New Markets, New Opportunities in Forex Trading

By Soh Tiong Hum

What was mostly the realm of large financial institutions and institutional traders is now accessible to retail traders through the various online trading platforms.

Do you have limited time to trade stocks in the day? Do you face a disadvantage at making money in a bear market? Do you feel that you face excessive risk when you hold your stock portfolio overnight? If the answer is a resounding yes to all of the questions above, then you will have your concerns and questions answered in the foreign exchange (Forex) market.

In the past, foreign exchange trading was largely limited to hedge funds, managers of large amounts of capital, major corporations and international investors. This was due to barriers from capital requirements, regulations and technology. Today, this market is equally accessible to retail traders because many firms provide leveraged trading as well as free trading platforms, charts and real-time news.

WHAT IS FOREX?

Most investors or traders will be familiar with the stock market. The Currency Market is now gaining more recognition as more traders are starting to look for an alternative to the equities. The Currency Market is also called the Foreign Exchange, or “Forex”, or “FX”. It is considered the largest financial market in the world. Moreover, it is a component of trade between nations. Participants in this market include governments, central banks, large banks and financial institutions, companies, currency speculators.

Transactions involve a party purchasing a currency while paying with another. This market exists because countries around the world use different currencies which need to be converted for the purpose of buying goods and services. If you cannot imagine what it is like, consider that when you want to visit a country such as the United States for holiday, you are going to spend the US Dollar (USD) while shopping for local products and paying for services. Therefore you need to first acquire some USD. By visiting the money changer, your action of purchasing the USD means that you have to give up your Singapore Dollar (SGD). Doing so, you have sold the SGD concurrently.

When you exchange money, you will encounter the exchange rate, which is really the ratio of how much one currency such as the USD can change for another like the SGD. Exchange rates between currencies fluctuate moment to moment. Therefore there exist currency traders who do not buy currencies for the purpose of buying goods and services. Instead traders make profits by capturing price differences created by the exchange rate fluctuations. With the Internet, retail forex traders participate in this activity by opening and closing positions through forex trading brokerages.

The forex market has the following features:

- Trades 24 hours a day and 5 days a week – A trader will have the opportunity to take advantage of the different market conditions at any time.
- It is the largest and most liquid market – this translates into greater flexibility for the trader to enter and exit the market during any market condition, with almost no daily trading limit.
- Daily average volume was last reported to be US$ 4 trillion in April 2007 by the Bank of International Settlement.
- Market moving factors that affect the currency market are macro-economic matters and global affairs, government policies.
- No central exchange unlike stocks. The forex market consists of a global network of dealers that trade with clients through electronic networks. It is usually referred to as an over the counter or OTC market.

ATTRACTIVE PLAYING FIELD

Retail traders who trade currencies actively find it attractive over stocks trading:

- Round the clock trading means that traders can find opportunities to trade breaking news or square losing positions on a real-time basis even when the local stock market might be closed for the day.
- The 24-hour nature also means that anyone can find a trading period to suit his or her lifestyle.
- Plenty of resources available in terms of free news, analysis and charting tools.
- Trading cost is low because there is no exchange or clearing house in the FX market. As a result, commissions and clearing fees are eliminated from transaction costs.
- Scale-able trading sizes that fit beginners and professional alike.

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- Long and short positions can be taken with equal ease unlike the stock market where there are often limitations to short-selling.
- Leveraged trading accounts and ample daily fluctuation mean that traders can make money within short period of time spanning mere minutes to hours.
- The size of the market and diversity of players means that there is a level playing field; no player can have complete and sustained intervention in the market.

All of the above are salient reasons for forex traders. Day traders and speculators do not like the buy-and-hold approach to making money. Each position carried overnight carries substantial event risk. A 'buy-and-sell quickly' approach on the other hand must offer plenty of market movement yet low cost of transaction because traders place a lot more buy and sell orders than investors. Forex trading offers traders such benefits.

In addition, one of the biggest deterrents to trading in stocks is the 'long' bias. There are usually limitations and even penalties to short selling which means that in bear markets, traders lose money-making opportunities. During bear markets, bearish speculators ask: if we can have irrational speculative buying, why can't we have irrational speculative selling? In forex trading, such concerns do not exist.

The most attractive reason that most traders who have encountered forex trading for the first time is the scale-able exposure. In forex trading, traders keep score by counting the number of pips they have won. A pip is the smallest unit of price for any currency. Forex trading brokerages offer the choice of contract sizes that suit the trader to such an extent that the value of one pip can range from ten cents (in a micro contract) to ten dollars in a standard contract. Amateurs can trade the micro contract in the beginning and have the option to up-size when they become proficient. There is no higher limit on the amount that a professional can trade.

ANYONE CAN TRADE FOREX

If you have experience trading the stock market, it is frustrating in this bear market (long positions don't make money and obstacles make short-selling difficult). You won't face this in the forex market.

To start forex trading, do the following:

- Understand the market by doing some reading. Visit http://www.babypips.com which is a good beginner's guide to forex trading.
- Get a demo trading account that allows you to trade with virtual money from local forex brokerages. Most of the brokerages which offer CFD trading are likely to offer forex trading.
- Most professional forex traders either speculate the outcome of economic news announcements or apply technical analysis. Websites such as http://www.forexstreet.com or http://www.forexfactory.com provide the time of news announcements. Make sure you understand how each piece of news such as interest rate decision or Consumer Price Index announcement can affect currency exchange.
- Personally I find technical analysis most compelling in the forex market. Forex rates often come within two to three pips of technical studies such as Fibonacci retracements or simple trend lines. That is really a precision of less than 0.1% deviation. Google up good courses on 'practical technical analysis in Singapore' to find a good local provider.

Think new market, think new opportunities.

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