Currency Trading Market Introduction

Currency is the ultimate commodity. A foreign currency trade takes place every time a company or government buys or sells products or services in a foreign country; one currency is exchanged for another. A large number of individuals and organizations also do currency trading for speculative purposes. So, it is no surprise that the foreign currency exchange market, also known as "FOREX" or "FX" market, is the largest financial market in the world.

For day traders and swing traders, the currency market provides an alternative to stock market and futures trading. A trader only has a few major currencies to trade (the Dollar, Yen, British Pound, Swiss Franc, and the Euro are the most popular), whereas he is faced with tens of thousands of stocks to choose from.

Currency trading also provides greater leverage than stocks and futures, and the minimum investment required to open a currency trading account is much lower. All of these advantages compounded with the ability to choose flexible trading hours, has resulted in many equity and futures traders deserting the stock market to trade currencies.

The most actively traded currencies like the EUR/USD and USD/JPY can change up to 18,000 a day by some estimates. This shows the tremendous liquidity and depth of the currency market.

Currencies are traded continuously through out the day. Banks and other institutions are constantly trading the dollar, euro and other foreign currencies. Whether in London, Tokyo or New York, currency traders are scalping the currency market.

Around the world, trading hours overlap as some financial markets close and others open for trading. Trading takes place in New York, London, Hong Kong, Singapore, Frankfurt, Tokyo, and many other financial markets. These financial markets are linked to one another in a unified market, so at any given time one or more financial markets are open for currency trading.

The Currency Spot Market

A currency spot trade is the most popular transaction in the world. The spot rate is the current market price or cash rate for a currency pair.

Bid and Ask

When trading currencies, the trader sees two prices: a bid and an ask. This is the same as in stocks and futures. The "bid" is the price a bank or market maker is willing to pay for the currency. The "ask" is the price at which the market maker or bank is willing to sell the currency at. The online currency trader could then, buy from the bank or market maker at the "ask" and sell at the "bid."

The difference between the bid and ask price is called the spread. The more liquid or active the currency is, the lower the spread. Since the level of liquidity in the major currencies like the EUR/USD, USD/JPY, GBP/USD, and USD/CHF, is so great, the spreads are very tight. The reasons for this is that there are trades being made every few seconds creating liquidity, meaning there will always be a buyer for every seller.

Currency Quotes - Base Currency and Counter Currency

A currency trade involves two currencies: the base currency and counter currency. In a currency quote the base currency is displayed first followed by the counter currency; for example, EUR/USD. For this currency pair, the base currency is the Euro and the counter currency is the US Dollar.

The exchange rate provides the price of the base currency relative to the counter currency; i.e., how much is one Euro (base currency) worth in US Dollars (counter currency)?

So if the currency quote for EUR/USD was 1.2048 / 52, this would mean that if a currency trader was buying, he would pay 1.2048 Euro for 1 dollar and he would receive 1.2052 Dollars for each Euro when selling. When the exchange rate rises, it means the base currency is getting stronger against the counter currency. When the exchange rate falls, the opposite is true.

"PIPS"

"Pip" stands for "price interest point" in the currency market, and it represents the smallest fluctuation in price for a given currency pair. For most currencies the exchange rate is carried out to the fourth decimal place. In this case, a pip is 1/10,000th of the counter currency or 0.0001.

For example if the Ask price in the EUR/USD is 1.2048 and it goes up 1 pip, the resulting rate will be 1.2049. Some exchange rates, like the dollar - yen, are only carried out to two decimal points. Fore these currency pairs, a pip is worth 1/100th of the counter currency.

One of the advantages of currency trading over stock trading is simplicity. A currency trader or swing trader could concentrate on a few extremely liquid currencies rather than worrying about thousands of stocks to choose from. For that reason, a novice trader should use this to his advantage and concentrate on one or a few of the major currencies.

Currency Trading vs Investing

There is a very big difference between trading and investing. Currency trading is not investing. It is considered speculation (like day trading stocks). Every portfolio requires a certain portion of speculation and investments. With the low minimum required ($3,000 for a standard account / $300 for a mini account) required to start trading currencies, online currency trading can be the perfect tool to deal with the speculative portion of any portfolio.

The approach that should be taken when investing and trading should be different. Investing requires the thorough fundamental analysis of a security to determine if it is attractive or not. For example, to increase the probability of making a good stock investment, an individual should try to buy that stock at a good price. In order to do that, the investor needs to determine if the current price of the stock in the market is attractive relative to the stocks intrinsic (real) value by studying the company's financial statements, earnings trends, current and future business environment, quality of management, and many, many other factors. In making the investment, the investor is not concerned with what is going to happen to the price of the stock the next day, because investments are long-term in nature.

Speculation (like currency trading) is short-term in nature. A day trader buying euros versus the dollar is not trying to predict what is going to happen to the euro in the next 10 years. He is concerned with the price fluctuations after he enters a position. His goal is for the euro to appreciate in value as soon as possible after his purchase. In order increase his chances of trading successfully, a currency trader will study the past price history of the currency pair he is trading and compare it to the current prices to determine what the price is PROBABLY going to do next.

This study of prices is called "technical analysis. For speculation, trading currencies is a lot more advantageous than trading stocks because a lot less money is required to trade currencies and currency trading offers superior margin requirements and flexible trading hours (24 hours a day)

Although some claim that no speculation is profitable, this is far from the truth. The reason why many disagree with speculation is because of a misunderstanding of what speculation can be. Pure speculation is equivalent to going to a casino and betting everything on the roulette table. This type of speculation will always lead to financial ruin.

Most people think that all speculation is like this. Currency trading, on the other hand, if performed correctly, is a form of controlled speculation, where the chances of success are greater. How does online currency trading become controlled speculation? When the trader treats it as a business and dedicates the time to learn the required skills to increase his chances of success.

Before a currency trader starts trading, he needs to understand how the currency market works, how to operate his trading software, and how to apply technical analysis to the currency pairs he is trading. Stop letting luck determine your outcome in currency trading. Learn the right way.

Calculating Profit and Loss in Currency Trading

The online trading Platform calculates profit and loss (P&L) for every currency position in real time. This allows currency traders to track their gains and losses in real time with every change in the currency market. The table below was designed to give the currency trader and idea of the dollar value of a pip for the major currency pairs.

This is provided as a reference only and does not have to be committed to memory. Please note that the currency pairs where the USD is the counter currency have a static pip value (US$10), whereas the pairs where the USD is the base currency have variable pip values in terms of the USD (these are highlighted in red).

Approximate USD Value for a 1 "pip" Move

Currency	1 pip	Contract Size	Exchange Rate*	Value (1 pip)
EUR/USD	0.0001	100,000 EUR	1.2045	US$10.00
GBP/USD	0.0001	100,000 GBP	1.8084	US$10.00
USD/JPY	0.01	100,000 USD	109.35	US$9.15
USD/CHF	0.0001	100,000 USD	1.2764	US$7.83
AUD/USD	0.0001	100,000 AUD	0.7642	US$10.00
USD/CAD	0.0001	100,000 USD	1.2506	US$7.99

***Prices taken on 15/06/05**

When the USD is the counter currency, it is easier to calculate the value of one pip and the pip value is static.

Example of static pip value:

EUR/USD (using values above) 1 pip = 100,000 EUR x 0.0001 USD / EUR = US$10.00 When the USD is the base currency, an extra step must be performed to convert the pip value into dollars. This is done by dividing by the current foreign exchange rate.

Example of variable pip value:

USD/JPY (using values above) 1 pip = 100,000 USD x 0.01 JPY / USD = 1000 JPY / 117.82 JPY/USD = US$8.49

Currency Trading on Margin

One of the tremendous advantages of currency trading is the huge leverage traders have at their disposal. Trading on margin means that the trader does not need to deposit the entire amount of the transaction. A portion of the value of the transaction is provided by the brokerage firm where the trader opened his account.

For equities, the margin requirement is 25% for positions that are entered and closed during the day and 50% for positions carried overnight (from one trading day to another). That means that a trader only needs to deposit 25% or 50% of the value of the trade respectively. Consequently, the leverage enjoyed by stock traders can be from 2:1 to 4:1.

How does the margin requirement for currency trading compare to equity trading? To trade currencies, the margin requirement is only 1%. That means that a currency trader only needs to deposit $1,000 for every $100,000 of currency traded.

Thus, the leverage is 100:1, much greater than for equity trading. A leverage of 100 to 1 means that every 1% move in the value of the foreign currency exchange rate gets multiplied one hundred times.

Even though the minimum margin requirement with Currency Trading is 1%, the currency trader does not have to take advantage of the entire amount of leverage he has available. The greater the leverage used, the more speculative the trading becomes. The amount of leverage the currency trader should use depends on his risk tolerance and on his desire to take risk.

No matter what the amount of leverage that the trader decides to use is, clients who open accounts will not have debit balance risk; that is, a client can never lose more than he deposits in his account.

Types of Orders in Currency Trading

These are the orders that can be placed when trading currencies online or on the phone:

Market Orders

A market order is an order to buy or sell a currency at the current market price. When placing a market order, the currency trader specifies the currency pair he wants to buy or sell (EUR/USD, USD/JPY, etc.) and the number of lots he is interested in buying or selling. The currency trader will pay the Ask price when buying and the Bid price when selling.

A market order is the easiest and simplest order to place when trading currencies online. With single-click online currency trading platforms, to buy, the trader will simply click a button labelled "BUY" and to sell, a button labelled "SELL." Thus, with a single click of the mouse button, a currency trader can buy and sell currencies almost instantly.

When placing a currency market order over the phone, the same situation described above applies. A trader will ask the dealer to buy or sell a specific number of lots of a given currency after obtaining a two-way quote from the dealer.

Limit Orders

A limit is an order to buy or sell a currency at a specified price or better. In a limit order, the currency trader not only specifies which currency he wants to buy or sell, but also at which price he wants to do so. For example, if a trader places a limit order to buy 2 lots of EUR/USD at 1.2110, the order could only be executed at an exchange rate equal to 1.2110 or lower (which is better for a buyer).

When placing a limit order, the trader also specifies the duration for which the order is to remain active while it is not executed.

Stop Orders

The stop order (also known sometimes as the stop loss order) is an order that is activated when a specified price is reached. A stop order becomes a regular market order when the exchange rate reaches a specified level. Stop orders can be used to enter the market on momentum or to limit the potential loss of a position.

Stop orders are extremely important in foreign currency trading and should be used by all traders that want to participate in the currency markets. Just like for limit orders, when placing a stop order a trader must specify for how long that order is to remain active.

Example of using a stop order to protect a position:

A currency day trader buys 100,000 (1 lot) of EUR/USD at 1.2305 in anticipation of an expected 80 pip rally in the euro. In order to protect himself from an unmanageable loss, the trader places a stop loss order 1.2285 (20 pips below the current price). This way, if the euro drops instead of rises against the dollar, the trader's loss is limited to 20 pips ($200).

Example of using a stop order to buy on momentum:

A currency trader expects the US dollar to rally versus the Japanese yen, but is hesitant to enter a buy order because the USD/JPY is getting close to a short-term resistance at 118.00. The trader instead places a buy stop order 10 pips above the resistance level. His stop is thus placed at 118.10. Unless the USD/JPY goes to 118.10, the currency trader's order won't be activated. By doing this, the trader is waiting for the USD/JPY resistance level to be broken before entering the trade; in other words, he is waiting for the upward momentum on the dollar versus the yen to be confirmed before buying.

Currency Trading Examples

All currency trades involve the buying of one currency and the selling of another, simultaneously. Currency quotes are given as exchange rates; that is, the value of one currency relative to another. The value of the exchange rate in the currency market is determined by the relative supply and demand of both currencies.

When a currency trader places a trade he wants the currency purchased to appreciate in value versus the currency sold. His ability to determine the direction that the exchange rate will move, will dictate his gain or loss in a FOREX transaction. Let's do an example with a currency quote obtained from the currency trading system.

Example of a currency trade

The current bid-ask price for EUR/USD is 1.2120/1.2123, meaning you can buy 1 euro (EUR) for 1.2123 US dollars (USD).
Suppose you feel that the EUR will appreciate in value against the dollar. To execute this strategy, you would buy Euros with dollars and then wait for the exchange rate to rise.

So you make the trade: purchasing 100,000 EUR (1 lot) at 1.2123 (121,230 Dollars). (Remember, at 1% margin, your initial margin deposit would be 1,000 Euros or 1,212.30 USD.) Automatically you set a stop loss of 30 pips in case the Euro goes down, by placing a sell stop order at 1.2096. Having a stop loss in place when trading currencies is extremely important, in case the currency bought or sold goes against you.

Although no one likes to take a loss, placing stop losses in currency trading is part of smart money management and will play a big role in improving a currency trader's potential for success. The example shown here of a 30 pip stop loss is completely arbitrary and should by no means be used in every currency transaction.

As you expected, EUR/USD rises to 1.2236/39. Now you must sell Euros for Dollars to realize any profit. You can now sell 1 EUR for 1.2236 Dollars. When you sell the 100,000 Euros at the current EUR/USD rate of 1.2236, you will receive 122,360 USD.

Since you originally sold (paid) 121,230 USD, your profit is US $1130.
Total profit = US $1130.00 (113% return on an initial margin deposit of 1,000 Euros)

Technical vs Fundamental Analysis in the currency markets

Trading currencies can be done using technical analysis, fundamental analysis, or a combination of the two. Technical analysis involves the study of past foreign currency exchange rates to determine what a currency is likely to do in the future. Even though it is impossible to predict what a currency will do in the future, a currency trader will increase his chances of being right if he applies technical analysis correctly.

Technical analysis is applied on a currency chart of a certain period depending on how frequently the currency trader is willing to buy and sell a currency. For example, a currency day trader may use a candlestick chart with a 30-minute period to generate his signals while a multiple-day position trader may use a 1 or 2-hour chart. The trader can then use various technical indicators in combination with the trend of the specific currency pair he is looking at to make a buy or sell decision.

One common mistake a currency trader makes in applying technical analysis is to forget the reason why technical analysis works and to rely on it blindly. Technical analysis works because many people use it. It is like a self-fulfilling prophecy. When people become overly dependent on technical analysis to trade, they might continuously change their trading style trying to find the elusive magical combination of technical indicators that work or a different trading system. Consequently, they fail to obtain the necessary trading experience that comes from practicing the same thing over and over.

Fundamental analysis in the currency market involves the use of different information and statistics to try to determine what the price of a currency "should" logically do. The fundamental currency trader will try to forecast the future price movements of a currency pair based on his analysis of the economy, political situation, and other factors and statistics of the relevant countries involved.

One big disadvantage in relying solely on what logically "should" happen to a currency exchange rate is that over confidence in the analysis could result in the justification of losses. Your losses must be limited in currency trading.

If a fundamental analyst concludes that the price of a currency should rise versus another currency, then he might be tempted to let his losses accumulate if the price drops instead while he waits (or "hopes") for the price to go up. This is the reason why it is important for a currency trader to also use technical analysis even if he is mainly relying on fundamentals. Many currency traders use a combination of technical analysis and fundamental analysis to trade currencies.

There is also a large number that simply uses technical analysis to trade. Although some people are involved in trading currencies only using fundamental analysis, we do not recommend it.

Trading currencies with a strategy

Currency trading or any other type of trading has to be done via a strategy; that is, a set of steps and principles that the day trader or position trader will follow with strict discipline to improve his chances of succeeding. A trading strategy is like the floor plan of a house. The floor plan has to exist before the building begins.

Imagine building the house from scratch with no floor plan. What a successful endeavour that will be, right? This section was put together to give prospective and experienced traders alike important do's and don'ts about trading currencies online. Taking these steps will improve a currency trader's chances of trading profitably.

Currency trading is only for part of your investment money

In the realm of investing, FOREX trading could be considered speculation. Only a portion of an investor's portfolio should be earmarked for speculation while the rest should be in long-term, fundamentally sound investments. Therefore, online currency trading should only be done with a part of your entire portfolio (not with all of it).

You must limit your losses in currency trading

If a currency trader wants to survive in this business, he must learn to limit his losses. This is one of the keys to smart money management. A trader must have a systematic way to limit his losses and must follow his system religiously. By limiting his losses, a currency trader will protect a greater part of his trading capital when he is wrong. This will allow him to stay in the game a lot longer and improve his probability of trading the currency market successfully.

The best way to limit a loss is by using a stop order. The currency trader will set his stop levels depending on the time frame he is trading (tighter for day traders and less restrictive for swing or position traders) and his technical analysis assessment of the currency market.

FOREX trading is a business and requires training & practice

Why not treat foreign currency trading like any other business? Doesn't it make sense that if a person has relevant knowledge and experience about a business, his chances of having a successful business increase dramatically?

The same is true for trading currencies. A person should take the time to learn important trading principles and practice on a demo account. Open an account and this allows you to practice currency trading in a lifelike environment.

Know the trends of the Currency market before trading

Every currency trader should identify the existing markets trend before trading. The reason for this is that trading in the direction of the existing trend will increase a currency trader's probability of making money. Furthermore, knowing the existing trend will also prepare the trader to take action when a currency changes trend direction.

The currency trader should have answers to questions such as, "What is the long-term trend of the dollar versus the yen?" or "What is the euro doing in the short term versus the dollar?" before jumping into the market.

The FOREX trader should also decide the time frame that he will be using to trade in order to determine which trend will be the most important. For example, a currency day trader should be more concerned with the trend in the very short term, than with the trend for the past year.

Decide what type of FOREX trader you will be

Is your goal to trade actively in the short-term, not holding positions for more than a few hours, or do you want to trade occasionally while holding positions for a few days? Your answer to questions like this one will have important implications on the way you should trade currencies.

For the most part, a currency day trader should be more concerned with short-term trends and near-term support and resistance levels. A longer-term position trader, on the other hand, will not pay much attention to very short-term fluctuations in currency prices and focus instead on the longer-term perspective, as far as trends and technical price levels go.

Each of these trading styles requires a different approach to the market and a different implementation of stop loss levels.

Trade currencies in multiple lots

It is safer to get into a currency position in multiple lots than to do it all at once. Rather than to risk all he's got into one trade, a trader can scale into a position in parts, adding more lots if he is right and risking less if he is wrong.

Lose the urge to trade currencies every day

A common mistake of a novice FOREX trader is to force himself every day because of daily goals or excitement. Not all days are good to trade. Sometimes the currency market is not moving or the currencies are in a level where it does not make sense to take a position. If a trader still forces himself to enter a position on that day because of excitement, his chances of losing money increase.

Sometimes day traders also force themselves to trade because they have daily goals to meet. This is not a wise thing to do because the market does not always provide good profit opportunities.

A trader who forces himself to trade on that day is like a treasure looking for treasure in a place where no treasure exists. That is the reason that daily goals are dangerous. A trader should look to make whatever the market provides on that day rather than a set money figure.

Stick to your trading plan

Sticking to a logical trading style that a currency trader has studied and practices is essential in currency trading. Many traders get paralysed, by over analysing everything and always looking for another magical trading system or indicator to enhance their current system. This is a frequent reason why many traders don't make money. Sticking to your trading system is a must to build discipline in currency trading.

Over 100 years before traditional bar and point and figure analysis originated, the Japanese were using their own style of technical charting that would eventually evolve into the candlestick techniques they currently use today. Many candlestick patterns are similar to those of Western technical analysis but they have several advantages. One advantage is in their descriptive names. For example, the equivalent of a bearish one-day reversal, one where price gaps higher on the open, continues to make new highs but changes course to end up closing lower, is called a "dark-cloud cover." As its name implies, the market is about to get stormy and investors should make preparations (i.e.-sell).
While it is important to view the markets as other participants do, candlestick charting offers other unique advantages. One important advantage comes from the combining of patterns. These often reveal changes in volatility and momentum without the use of oscillators and

other derivatives of price. By using oscillators in addition to candlesticks, the analysis becomes very powerful.

Reading Candlesticks

Like a bar chart, the daily candlestick line contains the open, high, low, and close for the market for a specific day. However, unlike a bar the candlestick has a wide part which is called the "real body". It represents the range between the open and close. When the real body is black (i.e., filled in) it means the close was lower than the open. If the real body is white (i.e., empty), it means the close was higher than the open. See the candlestick illustrations on the bottom of page 3.

The thin lines above and below the real body, which resemble the wicks of the candle, are called the "shadows." The shadows represent the high and low of the day. The shorter the upper shadow on a black body, the closer the open was to the high. A short upper shadow on a white body means that the close was near the high. The relationship between the day's open, high, low and close determine the look of the daily candlestick. Real bodies can be long or short and black or white. Shadows can be long or short as well.

Basic Candlestick Shapes

Long Black Body. This represents a bearish period in the market. Prices experienced a wide range, and the market opened near the high and closed near the low of the period.
Long White Body. This is the opposite of a long black body, and represents a bullish period in the market. Again, prices experienced a wide range, however, the market opened near the low and closed near the high of the trading period.
Spinning Tops. These are small real bodies, and can be either black or white. The small body represents a relatively tight range between the open and close for the period. In a trading range environment, spinning tops are neutral, but they may become important parts of other chart patterns.
Doji Lines. These illustrate periods where the opening and closing prices for the period are the same. The length of the shadows can vary. Doji lines are important in a variety of patterns.

Reversal Indicators

Just like with Western analysis, candlesticks can forecast changes in market direction. Some have only one candle, usually with a specific shape. Others have two or more candles combining simple candles with more exotic shapes.

The simplest reversal pattern is the ***Umbrella*** candlestick. It gets its name from its somewhat remote resemblance to a rain umbrella but can be more objectively recognized by two features: 1) a spinning top real body at the upper end of the entire trading range, with little or no upper shadow, and 2) a lower shadow that is at least twice the length of the real body. The color of the real body is not important.

Umbrellas can be either bullish or bearish depending on where they appear in a trend. If they occur during a downtrend, they are called ***hammers*** and are bullish, as in "the market is 'hammering out' a base." If an umbrella appears in an uptrend it is bearish, and is referred to as a ***hanging man*****.** The latter's ominous name is derived from its look of a hanging man with dangling legs.

The ***engulfing pattern*** is a strong reversal signal, especially after a prolonged trend. It is similar to the Western reversal pattern. Only the real body is important in this formation; shadows are virtually ignored.
The bearish engulfing pattern has a black real body that engulfs the prior day's white real body. This pattern is bearish during an uptrend. Conversely, a white body at the bottom of a downtrend that engulfs the prior day's black body is a potentially bullish signal.
The ***piercing line*** is a bullish pattern. This combination is composed of a long black body followed by a white body. The white body should open lower and then close above the center of the black body. Here, the market gaps lower on the opening and then retraces to close above the midpoint of the previous period's black body. If the white body does not "pierce" this halfway point, more weakness can be expected in the market.

As mentioned earlier, the ***dark cloud cover*** is a bearish pattern. This is the opposite of a piercing line. A strong white body is immediately followed by a black body. A dark cloud cover must have a black body opening above the high of the previous white body as well as closing below the white body's center.

There are various candle combinations called ***stars (hoshi)***, so named because they are located significantly above their preceding candles like a star in the sky. All stars are reversal indicators and are more important after prolonged trends or large moves. A star is a small real body or a doji made on a gap that follows a long real body. Even if the shadows overlap, the formation is still considered a star, since only the real bodies are important.

The ***morning star*** pattern is a signal of a potential bottom in the market. It is aptly called a morning star because it appears just before the sun rises (in the form of higher prices). After a long black body, we see a downside gap to a small real body. This is followed by a white body that closes above the midpoint of the black body made just before the star. The morning star is similar to a piercing line with a "star" in the middle.

The ***evening star*** formation is the reverse of the morning star. Aptly named because it appears just before darkness sets in, the evening star is a bearish signal. Basically, the evening star is similar to a dark cloud cover with a "star" in the middle.

The ***doji star*** appears after a prolonged move, and is composed of a gap and a doji line (remember a doji is when the open and the close are the same price). This is often the sign of an impending top or bottom. Doji stars often mark imminent turning points in the market, but more conservative traders should wait for the next day's body to confirm a change in price trend.
The ***shooting star*** pattern appears at short-term tops in the market, and is a bearish signal. As its name suggests, the shooting star is a small real body at the lower end of the price range with a long upper shadow.

Harami lines are similar to an inside day in contemporary Western analysis. But while an inside day is usually considered neutral, the harami line is an indication of a waning of momentum. The small body of the harami line is contained within the long body directly preceding it. (Harami appropriately means pregnant in Japanese). If the harami line is also a doji, it is referred to as a ***harami cross***.

These patterns indicate that the market is at a point of indecision and a trend change, or a reversal, is possible. The harami cross pattern is useful in forecasting trend changes - especially after a long white body in an uptrend.

Continuation Indicators

Candle patterns can also indicate that the market will continue its current trend. There are many types that occur but for this introduction we'll only briefly cover one, the ***window (ku)***.

A window is the same as a gap in contemporary western analysis. With bar charts, we say "filling in the gap," the Japanese expression is ***"closing the window."*** Our experience is that gaps often become support or resistance areas. And windows (i.e., gaps) are viewed in the same context as support or resistance. Shadows are also considered in closing the window. Unclosed windows signal continuation of the trend

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Dojis

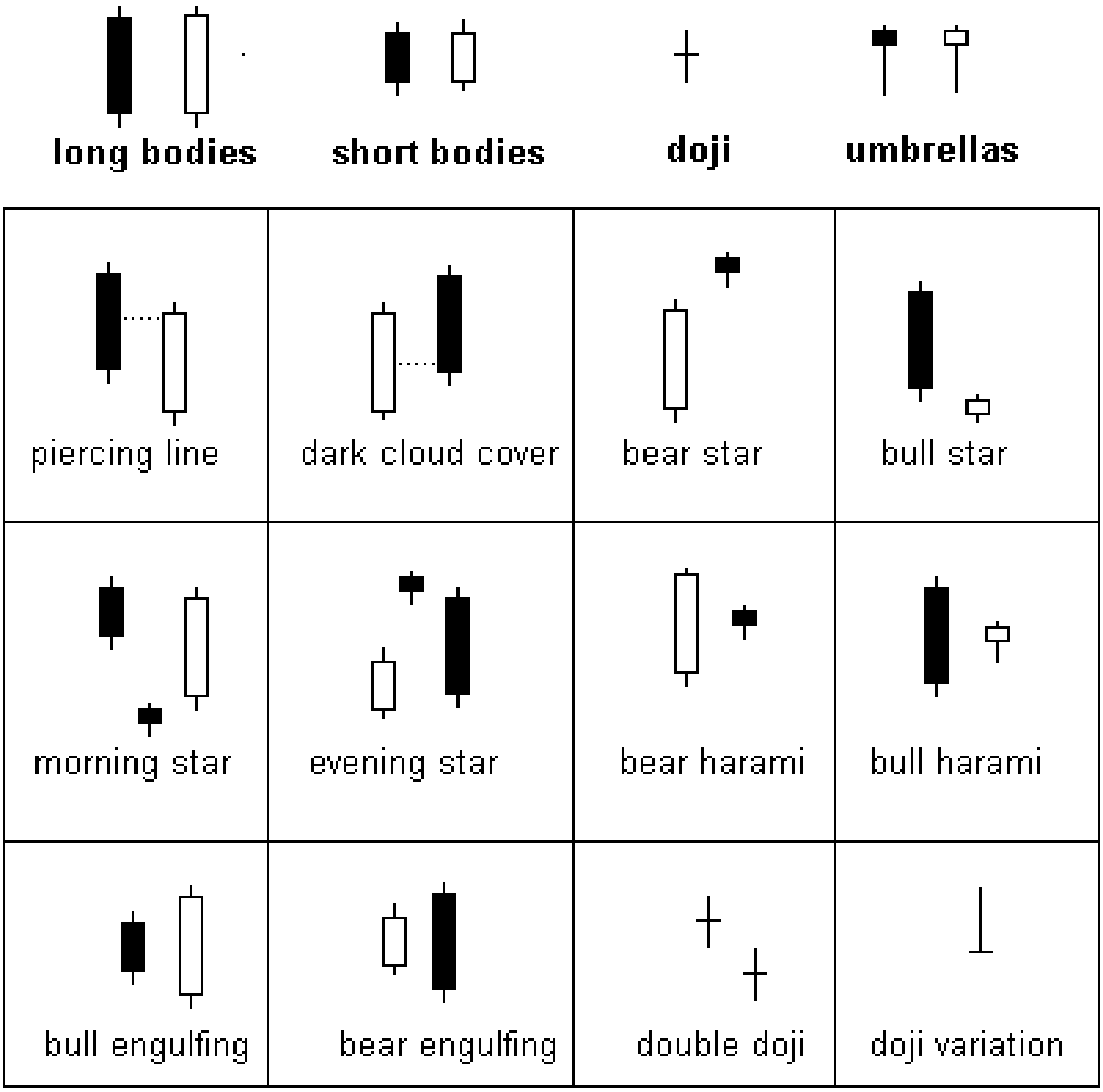
Doji lines are important enough to get their own discussion. Basically, dojis reflect indecision which makes sense since the market closed unchanged for the day after trading significantly higher and lower intraday.

If you see two or more doji lines within a short time in a market where this normally does not occur, then a sttrong move is possible. ***Double dojis*** may foretell an increase in market volatility. Option traders who are confident of price direction could use this signal to buy options (assuming volatility levels are attractive).

They could benefit from premium expansion based on increased volatility and a significant price move. For those not confident about the direction of the break, a long straddle or strangle (or similar long volatility plays) may be considered.

Doji days can become support or resistance, usually on a short-term basis. And a series of three doji lines after a prolonged move could signal a rate and important top or bottom.

Variations on doji patterns have interesting names like rickshaw man (very long shadows) and gravestone (no lower shadow and a very long upper shadow). However, their significance remains the same as other dojis.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