KEVIN DAVEY

Would you rather be a 'shark' or a 'minnow?' Kevin Davey shares what needs to be done to survive and thrive as a 'minnow' in the Forex ocean

How to Swim the Forex Ocean . . . and not get Eaten by Sharks

I must be an idiot. You know – the kind of person who drives the wrong way on a one-way street. Someone who pushes a door to open it, rather than pulling the handle like the sign says. A plain old idiot – why do I put myself in this class? Simple – the Forex market.

I never realized the Forex market was as easy as following some color-coded signals, clicking the mouse and counting the profits. All these years I could have been making huge amounts of money – so easily a child could have done it. I should stop being an idiot and just attend that free Forex seminar that is conveniently being held at a local hotel, and learn all about what I have been missing.

Sure, I finished second in a worldwide futures trading contest in 2005 with a 148% return, but it took nearly 15 years to get to that point. Even today, trading futures is a constant emotional and mental struggle. I should have been trading Forex all along, since everyone on television and in direct mail tells me it is so easy.

Except, I know it is not that easy.

In reality, Forex is an 'ocean' of professional traders (sharks), just waiting to devour the little minnows. If you have not figured out who the minnows are in this picture, well, my friend, just take a quick look in a mirror.

So, how can you evolve from 'minnow' status into full-fledged 'shark?' My 15 years of speculating experience, primarily in the futures market and more recently the Forex market, points to three major areas:

Know the market
Know the competition
Know your plan of attack

Fulfill all three of these requirements and your chances of avoiding the 'sharks' rise like the ocean tide. Neglect even one of these areas and you become 'shark' bait.

Know the Market

The first step to swimming in the Forex 'ocean' is to know what the waters are like. Do you know what a 'pip' is? If you do, can you calculate the pip value in US dollars for the EUR/USD pair? What about the EUR/JPY pair? If not, it is important that you learn the basics first.

Take time to learn. We will talk about the competition later, but rest assured, your competition knows all about the Forex market. Where do you learn the Forex basics? Websites and books abound on the Forex market – it is an excellent idea to read a few of these books and use the Internet to find good educational (not just sales hype) sites.

One key item to learn about is transaction costs. Even though most Forex dealers do not charge commissions when you make your own trading decisions, there is still a trading cost. It is called the 'bid/ask spread.' This spread can range from \$20 to \$80 per trade, and is something that must be overcome in order to be successful. All things being equal, trading pairs with small bid/ask spreads is the best way to go.

Once you do enough research, you will probably come to the conclusion that you should focus your efforts on the major currency pairs. This would be the ones that include the US Dollar, Japanese Yen, British Pound and Euro. Forex pairs with these currencies typically have the lowest spreads, the highest liquidity and the most fundamental information available. But do not take my word for it – research the market until you feel comfortable with whatever pairs you want to trade.

Know Your Competition

Why should you bother to know your competition in the Forex market? Simply put,

Forex is a zero sum game – for every dollar someone wins, someone else loses that dollar. Taking from others is the only way that wealth is created in the Forex market. It is not like the stock market where almost everyone (except a small minority of short sellers) benefits from rising stock prices. Forex is definitely not a 'win/win' situation, but rather 'win/lose.' Knowing this rule and recognizing your competition's tendencies, can help to give you that elusive edge.

Who are the major players in Forex? Banks, hedge funds and multinational corporations are all big players and they make a lot of money from Forex. One automobile company recently attributed a large portion of its earnings to its Forex trading activities. These groups should strike fear into the little 'minnows' because these groups are the professional 'sharks.' These organizations trade day and night, know the 'ins and outs' of the market and eat the weak. Big moves in the market are usually the result of the activities of professionals, so following their lead and following the trends they start may be a good strategy.

In the same waters that the professional 'sharks' swim, there are also a lot of 'minnows.' They are also your competition, so knowing their tendencies can help you exploit them. For example, unsophisticated 'minnow' traders are likely to put stop-loss orders at obvious support or resistance levels. Knowing this, you can exploit this tendency and feed on them. Also, think about the first 'sure thing' chart formation that you ever learned about. Chances are that new traders are just learning about that formation now, so you could fade their trades and likely do all right.

Think of it this way – defeating a foe sitting at his desk in his home office trading the Forex market in his bunny slippers is probably easier than defeating an MBA with a \$5000 suit who trades via complex neural network arbitrage programs. So, try to mimic and follow the 'sharks' and eat the 'minnows.' This is where having a plan to make you a more agile 'minnow' or even turn you into a 'shark' is critical.

Know Your Plan of Attack and Take Steps To Not Be a 'Minnow'

Once you really know the Forex market and really know the competition, chances are you will be very scared. If you are not scared, you probably need to return to Steps One and Two and spend more time learning. The Forex market is very difficult and you are a 'minnow' swimming in some deep waters. Do not kid yourself into thinking Forex trading is easy.

Once you realize that Forex is tough work, you are ready to determine your plan of attack. There are really two ways to do this – either on your own or with an advisor. If you decide to do it on your own, plan on spending from 500 to 1000 hours of your time and \$2,000 to \$5,000 for software, books, seminars, etc. Like it or not, that is what it takes to develop a good trading system. If you try to short-change this effort, your trading results will likely reflect that fact. You get out only what you put in.

An alternative is to use an advisor or an advisory service. This will take less time than going it on your own, but you must be willing to perform 'due diligence' on any advisor you may find. Blindly following signals from an unknown Internet service or turning your money over to an unknown advisor is a sure way to lose your money.

Conclusion

So there you have it – a brief overview of how to swim the FOREX waters. The key, I have found, is to treat Forex trading as a business, not as a hobby. Take the time to really understand the markets and what moves them. Realize that you are up against professional traders who will take advantage of any weakness in your trading system or your trading psychology that they can find. Finally, have a plan and be willing to invest the time and money to develop your plan. If you perform all three of these tasks, you might just find yourself surviving and thriving in the waters of the Forex ocean.

Happy swimming!

Kevin Davey finished in 1st place in a worldwide futures trading contest in 2006, with a 107% return. In addition, he finished in 2nd place in a worldwide futures trading contest in 2005, with a 148% return. Kevin can be reached at kdavey@kjtradingsystems.com or via his website http://www.kjtradingsystems.com