



# BEGINNERS GUIDE TO FOREX

KNOW MORE ABOUT FOREX TRADING AND THE MARKETS

**"Learning is the eye  
of the mind."**



# Forex, you have already traveled abroad?

Then you've probably crossed your first step into the forex market . Indeed, when at the airport or train station you make a change of currency (ie a currency change against another), then this one is made on the Forex market.

## A GLIMPSE...

Foreign exchange transactions encompass everything from the conversion of currencies by a traveler at an airport kiosk to billion-dollar payments made by corporations, financial institutions and governments.

Comprising of the largest turnover and the most liquid financial market in the world, with average daily volumes in the trillions of dollars forex opens several raw opportunities for traders apart from exchange-limited instruments such as stocks, indices, commodities etc.



**THE BULL  
AND  
THE BEAR**

**GAME**

Whether you're a **Power Trader** or a **Newbie** or a you're likely to hear just about anything—market movements, outlooks and stocks —being described as bullish or bearish.



## **A BULLISH TRADER**

Buys a financial product to sell at a HIGHER price.

### **IN A TRADITIONAL BULL MARKET**

Currencies, stocks, commodities etc are rising in value.

Traders buy to enter the market and find profit potential.

## **A BEARISH TRADER**

Sells a financial product to buy at a LOWER price.

### **IN A TRADITIONAL BEAR MARKET**

Forex, stocks, commodities are declining in value.

Traders sell to exit the market and minimize losses and find profit potential.



# TWO TRADE OPPORTUNITIES

## BUY

If you believe the current value of the euro is strengthening against the US dollar, you might enter a trade to buy euros in the hopes that the currency's value will become stronger compared to the US dollar. In this scenario, you think the euro is bullish (and the US dollar is bearish).

## SELL

Conversely, if you think the current value of the euro will weaken against the US dollar, you might enter a trade to sell euros in the hopes that the currency's value will become weaker compared to the US dollar. In this scenario, you think the euro is bearish (and the US dollar is bullish).

## WHAT IS FOREX TRADING?

Also known as foreign exchange or currency trading, forex is one of the most traded markets in the world. In forex trading, traders hope to generate a profit by speculating on the value of one currency compared to another. This is why currencies are always traded in pairs—the value of one unit of currency doesn't change unless it's compared to another currency.

CURRENCY PAIRS APPEAR LIKE THIS:

# EUR/USD

The first currency listed is the base currency.

The second currency is called the quote or terms currency.

A SAMPLE QUOTE COULD BE:

# 1.3382

The base currency is always worth one. The quoted price shows how much of the quote currency you'll get for one unit of the base currency. So in this case, 1 EUR is worth approximately 1.33 USD

## Did you know?

The buy or sell action you take to enter a trade always applies to the base currency. The opposite action automatically applies to the quote currency. So, if you buy the EUR/USD, this means you're buying euros and selling US dollars. If you sell the EUR/USD, you're selling euros and buying US dollars.

# PIP (PRICE INTEREST POINT)

By now, you may feel comfortable and even a little excited about trading forex: you know who trades it, when to trade it, and what currencies are available. In this section, we'll discuss some concepts you need to know before you trade your first currency pair.

## WHY ARE CURRENCY PAIRS SHOWN IN FOUR DECIMAL PLACES?

Typically in forex, currency pairs display their prices with four decimal points. A few, such as the Japanese yen, display two decimal places. No matter what currency pair you're trading, the last large number behind the decimal always represents a pip, the main unit price that can change for the currency pair. As you trade, you'll track your profits (or losses) in pips.

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As you may already know, the change in currency value relative to another is measured in "pips," which is a very, very small percentage of a unit of currency's value. To take advantage of this minute change in value, 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 unit (standard) lot size. We will now recalculate some examples to see how it affects the pip value.

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

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

## PIP

The fourth unit after the decimal point, which is the smallest unit of an exchange rate.

| LOT      |      | NUMBER OF UNITS |
|----------|------|-----------------|
| STANDARD | 1.00 | 1,00,000        |
| MINI     | 0.10 | 10,000          |
| MICRO    | 0.01 | 1,000           |

## WHAT IS SPREAD?

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

When you buy a currency, you will use the offer or ASK price.

When you sell, you will use the BID

## SPREAD

1.3000

1

1.3001

The first rate (1.3000) is the price at which you can sell the currency pair. The second rate (1.3001) is the price at which you can buy the currency pair. The difference between the first and second rate is called the spread. This is the amount that a dealer charges for making the trade.



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.

All the bank asks from you is that you give it \$1,000 as a good faith deposit, which it will hold for you but not necessarily keep.

Sounds too good to be true? This is how forex trading using leverage works.

Typically the broker will require a trade deposit, 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, if the allowed leverage is 100:1 (or 1% of position required), and you wanted to trade a position worth \$100,000, but you only have \$5,000 in your account.

No problem as your broker would set aside \$1,000 as down payment, or the “margin,” and let you “borrow” the rest. Of course, any losses or gains will be deducted or added to the remaining cash balance in your account.

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.

## HOW TO CALCULATE PROFIT/LOSS?

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

Let's buy U.S. dollars and sell Swiss francs.

The rate you are quoted is 1.4525 / 1.4530. Because you are buying U.S. dollars you will be working on the “ASK” price of 1.4530, the rate at which traders are prepared to sell.

So you buy 1 standard lot (100,000 units) at 1.4530.

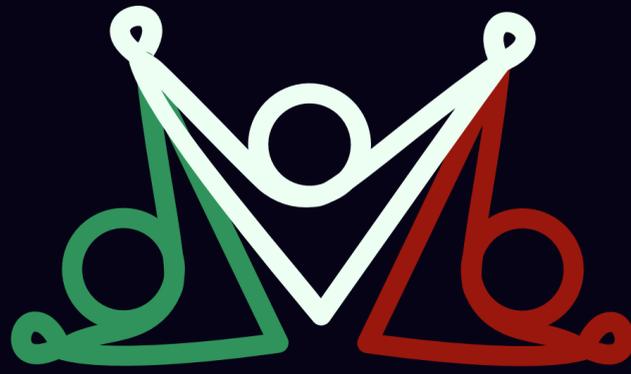
A few hours later, the price moves to 1.4550 and you decide to close your trade.

The new quote for USD/CHF is 1.4550 / 1.4555. Since you initially bought to open the trade, to close the trade, you now must sell in order to close the trade so you must take the “BID” price of 1.4550. The price which 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  $(.0001/1.4550) \times 100,000 = \$6.87$  per pip  $\times 20$  pips = \$137.40

Bid-Ask Spread



## SO HOW DOES LOT, PIPS AND LEVERAGE WORK TOGETHER?

Let's imagine that you just bought 10,000 EUR/ USD on 50:1 as we discussed in the previous example on leverage. You purchased at 1.30000 then closed the trade by selling at 1.30200. This means you've earned 20 pips.

$$0.0001 \times \text{US\$}10,000 = \text{US\$}1 \text{ per pip}$$

For your 20 pip trade, you would have earned US\$20.

Not all of the pips you'll earn will be worth US\$1. The value of a pip depends on the lot size of your trade, how many lots you're trading, the currency pair and your account currency.

While you can manually calculate this or use online pip calculators to learn the value of a pip before you trade, most trading applications, like the FOREXTrader platform, automatically calculate pip values and convert them to the currency you're trading.

