FAC Summer Project '24

Deciphering Decisions

Financial Instruments

Types of Trader

- Hedgers
- Speculators
- Arbitrageurs

Forward Contracts

A forward contract is a customized financial agreement between two parties to buy or sell an asset at a specified future date for a price agreed upon today.

Specification of futures contracts

- Asset
- Contract Size
- Delivery Arrangement
- Delivery Month
- Price Quote

Futures Contracts

Futures are standardized financial contracts obligating the buyer to purchase, and the seller to sell, a specific asset at a predetermined future date and price.

Futures vs Forward Contract

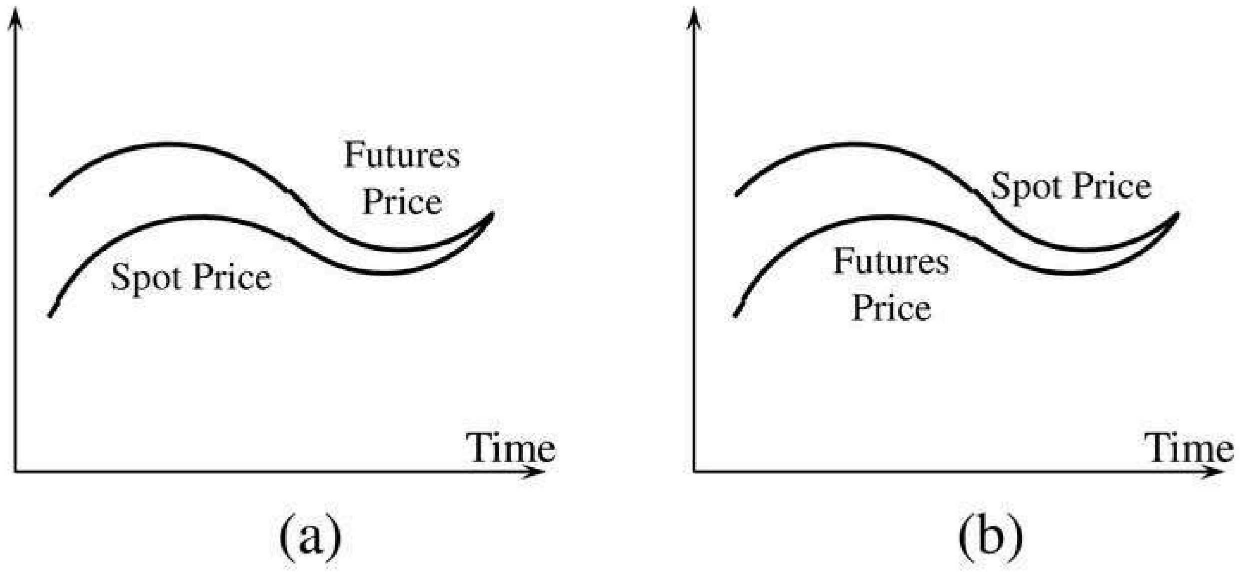
Forward	Futures
Private agreement between the parties	Subject of exchange trading
No standardization	Standardization (price, date, conditions)
Single delivery date specified	Date range during which delivery is possible
Settled at the end of the contract validity	Settled daily
Physical delivery is common	Physical delivery is missing

How different traders use the instruments

- Hedgers- Uses futures mainly to offset some existing holding
- Speculators-Uses futures to bet on an asset going up or down
- Arbitrageurs- Uses futures to exploit inefficiencies in the market

Should Futures and Spot price be the same?

Convergence of Futures to Spot



What if the Future price does not equal to the Spot price?

Basis Risk

- Basis = Spot Price – Futures Price.
- How does basis effect hedging?

Cross Hedging

- When is this done?
- Why is this done?
- How is this done?

Risk Free Rate

Bonds and their pricing

Futures and their pricing

That’s all !!

THANK YOU