TYPES OF FOREX MARKET ANALYSIS

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Foreword

Trading is an incredibly hard past time. Many people have become rich by trading in the forex market but, nevertheless many others have lost. Education is key to your development but with so many websites, videos, and general material it's hard to know what will help.

It's always best to stick to the basics, and then move forward to a more advanced level. The eBooks give you the basic information and look to build on that base knowledge to leave you in the best position to continue or begin your trading journey. The information provided is not just for beginners but can be used by traders with different skill sets, even as a simple reminder.

We have taken all reasonable measures to ensure the accuracy of the information contained herein but we do not accept any liability for any omissions or errors. The content of this E-book and all related correspondence are neither a solicitation nor an offer to purchase or sell any financial instrument. Examples are provided for illustrative and educational purposes only and should not be used as investment advice or strategy.

No representation is being made that any account or trader will or is likely to achieve profits or loses similar to those discussed in this e-book.

Three Types of Forex Market Analysis

- Technical Analysis
- Fundamental Analysis
- Sentiment Analysis

Technical Analysis

Forex technical analysis involves looking at patterns in price history to determine the higher probability time and place to enter a trade and exit a trade. As a result, technical analysis in forex is one of the most widely used types of analysis.

Since FX is one of the largest and most liquid markets, the movements on a chart from the price action generally gives clues about hidden levels of supply and demand. Other patterned behavior

such as which currencies are trending the strongest can be obtained by reviewing the price chart. An example of this can be seen below in the GBP/USD chart where the US dollar is strengthening against the Pound Sterling.

Trend Lines

Trend lines are probably the most common form of technical analysis in forex trading. A trendline is a line drawn over pivot highs or under pivot lows to show the prevailing direction of price. Trendlines are a visual representation of support and resistance in any time frame. They show direction and speed of price, and also describe patterns during periods of price contraction.

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There are three types of trends:

- Uptrend (higher lows)
- Downtrend (lower highs)
- Sideways trends (ranging)

An uptrend describes the price movement of a financial asset when the overall direction is upward. In an uptrend, each successive peak and trough is higher than the ones found earlier in the trend. The uptrend is therefore composed of higher swing lows and higher swing highs. As long as the price is making these higher swing lows and higher swing highs, the uptrend is considered intact. Once the price starts making lower swing highs or lower swing lows, the uptrend is in question or has reversed into a downtrend.

Some traders and investors only choose to trade during uptrends. These trend traders utilize various strategies to take advantage of the tendency for the price to make higher highs and higher lows.

An uptrend provides investors with an opportunity to profit from rising asset prices. Selling an asset once it has failed to create a higher peak and trough is one of the most effective ways to avoid large losses that can result from a change in trend. Some technical traders utilize trendlines to identify an

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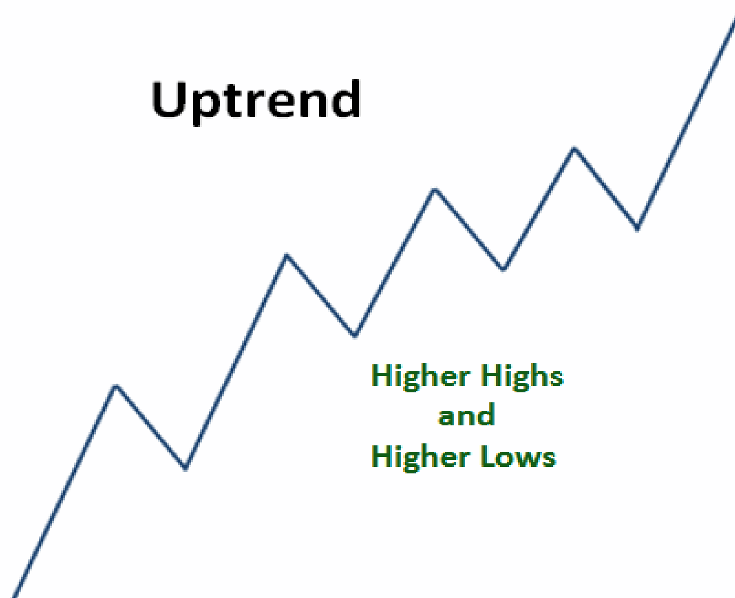
uptrend and spot possible trend reversals. The trendline is drawn along the rising swing lows, which helps show where future swing lows may form.

Moving averages are also utilized by some technical traders to analyze uptrends. When the price is above the moving average the trend is considered up, but when the price drops below moving average it means the price is now trading below the average price over a given period and may therefore no longer be in an uptrend. While these tools may be helpful in visually seeing the uptrend, ultimately the price should be making higher swing highs and higher swing lows to confirm that an uptrend is present. When an asset fails to produce higher swing highs and lows, it means that a downtrend could be underway, the asset is ranging, or the price action is choppy and the trend direction is hard to determine. In such cases, uptrend traders may opt to step aside until an uptrend is clearly visible.

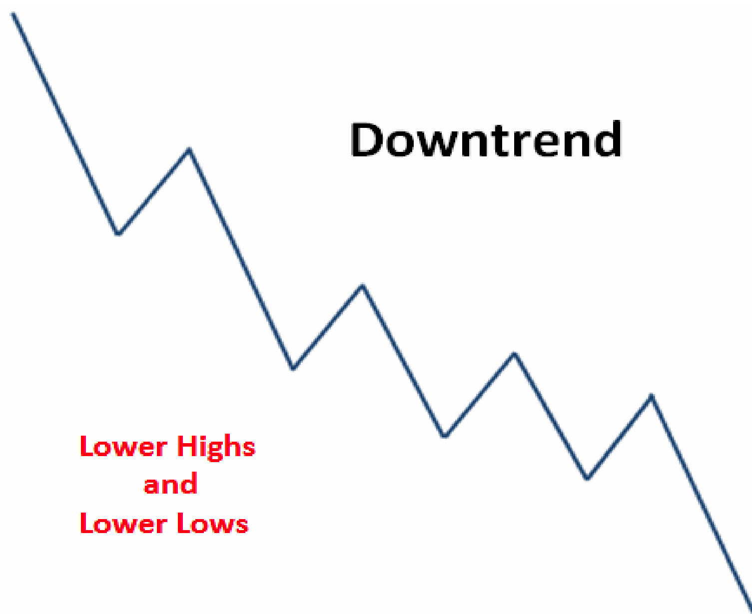


A downtrend occurs when the price of an asset moves lower over a period of time. While the price may move intermittently higher or lower, downtrends are characterized by lower peaks and lower troughs over time. Notice how each successive peak and trough is lower than the previous one. For example, the low at Point 3 is lower than the low at Point 1. The downtrend will be deemed broken once the price closes above the high at Point 4.

An uptrend is the opposite of a downtrend, while markets that are moving sideways are known as *ranging* or *range-bound* markets. Many traders seek to avoid downtrends because they can

adversely affect the value of any investment. A downtrend can last for minutes, days, weeks, months, or even years, so identifying a downtrend early is very important. Once a downtrend has been established (series of lower peaks) a trader should be very cautious about entering into any new long positions.

Short sellers seek to profit from downtrends by borrowing and then immediately selling shares with the agreement to repurchase them in the future. These are known as short positions or short selling. If the asset's price continues to decline, the trader profits from the difference between the immediate sale price and the lower future repurchase price. Often times, traders use technical indicators and chart patterns to identify and confirm downtrends. Moving averages, for example, can be used to identify the overall trend. If the price is lower than a moving average, the stock is likely to be in a downtrend, and vice versa for an uptrend. Momentum indicators, such as the relative strength index (RSI), can also show the magnitude or strength of the downtrend at a given point in time, which can help when deciding whether or not to enter a short position.



A sideways trend is the horizontal price movement that occurs when the forces of supply and demand are nearly equal. This typically occurs during a period of consolidation before the price continues a prior trend or reverses into a new trend.

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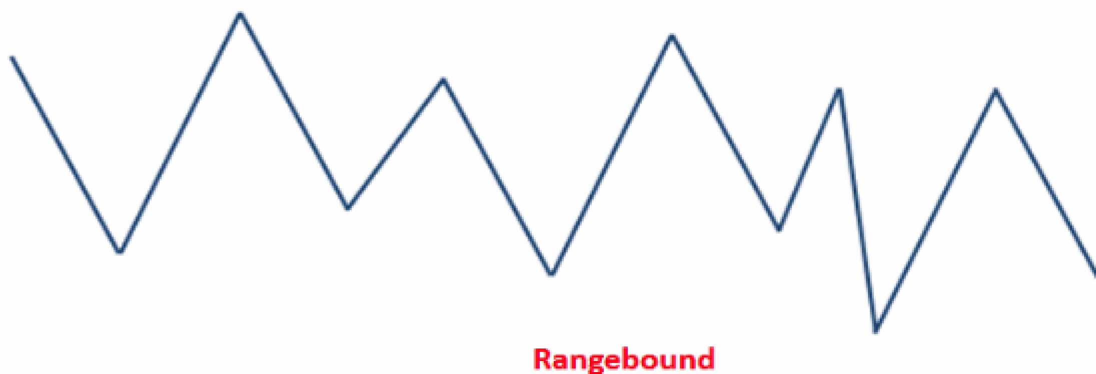
A sideways price trend is also commonly known as a "horizontal trend." Sideways trends are generally the result of a price traveling between strong levels of support and resistance. It is not uncommon to see a horizontal trend dominate the price action of a specific asset for a prolonged period before starting a new trend higher or lower. These periods of consolidation are often needed during prolonged trends, as it is nearly impossible for such large price moves to sustain themselves over the longer term.

Volume, which is an important trading indicator, mostly remains flat during a sideways trend because it is equally balanced between bulls and bears. It shoots up (or down) sharply in one direction, when a breakout (or breakdown) is expected to occur. When analyzing sideways trends, traders should look at other technical indicators and chart patterns to provide an indicator of where the price may be headed and when a breakout or breakdown may be likely to occur.



Fundamental Analysis

Fundamental analysis is a way of looking at the forex market by analyzing economic, social, and political forces that may affect the supply and demand of an asset. Using supply and demand as an indicator of where price could be headed is easy.

The better shape a country's economy is, the more foreign businesses and investors will invest in that country. Fundamental analysis is the process of looking at a business at the most basic or fundamental financial level. This type of analysis examines the key ratios of a business to determine its financial health. Fundamental analysis can also give you an idea of the value of what a company's

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stock should be. It takes several factors into account, including revenue, asset management, and the production of a business as well as interest rate.

Many investors use fundamental analysis alone, but it can be particularly helpful to use it in combination with other tools to evaluate stocks for investment purposes. The goal is to determine the current worth of the stock, and, perhaps more importantly, to identify how the market values the stock. Even if you don't plan to do an in-depth fundamental analysis yourself, understanding the key ratios and terms can help you follow stocks more closely and accurately.

For example, let's say that the U.S. dollar has been gaining strength because the U.S. economy is improving. As the economy gets better, raising interest rates may be needed to control growth and inflation. Higher interest rates make dollar-denominated financial assets more attractive. As a result, the value of the dollar will likely increase.

Sentiment Analysis

Each trader has his or her own opinion of why the market is acting the way it does and whether to trade in the same direction of the market or against it. The market basically represents what all traders feel about the market. Each trader's thoughts and opinions, which are expressed through whatever position they take, helps form the overall sentiment of the market regardless of what information is out there.

The problem is that as retail traders, no matter how strongly you feel about a certain trade, you can't move the forex markets in your favor. Sentiment Analysis also known as *Opinion Mining* is a field within Natural Language Processing (NLP) that builds systems that try to identify and extract opinions within text. Usually, besides identifying the opinion, these systems extract attributes of the expression e.g.:

- *Polarity*: if the speaker expresses a *positive* or *negative* opinion,
- *Subject*: the thing that is being talked about,
- *Opinion holder*: the person, or entity that expresses the opinion.

Trading Multiple Time Frames in Forex

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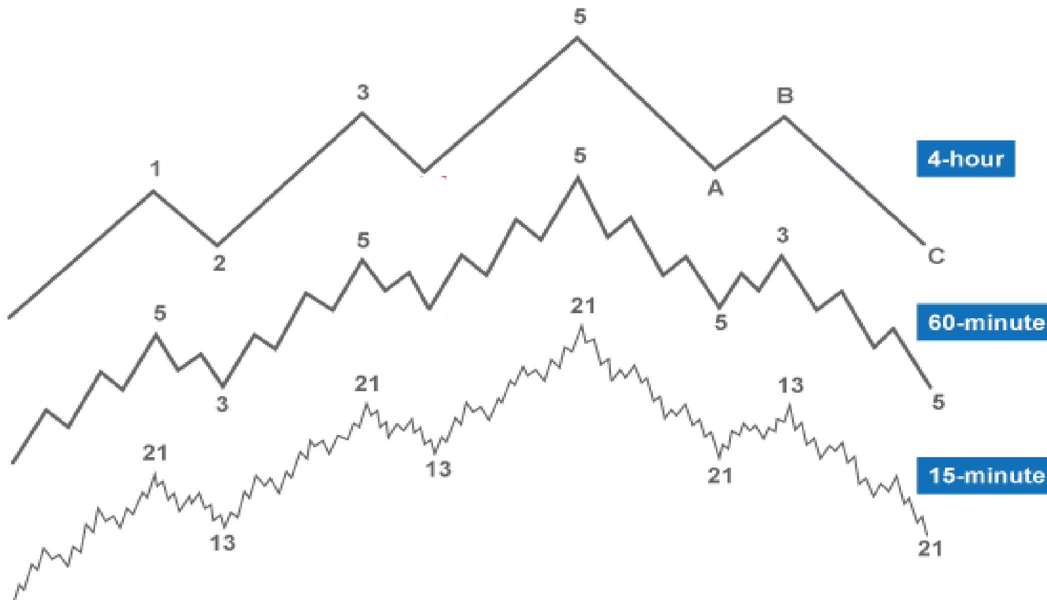
Multiple time frame analysis is simply the process of looking at the same pair and the same price, *but on different time frames*. Remember, a pair exists on several time frames – the daily, the hourly, the 15-minute, heck, even the 1-minute! This means that different forex traders can have their different opinions on how a pair is trading and both can be completely correct.



One may see that EUR/USD is on a downtrend on the 4-hour chart. As you can see, this poses a problem. Trades sometimes get confused when they look at the 4-hour, see that a sell signal, then they hop on the 1-hour and see price slowly moving up. Each forex trader should trade a specific time frame that fits his or her own personality. Finding the right time frame for your trading is not an easy task. A Forex trader faces a wide variety of choices when the trading career is started... and choosing the chart type and time frame configuration is one of them. Also, read the weekly trading strategy that will keep you sane. How to tackle it and what things should be considered? First, the time frame choice is connected to your trading style. Here is a list to provide an essential idea:

- In case of a position trader - use higher time frames like a weekly chart
- In case of a swing trader - use intermediate time frames like a 4-hour chart
- In case of an intra-day trader - use lower time frames like a 15-minute chart

Multiple time frame offers the chance for traders to read what the big money is doing; instead of trying to follow someone on TV. It offers the possibility for traders to improve and enhance their strategy's performance via better entries, exits, trade management, money management, etc.

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What Time Frame Should I Trade?

New forex traders will want to get rich quick, so they'll start trading small time frames like the 1-minute or 5-minute charts. For some forex traders, they feel most comfortable trading the 1-hour charts. This time frame is longer, but not too long, and trade signals are fewer, but not too few. Trading on this time frame helps give more time to analyze the market and not feel so rushed.

What Time Frame Is Best for Trading?

In the table below, we've highlighted the basic time frames and the differences between each.

TIME FRAME	DESCRIPTION	ADVANTAGE	DISADVANTAGES
LONG-TERM	Long-term traders will usually refer to daily and weekly charts. The weekly charts will establish the longer-term perspective. Trades usually from a few weeks to many months, sometimes years.	Don't have to watch the markets intraday. Fewer transactions mean less times to pay the spread. More time to think through each trade	Large swings. Usually 1 or 2 two goods a year so PATIENCE is required. Bigger account needed to ride longer term swings. Frequent losing months
SHORT-TERM (SWING)	Short-term traders use hourly time frames and hold trades for several hours to a week.	More opportunities for trades. Less chance of losing months. Less reliance on one or two trades a year.	Transaction costs will be higher (more spreads to pay). Overnight risk becomes a factor
INTRADAY	Intraday traders use minute charts such as 1-minute or 15-minute. Trades are held intraday.	Lots of trading opportunities. Less chance of losing months. No overnight risk	Transaction costs will be higher. Mentally more difficult due to the need to change biases. Profits are limited by needing to exit at the end of day.

You also have to consider the amount of capital you have to trade. Shorter time frames allow you to make better use of margin and have tighter stop losses. Larger time frames require bigger stops, thus a bigger account, so you can handle the market swings without facing a margin call.

Why You Should Look at Multiple Time Frames When Trading Forex

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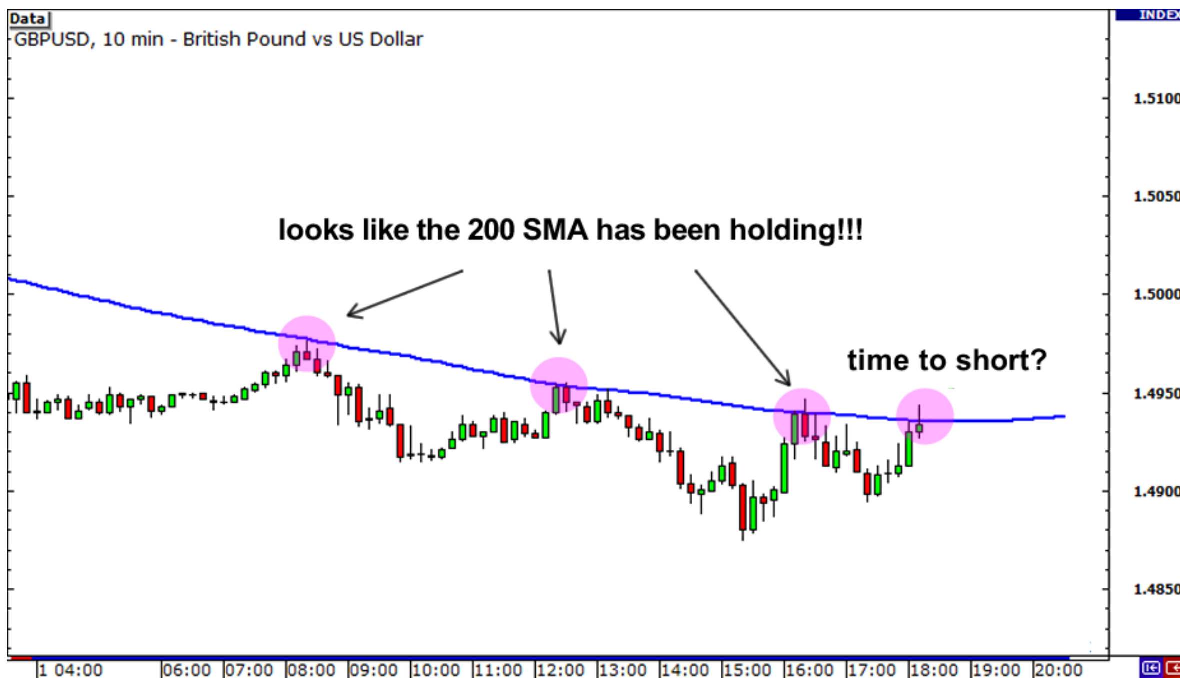
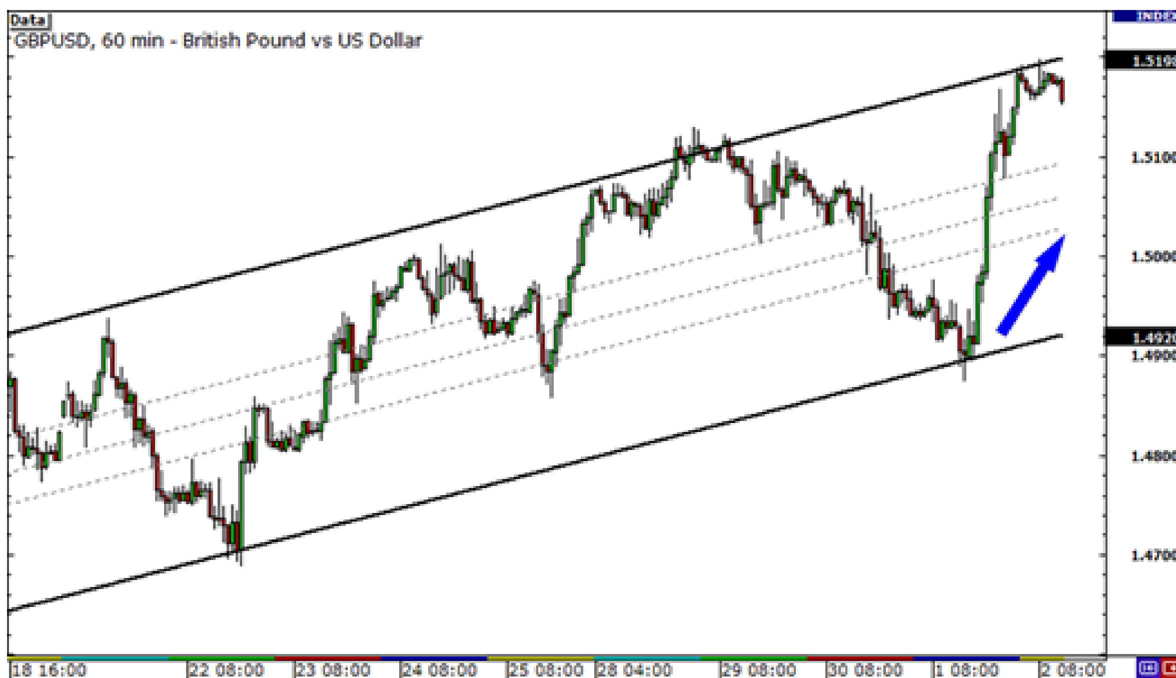
Many traders use multiple time frame analysis techniques. This can result in a most reliable forex strategy as it offers the opportunity for traders to understand the market structure in a much deeper and profound way than any single time frame analysis can do. It offers the chance for traders to read what the big money is doing; instead of trying to follow someone on TV.
It offers the possibility for traders to improve and enhance their strategy's performance via better entries, exits, trade management, money management, etc. Let's compare this with a single time frame strategy… the single one offers a very limited view of the market and leaves traders often confused as to why their setup is failing.
Let's take a look at the 10-minute chart of GBP/USD at 8:00 am GMT. We've got the 200 simple moving average (SMA) on, which appears to be holding as resistance.



Contrary to the expectations, the pair closed above resistance and rose another 200 pips!

If you had been looking at the one hour chart, you would have noticed that the pair was actually at the bottom of the ascending channel. What's more, a doji had formed right smack on the support line! A clear buy signal!



The ascending channel would have been even clearer on the 4-hour chart.

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All of the charts were showing the same price data. They were just different time frames of that same data. When the market did stall or reverse on the 15-minute chart, it was often because it had hit support or resistance on a larger time frame. Trading using multiple time frames has probably kept us out of more losing trades than any other one thing alone.

How to Use Multiple Time Frame Analysis to Find Better Entry and Exit Points

Most traders seem to be able to grasp the importance of using the next higher timeframe to get a big picture view. But many of them seem to stop there and forget to zoom down to the next lower timeframe in order to optimize their entries.

As you may know or will soon come to realize, that in forex trading, in order to be consistently profitable, you must take advantage of every edge that is available. By ignoring optimal trade execution methods, you are leaving money on the table. So, to realize the best trade execution, you should zoom into the next lower timeframe than the one you were using and execute from there. This is a crucial concept to understand. Most traders, on the other hand, typically take the opposite stance. They will chase a trade until they are filled regardless of how far price has moved away from their anticipated entry point.

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Now for the exits trades you could set a stop loss and target the very moment that you enter a trade. The price will either hit your stop for a small loss or hit your target for a nice profit. Sooner or later, you will realize that the moment that you are in a trade, all your biases will come into play and haunt you during your trade management. It is one of the most difficult aspects of trading, and each trader will have to work on an approach most suited to them. For example, you are looking at this chart below you'll note price that price is looking not too good. Maybe you'll say it's a long-term down trend because you have lower highs:

Or maybe the price just retested and swing high over here:

You're still not looking too good, because if we draw a long-term trend line...it's still pointing lower:

But when you go down to the lower timeframe or rather your entry timeframe, you see this:

Price doesn't look bearish at all, it looks pretty bullish. Why is that? Because you want to trade with the current swing on the higher timeframe. The current swing on the higher timeframe is this portion over here:

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This is the portion that you want to focus on. It's bullish then on your lower timeframe, you want to be long. Imagine if you're looking to go short just because you saw that the higher timeframe is looking long-term bearish, and you're looking to go short on the lower timeframe. Chances are you're going to get stopped out repeatedly over time. Because you are going counter trend on your current timeframe. So, you want to focus on the current swing on the higher timeframe.

Trading with Three Time Frames

We feel that this gives us the most flexibility, as we can decipher the long, medium and short-term trends. What you'll think is, "Okay, maybe I should be looking to short."

Determine Main Trend

The largest time frame we consider our main trend – this shows us the big picture of the pair we want to trade. For example, on the daily chart below, EUR/USD is trading above the 200 SMA which tells you that the main trend is UP.

Determine Current Market Bias

The next time frame down is what we normally look at, and it signals to us the medium term buy or selling bias. Below is a 4-hour chart and it’s clear that EUR/USD continues to have a bullish bias.

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Determine Entry and Exit

The smallest time frame shows the short term trend and helps us find really good entry and exit points.

Multiple Time Frame Combinations

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You can use any time frame you like as long as there is enough time difference between them to see a difference in their movement. You might use:

a) 1-minute, 5-minute, and 30-minute
b) 5-minute, 30-minute, and 4-hour
c) 15-minute, 1-hour, and 4-hour
d) 1-hour, 4-hour, and daily
e) 4-hour, daily, and weekly and so on.

When you're trying to decide how much time in between charts, just make sure there is enough difference for the smaller time frame to move back and forth without every move reflecting in the larger time frame.

Market Sentiment

Market sentiment (also investor attention) is the general prevailing attitude of investors as to anticipated price development in a market. This attitude is the accumulation of a variety of fundamental and technical factors, including price history, economic reports, seasonal factors, and national and world events.
If investors expect upward price movement in the stock market, the sentiment is said to be bullish. On the contrary, if the market sentiment is bearish, most investors expect downward price movement. Market sentiment is usually considered as a contrarian indicator: what most people expect is a good thing to bet against. Market sentiment is believed to be a good predictor of market moves and a good indicator to hedge risk, especially when it is more extreme. Very bearish sentiment is usually followed by the market going up more than normal, and vice versa.
Market sentiment is monitored with a variety of technical and statistical methods such as the number of advancing versus declining stocks and new highs versus new lows comparisons. A large share of the overall movement of an individual stock has been attributed to market sentiment. The stock market's demonstration of the situation is often described as all boats float or sink with the tide, in the popular Wall Street phrase *"the trend is your friend"*. In the last decade, investors are also known to measure market sentiment through the use of news analytics, which include sentiment analysis on textual stories about companies and sectors.

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How to Develop a Market Sentiment-Based Approach

As a forex trader, it is your job to gauge what the market is feeling. We can't tell the market what we think it should do. But what we can do is react in response to what is happening in the markets. Note that using the market sentiment approach doesn't give a precise entry and exit for each trade. Of course, you can always combine market sentiment analysis with technical and fundamental analysis to come up with better trade ideas.

In stocks and options, traders can look at volume traded as an indicator of sentiment.

If a stock price has been rising, but volume is declining, it may signal that the market is overbought. Or if a declining stock suddenly reversed on high volume, it means the market sentiment may have changed from bearish to bullish. Unfortunately, since the forex market is traded over-the-counter, it doesn't have a centralized market. This means that the volume of each currency traded cannot be easily measured.

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