

Personal Guide to forex trading by <http://www.theforexblogger.com>
FOREX or Foreign Exchange market kick-start in 5 simple steps

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1. The FOREX

For all of you who haven't read anything about [FOREX](#) yet, this is the ultimate answer - A short and pretty useful introduction for all you rookie investors who are seeking to dive right in that big fish-bowl called the **Foreign Exchange market**, with some tips, basic knowledge and glossary.

1a. Foreign Exchange market introduction

The **FOREX** or **Foreign Exchange market** is the largest financial market in the world, growing every day with more than \$3 milliard changing hands on a daily basic, With unlimited amount of contracts and clients, no wonder it's called "the perfect market". We all used [FOREX](#) before, if we traveled to another county and bought their currency, or ordered a book via the internet; we used the [Foreign Exchange market](#). Also large international corporations that do business in many nations find value in keeping their cash reserves in a variety of nations, and holding their funds in a variety of ways. For example, a US company may have a percentage of its working capital in US dollars, but if it does quite a bit of business in Europe it may also find it beneficial to keep a percentage of its money in European banks in Euros. There is profit to be made in investment and speculation in the currency or [FOREX](#) markets as many individual investors have discovered over the years. The [FOREX](#) is the most liquid market in the world with the ability to make instant deals without the risk of being stuck with useless products.

1b. FOREX background and history

In the beginning countries would trade with each other using the barter system. If one nation needed wool but had lumber, they would trade one product for another. This was pure trading. This type of economy has many limitations, but served mankind well for many centuries.

The **foreign currency trading** originated in 1973 and built over the ruins of the Bretton Woods agreement that used gold to back each currency (who was abandoned in 1971), what made the [FOREX](#) a free market based on supply and demand for all. In the beginning the main players were the exchange consumers such as: imports, exports, foreign companies and etc. Now days the [Foreign Exchange market](#) comprised of over 97% private investors and brokers, a fact which made it impossible for central banks, commercial banks and hedgers (large mutual fund companies that control vast amounts of money and are able to manipulate the value of a currency through speculation) to influence the market for the long term. During 2002-2003 the central bank of Japan tried to reinforce the USD against the JPY by buying USA debenture in hope to encourage the weak export sector. If they had succeeded the Japanese could have gained more sales in

the USA, but in fact the interfering last only a few hours and didn't prevent the JPY strengthening in a few days.

The major cities in which trades occur are London, New York and Tokyo. This covers a 24-hour period. When Asian trading ends, European trading begins, and when European trading ends, American trading opens and when American trading ends, it is time for Asian trading to open again, and on and on it goes.

1c. How do I trade in the **FOREX** market?

In **FOREX** you can buy and sell currencies through a broker, buying one currency is actually selling other currency. The lost or profit on **Foreign Exchange market** trading depends on the foreign currency movements. Due to the fact the **foreign currency exchange** is a ratio between two currencies; they will always come in pairs (I.e. USD/JPY EUR/USD and etc). Therefore, if we believe that the USD will grow stronger from the CAD, we'll sell our CAD in favor of retaining USD. Remember, currencies always come in pairs, there are common mistakes in the different media such as saying: "The CAD/USD ratio stands on 4.41". There are two mistakes in that saying;

1. Currency ratio will always show in 5 digits (i.e. 4.4105 instead of 4.41), Investors make most of their profit from the movements in front of the point, Each point counts from right to left, so saying that the USD/CAD ratio increase 100 points means that the ratio moved from 4.4105 to 4.4205.
2. When writing currencies pairs the base (leading) currency will always be written first to the counter/quote (weaker) currency. The CAD will always be lead by the USA so by saying the CAD/USD=4.4105 is actually saying that 1 CAD=4.4105 USD, which is wrong.

Accuracy is the keyword in **FOREX**, an average deal sums up in 2-5 seconds! So it's important to be precise when making a contract through your broker.

Currency shortcuts:

USD (U.S. dollars)
GBP (United Kingdom pounds)
JPY (Japanese yen)
CAD (Canadian dollars)
EUR (European euros)
AUD (Australian dollars)
CHF (Swiss francs)
CNY (China Yuan)
CZK (Czech koruna)
HKD (Hong Kong dollar)
HUF (Hungarian Forint)
ILS (New Israeli Shekel)
INR (Indian Rupee)
KRW (Korean Won)
MXN (Mexican Peso)
PLN (Polish Zloty)
SGD (Singapore dollar)
ZAR (South African Rand)
THB (Thai Baht)

The fact that London is the world capital of **FOREX** put the GBP in the lead, until not so long ago. Nowadays the EUR leads all the currencies. The US dollar is the most commonly traded currency, involved in almost 90% of all trades. The Euro is next with 38% of all trades, followed by the yen (20% of all trades and the pound (17% of all trades). It's important to highlight the fact that the leading currency has nothing to do with the currency ratio; it's a permanent arrangement, made by the commercial banks, that comes to ease the form of speech and simplify things for the investors and brokers.

Base currency	Counter currency
EUR	GBP,JPY,USD,ILS
GBP	ILS,JPY,USD
USD	CAD, CHF, ILS, JPY

2. FOREX trading formations

2a. Leverage

Leverage is a professional term that describes the abilities of the liquid source, Broker, Company or a bank to supply credit to his clients. Basically, leverage is the ratio between the money you deposit in your account (MARGIN) to the actual value; with this system the investor doesn't need to invest enormous amounts of money to start a contract. I.e. using \$1,000 to buy a **FOREX** lot (contract) with a \$100,000 value, this means the trade has a leverage of 100 to one. This amount of leverage allows an investor to make good profits very quickly. But always remember, with the opportunity of high profits also comes high risk.

2b. Spot Market

This is the basic **foreign currency exchange** trade arrangement for buying and selling currencies that are usually for settlement within 2 business days, also known as the value date. "Spot day" formed due to the fact that it used to take two business days to transfer currencies between two countries.

The exchange rate, which used to set the day of the currency transfer, based on the foreign exchange rate for that day and the difference between the interests for two business days. Nowadays, import and export demands for physical money is very low and most of the investors and brokers on the **FOREX** platform perform spot deals/contracts which are actually deals without any delivery which expire after two business days.

Aware to the fact that most investors are interested in holding a deal for more than two days, most broker companies use an automatic "roll-over" for a contract, with no extra charges. Therefore the investor has a chance to hold a contract more than two days and even a full year.

3. Analysis and forecasting the FOREX

3a. Analyzing the foreign exchange market

Among the traders there are two systems for trading **FOREX**, the fundamental and the technical. The fundamental system stands for trading based on both political and economic factors to help determine trades, using past economic data that affects the currency or the country where currency was traded. The technical system stands for trading based on charts and try to predict where the prices are going by analysis of historical price activity. most short-term expert traders and brokers use this system.

There is an everlasting argument between the two sides of this barricade and it always was a tricky one, which requires knowledge and combination of both systems. The fundamental analysts mainly emphasize commercial banks and hedgers meetings, employment and unemployment data, and interests and inflationary measures. On the other hand, traders who use the technical system identify support and resistance points, trends and modification.

Remember, so far neither of the systems is a proved formula, the best way is to merge the two.

3b. The fundamental approach

The fundamental approach believes that differences in value of currencies come from the daily news. Changes in gross domestic product growth, inflation, interest rates, budget and trade deficits, hedge funds markets, surpluses and other economic conditions will cause changes in currency values. For this reason investors and traders follow the news very closely. There are 24-hour cable news channels and many web sites devoted to news for currency traders. From those characteristics they analyses changes in supply and demand requests.

The government has big influence on the **FOREX** market; through their central bank the government can stand in the way of the market and interfere in a direct or indirect way in purpose to prevent their local currency from unwanted movement. Usually the government can always affect the market in the short-term.

There are 3 ways to analyze the **foreign currency exchange** through the macro economy and from each one of them you can come to a conclusion about the future of a local currency:

1. The product. The product represents the value of a year's production, the crude product to be accuracy (GDP). The GDP includes all the financials performance of the local companies in crude products terms. Any influence on those components can affect the local currency rate.

2. Payment balance. Payment balance assumes the currency rate is in equilibrium. A country that suffers from deficit may suffer from loss of balance in the currency that is in her possession and in result her local currency rate will be in a downward movement. As the local currency is lower it is increasing the attraction of exports products and raise the imports prices.

3. Interests. A raise or decrease of one currency against another one has to be neutralized by changes in the interest differences between two of them. I.e. if the interest in the USA grew higher than the interest in Japan the USD would get stronger against the JPY.

Currencies with high interest enjoy an increase in their value. In actual fact this increase comes from funds movements to the market and reinforcement of the local currency. A central bank can interfere in the financial market by raising or lowering the interest, also for matching the interest to the market and also for affecting the inflation. Therefore determining the interest is considered as one of the biggest occasions in **the foreign currency exchange market.**

3c. The Market and forecasting

The fundamental analysis is necessary for the **FOREX** dynamics and contains the reference and forecasting elements. The forecasting is created based on economic measures, data which doesn't have the ability to route the currency course.

Forecasting is the market psychology.

In the year 2000 the EUR got weaker against the USD despite the positive information in the EUR coalition, as a result of the market momentum that prefer investing in the USD due to its growth, the lack of inflation and forecasting of its interest increase in the USA.

3d. Indicators

The commercial market is influenced by numerous amounts of economic records which create together a list of indicators that influence the **FOREX**, such as:

- Producer price index (PPI)
- Consumer price index (CPI)
- Gross domestic product (GDP)
- Trade balance and current account
- Employment report
- Payrolls
- Consumer confidence
- Durable goods orders
- Retail sales

3e. The Technical approach

The technical approach is an integral part of everyday trading in **FOREX** and has more advantages from the fundamental approach. For example, in lack of economy information you can trade in a technical formation according to known limits or predictable market trends. The technical approach basically prevent the trader any emotional interfering or lack of confidence in relevant economic information, most successful traders use the technical approach.

Charles Henry Dow, the former of the “DOW JONES”, came to conclusion that the market moves in two lines, one above the market and the other underneath. The upper line is called “the resistance line” and the lower “the support line”. In technical analysis investors identify those lines and if a currency rate breaks one of those lines it’s a flashlight that it will keep moving in the same direction of the breakout and that this is the time to invest.

A trend defined as one when, in case of bullish, there are two ebb points heading up and two peak points moving up. In case of bearish, there are two peak points moving down and two ebb points moving down. When one of those points breaks its mean there is a trend movement in that direction, and it is almost always recommended to invest in favor of the trend direction.

3f. Candlesticks

Candlesticks were invented in Japan. The candles are sorted by short periods of time and characterize a few datum: Daily peak, daily low, opening point and closing point. The candlestick chart is the most useful way to measure the sentiments of other traders. Candlesticks contain the same data as a normal bar chart but emphasize the relationship between opening and closing prices. The narrow stick represents the range of prices traded during the period (high to low) while the colored part of the candle represents the gap between the opening point to the closing point in a specific time frame and is called "the body" (If the close is higher than the open - the mid-section is hollow or shaded blue/green and If the open is higher than the close - the mid-section is filled in or shaded red). The benefit in candlesticks is the ability to highlight trend weakness and reversal signals that may not be visible on a normal bar chart. While candlesticks may offer useful pointers as to short-term direction, trading by using candlestick signals alone is not wise or recommended.

3g. Relative strength index (RSI)

These bar charts measure the strength of the bullish days against the bearish days in a specific requested time frame. This measure is called oscillator and his aim is to identify the power level of a trend. The RSI don't come to flashlight you about a trend but to confirm it. When you see a breakout trend you can check the RSI to see if your forecasting is justified, the RSI goes to help the investor with his decisions. The RSI also can show deviation between itself and the market trend, what you can see as a warning sign that the trend doesn't have a momentum and it's a risk to invest and this way the RSI prevents mistakes. Investing when the market and the RSI are synchronized about a trend is wise since the chances of success are high.

3h. Fibonacci and the [FOREX](#) Market

Fibonacci was a brilliant mathematician who wrote several books. His father was Guilielmo, of the Bonacci family. His father was a diplomat; therefore Fibonacci was educated in North Africa, where he learned accounting and mathematics. He is most well known discovery was the sequence 1, 1, 2, 3, 5, 8, 13, 21, 34, 55, etc, basically it's said that each number is the sum of the two numbers before him. In the column above you can see that the ratio between the number in an upper movement aspire to 61.8%, when examine the ratio between a number in the column between a following number in jumping of one number ahead. I.e. the ratio 5 to 13 aspires to 38%, those ratios founded in the nature by Fibonacci in snails, shells, between the middle finger and the arm, patterns of leaves, grass and flowers, etc. As a result of that fact investor adopted that system. The FOREX is a liquid market and therefore in any chart, you will see many wiggles, as price advances and retraces and will often retrace in Fibonacci proportions, and advance in Fibonacci proportions, not any time and not accurate by the inch but often

and in very similar measures. Fibonacci lines are one of the most common analysis systems among investors, the system states that each trend goes through changes at some points and that the goal is to forecast when exactly these changes will take place. The Fibonacci line for the trend is stretched throughout the width of a chart and produces three possibilities for trend changes. Each level is a certain percentage from the trend sum. The three levels are 61.8%, 50% and 38.2%. On any level there are two possibilities for an uplifting breakout, and for the movement of the change or reversal back to the trend. On any Fibonacci level, if there is a reversal of the change back to the trend, we will turn to the candlestick indicator for verification. Expert traders and brokers wait for a couple of candlestick indicators before deciding to invest in a certain trend movement.

In conclusion, the technical approach allows us to trade without any emotional intervening. In search for chances like main levels breakout you can gain a lot of profit by neutralization the risk that goes with trading. There is a physiologic side because the fact that most of the market is reading charts. As many investors will look on the same chart, the movement breakout becomes more meaningful.

4. Rookie mistakes and how to avoid them

Learning anything new can lead to mistakes, but making mistakes can be a natural part of the learning process. When learning to trade or invest in [FOREX](#), mistakes can lead to lose of profits and can become expensive. A good investor will understand the market they are using for trading. Whether you are new or experienced, you can still make mistakes. There are common errors that many traders and investors make when trading on the **FOREX** market. With a little research, you can learn how to avoid common **FOREX** trader mistakes and move on.

Using too much margin when trading or investing on the [FOREX](#) market can lead to costly mistakes. Margin is the use of borrowed money to purchase securities. While it is true that using margins can help you make more money, it can also make your losses bigger. When new investors look at margins as “free cash”, they in fact have the potential to lose much more money. Margins are not free money and using them too often can end up creating more debt than profits. You would not buy stocks using a credit card, so you would not use margins to trade currency. When investors use margins when trading on the **FOREX** market, it requires the investor to have to watch their investments much more closely than when margins are not used. Margins should never be used if the investor does not have the experience or time to closely monitor their trades.

Another common, but costly mistake is when investors buy and trade on unfounded tips. This is one of the most common mistakes, even with more experienced traders. It is easy to be tempted to buy or trade currency or even stocks when you overhear someone talking about “the next big thing”. Sometimes this can be helpful, but more often than not, it will only lead to losses. Do not fall victim of investing and trading based on tips you hear or read about on television or on the Internet. If you hear about a trade that interests you, then best tip is to do some research and talk to your broker before trading or investing. You can also benefit from getting a second opinion on a **FOREX** tip before buying, selling or trading any form of currency.

Not understanding how the [foreign exchange market](#) works is yet another costly mistake that new traders and investors make. Understanding the terminology of **FOREX** is very important to new traders. There are tutorials and free demos widely available on the Internet that allows traders and investors to learn how to use the **FOREX** market to their advantage. In addition, it is wise to choose an experienced broker that can help you trade and invest. These brokers should know everything about the **FOREX** market and can help traders and investor make wise choices. Find a broker that is tied with a good financial institution and that has experience in [FOREX](#).

Also, another common mistake is when traders and investors buy or sell when the rate on currency is cheap. Sometimes this is a good move, but just because the rate is low, does not mean that it will profit the investor. Instead of choosing a currency to buy or trade, it is best to look at all of the factors that affect the exchange rate and look at the trends and history. Avoid buying or selling any currency just because the rate is low. Most of the time, there is a distinct reason why these rates are low. Research the trends of the currency and find out, which ones are the best profit makers when trading on the foreign exchange market.

Last of all, another common mistake that costs money for both new and experienced traders is that they underestimate their trading abilities. Some investors feel that they do not understand [FOREX](#) well enough to trade to their fullest ability. Anyone with willingness to learn can profit with some education and research. It can take some time to learn the aspects of the foreign exchange market, but even new investors can learn how to successfully trade.

All this goes to show that you must do your homework. Do not rush into thinking that it will all be easy. There are a lot of big boys playing this game and most of them will not lose any sleep if you lost an arm and a leg. Like any investment, do not mortgage your first born in order to get started.

5. The trader's Ten Commandments

1. Invest in a trend! Buy when the trend is bullish and sell when the trend is bearish.
2. Accumulated gain and cut losses with no hesitation.
3. Always use the "Stop-loss", even if it seems you made a mistake and the market is back up. Remember! Most of the biggest losses caused by not using the stop-loss orders.
4. Planning strategies is important for continuing gaining profit. Do not trade impulsively and emotionally - control your urges. Changes according to urges in pressure time usually will ruin your gain and the consistency of your strategy.
5. Use the advantage in leverage for more profit, but study it first and use it with caution.
6. Increase only the beneficial contracts. The "average-system" only raises your risks.
7. Use the "stop-loss" in a balanced point at first and only then to a profit point.
8. Increase the profitable position in the original position amount or less. It is time to enlarge your exposure when you are on a trend movement.
9. Close losing contracts before closing profitable contracts.
10. Take a day off... rest for a while... [FOREX](#) will be waiting for you tomorrow.

[FOREX glossary:](#)

Bid – to buy

Ask – to sell

Liquidity – financial ease of transaction, i.e. cash

Trading volume – the amount traded

Bid/ask spread (pips) – the difference between the proposed buying price and the actual selling price

OTC – over the counter

Exchange rate – the difference between currency values; for instance, a Canadian dollar is valued at .86 of a US dollar

Hedge funds – large mutual fund companies that control vast amounts of money and are able to manipulate the value of a currency through speculation

Central bank – the national bank of a nation, which usually exerts control over the value of that currency

Bullish (Trading Trend) - When price moves consistently in one direction in the market, a trend occurs. When the direction is higher

Bearish (Trading Trend) - When the direction of the price is moving lower

Trend Reversal - the direction of market prices is changing

Trading Range - The trading range is actually a sideways chart pattern. It is often used to represent a resting period before the original trend is resumed

Marginal trading - trading with a borrowed capital

Leverage - the ratio between the money you deposit in your account (**MARGIN**) to the actual value, i.e. using a \$1,000 to buy a FOREX lot (contract) with a \$100,000 value

Fundamental analysis - doesn't rely on Forex charts. It uses both political and economic factors to help determine trades

Technical analysis - try to predict where the prices are going by analysis of historical price activity

Spot Market - Market for buying and selling currencies that are usually for settlement within 2 business days, also known as the value date

Exchange Rate - When the value of one currency is expressed in the terms of another

Currency Pair - All currencies must be sold in pairs. There are two currencies that make up an exchange rate, so when one currency is bought, the other is simultaneously sold and vice versa.

Base Currency- This is the *first currency* in a pair (*EUR/USD*).

Counter Currency- This is the *second currency* used in a pair. The counter currency is also known as the “terms” currency (*EUR/USD*).

Sell Quote - This quote is normally displayed on the left side and represents the price that you can sell the base currency for. The sell quote is also referred to as the “bid” price. For instance: *EUR/USD* quotes 1.3200/03, and then you can sell one Euro for 1.3203 USD.

Buy Quote - This quote is normally displayed on the right side and represents the price that you can buy the base currency for. The buy quote is also referred to as the “ask” or “offer” price. For instance, *EUR/USD* quotes 1.3200/03, and then you can buy one Euro for 1.3203 USD

Resistance – A high point in a market chart that recurs regularly. Generally, it’s the point where the market (or currency) will begin a downturn

Support – A low point in the market chart that recurs regularly. Generally, it’s the point where the market (or currency) will begin to climb back up.

Gross domestic product (GDP) - represents the total market value of all goods and services that are normally produced within any given country

CPI - is the measure of the change in the prices of consumer goods in 200 categories

Cross rate - is used to convey the proportional values between the two currencies when it’s not across the USD. For instance, if the quote is *DEM/SFR* at .7000, this means that one German Mark can be exchanged for only .7 Swiss Francs.

Going long – investing in the **leading currency** (for example **USD/JPY** = 1.243)

Going short – investing in the **counter** currency by saying it will get stronger against the base (leading) currency **USD/JPY** (for example **USD/JPY** = 1.243)

Lot (standard lot) – \$100,000 contract value (\$10,000 margin)

Mini Lot - \$10,000 contract value (\$1,000 margin)

Pips – the smallest rise of a change in price (1/10,000 of the value), i.e. EUR/USA price changes from 1.2834 to 1.2836 the price has changed by 2 pips.

Pivot points – is a datum that analysts use as an important tool to predict low (support) and high (resistance) points of the graph. If one of those points is broken it's expected to move in the same direction (if in downward movement, then the market is bearish).

Important! - Pivot points are short-term trend; they need to be recalculated each business day separately.

Currency shortcuts:

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AUD (Australian dollars)
CHF (Swiss francs)
CNY (China Yuan)
CZK (Czech koruna)
HKD (Hong Kong dollar)
HUF (Hungarian Forint)
ILS (New Israeli Shekel)
INR (Indian Rupee)
KRW (Korean Won)
MXN (Mexican Peso)
PLN (Polish Zloty)
SGD (Singapore dollar)
ZAR (South African Rand)
THB (Thai Baht)

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