



When using a demo account does and does not work

Learning to trade without risk has been made so much easier with nearly every broker offering a demo account for traders to practice on, but do these really do the trader any good? I regularly read conflicting views on whether traders should use them, so here is my view.

It started off well.....

I have heard from lots of new traders the story of how they were doing really well to start with, and then all of a sudden things went wrong. It is probably not a great surprise to hear that the sudden change coincided with changing from a demo account to using their real account. So what happened?

Well there are a few things that might change here. Firstly, there is the pure dynamics of the platform. Some demo accounts bear little resemblance to the real market in terms of the speed of orders being filled. So that puts some of the blame on the brokers, but I do not believe it is the main cause.

Next in line is the psychology of the trader. When real money is on the line it is surprising how different a trader may react to the moves in the market and snatch at profits. As I wrote recently their patience remains amazingly great in their losing trades yet they have little patience for their winning trades.

What I have come across more recently is an even bigger problem for those changing over to a real cash account. That is that the trader becomes particularly selective with their trades that they take, trying to cherry pick only the best. Of course the intention is good, but the reality is that when we have produced a strategy we need to take all the set ups to get the same probability and let's face it not all the entries look pretty at times, but a set up is a set up!

The next and maybe the biggest problem, is when using a demo account traders may also take trades they would not normally take as 'it does not matter as it's not for real'. Of course the problem here is that the results which may be good or bad will not be anything like the reality of when they go live.



How demo accounts help?

The most important thing a demo account can do is let you learn how to actually place the trade without risking money. Whilst most platforms are reasonably easy to use for the seasoned trader, it is the placing of those very first trades that sometimes results in mistakes and hence a loss of money and confidence. It is useful to learn how to place all the different types of orders as well as the normal market orders and watch how they execute.

Some people will use them to test their trading systems, we did, and found that the reality bore little resemblance to test environment. I would therefore suggest you only do this to ensure your orders are getting processed if you have automated the trades but thereafter you need to move to a cash account.

What you need to ensure if you are going to use a demo account

Firstly I would suggest that you ensure that the prices you are being quoted on the demo account are realistic. Also there is no point setting yourself up with a \$100,000 demo account if you are going to be trading with \$5000 as if you are using the demo account it needs to be as close to realism as possible.

Probably the most important rule is to trade it as it is real money. That means applying the correct position sizes; apply stops according to your strategy; do not start doubling up on losing positions as it 'it is not for real'; only take trades that you would if you were trading with cash.

A much better solution

There is a much better solution which will ensure you will not lose a lot of money plus ensure you prepare yourself from a psychological point. This is to take advantage of macro size trading. If you wish to spread bet you can open a trade with as little as 50p a point through ETX, although after you have placed a stop or limit order you can then reduce the size to as little as 5p per point. It is recommended that the size is either reduced immediately or if you are confident when it is at break even or in profit.

ETX do now offer a better solution now though, as they have launched their MT4 platform which allows you to trade at 0.01 of a contract (around 6.5 pence a point).



Pepperstone offer an alternative MT4 platform with even tighter spreads. You can open their razor account which gives you a spread of around 0.2 on the euro and 0.5 on cable although you do get charged AUS\$3 per \$100,000 which equates to around 0.75 spread.

You can find out more about these accounts from our website <http://ezeetrader.com/>

With Pepperstone you can also use their web based software if you do not like using an MT4 platform still allowing you to trade at these smaller sizes. Personally I think the functionality of the MT4 platform is pretty good. You can move your stops and limits orders from the charts and it is very basic.

Some may argue that macro accounts may themselves get filled more efficiently than full size contracts, but that really depends on the broker, although as you move up in size it is inevitable that you see difference in fills. But the key point is that you will be working with real money and getting into the right mode early on.

Conclusion

In my opinion demo accounts have just one use, that is to learn how to place the different orders and familiarise yourself with the functionality of the platform. Thereafter for the best results a live macro account will get you up to speed and help you build the mental muscle.

Good luck,

Kym Watson.