EXAMPLE ANSWER MIDTERM 22-2 Q1

PART I.

1. In ancient times, derivatives conditions were embedded in contracts as trades are based on samples for the difficulty of transportation. Options allow refusing delivery if goods are different than samples. Bill of change is the early form of forward foreign contracts and became the fundamental method for loans. Ancient Greeks used options. In 6th century, Medieval Christianity dominated economic and developed Scholastic doctrine so interest rate was embedded in exchange rate for commercial transactions as risk exists. After the First Crusade, medieval fair was hosted in Bruges as the expansion of trades but relocated to Antwerp for lower cost, tax-free, and better location. In 1531, a new building for trade called Antwerp exchange opened where options are unbundled that allows speculation and provided transferability of contracts. Time bargains contracts is developed by settling by differences that physical delivery of commodity is not required, which differentiate from to arrive contracts. Because the Spanish sacked Antwerp Exchange, trading moved to Amsterdam Exchange in 17th century and underline goods transaction got unbundled from derivative transactions that provided speculative. Difference trading is when gains and losses are calculated on the settlement date which is pure speculating trading. To settle difference trading, the clearing mechanism, *rescontre,* is created which is the beginning of clearinghouses. In blanco sales ban restricted traders from trading without having actual possession due to short squeeze and bear raid. In England, brokers relocated from exchanges to coffeehouse after 1694 market collapse. Mississippi scheme is the subscription sales of IPO that cause cash market collapse in Summer 1720. Because of the South sea bubbles, the Barnard's Act banned the use of options trading. In Japan, a more formulaized exchangeable time bargain future contracts on rice bills was developed in 18th century. American has a daily settlement and short dated market. In 19th century, institutionalization of trading in time bargain contract happened in Chicago. Chicago Board of Trade standardized commodity for delivery and created clearing mechanism ensure contract is settled in 1859. Rules was made in 1863 for penalizing not fulfilling contract and the General Rules of the Board of Trade introduced in 1865 including standardized contract terms, only members allow to trade, and margin deposits. In Canada, due to agrarian discontent for the Winnipeg Exchange for its monology, futures market are not developed until 1980s with Canadian government highly restricted commodity futures market. In 1872, NYMEX is created and CME was created.