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Trading PLACES

Understanding the ups and downs of financial markets

Taking your first step in financial markets can seem daunting, but with a wealth of resources and platforms available to retail investors, they have become more accessible than ever. In this ebook, we guide you through the fundamentals you need to launch your own journey into the world of trading.

1. Understanding the Market Basics

2. CFDs on Stocks & Indexes – Setting Up Your Trades

3. FX – Trading the World's Biggest Market

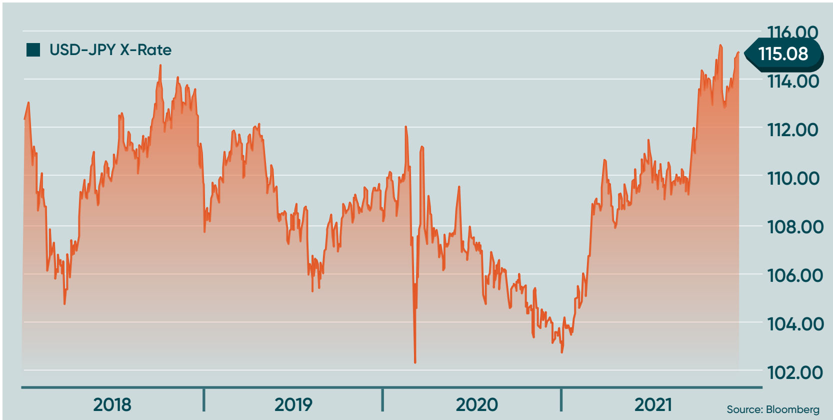
4. CFDs on Commodities – Making the World Go Round

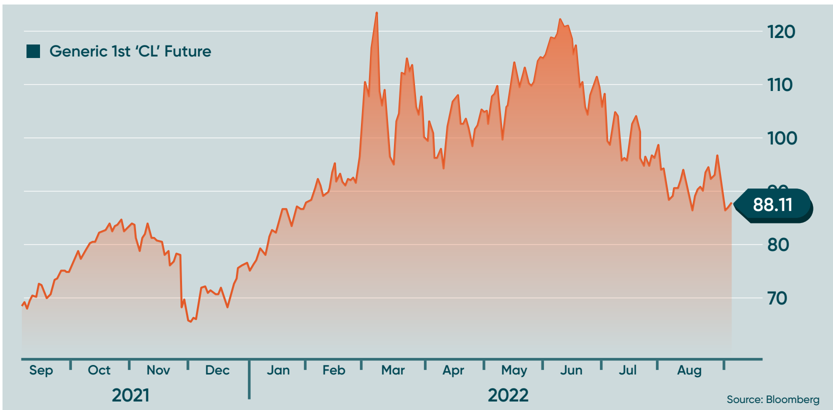
1 Understanding the Market Basics

As long as humans have had goods and assets to trade, there have been markets. Even in today's world, where financial markets can appear highly complex to the average person, the market system boils down to the same essential thing: buyers and sellers coming together and wanting the best prices for the most profit.

The majority of non-professionals (known as "retail investors") who participate in modern financial markets prefer a "buy and hold" strategy – investing in stocks, bonds or funds for the purposes of long-term value growth. History has shown that this is an effective way of growing wealth, provided investors make solid choices and stick with them, perhaps making small adjustments from time to time.

History also showed that markets go through regular cycles – periodically seeing extended periods of growth (known as "bull markets") and decline (known as "bear markets"). Within these extended cycles are smaller mini-cycles, which can play out over months, weeks, days, and even hours. The more regular these cycles are, and the larger the peaks and troughs in the market, the more "volatile" a market is said to be.





Over the course of four years, the US Dollar-Yen rate (top) was relatively stable, moving within a narrow range. By contrast, crude oil prices (bottom) recently experienced a period of volatility.

For the retail investor with a long-term buy-and-hold portfolio, these cycles can be a psychological challenge. It can be difficult to watch and do nothing when the value of your investments has dropped 10%, 20%, or worse – as happened this year, or during the Global Financial Crisis in 2008.

Many investors succumb to panic and sell, only to regret it later when the growth cycle returns.

So, is there anything investors can do, apart from just sit and wait?

The answer is yes.

1 Understanding the Market Basics

Short-term advantages

Long-term investments make financial sense, but investors can also use short-term trading to their advantage. Allocating a small percentage of investable capital to trading instruments such as Contracts for Difference (CFDs) offers specific opportunities not available to buy-and-hold investors.

Short-term trading can:

- Smooth out the volatility of a long-term portfolio.
- Hedge against unexpected movements in portfolio holdings.

CFDs are an example of a "derivative." These are contracts that derive their value from an underlying asset. If you trade a CFD on Microsoft, you are not buying and selling Microsoft shares, but a contract of which price moves up and down in tandem with the Microsoft share price.

CFDs offer several advantages to retail investors:

- You can trade many different markets without owning them personally (stocks, indexes, foreign exchange, commodities, funds, cryptocurrencies).
- The initial stake for trading CFDs can be much smaller than on the underlying market value. By employing "leverage" (see next section), CFDs enable an investor to put up only a fraction of the total contract value.
- CFDs enable investors to create trading opportunities from both rising and falling prices, and high market volatility.
- CFD prices move in lockstep with the underlying market, so they are simple to track.
- Some CFD trading platforms enable potential investors to practice trading for free before committing their own money.

In essence, trading CFDs is straightforward. You Buy a CFD contract if you think a price will rise and Sell a contract if you think the price will fall.

If you are an inexperienced trader, however, there are several steps you should take before jumping in.

Before you begin

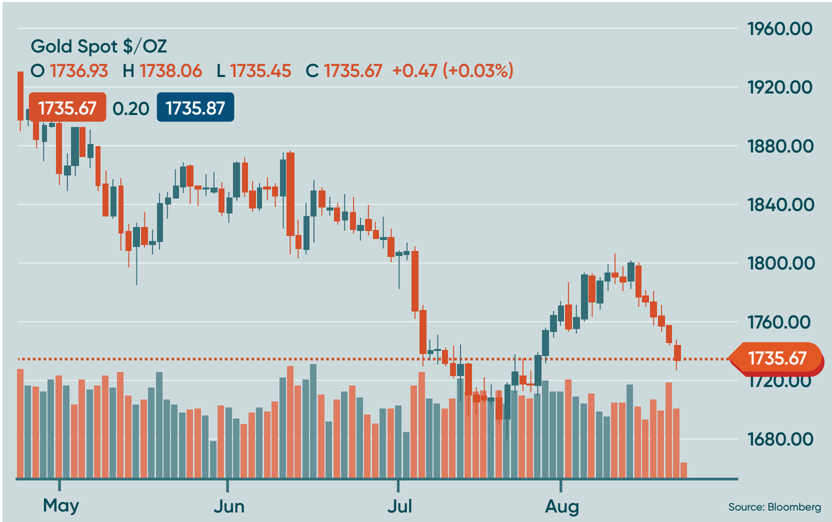
Throwing money into CFD trading before you understand the markets you want to trade, and how derivatives work, is like climbing into a car for the first time and trying to drive without taking lessons.

Firstly, consume every possible education resource you can find. One such platform - Vantage's Academy - contains a wealth of information and ideas, ranging from analysis to markets news, to free webinars and trading guides. Take the time to absorb as much of this as possible and get into the habit of following business and financial news every day.

Secondly, learn the terms of trading and use a Demo trading account to get familiar with your trading environment and how markets function, whether you're using ProTrader, MetaTrader, or another platform.

1 Understanding the Market Basics

Learn to Read the Charts



This Gold price chart can look like a confusing jumble to a newcomer, but once learned, it can be relatively simple to understand.

Near the top is a row of six numbers:

O – The price of gold when trading Opened for the day.
H – The Highest price that day.
L – The Lowest price that day.
C – Current price (or Closing price for previous trading days).

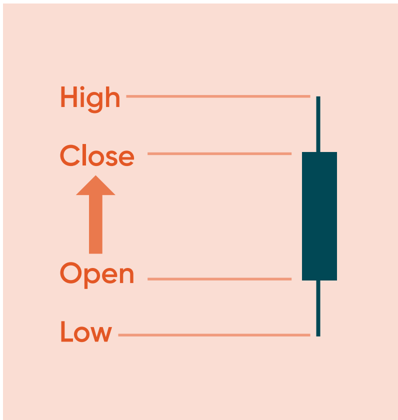
The number to the right of the Closing price shows how much the price moved up (green) or down (red) that day (in this example, the price has increased US$0.47). The number in brackets at the far right expresses that price movement as a percentage.

Beneath that row is a set of three figures:

1735.67 – is the "Bid" price if you want to Sell a Gold contract.
1735.87 – the "Ask" price to Buy a Gold contract.
0.18 – is the **"Spread"** between those two prices. The "Spot" price (the actual price of an ounce of gold at that very moment) is halfway between the Bid and Ask prices. Brokers make money from these small variations from the Spot price, and Spreads vary from asset to asset.

The price graph dominates the chart. This particular example, comprising a series of red and green boxes, is called a **candlestick** (or candle) chart, and is the most commonly used by traders. Each box represents a day's trading and can be interpreted as shown. (When the price drops, the box would be red and the Close-Open positions would be reversed.)

The red and green bar below the price chart shows the Trading Volume that day (the amount of shares that changed hands).

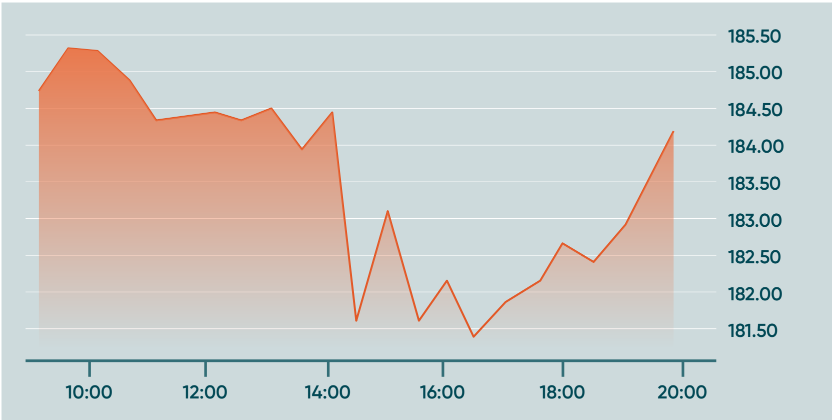


In the next section, we'll use the example of Stocks and Index markets to show how to set up trades, use leverage, protect yourself from risk, and use CFDs to hedge your existing share portfolio.

2

CFDs on Stocks & Indexes – Setting Up Your Trades

The stock market is the most popular entry point into financial trading for retail investors. Most of us understand the basic concept: a company sells shares to investors, and the price of those shares rises and falls based on how investors feel about that company's prospects.



If you're buying companies for their long-term prospects, why bother with short-term trading?

To get a different perspective, look at this graph on the right of a company's one-day share price movement. The stock opened at about 184.75 and closed at about 184.25. For the buy-and-hold investor, this is a small and insignificant change, since that position is being held for the future.

But if you were to look at the swings in price during the day – a steep drop, followed by a recovery, with several peaks and troughs in between. For a CFD trader, that's at least two opportunities to generate income from a stock which daily price would be reported as "little changed."

Getting started

Of all markets, stocks are the most common to follow.

To start off, focus on companies, countries, or sectors that you already know something about, or which interest you. Read up on them, follow news about them, study analyst reports, learn about the sectors in which they operate, and familiarise yourself about the factors that affect their share prices: earnings reports, industry outlooks, government policy, international trade, supply chains, labor issues, executive reputation, analyst ratings ... all these can impact market sentiment.

It cannot be overstated how important market knowledge is. Far too many new traders lose money because they fail to understand the market. The Vantage education page is an excellent starting point.

Alternatively, many traders invest in Indexes or Index Funds, which mirror an index. An index can be broad (like the Standard & Poor's 500) or more sector-focused (like the Nasdaq). Index investing has several advantages: **it spreads risk** (when one company or sector is dropping, others may be rising), reflects **market momentum** (positive sentiment in one company or sector often spills over to others), and **saves a lot of time** (index investors don't need to research specific companies). Indexes have also historically delivered better long-term returns than managed funds.

Once you're familiar with the assets you want to trade, spend a little time on your Demo account to get a feel of the market.

Next, you should consider **developing a trading plan and stick to it**. This is essential for every market you want to trade, because it defines what you want to achieve, how to achieve it, and also your

2 CFDs on Stocks & Indexes - Setting Up Your Trades

exit strategy when things go wrong. Sticking to your plan helps you to avoid the panic decisions of **emotional trading**, which is a trader's worst enemy. The most successful traders are usually the most disciplined.

Second, prepare a **trading diary**, and keep a record of every trade, profit and loss. This helps you gain perspective when things might appear to be going badly (for example, two failed trades in a day might take an emotional toll, but seeing that you've made a profit over the past month will ease the pain).

Answering the following questions can help you draft a plan:

- Why am I trading? ("To hedge my other investments, become a ful-time trader...?) Set realistic targets.
- Which markets will I trade, and how much do I know about them?
- What's the total size of my investment pool? (This should only be an amount you can afford to live without.)
- What's the maximum percentage of this money I will invest in each trade?
- What's my target percentage outcome from each trade?
- What percentage of each trade can I accept losing?

The following sections will guide you through the process of trading stocks/index CFDs, and these basics apply to other markets, too.

Setting up trades

Before making a trade, answer a few key questions.

Long or Short? First, decide if you think the price of your chosen asset will rise or fall. If you think it will rise, you Buy a CFD ("go Long"). If you think it will fall, you Sell ("go Short").

Allocation: Decide how much you can afford to lose. As a general rule, allocate no more than 10% (preferably less) of your total trading fund to any one deal.

Setting margins: It's extremely important to understand the concept of "leverage" and "margin" before you start trading derivatives such as CFDs.

A 1:20 margin means you must invest $1 for every $20 of the total deal value. For example, if you buy CFDs equivalent to $2,000 worth of Shopify shares, you must commit $100 of your own money.

Be sensible with leverage. If you don't protect your trade, losses can spiral out of control very quickly if the market moves against you.

Loss protection: Use **Stop** and **Limit Orders** to protect your money; these place a fence around your trade and ensure your losses cannot exceed a certain amount. Stop Orders trigger the closing of a position at a pre-determined level. Limit Orders lock in profits by closing trades at a pre-set price (this is to safeguard against volatility).

2 CFDs on Stocks & Indexes - Setting Up Your Trades

Making trades

Now we're ready to put it all together with a trading example:

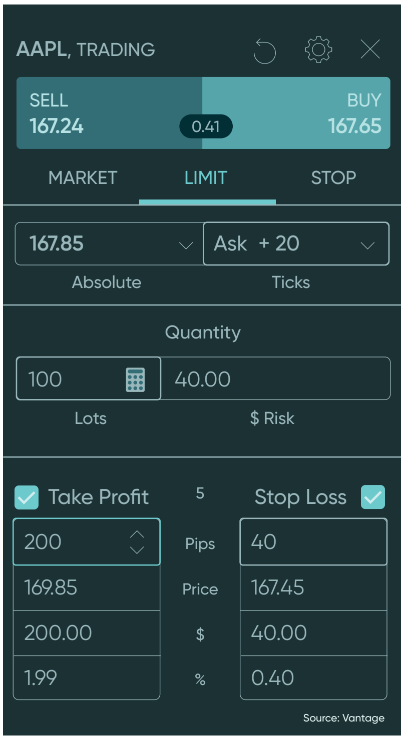
Joe and Holly are new to trading. They believe Apple Inc. shares will rise after an upcoming earnings announcement, so they decide to buy 100 Apple CFDs, which are trading at 167.65. Purchasing 100 actual shares would cost $16,765. With a 1:20 margin, the trade will require $838.25 of their capital (167.75 x 100 / 20).

They are initially targeting conservative gains while they learn the market, so they enter a Limit Order at 20 ticks above the buy price (1 tick = $0.01). This will close the trade automatically if the Apple share price rises 20 cents to 169.85, and they will make $0.10 per tick from the increase. So their potential profit is:
$0.10 per tick x 20 x 100 lots = $200

They are keen to minimize any losses, so they enter a Stop Loss order that will close the trade if the price drops to 167.45, limiting their potential loss to $40.

Using CFDs to Hedge: If Joe and Holly already own Apple shares in a long-term portfolio, they could use CFDs to offset any downside risk. For example, if they were concerned that poor earnings might impact the Apple share price in the short term, they could Sell Apple CFDs, which would take advantage of a decline, and balance out any short-term loss in their portfolio.

In the next section, we look at trading Foreign Exchange, how to monitor the markets, and offer more essential trading tips.



The information is intended for educational purposes only. Past performance is not an indication of future results.

3

FX - Trading the World's Biggest Market

Foreign exchange (FX) is the world's biggest market. About $5-6 trillion worth of currency changes hands every day. Most of it flows among financial institutions, bundled into large "Lots" of 100,000 units each. Previously, the size of these Lots placed forex trading beyond the average investor, but the emergence of online platforms has made the market much more accessible and popular among retail traders.

Currency trading is not quite as simple as the transactions we've all done at the money exchange booth. First, it's important to understand the market.

There are three basic types of contracts in the forex market:

Spot: Transactions involving the immediate exchange of two currencies.

Forward: An agreement to buy or sell a set amount of currency, at a set rate, on a set future date (or a date range).

Futures: A version of a forward contract that is legally binding.

Understanding Rates

Exchange rates are quoted in pairs, involving three-letter codes – most of us are familiar with major ones like EUR, USD, or AUD.

The currency quoted first is called the **Base** – this is the currency you are Buying (or Selling, if going Short).

The second currency in the pair is called the **Quote**.

So, if you believe that the British pound is going to strengthen against the Australian dollar, for example, you will buy the GBP/AUD pair – and Sell the same pair if you think the AUD is going to get stronger (using the same Stop and Limit protection strategies we discussed in Section II).

The vast majority of the world's forex trading involves seven currencies known as **the Majors**: the US dollar (USD), euro (EUR), Japanese yen (JPY), British pound (GBP), Canadian dollar (CAD), Swiss franc (CHF), and Australian dollar (AUD). Trading in these pairs is highly "liquid", which means there is always a high volume of money flowing in and out of the market. One rung below the Majors are the Minors (including the Singapore and Hong Kong dollars), then Exotics (including the Hungarian forint and Turkish lira). Trading "illiquid" Exotic pairs can mean spreads are wider, and the markets are slower moving.

FOREX

Symbol	Last	Chg	Chg%
EURNZD	1.61984	0.00000	0.00%
EURPLN	4.74802	0.00000	0.00%
EURSEK	10.63248	-0.00064	-0.01%
EURSGD	1.38848	0.00011	0.0
EURTRY	18.03494	0.00060	0.00%
GBPAUD	1.69789	-0.00039	-0.02%
GBPCAD	1.52330	0.00010	0.01

Source: Vantage

A typical view of currency pairs whereby the first three letters represent the base currency, and the last three letters represent the quote currency.

Like every other market, currency rates are driven by supply and demand, and by confidence. If the level of investor confidence in a country's economic prospects grows, its currency is likely to strengthen, and vice versa.

3 FX - Trading the World's Biggest Market

Pips

Forex rates tend to move in very small increments, which is why prices feature so many decimal places, and the Lots traded on the market are so large.

Each movement in value is called a **Pip**, which is usually the fourth decimal place. So, if the euro strengthens from USD 0.99259 to USD 0.99269, that movement is called one pip. The main exception among the Majors is the USD/JPY pair, for which a pip is the second decimal place.

This is important to know, because when trading forex CFDs each pip of movement will correspond to a certain gain or loss in your trade.

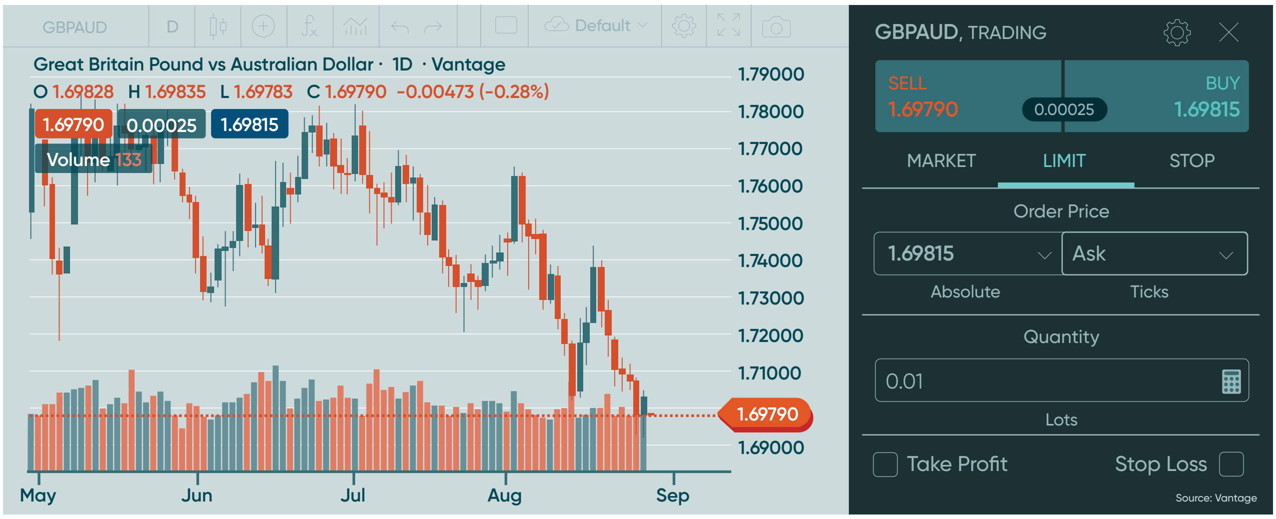
Pros & cons of trading forex CFDs

Pros:

– Markets are open 24 hours, which means you can trade even on the weekends.
– Trade is highly liquid.
– CFD traders can commit much smaller amounts of capital to each trade compared with the open market.
– Markets tend to be less vulnerable to manipulation.
– Forex markets are fast-moving, offering potential for quick returns.

Cons:

– High volatility means traders need to be alert and nimble.
– Market is weighted in favor of large institutional traders.



A forex price and trading ticket screen. Round-the-clock trading and a highly liquid market present attractive opportunities for forex CFD traders.

3 FX - Trading the World's Biggest Market

Preparing to trade

If you're new to forex trading, it is recommended to start with the major pairs. Major pairs are less likely to deliver unwelcome surprises, and it's easier to keep track of the factors that influence changes in rates.

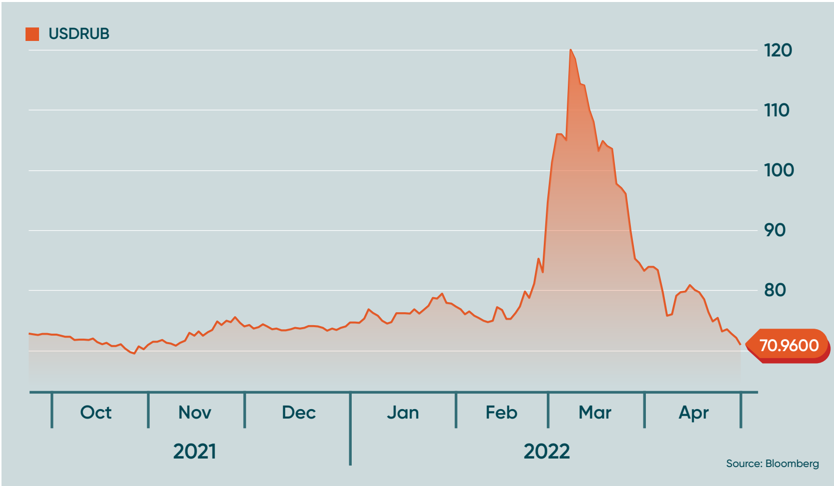
As always, knowledge, education, and discipline are the keys to success. Tap into Vantage's forex education resources before committing your money.

Make a plan – Next, decide how to plan your trades. Forex traders, like all financial-market professionals, employ two approaches:

1) Fundamental

Traders use real-world information about their market to inform their decisions. For instance, if the Australian government announces disappointing trade figures, traders might Short the Australian dollar (e.g. Buy USD/AUD CFD contracts).

There are a range of forces that move money markets, and it's important to know what they are and to keep track of them. They include:



The impact of market shocks: after months of stability, the invasion of Ukraine triggered a plunge in the Russian Rouble against the US Dollar.

– Central banks: Central-bank policy is a key factor affecting exchange rates. Market reactions to changes in policy (interest rates, money supply, bond-buying) often push currencies higher or lower.

– Credit ratings: These are scores assigned to countries by agencies such as Moody's and Fitch. The score is meant to gauge each country's ability to pay its debts. A positive or negative adjustment in these ratings is often reflected in exchanges rates.

– Economic data: Governments release regular scheduled announcements and data: GDP, inflation, manufacturing, trade, etc. Any surprises can boost or hurt demand for that country's currency. Keep these dates in your calendar. Informed traders who track economic news closely can often pre-empt these announcements.

– News: Keep abreast of political and economic news. Markets move on trade tensions, political developments, military conflict, decisions by major institutions like the World Bank or IMF. Staying informed helps to shield you against market shocks such as the war in Ukraine, which sent the Russian ruble plummeting in March 2022.

2) Technical

Traders employ mathematical models to identify past patterns in the behavior of a market and use those patterns to spot unfolding trends and predict future direction.

Most professional traders use a combination of these two approaches. Brokers such as Vantage have integrated solutions like MT4 and MT5 that offer a range of technical tools that can be applied to price charts, such as Moving Averages, and the Relative Strength Index. Though they could seem complex, use your Demo account to learn the basic signals these tools offer.

Practice for a while, combining your observations of fundamentals with technical signals to build your market experience.

4 CFDs on Commodities – Making the World Go Round

Until recently, the trade in commodities was all physical – the buying and selling of food, materials, and fuel that has sustained human civilization for thousands of years. These days, most commodity transactions exist only on paper for the purposes of speculating on prices, or hedging future costs. The vast majority of modern traders have no desire to take delivery of 25 tons of copper or 5,000 bushels of soybeans.

Commodities are split into two general categories: **Hard** (things that are mined and extracted from the earth, like metals and oil) and **Soft** (things that are grown or farmed, like wheat or orange juice).

Most trading comes in the form of **derivatives** that are based on current prices or speculation on future prices. Like forex, commodity markets trade in very large contract sizes (1,000 barrels of oil, 5,000 bushels of wheat) that place them beyond the reach of the average investor.

By using CFDs, however, retail traders could enter these highly liquid markets with smaller capital.

Advantages of trading commodity CFDs

Diversification: Historically, commodities have a low correlation with other markets (meaning price movements mirror each other less frequently). This makes them a useful tool in balancing your portfolio.

Volatility: Commodity prices are historically more volatile than stocks and forex (coffee, for example, has had a volatility range of 11-90% over the past decade, compared to 4-15% for the Dollar Index). While this is a headache for long-term investors, for CFD traders it offers ample opportunities to benefit from large daily price swings.

Hedging: In today's inflationary environment (of which rising commodity prices are a defining feature), traders can consider diversifying their portfolios to capture potential price gains.

What moves the markets?

Naturally, supply and demand lie at the heart of commodity pricing, more transparently perhaps than other markets.

There are two stark recent examples of this: the plunge in crude oil prices in the early months of the Covid-19 pandemic as countries went into lockdown, people stopped commuting, and planes were grounded; and the surge in wheat prices after the invasion of Ukraine (Russia and Ukraine accounted for more than a quarter of global wheat supply before the war).

In March 2022, wheat prices surged after the Russian invasion of Ukraine threatened global supplies – a stark example of the power of supply and demand.

4 CFDs on Commodities - Making the World Go Round

For a new trader, the challenge is to learn what factors influence supply and demand in the markets you want to trade. What drives the biggest market players to buy or sell over 29 billion futures contracts per year.[1]

It's worth remembering that markets respond to **perceptions of future supply and demand**, not necessarily actual supply and demand.

The supply cycle

Prices of most commodities move in a broad long-term cycle: strong supply forces prices down –> lower prices discourage production –> reduced production cuts supply –> low supply drive up prices –> rising prices encourage production, and so on. While this information doesn't impact daily price changes so much, it pays to know where a commodity stands in the cycle.

Consumer demand

Organizations and governments produce hefty amounts of data on consumer demand, and traders pay attention to these because they flag long-term trends that affect prices.

The world economy

Follow the release of macroeconomic data, which can contain clues to future prices. Why did record crude prices prompt Indonesia to ban palm oil exports? What effect will a collapsing Chinese real estate market have on the price of copper? The commodity world is a complex web of intricate links – learning about them increases your effectiveness as a trader.

The dollar

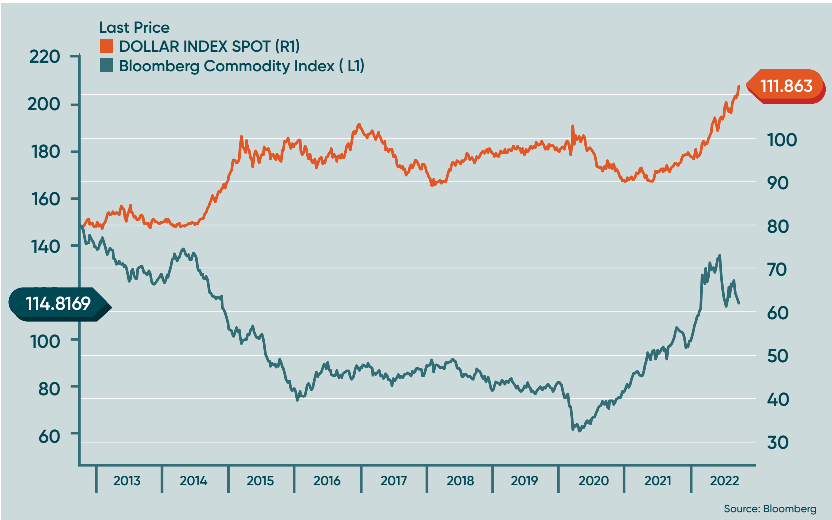
Commodities are priced in U.S. dollars. If the dollar is strong, commodities become more expensive in other currencies, which tends to force a repricing in U.S. supplies, forcing prices down.

Weather

Which countries are the largest suppliers of which commodities? Are they being affected by droughts, floods? Traders in agricultural commodities keep a very close eye on weather reports and forecasts during key crop periods.

Geopolitics

Labor strikes, military conflict, trade disputes, and political strife can all impact supply lines between among major trading nations.



The US dollar tends to have an inverse relationship with commodity prices. In the chart above, the Dollar Index, which tracks the value of the Dollar against a basket of foreign currencies, increases in value as commodity prices decrease.

1 Source: FIA

4 CFDs on Commodities - Making the World Go Round

What markets can I trade?

The Vantage platform offers CFDs on a range of major commodities:

Energy: Crude Oil, Natural Gas, Gasoline
Precious Metals: Gold, Silver, Palladium, Platinum
Base Metals: Copper
Soft Commodities: Cocoa, Coffee, Cotton, Orange Juice, Soybeans, Sugar, Wheat

Each of these markets has its own unique supply-demand characteristics. Professional commodity traders tend to specialize, because the array of factors that affect each market can be complex. So, it's worth selecting one or two commodities and learning as much as you can about them, rather than throwing yourself into generalized trading.