What is the meaning of 'long' or 'short' positions?

Long and short positions are nothing but two methods of trading stocks. Here's throwing light on them.

Many investors use a host of strategies to earn profits by trading stocks. One such strategy is going long or going short on a stock. Let us understand what these phrases mean and how are they useful to traders.

Long position

Taking a long position means buying a contract with the intention of selling it at a higher price later and thereby making profit. However, if the price goes down, the trader has to bear the loss up to the extent of the fall in price. Many traders use the terms 'buy' and 'long', inter-changeably.

Example: Say you purchase 100 shares of ABC at Rs 20 per share. So, you pay a total of Rs 2,000 for this transaction. If a month later the price of this stock moves up to Rs 25, you sell these stocks and earn a profit of Rs 500 (Rs 5 x 100 shares).

Short position

Taking a short position means selling a stock first with the intention of buying it back at a lower price, thereby making a profit from the difference in price. In such a transaction, the trader borrows a set of stocks from the broker, and sells it in the open market. He has to buy these stocks later since the borrowed stocks must be returned to the broker. In such a scenario, if the price of the stock falls, the trader will make a profit, and in case it goes up, he will incur losses.

Example: Say you sell 100 shares of ABC at Rs 10 per share. So, you receive a total amount of Rs 1,000. If, after a month, the price of this stock comes down to Rs 7, you buy 100 shares again for Rs 700, making a total profit of Rs 300 (Rs 1,000 – Rs 700).