

Introduction to Forex Trading



“The mark of a well-educated person is not necessarily in knowing all the answers, but in knowing where to find them.”

Douglas Everett

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What is Forex



The forex market is the world's largest financial market

Forex trading occurs from Monday morning in New Zealand until midnight Friday on the west coast of the USA

If you have traveled, you probably already have forex trading experience: when you buy the currency of your destination country while paying with your own currency, that is forex trading.

Forex traders buy and sell currencies for profit or to protect investments. An estimated USD 5 trillion is traded daily, most of it speculative.

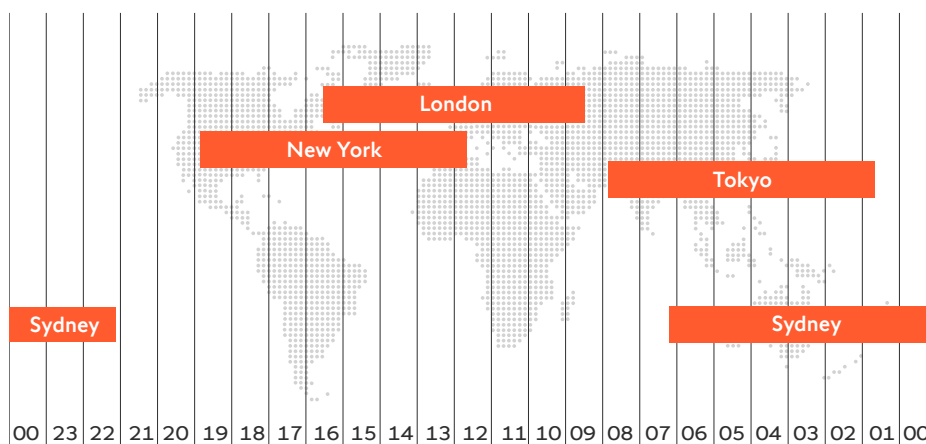
The forex market is the world's largest financial market, and since trading is between market participants, there is no "open" or "close" of market except on weekends.

In other words, forex trading occurs from Monday morning in New Zealand until midnight Friday on the west coast of the USA.

You might enjoy trading the major currency pairs, or have knowledge about the strength of an exotic currency, or a feel for commodities; some opportunities present themselves to people who keep up with news and events, while others require patient analysis. Traders bring their own strengths and preferences to their trading and, over time, create their own trading style.

Most traded currency pairs

**EUR/USD
USD/JPY
GBP/USD
USD/CHF**



What affects the Forex market

People trade forex based on expectations of the future, which are shaped by many factors.

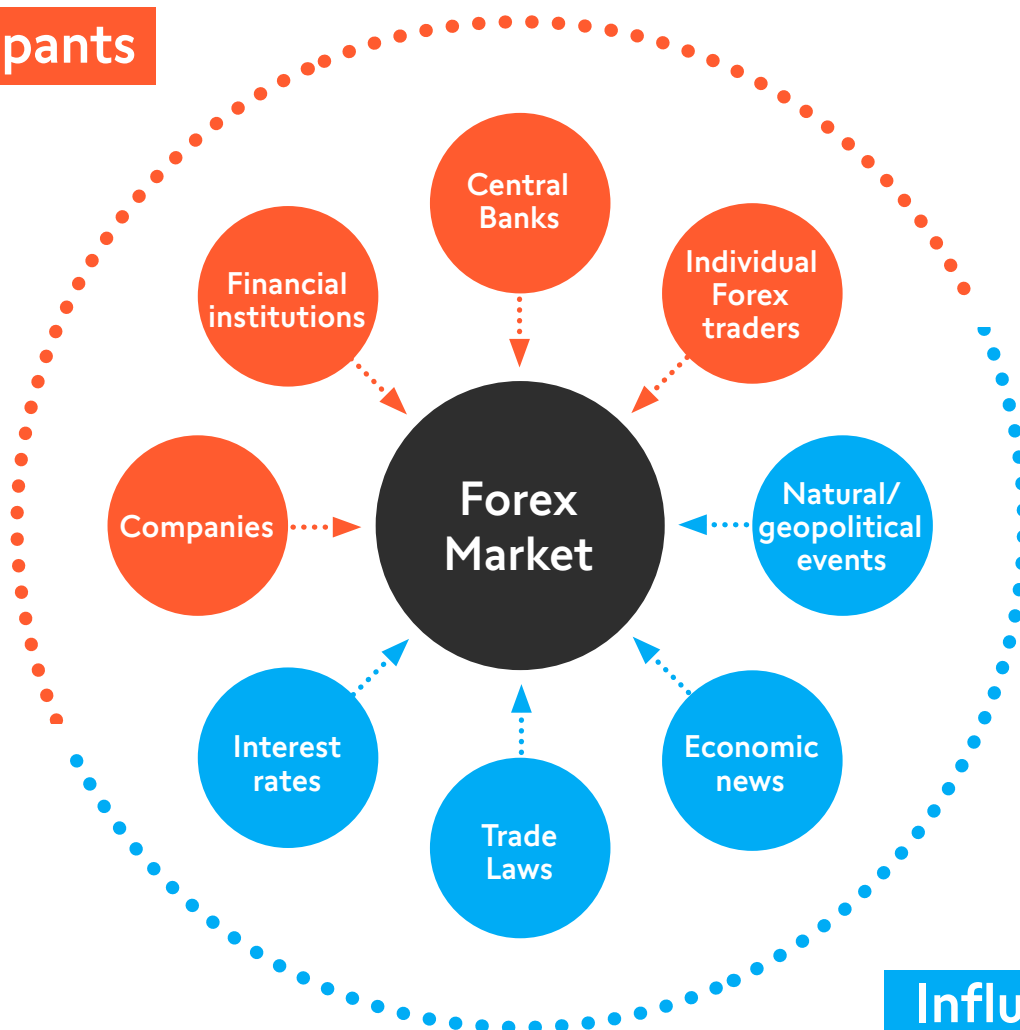
Each market participant has their goals; some are companies who are hedging currency exposure to protect their business; some are fundamental traders who focus on factors that affect the strength of whole economies; others are technical traders who look for price patterns to trigger their trades.

In addition, there are central banks, hedge funds and financial institutions who all bring different goals and interpretations to their trading.

The various market participants place different weight on information about interest rates, policy (laws), economic announcements and natural or man-made events: all affect expectations and thus market movements.

Remember that in the forex market, you can profit from down-turns as well as rising prices.

Participants



How a Forex trade works

Similar to your vacation pocket money, forex trading always involves two currencies. The base currency is the one you are buying or selling, and its price is given in the quote currency:

Base currency/**Quote currency**

EUR/**USD**

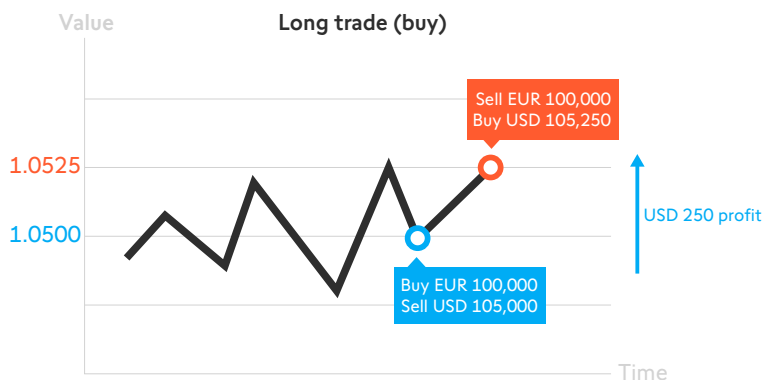
1/**1.0500**

One Euro costs 1.05 US dollars.

Imagine that you believe the EUR will rise in value relative to the USD. You buy EUR 100,000, paying USD 105,000 from your trading account (regardless of the account's denomination).

The EUR indeed rises a great deal, to 1.0525 at the end of the day. Therefore, when you close your position by selling the EUR 100,000, you receive USD 105,250, earning USD 250.

You might ask, "where did I get USD 105,000 from in the first place?" and the answer might be that you have USD 2,000 in your trading account, and your broker enables you to borrow USD 100 for each US dollars in your account. With this 100:1 margin, you can enter forex positions with values of up to USD 200,000. If you did have USD 2,000 in your account and earned USD 250, you earned 12.5% of your account value on this trade.



Margin

Also called leverage, margin is money borrowed from your Forex broker. Leveraging amplifies price changes and thus the profit or loss from a given trade. A 2% margin means that you can command positions that are 50 times greater than the funds in your account.

Lot

A lot is a unit used in trading, especially on MetraTrader MT4/MT5 platforms. At Swissquote, 1 lot is 100,000 of the base currency. In other words, in the example, 1 lot is traded.

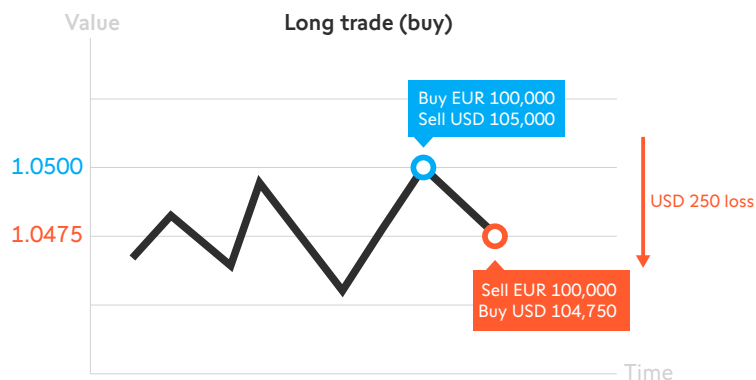
1 lot = 100,000 units of base currency

1 mini-lot = 10,000 units of base currency

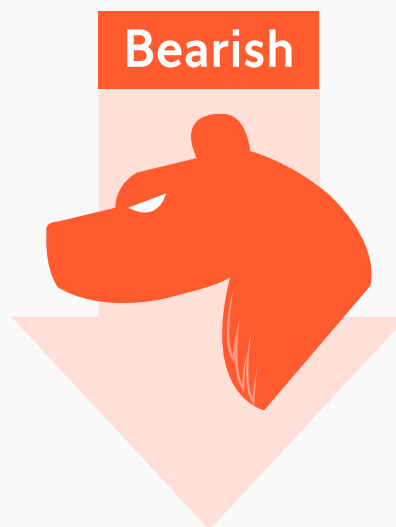
1 micro-lot = 1,000 units of base currency

It is possible to trade less than 1 lot. For example, to trade 10,000 of the base currency (called a mini lot), type 0.1 lot into the Volume field. To trade 1,000 of the base currency (called a micro lot), write 0.01 lot. The smallest enabled trade size is a micro lot. Trade sizes are given in lots on the trading platform, so keep this in mind!

Now imagine that in the example above, the Euro did not rise; indeed instead it fell to 1.0475 at the end of the day. Therefore, when you close your position by selling the EUR 100,000, you receive USD 104,750, loosing USD 250.



You think a **currency will rise**
You buy the currency
You take a **Long** position



You think a **currency will fall**
You sell the currency
You take a **Short** position

When you trade Forex, you have the choice between buying or selling a currency pair.

When you buy,
you are said to be **Bullish**

When you sell,
you are said to be **Bearish**

Trading strategies

Fundamental trading

Some traders find opportunities to trade by looking at fundamental indications of economic health. For example, supply and demand for a currency decide the price and liquidity, so traders keep an eye on the central bank's interest rates to see which way the market might move.

If a currency has a high interest rate, it might be profitable to invest for the interest alone; however, the reason for the high interest rate might be economic instability. All market participants trade based on their information and expectations.

Fundamental traders look at indicators such as employment rate, inflation and consumer sentiment as well as news about policy changes, interest rate and events. Much of this information is announced by governments according to a schedule, so it is possible to find or create "economic calendars" that will provide inspiration.

Events that move a given currency quickly enable intra-day trades, i.e. trades that are opened and closed on the same day. If your expectation is for price movement over longer time, you will hold your trading position open for longer; in general, your position is closed at 22.00 GMT and rolled over ("swapped") into a new trade opened immediately after. This new position takes into account the closing price and adds or subtracts interest.

Anything that makes an economy look stronger points at taking long positions, while weaknesses point at taking short positions.



Carry trade

If one currency has a low interest rate and the other a high interest rate, you can participate in carry trading by buying the currency with the high interest rate while selling the currency with the low interest rate. While you pay the low interest on the currency you borrowed to sell, you receive the high interest on the currency you bought.

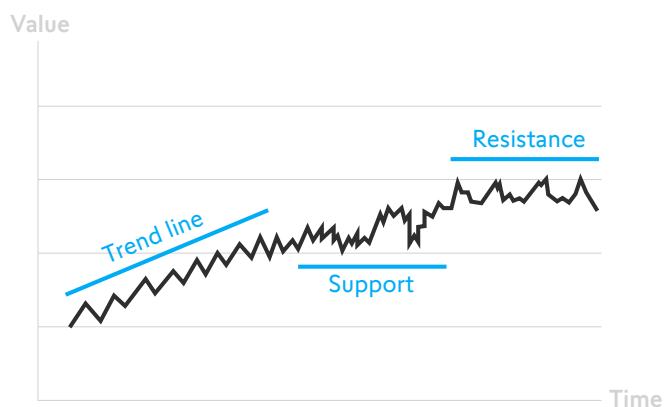
Technical trading

Most forex traders use charts to decide when to enter and exit trades, and technical traders in particular pay attention to price patterns. By looking at charts and weighing price, volume, volatility and timing, it is possible to find patterns that indicate opportunities.

For example, if the price of a currency repeatedly reaches a given value but does not rise above or fall below it, the currency is said to have found a resistance or support level. Many traders will keep an eye on past patterns and have an opinion on how far the price will move if it does break the support or resistance level.

Over time, various analyses have been developed and built into our trading platforms. Some are simple classics, others are more difficult to apply, and still others are well suited to some currencies but not others.

You can take a position at any time - any expectation you have will point to an opportunity to buy or sell.



Technical Analysis tools

Resistance:

key price level where the asset price tends to find resistance as it rises. This means the price is more likely to “bounce” off this level and fall afterwards.

Support:

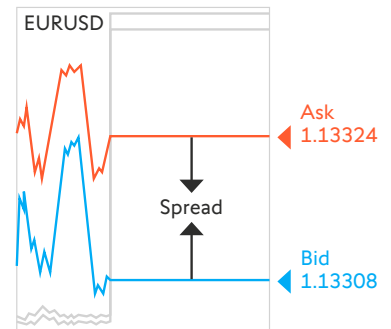
key price level where the asset price tends to find support as it falls. This means the price is more likely to “bounce” off this level and rise afterwards.

Trend line:

It is formed when a diagonal line can be drawn between a minimum of three or more price pivot points.

Trading platforms

The forex market participants create the forex market; this is called an **Over-the-Counter (OTC) market**. This is in contrast to, for example, the stock market, where all trades go through stock exchanges.



You access this market using a trading platform provided by a broker. At Swissquote, investors can trade Forex with the popular MetaTrader 4 or 5. On top, Swissquote provides spreads as narrow as 0.8 pips and offers margin as low as 0.25% on most pairs.

When you have selected your trading platform, familiarize yourself with the available spreads and tools. Swissquote provides demo versions that enable you to try everything using virtual money. Try the charts and indicators, and explore orders, which are automatic trades based on your expectations, used to open or close positions at predefined price points.

Spread

The difference between the price you can buy and sell at is the spread. The spread is the broker's fee and reflects liquidity and risk. Although many brokers apply commissions in addition to the spreads they advertise, at Swissquote, there are no other fees or commissions.

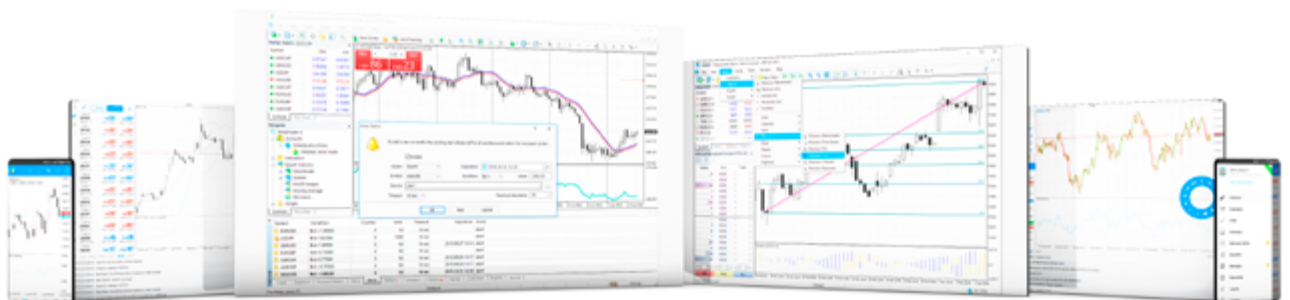
Pip

Forex price changes are given in pips. One pip is a change in the fourth decimal point (except for JPY, for which it is the second decimal point). Another way to look at it is that the pip is often the 5th digit in the quote currency regardless of decimals.

EUR/USD = 1.1275 | USD/JPY = 106.78



MetaTrader 4 & 5



How to start trading Forex

1

Go to www.swissquote.eu

2

Open a demo account.

3

You can practice Forex trading with
USD 100,000 virtual money.
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