The Different Types of Orders in the Stock Market

The three basic orders that are normally used in placing trades are market, stop and limit orders, but there are certain subtle variations of which traders need to be aware. These give added security and precision, and there are times when more than one type of order is applicable.

MARKET (AT BEST) - the basic trade

Here the trader buys or sells at the best price available in the market for the size of trade in shares or index points. Variations on this include a Market on Opening trade, which is where the trade is to be executed during the opening range of trading at the best possible price obtainable within that range. At the end of each day's session, a Market on Close order is completed during the final minutes of trading at whatever price is available.

LIMIT ORDERS – buying lower or selling higher

The idea behind a limit order is to define the entry or exit price, and here the aim is to buy below the current price, or sell above it. Clearly this will not always be possible, but a time limit can be set as in "Good for the day" or "Good till cancelled" orders (see below). As with most orders, the instruction can be changed at any time prior to execution. The word limit is often replaced by 'target', but generally the latter is only used with reference to closing positions.

STOP ORDERS – more complex

Stop orders can be used both to open and close positions, and in effect are the reverse of limits, so that instead of for example a higher price triggering a limit order to sell to close an opening long position, here the stop provides a buy signal. This can be to protect a loss on a short position, or to initiate a new buy order. Traders often use these orders to open a new long position by entering a share on a breakout upwards, and this is known as a Buy stop.

On the downside, the idea is to sell if the price falls to a certain level (Sell stop), and typically this is the most common way of protecting open long positions. Again, however, these orders can be used to open new short positions if a share breaks down below a pre-set level.

It should be remembered that execution prices are not guaranteed with stops, nor limits for that matter, as an adverse news event or a gap opening on the next session may mean that the share price does not trade at the stop level. In these cases, the stop is triggered at the next trading price in the market. Traders can however use Guaranteed stops (see below)

A Stop limit order consists of two prices and is an attempt to gain more control over the price at which a stop is filled. The first part of the order is placed as a normal stop order, and the second part of the order specifies a limit price. The rationale here is that once a stop is triggered, the trader does not wish to be filled beyond a set limit price. Stop limit orders should usually not be used when trying to exit a position, as the limit side of the instruction might not be filled if there is a sharp price movement.

There are times when a trader wishes to protect ongoing profits by moving stops accordingly, and here a Trailing stop order can be used. A trailing stop to sell raises the stop price as the share price increases, but does not lower the stop price when the market price decreases. Although trailing stops are useful for backtesting an existing trading system, most online systems do not have a facility for automatic adjustment, and the trader simply needs to amend the stop as needed. Once the stop price is reached, the order becomes a market order.

Guaranteed Stops are used by many traders and here the stop level is guaranteed by the broker, so that the client is fully protected in the case of a sharp adverse move. There is an insurance cost for this, so the commission paid and the spread on trading is often higher and the order is not flexible.

VARIATIONS

Market if touched (MIT)

These orders are used similarly to limits in as much as buy MITs are placed below the current price and sell MITs are placed above. Once the limit price is touched or passed through, they become a market order, so execution may be at, above, or below the originally specified price.

One cancels the other (OCO)

This is a rarer order, where a combination of two order instructions is left in place to confirm an action dependent on how the share performs in either direction. As an example, an investor may have an existing long position, and wish to add a further position should the holding show strength. If, however, the price falls, a stop may be set for protection, and if executed this clearly alters the strategy and cancels the first order.

Fill or Kill

This type of order gives an instruction to buy or sell at a specified price and to immediately cancel the order if it is unable to be filled in total. There is a slight variation on this, the All or none order, which differs from a fill or kill order in that immediate execution is not required.

Good for the day (GFD)

An order either to buy or to sell a security which remains in effect until the end of the trading session, at which time it is cancelled.

Good Till Cancelled (GTC)

An order either to buy or to sell a security which remains in effect until it is cancelled by the customer or until it is executed by the broker. Traders should be aware that if an order is left in the system having been closed manually, that order may be filled at a later stage giving in effect a reverse position, so close monitoring of all pending orders is advisable.

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