Derivatives

Accounting & Finance

The four building blocks, and what each obliges.

Instrument and obligation.

Instrument	Gives	Obligation
Forward	A price agreed now for later	Both sides must transact
Future	A standardised, exchange-traded forward	Both sides, margined daily
Option	The right, not the duty	Buyer chooses; seller must comply
Swap	An exchange of cash flow streams	Both sides, over time

An option buyer's loss is capped at the premium. An option seller's loss can be unlimited. That asymmetry is the key risk.