Chapter 1 — Introduction

Derivatives are financial instruments whose value is derived from (hence, the name *"derivatives"*) the value of an underlying variable. This underlying could be an asset, index, commodity, currency, rate or even event. They are commonly used for **hedging risk, speculation, and arbitrage**.

> **Note**
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> **Contact Information:**
> **Name:** Dr. Sankalp Purushottam Naik
> **Email:** sankalpnaik@outlook.in

These notes provide an overview of **Chapter 1: Introduction**. It covers foundational concepts and illustrative examples to help readers understand the basics of derivatives.

1 Types of Derivatives

Derivatives can be broadly classified into the following categories:
1. **Forwards**: Customized contracts between two parties to buy or sell an asset at a specified price on a future date.
2. **Futures**: Standardized contracts traded on exchanges to buy or sell an asset at a predetermined price at a specified time in the future.
3. **Options**: Contracts that give the holder the right, but not the obligation, to buy or sell an asset at a specified price before or on a certain date.

4. **Swaps**: Agreements to exchange cash flows or other financial instruments between two parties at specified intervals.

2 Key Concepts