Forex Trading London

EDUCATING TRADERS

# Top 10 Forex Trading Essentials

By

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# The Top 10

# Forex Trading Essentials That You Need to Master

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**Educating and Coaching Traders**

**Building Strong Foundations**


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# The Top 10 Forex Trading Essentials That You Need To Master

This assumes that you already know how to use your chosen Trading Platform such as MT4/MT5, or similar, to enter and exit trades and use some of its' tools. When learning '**How to Trade Forex'**, there are certain key things you need to master in order to progress, try and think of them as the Foundation stones of your Trading skills. They are:

## 1. Risk & Money Management

Professional, Proprietary and experienced Retail Traders employ robust Risk and Money Management, where they only risk a small percentage of their trading capital on any one trade, normally 1% OR LESS. They may have several positions open in any one trade too, but they will still stick to that 1% rule. This means that they are employing a Stop Loss too, to tell them when they are wrong in terms of their chosen market direction and/or their entry timing. Essentially robust Risk & Money Management should ensure longevity as a trader. Position size should vary from trade to trade, as it is a function of the amount of trading capital available, the chosen Risk % and the trade specific Stop Loss Size. It is also worthy of note that any money used for trading and investing should be 'Risk Capital', meaning that it is separate and additional to any savings and money required to maintain your standard of living (overheads!). If you never break this rule and have a good Risk:Reward ratio on your trades (1:2 or better), then you can have more losing than winning trades and still make money.

## 2. Supply & Demand – LOOK LEFT

The markets actually move because of Buy and Sell orders being fulfilled. If there are more Buy than Sell orders in terms of monetary value then the market will rise, so there will be Demand outstripping Supply, and vice versa for more Sell than Buy orders, then the market will fall and Supply will outstrip Demand. Where price falls sharply away from a level and hasn't retested it yet, that normally forms a level or zone where price might get rejected in the future – almost like Market Memory. Similarly, where price has moved up strongly from a level that has yet to be retested, that level or zone is known as a Demand level or zone.

Before crossing the road in countries that drive on the right-hand side of the road, pedestrians LOOK LEFT, then Right and then LEFT AGAIN, in order to stay safe. By LOOKING LEFT on your charts you can identify such Supply and Demand zones/levels and the project them across to the Hard Right Edge (where time is now). Such levels can be traded to and away from if you know


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what you are doing and have a strategy that allows that. So when trading LOOK LEFT and Stay Safe!

Within this topic, is also included Resistance and Support. Supply can be thought of as Resistance and Demand as Support. However, there is a subtle difference in that horizontal levels of Support, when broken become Resistance and horizontal levels of Resistance, when broken, become Support. When broken, these identifiable levels Flip to the opposite of what they were before that break. This is why and how price can seem to move up and down, over time, like a rising or falling staircase.

Additionally, Trend Lines link together the candle wick tops or bottoms and can represent diagonal Support or Resistance.

Lastly, key Moving Averages such as the 200 Simple Moving Average can act as Dynamic Support and Resistance.

Summing up though, Horizontal Supply and Demand (Resistance and Support) Rule over the rest!

## 3. Price Action (Inc. Japanese Candlestick Patterns)

The price movement of any financial instrument can be mapped over time using either a continuous line, a bar or a candlestick. The bar or candlestick also represents a particular period of time such as 1hr or 15mins. When these bars or candlesticks are plotted covering a certain time window, such as a day, a week, a month or more, they represent the historic movement or **PRICE ACTION** of that financial instrument.

Candlesticks were created to help Japanese traders make sense of price action in the Rice Markets several hundred years ago. A candlestick shows the open, high, low and close price of a particular time period such as 1hr. There are certain Japanese Candlestick patterns that can be predictive of future price direction. They have such names as a Doji, Hammer, Shooting Star, Pin-bar, Hanging Man, Evening Star, Morning Star, Spinning Top, Engulfing, Piercing etc, plus lots more. When trading away from Supply or Demand (Resistance and Support) you can look for what I call ‘Rejection’ candlesticks, these are ones that show that price has been rejected at these levels.

When considering if a currency pair is trending, we can look at the consecutive highs and lows to see if they are both rising or falling in levels over time. For an uptrend you would expect to see consecutive Higher Highs and Higher Lows. Similarly, for a downtrend you would look for consecutive


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Lower Highs and Lower lows. You can also ask yourself the following to help you focus in on the price action for clues:

> 'What has price done, what is price doing now, what could price do next and do I want to get involved?'

If price is not trending then it may be consolidating/moving sideways in a range or creating what are known as Common Patterns, such as a Head and Shoulders, a Flag or a Triangle.

Additonally, when you become experienced at looking and reading price action, it can be helpful to know that the market moves in waves. These waves can be Impulsive or Corrective in nature. An impulsive wave normal consists of 5 sub-waves but can be more and this is normally followed by a Corrective wave which normally consists of 3 sub-waves. The combination of both these wave types is known as an Elliott Wave. Identifying and reading Elliott waves can be subjective but being able to count such Wave Forms can help enormously in trying to predict where the market might be going next. In fact, an Elliott Wave is a form of Common Pattern.

## 4. Common Patterns

There are many Common Patterns which occur in most financial markets, such examples are: Flags, Pennants / Triangles, Rising and Falling Wedges, Head and Shoulders, 123s, ABCD moves, Elliott Waves, 3 Drives, Ms and Ws a.k.a. Harmonic Price Patterns various, and many more. It can be really useful to recognise such patterns as and when they occur, as they can be predictive in terms of market direction and how far price might move.

Common Patterns actually occur quite frequently inside Elliott Waves at various point of the price movement cycle. The first thing to do is to study what these common patterns look like and how to highlight their shapes on the charts and also to train the brain to see them amongst the price action. Most common patterns have associated strategies to be able to trade them. We teach a variety of these in our Forex Foundation Course and in our One to One Personal Coaching and Mentorship Programme.

## 5. Multi-Timeframe Analysis (MTFA)

Mult-Timeframe Analysis or MTFA is a term used by traders to describe a methodology of looking at their charts in a systematic Top Down or Bottom Up approach, in terms of time frames. When conducting Technical Analysis, it can really help if you start by first looking at the Monthly chart of a currency pair and noting what you see. Are there any key levels of Supply or Demand


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that have yet to be retested? Are there any key support or resistance levels of note? Are there any key or significant Support or Resistance Trend Lines that could be drawn? Is price trending up or down? Or is price consolidating in a range? Are there any common patterns forming or fully formed that should be highlighted? Are there any key Fibonacci levels that need to be noted, also where could price may go next or might turn at or where has price been rejected? Once you have exhausted your ideas on a Monthly chart, then next go to the Weekly Chart and repeat the process, then the Daily chart, then 4-hour and even the 1-hour chart. Note what you see for each time frame. Ask yourself, are there any Confluences taking place across multiple timeframes, as these can be market sweet spots, where price can turn. A confluence is where several things may be occurring on different time frame charts but at the same point in time and space. Also if you see a potential trade set up, say on the 4-hour chart, you should have enough information to nail its' Context in terms of the next few higher time frames as that can effect target expectations and whether you may wish to take a counter-trend trade or not and so on. When I have become a bit lazy and not undertaken my regular MTFA, these have been the times when I have not traded well. Get MTFA into your Monthly/Weekly and Daily routines. At the very worst before taking any trade look at least two timeframes up and one or possibly two timeframes down. By looking up, you should have a better idea of context and by looking down you may decide to wait for a better and tighter entry.

## 6. Fibonacci and Other Tools

The mathematical series devised/discovered by Leonardo Fibonacci is ever present in the shapes formed in the natural world and also when applied to the financial markets. The question of why can be debated at length, however, price repeatedly respects key Fib levels as it moves up and down in waves. To find such levels we can use Fib tools freely available in most decent trading platforms, including MT4 and 5. I recommend you become proficient in the use of the Fib Retracement and Projection tool, plus Fib Fans and Fib Expansions. Additionally, I would also highly recommend that you start learning how to use the Andrews Pitchfork. We teach all this in our Forex Foundation Course.

## 7. Correlations

Within the financial markets there are quite a few financial instruments and currency pairs that are either fully positively correlated or oppositely/negatively correlated and some a partially correlated. If you are trading a currency pair that you know is correlated to something else then wouldn't it be a good idea to check that too to see if it either is or isn't in


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tandem with your chosen currency pair. For example, the EURGBP is oppositely correlated to the GBPCHF. The major currency pairs that are quoted in USD are partially correlated to the USD Index because the USD makes up half the equation, so before trading something like the EURUSD, GBPUSD or AUDUSD or even the USDCHF then it might be a good idea to check the USD Index. The USDCAD is oppositely correlated to the Oil and the positively correlated to the USD Index. The JPY quoted pairs tend to move in the same direction as the major Indices. This is due to how money flows and we'll cover that in the next but one section.

## 8. News Flow & Economic Calendar

Before you cross the road, you look left as previously covered, so you don't walk out in front of a car, bus or lorry! When trading we also need to be aware of the up and coming expected economic news flow. There are certain events that we need to be risk averse to, such as Non-Farm Payroll (NFP) which occurs on the 1st Friday of every month except when the 1st is a Friday and then it will be the following Friday or if a Bank or National Holiday it may occur on the 1st Thursday of the month. Other key news events to be particularly aware of are the US Federal Reserve Interest Rate Decision day made by the Federal Open Monetary Policy Committee (FOMC), other major Central Bank Interest Rate decision days and so on. During such news events, particularly when the figures are different from that expected, we can see some strong market moves and you don't want to be on the opposite side of those. So, check the Economic News Calendar as part of your Trading Preps and don't get run over by a bus! If you are already in a trade that is protected by a better than or Break even stop then sometimes these events can work in your favour, but always be risk savvy and stay safe!

## 9. The Markets, Money Flow – Risk On & Off

Having an understanding of how the financial markets work and how money flows in these markets can help a currency trader. The following is **my** view and understanding of how things work, whether correct or not, it has helped my trading, to view the markets in this way. Firstly, behind every financial instrument is a Market Maker who is responsible for the management of all the Buy and Sell orders and in effect 'makes' the market. This is a business and therefore a Market Maker needs to be profitable, they have client orders to fill at pre-determined prices and also have the ability to move the markets to some extent. They will know where the obvious stop losses are being placed and may take advantage of them in order to fill their orders and make their own book. It is not personal when your stops get hit, it is the Market Makers running their business to best effect and do it to fill orders. So, if you


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are trying to catch a market turn be wary of spikes and whipsaw movements and try an let the Market Makers show their hand first and then join the party. The Hand over period between trading sessions can see Spreads increase up and own and the first hour or so of when markets open in London and New York can see previous highs and lows taken out before the trend or the move of the day takes place. Such moves are there to outsmart the novice or weaker traders and thus orders can be filled. If you can recognise when and how such moves occur, you can learn to jump on the coat tails of the big money and then you are likely to be part of a profitable move. More on this in the next section when we discuss timing.

Most brokers now have straight through dealing, where you place your trade and the broker sends that order or a bunch of those orders straight through to the Market Maker without any interference. The Broker makes it's money from the spread it adds to the Market Makers spread. Additionally, some Brokers run an A and B book. Its' consistently profitable clients will be in one grouping or book and its' consistently losing or loss-making clients will be in the other group or book. This then allows the broker to trade against the loss-making group and make additional profits.
The Forex markets are mostly speculative and a lot of times when economic news comes out as expected, it is already priced in. Now you understand the mechanics a bit more, let's consider how the money flows around the world.

When things get Risky, money tends to flow form riskier assets such as stock and shares into what are called 'safe havens', such as Gold (XAU), the Swiss Franc (CHF), the Japanese Yen (JPY) and more lately the US Dollar (USD). Note that currently the USD is what is known as the Reserve Currency of the world. So, when Indices are rising then such safe havens can weaken as the money moves from them to buy riskier investments. Similarly, when the Indices are falling then the safe havens can benefit. The JPY quoted currency pairs such as the EURJPY, GBPJPY and AUDJPY can strengthen or weaken depending upon whether there is RISK ON or RISK OFF that day, week etc. A JPY quoted currency pair can thus be a proxy for Risk On/Off. So before trading such a currency pair look to see what the major indices are doing (Correlations!).

There are other aspects to this topic but what is described above should suffice for now and provide plenty of food for thought.

## 10. <u>The Best Times To Trade</u>

We have already touched on timing so let's expand that further. The greatest volumes of orders and thus money flow occurs during the overlaps of the


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Major trading sessions, Asia and London and London and New York. Consequently the biggest moves are also likely during these times, so if you are an intra-day trader then these overlaps times are probably the best times for you to trade whilst being aware of the likelihood of Market Maker tactics particularly during the 1st hour or so of the London and New York opens. Such moves can start up to an hour before London or New York opens too. As a predominant Swing Trader, it can be best to wait until these Market opening moves have been completed before considering entering the markets.

Experience has taught me that Mondays can be a day of false signals and it is often better to wait for things to become clearer. In the run up to such events as NFP and FOMC the markets can tighten up and so it can be better to wait until after these have occurred, if you are not trading the News. You can experience extreme whipsaws during such events and you don't want to be over exposed to these as holding a trade can be extremely difficult. Better to wait for the dust to settle and more clarity to return. Often the best trade is NO TRADE at all.

Sometimes you can get an unexpected move on currency pairs as time nears 4pm UK time, which is the time when the next day's currency exchange rate for many businesses and banks is Fixed, so just be aware of that. Plus, you can get some unexpected moves on certain days when Forex Options expire.

Try not to open trades going into the weekend say after 3 or 4pm on a Friday. I will however, hold Swing trades that are already in the money and generally at Break Even or better. You can get Sunday opening gaps in the currency markets, so you need to be aware of that in terms of managing your risk.

Lastly in this section, getting your entry timing right is also a challenge when trading. Often by exercising Patience and Discipline in bucket loads you can get better entries, particularly if you can stop yourself being seduced by certain price action and wait for your trade entry to be confirmed, either by a close of candle beyond a certain level or a break out followed by a decent pullback for what I call a 'Goodbye Kiss'. By entering trades on pullbacks, we can better manage our risk.

- **Summary**
  So now you have an idea of 10 essential areas or topics that you can work on as you build the foundations of your trading skillset. There is more to trading the currency (Forex) and other financial markets, but without having mastered the above you are unlikely to be able to progress in your development. Most novice traders will focus in on trying to find strategies to use, and whilst they are needed, the more you learn about trading, the less important they become, as they are just the market entry reason. Planning and exiting are just as if not more


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important, as is getting to grips with what goes on inside your head as a trader, namely Trading Psychology or Mindset. However, you probably can't attempt to tackle your Trading Mindset successfully without first having the foundations in place and have a methodology for trading the markets. Once you have those addressed then you can go to work on your head! One last Top Trading Tip is '**to always expect the unexpected!**'. If you can do 'What Ifs' and ask yourself 'What's Next' when planning trades then that should help you, when such unexpected moves take place. After all, trading is all about managing uncertainty when trading the 'Hard Right Edge' of the charts.

If you would like to know more about our next Forex Trading Foundation Course (starts in January 2021) then just send an email to:

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If you want to know more about our One to One Personal Coaching and Mentorship Programme then just go here:

Personal Coaching and Mentorship Programme

Thanks for taking the time to digest the above and I hope it has helped in some way on your trading development journey.

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