TOPIC: MARKET FOR CURRENCY FUTURES AND CURRENCY OPTIONS

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Currency Futures

Currency futures are a forex futures trading instrument with a currency future exchange rate as the underlying asset, such as the euro to US dollar exchange rate or the British Pound to US dollar exchange rate. Currency futures are fundamentally the same as all other futures markets (index and commodity futures markets) and are traded in the same manner.

Currency futures are based on two different currencies' exchange rates. The euro and the dollar (EUR/USD) are an example of a currency pair with an exchange rate. The first currency indicated in the pair is the governing currency.

Futures dealers are concerned about the euro price in this situation. Traders purchase a contract for a specific amount, and the contract's value fluctuates with the value of the euro. Currency futures only trade in one contract size, so traders must trade in multiples of that.

Features of Currency Futures

Mentioned below are the key attributes of currency futures prices:

1. **Underlying Asset:**

   This is the currency exchange rate that has been specified.

2. **Expiration Date:**

   This is the final settlement for cash-settled futures. It is the date on which the currencies are exchanged for physically delivered futures.

3. **Size:**

   The sizes of contracts are all the same.

4. **Margin Requirement:**

   An initial margin is necessary to enter into a futures contract. A maintenance margin will be established, and if the original margin goes lower than this level - a margin call will occur, requiring the trader or investor to deposit money in order to raise the initial margin over the maintenance margin.

Currency Option

A currency option (also known as a forex option) is a contract that gives the buyer the right, but not the obligation, to buy or sell a certain currency at a specified exchange rate on or before a specified date. For this right, a premium is paid to the seller.

Currency options are one of the most common ways for corporations, individuals or financial institutions to hedge against adverse movements in exchange rates.

Features of Currency Option

- Currency options give investors the right, but not the obligation, to buy or sell a particular currency at a pre-specific exchange rate before the option expires.
- Currency options allow traders to hedge currency risk or to speculate on currency moves.
- Currency options come in two main varieties, so-called vanilla options and over-the-counter SPOT options.

Exchange rate determination in the forward markets

A forward market is an over-the-counter market that determines the price of a financial instrument or asset for delivery in the future. Forward markets can be used to trade a variety of instruments, but the word is most commonly associated with the foreign exchange market.

1. Investment assets vs. consumption assets Short selling
2. Assumptions and notations
3. Forward price for an investment asset that provides no income
4. Forward price for an investment asset that provides a known cash income
5. Forward price for an investment asset that provides a known dividend yield
6. Valuing forward contracts
7. Forward prices and futures prices
8. Stock index futures
9. Currency futures
10. Commodity futures
11. Cost of carry

Salient features of FEMA

Foreign Exchange Management Act, 1999 (FEMA) came into force by an act of Parliament. It was enacted on 29 December 1999. This new Act is in consonance with the frameworks of the World Trade Organisation (WTO). It also paved the way for the Prevention of Money Laundering Act, 2002 which came into effect from July 1, 2005. This topic would be of importance in the IAS Exam for both Prelims and Mains. In this article, you can learn all about FEMA and FERA for the IAS exam economy segment.

1. It gives powers to the Central Government to regulate the flow of payments to and from a person situated outside the country.
2. All financial transactions concerning foreign securities or exchange cannot be carried out without the approval of FEMA. All transactions must be carried out through "Authorised Persons."
3. In the general interest of the public, the Government of India can restrict an authorized individual from carrying out foreign exchange deals within the current account.
4. Empowers RBI to place restrictions on transactions from capital Account even if it is carried out via an authorized individual.
5. As per this act, Indians residing in India, have the permission to conduct a foreign exchange, foreign security transactions or the right to hold or own immovable property in a foreign country in case security, property, or currency was acquired, or owned when the individual was based outside of the country, or when they inherit the property from individual staying outside the country.