MATCHBOOK FX

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About Forex

What is Forex?

Foreign Exchange (Forex) trading is simply the exchanging of one currency for another - Each Forex trade can theoretically be viewed as a 'spread ' trade where to buy one currency you must sell another.

Convention dictates that currencies are measured in units per 1 USD. For example, 1 USD is worth approximately 125 JPY (Japanese Yen) or 1 USD is worth approximately 1.5000 CHF (Swiss Francs). As a result, when USDJPY appreciates in value, it is the USD which has appreciated in value relative to the JPY and not vice-versa. Position-wise, to own or be 'Long' USDJPY means that you are long the USD and concurrently short the JPY. USD, therefore, is the default 'lead' currency.

There are, however, 4 exceptions to the USD based currency pairs. They are EUR (Euro), GBP (British Pound), AUD (Australian Dollar), and NZD (New Zealand dollar or 'Kiwi'). In these cases, the market is measured in terms of amount of USD per 1 EUR, GBP, AUD and NZD and they are the 'lead' currencies.

USDJPY Daily Bar

About the FX Market

The foreign exchange market is not a "market" in the traditional sense. There is no centralized location for trading as there is in futures or stocks. Trading occurs over the telephone and on computer terminals at thousands of locations worldwide. Foreign Exchange is also the world's largest and no one player, governments included, can directly control the direction of the market, which is why the FOREX market is the most exciting market in the world. Central banks, private banks, international corporations, money managers and speculators all deal in FOREX trading.

FOREX WORKSHOP

Topics Covered

A. Market Conventions

FX trading involves buying one currency while selling another with the hopes of benefiting from exchange rate fluctuations. An FX trade involves trading a base currency in exchange for an exchanged currency.

Example A1 Buying 100,000 USDJPY at a rate of 105.00

In this example the base currency is US dollars (USD) and the exchanged currency is Japanese Yen (JPY). The exchange rate of 105 represents the number of JPY that can be exchanged for 1 USD. Therefore buying 100,000 USDJPY at 105 translates into buying 100,000 USD in exchange for 10,500,000 JPY.

It is important to note that the base currency is always the first currency represented in a currency pair and the exchanged is always the second. Convention dictates which currency in a given pair will be the "base" and which will be the "exchanged". The next example will show how the previously discussed definitions are applied to a different currency pair.

Example A2 Selling 100,000 GBPUSD at a rate of 1.6400

In this example the British Pound (GBP) is the base currency and USD is the exchanged. An exchange rate of 1.6400 implies that each 1 GBP can be exchanged for 1.6400 USD. Therefore selling 100,000 GBPUSD at 1.6400 translates into selling 100,000 GBP in exchange for 164,000 USD.

Market convention has created the following hierarchy to determine which will be the base currency in any given pair.

1-EUR (Euro) for EUR vs. USD or EURUSD
2-GBP (British Pound) for GBP vs. USD or GBPUSD
3-USD (US Dollar) for both USDCHF and USDJPY

Therefore, based on this convention, the major pairs traded in the spot FX market are EURUSD, GBPUSD, USDJPY, and USDCHF.

B. PROFIT AND LOSS CALCULATIONS

This section will show how movements in exchange rates can generate profits and losses. This concept is most easily understood through examples.

Example B1:

By selling EURUSD a trader is speculating that the EUR will depreciate relative to the USD. As discussed in the previous section Selling 100,000 EURUSD at 1.0150 translates in to selling 100,000 EUR in exchange for 101,500 USD. In this example the EURUSD exchange rate moves lower from 1.0150 to 1.0100 before the position is covered. At an exchange rate of 1.0100 the 100,000 EUR sold earlier can be bought back for only 101,000 USD resulting in a profit of 500 USD (101,500 - 101,000). It may be useful to note that based on this example that each "pip" movement in exchange rate on a 100,000 EURUSD position is equal to $ 10 USD in profit or loss.

It may also be helpful to note that profits and losses are initially generated in the "exchanged" currency. In the case of EURUSD the exchanged currency is USD and the profit is in USD. As you will see in the following example when the exchanged currency is not USD another step must be taken to convert profits back in to USD terms.

Example B2 Buying 100,000 USDJPY at 105.00 and selling it back at 105.30

In this example the trader is speculating the USD will appreciate relative the JPY. When the position is opened, 100,000 USD is purchased in exchange for 10,500,000 JPY. As the exchange rate moves higher the amount of JPY that can be exchanged for 100,000 USD increases. At a rate of 105.30 the 100,000 USD can be sold back (covered) for 10,530,000 JPY resulting in a profit of 30,000 JPY (10,530,000-10,500,000). This 30,000 JPY profit is then converted back in to USD by dividing by the applicable prevailing USDJPY exchange rate. For MBFX customers the applicable rate will be end of day "re-Val" or NY closing rate. In this example we will use 105.30 as the applicable rate since that is where the position was closed. So 30,000 JPY/ 105.30= $284.90 USD in profits.

C. EXECUTIVE SUMMARY

On a 100,000 EURUSD position each "pip" is equal to 10 USD
On a 100,000 GBPUSD position each "pip" is equal to 10 USD
On a 100,000 USDJPY position each "pip" is equal to 1000 JPY or approximately $9.52 USD
On a 100,000 USDCHF position each "pip" is equal to 10 CHF or approximately $6.41 USD

GENERALIZED P+L CALCULATION FORMULA:

POSITION SIZE (In base currency terms) x (EXCHANGE RATE WHEN POSITION IS CLOSED - EXCHANGE RATE WHEN POSITION WAS OPENED) = PROFITS/LOSSES (In exchanged currency terms)

To convert P+L in to USD terms divide PROFITS/LOSSES by applicable USD[EXCHANGED CURRENCY] rate

i.e. 500 CHF divided by applicable USDCHF rate of 1.5600 =$ 320.51 USD

If you have any further questions please call the Matchbook FX help desk, 24 hrs, at (800)355-5255

Benefits of Trading Spot FX

1. Liquidity

1. LIQUIDITY: FOREX investors never have to worry about being "stuck" in a position due to a lack of market interest. In this US$1.5 trillion dollar per day market, major international banks are always willing to provide both a bid (buying) and ask (selling) price. Liquidity is a powerful attraction to any investor as it suggests the freedom to open or close a position at will. Because the market is highly liquid, most trades can be executed at a single market price. This avoids the problem of slippage found in futures and other exchange-traded instruments where only limited quantities can be traded at one time at a given price. The six major currencies (JPY, EUR, CHF, GBP, CAD & AUD) are generally considered to be the most liquid

2. LEVERAGE: FOREX investors are permitted to trade foreign currencies on a highly leveraged basis - up to 25 times their investment in the case of MatchbookFX. An investment of US $10,000 would permit one to trade up to US $400,000 worth of any particular currency.

3. 24 HOURS: A substantial attraction for participants in the FOREX market is that it is open 24 hours per day. An individual can react to news when it breaks, rather than waiting for the opening bell when everyone else has the same information, as is the case in many markets. This may enable market participants to take positions before an important piece of information is fully factored into the exchange rate. High liquidity and 24 hour trading allow market participants to exit or open a new position regardless of the hour.

4. SIZE FLEXIBILITY: MatchbookFX allows greater flexibility with respect to your desired trade quantity. On MatchbookFX, you can trade ANY DESIRED AMOUNT over $100,000 USD, specifically tailored to your needs or risk tolerance. Size or quantity flexibility can be especially useful to corporate treasurers who need to hedge a future cash flow or portfolio managers who need to hedge foreign equity exposure.

5. SETTLEMENT FLEXIBILITY - This concept, a corollary to point # 4, allows you to trade for various settlement dates or 'maturities' out to 1 year further allowing you to tailor your trades or hedges to your specific needs. This feature of trading forex on MatchbookFX differs from futures where settle dates are relegated to 4 'expirations' per year, and can also be quite useful to corporate treasurers and portfolio managers.

6. NEVER A 'BEAR' MARKET: Another advantage of the FOREX market is that there is no 'bear' market, per se. Currencies are traded in pairs, for example US dollar vs. yen or US dollar vs. Swiss franc. Every position involves the selling of one currency and the buying of another. If one believes the Swiss franc will appreciate against the dollar, one can sell dollars and buy Swiss francs. Or if one holds the opposite belief, one can buy dollars for Swiss francs. The potential for profit exists as long as there is movement in the exchange rate or price. One side of the pair is always gaining, and provided the investor picks the right side, a potential for profit ALWAYS exists.

7. FREE AND FAIR FLOW OF INFORMATION: Ever notice in the stock market that a certain stock is suddenly down 5% or more but you have absolutely no idea what caused such a quick spike? Usually, it's not until the next morning when you read it in the newspaper that you find out that earnings forecasts have been revised downward; or that an insider at a particular company has resigned; or that some other influential piece of information was released that you were not privy to. Imagine how much money you could have saved had you known this vital information at the

Cash FX vs. Currency Futures

As an investor it is important for you to understand the differences between cash FOREX and currency futures.

- In currency futures, the contract size is predetermined. With MatchbookFX (SPOT FX), you may trade any desired amount above $100,000 USD
- The futures market closes at the end of the business day (similar to the stock market) If important data is released overseas while the U.S. futures markets is closed, the next day's opening might sustain large gaps with potential for large losses if the direction of the move is against your position. (Note: Recently, Globex ™ introduced overnight currency trading but liquidity is poor and bid/ask spreads are unduly wide) The Spot forex (MATCHBOOK FX) market runs continuously on a 24-hour basis from 7:00 am New Zealand time Monday morning to 5:00 pm New York Time Friday evening. Dealers in every major FX trading center (Sydney, Tokyo, Hong Kong/Singapore, London, Geneva and New York/Toronto) ensure a smooth transition as liquidity migrates from one time-zone to the next.
- Furthermore, currency futures trade in non-USD denominated currency amounts only whereas in spot forex, an investor can trade either in currency denominations, or in the more conventionally-quoted USD amounts.
- The currency futures pit, even during Regular IMM (International Money Market) hours suffers from sporadic lulls in liquidity and constant price gaps. The spot forex market offers constant liquidity and market depth much more consistently than Futures.
- With IMM futures one is limited in the currency pairs he can trade - Most currency futures are traded only versus the USD - With spotforex, (as with MatchbookFX) one may trade foreign currencies vs. USD or vs. each other on a 'cross' basis as well - ex: EURJPY, GBPJPY, CHFJPY, EURGBP and AUDNZD.

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