Title:
Do Not Lose Your Shirt With a Margin Account

Word Count:
643

Summary:
Introduction to FOREX margin accounts and how they work.

Keywords:
forex, forex trading, forex online, learn forex

Article Body:
The key to the FOREX market for the average investor is the margin. Without margin trading currency trading would be beyond most investors. I will explain what the margin is and how it works.

When you have a margin account you are able to control large amounts of currency with a relatively small cash deposit. When you have a margin account with a broker you are in effect borrowing money from the broker to control a larger lot of currency. Currency is normally sold in lots with a value of $100,000. A common term used when discussing margin accounts is leverage. Leverage is how much you can control with a certain amount of money. The leverage is usually displayed as a ration such as 1:100. That would allow you to control currency worth 100 times the amount of money you have invested.

To better explain this in a FOREX exchange with a 1% margin account you could control $100,000 worth of a currency while only investing $1000. Margin accounts can allow you to greatly increase your profit; they also allow you to increase your risk. With a margin account it is possible for a trader to lose more than their initial investment. With a little prudence though losses can be minimized. Most brokers will terminate a trade before the losses exceed the original deposit.

Benefits
As discussed before a margin account allows you to buy more with the money you have which can greatly increase your profit on successful trades. By controlling a $100,000 worth of currency for only $1000 the potential gain is greater. When dealing with large lots of currency even small changes can produce significant results.

Currency on the FOREX market is traded in far more precise units than actual cash is. As an example the American dollar is traded down to four decimal points. So when you were to quote the dollar against another currency you will see a price like $1.7834 instead of $1.78. A PIP is the smallest unit when trading currencies, when dealing with $100,000 lots then each pip is worth about $10.

If the price of the American dollar changes from $1.7834 to $1.7934, you have a net difference of 100 pips. If you have a lot of $100,000 then that 100 pips will translate to $1000 where as if you were not using the margin your original $1000 would only show a profit of $10. Hardly what most would consider a highly profitable trade?

In short the primary benefit of using a margin account is that it can greatly increase the profit margin of a trade.

Risks

Since there is such a significant increase in profit potential when using a margin account it only stands to reason that there is also an increase. In fact it is quite possible to have your entire margin account wiped out fairly quickly. When using a 1% margin account a shift in the currency of a single penny will cost you $1000.

The FOREX exchange has many safety features to help you reduce the risk of this happening. One example is a stop loss order. A stop loss order will automatically close out your position in a currency if the price crosses the point you have set. This allows you to limit your losses while still having the opportunity to realize a profit.

Another risk that many people overlook is that if the price nears the point where your losses are close to being equal to the value of your margin account your broker may close out your position. If you were trying to rid out a temporary downturn that you expect to turn around soon you could find that your broker has closed it causing you to lose your entire balance and have no option to make a profit if the price moves up again.

This is a basic introduction to margin accounts and how they work, visit the website listed below to learn more about the FOREX market.