



SNS College of Technology

Coimbatore - 35



23BAE703- Derivatives and Risk Management

Unit I – Introduction to Derivatives



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Recap

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Forwards Contract



Guess the Topic!

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Futures Contract



Points to Discuss

- **Futures Contract– Meaning**
- **Futures Contract – Types**
- **Futures Contract - Settlement**
- **Futures Contract-Closure**

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REcap

➤ Forward Contract Meaning

➤ Types

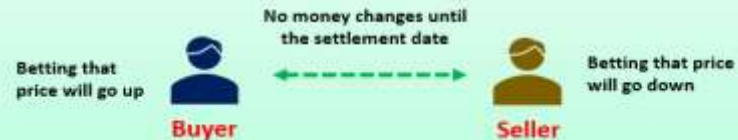
➤ Settlement

➤ Closure



Forward Contracts

A forward contract is a customized contract between two parties to buy or sell an underlying asset on time at a price agreed today.



Forward Market



Forwards, Futures and Swaps





Futures contract

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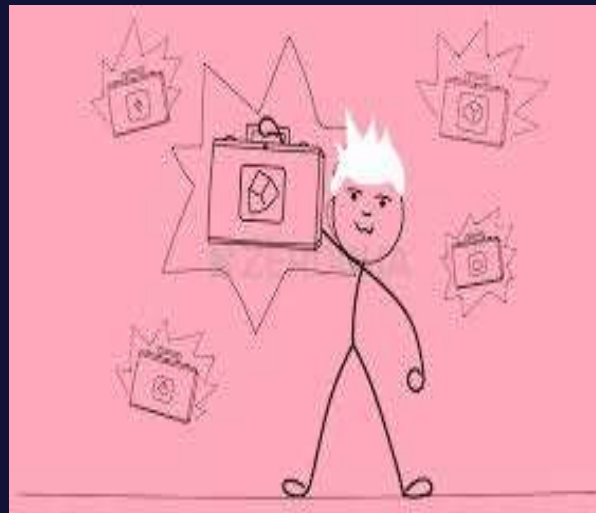
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- A futures contract is an agreement between two parties to buy or sell an asset at a certain time in the future at a certain price.





Forward contract

- It is a standardized exchange-traded contracts

Futures Contracts
are an agreement to
buy or sell commodities such as



wheat corn oil

for a specific price on a future date.



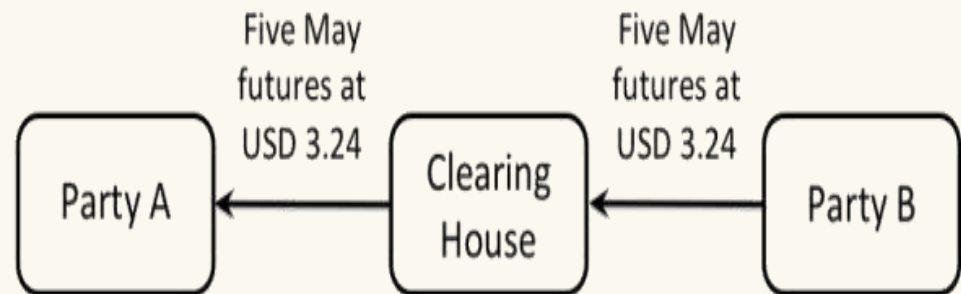
Forward contract

- Example:
- Two parties entered into the futures contract on 5, May at a pre-agreed price of USD \$3.24.
- Implemented / executed the contract on 5, May at the specified price

Two parties transact a futures contract.



It is implemented as two contracts.





Futures Contract



Future Contract Between Buyer and Seller

Buyer

Buy 100 gallon after 2 months on 1st August 2015



Seller

Sell 100 gallon after 2 months on 1st August 2015

On the price

Futures Market

A financial exchange where people can trade futures contracts.

Farmer



SELL

Futures Exchange

FUTURES CONTRACT

Product:



Delivery: 7/11/2018

QTY: 4,000 Bushels

Price: \$4.50

Signature _____

Trader



BUY

Commodities



BREAK



Futures contract

- Important Terminologies
 - Standardization
 - Clearing House
 - Settlement Price





Futures Contract: Steps

Get a trading accounts

Arrange for margin money – the percentage of the contracts total value

Deposit margin money with broker, who passes it on to the exchange

Place buy/sell order with trader

Exchange match your order if seller/buyer available at given price



Futures Contract



THERE ARE TWO MAIN TYPES OF FUTURES CONTRACTS

FINANCIAL FUTURES

WHICH INCLUDES:

- stock indexes
- currency markets
- interest rate products

PHYSICAL FUTURES

WHICH INCLUDES:

- energy markets
- metals
- agricultural
- softs



Types

- **Currency Futures**
- **Stock Futures**
- **Index Futures**
- **Commodities Futures**





Futures Contract: Termination

**Delivery of
the asset
specified in
the contract**

**Cash
Settlement
at
expiration**

**A position
can be
terminated
by making a
close-out or
offsetting
trade in the
futures
market**

**Exchange
for
Physicals –
off the floor
of the
exchange
(called an
ex-pit
transaction)**



Assessment

Futures markets have grown rapidly because futures

- (a) are standardized.
- (b) have lower default risk.
- (c) are liquid.
- (d) all of the above.

All of the above



Summary

- Meaning of Futures Contract
- Important Terminologies
- Steps involved
- Types
- Settlement
- Closure





References

- <https://www.investopedia.com/terms/f/futurescontract.asp#:~:text=A%20futures%20contract%20is%20a, trading%20on%20a%20futures%20exchange.>

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THANK YOU...

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