The Forex Basics

Contents

In the following PDF we are going run through everything FOREX, we are going to look at the very basics to help you gain more of an understanding of what the foreign exchange market actually is, how it works and how professional traders benefit from it.

As well as going over what the foreign exchange market is, we will look at some of the history behind it and we will be explaining how it's possible for people like ourselves to trade this huge market. Furthermore, we will go through how it all works, breaking it down talking about everything you need to know before you even think about placing a trade.

To finish off this PDF, we will then run through some of the terminology professional traders use and the brokers we work with, why we use them and look at how how they work and how they benefit us.

Upon completing this PDF file and taking notes from it, you should have a greater understanding on the foreign exchange market as a whole. I will have a set of Q & A's at the end for you to answer, lets see how well you get on!

1 What is the Foreign Exchange Market (Forex Market)

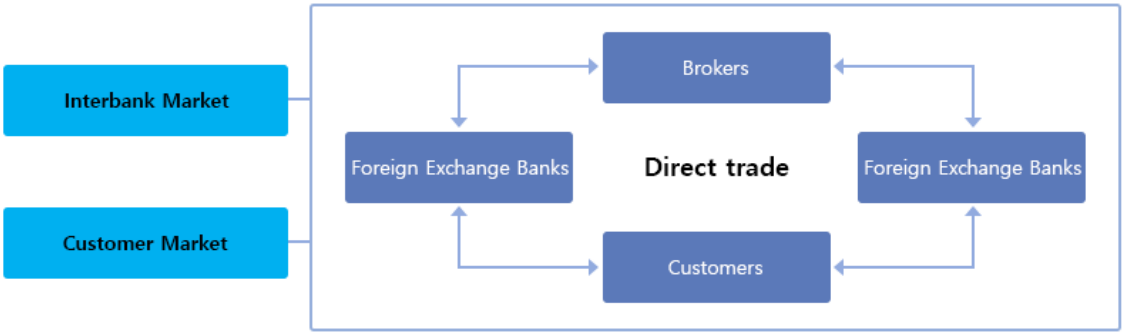
The Foreign Exchange market is actually the largest financial market in the world, with an average daily turnover of around $6 trillion. This huge trading volume outweighs and exceeds other major markets including both stocks and bonds. Forex is a huge OTC (Over-The-Counter) global market place that determines the exchange rate for currencies around the world, it was one of the original financial markets formed to help bring structure to the global economy.

Those involved in the foreign exchange market are able to buy, sell, exchange and speculate on currencies making profits from these transactions. The markets are made up of Forex Dealers, Commercial Companies, Central Banks, Hedge Funds, Investors and **Retail Forex Brokers** like ourselves.

Currencies are important to most people around the world, whether they realise it or not, because currencies need to be exchanged in order to conduct foreign trade and business, an example of this would be the trading or import of foods or building materials. We receive all that from other countries! In fact 80% of British foods are imported from other countries. This is one key reason why foreign exchange is heavily relied on.

An example of the importance of foreign exchange; If a British super market had to buy carrots from Spain they would have to pay in Euros. This means that the UK importer would have to exchange the equivalent value of Great British Pounds (GBP) into Euros (EUR). The same applies for travelling; A British tourist in the US can't pay in GBP because it's not the locally accepted currency. Therefore, The tourist has to exchange their GBP into the local currency at the current exchange rate.

The Forex Market is made up of two levels; The Interbank Market and then the Over-The-Counter market better known by **OTC**. The Interbank market is where large banks and hedges trade the market for purposes like hedging and balancing sheet adjustments. The **OTC** market is where individuals like You and I trade through online platforms like MetaTrader4 and with brokers like BDSwiss & AxiTrader.



Direct Trade Cycle

1.1 The History of Forex

Going back to the early 1900's, currency as we know it was comprised of precious metals like gold and silver but that system collapsed after the second World War when the Bretton Woods agreement came into play, which resulted in three international organisations facilitating the economy across the globe.

The New system replaced Gold with USD as **peg** (Fixed Exchange Rate) for international currencies, that's when the promise was made to back up dollar supplies with equivalent gold reserves. Fortunately for us the Bretton Woods system became redundant in 1971 when US president Richard Nixon announced "temporary" suspension of dollars being converted to gold, which meant that currencies as a whole are now free to choose their own **peg** and their value is determined by supply and demand in international markets.

The Bretton Woods system being made redundant meant that people like us were and are able to covert one currency to another for financial gain. More Major Currencies were allowed to float freely against one another which is why you have Major, Minor and Exotic pairs when trading the Forex Market and you can actively trade with them all.

1.2 The Spot Market

The spot market Is basically where people like ourselves (Retail Forex traders) trade. It is the most common form of trading as it involves buying and selling currencies based on their current price and not future or past prices. A spot price is the current cost that a financial instrument is valued at, it is the price that it can be sold or bought at with an immediate effect.

Traders can create a spot price, different to the current one, by placing buy and sell orders. For the trade to activate and execute the spot price would have to match your order which in liquid markets - like Forex - that change can happen in seconds. More about buy and sell orders can be found below.

1.3 How can we trade Forex

Originally, before the invention of the internet, trading Forex and other commodities was very difficult as an individual investor. Most currency traders were large Multinational Corporations, Hedge Funds or high-net-worth individuals because Forex trading required a lot of money especially if your wanting to grow your capital.

But now with the help of the internet, a retail market aimed at the likes of Retail Forex traders like ourselves was created and emerged, providing easy access to the Foreign Exchange Markets, either through the banks themselves or brokers making a secondary market. Most online brokers like BDSwiss and AxiTrader offer very high leverage to individual traders so we can profit more from the trades we place, but in-turn means we could incur bigger losses.

1.4 What Impacts the Forex Market

There are a number of factors that effect the Forex market but the biggest ones are: political instabilities, economic performances, recession and inflation rates. A country with less risk for political turmoil is more attractive to foreign investors. As a result, this draws investment away from other countries with more political and economic stability. When a country experiences a recession, its interest rates are likely to fall, decreasing its chances to acquire foreign capital. As a result, the currency weakens in comparison to other countries.

An example of how much fundamentals can affect the markets can be seen above. This was an event that happened back in March of 2020. The UK announced its first National Lockdown causing all Retailers, Schools and any other services to close immediately and all unnecessary social contact should cease due to the Covid-19 pandemic.

This caused the value of the GBP to drop massively as all means of life was put on hold with everything being closed. As a result of this, the UK's economic growth had stalled, this was just added strain to the Sterling as we already had a lot of complications as a country anyway due to Brexit coming into affect later that year.

Staying up to date with current News such as Brexit is important as it can cause uncertainty in the markets. You do not want to be on the wrong end of a trade when the markets make an immense move like this.

2 How Does The Foreign Exchange Market Work

The Foreign Exchange Market is tradable 24 hours a day, five days a week. It runs from Monday to Friday, with the market closing at 10PM Friday and re-opening again 10PM Sunday GMT. The trading sessions start each day in Australia and ends in New York, the major centres are Sydney, Tokyo, London and New York. Throughout the day specific pairs will become more active and will offer bigger moves as it will be within their time session, below you will see the Forex Market Sessions.

FOREX MARKET SESSIONS																							
GMT																							
5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	1	2	3	4
		LONDON																					
							NEW YORK																
																SYDNEY							
																		TOKYO					

The market determines the value - better known as the exchange rate - of all the currencies. Currencies are always listed in pairs, so when placing a trade on a pair you are essential betting that a central bank will ease or tighten and that one currency will strengthen against the other, whether it be your base or quote currency that'll depend on your entry execution.

In its simplest form, you are wanting to buy when the value of the base currency goes up and sell when the value of the base currency goes down, this is because you make profit based on the difference in price from when you first execute the trade to when you close it.

2.1 Base & Quote Currencies

With every pair you have a Base Currency and a Quote Currency, your base currency is the first currency appearing in a pair quotation and your quote currency is the second currency quoted. An example of this can be seen below, GBP is your **Base** and USD is your **Quote**.

GBP/USD

All Forex trades that are executed on the market involve the simultaneous purchase of one currency and a sale of another, but the currency pair itself can be seen as a single unit. If you were to place a **BUY** trade on a pair you would be buying the base currency and implicitly be selling the quote currency and vice versa for a **SELL** trade. The bid shows you how much of the quote currency you need to get one unit of the base currency, an example of this can be seen in the **Asking Price** section below.

The four most heavily traded currency pairs will offer you the most movement and deliver you with the most profit if traded correctly and the markets move in your favour, these pairs are the following:

GBP/USD - Great British Pound vs U.S Dollar
EUR/USD - Euro vs U.S Dollar
USD/JPY - U.S Dollar vs Japanese Yen
USD/CHF - U.S Dollar vs Swiss Franc

2.2 Asking Price

When trading pairs they will be associated with an asking price, that asking price is how much it costs in the Quote currency to buy **one** unit of the Base currency, so for example:

If the price of GBP/USD was 1.3451 it means that it costs 1.3451 USD to buy one GBP. If for example the price increases to 1.4051 then it now costs 1.4051 USD to buy one GBP meaning the GBP has increased in value where as the USD has decreased because it now costs more to buy one GBP.

2.3 Lot Size

When you trade the Forex Markets, the currency pairs are traded in Lots. Lots are units used to measure a transaction amount, in layman's terms, it's the number of currency units you will buy or sell. The measurements of Lots sizes are **Micro**, **Mini** and **Standard** Lots.

LOT	NUMBER OF UNITS	LOT SIZE
Standard	100,000	1.00
Mini	10,000	0.10
Micro	1,000	0.01

When you place a trade, they will take place in set blocks of currency like listed above. These can trade as many blocks as you like, as long as you have the **Equity**, **Free Margin** and **Leverage** in and on your account to back it. Below is some examples to help you understand lot sizes more.

LOT SIZE	NUMBER OF UNITS
0.07	7,000
0.22	22,000
3.00	300,000
1.46	146,000

2.4 Forex Leverage

In order for us to profit well, having little equity leverage is a must. This is why brokers exist and why they are so useful to everyday traders like ourselves. Using leverage in Forex transactions allows a trader to take on a larger position in a trade without having to pay the full purchase price. This is achieved by using borrowed funds from the broker to increase your position beyond what would be available from your own equity. Having leverage and taking advantage of this means you can increase your lot size which gives you the opportunity to buy and sell a larger number of units, resulting in greater profitability. However, it also means your potential losses are amplified.

For example, traders who have a £1,000 trading account can trade £100,000 worth of currency with a margin of 1%. This is referred to as having a **100:1** leverage. The profit and losses made will be based on the £100,000 national amount. Most brokers offer a leverage up to 400:1 meaning for every £1,000 you have you can trade £400,000.

With most brokers you can change your leverage to suite you, depending on your equity and account size your leverage will change. A Retail trader with £1,000 might use a leverage of anywhere between 100:1 to 400:1, but someone with an account size of £100,000 might use a leverage of just 10:1.

Below is a table of different leverage sizes and the money it would allow you to trade with.

YOUR EQUITY	LEVERAGE SIZE	MARGIN
£1,000	10:1	£10,000
£1,000	100:1	£100,000
£1,000	400:1	£400,000
£50,000	10:1	£500,000
£50,000	100:1	£5,000,000
£50,000	400:1	£20,000,000

These numbers may seem a little excessive. But in order to make worthwhile profits you will need to be trading with this kind of money which is given by leverage. This is so you can buy or sell enough units to make enough profit per trade.

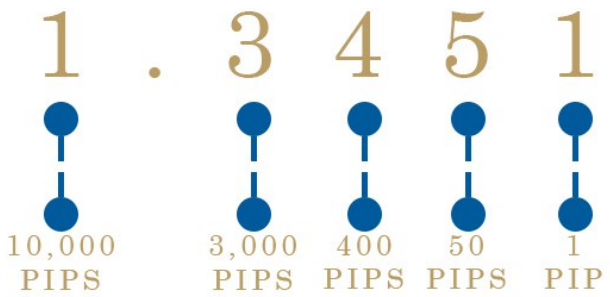
Leverage is important to Retail Traders because before the internet and before brokers came into the equation it was only corporate companies and hedge funds that traded these markets as they were the only ones with the equity to trade in volume.

To put it in context, If for example we had no leverage and we bought just £1 GBP for $1.3451 like we stated previously and the cost of the GBP changed from $1.3451 to $1.4051, that's taken an increase in value of $0.06 which is great, but that kind of change in price can take a week if not longer. So without brokers providing us with leverage, our profits from trades would be so minuscule it would make the process pointless.

But lets say you've got a leverage of 100:1 on a £1,000 account, that gives you the ability to buy £100,000 worth so that profit is no longer $0.06 its $6,000, now that's worth it. Again if you bought and the price didn't go up, instead it went down $0.06 it doesn't mean your in debt of $6,000 what would happen Is your account would just go to 0.00 funds and the trade would close automatically, this is called blowing your account. How do we stop this from happening? With a SL set by pips and good risk management.

2.5 Pips

PIP stands for **Point In Percentage**, and is a term used to measure the smallest change in price that can be made in the Forex market. Most currency pairs other than JPY (Japanese Yen) are priced out to four decimal places and the pip change is the last (fourth) decimal point. JPY pairs are quoted with two decimal places, making a notable exception.
Pips are not only used to measure the spread between the bid and ask prices of the currency pair your trading, but it is also used to measure how much you have gained or lost from a trade. This is useful when generating trades and monitoring progress and performance. Below I have drawn out a Pip map below to help you understand how to read pips.



The movement of a currency pair determines whether a trader makes a profit or loss from his or her positions at the end of the day. So going back to the example we used earlier we had GBP/USD valued at 1.3451. If this was bought and the price increased like previously stated, then you will profit because the GBP increases in value relative to the US dollar.

So let's break it down; If you had a **Buy** entry at 1.3451 and then exited after the increase, closing your trade at the new price of 1.4051, how many pips did you profit? Your answer should be 600 pips.
Let's do another example, this time using a Yen pair which is always quoted with two decimal places. If we sold GBP/JPY at 138.62 and closed the trade at 139.14, did we profit from the trade or lose from the trade? How many pips did we win or lose by?
Well we lost on the trade because we placed a sell order in hopes that the value would go down but it actually took an increase and it increased by 52 pips meaning we lost 52 pips.

Now we have a good understanding about what **pips** are and how to read them, we now need to know what value a pip movement holds, 1 pip movement can be valued differently from one person to then next depending on there **Lot** size. Below is a basic guide on the value a pip holds dependent on Lot size.

LOT SIZE	NUMBER OF UNITS	VALUE OF 1 PIP MOVE
0.01	1,000	$0.10
0.10	10,000	$1.00
0.50	50,000	$5.00
1.00	100,000	$10.00

So going back to the first example with GBP/USD with it moving 600 pips in profit we had a result of $6,000 before conversion on a £1,000 account with a 100:1 leverage that would be using what lot size? Your answer should be 1.00, a standard lot because we used all of our free margin which was 100,000 units. How do we work this out?

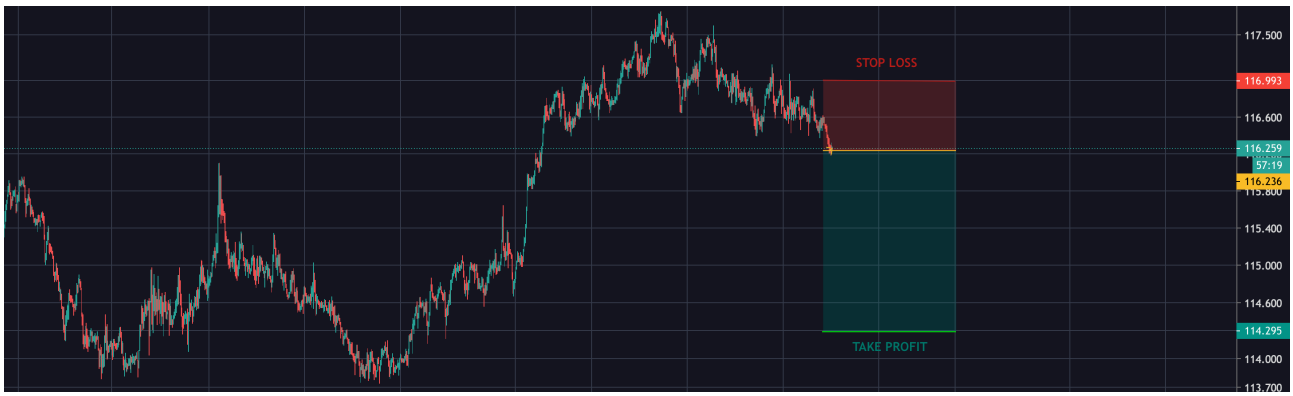
Well £10.00 (which on average is the value of 1 pip move for a 1.00 lot size) **X** 600 (which is the amount of pips it moved) = $6,000. Now with example two we lost 52 pips, again depending on your lot size your loss will vary. To work it out we do the same thing as last time 52 **X** your value per 1 pip.

2.6 Stop Loss & Take Profit

When placing a trade whether it be a **Buy** or **Sell** on a Forex pair there's a few things you need to consider. Such as; When is it best to enter depending on the trend, how much am I willing to risk and how much can I see it profiting.

A **Stop Loss** is designed and used to limit an investors loss on a security position that makes a wrong move. Its important you bear in mind short-term price fluctuations when applying a stop loss as it could activate if you put your Stop Loss too tight to your entry. When looking at placing a position it's important to look at the potential of the trade and how much I could profit from it in terms of pips. For example if the potential Take Profit is 50 pips then the investor would look at risking a maximum of half which would be 25 pips, keeping the ratio in favour of my Take Profit.

Take Profits are the opposite to Stop Losses, **TP's** are used to close a position for you when a trade hits a specific target price. This means the trade doesn't need to be constantly monitored and with both your **SL** and **TP** in place, the trade can be left running with confidence if the analysis you've done is thorough enough.
It's important that anyone trading does not exceed their expectations with a trade and the trend its taking as you don't want to miss your take profit and it reverse. A Take Profit should be placed at a point where you could see the price exceeding a certain value to ensure that the target price is met.



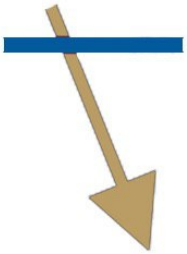
An example of a sell trade is above. Indicating both its SL & TP. We will go through more about SL & TP in our Risk Management PDF, going more in-depth about how, where and when to place them. It's very important to implement a SL and TP in all trades just to help lower that risk of burning away at your equity. Traders find their SL depending on a few factors, it might not just be based on the charts but maybe time, volatility or percentage.

2.7 Buy & Sell Orders

There are five different types of orders that can be applied to a trade, depending on what your analysis suggests will determine whether you are going to buy or sell at that current price, or later down the line when the price either moves up or down. An Instant execution is the most commonly used and that is just buying or selling at the current **dot** price, the rest can be seen and explained below.

SELL STOP

A Sell Stop is placed below the current entry price, the idea of a sell stop is that it touches the price set in the order and continues to fall in the same direction.



BUY STOP

A Buy Stop is placed above the current entry price, the idea of a buy stop is that it touches the price set in the order and contines to rises after being avtivated.

SELL LIMIT

A Sell Limit is placed above the current entry price, the idea of a sell limit is that it touches the figures set in the order and then falls back down in bearish move.

BUY LIMIT

A Buy Limit is placed below the current entry price, the idea of a buy limit is that it touches the price set in the order and then rises in a bullish move.

3 Brokers

There are four main types of broker, you have **Stock** Brokers, **Forex** brokers, **Full-Service** brokers and **Discount** brokers. While they all act as a facilitator between you and another party, they all operate differently from one another. Some brokers are 'execution only' Brokers, while others execute, offer advice and manage your portfolio for their clients, so it's all about finding the best one, and one that suits the client and their needs.

3.1 What Are They

A Broker is a company that can organise and execute financial transactions on behalf of another party, that being you. They can do this across a number of different assets alongside Forex such as **Stocks**, **Real Estate** and **Insurance**.
A Broker will usually charge a small commission fee for the order to be executed, this is known as the spread. Most brokers allow customers to trade in other currencies, giving us access to trade any pair we like, so someone trading in the UK investing with GBP could trade a USD/JPY pair with ease. Furthermore, Brokers offer leverage with every trading account meaning you can benefit and profit more, as you have the ability to buy or sell greater units because your equity is technically larger. So a 100:1 leverage would mean for every £1 in your account you have £100 to trade.

3.2 Spread

Forex Brokers will quote you two different prices for a currency pair, the bid price and the asking price. The Bid price is the price at which you can SELL the base currency which is the first currency quoted in a pair.
The Ask price is the price at which you can BUY the base currency, the difference between these two prices is known as the spread. This is how "no commission" brokers make their cut; instead of charging a separate fee for making a trade, the cost is built into the buy and sell price of the currency pair.
To put it simply they make money by selling the currency to you, the trader, for slightly more than they paid to buy it. You also have both Fixed spreads and Variable spreads. Luckily for us, both our brokers give us variable meaning they can change within a range, where as a fixed spread always stays the same. If your spread is 0 they are selling you the pair for the price they buy it for. The lower the spread the better.

3.3 How Do They Work

Forex Brokers are compensated in two ways. The first is through the bid-ask spread of a currency pair, they basically make a small profit on all trades that we place, the lower the spread the lower the **coms** (commission) they earn. This is something most retail traders don't even notice as its literally pennies. Some brokers also charge additional fees. Some charge a fee per transaction or a monthly fee for access to a particular software interface or for access to special trading products such as exotic options etc, but this is how brokers are always profiting and making money.

3.4 Our Brokers

LAGFX have taken great care in finding the best brokers we can, we are currently working with two different brokers, **BDSwiss** and **AxiTrader**. Both Brokers are regulated with the FCA and are trusted brokers in the world of trading so you have nothing to worry about in terms of security. They are offering great spreads as low as 0 and a leverage up to 400:1 meaning you can maximise those profits on every trade that is placed.

BDSwiss
BDSwiss Group offers leading Forex and CFD investment services to more than a million clients worldwide. BDSwiss as a brand was established back in 2012 and has since then been providing award-winning conditions, world-leading platforms, competitive pricing and optimal execution on more than 1000 underlying CFD instruments. They have a trading volume of over $84 Billion, with over 1.5 million registered accounts to date offering their services world wide to over 186 countries.

They offer an average spread of 25 with most forex majors like the GBP & USD pairs which is about 2.5 pips. BDSwiss are also flexible in terms of leverage meaning you can change this whenever you like in your account setting, this leverage can go anywhere up to 400:1 meaning for every £1 in you account you they give you £400 to trade.

AxiTrader
As a Retail Client you enjoy the greatest protection with rules and regulations imposed by the Financial Conduct Authority (FCA) and the European Securities and Markets Authority (ESMA). These regulators are designed to ensure you are given every opportunity and assistance when trading in financial markets. Axi offer there traders with the tools, opportunities and support you need to find your edge which will help you capitalise.

Axi offer their services to over 100 countries all around the world and have over 60,000 active traders and are growing every day. Through there high-performance technology and ongoing investments, they offer lighting-fast executions, raw spreads as little as 0 and flexible leverage, and this is all across a wide range of FX pairs, commodities, stocks and indices. Axi trader want to give their traders more, they are always offering innovative products that will give you the upper hand. Solutions like PsyQuation will help help sharpen your strategies using the power of AI analytics. We highly recommend Axitrader as a broker if your serious about trading.

If you're wanting to trade with either of these brokers the team at LAGFX would be more than happy to guide you through the sign-up process. We will provide you with the reassurance and advice that you'll need to make your decision on which broker you choose as its important you chose one that's going to best fit your needs. If you are going to be trading with a large equity, and have past experience with the trading world, BDSwiss might be best for you.
If your new to trading and your initial investment will be relatively small and your wanting that added support we would recommend Axi, but drop us a message and we will talk you through your options.

4 Forex Terminology

Day trading terminology is something every trader will need to understand, at first it may seem like a new language, but its an important aspect of trading. This is especially important when reading reports, market breakdowns or any material that is trading related you will see terms that any normal person won't understand.

Day Trading

Day Trading is defined as the simple act of buying and selling stocks, shares, forex or whatever it is your investing in with the intention of closing the trade in the same day. If you consider yourself a day trader you're looking to capitalise on a trade price movement in the same day you wouldn't usually hold the trade overnight. You will look for patterns in the market and use them to dictate future price moves that you can profit from, using the **15M**, **1H** & **4H** time frames to find these patterns.

Swing Trading

Swing Traders usually trade the markets and hold there trades overnight, sometimes more than one night, these trades are considered to be very short-term investments. When holding trades for a few days you would be looking at the overall trend of the pair or commodity your trading, this can be seen on the **4H** and **1D** time frame.

Scalp Trading

Scalping is a trading style that profits from small price changes, this trading style is seen as very risky but the reward and potential can be very much worth it. One large loss could easily eliminate the several small gains you've made so it's important to have a strict exit strategy in place and to no let your emotions dictate your analysis.

Bull or Bullish

As a simple explanation, it's a term used for any strong upward movements in Stocks & Forex. So, if the price or trend is moving up, increasing in value it would be classed as a bullish trend or a bullish move.

Bear or Bearish

Now as for a bear or bearish move, its the opposite to bull or bullish. So, if the price of share or Forex pair was moving down or there was a downward trend you will most likely see the term bearish move or a bearish trend.

Divergence

Divergence is a trading concept that forms when a Forex pairs price diverges from a momentum oscillator, such as the MACD, which is commonly used when trading the Forex markets, it typically indicates a reversal in the prices direction. A positive divergence happens only when the securities price shifts lower while the indicator starts to rise to a new high and fails to achieve the same momentum, this would be bullish. The the opposite happens with bearish trends.

Volatility or Volatile

Volatility is a measure of the pairs stability and is usually calculated as the standard deviation derived over a given period of time. If a pair is very volatile, it can be seen as choppy if your day trading or swing trading, so you probably wouldn't want to trade it as it could activate your SL before continuing its trend. Volatility can happen for a numerous amount of reasons but mostly due to **Fundamentals**.

5 Summary

So here we are, you've made it to the end of the PDF and you should have watched and taken notes from the video. The information that's been provided should be enough to get your bearings and gain a solid understanding of Forex and the Markets.

5.1 Summary on PDF

We've spoken about the history of the markets, where it came from and how far it's come up to this point. This is a fascinating subject and amazing as it gives us that potential and opportunity to trade and make as much money as we can and want, the sky is our limit.

We have also broke down the Forex market and explained how It works. From Pips to Lot sizes and from Leverage to Spreads. Understanding these basics makes things a lot easier to grasp when wanting to develop your skills and trading ability.

We then spoke about brokers, their role and how they help Retail Traders like ourselves prosper from the trading markets. They act as the middle man and help us become successful and financially free.

And then to close off the PDF we went through some of the basic terminology used when trading and doing your weekly market breakdowns, which again is a must if your wanting to take trading seriously.

If you have taken the time to make notes and go through everything we have spoken about and you're feeling confident in what you've read, you will be more than ready to take the next step into the trading world!

Now it's time to get stuck in and learn the strategies and the indicators used to generate the trades we do to profit well, and how to implement good risk management in those trades to help ensure that your equity is safe and you're not overly exposing yourself to the market.

If you have purchased the full **Starter** or **Advanced** Course you will find these labelled **Risk Management** and **Indicators** along side the videos, Lets make some money!

5.2 Test Time

Write your answers down the questions then go back and see if you were right, don't cheat ;) if you got the answers right, you are well on your way to becoming a successful trader, best of luck!

What is a pip?

What Lot Size gives you a 1 Pip value of £7.00?

How many units is 1.00 lots?

30:1 leverage gives you how equity to trade with per £1?

Whats direction is a trend going if it's bullish?

Whats a Buy Limit?

Whats a Sell Stop?

GBPUSD - Which is the base currency?

What time does the London time session start and finish GMT?

What are Stop Loss' & Take Profits used for?

Whats a Spread?

Why do we need Brokers?

What are the four most heavily traded currency pairs?