



HotForex
Honesty - Openness - Transparency

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Chapter 1

Advantages of the Forex Market

What is the Forex Market?

The Forex market is the trade arena which allows investors to trade foreign currencies throughout the trading day. This market is the largest in the world and has a daily turnover of 3 trillion USD.

The market is active 24 hours a day, 5 days a week. The value of the currencies changes every moment throughout the day according to supply and demand levels.

The Forex market is the most secure medium of investment in the world, in comparison to other channels with a risk factor, such as: stocks, options, bonds and more.

Just as in a regular market we buy and sell vegetables and in the stock market we buy and sell stocks. In the Forex market we buy and sell currencies, this is our product. There are more than 100 currency pairs in the world which can be traded.

Currency exchange rates are uniform throughout the whole world. If the exchange rate of the Euro in relation to the USD is 1.5220 in London, it will be 1.5220 in Congo, New York, Australia and Hong Kong.

The Forex market is largely composed of speculators.

Speculators are people like me, or perhaps like you, who buy and sell currencies to profit from the change in the exchange rate of a currency. Only five percent of the transactions are for real purposes of commerce such as: industry, tourism, etc. The remaining 95 percent are for speculation purposes.

This is the zero-sum game: the total gains are equal to the total losses.

What affects the Forex market?

The Forex market is affected solely by macroeconomic data, not by microeconomic data. What is macroeconomic data? Raising of the interest rate in a country, the unemployment rate of a country and political conflicts within the country. On the other hand, microeconomic data are the balance reports of a very large company in the country, a large business deal which a large company is about to execute and/or has executed, and more.

The microeconomic data does not interest the Forex market and does not affect it.

In other words, the Forex market is affected by large-scale and international events.

The Forex market is comprised of: currencies and commodities. Today, some brokers also allow trading of indices, futures contracts and certain stocks.

All the strategies and technical analyses that you will learn here are relevant for currencies as well as for commodities.

Before we learn what an exchange rate is and how we buy and sell currencies, let's understand more clearly the advantages of the Forex market based on the characteristics which I have presented so far:

The Forex market has 2 principle advantages:

The first advantage is: liquidity.

Have you ever bought a stock and couldn't sell it a specific moment?

Example: You have bought a particular stock. The stock had risen greatly in only a few months and all of a sudden the CEO resigned, at that moment there was a pause in the trade which lasted a few hours, and the next day the stock decreased by 10%.

You are stuck with the stock!

In the Forex market such a thing would never occur.

If you have Euros, Pounds, Swiss Francs or any other tradable currency, you can sell it at any point in time.

You will never get stuck with a currency, and this is a great advantage of currency trading. As traders, it doesn't matter what you buy, what important is that at any moment you can cash in your goods – there will always be a buyer.

There is one very important rule to remember: Until you cash in your goods, there is no knowing whether you have gained or lost.

The second advantage is: In the Forex market there is no control by external financial bodies.

A speculator, as great as he/she is, cannot influence the exchange rate.

Central banks intervene in the trading once every decade and are successful in effecting the value of the currency by a total of two percent, a movement of this kind lasts for only a few hours and then the exchange rate returns to its natural price.

This goes to say that currency trading is fair, and no body, as large as it may be, can affect the market.

On the other hand, in the case of stock and options, a large broker has the ability to inject tens of millions of USD and by doing so they can change the price of the stock by tens of percentage points – and unfortunately they do so from time to time. 10

What advantages do we have in a market which is influenced by macroeconomic data and not microeconomic data?



The first advantage – it is much easier to follow and trade, due to the availability and minimal amount of data.

For stocks, for example, there are many factors which must be followed.

Imagine that you own 4-5 stocks in the NYSE. Let's assume that you are serious investors, not gamblers.

You have to know who the shareholders are in every company you invest in, what the multiplier is, what the balance sheets look like, the gains and losses report, internal information, such as, for example, resignation of an executive, a large future contract, and so on and so forth. One must know so much information that following them on a daily basis would require many hours each day.

In the Forex market there are five to six significant data in a month. The firm through which you trade will provide you with these data in real time, and you, with the knowledge that you will gain, will trade accordingly.

Do you understand the significance? 5-6 pieces of significant information in a month, that's all. You won't have to live in constant chase after changes in companies in which you invest.

The second advantage – the important information reaches everyone at the same time.

Let's assume that I am the marketing manager of a large pharmaceutical company, and I am on a flight returning from China, and in my hands is a closed contract with the government of China, a contract which is expected to increase the profitability of the company by 100 billion USD a year.

Who knows about the deal? myself, the CEO, his wife and her brother. And they don't do anything with that knowledge, right? 'laughter' You made me laugh!!!

Until it is reported in the news that a huge deal took place with China, there are people who already know, who have made use of it, and the price of the stock already reflects the news. You will be in the second level of decision makers.



Haven't you ever met someone who told you that he/she bought a specific stock based on insider information and the next day it rose by 20%? Yes, yes... it happens...

In the global foreign exchange market, when the American federal reserve Governor publish a decision to increase the interest rate, the whole world knows it in the same exact second and can respond immediately – to buy or sell the USD. There is nobody who has insider information beforehand and who make use of it in an unfair manner.

Market research and analysis

The two main approaches for analyzing the movements in the Forex market are the “fundamental analysis” approach and the “technical analysis” approach.

The fundamental analysis focuses on financial and economical theories, as well as political developments, to determine the forces of supply and demand.

The technical analysis focuses on price levels and trade volumes, and from these data expectations are formed for future levels of the market.

The main difference between technical analysts and fundamental analysts is that the fundamental analysts concentrate on causes of movements in the market, whereas technical analysts concentrate on the effects of movements in the market.



Exercises

Question 1:

What is the turnover of the Foreign Exchange Market?

- A. \$100,000USD per day
- B. \$500,000,000USD per week
- C. \$3,000,000USD per day
- D. Over \$3,000,000,000,000USD per day

Question 2:

Does a liquid market constitute an advantage for a trader?

- A. Definitely, because this prevents the trader from being stuck with merchandise for which there is no supply or demand
- B. No, a liquid market does not provide any relative advantage
- C. Sometimes, depending on the hours of trade
- D. Yes, only in a time of data and notifications

Question 3:

What are the main advantages of the Foreign Exchange Market?

- A. There are no factors which can influence the market
- B. It is very easy to follow the market due to availability and the small quantity of data
- C. The information reaches everyone at the same time
- D. All of the above answers are correct

Question 4:

The Foreign Exchange Market is mainly influenced by:

- A. Large, international events
- B. Micro data
- C. Macro data
- D. Answers A and C are correct

Question 5:

What is the percentage of speculators on the Foreign Exchange Market?

- A. 10%
- B. 30%
- C. 75%
- D. 95%

Question 6:

When the Euro's rate in London is 1.2000, what is the Euro's rate in Australia?

- A. 1.3000
- B. 1.2500
- C. 1.2000
- D. All of the above answers are correct

Question 7:

How much significant data is there on the Foreign Exchange Market during the course of a month?

- A. 3
- B. 5-6
- C. 20
- D. 50

Answers:

D,A,D,D,D,C,B

*"The essence of knowledge is, having it, to apply it:
not having it, to confess your ignorance."*

Confucius



Chapter 2

Elementary concepts of the Forex Market

Currency pairs , buying and selling rates

In foreign currency trading there are always currency pairs – the base currency and the counter currency.

The base currency – it is in essence our product, it is denoted on the left side of the pair. We always buy or sell the base currency.

The counter currency – it is the means of payment and is denoted on the right side of the pair. In a transaction involving the EUR/USD I buy or sell the Euro against the USD wherein the means of my payment is the USD.

The exchange rate is the price of one unit of the base currency in terms of the counter currency. Let's take a look at the Euro against the USD: One Euro is equal to 1.5220 USD.

EUR/USD	1.5220
GBP/USD	1.4595
USD/JPY	91.19
USD/CHF	1.1458
NZD/USD	0.6788
AUD/USD	0.8400
USD/CAD	1.0385
AUD/CAD	0.8723

Spread

Spread is the difference between the buying price and selling price and is the commission which you pay, as currency traders.

***For example:** If, for instance, you want to convert USD to Euros at the bank. They will tell you that the buying price is 1.56 and that the selling price is 1.49. In other words, in order to buy one Euro you would have to pay a little more than one and a half USD. If in that very moment you would want to sell your one Euro to the bank, the bank will buy one Euro at a price slightly lower than one and a half USD, so if you sold 1000 USD to the bank you received 641 Euros. By selling the Euros back you will get only 955 USD.*

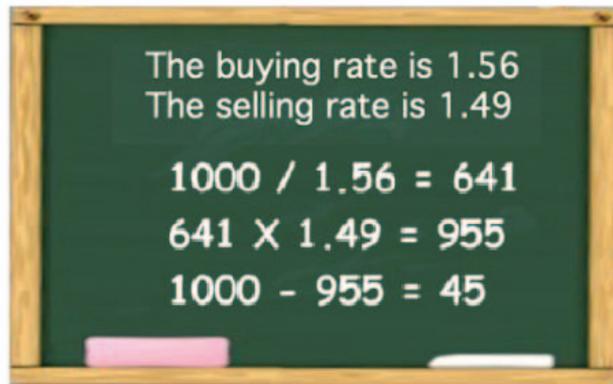
You paid 1000 USD and received 955 USD, so where are the other 45 USD?

This is the profit of the CHANGE store – this is the commission they charge from their customers.

This is the only commission that you will pay; in the Forex market there are no additional commissions.



It is implied by such that we will always lose because of the spread in the first second after the trade.



Pips

Another important concept in the Forex market is “pips” – pip (singular), pips (plural)

In the Forex market the exchange rate rises by pips and falls by pips. For most of the currencies, the pips are denoted 4 places after the decimal point.

In other words, if the EUR/USD rate is 1.5220 then the number of the pip is 0.

If the exchange rate was previously 1.5220 and now it rose by one pip, the exchange rate will be 1.5221.

If the exchange rate fell by 10 pips, it would be 1.5210 and so on.

The Japanese Yen is different: For the Japanese Yen the pip is denoted at two places after the decimal point, meaning that, if the USD/JPY is at 88.57, then the pip is equal to 0.01. If the exchange rate rises by 3 pips it would be equal to 88.60 and if it decreases by 27 pips the exchange rate would be 88.30.

Average daily fluctuation

To become acquainted with the concept, the average daily fluctuation of the EUR/USD is about 100 pips a day. On more turbulent days the fluctuation reaches 200-300 pips, on calmer days the fluctuation reaches 50-60 pips.

And in terms of percentage?

If the exchange rate is currently 1.5220 and I want to announce tomorrow that it rose by one percent, it would be represented by a rise of 152 pips.

So if we said that the daily fluctuation of the EUR/USD is about 100 pips a day, by what percent does the EUR/USD fluctuate on average? About 0.7%-0.8%. and in more turbulent periods – 2% at most.



From this we can learn of a new and important advantage that exists in the Forex market – this market is stable, and I'm referring mainly to the major currencies: Euro, USD, Pound, Yen and Swiss Franc.

This is a stable market, with exchange rate fluctuations of half a percent up to one and a half percent throughout the day. There is no possibility that you will trade a currency and lose 10%-15% in one day.

Value of pips

Let's now learn the value of every pip within the confines of a particular transaction. If the exchange rate of the EUR/USD is 1.5220 and you want to buy 100,000 Euros, how many USD do you have to pay? 152,200 USD, of course. A second passes and the exchange rate rises to 1.5221. By how many pips did the exchange rate rise? By one pip. And what is the current value of the 100,000 Euros? 152,210 USD. Which is 10 USD more.

The value of one pip in a transaction of 10,000 Euros is one USD.

In other words: In a transaction of 100,000 Euros, each pip has a value of 10 USD.

And in a transaction of one million Euros – 100 USD.

How are pips calculated?

We take the amount of the transaction that we have performed in terms of the base currency and divide by 10,000 – this is the value of one pip in terms of the counter currency.

For example: For a transaction of 100,000 Euros we divide by 10,000, and we get 10. This means that the value of every pip is \$10.

If we execute a transaction of 30,000 Euros, every pip worth is 3 USD.

For the Japanese Yen the calculation is slightly different. We divide the amount of the transaction in terms of the base currency by 100 and that is the value of the pip.

For example: A transaction of 100,000 USD in the currency pair USD/JPY, we divide by 100 and the result is 1,000 Yen. Assuming that the exchange rate is 88.00, we divide the 1,000 by 88, meaning, 11.36 USD per pip.

Example: We will take the currency pair of EUR/GBP and a transaction of 100,000 Euros, each pip is worth 100,000 divided by 10,000 and is therefore worth 10 USD. And in what currency are we paying in? In Pounds. Meaning that every pip is equal to 10 Pounds.

Size of the spreads

Do you know what the accepted ask/bid spread is for the EUR/USD exchange rate? 3 pips.

So in order to perform a transaction of 100,000 Euros, which is equal to 152,000 USD how much commission must one pay?

If every pip is equal to 10 USD in a transaction of 100,000 Euros, and the spread is 3 pips, we will pay 30 USD in commission – a onetime payment which includes the purchase and the sale.



Commissions

If to compare the commissions rate paid in the stocks market we will notice that in the Forex market the commissions rate are very low.

For example, in a 10,000 Euro trade the stock's commission is half a percent hence 50 Euro. In Forex however you will pay only 3 USD commission for a 10,000 Euro trade, for a 100,000 Euro trade you will pay only 30 USD commission and so on and so forth.

The commissions are very low compared to the stock market

Commission in foreign exchange	Commission in shares	Size of the transaction
3 Pips = \$3	0.5% = €50	€10,000
3 Pips = \$30	0.5% = €500	€100,000



Trading rules

If you trade a certain product, and you think that its price will rise, you will buy it and if its price indeed rises, you will profit when you sell it, and if you are wrong and its price goes down, you will lose.

For example, if you trade wood, and you think the wood price will rise, you buy 10 tons of wood when the wood price is 100 USD per ton. And later you sell it when the price rises to 150 USD per ton, you have profited 500 USD.

If you thought that the wood price would decrease, you would wait until the price reached 50 USD per ton, and then you would have bought the same 10 tons at only 500 USD.

The rules are:

A trader who thinks the value of his product is going to rise, buys more goods and waits for the price to rise in order to sell.

A trader who thinks that the value of a product is going to fall, rushes to sell the goods and make the most of his money.

Traders do not always have to lose everything or gain everything, the trade can be stopped in the middle, and such a situation will be expanded upon further later.

Let's translate this into terms of Forex market:

If you expect the exchange rate of a currency to rise, you will buy it.

If you expect the exchange rate of a currency to drop you will sell it.

The sum which you profit or lose depends on the volume of the transaction which you perform. The greater the transaction is, the more you can profit, but you will take on a greater risk and the smaller the transaction is, the smaller the profit will be but you will have taken on a smaller risk. Trading currencies is exactly like buying and selling wood, tomatoes or cucumbers. We buy the goods when we think the price will rise, and we sell the goods when we think the price will fall.



Transaction / Position

In order to complete a transaction we need to perform a purchase and a sale. If a purchase and a sale were not performed, then the transaction was not completed, and it doesn't matter if you are going to gain or lose in the course of the transaction.

Remember, this is an important rule: realization of the gain or loss occurs only when the transaction is complete.

Position is in essence a transaction.

Opening of the position - opening of a transaction for a currency pair.

Open position – a position which hasn't yet been closed, in other words, the transaction has not yet been completed.

Closed position – a transaction which has been completed, the actions of purchase and sale have been performed.

Leverage

What changes the whole picture, and turns the Forex market into a market of opportunities to profit a lot of money in a short span of time, is leverage.

But...of course, leverage causes trading to become more risky.

So what is leverage?

Brokers allow you to perform transactions in sums of money which are much larger than the amounts that you have in your account. Sometimes even up to 400 times more than what you have invested.

Forexample: You have deposited 1000 USD, the exchange rate of the Euro against the USD is 1.5220. And you believe that the price of the Euro is about to rise by 100 pips. That is your opinion.

You can pick up the phone and call the broker or give an order via the computer, 24 hours a day “please buy me 100,000 Euros”

Despite the fact that you have deposited 1000 USD and 100,000 Euros cost 152,000 USD, in this case you have taken advantage of a leverage of 152 times the money which you have in your account.

In a transaction of 100,000 Euros, how much is each pip worth. We learned it already, remember? 10 USD. Let's assume that the exchange rate indeed rose to 1.5320. How many pips have you earned? 100. And how much money have you earned? $100 \times 10 = 1000$ USD.

Let's deduct the commission, and the net profit from the transaction will be 970 USD.

Nearly a 100% return in one day. How great!

But... what will happen if the exchange rate falls to 1.5120?

You have lost 100 pips, you have lost all of your 1000 USD.

Should you leverage?

Later on you will learn whether it is worthwhile to leverage your transactions and by how much. But one must always remember, for whoever wants to leverage – the option is always available, but it's risky.

When there is a leverage of 300 times you can perform a transaction of 300,000 Euros as well, and if the price rose by 100 pips, you can even earn a 300% return in one day. But if the exchange rate decreases by 33 pips, you have lost your whole investment.

Why do the firms allow us to leverage?

The answer is simple: It is preferable for them that we perform a transaction of one million Euros rather than a transaction of 10,000 Euros, in this way the broker earns a commission of 300 USD and not 3 USD.

Later on you will learn what your interest is as traders, and why you shouldn't be tempted to leverage transactions.





Exercises

Question 1:

What is the meaning of the word “SPREAD”?

- A. The base exchange rate
- B. The currency exchange rate
- C. The secondary currency exchange rate
- D. The difference between the selling price and the purchase price

Question 2:

What is the average daily fluctuation of the main currencies on the Foreign Exchange Market?

- A. 10%
- B. 1%
- C. 15%
- D. 100%

Question 3:

In a EUR/USD currency pair, you purchased Euro. The deal is for €150,000. What is the value of each pip?

- A. 1.5\$
- B. 10\$
- C. 15\$
- D. 20\$

Question 4:

What is the secondary currency (or variable currency) and where is it to be found?

- A. The secondary currency is our product and it is always found on the right hand side of the currency pair
- B. The secondary currency is the method of payment and is always found on the left hand side of the currency pair
- C. The secondary currency is our product and is always found on the left hand side of the currency pair
- D. The secondary currency is the method of payment and is always found on the right hand side of the currency pair

Question 5:

At the time of the deal opening, the account will be in a state of:

- A. A positive balance of 10 pips
- B. A negative balance of 10 pips
- C. A positive balance of the spread
- D. A negative balance of the spread

Question 6:

In a EUR/USD currency pair, the currency rate is 1.2200/1.2203. You purchased €200,000. The currency rate reached 1.2250/1.2253 and you closed the position. How many pips did you make?

- A. 57.
- B. 47.
- C. 50.
- D. 53.

Question 7:

In a EUR/USD currency pair, the currency rate is 1.2200/1.2203. You purchased €200,000. The currency rate reached 1.2250/1.2253 and you closed the position. How much money did you make?

- A. 1140\$
- B. 940\$
- C. 1000\$
- D. 1060\$

Answers:

D,B,C,D,D,B,B



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