Understanding of forex trading

Our first grade in forex literacy is for understanding how to read the price quote. In forex, currencies are always quoted in pairs. In other words, it's only possible to value a currency in terms of another one. If you want to buy 100 Euros, how are you going to pay for it? If you were to pay in euros, you'd not be currency trading, and when you use another currency to fund your purchase of the euros, you're actually creating a forex quote.

It's actually quite easy to evaluate forex quotes once you get the hang of it, and the fastest way to learn is by considering some examples:

EUR/USD 1.2786

So what does the above quote tell us? What it says is that 1 Euro is able to buy 1.27 units of the US currency. Or, continuing on our previous transaction, we would have to pay

127 USD for 100 Euros we wanted to buy.

But in fact this value is only the average of the bids (price to buy) and offers (price to sell) for a currency pair at a particular time. The bid-ask spread is usually very low for the most liquid pairs, such as the EUR/USD, but at times of illiquidity in the markets, as before a statistical news release, or a central bank decision, the spread can widen to much greater levels.

The quote represents the best pricing that the world market offers for a currency pair at a particular moment. A quote on a computer does not usually include all of the offers and bids all over the world, but because of the very liquid nature of the forex market, any significant difference in quotes across different parts of the world is very quickly eliminated through computer-based, automatic arbitrage, and consequently, except at times of market turmoil the difference between regional quotes is quite low.

So let's say return to the EUR/USD quote. Our quote is at 1.2786, and the bid-ask spread is at 0.009, as stated by the broker. What this means is that there's a difference of 0.9 cent between what you pay to buy the same currency pair, and what you'd receive if you were selling it. There's always a spread in even the most liquid markets, but the spread is

usually widened further by the brokerage firm, so that it can make a profit from the individual traders' deals.

The important point to keep in mind when evaluating quotes is that one quote is valid for only a fraction of a second. At times of market tension, great fluctuations can occur within the scope of one minute, rendering the quote almost useless. Despite the great focus on prices and price patterns among many traders, it's always advisable to keep the time of the day, of the year, and the emotional atmosphere of the market in mind while deciding on what we should do about a particular quote. For example, quotes during the last few weeks of the year, or in the Thanksgiving week, or at about an hour before the opening of the US market have far less value in determining future price direction and trends than those seen during an ordinary business day at regular hours. So, to repeat, the trader must not only know the price quote at a given moment, but also the seasonal, hourly, and emotional backgrounds that influence the quote before he decides to make a trade on the information.

That skill can be gained through practice, and is perhaps easier learned through experience than reading.