Things You Must Know About Crypto Leveraged Trading

Original:
https://www.btcc.com/en-US/academy/research-analysis/things-you-must-know-about-crypto-leveraged-trading

Leveraged trading in cryptocurrency has become so popular today, while it can be very confusing, especially for beginners. Hence before experimenting with leverage, it's crucial to understand what it is and how it works. This article will focus on leverage trading in crypto markets.

What Is Leverage In Crypto Trading?

As one of the most important features in crypto trading, leverage refers to using borrowed capital to make trades. Leverage trading can amplify your buying or selling power, allowing you to trade with larger amounts. So even if your initial capital is small, you can use it as collateral to make leveraged trades, through which your trading profits will be multiplied more than the original investment could bring. While leveraged trading can magnify the potential trading rewards if the market moves in traders' favor, it can also magnify the risk if the market goes against their position, which may lead to substantial losses. That's why you must be careful when using leverage to trade crypto.

The amount of leverage is also described as a ratio, such as 1:10 (10x), 1:50 (50x), or 1:100 (100x). It shows how many times your initial capital is multiplied. Different levels of leverage are offered by different crypto exchanges, with some providing 100x leverage allowing traders to open a position that is 100 times the value of their initial deposit, others limiting the leverage to 10x, 20x, or 50x.

How Does Crypto Leveraged Trading Work?

Leverage trading is often referred to as margin trading. Margin is the minimum percentage of the amount that is required by the trader as collateral in order to open an increased position. Before you can borrow funds and start trading with leverage, you need to deposit funds into your trading account. The initial capital you provide is what we call the collateral. The collateral required depends on the leverage you use and the total value of the position you want to open. Leverage is exactly the amount by which you can multiply your position during trading. So, if a margin trader opens a trade with 100x leverage, his exposures and potential profits will be multiplied by 100 times.

For example, imagine that you have $100 in your exchange account but want to open a position worth $10,000 in Ethereum (ETH). Then you need to choose a 100x leverage to achieve this.

On the other hand, if you want to open a $5,000 position on Bitcoin (BTC) with 100x leverage, you only need to use $50 (1/100 of $5,000) as collateral for the borrowed capital.

Now assume that the price of BTC increases by 20%. In this case, the profit gained from that position would be $1,000, the same a trader with $5,000 in their trading account would make from a standard position with no leverage. So, if you had not used leverage, you would have earned $10 only on your $50 capital.

However, if the BTC price drops 20%, your position would be down $1,000. Since your initial capital (collateral) is only $50, a 20% drop would cause a liquidation (your balance goes to zero). In fact in this case, you could get liquidated even if the market only drops 10%. To avoid being liquidated, you need to add more funds to your wallet to increase your collateral before the liquidation price is reached. In most cases, the exchange will send you a margin call before the liquidation happens (e.g., an email telling you to add more funds).

Why We Trade With Leverages?

As explained above, the attraction of crypto leveraged trading is clearly evident. Generally we can summarize the benefits of leveraged trading as follows:

- **Magnified profits.** Traders with less capital can receive the same profit as those with higher capital by using 100x leverage to increase their position size. This is a great shortcut to grow the trading accounts faster by benefitting from higher returns. As mentioned above, even if your trading account holds $50, you can open a position of $5,000 with 100x leverage.

- **Enhanced capital liquidity & gearing opportunities.** When you need less fund, you have the free capital to hedge your portfolio with multiple trades at the same time, which helps get the most out of your money and minimize the investing risks. For example, you can open a short hedge for protecting against the loss of a failed long position in the event where the value of the asset falls

Risk Management In Leveraged Trading

It is evident that crypto trading with leverage has both advantages and risks. If the trade is successful, traders can earn profits based on the increased position size, if unsuccessful, however, it is another story.

Trading with high leverage might require less fund to start with, but it increases the risks of liquidation. The higher the leverage, the higher the risks and the smaller your volatility tolerance will be. If your leverage is too high, even a 1% price down could lead to substantial losses. Therefore, using lower leverage would give you more margin of error to trade. This is why many crypto exchanges have limited the maximum leverage available to new users.

Risk management strategies like stop-loss and take-profit orders help minimize losses in leveraged trading. You can rely stop-loss order to automatically close your position at a specific price, which is very helpful when the market moves against you because it can protect you from huge losses. Take-profit order is the opposite: it can automatically close when your profits reach a certain value. This allows you to secure your earnings before the market condition changes.

At this point, you should be clear that leveraged trading is a double-edged sword that can multiply both your profits and losses exponentially. It involves a high level of risks, especially in the volatile crypto market where wild price movements are common. At BTCC, we encourage you to take risk management seriously whenever trading with leverage. And BTCC also provides many effective tools to help you control your trading risks. You should always be extra careful, and don't forget to DYOR (Do You Own Research) to understand how to use leverage properly and plan your trading and risk management strategies.

Leveraged Trading Fees

The interest rate on offer with leveraged trading is a further aspect that needs to be considered, it depends on the length and leverage of your position and varies from exchange to exchange. The fee is not usually applied to the initial investment but to the increased position size. This is fair because a trader who is opening the trade with the same size of position without leverage would pay the same. In some cases, the broker or trading platform takes extra funding fees for margin trades, which means that you may end up paying fairly high-interest rates.

This is why it is essential to choose a crypto trading platform that offers low fees and preferably does not charge additional funding fees. BTCC seems to be a very good choice from this perspective where you can trade hot cryptocurrencies like Bitcoin, Ethereum and many other altcoins with 100x leverage.

In conclusion

Leverage allows you to get started easily with a lower capital and the potential to gain higher profits. However, leverage combined with crypto market volatility could also cause quick liquidation, especially if you're taking 100x leverage to trade. Hence keep in mind that always trade with caution and evaluate the risks before taking on leveraged trading. You should never trade funds you cannot afford to lose, especially when using leverage.

For those who decide to proceed, the next step will be to choose the best crypto exchange with leverage, which is not always easy as there are many cryptocurrency platforms offering leveraged trading. For this purpose, you can refer to our another related article for more information.

Related Posts:

What is Leverage in Cryptocurrency? How Can I Trade at 100X Leverage?

How to trade contracts on BTCC? BTCC Account Guide.

Best Crypto Exchange to Trade with Leverage

Best High Leverage Crypto Trading Exchange Platform