Advanced Order Types Put Forex Trading On Auto-pilot

By Soh Tiong Hum

Introducing "fire and forget orders" for busy individuals.

Sophisticated brokerages offer advanced order types in their trading platform. These orders are critical to risk management in the fast moving, 24-hour Forex market although they may also be available in some stock brokerage trading platforms. Although they are very much taken for granted by seasoned traders, individuals who have just encountered them can be at a loss.

This article will discuss commonly encountered advanced orders, and subsequently, teach traders how to use them to power up their trading.

MARKET ORDER

The market order is one that most if not all of us are familiar with. When we enter to buy or sell a position at the best available current price, we are in fact entering at market order. It is the opposite of the limit order which we will cover shortly.

Market orders are executed manually.

LIMIT ORDER

A limit order is an order placed to buy or sell a position at a specific price or better. It is very much like an automated queue and has a fire-and-forget nature. That means the trader can log off the system and move on to other tasks while the order stays active.

Limit orders are used when traders want to buy or sell a position at a desired price but do not have the luxury to wait. He or she trader may have to wait for some time for the price level to be reached. For the 24-hour forex market, desired price levels may be reached only during sleeping hours. For traders who have a full time career, those hours could also mean working hours in the daytime.

The limit order can be used to open a new position or exit an existing position. A buy limit creates a new long position or closes an existing short position. A sell limit creates a new short position or closes an existing long position.

Limit orders work in conjunction with time limits. This mean that limit orders can be set with an effective duration. After the effective duration has lapsed, the order will be cancelled by the system automatically. In contrast, limit orders can also be good-till-canceled or GTC. Traders must log into the system and cancel the order manually.

For a busy trader who does not have the luxury to watch the market constantly, an open position poses risk. It is especially so with leveraged instruments such as forex futures and commodities. The stop order can be utilized to cap the maximum loss.

STOP ORDER

The stop order or stop-loss order is associated with an open position. For a busy trader who does not have the luxury to watch the market constantly, an open position poses risk. It is especially so with leveraged instruments such as forex futures and commodities. The stop order can be utilized to cap the maximum loss.

The order can be placed at a desired distance from the price where the position was opened. This distance represents the maximum loss that the trader is willing to tolerate.

For example, trader John went long on the USDJPY at 96.50. He is willing to tolerate a maximum loss of 50 pips. Therefore, he enters a stop order of 96.00 and logs off the system. No matter how high USDJPY goes, John's long position will be closed when it falls to 96.00.

Traders might also encounter two other terms, hard stop and trailing stop. The hard stop is placed at a fixed level and good-till-canceled. In the above example, John's stop is a hard stop. John might also employ a trailing stop. The trailing stop is designed to follow the open position from a distance. Therefore it can be used to protect partial profits automatically if a position is expected to move dramatically.

We can understand the trailing stop if we look at the following sequence of events as an illustration:

1. John buys USDJPY at 96.50
2. He decides not to place a target price
3. So John places a 50-pip trailing stop; the stop starts at 96.00
4. When John is away, the USDJPY visits a high of 97.45 but starts to fluctuate
5. The trailing stop follows 50 pips behind the highest price to 96.95
6. USDJPY's fluctuations bring it temporarily to a low of 97.25 but the stop is not triggered; the position remains open
7. Another development in the market sets USDJPY rally to a new of 97.70
8. The trailing stop moves to 97.20 or 50 pips behind
9. John's luck runs out when USDJPY hits 97.20 and activates the trailing stop; his long position is closed
10. Between John's opening price of 96.50 and the highest level of 97.70, USDJPY move a maximum 120 pips
11. Using the trailing stop cleverly, John was able to use the system to capture 70 pips all the time while he was away

ONE-CANCEL-OTHER

The last advanced order to visit is the one-cancel-other or OCO. This is a typical combination of the limit and stop orders to carry out fully or partially automated open and closing of positions.

A. John places a limit order to sell the EURUSD at 1.4000
B. He has a stop order of 50 pips on top of the sell at 1.4050 and a limit order to take profit 100 pips away at 1.3900
C. The stop order and the take profit limit order at 1.3900 does not activate if the first order to open the sell position is not triggered
D. When the limit to sell the EURUSD at 1.4000 is triggered, the other two orders come into action
E. If EURUSD hits 1.3900 first, the system takes profit automatically for John and the trailing stop is also cancelled
F. If EURUSD hits 1.4050 first, the system takes loss automatically for John and his take profit is cancelled

TRADING FOR A LIVING FOR THE BUSY INDIVIDUAL

Many aspiring individuals share with me their vision of trading for a living. What's common is the passion to be accountable for one's self and the willingness to put in long hours. It doesn't mean that professional traders like to sit in front of their trading screens all the time. That's bad for your health and utterly unnecessary. Why not trade while you maintain your career or take care of your family or even be out socializing or taking a holiday. A clever way to do all of that at the same time is to make use of all that technology and functionality that brokerages put into our hands. The advanced order types that I presented here are the more common ones. There are plenty more. I hope I have opened the door so that you can carry on your own discovery. ■

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