Unit-I

Lecture-10

Different types of Foreign exchange market are as follows:

Spot Market
The spot market is a market in which quick transactions regarding currency exchange takes place. Here buying and selling of currencies is done for immediate delivery. Immediate payment at the current exchange rate is provided to buyers and sellers in the spot market. The Trade-in spot market takes one or two days for settlement of transactions and allows traders to open to the volatility of the currency market. This can increase or decrease price, between agreement and trade. Spot market almost accounts for one-third of currency exchange transactions.

Forward Market
It is a market in which transactions are done for doing trade at some future date. Here both payment and delivery are done at future date at agreed exchange rate also termed as the forward exchange rate. The contract is made between buyers and sellers for sale and purchase of currency after 90 days. Forward contracts are non-standardized contracts. It means that these contracts can be customized or tailored according to the needs of participants. At the time of entering the contract, no security deposit is required as no money exchange takes place.

Future Market
Future market is also similar to the forward market. In future market, contract are made between buyers and sellers to do trade in future. All payments and delivery in this market are done at decided exchange rate which is also termed as future rate. Whereas future contracts are standardized contracts and cannot be customized. These contracts are standardized in terms of their date, features, size, and cannot be negotiated. Trading on future market is centralized on stock exchanges like BSE, NSE, and KOSPI.

Swaps Market
Swap market is one where transactions for simultaneous lending and borrowing of two different currencies are done between investors. It is a contract between two or more parties for exchanging cash flows on the basis of a predetermined notional principal amount. In the swap market, there two types of swap transactions done that are currency swap and interest swap. Currency swap is an exchange of a fixed currency rates of one country with a floating currency rate of another country. Interest swap means the exchange of floating interest rate with a fixed rate of interest.

Options Market
The options market is one where transactions are done for exchanging one currency with at agreed rate and on a specified date. Under the option contract, it is an option for an investor to convert the currency but not under any obligation to do so. The buyer of the option has the right but not an obligation to sell or purchase the underlying currency in the contract at future date and at agreed rate. Options are of two types that

is call option and put option. A put option gives the right to sell and call option gives the right to buy.

Functions of Foreign Exchange Market

The various functions of the Foreign Exchange Market are as follows:

- **Transfer Function:** The basic and the most obvious function of the foreign exchange market is to transfer the funds or the foreign currencies from one country to another for settling their payments. The market basically converts one's currency to another.
- **Credit Function:** The FOREX provides short-term credit to the importers in order to facilitate the smooth flow of goods and services from various countries. The importer can use his own credit to finance foreign purchases.
- **Hedging Function:** The third function of a foreign exchange market is to hedge the foreign exchange risks. The parties in the foreign exchange are often afraid of the fluctuations in the exchange rates, which means the price of one currency in terms of another currency. This might result in a gain or loss to the party concerned.