

Quickstart Guide to Trading Forex

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Quickstart Guide to Forex

Here is where you begin your illustrious forex trading career.

Our Quickstart guide is a series of Forex lessons created to quickly familiarize the clueless or kinda-clueless with the Forex world.

Every industry has its own collection of jargon, and Forex is no exception. You have to grasp Forex gobbledygook before you can start trading. The lessons are designed to help you gain a better understanding of what the Forex market actually is, who participates in this foxy market, and how you can make money trading Forex.

By the time you finish reading this guide, the slang of currency trading will have become second nature to you.

You'll probably be all fired up and hyped about forex trading and be tempted to open a real account and start trading your rent money. Don't do it! This guide was made to make sure you're properly equipped with the right knowledge before moving forward to our School of Pipsology.

Our Top Secret Recipe for Creating the Ultimate Business

Here are the **TOP SECRET** ingredients needed to create the ultimate business:

1. You
2. Computer
3. Internet connection
4. Desk (or sofa)

That's it! No employees. No advertising. No cold calling. No inventory.

properly trained Forex trader can potentially earn **BIG PROFITS** in every single month, week, or day! (Off course a poorly trained Forex trader can suffer big losses as well.)

Let's continue on the with the TOP SECRET directions for creating the ultimate business:

1. Walk ten steps and
2. Sit in front of your computer (or sit on your sofa and place laptop on your lap)
3. Turn on computer and make sure Internet connection is working
4. Open charts and trading platform
5. Trade currencies
6. Make money!

Presto! You've just learned how to create the ultimate business.

Consider the Following and Judge for Yourself

- YOU ARE YOUR BOSS!
- You don't need any customers!
- You don't need employees!
- You can operate from home, work, vacation or anywhere else in the world as long as you have an Internet connection.
- You never have to worry about job security, harassment or any other employment-related anxiety.
- YOU ARE YOUR OWN BOSS!
- You never need to worry about employer payroll, strikes, theft, rent increases, health inspectors, lease problems, being sued, etc...
- You don't need to do any cold calling.
- You decide which days you wish to work - You make the decision to take a vacation at a moment's notice.
- YOU ARE YOUR OWN BOSS!

The Skinny on Forex Trading

What is FOREX?

The Foreign Exchange, also referred to as the "FOREX" or "Forex" or "FX" or "Spot FX" market is the largest financial market in the world, with a volume over \$1.95 trillion a day. If you compare that to the \$25 billion a day volume that the New York Stock Exchange trades, you see how giant the Foreign Exchange really is. It's actually more than three times the total amount of the stocks and futures markets combined!

What is traded on the Foreign Exchange? The answer is money. Forex trading is the simultaneous buying of one currency and selling of another. Currencies are traded through a broker or dealer and are traded in pairs; for example the Euro dollar and the US dollar (EUR/USD) or the British pound and the Japanese Yen (GBP/JPY).

This kind of trading is often very confusing to people because they are not buying anything physical. Think of buying a currency as buying a share in a particular country. When you buy, say, Japanese Yen, you are in effect buying a share in the Japanese economy, as the price of the currency is a direct reflection of what the market thinks about the current and future health of the country's economy.

In general, the exchange rate of a currency versus other currencies is a reflection of the condition of that country's economy compared to the other countries' economies.

Unlike other financial markets like the New York Stock Exchange, the Forex spot market has neither a physical location nor a central exchange. The Forex market is considered an Over-the-Counter (OTC) or 'Interbank' market, due to the fact that the entire market is run electronically, within a network of banks, continuously over a 24-hour period.

Until the late 1990's, only the "big guys" could play this game. The initial requirement was that you could trade only if you had about ten to fifty million bucks to start. Forex was originally intended to be used by bankers and large institutions and not by us "little guys". However, because of the rise of the Internet, online Forex trading firms are now able to offer trading accounts to 'retail' traders like us.

All you need to get started is a computer, a high-speed Internet connection, and the information contained within this site. BabyPips.com was created to introduce beginning traders to all the essential aspects of foreign exchange in a fun and easy-to-understand manner.

What is a Spot Market?

A spot market is any market that deals in the current price of a financial instrument.

Which Currencies Are Traded?

Any currency backed by an existing nation can be traded at the larger brokers. The most popular currencies along with their symbols are show below:

Symbol	Country	Currency
USD	United States	Dollar
EUR	Euro members	Euro
JPY	Japan	Yen
GBP	Great Britain	Pound
CHF	Switzerland	Franc
CAD	Canada	Dollar
AUD	Australia	Dollar

Forex currency symbols are always three letters, where the first two letters identify the name of the country and the third letter identifies the name of that country's currency.

When Can Currencies Be Traded?

The spot FX market is unique to any other market in the world. It's like a Super Wal-Mart where the market is open 24-hours a day. Somewhere around the world, a financial center is open for business, and banks and other institutions exchange currencies, every hour of the day and night with generally only minor gaps on the weekend.

The foreign exchange markets follows the sun around the world, so you can trade late at night if you're a vampire or in the morning if you're an early bird. Keep in the mind though, the early bird doesn't necessarily get the worm in this market. You might get the worm but a bigger nastier falcon can sneak up and eat you too.

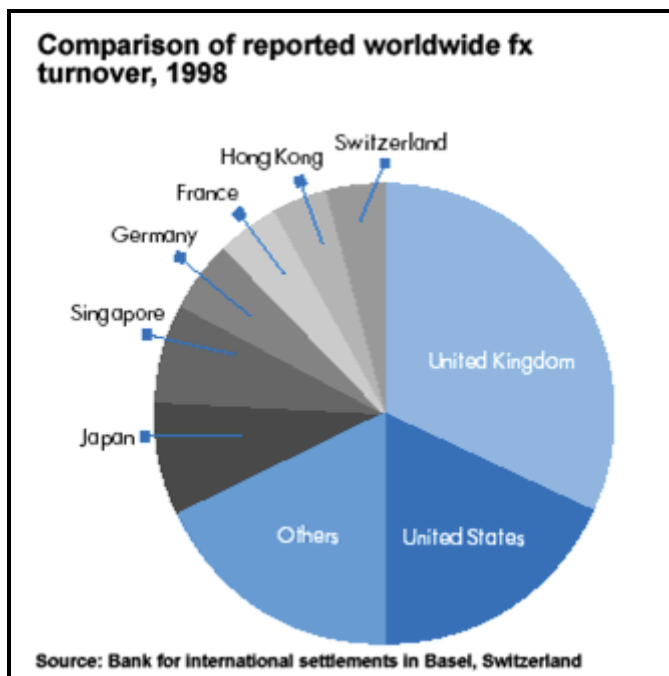
Time Zone	New York	GMT
Tokyo Open	7:00 pm	0:00
Tokyo Close	4:00 am	9:00
London Open	3:00 am	8:00
London Close	12:00 pm	17:00
New York Open	8:00 am	13:00
New York Close	5:00 pm	22:00

The Forex market (OTC)

The Forex OTC market is by far the biggest and most popular financial market in the world, traded globally by a large number of individuals and organizations. In the OTC market, participants determine who they want to trade with depending on trading conditions, attractiveness of prices and reputation of the trading counterparty.

The chart below shows global foreign exchange activity. It represents the results of a study conducted in 1998 by the Bank for International Settlements (BIS). In comparison, while the total daily trading volume worldwide was estimated at about US\$1.5 trillion, only about 12 billion dollars was estimated for currency futures - less than a tenth of one percent!

From the chart below, it is evident that the UK provides the greatest portion of worldwide forex activity. This is despite the fact that the British Pound is only the fourth most widely traded foreign currency in the world.



Why Trade Foreign Currencies?

There are many benefits and advantages to trading Forex. Here are just a few reasons why so many people are choosing this market:

- **No commissions.** No clearing fees, no exchange fees, no government fees, no brokerage fees. Brokers are compensated for its services through the bid-ask spread.
- **No middlemen.** Spot currency trading away with the middlemen and allows clients to interact directly with the market responsible for the pricing on a particular currency pair.
- **No fixed lot size.** In the futures markets, lot or contract sizes are determined by the exchanges. A standard-size contract for silver futures is 5000 ounces. In spot Forex, you determine the lot size. This allows traders to participate with accounts as small as \$300.
- **Low transaction cost.** The retail transaction cost (the bid/ask spread) is typically less than 0.1 percent under normal market conditions. At larger dealers, the spread could be as low as .07 percent. This will be explained later.

- **A 24-hour market.** There is no waiting for the opening bell. From Sunday evening to Friday afternoon EST, the Forex market never sleeps. This is very desirable for those who want to trade on a part-time basis, because you can choose when you want to trade--morning, noon or night.
- **No one can corner the market.** The forex market is so huge and has so many participants that no single entity, not even a central bank, can control the market price for an extended period of time. Even interventions by mighty central banks are becoming increasingly ineffective and short-lived. Central banks are becoming less and less inclined to intervene to manipulate market prices.
- **Leverage.** In Forex trading, a small margin deposit can control a much larger total contract value. Leverage gives the trader the ability to make extraordinary profits and at the same time keep risk capital to a minimum. For example, Forex brokers offer 200 to 1 leverage, which means that a \$50 dollar margin deposit would enable a trader to buy or sell \$10,000 worth of currencies. Similarly, with \$500 dollars, one could trade with \$100,000 dollars and so on. But leverage is a double-edged sword. Without proper risk management, this high degree of leverage can lead to large losses as well as gains.
- **High Liquidity.** Because the Forex Market is so humongous, it is also extremely liquid. This means that with a click of a mouse, under normal market conditions, you can instantaneously buy and sell at will. You are never "stuck" in a trade. You can even set your online trading platform to automatically close your position at your desired profit level (limit order), and/or close a trade if a trade is going against you (stop loss order).
- **Free "Demo" Accounts, News, Charts, and Analysis.** Most online Forex brokers offer free 'Demo' accounts to practice trading, along with breaking Forex news and charting services. These are very valuable resources for "poor" traders who would like to hone their trading skills with 'virtual' money before opening a live trading account.
- **'Mini' Trading:** You would think that getting started as a currency trader would cost a lot of money. The fact is, it doesn't. Online Forex brokers offer "mini" trading accounts with a minimum account deposit of \$300. This makes Forex much more accessible to the average individual who doesn't have a lot of start-up trading capital.

What Tools Do I Need to Start Trading Forex?

A computer with a high-speed Internet connection and all the information on this site is all that is needed to begin trading currencies.

What Does It Cost to Trade Forex?

An online currency trading (a “mini-account”) may be opened for as little as \$300. Do not laugh – mini-accounts are good way to get your feet wet without taking a bath. In Forex, you select how much of any particular currency you wish to buy or sell. For a mini account, we'd recommend at least \$5,000 to start, and we explain why in our School of Pipsology (shameless plug).

How You Make Money Trading Forex

In the foreign exchange market, you buy or sell currencies. Placing a trade in the foreign exchange market is simple: the mechanics of a trade are very similar to those found in other markets (like the stock market), so if you have any experience in trading, you should be able to pick it up pretty quickly.

The object of forex trading is to exchange one currency for another in the expectation that the price will change so that the currency you bought will increase in value compared to the one you sold.

Example of making money by buying Euros

Trader's Action	EUR	USD
You purchase 10,000 euros at the EUR/USD exchange rate of 1.18	+10,000	-11,800*
Two weeks later, the trader exchanges his 10,000 euro back into US dollar at the exchange rate of 1.2500.	-10,000	+12,500**
The trader has earned a profit of \$700.	0	+700

*EUR \$10,000 x 1.18 = US \$11,800

** EUR \$10,000 x 1.25 = US \$12,500

An exchange rate is simply the ratio of one currency valued against another currency. For example, the USD/CHF exchange rate indicates how many U.S. dollars can purchase one Swiss franc, or how many Swiss francs you need to buy one U.S. dollar.

How to Read an FX Quote

Currencies are always quoted in pairs, such as EUR/USD or USD/CHF. The reason they are quoted in pairs is because in every foreign exchange transaction you are simultaneously buying one currency and selling another. Here is an example of a foreign exchange rate of the British pound versus the U.S. dollar:

GBP/USD = 1.7500

The first listed currency is known as the **base currency**, while the second is called the **counter or quote currency**.

The currency to the left of the slash ("/") is called the **base currency** (in this example, the British pound) and the one on the right is called the **quote currency or counter currency** (in this example, the U.S. dollar).

When buying, the exchange rate tells you how much you have to pay in units of the quote currency to buy one unit of the base currency. In the example above, you have to pay 1.7500 U.S. dollar to buy 1 British pound.

When selling, the exchange rate tells you how many units of the quote currency you get for selling one of the basis currency. In the example above, you will receive 1.7500 U.S. dollar when you sell 1 British pound.

The base currency is the “basis” for the buy or the sell. If you buy EUR/USD this simply means that you are buying the base currency and simultaneously selling the quote currency.

You would buy the pair if you believe the base currency will appreciate relative to the quote currency. You would sell the pair if you think the base currency will depreciate relative to the count currency.

Symbol	Country	Currency
USD	United States	Dollar
EUR	Euro members	Euro
JPY	Japan	Yen
GBP	Great Britain	Pound
CHF	Switzerland	Franc
CAD	Canada	Dollar
AUD	Australia	Dollar



Long/Short

First, you should determine whether you want to buy or sell.

If you want to buy (which actually means buy the base currency and sell the quote currency), you want the base currency to rise in value and then you would sell it back at a higher price. In trader's talk, this is called "going long" or taking a "long position". Just remember: long = buy.

If you want to sell (which actually means sell the base currency and buy the quote currency), you want the base currency to fall in value and then you would buy it back at a lower price. This is called "going short" or taking a "short position". Short = sell.

Bid/Ask Spread

All Forex quotes include a two-way price, the **bid** and **ask**. The bid is always lower than the ask price.

The bid is the price in which the dealer is willing to buy the base currency in exchange for the quote currency. This means the bid is the price in which you the trader will sell.

The ask is the price at which the dealer will sell the base currency in exchange for the quote currency. This means the ask is the price in which you the trader will buy.

The difference between the bid and the ask price is popularly know as the **spread**.

Let's take a look at an example taken from a trading software:

On this EUR/USD quote, the bid price is 1.2293 and the ask price is 1.2296. Look at how this broker makes it so easy for you to trade away your money. If you want to sell EUR, you click "Sell" and you will sell Euros at 1.2293. If you want to buy EUR, you click "Buy" and you will buy Euros at 1.2296.

EUR/USD	
Sell	Buy
1.22	1.22
93	96
Low	High
1.2277	1.2304

On this EUR/USD quote, the bid price is 1.2293 and the ask price is 1.2296. Look at how this broker makes it so easy for you to trade away your money. If you want to sell EUR, you click "Sell" and you will sell Euros at 1.2293. If you want to buy EUR, you click "Buy" and you will buy Euros at 1.2296.

In the following examples, I am going to use fundamental analysis to help us decide whether to buy or sell a specific currency pair. If you always fell asleep during your economics class or just flat out skipped economics class, don't worry, we will cover

fundamental analysis in a later lesson. For right now, try to pretend you know what's going on.

EUR/USD

In this example euro is the base currency and thus the “basis” for the buy/sell.

If you believe that the US economy will continue to weaken, which is bad for the US dollar, you would execute a **BUY** EUR/USD order. By doing so you have bought euros in the expectation that they will *rise* versus the US dollar. If you believe that the US economy is strong and the euro will weaken against the US dollar you would execute a **SELL** EUR/USD order. By doing so you have sold euros in the expectation that they will *fall* versus the US dollar.

USD/JPY

In this example the US dollar is the base currency and thus the “basis” for the buy/sell.

If you think that the Japanese government is going to weaken the Yen in order to help its export industry, you would execute a **BUY** USD/JPY order. By doing so you have bought U.S dollars in the expectation that they will rise versus the Japanese yen. If you believe that Japanese investors are pulling money out of U.S. financial markets and converting all their U.S. dollars back to Yen, and this will hurt the US dollar, you would execute a **SELL** USD/JPY order. By doing so you have sold U.S dollars in the expectation that they will depreciate against the Japanese yen.

GBP/USD

In this example the GBP is the base currency and thus the “basis” for the buy/sell.

If you think the British economy will continue to do better than the United States in terms of growth, you would execute a **BUY** GBP/USD order. By doing so you have bought pounds in the expectation that they will rise versus the US dollar. If you believe the British's economy is slowing while the United State's economy remains vibrant, you would execute a **SELL** GBP/USD order. By doing so you have sold pounds in the expectation that they will depreciate against the US dollar.

USD/CHF

In this example the USD is the base currency and thus the “basis” for the buy/sell.

If you think the Swiss franc is overvalued, you would execute a **BUY** USD/CHF order. By doing so you have bought US dollars in the expectation that they will appreciate versus the Swiss Franc. If you believe that due to instability in Iraq and in U.S. financial markets the dollar will continue to weaken, you would execute a **SELL** USD/CHF order. By doing so you have sold US dollars in the expectation that they will depreciate against the Swiss franc.

I don't have enough money to buy \$10,000 EUR. Can I still trade?

You can with margin trading! Margin trading is simply the term used for trading with borrowed capital. This is how you're able to open \$10,000 or \$100,000 positions with \$50 or \$1,000. You can conduct relatively large transactions, very quickly and cheaply, with a small amount of initial capital.

Margin trading in the foreign exchange market is quantified in lots. We will be discussing "lots" more in-depth on our next lesson. For now, just think of the term "lot" as the minimum amount of currencies you have to buy. When you go to the grocery store and want to buy an egg, you can't just buy a single egg, they come in dozens or "lots" of 12. In Forex, it'd be foolish to buy or sell \$1 EUR, they usually come in "lots" of \$10,000 or \$100,000 depending on the type of account you have.

For Example:

You believe that signals in the market are indicating that the British Pound will go up against the US Dollar. You open 1 lot (\$100,000) for buying the Pound with a 1% margin at the price of 1.5000 and wait for the exchange rate to climb. This means you now control \$100,00 worth of British Pound with \$1,000. Your predictions come true and you decide to sell. You close the position at 1.5050. You earn 50 pips or about \$500. (A pip is the smallest price movement available in a currency). So for an initial capital investment of \$1,000, you have made 50% return. Return equals your \$500 profit divided by your \$1,000 you risked to trade.

Your Actions	GBP	USD	Your Money
You buy 100,000 pounds at the GBP/USD exchange rate of 1.5000	+100,000	-150,000	\$1,000
You blink for two seconds and the GBP/USD exchange rate rises to 1.5050 and you sell.	-100,000	+150,500**	\$1,500
You have earned a profit of \$500.	0	+500	

When you decide to close a position, the deposit that you originally made is returned to you and a calculation of your profits or losses is done. This profit or loss is then credited to your account.

We will also be discussing margin more in-depth in the next lesson, but hopefully you're able to get a basic idea of how margin works.

Rollover

No, this is not the same as rollover minutes from your cell phone carrier. For positions open at 5pm EST, there is a daily rollover interest rate that a trader either pays or earns, depending on your established margin and position in the market. If you do not want to earn or pay interest on your positions, simply make sure it is closed at 5pm EST, the established end of the market day.

Since every currency trade involves borrowing one currency to buy another, interest rollover charges are an inherent part of FX trading. Interest is paid on the currency that is borrowed, and earned on the one that is purchased. If a client is buying a currency with a higher interest rate than the one he/she is borrowing, the net differential will be positive (i.e. USD/JPY) – and the client will earn funds as a result. Ask your broker about specific details regarding rollover.

Are you still confused and in need of an example? Well we discuss rollover more in depth in our School of Pipsology, so you'll have to go there to learn more.

Demo Trading

You can open a demo account for free with most Forex brokers. This account has the full capabilities of a "real" account including live market rates, access to real-time market analysis, and the ability to execute trades off streaming prices. Why is it free you ask? It's because they want you to learn the ins and outs of their trading platform so you'll fall in love with it and deposit real money. The demo account allows you to learn about the Forex markets and test your trading skills without any risk.

YOU SHOULD DEMO TRADE FOR AT LEAST 2 MONTHS BEFORE YOU EVEN THINK ABOUT PUTTING REAL MONEY ON THE LINE. I REPEAT, YOU SHOULD DEMO TRADE FOR AT LEAST 2 MONTHS BEFORE YOU EVEN THINK ABOUT PUTTING REAL MONEY ON THE LINE.

"Don't Lose Your Money" Declaration

Place your hand on your heart and say...

"I will demo trade for at least 2 months before I trade with real money."

Now touch your head with your index finger and say...

"I am a smart and patient Forex trader!"

Know Your P's & L's: Profit, Loss, Pips, Lots, and Leverage

Here is where we're going to do a little math. You've probably heard of the terms "pips" and "lots" thrown around, and here we're going to explain what they are and show you how they are calculated.

Take your time with this information, as it is required knowledge for all Forex traders. Don't even think about trading until you are comfortable with pip values and calculating profit and loss.

What the heck is a Pip?

The most common increment of currencies is the Pip. If the EUR/USD moves from 1.2250 to 1.2251, that is ONE PIP. A pip is the last decimal place of a quotation. The Pip is how you measure your profit or loss.

As each currency has its own value, it is necessary to calculate the value of a pip for that particular currency. In currencies where the US Dollar is quoted first, the calculation would be as follows.

Let's take USD/JPY rate at 119.80 (notice this currency pair only goes to two decimal places, most of the other currencies have four decimal places)

In the case of USD/JPY, 1 pip would be .01

Therefore,

USD/JPY:

119.80
.01 divided by exchange rate = pip value
 $.01 / 119.80 = 0.0000834$

This looks like a very long number but later we will discuss lot size.

USD/CHF:

1.5250
.0001 divided by exchange rate = pip value
 $.0001 / 1.5250 = 0.000655$

USD/CAD:

1.4890
.0001 divided by exchange rate = pip value
 $.0001 / 1.4890 = 0.0006715$

In the case where the US Dollar is not quoted first and we want to get the US Dollar value, we have to add one more step.

EUR/USD:

1.2200
.0001 divided by exchange rate = pip value
so
 $.0001 / 1.2200 = \text{EUR } 0.0008196$

but we need to get back to US dollars so we add another calculation which is

EUR x Exchange rate
So
 $0.0008196 \times 1.2200 = 0.0009999$

When rounded up it would be 0.0001

GBP/USD:

1.7975
.0001 divided by exchange rate = pip value
So
 $.0001 / 1.7975 = \text{GBP } 0.0000556$

But we need to get back to US dollars so we add another calculation which is

GBP x Exchange rate

So

$$0.0000556 \times 1.7975 = 0.0000998$$

When rounded up it would be 0.0001

You're probably rolling your eyes back and thinking do I really need to work all this out and the answer is no. Nearly all forex brokers will work all this out for you automatically. It's always good for you to know how they work it out.

In the next section, we will discuss how these seemingly insignificant amounts can add up.

What the heck is a Lot?

Spot Forex is traded in lots. The standard size for a lot is \$100,000. There is also a mini lot size and that is \$10,000. As you already know, currencies are measured in pips, which is the smallest increment of that currency. To take advantage of these tiny increments, you need to trade large amounts of a particular currency in order to see any significant profit or loss.

Let's assume we will be using a \$100,000 lot size. We will now recalculate some examples to see how it affects the pip value.

USD/JPY at an exchange rate of 119.90
(.01 / 119.80) x \$100,000 = \$8.34 per pip

USD/CHF at an exchange rate of 1.4555
(.0001 / 1.4555) x \$100,000 = \$6.87 per pip

In cases where the US Dollar is not quoted first, the formula is slightly different.

EUR/USD at an exchange rate of 1.1930
(.0001 / 1.1930) X EUR 100,000 = EUR 8.38 x 1.1930 = \$9.99734
rounded up will be \$10 per pip

GBP/USD at an exchange rate or 1.8040
(.0001 / 1.8040) x GBP 100,000 = 5.54 x 1.8040 = 9.99416 rounded up
will be \$10 per pip.

Your broker may have a different convention for calculating pip value relative to lot size but whichever way they do it, they'll be able to tell you what the pip value is for the

currency you are trading is at the particular time. As the market moves, so will the pip value depending on what currency you are currently trading.

How the heck do I calculate profit and loss?

So now that you know how to calculate pip value, let's look at how you calculate your profit or loss.

Let's buy US dollars and Sell Swiss Francs.

The rate you are quoted is 1.4525 / 1.4530. Because you are buying US you will be working on the 1.4530, the rate at which traders are prepared to sell.

So you buy 1 lot of \$100,000 at 1.4530.

A few hours later, the price moves to 1.4550 and you decide to close your trade.

The new quote for USD/CHF is 1.4550 / 1.4555. Since you're closing your trade and you initially bought to enter the trade, you now sell in order to close the trade so you must take the 1.4550 price. The price traders are prepared to buy at.

The difference between 1.4530 and 1.4550 is .0020 or 20 pips.

Using our formula from before, we now have $(.0001/1.4550) \times \$100,000 =$
 $\$6.87 \text{ per pip} \times 20 \text{ pips} = \137.40

Remember, when you enter or exit a trade, you are subject to the spread in the bid/offer quote.

When you **buy a currency you will use the offer price** and when you **sell you will use the bid price**.

So when you **buy** a currency, you pay the spread as you **enter** the trade but not as you exit. And when you **sell** a currency you don't pay the spread when you enter but only when you **exit**.

What the heck is Leverage?

You are probably wondering how a small investor like yourself can trade such large amounts of money. Think of your broker as a bank who basically fronts you \$100,000 to buy currencies and all he asks from you is that you give him \$1,000 as a good faith deposit, which he will hold you for but not necessarily keep. Sounds too good to be true? Well this is how forex trading using leverage works.



The amount of leverage you use will depend on your broker and what you feel comfortable with.

Typically the broker will require a minimum account size, also known as account margin or initial margin. Once you have deposited your money you will then be able to trade. The broker will also specify how much they require per position (lot) traded.

For example, for every \$1,000 you have, you can trade 1 lot of \$100,000. So if you have \$5,000 they may allow you to trade up to \$500,000 of Forex.

The minimum security (margin) for each lot will vary from broker to broker. In the example above, the broker required a one percent margin. This means that for every \$100,000 traded, the broker wants \$1,000 as a deposit on the position.

What the heck is a Margin Call?

In the event that money in your account falls below margin requirements (usable margin), your broker will close some or all open positions. This prevents your account from falling into a negative balance, even in a highly volatile, fast moving market.

Example #1

Let's say you open a regular Forex account with \$2,000 (not a smart idea). You open 1 lot of the EUR/USD, with a margin requirement of \$1000. Usable Margin is the money available to open new positions or sustain trading losses. Since you started with \$2,000, your usable margin is \$2,000. But when you opened 1 lot, which requires a margin requirement of \$1,000, your usable margin is now \$1,000.

If your losses exceed your usable margin of \$1,000 you will get a margin call.

Example #2

Let's say you open a regular Forex account with \$10,000. You open 1 lot of the EUR/USD, with a margin requirement is \$1000. Remember, usable margin is the money you have available to open new positions or sustain trading losses. So prior to opening 1 lot, you have a usable margin of \$10,000. After you open the trade, you now have \$9,000 usable margin and \$1,000 of used margin.

If your losses exceed your usable margin of \$9,000, you will get a margin call.

Make sure you know the difference between **usable margin** and **used margin**. If the equity (the value of your account) falls below your usable margin due to trading losses, you will either have to deposit more money or your broker will close your position to limit your risk and his risk. As a result, you can never lose more than you deposit.

If you are going to trade on a margin account, it's vital that know what your broker's policies are on margin accounts.

You should also know that most brokers require a higher margin during the weekends. This may take the form of 1% margin during the week and if you intend to hold the position over the weekend it may rise to 2% or higher.

The topic of margin is a touchy subject and some argue that too much margin is dangerous. It all depends on the individual. The important thing to remember is that you thoroughly understand your broker's policies regarding margin and that you understand and are comfortable with the risks involved.

Some brokers describe their leveraging in terms of a leverage ratio and other in terms of a margin percentage. The simple relationship between the two terms are:

$$\text{Leverage} = 100 / \text{Margin Percent}$$

$$\text{Margin Percent} = 100 / \text{Leverage}$$

Leverage is conventionally displayed as a ratio, such 100:1 or 200:1.

Would You Like Fries with Your Pips?

The term "order" refers to how you will enter or exit a trade. Here we discuss the different types of orders that can be placed into the foreign exchange market. Be sure that you know which types of orders your broker accepts. Different brokers accept different types of orders.

Order Types

Basic Order Types

There are some basic order types that all brokers provide and some others that sound weird. The basic ones are:

- **Market order**
A market order is an order to buy or sell at the current market price. For example, EUR/USD is currently trading at 1.2140. If you wanted to buy at this exact price, you would click buy and your trading platform would instantly execute a buy order at that exact price. If you ever shop on Amazon.com, it's (kinda) like using their 1-Click ordering. You like the current price, you click once and it's yours! The only difference is you are buying or selling one currency against another currency instead of buying Britney Spears CDs.
- **Limit order**
A limit order is an order placed to buy or sell at a certain price. The order essentially contains two variables, price and duration. For example, EUR/USD is currently trading at 1.2050. You want to go long if the price reaches 1.2070. You can either sit in front of your monitor and wait it for it to hit 1.2070 where you would then click a buy *market order*. Or you can set a buy *limit order* at 1.2070, then walk away from your computer and attend your ballroom dancing class. If the price goes up to 1.2070, your trading platform will automatically execute a buy order at that exact price. You specify the price at which you wish to buy/sell a certain currency pair and also specify how long you want the order to remain active (GTC or GFD).
- **Stop-loss order**
A stop-loss order is a limit order linked to an open trade for the purpose of preventing additional losses if price goes against you. A stop-loss order remains in effect until the position is liquidated or you cancel the stop-loss order. For example, you went long (buy) EUR/USD at 1.2230. To limit your maximum loss, you set a stop-loss order at 1.2200. This means if you were dead wrong and EUR/USD drops to 1.2200 instead of moving up, your trading platform would automatically execute a sell order at 1.2200 and close out your position for a 30

pip loss (eww!). Stop-losses are extremely useful if you don't want to sit in front of your monitor all day worried that you will lose all your money. You can simply set a stop-loss order on any open positions so you won't miss your basket weaving class.

Weird Sounding Order Types

- **GTC (Good 'til canceled)**

A GTC order remains active in the market until you decide to cancel it. Your broker will not cancel the order at any time, therefore it's your responsibility to remember that you have the order scheduled.

- **GFD (Good for the day)**

A GFD order remains active in the market until the end of the trading day. Because foreign exchange is a 24-hour market, this usually means 5pm EST since that's U.S. markets close, but I'd recommend you double check with your broker.

- **OCO (Order cancels other)**

An OCO order is a mixture of two limit and/or stop-loss orders. Two orders with price and duration variables are placed above and below the current price. When one of the orders are executed the other order is canceled. Example: The price of EUR/USD is 1.2040. You want to either buy 10,000 at 1.2095 over the resistance level in anticipation of a breakout or initiate a selling position if the price falls below 1.1985. The understanding is that if 1.2095 is reached, you will buy 10,000 and the 1.1985 order will be automatically canceled.

Always check with your broker for specific order information and to see if any rollover fees will be applied if a position is held longer than one day. Keeping your ordering rules simple is the best strategy.

Summary

The basic order types (market, stop loss, and limit) are usually all that most traders ever need. Unless you are a veteran trader (yeah right), don't get fancy and design a system of trading requiring a large number of orders sandwiched in the market at all times – stick with the basic stuff first.

Make sure you fully understand and are comfortable with your broker's order entry system before executing a trade. **DO NOT** make a trade with real money *until* you have an extremely high comfort level with the trading platform and order entry system (and also finished School of Pipsology).

How to Choose an Online Forex Broker

Before trading Forex you need to set up an account with a Forex broker. What exactly is a broker? In simplest terms, a broker is an individual or a company that buys and sells orders according to the trader's decisions. Brokers earn money by charging a commission or a fee for their services.

You may feel overwhelmed by the number of brokers who offer their services online. Deciding on a broker requires a little bit of research on your part, but the time spent will give you insight into the services that are available and fees charged by various brokers.

Is the Forex broker regulated?

When selecting a prospective Forex broker, find out with which regulatory agencies each dealer is registered. The Forex market is label as an “unregulated” market, and it basically is. Regulation is typically reactive, meaning only after you’ve been bamboozled out of your entire savings will something be done.

In the United States a broker should be registered as a Futures Commission Merchant (FCM) with the Commodity Futures Trading Commission (CFTC) and a NFA member. The CFTC and NFA is here to protect the public against fraud, manipulation, and abusive trade practices.

You can verify Commodity Futures Trading Commission (CFTC) registration and NFA membership status of a particular firm or individual and check their disciplinary history by phoning NFA at (800) 621-3570 or by checking the broker/firm information section (BASIC) of NFA's Web site at www.nfa.futures.org/basicnet/.

Among the registered firms, look for those with clean regulatory records and solid financials. Stay away from non-regulated firms!

Customer Service

Forex is a 24-hour market, so 24-hour support is a must! Can you contact the firm by phone, email, chat, etc. Do the reps seem knowledgeable? The quality of support can vary drastically from broker to broker, so be sure to check it out before opening an account.

Here’s a good tip: choose several online brokers and contact their help desks. Seeing how quickly they respond to your questions can be key in gauging how they will respond to your needs. If you don't get a speedy reply and a satisfactory answer to your question



you certainly wouldn't want to trust them with your business. Just be aware that as in other types of businesses, pre-sales service might be better than post-sales service.

Online Trading Platform

Most, if not all, Forex brokers allow you to trade over the Internet relatively easy. The backbone of any trading platform is, of course, the order entry and exit process. Trading software is very important. Get a feel for the options that are available by trying out a demo account at a few online brokers.

Closely examine the dealer's screen layout. It should include the ability to view real-time currency quotes, an account summary showing your current account balance with realized and unrealized profit and loss, margin available, and any margin locked in open positions.

Most trading platforms are either Web-based, in Java, or a client-based program you can install on your computer. Which version you choose is your personal preference, Web based software is housed on your brokers web site. You won't have to install any software on your own computer and you'll be able to log in from any computer that has an Internet connection.

A client-based software program, or one that you download and install into your own computer will limit you to transactions only to that computer.

Usually, the "download and install" program runs faster, but most programs are operating system specific. For example, most brokers only offer their trading platform application to run on Microsoft Windows. If you are a Mac user, you won't be able to install the application and will either have to use your dealer's Web-based or Java-based trading platform. These two (the Web or Java-based) will run on any computer since they run through your browser.

Java-based software programs are preferred by most brokers who think they are more safe and reliable. Java-based software tends to be less vulnerable to attack from viruses and hackers during transmissions than "download and install" software. Be sure to open a demo account and test out the broker's platform before opening a real account!

Don't forget your high speed Internet connection

The Forex market is a fast moving market and you will need up-to-the minute information to make informed transactions. Make sure you have a high speed Internet connection. If you don't, you might as not even bother trading. Dial-up will absolutely not

work for Forex! If you plan to trade online you will need a modern computer and high speed Internet connection. I can't stress this enough!

Bells and Whistles

Any Forex broker worth his salt should offer you real-time quotes and allow you to quickly enter and exit the market. These are minimal requirements of any trading software. Upgraded software packages are usually offered at an extra monthly fee by brokers.

Most dealers now offer integrated charting and technical analysis packages with their trading platforms. These are definitely worth exploring if the charts or technical tools offered are of value to your method of trading. The level of integration with the trading platforms varies and is worth understanding carefully.

Mini-Accounts

Most dealers offer very small "mini-accounts" for as little as \$300. Mini-accounts are a great way to get started and test your trading skills and gain experience.

Broker Policies

Before selecting an online Forex broker, you should closely examine their features and policies. These include:

- **Available Currency Pairs**
You should confirm that the prospective broker offers the at minimum the seven major currencies (AUD, CAD, CHF, EUR, GBP, JPY, and USD).
- **Transaction Costs**
Transaction costs are calculated in pips. The lower the number of pips required per trade by the broker, the greater the profit that the trader makes. Comparing pip spreads of half dozen brokers will reveal different transaction costs. For example, the bid/ask spread for EUR/USD is usually 3 pips, but if you can find 2 pips, that's even better.
- **Margin Requirement**
The lower the margin requirement (meaning the higher the leverage), the greater the potential for higher profits *and* losses. Margin percentages vary from .25 and up.

Low margin requirements are great when your trades are good, but not so great when you are wrong. Be realistic about margins and remember that they swing both ways.

- **Minimum Trading Size Requirement**
The size of one lot may differ from broker to broker, spanning 1,000, 10,000, and 100,000 units. These brokers usually offer a mini-lot, which is one-tenth of a lot. Some brokers even offer fractional unit sizes (called odd lots) which allow you create your own unit size.
- **Rollover Charges**
Rollover charges are determined by the difference between the U.S. interest rates and the interest rates of the other country. The greater the interest rate differential between the two currencies in the currency pair, the greater the rollover charge will be. For example, if the British pound has the greater interest differential with the U.S. dollar, then the rollover charge for holding British pound positions would be the most expensive. On the other hand, if the Swiss Franc were to have the smallest interest differential to the U.S. dollar, then overnight charges for USD/CHF would be the least expensive of the currency pairs.
- **Margin Account Interest Rate**
Most brokers pay interest on a trader's margin account. The interest rates normally fluctuate with the prevailing national rates. If you decide to take an extended break from trading, the money in your margin account will be accruing interest
- **Trading Hours**
Nearly all brokers align their hours of operation to coincide with the hours of operation of the global Forex market: 5:00 pm EST Sunday through 4:00 pm EST Friday.

Other Policies

Be sure to scrutinize a prospective broker's "fine print" section to be fully aware of all the nuances that a specific broker may impose on a new trader.

Finding the right broker/dealer is a critical part of the process. It's not easy and requires some real work on your part. Don't pick the first one that looks good to you. Keep looking.

Summary

What to look for in an online Forex broker/dealer:

1. **Low Spreads.**

In Forex trading the 'spread' is the difference between the buy and sell price of any given currency pair. Lower spreads save you money.

2. **Low minimum account openings.**

For those that new to Forex trading and for those that don't have thousands of dollars in risk capital to trade, being able to open a mini trading account with only \$300 is a great feature for new traders.

3. **Instant automatic execution of your orders.**

This is very important when choosing a Forex broker. You want what we call a WYSIWYG (wizeewig) broker! This means you want instant execution of your orders and the price you see and "click" is the price that you should get...**What You See Is What You Get!**

Don't settle with a firm that re-quotes you when you click on a price or a firm that allows for price 'slippage'. This is very important when trading for small profits.

4. **Free charting and technical analysis**

Choose a broker that gives you access to the best charting and technical analysis available to active traders. Look for a broker that provides free professional charting services and allows traders to trade directly on the charts.

5. **Leverage**

You don't want too much leverage. Firms offering excessively high leverage aren't looking out for the best interest of their customers. A good rule of thumb is to not use more than 100:1 leverage for Standard (100k) accounts and 200:1 for Mini (10k) accounts.

Opening an Online Trading Account

Opening a new account with online Forex broker usually consists of four simple steps:

1. **Selecting an account type**
2. **Registration**
3. **Account activation**
4. **Account confirmation**

You may want to think about opening demo-accounts with two or three broker/dealers first. Then register for a live account with the broker you feel most comfortable with. Take time making a decision you can live with. Don't be rushed and don't be afraid to ask lots of questions.

Account Types

Forex brokers offer individual and corporate accounts. You'll be able to choose different account types based on the size of your initial deposit. For new traders who are smart and don't want to risk a lot of money while learning, they open a mini-account. Experienced traders or anybody with lots of money to play with would open a regular account which requires a much larger initial deposit.

Always read the fine print.

You might see a "managed account" option. With this type of account, your broker/dealer basically trades your money on the Forex market for you. This is similar to opening an account with a mutual fund. Opening a managed account usually requires a pretty big minimum deposit of \$25,000 or higher and you share profits with the broker. We want *you* to learn how to trade your own account, so don't pick this option.

Make sure you open a **Forex spot account** and not a forwards or futures account. We're not going to bother even discussing what forwards or futures account are. Just stay far away from them for now.

Registration

You will have to submit paperwork in order to open an account and the forms will vary from broker to broker. They are usually provided in PDF format and can be viewed and printed using Adobe Acrobat Reader program.

Account Activation

The broker will email you the required steps to activate your new trading account after they receive all of the necessary application forms.

Account Confirmation

Up account activation, your broker will usually email you your user name and password which you'll use to access your live account. They'll also email you instructions on how to deposit money into your account.

So all that's left is for you to login and start trading. Pretty easy huh?

But wait a darn minute!



We strongly advise you spend some time at our **School of Pipsology** before you start risking real money.

Why?

Because if you don't, **you will lose all of your money** and freak out!
You're probably thinking, "So if I read through your **School of Pipsology** first, I will not lose any money?"

No, we're not saying that. You will still probably lose money...

But you'll lose **LESS**, much less, *and* probably feel fine that you lost money. Come join us at our **School of Pipsology** and you'll understand what we mean.

Forex versus Stocks

Forex versus Stocks Advantages		
Advantage	Forex	Stocks
24-hour Trading	YES	NO
Commission Free Trading	YES	NO
Instant Execution of Market Orders	YES	NO
Short-Selling without an Uptick	YES	NO

24-Hour Market

The Forex market is a seamless 24-hour market. Most brokers are open from Sunday at 2PM EST until Friday at 4 PM EST with customer service available 24/7. With the ability to trade during the U.S., Asian, and European market hours, you can customize your own trading schedule.

Commission Free Trading

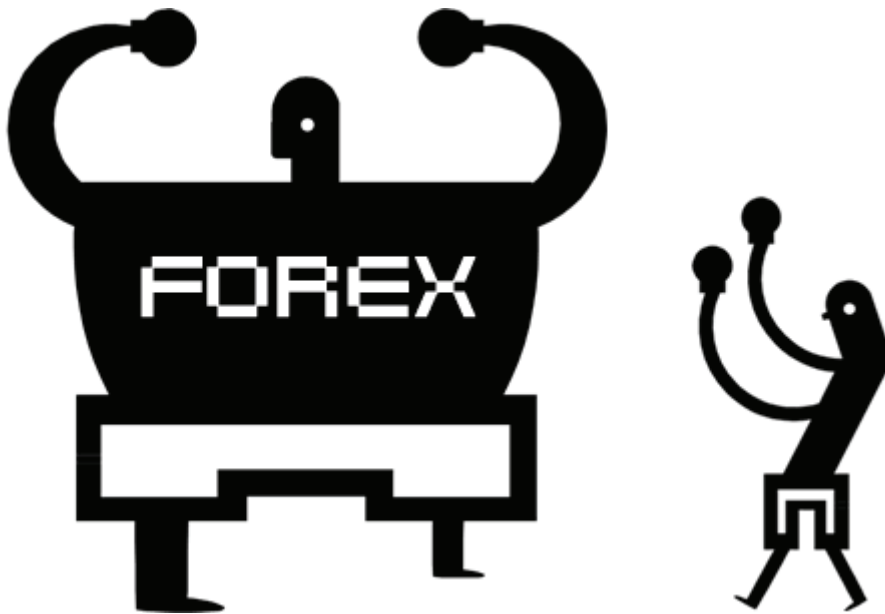
Forex brokers charge no commission or additional transactions fees to trade currencies online or over the phone. Combined with the tight, consistent, and fully transparent spread, Forex trading costs are lower than those of any other market. Forex brokers are compensated for its services through the bid-ask spread.

Instantaneous Execution of Market Orders

Your trades are instantly executed under normal market conditions. You also have price certainty on every market order under normal market conditions. What you click is the price you get. You're able to execute directly off real-time streaming prices (Yeeeah!). There's no discrepancy between the displayed price shown on the platform and the execution price to enter your trade.*

Short-Selling without an Uptick

Unlike the equity market, there is no restriction on short selling in the currency market. Trading opportunities exist in the currency market regardless of whether a trader is long or short, or which way the market is moving. Since currency trading always involves buying one currency and selling another, there is no structural bias to the market. So you always have equal access to trade in a rising or falling market.



Look at Mr. Forex. He's so confident and sexy. Mr. Stocks has no chance!

More Reasons to Like Forex

No Middlemen

Centralized exchanges provide many advantages to the trader. However, one of the problems with any centralized exchange is the involvement of middlemen. Any party located in between the trader and the buyer or seller of the security or instrument traded will cost them money. The cost can be either in time or in fees. Spot currency trading does away with the middlemen and allows clients to interact directly with the market-maker responsible for the pricing on a particular currency pair. Forex traders get quicker access and cheaper costs.

Buy/Sell programs do not control the market

How many times have you heard that "fund A" was selling "X" or buying "Z"? Rumor had it that the funds were taking profits because of the end of the financial year or because today is "triple witching day", all as an explanation of why this stock is up or the market in general is down or positive on the session.

The stock market is very susceptible to large fund buying and selling, and it's not uncommon for a fund to run a particular issue for a few days. In spot currency trading, the liquidity of the Forex market makes the likelihood of any one fund or bank to control a particular currency very slim.

Banks, hedge funds, governments, retail currency conversion houses and large net-worth individuals are just some of the participants in the spot currency markets where the liquidity is unprecedented.

Analysts and brokerage firms are less likely to influence the market

Have you watched TV lately? Heard about a certain Internet stock and an analyst of a prestigious brokerage firm accused of keeping its recommendations, such as "buy" when the stock was rapidly declining? It is the nature of these relationships.

No matter what the government does to step in and discourage this type of activity, we have not heard the last of it. IPO's are big business for both the companies going public and the brokerage houses. Relationships are mutually beneficial and analysts work for the brokerage houses that need the companies as clients.

That catch-22 will never disappear. Foreign exchange, as the prime market, generates billions in revenue for the world's banks and is a necessity of the global markets. Analysts in foreign exchange don't drive the deal flow, they just analyze the forex market.

8,000 stocks versus 4 major currency pairs

There are approximately 4,500 stocks listed on the New York Stock exchange. Another 3,500 are listed on the NASDAQ. Which one will you trade? Got the time to stay on top of so many companies? In spot currency trading, you have 4 major markets, 24 hours a day 5.5 days a week. Concentrate on the majors and find your trade.

*Stop, limit, and entry orders are only guaranteed under normal market conditions. Fills are instantaneous most of the time, but under extraordinarily volatile market conditions order execution may experience delays.

Forex versus Futures

Forex versus Futures Advantages		
Advantage	Forex	Futures
24-hour Trading	YES	NO
Commission Free Trading	YES	NO
Up to 400:1 Leverage	YES	NO
Price Certainty	YES	NO
Guaranteed Limited Risk	YES	NO

Liquidity

The spot Forex market is a \$1.9 trillion daily market, making it the largest and most liquid market in the world. This market can absorb trading volume and transaction sizes that dwarf the capacity of any other market. If you compare this to the \$30 billion per day futures market it becomes clear that the futures markets provide only limited liquidity. The market is always liquid, meaning positions can be liquidated and stop orders executed without slippage.

24-Hour Market

Unlike most futures exchanges, the currency market is a seamless 24-hour market. At 2:15 p.m. EST Sunday, trading begins as markets open in Sydney and Singapore. At 7 p.m. the Tokyo market opens, followed by London at 2 a.m., and finally New York at 8 a.m. As a trader, this allows you to react to favorable or unfavorable news by trading immediately. If important data comes in from England or Japan while the U.S. futures market is closed, the next day's opening could be a wild ride. (Overnight markets in futures currency contracts exist, but they can only be thinly traded, are not very liquid and are difficult for the average investor to access).

Commission Free Trading

In the currency market, you pay NO commissions and NO exchange fees. Because you deal directly with the market maker via a purely electronic online exchange, you eliminate both ticket costs and middleman brokerage fees. There is still a cost to initiating any trade, but that cost is reflected in the bid/ask spread that is also present in futures or equities trading. Brokers are compensated for their services through the bid-ask spread.

Price Certainty

The futures and equities market does not offer instant execution or price certainty. Even with electronic trading and limited guarantees of execution speed, the price for fills on market orders is far from certain. In the futures and equities market, the prices quoted by brokers often represent the LAST trade, not necessarily the price for which the contract will be filled. In contrast, when trading Forex, you get rapid execution and price certainty under normal market conditions.*

Guaranteed Limited Risk

For the purpose of risk management, traders must have position limits. This number is set relative to the money in a trader's account. Risk is minimized in the spot FX market because the online capabilities of the trading platform will automatically generate a margin call if the required margin amount exceeds the dollar value of the account as a result of trading losses. All open positions will be closed immediately regardless of the size or the nature of positions held within the account. If the futures market moves against you, your position may be liquidated at a loss and you will be liable for any resulting deficit in the account.

*Stop, limit, and entry orders are only guaranteed under normal market conditions. Fills are instantaneous most of the time, but under extraordinarily volatile market conditions order execution may experience delays.

Impress Your Date with Forex Trading Lingo

As in any new skill that you learn, you need to learn the lingo...especially if you wish to woo your love's heart. You, the newbie, must know certain terms like the back of your hand before making your first trade. Some of these terms you've already learned, but it never hurts to have a little review.

Major and Minor Currencies

The seven most frequently traded currencies (USD, EUR, JPY, GBP, CHF, CAD, and AUD) are called the major currencies. All other currencies are referred to as minor currencies. Do not worry about the minor currencies, they are for professionals only. Actually, on this site we will only be covering what we call the Fab Five (USD, EUR, JPY, GBP, and CHF). These pairs are the most liquid and are the only currencies we actually trade.

Cross Currency

A cross currency is any pair in which neither currency is the U.S. dollar. These pairs exhibit erratic price behavior since the trader has, in effect, initiated two USD trades. For example, initiating a long (buy) EUR/GBP is equivalent to buying a EUR/USD currency pair and selling a GBP/USD. Cross currency pairs frequently carry a higher transaction cost. The three most frequently traded cross rates are EUR/JPY, GBP/EUR, and GBP/JPY.

Base Currency

The base currency is the first currency in any currency pair. It shows how much the base currency is worth as measured against the second currency. For example, if the USD/CHF rate equals 1.6350, then one USD is worth CHF 1.6350. In the Forex markets, the U.S. dollar is normally considered the "base" currency for quotes, meaning that quotes are expressed as a unit of \$1 USD per the other currency quoted in the pair. The primary exceptions to this rule are the British pound, the Euro, and the Australian dollar.

Quote Currency

The quote currency is the second currency in any currency pair. This is frequently called the pip currency and any unrealized profit or loss is expressed in this currency.

Bid Price

The bid is the price at which the market is prepared to buy a specific currency pair in the Forex market. At this price, the trader can sell the base currency. It is shown on the left side of the quotation.

For example, in the quote **EUR/USD 1.2812/15**, the bid price is 1.2812. This means you can sell one U.S. dollar for 1.2812 Euros.

Ask Price

The ask is the price at which the market is prepared to sell a specific currency pair in the Forex market. At this price, you can buy the base currency. It is shown on the right side of the quotation.

For example, in the quote **EUR/USD 1.2812/15**, the ask price is 1.2815. This means you can buy one U.S. dollar for 1.2815 Euros. The ask price is also called the offer price.

Bid/Ask Spread

The spread is the difference between the bid and ask price. The “big figure quote” is the dealer expression referring to the first few digits of an exchange rate. These digits are often omitted in dealer quotes. For example, the USD/JPY rate might be 118.30/118.34, but would be quoted verbally without the first three digits as “30/34”.

Quote Convention

Exchange rates in the Forex market are expressed using the following format:

Base currency / Quote currency Bid / Ask

Transaction Cost

The critical characteristic of the bid/ask spread is that it is also the transaction cost for a round-turn trade. Round-turn means both a buy (or sell) trade and offsetting sell (or buy) trade of the same size in the same currency pair. In the case of the EUR/USD rate of 1.2812/15, the transaction cost is three pips.

The formula for calculating the transaction cost is:

Transaction cost = Ask Price – Bid Price

Pip

A pip is the smallest unit of price for any currency. Nearly all currency pairs consist of five significant digits and most pairs have the decimal point immediately after the first digit, that is, EUR/USD equals 1.2538. In this instance, a single pip equals the smallest change in the fourth decimal place, that is, 0.0001. Therefore, if the quote currency in any pair is USD, then one pip always equal 1/100 of a cent.

One notable exception is the USD/JPY pair where a pip equals \$0.01.

Margin

When you open a new margin account with a Forex broker, you must deposit a minimum amount with that broker. This minimum varies from broker to broker and can be as low as \$100 to as high as \$100,000.

Each time you execute a new trade, a certain percentage of the account balance in the margin account will be earmarked as the initial margin requirement for the new trade based upon the underlying currency pair, its current price, and the number of units traded (called a lot). The lot size always refer to the base currency.

For example, let's say you open a mini-account which provides a 200:1 margin or .5% margin. Mini-accounts usually trade mini-lots which are \$10,000. So if you were to open one mini-lot, instead of having to provide the full \$10,000, you would only need \$50 ($\$10,000 \times .5 = \50).

Leverage

Leverage is the ratio of the amount used in a transaction to the required security deposit (margin). It is the ability to control large dollar amounts of a security with a relatively small amount of capital. Leveraging varies dramatically with different brokers, ranging from 10:1 to 400:1.

Margin + Leverage = Possible Deadly Combination

Trading currencies on margin lets you increase your buying power. If you have \$5,000 cash in a margin account that allows 100:1 leverage, you could purchase up to \$500,000 worth of currency because you only have to post one percent of the purchase price as collateral. Another way of saying this is that you have \$500,000 in buying power.

With more buying power, you can increase your total return on investment with less cash outlay. But be careful, trading on margin magnifies your profits AND losses.



Margin Call

All traders fear the dreaded margin call. This occurs when your broker notifies you that your margin deposits have fallen below the required minimum level because an open position has moved against you.

Trading on margin can be a profitable investment strategy, but it is important that you take the time to understand the risks. You should make sure you fully understand how your margin account works. Be sure to read the margin agreement between you and your broker. Talk to your broker if you have any questions.

The positions in your account could be partially or totally liquidated should the available margin in your account fall below a predetermined threshold. You may not receive a margin call before your positions are liquidated (the ultimate unexpected birthday gift). Margin calls can be effectively avoided by monitoring your account balance on a very regular basis and by utilizing stop-loss orders (discussed later) on every open position to limit risk. For ease of use, most online trading platforms automatically calculate the profit and loss your open positions.

Protect Yo Self Before You Wreck Yo Self!

Before we go any further we are going to be 100% honest with you and tell you the following before you consider trading currencies:

1. **All forex traders, and I mean all traders lose money on trades.** Ninety percent of traders lose money, largely due to lack of planning and training and having poor money management rules.
2. **Trading forex is not for the unemployed, those on low incomes, who can't afford to pay their electricity bill or afford to eat.** You should have at least \$5,000 of trading capital (in a mini-account) that you can afford to lose. Don't expect to start an account with a few hundred dollars and expect to become a kazillionaire.

The foreign exchange market is one of most popular markets for speculation, due to its enormous size, liquidity and tendency for currencies to move in strong trends. You would think traders all over the world would make a killing, but success has been limited to very small percentage of traders.

Many traders come with false hope of making a gazillion bucks, but in reality lack the discipline required for trading. Most people usually lack the discipline to stick to a diet or to go to the gym three times a week. If you can't even do that, how do you think you're going to succeed trading?

Short term trading is not an amateur's game and is rarely the path for quick riches. You can't make gigantic profits without taking gigantic risks. A trading strategy that involves taking a massive degree of risk means suffering inconsistent trading performance and often suffering large losses. A trader who does this probably doesn't even have a trading strategy - unless you call gambling a trading strategy!

Forex Trading is not a Get-Rich-Quick Scheme!

Forex trading is a SKILL that takes TIME to learn. Skilled traders can and do make money in this field. However like any other occupation or career, success doesn't just happen overnight.

Forex trading isn't a piece of cake as some people would like you to believe. Think about it, if it was, everyone would already be gazillionaires. The truth is even expert traders with years of experience still encounter periodic losses. Drill this in your head: there are no shortcuts to forex trading, it takes lots and lots of time to master.

There is no substitute for hard work and diligence. Practice trading on a demo account and pretend the virtual money is your own real money.

Do not open a live trading account until you are trading profitably on a demo account.

If you can't wait until you're profitable on a demo account. at least demo trade for 2 months. If you can't hold out for 2 months, cut your hands off.

Concentrate on 1 major currency pair.

It gets far too complicated to keep tabs on more than one currency pair when you first start trading. Stick with one of the majors because the spreads are the best and they are the most liquid.

You can be a winner at currency trading, but as in all other aspects of life, it will take hard work, dedication, a little luck, a lot of common sense, and an abundance of good judgment.

Happy Trading!