

8 Day Intensive Course

Course Overview and Lesson 1

This is the summary of lessons from the PowerCourse. Since every course is different, responses to the initial texts are not attached. Additionally, there may be small differences between this version and the version of the course that you took, as changes are ongoing. Finally, threads such as the introductions on lesson 1 and the rules for the online classroom are not included, since they are obsolete except as far as using the course is concerned. But without further ado:

If the charts do not entirely fit on the MS Word page, you can resize them or crop them (cut extra space off the sides) by using the Picture toolbar under View>Toolbars.

Lesson 1: Welcome to the FX PowerCourse

Tools of the Trade

In addition to the Online Classroom, students will need a few other tools to get through the course. All the tools involved in the Power Course Online are aimed at helping you become a better trader -- so it is to your advantage to use all the tools outlined below to your fullest advantage.

Demo Account. A demo trading account -- or a virtual trading account that provides you with virtual cash to practice trading in the FX market -- is the best tool any aspiring currency trader can use to improve his/her skill in the market. To download the FX Trading Station -- the software you will need to trade your demo account -- simply click [here](#).

You can login to your demo account by entering the user name and password you received in the introductory email. The demo account is an integral part of this course, as instructors will be assigning homework assignments involving placing trades on your demo on a regular basis. Towards the end of the course, instructors will review the statements of various students and highlight noteworthy points to the class.

News Plug-in. Another tool traders can use to stay abreast of the FX market is the FXCM news plug-in. The plug-in, a downloadable component that works in conjunction with the FX Trading Station, provides traders with real-time market news, technical analysis, and rumors about what is happening in the FX market. To ensure that you have an understanding of all the fundamental factors involved in trading, be sure to download the FXCM News Plug-in by clicking [here](#).

Supplemental Web Site. In addition to the material presented in the Online Classroom, the Power Course Online also includes a supplemental Power Course Student Site filled with additional trading strategies and advanced market topics. This material, while supplemental to the course, is invaluable to the student looking for more advanced material that will help them refine their trading strategy. To access the supplemental

Power Course Student Site, [click here](#).

FXTrek Desktop Charts

FXTrek is offering a free month long subscription to their desktop charts for all students in the course. These are excellent charts, and you will find that most of the examples that the instructors post are from these charts. Your login ID and password for the course will work for these charts as well during this trial month. You can download the actual software from the following link.

<http://iwizard.fxtrek.com/misc/down...partner=iwizard>

For any technical problems with these charts, you can log onto <http://www.learncurrencytrading.com/fxforum/> and select the FXTrek link under the Charting & Trading Services Experts link at the bottom. The forum on that page functions in the same manner as the forum for this course, and a response to your inquiry will be answered by FXTrek's technical support staff.

Nuts and Bolts of Trading

A) How Speculators Can Profit from FX Trading

What the Exchange Rate Means

Key Concepts

The base currency is the term for the first currency in the pair.

The counter currency is the term for the second currency in the pair.

The exchange rate represents the number of units of the counter currency that one unit of the base currency can purchase.

In a foreign exchange trade, clients are speculating on the exchange rate between two currencies. The exchange rate measures the relative value of a currency -- meaning it measures how much one currency is worth in terms of another currency.

For example, let's suppose the exchange rate for the GBP/USD (Great British pound/United States dollar) is 1.8455. This means that 1 British pound (the first currency in the pair, also known as the base currency) is the equivalent of 1.8455 US dollars (the second member of the pair, known as the counter currency). This is the standard quoting convention for exchange rates; the exchange rate represents how much 1 unit of the base currency (first currency in the pair) can purchase of the counter currency (second currency in the pair).

So, if the GBP/USD exchange rate were to rise from 1.8455 to 1.8555, that would mean that 1 GBP would have gone from being able to purchase 1.8455 US dollars to being able to purchase 1.8555 US dollars.

Measuring Exchange Rate Movement

Key Concepts

A pip is the unit of measurement for exchange rate movement.

The number of pips a currency pair moves determines how much a trader will earn or lose on the position.

A pip is the last significant digit in an exchange rate, and is the term used to define the unit of measurement for exchange rate movements. The number of pips that the exchange rate moves dictates how much a trader has gained or lost through an FX trade. In the example above, if the rate moves from 1.8455 to 1.8555, the pair has risen by a 100 points or pips.

How an FX Trade Works

Any foreign exchange transaction ultimately begins with two events:

- One currency is being borrowed.
 - The proceeds from the borrowed currency are used to finance the currency that is being bought.
- Currency pairs are typically traded in increments of 100,000 units of the base currency. A 100,000 unit increment in a currency trade is referred to as a lot. (For example, a trader who is trading 5 lots is trading 500,000 units of currency).

After gaining an intuitive understanding of how exchange rates move, one can begin FX trading, thereby speculating on the exchange rate so as to potentially reap profits from the fluctuating value of currencies. Essentially, clients can borrow one currency and buy another, and profit from exchange rate movements. This concept is most easily explained and understood through an example of an actual trade:

Trader A wishes to speculate on GBP/USD. Believing that the GBP will rise against the USD, or that the exchange rate will move upwards, the trader places an order to buy GBP/USD at a market rate of 1.8455. In terms of volume, let's assume that Trader A is speculating on 100,000 units of the base currency – which is the standard lot size, or trading increment, used in the foreign exchange market. Since the base currency is the first currency in the pair, we know that Trader A is speculating on the value of 100,000 British pounds with respect to the US dollar.

In this example, Trader A is buying British pounds, since he believes the pound will rise in value with respect to the US dollar. Accordingly, he finances the transaction of buying 100,000 pounds by borrowing an equivalent amount of US dollars.

For Trader A, the value of the amount borrowed is a function of the exchange rate. Since the exchange rate at the time of the transaction was 1.8455, we know that the market cost for 1 British pound was 1.8455 US dollars. Hence, 100,000 pounds cost \$184,550

($1.8455 * 100,000$). This borrowed amount of 184,550 USD must be paid back when the transaction is closed.

Let's assume that Trader A is correct in assuming that the British pound would rise in value with respect to the USD, and that the exchange rate moved to 1.8555 – 100 pips above the rate at which Trader A entered. If Trader A were to close his position now, the 100,000 pounds he purchased at the onset of the transaction would be sold, and his debt of 184,550 dollars would be paid off.

At an exchange rate of 1.8555, Trader A's 100,000 pounds are now worth 185,550 US dollars ($100,000 * 1.8555$). After repaying the borrowed amount of 184,550, this leaves him with a profit of \$1,000.

A summary of the transaction is as follows:

Initial transaction: Purchase of 100,000 pounds at a cost of 1.8455 US dollars per pound, or a total of 184,550 USD

Final transaction: Sale of 100,000 pounds at a price of 1.8555 US dollars per pound, or 185,550 USD

Amount of pounds initially purchased: 100,000

Amount of pounds sold through the closing transaction: 100,000

Net number of pounds: 0

Amount of dollars initially borrowed: 184,550

Amount of dollars purchased upon close of trade: 185,550

Dollars remaining after borrowed dollars are paid off: 1,000

Selling a Currency Pair Short

Key Concepts

Traders have equal opportunities to profit regardless of whether the exchange rate is rising or falling.

The number of pips a currency pair moves determines how much a trader will earn or lose on the position.

One of the premier advantages of the foreign exchange market is that profit opportunities are equally present in all market conditions; it is just as easy to profit when the exchange rate is declining as it is when the rate is rising. If, for example, Trader A believes the pound will fall against the value of the US dollar – meaning 1 pound will buy fewer US dollars – then he can simply place an order to sell GBP/USD. This trade works in essentially the same manner as the trade to go long (buy) the pair, with the only difference being which currency is being bought and sold.

Let's assume Trader A believes that the GBP will decline in value with respect to the USD -- in other words, that the exchange rate will fall from the 1.8455 level. Accordingly, he places an order to sell 1 lot of GBP/USD, thus borrowing 100,000 pounds and buying an equivalent amount of USD with the proceeds.

Since 1 pound can purchase 1.8455 US dollars at the time Trader A places his trade, he can purchase 184,550 US dollars with the 100,000 pounds he borrowed. As in the previous example, the borrowed amount will be repaid when the transaction is closed.

Let's assume that Trader A is correct in his belief that the pound will fall in value against the USD, and that the GBP/USD reaches 1.8355 – a drop of 100 pips from Trader A's entry point. Now, Trader A decides to take his profit and close out the trade. Accordingly, he must repay the 100,000 pounds that were borrowed. Since the cost of 1 pound has now dropped to 1.8355, this means that the cost of 100,000 pounds is 183,550 ($100,000 * 1.8355$). This amount is then subtracted from 184,550, which was the number of dollars that Trader A received when he initially placed the trade. The result is a profit of \$1,000 ($184,550 - 183,550$).

A summary of the transaction is as follows:

Initial transaction: 100,000 pounds were borrowed and exchanged for US dollars at a rate of 1.8455 US dollars per pound, or a total of 184,550 USD

Final transaction: The borrowed amount of 100,000 pounds was repaid at a cost of 1.8355 US dollars per pound, or a total of 183,550 USD

Amount of pounds initially borrowed: 100,000
Amount of pounds repaid via close of trade: 100,000
Net number of pounds: 0

Amount of dollars initially purchased: 184,550
Amount of dollars used to pay off the 100,000 pounds that were borrowed: 183,550
Dollars remaining after borrowed pounds are paid off: 1,000

In the examples given above, Trader A had the potential to earn a profit of \$1,000 when the exchange rate rose 100 pips and also when it fell 100 pips. For any currency pair in which the US dollar is the second in the pair – like the GBP/USD, EUR/USD, AUD/USD, and NZD/USD – the value of a pip is fixed at \$10 per 100,000 unit lot. In the Mini account, where a mini lot is 1/10th the size of a 100k lot, the pip value is 1/10th that of the 100K account. Accordingly, the pip value for any pair in which the USD is the counter currency is fixed at \$1.

Here is a list of the abbreviations for various currencies that are commonly traded in the FX market:

Currency Abbreviations

EUR = euro
GBP = Great British pound
USD = US dollar
CHF = Swiss franc
NZD = New Zealand dollar
AUD = Australian dollar
CAD = Canadian dollar
JPY = Japanese yen

B) Key Concept: Spreads

On your trading station, you will notice that there are two prices for each currency pair. Similar to all financial products, FX quotes include a "bid" and "ask". The bid is the price at which a dealer, for example FXCM, is willing to buy and clients can sell the base currency in exchange for the counter currency. The ask is the price at which a dealer is willing to sell and a client can buy.

BID = The Price at which the Trader (You) Can Sell

ASK = The Price at which the Trader (You) Can Buy

For example, say the EUR/USD is trading at 1.2245 x 1.2248. In this case, the bid is 1.2245 and the ask is 1.2248.

The difference between the bid and ask constitutes the spread. In the above example, the spread is 3 pips, or points. This differential reflects the cost of the trade. Essentially, the market would have to move 3 pips in your favor for you to break even, and 4 pips for you to be in your profit zone.

For example, say you bought the above currency at 1.2248. If you immediately sold, you would be filled at 1.2245. This represents a loss of 3 pips. The market would have to move up 3 pips to 1.2248 x 1.2251 for you to break even, and up to at least 1.2249 x 1.2252 for you to make a profit. This is because you bought at 1.2248 and you would have to sell at 1.2249 or higher to profit.

This spread of 3 pips represents the main source of revenue for the market maker (e.g. the firm that executes your trade). Please note that there exists a spread for all tradable instruments in all markets, regardless of whether both prices are transparent. On the FX Trading Station, this cost is made visible. An easy way to think of it is that if you were trading stocks and bought stock XYZ at \$50 and then wanted to sell right away, you would not be able to sell at \$50. You would have to sell at a lower price. This is because of the spread, and thus represents a hidden cost of trading in many equities and futures markets.

C) Margin

If you have a standard cash stock account, you know that money should be deposited for the full amount of the position you are trading, or if you have a margin account, for at least half of the position. This is in contrast to the FX market, where only a small percentage of the actual position value needs to be deposited prior to taking on the entering the trade. This small deposit, known as the margin, is not a down payment, but rather a performance bond or good faith desposit to ensure against trading losses. The margin requirement allows traders to hold positions much larger than their account value.

Margin requirements are as low as 1% (and as low as 0.5% on the mini account),

meaning for every standard lot size of 100,000 units, you must commit \$1,000. However, if you wanted to control a \$100,000 in the stock market, you would have to deposit at the very least, \$50,000. Even in the futures market you would have to deposit at least \$5,000 to control a \$100,000 position.

On your trading station, you can see that there are two types of margin: usable and used. Your used margin is the amount of funds you have committed to existing positions, and your usable margin is the amount of money you have available to commit to new positions. Account equity is your account balance plus or minus any floating profit or loss.

For example, say you open an account with \$10,000. At this point your account balance and equity are both \$10,000, your usable margin is \$10,000 and your used margin is \$0, as you have yet to place a trade. Next, you buy 7 lots of USD/JPY, which requires you to maintain \$7,000 in equity. Now your used margin is \$7,000 and your usable margin is \$3,000. Essentially, this means that you can sustain market losses totalling \$3,000 before your account equity falls below the minimum margin requirement of \$7,000, at which point the dealing desk will close all open positions. This automatic margin call feature prevents your account from ever reaching a negative account balance.

D) Types of Orders

The term "order" refers to how a trader can enter or exit a speculative position in the market. There are various ways of placing orders, and understanding the pros and cons of various order types is key to becoming a savvy trader.

To help make matters simple, let's divide orders into two categories: orders used to enter positions, and orders used to exit positions.

Orders Used to Enter Positions

Market Order

Key Concepts

- *Advantage: Ensures trader that he/she will be in the position*
- *Disadvantage: Far greater likelihood that trader is not getting the best price for the trade, or is assuming unnecessary risk.*

A market order is an order to buy or sell a currency pair at the current market price. For example, the FX Trading Station will always show two prices for every currency pair -- the price you can buy at (also known as the ask), and the price you can sell at (also known as the bid). For instance, the market could be pricing the EUR/USD at 1.2200 - 1.2205 -- meaning traders can buy the EUR/USD at 1.2205, but would have to sell at 1.2200.

These prices represent the current market prices, and traders who choose to enter market orders would be filled at the rate they see. The key advantage of market orders is that

they ensure the trader that he/she will be in the position. The key disadvantage, though, is that the trader may not get the best price he/she could have gotten had he/she used another order type. Another disadvantage -- and one that is often overlooked -- is that market orders are more conducive to being used recklessly and without discipline. Using other orders, like stop and limit orders, are better-suited for helping traders stay disciplined.

Entry Orders

- *Advantage: Greater likelihood that the trader will get the price he/she wants.*
- *Disadvantage: Market may not reach the rate the trader specified, and hence the trader may miss out on the opportunity.*

All entry orders are essentially contingent orders; they will only be filled if the market reaches the rate specified.

For example, suppose you are trading USD/JPY, and the current quote is 120.50-55. You can place an entry order to buy at 120.15, for example, so that your order will only be filled if the market reaches 120.15. This allows you to potentially receive a better price.

There are two types of entry orders: limit entry orders and stop entry orders.

Limit Entry Orders

Limit entry orders are classified as entry orders whereby the rate specified by the trader is either (1) below the current market rate if it is a buy order, or, alternatively, (2) above the market rate if it is a sell order. Essentially, limit entry orders should be used if the trader is expecting the market to reverse its direction at a certain rate. For example, if the USD/JPY is trading at 120.50 and the trader expects it to fall to 120.15 before reversing its direction, the trader would place a limit entry to buy at 120.15. Or, if the trader expected the rate to rise to 120.70 before falling, the trader would place a limit entry to sell at 120.70. In both cases, the trader is expecting a reversal at a certain level -- and hence is using a limit entry order.

Stop Entry Orders

Stop entry orders rely on rationale that is the opposite of limit entry orders; they involve either (1) placing orders to buy above the current market rate or (2) placing orders to sell below the current market rate. While limit entry orders can be used if a trader is expecting a reversal, stop entry orders should be used if the trader is expecting continuation of a trend beyond a certain point. As a result, stop entry orders are often safer; they allow a trader to enter positions only after the market has reached a certain rate and confirmed the strength of the trend.

Consider an example:

Suppose the current market rate for USD/JPY is at 117.04-09; in other words, traders can

enter the market to sell at 117.04 or buy at 117.09. There are two types of stop entry orders that a trader could place in such a situation:

- They could place an order to sell at a price below the current market rate -- i.e. they could place an order to sell at 116.75; if the sell rate in the spot market reaches 116.75, their sell order would be activated.
- Alternatively, they can place an order to buy above the current market rate -- i.e. they could place an order to buy at 117.50, and their order would only be filled if the market reached that rate.

In either case, the trader expects that the market will reach this level, it will break out and continue in this direction.

Orders Used to Exit Positions

The following are orders that can be used to exit positions:

Limit Orders (or take profit order)

- *Advantage: Helps trader maintain discipline, and is an effective way to lock-in profits.*
- *Disadvantage: May lead to premature profit-taking, as traders may end up getting out of positions too soon with too little profit.*

A limit order allows a client to specify the rate at which they will take profits and exit the market. Essentially, it defines the amount of profit that the trader is looking to capture on this particular trade.

Let's assume a trader has an open position where he is long (meaning he has bought) GBP/USD at 1.5800. In such a scenario, a trader can place a limit order to determine at what rate he will close his position and take his profits. So, for instance, if the aforementioned trader was looking to capture 100 pips on the GBP/USD, he would place a limit order at 1.5900; if the market reached that rate, he would be taken out of the market, and his profit from the trade would immediately be reflected in his balance.

Limit orders are great tools to help traders maintain discipline and lock-in profits. Still, though, they may result in premature profit-taking -- meaning they may cause traders to exit positions too early with profits that are too small relative to the risk involved in assuming the position. This is a common mistake made by novice traders, and often results in them blowing up their account.

Stop-Loss Order

- *Advantage: Allows trader to specify the maximum loss he/she is willing to take on a position.*

- *Disadvantage: Stops placed too tight may result in the trader being taken out of the market -- only to see the market reverse its direction and head in the direction the trader originally forecasted.*

It works like a limit order, but in an opposite fashion: it specifies the maximum loss that a trader is willing to accept on a given position.

For example, if a trader is long USD/JPY at 121.50 with a limit at 121.70, he may wish to maximize the loss he is willing to accept by placing a stop-loss order at 121.30. In such a case, if the market reached 121.30, he would be stopped out of the position and would suffer a loss no greater than 20 pips. Similarly, if a trader is short USD/JPY at 121.50 with a limit at 121.30 and only wants to suffer a loss of 20 pips, then he would place a stop loss order at 121.70. Accordingly, if the market reaches 121.70, the trader will be stopped out of the position and would have suffered a loss no greater than 20 pips.

Stop-loss orders are one of the most highly recommended tools for traders. They are crucial to ensuring that the trader does not blow up his/her account with a single trade, and can be vital when establishing risk-reward ratios to ensure that traders are not making foolish decisions. On the downside, stop-loss orders, if not placed at the appropriate level, can result in traders being taken out of positions at a loss -- when in fact the market may reverse itself.

E) Additional Resources

During the course you may wish to consult some additional resources for information concerning fundamental news releases, technical patterns, and other market related concepts.

For a searchable online glossary of terms please visit:
www.investorwords.com

You can access news about currencies at these links:
www.dailyfx.com
<http://biz.yahoo.com/fxcm/>

When we reach the technical analysis section of the course, an online glossary of candlestick patterns can be found through the following link:
www.litwick.com

Other technical analysis resource pages are
www.equis.com
www.stockcharts.com
and the supplemental website for this course
<http://www.learncurrencytrading.com/fxpcstudentnopass/>

When we reach the fundamental analysis section of the course, visit the Dismal Scientist for economic calendars and economic data release information:
www.dismal.com

You can also visit the Economic Calander on Yahoo!:

<http://biz.yahoo.com/c/e.html>

For general information on the FX market visit the Currency Markets sections of:

www.bloomberg.com

www.ft.com

G) Question of the Day

The two major market conditions are range-bound and trending. In a range-bound market, the price of a currency pair is moving back and forth between established high and low price levels on the chart. A trending market is exactly that-- the chart shows that the price is moving consistently higher or consistently lower.

In a market that is range-bound (where traders expect the price to move back and forth between the high and the low price levels), what might be a good trading strategy? What types of orders would you use to enter your positions? and finally, where would you place a stop-loss or a limit order?

Intro to Technical Analysis

A) The Logic of Technical Analysis

What is Technical Analysis?

· Technical analysis involves the forecasting of exchange rate movement based solely upon statistics and price patterns

Simply put, technical analysis is the analysis of the market based on price action. While fundamental analysis looks at economic factors and geopolitical conditions (such as economic numbers, capital flows, and key political events) in an attempt to forecast exchange rates, technical analysis relies on the statistics and patterns in price movement for its forecast. Technical analysis has gained great popularity in recent history, especially as trends in computerized trading continue to develop and active traders continue to refine their strategies to best assess what is going on in the market at all times. In today's marketplace, technical analysis has become an essential tool for any aspiring trader.

Why Technical Analysis Works

- Extremely popular, and hence offers insight into what many traders are doing*
- More clear-cut and less controversial than fundamental analysis*
- A simple way of making trading decisions*

Many traders believe that technical analysis is a self-fulfilling prophecy – in other words, it works solely because it is popular and is used by many traders. For example, many technical traders put a 20 day moving average line on charts not because the moving average itself is statistically important, but rather because it is an extremely common indicator used by active traders of all sizes. The rationale is simple: if so many traders are

basing their decisions off moving averages and other indicators, then those indicators must be watched closely, for they offer insight into what a vast majority of traders in the market are doing.

Because of this rationale, traders should focus on the most popular indicators in the trading community, and should use them in the most common way. This is the best way of tapping into the “psychology” of the market – in other words, it is a simple but highly effective way of understanding what other traders are up to, and how the market may move because of it. Contrary to popular belief, it is NOT a study that requires complex mathematics or computer algorithms. Rather, it is a study that requires looking at the same tools other traders use to understand what is happening in the market.

Below is a list of the most common indicators, all of which will be covered in the lessons that follow:

- Key Candlestick Patterns
- Fibonacci Retracements
- Moving Averages
- RSI
- Stochastics
- MACD
- Bollinger Bands

While it may seem intimidating, technical analysis is actually fairly simple – often far simpler than fundamental analysis. It simply requires an abundance of the two traits that are most necessary to be a successful trader: discipline and patience.

Different Time Frames

Technical analysis tools will be valid on all time frames, but we strongly recommend using daily charts for most of your analysis. Medium term positions based on daily charts, using hourly charts for more precise entry points, have two advantages over short term positions based on 5 or 15 minute charts.

1) The spread is less significant for a longer term position. 5 pips out of a price target of 20 is a huge obstacle to overcome on trade after trade. 5 pips out of a 100 pip target is manageable.

2) Longer term charts are statistically much more reliable, since they are based on more data. Indicators have a higher degree of reliability on a daily chart than on an hourly chart or 15 minute chart.

Trading on a weekly or monthly chart would likely be more accurate from a technical standpoint than a daily chart would be, but a slower time frame also means less precise entry points, and the wider stops necessary to trade a monthly chart are often beyond the capacity for many accounts. We recommend as a general rule risking no more than 2% of

your account balance on a single trade, and this is sometimes difficult with a monthly or weekly chart.

B) Technical Analysis Theory: Range-bound vs. Momentum

Support and Resistance

At the core of all technical analysis theory are two very simple concepts: support and resistance. Support can be defined as a “floor” through which the currency pair has trouble falling below. There is no scientific formula for calculating support; it is something that is typically “eyeballed” by traders, and hence involves somewhat of a subjective element.

Resistance, on the other hand, is simply the opposite: it is the upper boundary through which a currency pair has trouble breaking. Like support, resistance levels are somewhat subjective. Generally, if the market touches a certain level a number of times and cannot sustain a break above that level, it can be identified as resistance. See the charts below for an example of identifying support and resistance.

The reason why price has trouble breaking these levels is the presence of actual orders around these levels. A support level is simply a price area where buy orders tend to be, and so it takes more than normal selling pressure to break that level. Similarly, a resistance level is a price area where sell order tend to be, and so it takes more than normal buying pressure to break that level.

Support and Resistance in Range-bound Markets

The simplest way of using support and resistance in trading is to simply trade the range: in other words, traders can simply buy at support, and sell at resistance. A key advantage of this is that the market is range-bound approximately 80% of the time, making it a very viable strategy for most market conditions.

The downside of range-bound trading, though, is twofold:

- Range-bound trading generally does not yield substantial gains on a per-trade basis.
- When the market breaks out of the range, it often will make big moves. As a result, traders using range-bound strategies can suffer overwhelmingly large losses when the market breaks out of the range.

The chart below illustrates the concept of range-bound trading.



Note how this pair repeatedly fails to cross beyond certain support and resistance levels, and simply fluctuates between an upper and lower band.

Support and Resistance in Momentum Markets

Another way to use support and resistance is to trade outside of the range; in other words, to anticipate a breakout. This involves placing orders to buy above resistance and to sell below support. The rationale is that the market will gain momentum once it breaks out of the range, and thus by placing orders just below/above support/resistance, traders will be able to make big gains when the market moves out of the range. Momentum trading is a bit counter-intuitive, as it involves buying at a higher price and selling at a lower price.

Below is a chart that illustrates the concept of momentum trading. Note how the pair accelerates once it breaks out of a narrow range:

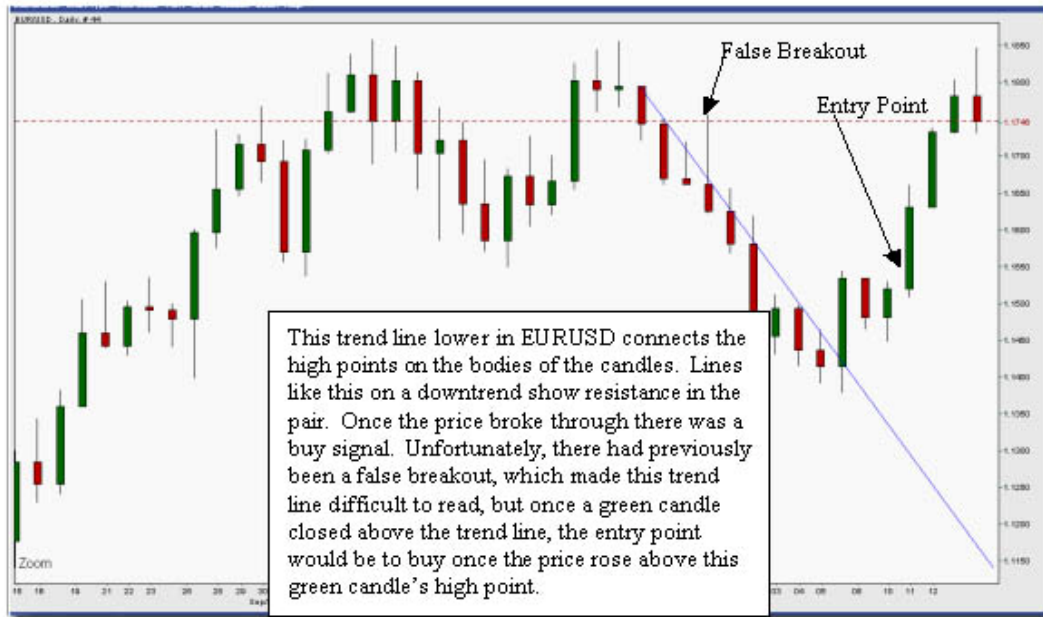


C) Price Channels

Support and Resistance do not have to be horizontal lines, and often in a market that is moving higher or lower, trend lines effectively connect the high points or the low points to create a price channel that acts similarly to a horizontal range. Support and resistance levels function in the same manner in a trending market as in a rangebound one. However the line that is following the trend--support in an uptrend or resistance in a downtrend) should be considered by far the stronger of the two. Only when there is a trade with minimal risk involved should you enter a position based only on the resistance line above the price in an uptrend.



The same trend lines can be drawn in a bear market where the price is continuously moving lower.



There is no exact formula for drawing such lines. Some traders prefer to connect only the bodies of the candles and to exclude the high and low points outside of the open and close, but that is not a requirement. If the line does not look valid to you, chances are it is not relevant, because other traders are using the same charts.

D) Question of the Day

1. Now that you have read about support and resistance, where would you place buy and sell orders relative to these levels when trading a breakout strategy? You can cite a specific chart if you would like to propose a specific support or resistance level and an order you would place.

2. Where would you place a stop-loss order once you initiate the position (relative to support and resistance)?