Beginning FOREX - How Are Lots Traded & What The Heck Is A Pip?

If you are new to Forex, no doubt you are confused by all of the strange and unfamiliar terminology. For example, what is a pip? Also, you are probably already aware that Forex trading can be risky. How can you limit your loss and best protect your funds? This article briefly covers how currency lots are traded to help you better understand how to plan your trading strategy and manage your funds.

In Foreign Currency Exchange (Prof FX), earnings are expressed in "pips". Pip is short for Price Interest Point, also called points. Whereas the smallest denomination in USD is the penny ($.01), in Currency Exchange, funds can be traded in an even smaller denomination, $0.0001. This means that very small movements in currency prices can create large profits.

So, a PIP is the smallest unit a currency can be traded in. The actual value of a pip is not a set price. If you are trading with a standard account, a pip is worth $10. If you are trading a mini account, a pip is only worth $1.

The value of a pip changes based upon the size of your account, because the size of your account affects how much currency you can leverage. A standard full size trading account is 100,000 units of the base currency. If you are trading in USD, a standard account has a value of $100,000 USD.

A mini lot is 10,000 units of base currency. If you are trading mini lots, you can leverage $10,000. This is why a pip in a mini account is worth less than a pip in a standard full sized account.

While Forex trading allows you to leverage more funds than you actually have, this can be a double edged sword. While you can make profits on funds that you leverage (rather than own), you can also have losses amplified as well. There are several ways, however, to manage your risk when trading Forex. If you are interested in trading Forex, you should have a definite trading strategy. You must educate yourself to know when to enter and exit the market and what kind of movements to anticipate.

You can also place something known as a stop loss order. Stop-loss orders the typical way traders minimize risk when placing an entry order. A stop-loss order to exit your position if the currency price reaches a certain point.

If you are taking a long position, you would place the stop loss order below current market price. For a short position, you would place a stop loss order above current market price. This technique allows you to manage your risk and, just as the name suggests, stop your losses at a certain point.

As you can see, Forex trading can be complex, but once you understand the basic fundamental principals of how lots are traded, its starts to come together for you. Foreign Currency Trading can be quite profitable and and exciting way to invest.