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FOREX · BEGINNER · LESSON 5 OF 15

How a Forex Trade Makes or Loses Money

Two complete trades from start to finish, the simple formula behind every profit and loss, the costs that come off the result, and why winning often is not the same as making money

11 min read 8 quiz questions with answer key

FOREX · BEGINNER · LESSON 5 OF 15

How a Forex Trade Makes or Loses Money

IN ONE SENTENCE

A forex trade makes or loses money according to how far the price moves, in which direction, and how big the position is. This lesson follows a winning long trade and a losing short trade step by step, shows how costs turn gross profit into net profit, and explains balance, equity and why the size of wins and losses matters more than how often you win.

The life of a trade

Every trade goes through the same four stages:

1. **Open.** You buy or sell a pair. A buy opens at the ask; a sell opens at the bid (Lesson 3).
2. **Open position.** While the trade is running, its result changes with every price move. This running result is called **floating** or **unrealized** profit or loss. It is not yet real money.
3. **Close.** You end the trade by doing the opposite: a buy is closed by selling at the bid, and a sell is closed by buying at the ask. You can close it yourself, or an order such as a stop loss or take profit can close it automatically.
4. **Realized.** Once the trade is closed, the result becomes **realized** profit or loss and is added to, or taken from, your account balance.

Many beginners treat a floating profit as money already earned, or refuse to close a floating loss in the hope that it will come back. Remember that nothing is final until the trade is closed.



Figure 1. The four stages of every trade. Profit or loss floats while the trade is open and becomes real only when it is closed.

A winning long trade

Anna expects the euro to strengthen. With EUR/USD quoted at 1.0848 / 1.0850, she **buys 1 standard lot** at the ask, **1.0850**. One standard lot is 100,000 euros, and for a pair ending in USD each pip is worth $10 (Lesson 4).

Over the next two days the euro rises. When the bid reaches **1.0910**, Anna closes the trade by selling at that price.

- Price change: 1.0910 − 1.0850 = 0.0060, which is **60 pips**.
- Profit: 60 pips × $10 = **$600**.
- The same result without pips: 0.0060 × 100,000 euros = 600 US dollars.

Notice that the spread is already included: Anna bought at the higher ask price and sold at the lower bid price. The only costs that can still be added are commission and overnight financing, which you will see below.

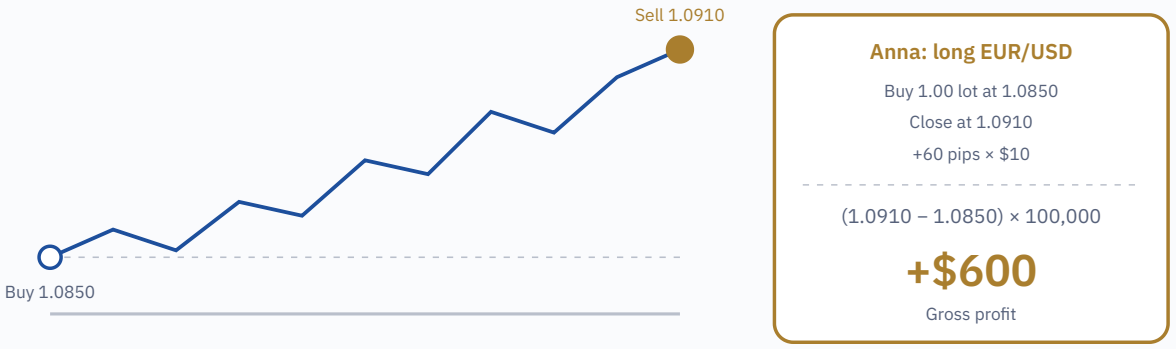


Figure 2. Anna's long trade. She buys at the ask, the price rises 60 pips, and she sells at the bid for a gross profit of $600.

A losing short trade

John expects the Japanese yen to strengthen against the dollar, so he **sells 0.50 lot of USD/JPY**, which is 50,000 US dollars, at the bid, **150.40**. He places a stop loss above a recent high to limit his loss if he is wrong.

Instead of falling, USD/JPY rises. His stop loss closes the trade by buying at the ask, **151.10**.

- Price change against him: 151.10 − 150.40 = 0.70, which is **70 pips**.
- In yen: 0.70 × 50,000 = **35,000 yen**, because USD/JPY is quoted in yen.
- In dollars: 35,000 ÷ 151.10 = about **$231.63**.

For a short trade, profit comes when the price falls, and loss when it rises. John's analysis was wrong, but his stop loss did its job: it kept the loss to a size he had chosen in advance. A loss like this

is a normal part of trading. Lesson 12 shows how to decide how much to risk on each trade.



John: short USD/JPY

Sell 0.50 lot at 150.40

Stopped out at 151.10

−70 pips = −35,000 JPY

−35,000 ÷ 151.10

−$231.63

Loss, limited by the stop

Figure 3. John's short trade. He sells, the price rises 70 pips instead of falling, and his stop loss closes the trade. The loss is worked out in yen and converted to dollars.

One formula for every trade

Both examples follow the same simple rule. The result of a trade, in the quote currency, is:

- **For a long trade (buy):** (close price − open price) × units
- **For a short trade (sell):** (open price − close price) × units

"Units" means the trade size in the base currency: 100,000 for 1 lot, 50,000 for 0.50 lot and so on. A positive answer is a profit, a negative answer a loss.

The answer comes out in the **quote currency**, the second currency of the pair. If that is the same as your account currency, you are done. If not, the platform converts it at the current rate, just as John's 35,000 yen became about $231.63. That is why the same number of pips can be worth slightly different amounts depending on the pair and on the exchange rate at the moment you close.

Long trade (buy)

(close − open) × units

Profit when the price rises

Short trade (sell)

(open − close) × units

Profit when the price falls

The answer is in the quote currency

If your account is in another currency, the platform converts it at the current rate.

Figure 4. The same simple formula works for every trade. Only the order of the prices changes between long and short.

From gross profit to net profit

The result from the formula is the **gross** profit or loss. What lands in your account, the **net** result, can be reduced by two other costs:

- **Commission.** On raw spread accounts the broker charges a fee per lot traded, for example $7 per standard lot for opening and closing (Lesson 3).
- **Swap.** If a trade is still open at the daily rollover, 5 p.m. New York time, it is charged or paid a small overnight financing amount called a **swap** or rollover fee. It depends on the interest rates of the two currencies and on the direction of the trade. It can be a cost or, sometimes, a small credit. On Wednesdays many brokers charge three days of swap to cover the weekend. Swaps are covered in more detail in the Intermediate level.

Suppose Anna traded on a raw spread account and held her trade over two nights. Her gross profit of $600, minus a $7 commission and $3 of swap, leaves a **net profit of $590**. For a single trade the difference is small. Over hundreds of trades, or for positions held for weeks, costs can decide whether a strategy makes money at all.

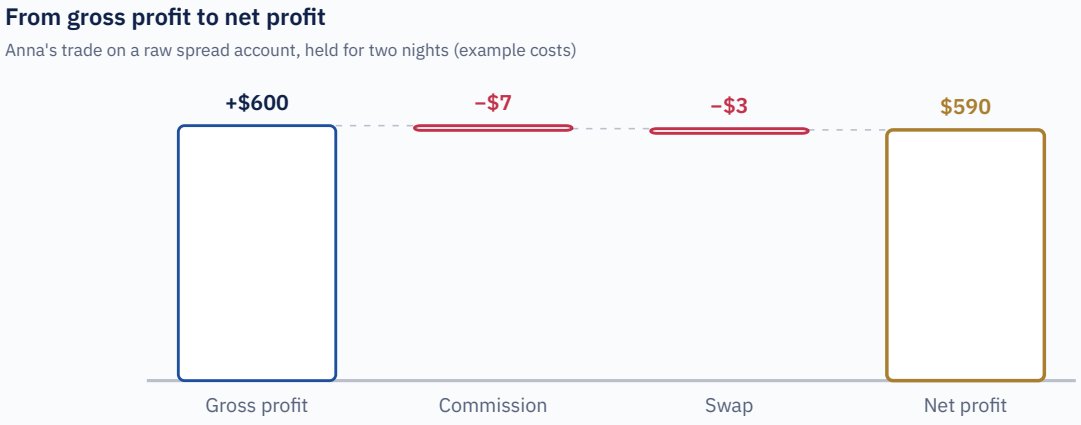


Figure 5. Commission and swap reduce gross profit to net profit. The spread is already included in the prices Anna bought and sold at. The costs are examples.

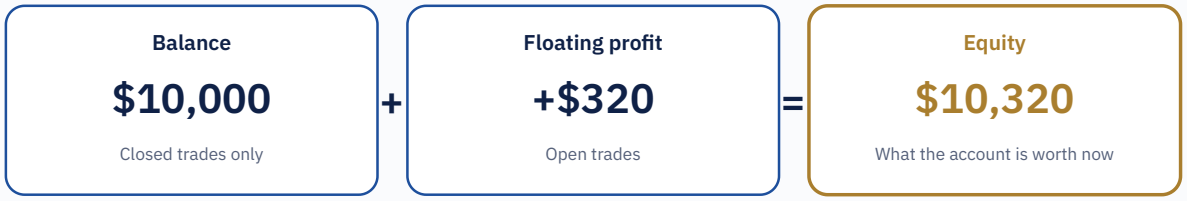
Balance, equity and floating profit

Your trading platform shows a few numbers at the bottom of the screen. Two of them are especially important:

- **Balance** is the money in your account from deposits, withdrawals and **closed** trades only. It does not change while a trade is open.
- **Equity** is your balance plus or minus the floating profit or loss of all open trades. It shows what your account would be worth if you closed everything right now.

Imagine Anna's account has a balance of $10,000. While her EUR/USD trade is open and 32 pips in profit, her floating profit is $320, so her equity is $10,320. If the price fell back, her equity would fall too, but her balance would stay at $10,000 until she closed the trade.

Equity is the number that really matters. Your broker uses it, not the balance, to decide whether you have enough money to keep trades open. Lesson 10 explains margin and what happens when equity falls too far.



The balance changes only when a trade is closed. Equity moves with every price change.

Figure 6. Balance, floating profit and equity, as shown on most trading platforms.

Winning often is not the same as making money

New traders often focus on how many of their trades win, called the **win rate**. But the money result depends just as much on how big the wins and losses are.

Look at ten trades: six winners of $100 each and four losers of $200 each. The win rate is 60%, which sounds good. But the six winners make $600 and the four losers cost $800, so the trader is down **$200**. Another trader who wins only four times out of ten, but makes $300 on each winner and loses $100 on each loser, finishes $600 ahead.

This is why professional traders think about the relationship between their average win and their average loss, usually called the **risk-to-reward ratio**, as well as their win rate. A common beginner habit, closing winning trades quickly to "lock in" profit while leaving losing trades open in the hope they recover, produces exactly the losing pattern above. Lesson 12 shows how to plan both sides of a trade before you open it.



Figure 7. A 60% win rate can still lose money if the losses are bigger than the wins.

EXAMPLE: THINKING IN PERCENTAGES

Dollar amounts mean little without the account size. Anna's $600 profit is 6% of a $10,000 account, but only 0.6% of a $100,000 account. John's $231.63 loss on a $5,000 account is about 4.6%. Thinking in percentages of your account helps you compare trades fairly and is the first step towards controlling risk.

Why this matters for traders

- **Know the result before you trade.** With the formula and the pip value, you can work out what a trade will make or lose at your target and at your stop before you click buy or sell.
- **Watch equity, not balance.** Open trades can change your equity quickly. A balance that looks healthy can hide large floating losses.
- **Count every cost.** Spread, commission and swap all come off your result. For trades held over many nights, check the swap rates on your platform.
- **Judge your trading by size as well as frequency.** Keep a record of your average win and average loss, not just how often you win. The trading journal in Lesson 15 makes this easy.

Key terms

Floating (unrealized) profit or loss	The running result of a trade that is still open. It changes with every price move.
Realized profit or loss	The final result of a closed trade, added to or taken from the account balance.

Gross profit	The result of a trade from the price move alone, before commission and swap.
Net profit	The result after all costs have been taken off.
Swap (rollover fee)	A small overnight financing charge or credit for trades held past the daily rollover, based on the two currencies' interest rates.
Balance	Account money from deposits, withdrawals and closed trades. It does not include open trades.
Equity	The balance plus or minus the floating profit or loss of all open trades.
Take profit	An order that closes a trade automatically when the price reaches a chosen profit level.
Win rate	The share of trades that end in profit.
Risk-to-reward ratio	The size of the possible loss on a trade compared with the size of the possible gain.

Key takeaways

1. A trade is opened, floats while it is running, and becomes realized profit or loss only when it is closed.
2. For a long trade the result is (close − open) × units; for a short trade it is (open − close) × units, in the quote currency.
3. If the quote currency is not your account currency, the result is converted at the current exchange rate.
4. Commission and swap turn gross profit into a smaller net profit; the spread is already included in the buy and sell prices.
5. Balance includes only closed trades, while equity includes open ones; the size of wins and losses matters as much as the win rate.

Test yourself

Circle one answer for each question. The answer key with explanations is on the next page. You can also take this quiz online at markettalks.info and see your score instantly.

1. What is floating (unrealized) profit?

A Profit already added to your balance
B The running result of a trade that is still open
C Profit from swap payments
D Profit that cannot be withdrawn for 30 days

2. Anna buys 1 standard lot of EUR/USD at 1.0850 and closes at 1.0910. What is her gross profit?

A $60
B $600
C $6,000
D $1,091

3. John sells USD/JPY and the price rises. What happens?

A He makes a profit
B He makes a loss
C Nothing, because USD/JPY is a yen pair
D He makes a profit only if he holds overnight

4. What is the profit or loss formula for a short trade, in the quote currency?

A (close − open) × units
B (open − close) × units
C (open + close) × units
D units ÷ (open − close)

5. A USD/JPY trade loses 35,000 yen and USD/JPY is 151.10. About how much is that in US dollars?

A $35.00
B $231.63
C $5,288
D $35,000

6. **Gross profit is $600, commission is $7 and swap is −$3. What is the net profit?**

A $610
B $600
C $590
D $593

7. **Your balance is $10,000 and your open trades show a floating loss of $450. What is your equity?**

A $10,450
B $10,000
C $9,550
D $450

8. **A trader wins 6 of 10 trades, making $100 on each win and losing $200 on each loss. What is the result?**

A +$600
B +$200
C −$200
D −$800

Answer key

1 B

The running result of a trade that is still open

Floating profit changes with every price move while the trade is open. It becomes realized only when the trade is closed.

2 B

$600

The price rose 60 pips. For a pair ending in USD, one standard lot is worth $10 per pip, so 60 × $10 = $600.

3 B

He makes a loss

A short trade profits when the price falls. If the price rises, the trade loses money.

4 B

(open − close) × units

For a short trade you sell first and buy back later, so you profit when the close price is lower than the open price: (open − close) × units.

5 B

$231.63

The result is in the quote currency, yen. Converting at 151.10 yen per dollar gives 35,000 ÷ 151.10, about $231.63.

6 C

$590

Net profit is gross profit minus all costs: $600 − $7 − $3 = $590.

7 C

$9,550

Equity is the balance plus or minus floating profit or loss: $10,000 − $450 = $9,550. The balance stays $10,000 until the trades are closed.

8 C

−$200

Six wins make $600 and four losses cost $800, so the trader is down $200 despite a 60% win rate. The size of wins and losses matters as much as how often you win.

SOURCES

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