

The image features three large, 3D block letters 'A', 'B', and 'C' in blue, yellow, and red respectively, arranged horizontally. They are set against a background of a world map with various financial data points like percentages and numbers overlaid. The letters are reflected on a glossy surface below them.

ABC

TRADING BASICS

▶ Tutorial Guide

Currency Pairs:

This is the term used to express one currency against another. Currency pairs are named by combining the 3-letter ISO codes of two currencies. The price of a currency pair always expresses the amount of the 2nd named currency needed to exchange against one unit of the first named currency.

Example: USDSAR = 3.7500 means 3.75 SAR can be exchanged to 1 USD

ISO codes:

AED	United Arab Emirates Dirham	SAR	Saudi Riyal
AUD	Australian Dollar	SEK	Swedish Krona
CAD	Canadian Dollar	SGD	Singapore Dollar
CHF	Swiss Franc	USD	US Dollar
DKK	Danish Krone	THB	Thai Baht
EUR	European Euro	TRY	Turkish Lira
GBP	British Pound	XAG	Silver
JPY	Japanese YEN	XAU	Gold
NOK	Norwegian Kroner	XPT	Platinum
NZD	New Zealand Dollar	ZAR	South African Rand

Bid and Ask:

A speculator may buy or sell any currency pair at any time; we say he is choosing 'direction'. A price quote of any currency pair always includes two prices; a bid as well as an offer. The bid price which is always lower is quoted first or on the left, it is the price at which an investor can sell the currency pair. The ask price is generally of a slightly higher value, quoted second and displayed on the right; it is the price at which a currency pair can be bought.

Example: USDJPY price quote is 120.60 / 120.63,
USDJPY can be sold at 120.60 (the bid) or bought at 120.63 (the ask).

Long and Short:

Are expressions used to describe the direction of a trade. After taking the offer, the speculator is buying a currency pair and will be considered to be long. By selling USDJPY on the bid, he is effectively short.

Going short on a currency pair expresses the view that the first named currency should lose value relative to the 2nd named currency. The seller is expecting a price drop, whereas the buyer or holder of a long position expects prices to rise.

Pips and Spreads:

The word 'pip' is used to describe a price difference. 1 pip is the smallest possible price change; it is an increase or decrease of 1 unit of the last decimal shown in a price.

Example: price change from 1.9225 to 1.9226 is 1 pip

CHFSAR price change from 3.0798 to 3.0785 is 13 pips

XAGUSD price change from 13.02 to 13.35 is 33 pips

The 'spread' is the price difference of the bid and the ask, in the above example of the USDJPY price quotation of 120.60 / 120.63, the spread was 3 pips. The more liquid the currency pair, the smaller or 'tighter' the spread will be quoted.

A lot of investors ask us about the value of one pip. The answer is not a fixed amount in US Dollars or another specific currency. The value of one pip will depend on the currency pair and trade amount; we will be able to fully answer the question at the end of this chapter.

Liquidity:

Liquidity is the term used to describe what amount of a specific currency pair can be exchanged without significantly changing current offer and demand. High liquidity means that the potential trade amount has to be very large in order to cause a significant price movement. Liquidity of each currency pair may differ strongly. The largest liquidity can be found in currency pairs that include currencies of large industrialized nations, such as the USD, EUR, GBP, JPY, CHF and CAD.

The NOK, DKK, SEK, AUD, NZD, SGD form the 2nd tier, their liquidity is fairly good and they can be traded normally, as long as trade amounts do not exceed \$100 million equivalent.

'Smaller' currencies, such as the THB, TRY, ZAR, SAR, AED but also precious metals Gold (XAU) and Silver (XAU) are freely exchangeable, due to liquidity constraints they may be at risk of much faster and larger price movements. Some of the smaller currencies could be pegged to another currency, such as the SAR which is fixed against the USD but will float against any other currency that floats against the US Dollar.

The most actively traded currency pairs in the world today are: EURUSD, USDJPY, EURJPY, GBPUSD, USDCHF, USDCAD, EURGBP, together they account for more than 80% of the daily traded volume. Due to the large amounts that are traded in these currencies by real money, they enjoy wide-spread coverage by economists and analysts.

Trading smaller currency pairs, such as NZDJPY, ZARCHF, USDTRL or XAUGBP may be just as rewarding for a currency speculator. Given its potential for large movements, risks are higher but so are potential returns. LQD MARKETS allows its clients to pick from a list of more than 60 cross currency pairs, encouraging you to take a look at alternatives.

Trading:

Once an investor has selected a currency pair and the direction he wants to trade to enter an exposure, he needs to choose the trade amount. Speculation in the foreign exchange market is done using leverage, meaning that the amount of currency that can be purchased or sold will be greater than the amount the investor puts at risk. The cash that the investor keeps on deposit serves as 'margin', and covers potential losses of the trade in progress.

Amounts:

In the professional world, standard trade amounts of 5 to 20 million are in order. Large trades of 100 million and more can be executed with large investment banks, which in turn will break up the trade into smaller units.

The trade amount, also known as the 'face amount' describes the number of units of the first named currency that will be traded:

Example: Investor A sells 1 million EURUSD: he is selling 1 million Euros in exchange for US Dollars

Private speculators generally trade in smaller amounts. Depending on their investment size and risk appetite, trade sizes vary between 10'000 and 10 million. To facilitate trade amounts the expression 'lot' was created:

Definition: 1 lot = 100'000 for all currencies

1 lot = 100 Ounces of GOLD

1 lot = 1'000 Ounces of SILVER

Example: Investor A buys 4.5 lots USDJPY: he is buying 450'000 US Dollars in exchange for Japanese YEN

The counter currency:

Remember that any trade is in fact an exchange of one currency against another at a certain price. An investor buying a face amount of the first named currency is by definition selling the counter amount of the second named currency. The counter amount is calculated by multiplying the face amount with the price at which a trade was done.

Open exposure:

The moment a new trade is done, the investor is exposed to market movements. The buyer will benefit from rising prices, the seller gains if prices fall. Regardless of direction or face amount, the value of the counter currency will change as the price of the currency pair moves. The net difference of the counter currency amount at the present market price compared to the trade entry price is called the 'unrealized Profit or Loss'

Example: Investor A sold 1.2 lots USDCHF at 1.2180

1 lot = 100 Ounces of GOLD

(exchanging -120'000 USD against +146'160 CHF)

Market Offer 1.2155: +120'000 USD against -145'860 CHF: profit CHF 300

Market Offer 1.2195: +120'000 USD against -146'340 CHF: loss CHF 180

The profit or loss is called unrealized Profit/Loss

The value of one pip:

We are now returning to the question of the value of 1 pip. Using the last example we can express the unrealized profit or loss in pips. Between the selling price of 1.2180 and the potential profit price of 1.2155 lie 25 pips. Knowing the potential profit is CHF 300, 1 pip represents CHF 12. This

calculation is also true for the difference between 1.2180 and 1.2195 which is 15 pips or 180 CHF: $180/15=12$ CHF per pip.

1 pip can be expressed as 0.0001 in the case of currency pairs quoted to the 4th decimal or 0.01 if the price quotation ends at the 2nd decimal such as USDJPY or XAUUSD. Its value always occurs in the counter currency; in CHF for USDCHF or XAUCHF and in USD in the case of EURUSD or AUDUSD. The pips value for each particular case is now simply calculated using the face amount:

Example: 3 lots XAUUSD: $300 * 0.01 = 3$ USD

4.5 lots EURGBP: $450'000 * 0.0001 = 45$ GBP

10.2 lots SARJPY: $1'020'000 * 0.01 = 10'200$ JPY

Calculating Profit and Loss:

A successful speculator captures the price difference of a currency pair by buying when the price is low and selling the same currency pair when the price is high(er). A completed trade is made up of a trade pair; it needs a 'buy' and a 'sell' of the same currency pair and of the same face amount to complete a trade. The face amount and the price difference of the two trades will determine the net profit or loss of the completed or 'closed' trade

Example: trade 1: BOUGHT 4.2 lots USDCHF at 1.2465

trade 2: SOLD 4.2 lots USDCHF at 1.2508

price difference: $1.2508 - 1.2465 = 0.0043$ (positive value = profit), amount 4.2 lots = 420'000

PROFIT: $420'000 * 0.0043 = 1'806$ CHF

NOTE: Trade amount is USD 420'000 (first named currency)

NOTE 2: Profit or Loss is expressed in CHF (second named currency)

NOTE 3: The profit/loss is then converted into the speculators

accounting currency, in the case of USD: $CHF 1806 / 1.2508 = USD 1'443.88$