will never disappear.

Much of the price of a stock is based on perception. For instance: when Martha Stewart decided to go to jail 3 weeks early, the stock of Martha Stewart rose 30% in a matter of a day. Why? She would be back out of jail 3 weeks sooner. That kind of thing does not happen in the Forex.

Foreign exchange, as the prime market, generates billions in revenue for the world's banks and is a necessity of the global markets. Analysts in foreign exchange have very little effect on exchange rates; they just analyze the Forex market.

Advantages	Forex	Stocks
24-Hour Trading	YES	No
Minimal or no Commission	YES	No
Instant Execution of Market Orders	YES	No
Short-selling without an Uptick	YES	No
No Middlemen	YES	No
No Market Manipulation	YES	No

Forex vs. Futures

The Forex market also boasts of a bunch of advantages over the futures market.

Liquidity

In the Forex market, $4 trillion is traded daily, making it the largest and most liquid market in the world. This market can absorb trading volume and transaction sizes that dwarf the capacity of any other market. The futures market trades a relatively small $30 billion per day.

The futures markets can't compete with its relatively limited liquidity. The Forex market is always liquid, meaning positions can be liquidated and stop orders executed with little or no slippage except in extremely volatile market conditions.

24-Hour Market

At 5:00 pm EST Sunday, trading begins as markets open in Sydney. At 7:00 pm EST the Tokyo market opens, followed by London at 3:00 am EST. And finally, New York opens at 8:00 am EST and closes at 4:00 p.m. EST. Before New York trading closes, the Sydney market is back open - it's a 24-hour seamless market!

This allows you to react to favorable or unfavorable news by trading immediately. If important data comes in from the United Kingdom or Japan while the U.S. futures market is closed, the next day's opening could be a wild ride. (Overnight markets in futures currency contracts exist, but they are thinly traded, not very liquid, and are difficult for the average investor to access.)

Minimal or no commissions

With Electronic Communications Brokers becoming more popular and prevalent over the past couple of years, there is the chance that a broker may require you to pay commissions. But really, the commission fees are peanuts compared to what you pay in the futures market. The competition among brokers is so fierce that you will most likely get the best quotes and very low transaction costs.

Price

When trading Forex, you get rapid execution and price certainty under normal market conditions. In contrast, the futures and equities markets do not offer price certainty or instant trade execution. Even with the advent of electronic trading and limited guarantees of execution speed, the prices for fills for futures and equities on market orders are far from certain. The prices quoted by brokers often represent the LAST trade, not necessarily the price for which the contract will be filled.

Guaranteed Limited Risk

Traders must have position limits for the purpose of risk management. This number is set relative to the money in a trader's account. Risk is minimized in the spot Forex market because the online capabilities of the trading platform will automatically generate a margin call if the required margin amount exceeds the available trading capital in your account.

During normal market conditions, all open positions will be closed immediately (during fast market conditions, your position could be closed beyond your stop loss level).

In the futures market, your position may be liquidated at a loss bigger than what you had in your account, and you will be liable for any resulting deficit in the account.

Advantages	Forex	Futures
24-Hour Trading	YES	No
Minimal or no Commission	YES	No
Up to 500:1 Leverage	YES	No
Price Certainty	YES	No
Guaranteed Limited Risk	YES	No

The Forex Market Structure

For the sake of comparison, let us first examine a market that you are probably very familiar with: the stock market. This is how the structure of the stock market looks like:

By its very nature, the stock market tends to be very monopolistic. There is only one entity, one specialist that controls prices. All trades must go through this specialist. Because of this, prices can easily be altered to benefit the specialist, and not traders.

How does this happen?

In the stock market, the specialist is forced to fulfill the order of its clients. Now, let's say the number of sellers suddenly exceed the number of buyers. The specialist, which is forced to fulfill the order of its clients, the sellers in this case, is left with a bunch of stock that he cannot sell-off to the buyer side.

In order to prevent this from happening, the specialist will simply widen the spread or increase the transaction cost to prevent sellers from entering the market. In other words, the specialists can manipulate the quotes it is offering to accommodate its needs.

Trading Spot FX is Decentralized

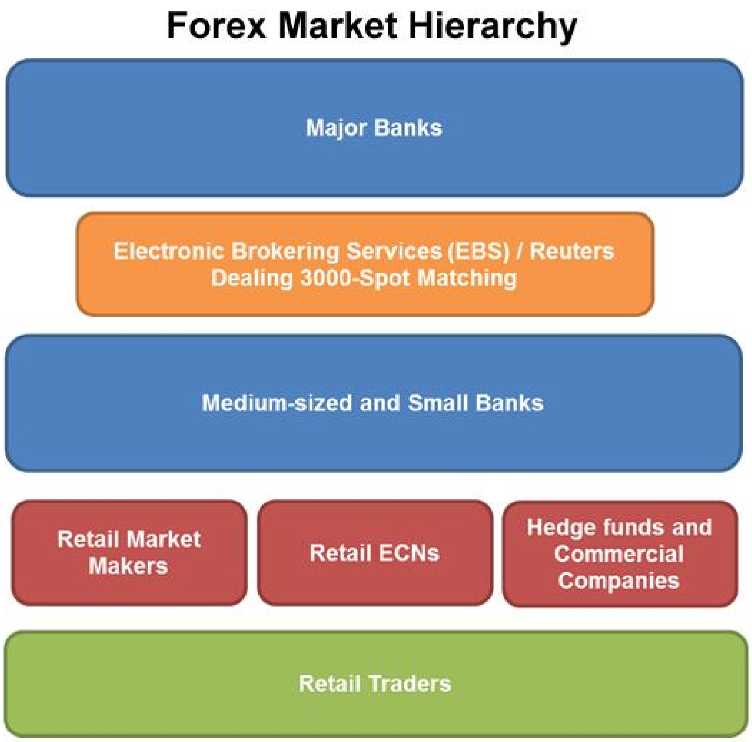
Unlike in trading stocks or futures, you don't need to go through a centralized exchange like the New York Stock Exchange with just one price. In the Forex market, there is no single price that for a given currency at any time, which means quotes from different currency dealers vary.

This might be overwhelming at first, but this is what makes the Forex market so great! The market is so huge and the competition between dealers is so fierce that you get the best deal almost every single time.

Also, you can trade the Forex anywhere you have an internet connection (or call your broker on your cell phone).

The FX Ladder

Even though the Forex market is decentralized there is a structure to it



Above graphic from babypips.com

At the top of the Forex market ladder is the interbank market. Composed of the largest banks of the world and some smaller banks, the participants of this market trade directly with each other or electronically.

All the banks that are part of the interbank market can see the rates that each other is offering, but this doesn't necessarily mean that anyone can make deals at those prices.

Next on the ladder are the hedge funds, corporations, retail market makers, and retail ECNs. Since these institutions do not have tight credit relationships with the participants of the interbank market, they have to do their transactions via commercial banks. This means that their rates are slightly higher and more expensive than those who are part of the interbank market.

At the very bottom of the ladder are the retail traders. Your Broker has a relationship with those higher up the ladder so you execute trades with him and he in turn executes all the trades with those higher up the ladder.

Market Players

It is important that you that you understand the nature of the spot Forex market and who are the main players.

Until the late 1990s, only the "big guys" could play this game. However, because of the rise of the internet, online Forex trading firms are now able to offer trading accounts to "retail" traders like us.

1. The Super Banks

Since the Forex spot market is decentralized, it is the largest banks in the world that determine the exchange rates. Based on the supply and demand for currencies, they are generally the ones that make the bid/ask spread.

These large banks, collectively known as the interbank market, take on an incredible amount of Forex transactions each day for both their customers and themselves. A couple of these super banks include UBS, Barclays Capital, Deutsche Bank, and Citigroup. You could say that the interbank market is THE foreign exchange market.

2. Large Commercial Companies

Companies take part in the foreign exchange market for the purpose of doing business. For instance, Apple must first exchange its U.S. dollars for the Japanese yen when purchasing electronic parts from Japan for their products. Since the volume they trade is much smaller than those in the interbank market, this type of market player typically deals with commercial banks for their transactions.

Mergers and acquisitions (M&A) between large companies can also create currency exchange rate fluctuations. In international cross-border M&As, a lot of currency conversations happens that could move prices around.

3. Governments and Central Banks

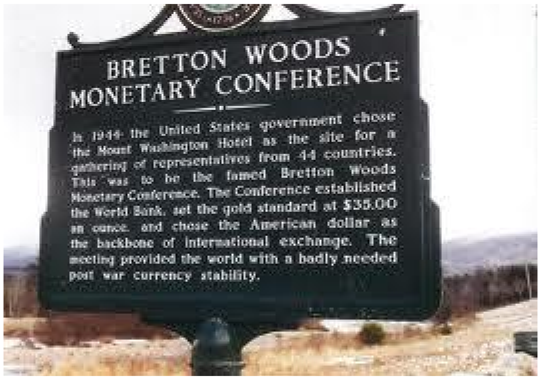
Governments and central banks, such as the European Central Bank, the Bank of England, and the Federal Reserve, are regularly involved in the Forex market too. Just like companies, national governments participate in the Forex market for their operations, international trade payments, and handling their foreign exchange reserves.

Meanwhile, central banks affect the Forex market when they adjust interest rates to control inflation. By doing this, they can affect currency valuation. There are also instances when central banks intervene, either directly or verbally, in the Forex market when they want to realign exchange rates. Sometimes, central banks think that their currency is priced too high or too low, so they start massive sell/buy operations to alter exchange rates. All of these transactions will take place in the Forex.

4. The Speculators

Comprising close to 90% of all trading volume, speculators can be almost anything. If you decide to trade Forex, you will be one of these.

History of the Forex



At the end of the World War II, the whole world was experiencing so much chaos that the major Western governments felt the need to create a system to stabilize the global economy.

Known as the "Bretton Woods System," the agreement set the exchange rate of all currencies against gold. This stabilized exchange rates for a while, but as the major economies of the world started to change and grow at different speeds, the rules of the system soon became obsolete and limiting.

In 1971, the Bretton Woods Agreement was abolished and replaced by a different currency valuation system. With the United States in the drivers seat, the currency market evolved to a free-floating one, where exchange rates were determined by supply and demand.

At first, It was difficult to determine fair exchange rates, but advances in technology and communication eventually made things easier.

In the 1990s, banks began creating their own trading platforms. These platforms were designed to stream live quotes to their clients so that they could instantly execute trades themselves.
Meanwhile, some smart business-minded marketing machines introduced internet-based trading platforms for individual traders.

Known as "retail Forex brokers", these entities made it easy for individuals to trade by allowing smaller trade sizes. Unlike in the interbank market where the standard trade size is one million units, retail brokers allowed individuals to trade as little as 1000 units!

Retail Forex Brokers

In the past, only the big speculators and highly capitalized investment funds could trade currencies, but thanks to retail Forex brokers and the Internet, this isn't the case anymore.

With hardly any barriers to entry, anybody could just contact a broker, open up an account, deposit some money, and trade Forex from the comfort of their own home. Brokers basically come in two forms:

1. Market makers, as their name suggests, "make" or set their own bid and ask prices themselves and

2. Electronic Communications Networks (ECN), who use the best bid and ask prices available to them from different institutions on the interbank market.

Market Makers

Let's say you wanted to go to Mexico to eat some tacos and have a margarita and watch the sun set on Puerto Vallarta at El Set restaurant. In order for you to transact in the country, you need to have some Mexican Peso's first by going to a bank or the local foreign currency exchange office. For them to take the opposite side of your transaction, you have to agree to exchange your home currency for Mexican Peso's at the price they set.

Like in all business transactions, there is a catch. In this case, it comes in the form of the bid/ask spread.

For instance, if the bank's buying price (bid) for EUR/USD is 1.2000, and their selling price (ask) is 1.2002, then the bid/ask spread is 0.0002. Although seemingly small, when you're talking about millions of these Forex transactions every day, it does add up to create a hefty profit for the market makers!

The market makers are then the fundamental building blocks of the foreign exchange market. Retail market makers basically provide liquidity by "repackaging" large contract sizes from wholesalers into bite size pieces. Without them, it will be very hard for the average Joe to trade Forex.

Electronic Communications Network

Electronic Communication Network is the name given for trading platforms that automatically match customer's buy and sell orders at stated prices. These stated prices are gathered from different market makers, banks, and even other traders who use the ECN. Whenever a certain sell or buy order is made, it is matched up to the best bid/ask price out there.

Due to ability of traders to set their own prices, ECN brokers typically charge a VERY small commission for the trades you take. The combination of tight spreads and small commission usually make transaction costs cheaper on ECN brokers.

Trading Sessions

Yes, it is true that the Forex market is open 24 hours a day, but that doesn't mean it's always active the whole day.

You can make money trading when the market moves up, and you can even make money when the market moves down.

BUT you will have a very difficult time trying to make money when the market doesn't move at all.
And there will be times when the market is very still.

Market Hours

Before looking at the best times to trade, we must look at what a 24-hour day in the Forex world looks like.

The Forex market can be broken up into four major trading sessions: the Sydney session, the Tokyo session, the London session, and the New York session. Below are tables of the open and close times for each session:

Summer

Time Zone	EDT	GMT
Sydney Open	6:00 PM	10:00 PM
Sydney Close	3:00 AM	7:00 AM
Tokyo Open	7:00 PM	11:00 PM
Tokyo Close	4:00 AM	8:00 AM
London Open	3:00 AM	7:00 AM
London Close	12:00 PM	4:00 PM
New York Open	8:00 AM	12:00 PM
New York Close	5:00 PM	9:00 PM

Winter

Time Zone	EST	GMT
Sydney Open	4:00 PM	9:00 PM
Sydney Close	1:00 AM	6:00 AM
Tokyo Open	6:00 PM	11:00 PM
Tokyo Close	3:00 AM	8:00 AM
London Open	3:00 AM	8:00 AM
London Close	12:00 PM	5:00 PM
New York Open	8:00 AM	1:00 PM
New York Close	5:00 PM	10:00 PM

You can see that in between each session, there is a period of time where two sessions are open at the same time. From 3:00-4:00 am EDT, the Tokyo session and London session overlap, and from 8:00 am-12:00 pm EDT, the London session and the New York session overlap.

Naturally, these are the busiest times during the trading day because there is more volume when two markets are open at the same time. This makes sense because during those times there is more money transferring hands. Typically you only want to be actively placing trades in these times – you can manage trades already placed during the off hours or let your brokers software.

If you are looking at the Sydney open and thinking why it shifts two hours. You'd think that Sydney's open would only move one hour when the U.S. adjusts for standard time, but remember that when the U.S. shifts one hour back, Sydney actually moves forward by one hour (seasons are opposite in Australia). You should always remember this if you ever plan to trade during that time period.

Let's take a look at the average pip movement of the major currency pairs during each trading session.

Pair	Tokyo	London	New York
EUR/USD	76	**114**	92
GBP/USD	92	**127**	99
USD/JPY	51	**66**	59
AUD/USD	77	**83**	81
NZD/USD	62	**72**	70
USD/CAD	57	**96**	96
USD/CHF	67	**102**	83
EUR/JPY	102	**129**	107
GBP/JPY	118	**151**	132
AUD/JPY	98	**107**	103
EUR/GBP	78	**61**	47
EUR/CHF	79	**109**	84

From the table, you will see that the European session normally provides the most movement.

Tokyo Session

The opening of the Asian session at 7:00 pm EST marks the start of the Forex clock. You should take note that Tokyo session is sometimes referred to as the Asian session, because Tokyo is the financial capital of Asia.

One thing worth noting is that Japan is the third largest Forex trading center in the world.
This shouldn't be too surprising since the yen is the third most traded currency, partaking in 16.50% of all Forex transactions. Overall, about 21% of all Forex transactions take place during this session.

Below is a table of the Asian session pip ranges of the major currency pairs.

Pair	Tokyo
EUR/USD	76
GBP/USD	92
USD/JPY	51
AUD/USD	77
NZD/USD	62
USD/CAD	57
USD/CHF	67
EUR/JPY	102
GBP/JPY	118
AUD/JPY	98
EUR/GBP	78
EUR/CHF	79

Here some key characteristics that you should know about the Tokyo session:

- Action isn't only limited to Japanese shores. Tons of Forex transactions are made in other financial hot spots like Hong Kong, Singapore, and Sydney.
- The main market participants during the Tokyo session are commercial companies (exporters) and central banks. Remember, Japan's economy is heavily export dependent and, with China also being a major trade player, there are a lot of transactions taking place on a daily basis.
- Liquidity can sometimes be very thin. There will be times when trading during this period will be like fishing - you might have to wait a long, long time before getting a nibble.
- It is more likely that you will see stronger moves in Asia Pacific currency pairs like AUD/USD and NZD/USD as opposed to non-Asia Pacific pairs like GBP/USD.
- During those times of thin liquidity, most pairs may stick within a range. This provides opportunities for short day trades or potential breakout trades later in the day.

- Most of the action takes place early in the session, when more economic data is released.
- Moves in the Tokyo session could set the tone for the rest of the day. Traders in latter sessions will look at what happened during the Tokyo session to help organize and evaluate what strategies to take in other sessions.
- Typically, after big moves in the preceding New York session, you may see consolidation during the Tokyo session.

Which Pairs Should You Trade?

Since the Tokyo session is when news from Australia, New Zealand, and Japan comes out, this presents a good opportunity to trade news events. Also, there could be more movement in yen pairs as a lot of yen is changing hands as Japanese companies are conducting business.

China is also an economic super power, so whenever news comes out from China, it tends to create volatile moves. With Australia and Japan relying heavily on Chinese demand, we could see greater movement in AUD and JPY pairs when Chinese data comes in.

London Session

Just when Asian market participants are starting to close shop, their European counterparts are just beginning their day.

While there are several financial centers all around Europe, it is London that market participants keep their eyes on.

Historically, London has always been at a center of trade, thanks to its strategic location. It's no wonder that it is considered the Forex capital of the world with thousands of businessmen making transactions every single minute. About 30% of all Forex transactions happen during the London session.

Below is a table of the London session pip ranges of the major currency pairs.

Pair	London
EUR/USD	114
GBP/USD	127
USD/JPY	66
AUD/USD	83
NZD/USD	72
USD/CAD	96
USD/CHF	102
EUR/JPY	129
GBP/JPY	151
AUD/JPY	107
EUR/GBP	61
EUR/CHF	109

Here are some facts about European session:

- Because the London session crosses with the two other major trading sessions--and with London being such a key financial center--a large chunk of Forex transactions take place during this time. This leads to high liquidity and potentially lower transaction costs, i.e., lower pip spreads.
- Due to the large amount of transactions that take place, the London trading session is normally the most volatile session.
- Most trends begin during the London session, and they typically will continue until the beginning of the New York session.
- Volatility tends to die down in the middle of the session, as traders often go off to eat lunch before waiting for the New York trading period to begin.

- Trends can sometimes reverse at the end of the London session, as European traders may decide to lock in profits. PAY ATTENTION TO THIS!

Which Pairs Should You Trade?

Because of the volume of transactions that take place, there is so much liquidity during the European session that almost any pair can be traded.

Of course, it may be best to stick with the majors (EUR/USD, GBP/USD, USD/JPY, and USD/CHF), as these normally have the tightest spreads.

Also, it is these pairs that are normally directly influenced by any news reports that come out during the European session.

You can also try the yen crosses (more specifically, EUR/JPY and GBP/JPY), as these tend to be pretty volatile at this time. Because these are cross pairs, the spreads might be a little wider though.

Next up, we have the New York session, a jungle where dreams are made of. Hey, isn't that an Alicia Keys song?

New York Session

The U.S. session begins at 8:00 am EST. Just like Asia and Europe, the U.S. session has one major financial center that the markets keep their eyes on. We're talking of course, about the "City That Never Sleeps" - New York City!

Below is a table of the New York session pip ranges of the major currency pairs.

Pair	New York
EUR/USD	92
GBP/USD	99
USD/JPY	59
AUD/USD	81
NZD/USD	70
USD/CAD	96
USD/CHF	83
EUR/JPY	107
GBP/JPY	132
AUD/JPY	103
EUR/GBP	47
EUR/CHF	84

Here are some tips you should know about trading during the U.S. session:

- There is high liquidity during the morning, as it overlaps with the European session.
- Most economic reports are released near the start of the New York session. Remember, about 85% of all trades involve the dollar, so whenever big time U.S. economic data is released, it has the potential to move the markets.
- Once European markets close shop, liquidity and volatility tends to die down during the afternoon U.S. session.
- There is very little movement Friday afternoon
- Also on Fridays, there is the chance of reversals in the second half of the session, as U.S. traders close their positions ahead of the weekend, in order to limit exposure to any weekend news.

Which Pairs Should You Trade?

Take note that there will be a ton of liquidity as both the U.S. and European markets will be open at the same time. You can bet that banks and multinational companies are burning up the telephone wires. This allows you to trade virtually any pair, although it would be best if you stuck to the major and minor pairs and avoid those more exotic ones.

Also, because the U.S. dollar is on the other side of the majority of transactions, everybody will be paying attention to U.S. data that is released. Should these reports come in better or worse than expected, it could dramatically shake up the markets, as the dollar will be jumping up and down.

Session Overlaps

Liquidity is strongest when there are more people participating in the markets.

Logically, you would think that this happens during the overlap between two sessions. If you thought that way, you'd only be half right. Let's discuss some of the characteristics of the two overlap sessions to see why.

Tokyo - London Overlap

Liquidity during this session is pretty thin for a few reasons. Typically, there isn't as much movement during the Asian session so, once the afternoon hits, it's pretty much a snooze fest. With European traders just starting to get into their offices, trading can be boring as liquidity dries up.

London - New York Overlap

This is the busiest time of day, as traders from the two largest financial centers (London and New York) begin duking it out.

It is during this period where we can see some big moves, especially when news reports from the U.S. and Canada are released. The markets can also be hit by "late" news coming out of Europe.
If any trends were established during the European session, we could see the trend continue, as U.S. traders decide to jump in and establish their positions after reading up what happened earlier in the day. You should watch out though, at the end of this session, as some European traders may be closing their positions, which could lead to some choppy moves right before lunch time in the U.S.

Best Days of the Week to Trade

So now we know that the London session is the busiest out of all the other sessions, but there are also certain days in the week where all the markets tend to show more movement.

Below is a chart of average pip range for the major pairs for each day of the week:

Pair	Sunday	Monday	Tuesday	Wednesday	Thursday	Friday
EUR/USD	69	109	142	136	145	144
GBP/USD	73	149	172	152	169	179
USD/JPY	41	65	82	91	124	98
AUD/USD	58	84	114	99	115	111
NZD/USD	28	81	98	87	100	96
USD/CAD	43	93	112	106	120	125
USD/CHF	55	84	119	107	104	116
EUR/JPY	19	133	178	159	223	192
GBP/JPY	100	169	213	179	270	232
EUR/GBP	35	74	81	79	75	91
EUR/CHF	35	55	55	64	87	76

As you can see from the chart above, it would probably be best to trade during the middle of the week, since this is when the most action happens.

Fridays are usually busy until 12:00 pm EST and then the market pretty much drops dead until it closes at 5:00 pm EST.

So based on all these, we've learned when the busiest times of the market are. The busiest times are the best times to trade because they give you a higher chance of success.

Best Times to Trade:

- When two sessions are overlapping of course! These are also the times where major news events come out to potentially spark some volatility and directional movements. Make sure you bookmark the Market Hours cheat sheet to take note of the Opening and Closing times.
- The European session tends to be the busiest out of the three.
- The middle of the week typically shows the most movement, as the pip range widens for most of the major currency pairs.

Worst Times to Trade:

- Sundays - everyone is sleeping or enjoying their weekend!
- Fridays - liquidity dies down during the latter part of the U.S. session.
- Holidays - everybody is taking a break.

- Major news events - you don't want to get whipsawed!
- During Major Sporting events (Super Bowl, World Cup etc.).

How You Make Money in Forex

In the Forex market, you buy or sell currencies.

Placing a trade in the foreign exchange market is simple: the mechanics of a trade are very similar to those found in other markets (like the stock market), so if you have any experience in trading, you should be able to pick it up pretty quickly.

The object of Forex trading is to exchange one currency for another in the expectation that the price will change, so that the currency you bought will increase in value compared to the one you sold.

Example:

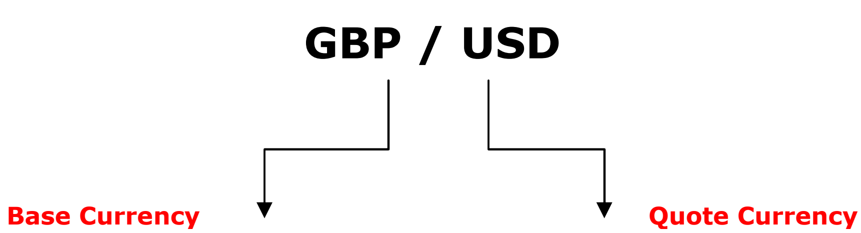
Trader's Action	**EUR**	**USD**
You purchase 10,000 Forex at the EUR/USD exchange rate of**1.1800**	+10,000	-11,800*
Two weeks later, you exchange your 10,000 Forex back into U.S. dollar at the exchange rate of **1.2500**	-10,000	+12,500**
You earn a profit of **$700**	0	+700

*EUR 10,000 x 1.18 = US $11,800
** EUR 10,000 x 1.25 = US $12,500

An exchange rate is simply the ratio of one currency valued against another currency. For example, the USD/CHF exchange rate indicates how many U.S. dollars can purchase one Swiss franc, or how many Swiss francs you need to buy one U.S. dollar.

How to Read a Forex Quote

Currencies are always quoted in pairs, such as GBP/USD or USD/JPY. The reason they are quoted in pairs is because in every foreign exchange transaction, you are simultaneously buying one currency and selling another. Here is an example of a foreign exchange rate for the British pound versus the U.S. dollar:



The first listed currency to the left of the slash ("/") is known as the **base currency** (in this example, the British pound), while the second one on the right is called the **counter or quote currency** (in this example, the U.S. dollar).

When buying, the exchange rate tells you how much you have to pay in units of the quote currency to buy one unit of the base currency. In the example above, you have to pay 1.51258 U.S. dollars to buy 1 British pound.

When selling, the exchange rate tells you how many units of the quote currency you get for selling one unit of the base currency. In the example above, you will receive 1.51258 U.S. dollars when you sell 1 British pound.

The base currency is the "basis" for the buy or the sell. If you buy EUR/USD this simply means that you are buying the base currency and simultaneously selling the quote currency. In layman's talk, "buy EUR, sell USD."

You would buy the pair if you believe the base currency will appreciate (gain value) relative to the quote currency. You would sell the pair if you think the base currency will depreciate (lose value) relative to the quote currency.

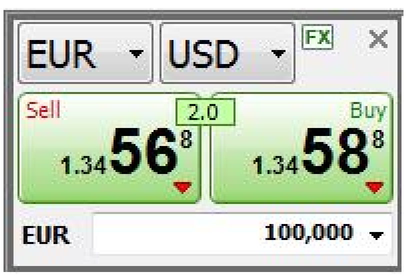
Long Positions / Short Positions

First, you should determine whether you want to buy or sell.

If you want to buy (which actually means buy the base currency and sell the quote currency), you want the base currency to rise in value and then you would sell it back at a higher price. In trader's talk, this is called "going long" or taking a "long position." Just remember: **long = buy.**

If you want to sell (which actually means sell the base currency and buy the quote currency), you want the base currency to fall in value and then you would buy it back at a lower price. This is called "going short" or taking a "short position". Just remember: **short = sell.**

Bid/Ask



All Forex quotes are quoted with two prices: the bid and ask. For the most part, the **bid** is lower than the **ask** price.

The **bid** is the price at which your broker is willing to buy the base currency in exchange for the quote currency. This means the bid is the best available price at which you (the trader) will sell to the market.

The **ask** is the price at which your broker will sell the base currency in exchange for the quote currency. This means the ask price is the best available price at which you will buy from the market. **Another word for ask is the offer price.**

The difference between the bid and the ask price is popularly known as the **spread**. The spread is the brokers fee for:

- Providing the relationship to the interbank market

- Providing your trading platform
- Lending you the money to execute the trade

On the EUR/USD quote above, the bid price is 1.34568 and the ask price is 1.34588. Look at how this broker makes it so easy for you to trade away your money.

If you want to sell EUR, you click "Sell" and you will sell Forex at 1.34568. If you want to buy EUR, you click "Buy" and you will buy Forex at 1.34588.

Margin Trading

When you go to the grocery store and want to buy an egg, you can't just buy a single egg; they come in dozens or "lots" of 12.

In Forex, it would be just as foolish to buy or sell 1 euro, so they usually come in "lots" of 1,000 units of currency (Micro), 10,000 units (Mini), or 100,000 units (Standard) depending on your broker and the type of account you have (more on "lots" later).

Margin trading is simply the term used for trading with borrowed capital. This is how you're able to open $1,250 or $50,000 positions with as little as $25 or $1,000. You can conduct relatively large transactions, very quickly and cheaply, with a small amount of initial capital.

Below is very important!

1. You believe that signals in the market are indicating that the British pound will go up against the U.S. dollar.
2. You open one standard lot (100,000 units GBP/USD), buying with the British pound at 2% margin and wait for the exchange rate to climb. When you buy one lot (100,000 units) of GBP/USD at a price of 1.50000, you are buying 100,000 pounds, which is worth US$150,000 (100,000 units of GBP * 1.50000).

   If the margin requirement was 2%, then US$3,000 would be set aside in your account to open up the trade (US$150,000 * 2%). You now control 100,000 pounds with just US$3,000.

3. Your predictions come true and you decide to sell. You close the position at 1.50500. You earn about $500.

Your Actions	**GBP**	**USD**
You buy 100,000 pounds at the exchange rate of **1.5000**	+100,000	-150,000
You blink for two seconds and the GBP/USD exchange rates rises to **1.5050** and you sell.	-100,000	+150,500
You have earned a **profit of $500**.	0	+500

When you decide to close a position, the deposit that you originally made is returned to you and a calculation of your profits or losses is done. This profit or loss is then credited to your account.

Rollover

For positions open at your broker's "cut-off time" (usually 5:00 pm EST), there is a daily rollover interest rate that a trader either pays or earns, depending on your established margin and position in the market.

If you do not want to earn or pay interest on your positions, simply make sure they are all closed before 5:00 pm EST, the established end of the market day.

Since every currency trade involves borrowing one currency to buy another, interest rollover charges are part of Forex trading. Interest is paid on the currency that is borrowed, and earned on the one that is bought.

If you are buying a currency with a higher interest rate than the one you are borrowing, then the net interest rate differential will be positive (i.e. USD/JPY) and you will earn funds as a result.

Conversely, if the interest rate differential is negative then you will have to pay.

Ask your broker or dealer about specific details regarding rollover.

Also note that many retail brokers do adjust their rollover rates based on different factors (e.g., account leverage, interbank lending rates). Please check with your broker for more information on rollover rates and crediting/debiting procedures.

Here is a chart to help you figure out the interest rate differentials of the major currencies. Accurate as of 10/4/2010.

Benchmark Interest Rates

Country	Interest Rate
United States	0.25%
Euro zone	1.00%
United Kingdom	0.50%
Japan	0.10%
Canada	1.00%
Australia	4.50%
New Zealand	3.00%
Switzerland	0.25%

Pips

You've probably heard of the terms "pips", "pipettes", and "lots" thrown around, so let's see how they are calculated.

This is important, as it is required knowledge for all Forex traders. Don't even think about trading until you are comfortable with pip values and calculating profit and loss.

What the heck is a Pip?

The unit of measurement to express the change in value between two currencies is called a "Pip". If EUR/USD moves from 1.2250 to 1.2251, that is ONE PIP. A pip is the last decimal place of a quotation, given that four decimal places are used for pairs without the Japanese yen. If a pair does include the Japanese yen, then the currency quote goes out two decimal places.

The term actually comes from dice where a dot is called a Pip. Remember, while this is anew business to you it is an old business (not the oldest HA!). Don't believe it? Who did Jesus kick out of the temple in the Bible Story? The Foreign Currency Changers!

Very Important: There are brokers that quote currency pairs beyond the standard "4 and 2" decimal places to "5 and 3" decimal places. They are quoting **FRACTIONAL PIPS**, also called pipettes. For instance, if GBP/USD moves from 1.51542 to 1.51543, it moved **ONE PIPETTE**.

As each currency has its own value, it is necessary to calculate the value of a pip for that particular currency. In the following examples, we will use quotes with 4 decimal places.

In currencies where the U.S. dollar is quoted first, the calculation would be as follows:

1. USD/CHF at 1.5250

.0001 divided by exchange rate = pip value
.0001 / 1.5250 = 0.0000655

2. USD/CAD at 1.4890

.0001 divided by exchange rate = pip value
.0001 / 1.4890 = 0.00006715

3. USD/JPY at 119.80

Notice this currency pair only goes to two decimal places (most of the other currencies have four decimal places). In this case, 1 pip would be .01.

.01 divided by exchange rate = pip value
.01 / 119.80 = 0.0000834

In the case where the U.S. dollar is not quoted first and we want to get the U.S. dollar value, we have to add one more step.

1. EUR/USD at 1.2200

.0001 divided by exchange rate = pip value
So .0001 / 1.2200 = EUR 0.00008196

BUT we need to get back to U.S. dollars so we add another calculation which is

EUR x Exchange rate
So 0.00008196 x 1.2200 = 0.00009999
When rounded up it would be 0.0001

2. GBP/USD at 1.7975

.0001 divided by exchange rate = pip value
So .0001 / 1.7975 = GBP 0.0000556

BUT we need to get back to U.S. dollars so we add another calculation which is

GBP x Exchange rate
So 0.0000556 x 1.7975 = 0.0000998
When rounded up it would be 0.0001

Nearly all Forex brokers will work all this out for you automatically, but it's always good for you to know how they work it out.

If your broker doesn't happen to do this, don't worry - you can use a Pip Calculator available on line.

Lots, Leverage, and Profit and Loss

In the past, spot Forex was traded in specific amounts called lots. The standard size for a lot is 100,000 units. There is also a mini, micro, and nano lot sizes that are 10,000, 1,000, and 100 units respectively.

Lot	Number of Units
Standard	100,000
Mini	10,000
Micro	1,000
Nano	100

As you already know, currencies are measured in pips, which is the smallest increment of that currency. To take advantage of these tiny increments, you need to trade large amounts of a particular currency in order to see any significant profit or loss.

Let's assume we will be using a 100,000 unit (standard) lot size. We will now recalculate some examples to see how it affects the pip value.

1. USD/JPY at an exchange rate of 119.80 (.01 / 119.80) x 100,000 = $8.34 per pip

2. USD/CHF at an exchange rate of 1.4555 (.0001 / 1.4555) x 100,000 = $6.87 per pip
In cases where the U.S. dollar is not quoted first, the formula is slightly different.

1. EUR/USD at an exchange rate of 1.1930 (.0001 / 1.1930) X 100,000 = 8.38 x 1.1930 = $9.99734 rounded up will be $10 per pip

2. GBP/USD at an exchange rate or 1.8040 (.0001 / 1.8040) x 100,000 = 5.54 x 1.8040 = 9.99416 rounded up will be $10 per pip.

3.

Your broker may have a different convention for calculating pip value relative to lot size but whichever way they do it, they'll be able to tell you what the pip value is for the currency you are trading is at the particular time. As the market moves, so will the pip value depending on what currency you are currently trading.

What is leverage?

You are probably wondering how a small investor like yourself can trade such large amounts of money. Think of your broker as a bank who basically fronts you $100,000 to buy currencies. All the bank asks from you is that you give it $1,000 as a good faith deposit, which he will hold for you but not necessarily keep. This is how Forex trading using leverage works.

You do the same thing when you buy a house and make payments instead of paying cash. You put a % for the sale price of the house down as a down payment, and make payments every month. You get to use the house and live in it, but the bank still owns the house until you pay it off. That is leverage. You control a $300,000 house with 5% down or $15,000.

The amount of leverage you use will depend on your broker and what you feel comfortable with.

Typically the broker will require a trade deposit, also known as "account margin" or "initial margin." Once you have deposited your money you will then be able to trade. The broker will also specify how much they require per position (lot) traded.

For example, if the allowed leverage is 100:1 (or 1% of position required), and you wanted to trade a position worth $100,000, but you only have $5,000 in your account. No problem as your broker would set aside $1,000 as down payment, or the "margin," and let you "borrow" the rest. Of course, any losses or gains will be deducted or added to the remaining cash balance in your account.

The minimum security (margin) for each lot will vary from broker to broker. In the example above, the broker required a one percent margin. This means that for every $100,000 traded, the broker wants $1,000 as a deposit on the position.

How do I calculate profit and loss?

So now that you know how to calculate pip value and leverage, let's look at how you calculate your profit or loss.

Let's buy U.S. dollars and Sell Swiss francs.

1. The rate you are quoted is 1.4525 / 1.4530. Because you are buying U.S. dollars you will be working on the "ask" price of 1.4530, or the rate at which traders are prepared to sell.
2. So you buy 1 standard lot (100,000 units) at 1.4530.
3. A few hours later, the price moves to 1.4550 and you decide to close your trade.
4. The new quote for USD/CHF is 1.4550 / 1.4555. Since you're closing your trade and you initially bought to enter the trade, you now sell in order to close the trade so you must take the "bid" price of 1.4550. The price traders are prepared to buy at.
5. The difference between 1.4530 and 1.4550 is .0020 or 20 pips.
6. Using our formula from before, we now have (.0001/1.4550) x 100,000 = $6.87 per pip x 20 pips = $137.40

Remember, when you enter or exit a trade, you are subject to the spread in the bid/offer quote. When **you buy a currency, you will use the offer or ask price** and when **you sell, you will use the bid price**.

Types of Orders

The term "order" refers to how you will enter or exit a trade. Here we discuss the different types of orders that can be placed into the foreign exchange market.

Be sure that you know which types of orders your broker accepts. Different brokers accept different types of orders.

There are some basic order types that all brokers provide.

Order Types

Market order

A market order is an order to buy or sell at the best available price.

For example, the bid price for EUR/USD is currently at 1.2140 and the ask price is at 1.2142. If you wanted to buy EUR/USD at market, then it would be sold to you at the ask price of 1.2142. You would click buy and your trading platform would instantly execute a buy order at that exact price.

If you ever online you are given a price your can buy it at. If you want the product, like and you like the current price, you click once and it's yours! The only difference is you are buying or selling one currency against another currency instead of buying a retail product.

Limit Entry Order

A limit entry is an order placed to either **buy below the market** or **sell above the market** at a certain price.

For example, EUR/USD is currently trading at 1.2050. You want to go short if the price reaches 1.2070. You can either sit in front of your monitor and wait for it to hit 1.2070 (at which point you would click a sell market order), or you can set a sell limit order at 1.2070 (then you could walk away from your computer to attend your ballroom dancing class).

If the price goes up to 1.2070, your trading platform will automatically execute a sell order at the best available price.

You use this type of entry order when you believe price will reverse upon hitting the price you specified!

Stop-Entry Order

A stop-entry order is an order placed to buy above the market or sell below the market at a certain price.

For example, GBP/USD is currently trading at 1.5050 and is heading upward. You believe that price will continue in this direction if it hits 1.5060. You can do one of the following to play this belief: sit in front of your computer and buy at market when it hits 1.5060 OR set a stop-entry order at 1.5060. You use stop-entry orders when you feel that price will move in one direction!

Stop-Loss Order

A stop-loss order is a type of order linked to a trade for the purpose of preventing additional losses if price goes against you. **REMEMBER THIS TYPE OF ORDER**. A stop-loss order remains in effect until the position is liquidated or you cancel the stop-loss order.

For example, you went long (buy) EUR/USD at 1.2230. To limit your maximum loss, you set a stop-loss order at 1.2200. This means if you were dead wrong and EUR/USD drops to 1.2200 instead of moving up, your trading platform would automatically execute a sell order at 1.2200 the best available price and close out your position for a 30-pip loss (eww!).

Stop-losses are extremely useful if you don't want to sit in front of your monitor all day worried that you will lose all your money. You can simply set a stop-loss order on any open positions so you won't miss your basket weaving class or elephant polo game.

Trailing Stop

A trailing stop is a type of stop-loss order attached to a trade that moves as price fluctuates.

Let's say that you've decided to short USD/JPY at 90.80, with a trailing stop of 20 pips. This means that originally, your stop loss is at 91.00. If price goes down and hits 90.50, your trailing stop would move down to 90.70.

Just remember though, that your stop will STAY at this price. It will not widen if price goes against you. Going back to the example, with a trailing stop of 20 pips, if USD/JPY hits 90.50, then your stop would move to 90.70. However, if price were to suddenly move up to 90.60, your stop would remain at 90.70.

Your trade will remain open as long as price does not move against you by 20 pips. Once price hits your trailing stop, a stop-loss order will be triggered and your position will be closed.

Other Types of Orders

Good 'Till Cancelled (GTC)

A GTC order remains active in the market until you decide to cancel it. Your broker will not cancel the order at any time. Therefore it's **your responsibility** to remember that you have the order scheduled.

Good for the Day (GFD)

A GFD order remains active in the market until the end of the trading day. Because foreign exchange is a 24-hour market, this usually means 5:00 pm EST since that's the time U.S. markets close, but we'd recommend you double check with your broker.

One-Cancels-the-Other (OCO)

An OCO order is a mixture of two entry and/or stop-loss orders. Two orders with price and duration variables are placed above and below the current price. When one of the orders is executed the other order is canceled.

Let's say the price of EUR/USD is 1.2040. You want to either buy at 1.2095 over the resistance level in anticipation of a breakout or initiate a selling position if the price falls below 1.1985. The understanding is that if 1.2095 is reached, your buy order will be triggered and the 1.1985 sell order will be automatically canceled.

One-Triggers-the-Other

An OTO is the opposite of the OCO, as it only puts on orders when the parent order is triggered. You set an OTO order when you want to set profit taking and stop loss levels ahead of time, even before you get in a trade.

For example, USD/CHF is currently trading at 1.2000. You believe that once it hits 1.2100, it will reverse and head downwards but only up to 1.1900. The problem is that you will be gone for an entire week because you have to join a basket weaving competition at the top of Mt. Fiji where there is no internet.

In order to catch the move while you are away, you set a sell limit at 1.2000 and at the same time, place a related buy limit at 1.1900, and just in case, place a stop-loss at 1.2100. As an OTO, both the buy limit and the stop-loss orders will only be placed if your initial sell order at 1.2000 gets triggered.

In conclusion...

The basic order types (market, limit entry, stop-entry, stop loss, and trailing stop) are usually all that most traders ever need.

Stick with the basic stuff first.

Make sure you fully understand and are comfortable with your broker's order entry system before executing a trade.

Also, always check with your broker for specific order information and to see if any rollover fees will be applied if a position is held longer than one day. Keeping your ordering rules simple is the best strategy.

DO NOT trade with real money until you have an extremely high comfort level with the trading platform you are using and its order entry system.

Demo Your Way to Success

You can open a demo accounts for FREE with most Forex brokers. These "pretend" accounts have the full capabilities of a "real" account.

But why is it free?

It's because the broker wants you to learn the ins and outs of their trading platform, and have a good time trading without risk, so you'll fall in love with them and deposit real money. The demo account allows you to learn about the Forex market and test your trading skills with ZERO risk.

YOU SHOULD TRADE ON A DEMO UNTIL YOU DEVELOP A SOLID, PROFITABLE SYSTEM BEFORE YOU EVEN THINK ABOUT PUTTING REAL MONEY ON THE LINE.

Concentrate on ONE major currency pair.

It gets far too complicated to keep track of more than one currency pair when you first start trading. Stick with one of the majors because they are the most liquid which makes their spreads cheap.

You can be a winner at currency trading but, as in all other aspects of life, it will take hard work, dedication, a little luck, a lot of common sense, and a whole lot of good judgment.

Understand The Market First

Before we go any further we are going to be 100% honest with you and tell you the following before you consider trading currencies:

1. **All Forex traders, and we mean ALL traders, LOSE money on trades.**
2. Ninety percent of traders lose money, largely due to lack of planning, training, discipline, and having poor money management rules.
3. If you hate to lose or are a super perfectionist, you'll also probably have a hard time adjusting to trading because all traders lose a trade at some point or another.
4. Don't be a Literalist – the market has lots of nuances and is NOT black and white
5. **DO NOT BECOME AN INDICATOR JUNKIE** – learn to trade and use indicators to prove what you already know about the possible currency movement.
6. **Trading Forex is not for the unemployed, those on low incomes, are knee-deep in credit card debt or who can't afford to pay their electricity bill or afford to eat.** Trade only with money you can afford to lose – should that happen.

Learn To Read Charts!

Charts are the key to understanding market movements! The better you get at reading charts the easier trading will become. Don't skimp on charts – this is your #1 tool to analyze the market. Using cheap charts with little functionality will hurt you not help you. Using charts that have little functionality is like trying to do heart surgery with kitchen knife and a magnifying glass.

Here's a chart from ProAct Traders.

You can see at a glance that you need to be selling this currency vs. buying it.

You should have at least $10,000 of trading capital (in a mini account) that you can afford to lose. Don't expect to start an account with a few hundred dollars and expect to become a millionaire.

The Forex market is one of the most popular markets for speculation, due to its enormous size, liquidity, and tendency for currencies to move in strong trends. You would think traders all over the world would make a killing, but success has been limited to very small percentage of traders.

The problem is that many traders come with the misguided hope of making a million dollars in three weeks, but in reality, they lack the discipline required for really learning the art of trading. Most people usually lack the discipline to stick to a diet or to go to the gym three times a week.

If you can't even do that, how do you think you're going to succeed one of the most difficult, but financially rewarding, endeavors known to man?

Short term trading IS NOT for amateurs, and it is rarely the path to "get rich quick". You can't make gigantic profits without taking gigantic risks. Slow and steady is the rule – plan on at least 6 months to get your feet under you.

A trading strategy that involves taking a massive degree of risk means that you can suffer form inconsistent trading performance and large losses. A trader who does this probably doesn't even have a trading strategy - unless you call gambling a trading strategy!

Forex Trading is NOT a Get-Rich-Quick Scheme

Forex trading is a LEARNED SKILL that takes TIME to learn. There is no Rocket Science in the Forex so the average person can learn to do it. The Forex is NOT COMPLICATED but it is COMPLEX.

Skilled traders can and do make money in this field. However, like any other occupation or career, success doesn't just happen overnight. Forex trading isn't a piece of cake (as some people would like you to believe).

Think about it, if it was, everyone trading would already be millionaires.

The truth is that even expert traders with years of experience still encounter periodic losses.

Drill this in your head: there are NO shortcuts to Forex trading.

It takes **EDUCATION** and lots and lots of **PRACTICE** and **EXPERIENCE** to master.

There is no substitute for hard work, deliberate practice, and diligence.

Practice trading on a **DEMO ACCOUNT** until you find a method that you know inside and out, and can comfortably execute objectively. Basically, find the way that works for you!!!

We at ProAct Traders and Forex Target Trading are dedicated to helping our traders succeed. Our Slogan says it all **"No Trader Left Behind".** We'd love to have you join us.

ProActTraders.com

ForexTargetTrading.com