

“Investors perception towards Derivative Market with special reference to shivamogga”

by Mr. Venkatesha. R ^[a] and Dr. Hiriappa. B ^[b]

Abstract

The history of derivatives may be new for developing countries but it is old for developed countries. The first derivatives as “futures” contracts were introduced in the Yodoya rice market in Osaka, Japan around 1960. The commodity derivatives market has been functioning in India since nineteenth century with organized trading in cotton. Exchange traded financial derivatives were introduced in India in 2000 at two major stock exchanges. NSE and BSE. There are various derivative instruments like index futures. Stock futures, index option, stock options, interest rate futures, currency option, currently traded in these exchanges. This paper investigates the perception of the investors in NSE and BSE derivatives markets. The study focuses on investor’s perception. The data were collected from 150 respondents via a questionnaire survey.

Keywords: *DS - Derivatives status, DM- Derivative market, II- Institutional investors, IP- Investor perception.*

^[a] Mr. Venkatesha. R, Research Scholar, Bharathiar University, Coimbatore, Tamil Nadu.	^[a] Dr. Hiriappa. B, Coordinator, Department of Post-Graduation Studies in Commerce, Government First Grade College, Thirthahalli, Karnataka State, India.
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1. Introduction

A derivative is a financial tool which derives its importance from the value of underlying entities such as an Asset Equities, debt, currencies, index or interest rate. The first derivative contract in India was launched on NSE was the nifty 50 index futures contract. A series of modifications in the financial markets paved way for the improvement of exchange – traded derivatives by the L.C Gupta committee, set up by the securities and exchange, board of India recommended appeared introduction of derivatives tools with bi-level instruction (i.e. self regulation by exchanges with SEBI providing the overall regulatory and supervisory role). Integration in the world’s commodity and financial market because of globalization and liberalization of the countries across the world. Varies types of risks, interest rate risk, foreign

exchange risk, Inflation risk etc. due to successful management of such type of risks have become major issue for market players and business houses.

Types of derivatives

Different types of derivatives instruments are forwards, future, option and swaps.

Forwards

A forward contract is a customized contract between two entities, where settlement takes place on a specific date in the future at today's pre-agreed price. This is an agreement between two parties to buy or sell an asset at a specified point of time in the future. In case of a forward contract the price which is paid or received by the parties is decided at the time of entering into the contract. A forward contract is traded in the over-the-counter market—usually between two financial institutions or between a financial institution and one of its clients. Forward contracts on foreign exchange are very popular example in forward contracts.

Futures

Futures are one of the important financial instruments in derivatives market. A futures contract is an agreement between the two parties to buy or sell an asset at a certain time in the future for a certain price. Futures contract are traded on the exchanges. Futures contracts give the holder an opportunity to buy or sell the underlying at a pre-specified price sometime in the future. They come in standardized form with fixed expiry time, contract size and price.

Options

An option is a financial derivative contract that provides a party the right to buy or sell an underlying asset at a fixed price by a certain time in the future. The party holding the right is known as the option buyer; the party granting the right is known as the option seller. **There are** two types' options: one is calls option and second is puts option.

SWAPS

SWAPS are one type of financial instruments in derivatives market. The term SWAPS refers to the private agreements between two parties to exchange cash flows in the future according to a prearranged formula. SWAPS are traded in Over the Counter Market.

Investopedia explains SWAP: If firms in separate countries have comparative advantages on interest rates, then a swap could benefit both firms.

2. Literature review

Bhatt. N Dr. Babraju conducted study on “Perception of Investor towards Derivatives as On Investment Avenue” in the year 2014. The derivatives are risk management tool that support in effective management of risk by various stockholders. Derivatives provide a chance to transfer risk from the one who wish to avoid it: to one who wish to agree it. India’s experience with the introduction of the equity derivatives market has been really encouraging and successful. The derivatives turnover on the NSE has surpassed the equity market turnover.

Dr. Kamleshghakar: Msd.Meetu conducted research on a derivatives market in India: evolution, trading in the year 2013. The Indian derivative market has become a multi-trillion dollar markets over the years. Marked with the ability to partially and fully transfer the risk by securing in, assets prices, derivatives are gaining popularity among the investors. Since the economic reforms of 1991 maximum efforts have been made to encourage the investors’ confidence by making the trading process more users friendly. Still, there are specific issues in this market. So the present paper is to attempt to study the evolution of the Indian derivatives market. Trading instrument in its various products and the future prospects of the Indian derivatives market.

Bose, Sachismitha conducted research on ‘The Indian derivatives market revisited’ in the year 2006. They found that derivatives products provide certain important economic benefits such as risk management, or redistribution of risk away from risk averse investors towards those more willing and able to bear risk. Derivatives also help price discovery. i.e. the process of determining the price level for any asset based on supply and demand. These functions of derivatives help in efficient capital allocation in the economy: at the same time their measure also poses a threat to the stability of the financial sector and the overall economy.

Naresh Gopal, University of Madras, “Views of The Market Participants On Trading, Regulation in The Derivatives Market”. Indian institute of capital markets 9th capital markets conference paper, January 25, 2006. The dynamic growth of the derivatives market, particularly futures and options and the perceived risks to the financial sector, continue to stimulate debate on the proper regulation of these instruments. Even though this market was initially fuelled by various expert team survey, regulatory framework, recommenders’ byelaws and rules there still a debate on the existing regulations such as is regulation needed. When and where regulation need? What are responsible and attainable goals of these regulations? Therefore, this article

critically examines the views of market participants on the existing regulatory issues in trading derivative securities in Indian capital market conditions.

3. Statements of problem:

The global liberation and integration of financial markets have created new investment opportunities, which in turn require the development of new instruments that are more efficient to deal with increased risks. The most of desired instruments that allow market participants to manage risk in the modern securities trading are derivative instruments. The main logic behind trading is that derivatives reduce risk by providing additional channels to invest with lower trading cost and it facilitates the investors to extend their settlement through the future constructs. They provide extra liquidity in stock market. In India, exchange traded financial derivatives were introduced in the year 2000. But even 16 years the institutional investors are actively engaged in this market. Hence this present study.

4. Objectives of study

- 1) To analyze the perception of investors towards investment in derivative instrument and market.
- 2) To know different types of financial derivatives.
- 3) To study the awareness about derivative market.

5. Research Methodology

This study research is based on primary data and secondary data. This primary data is gathered from investors in stock market. Secondary data are collected from journals articles and websites. This primary data is arranging for questionnaire method the subject of the study. The data collected was analyzed by using sample statistical technologies like percentages and paragraphs. This study is limited to Shivamogga city and it is subject to the views expressed by the respondents.

6. Limitations of the study

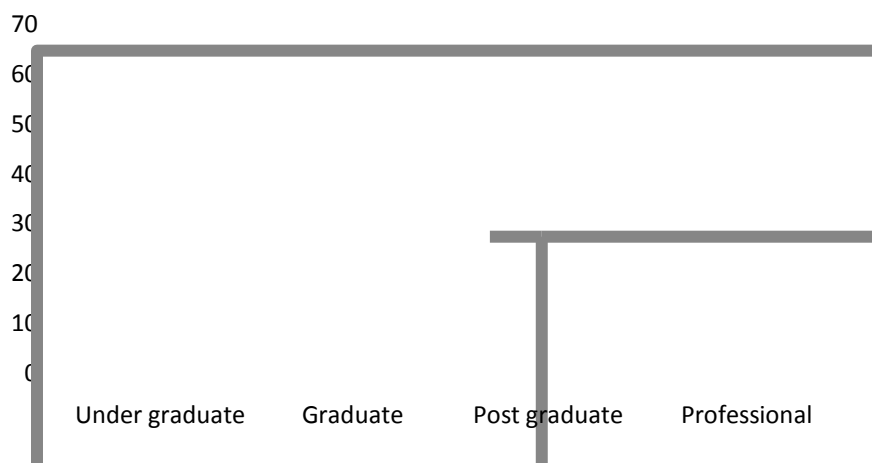
- 1) Due to lack of awareness about derivatives, many investors may not be responded accurately. The study is not focused on professional investors who have expertise and invests big amount in stock market. Because these professional investors are less in number and they are not easily accessible.
- 2) There is always sampling error. Investors’ response may be biased. And the study reflects only D-mat a/c holders’ view not all the investors in general.
- 3) One of the most serious limitations concerns the fact that the investors’ response is absolutely comes from subjective question and there is no way to reliably assess whether their actual behavior would mimic their answers.

7. Data Analysis and Interpretation:

Table no.1

Education qualification of respondents.

Educational qualification	No. of respondents	Percentage (%)
Under graduate	07	4.66
Graduate	99	66.00
Post graduate	32	21.33
Professional	12	08.00
Total	150	100%



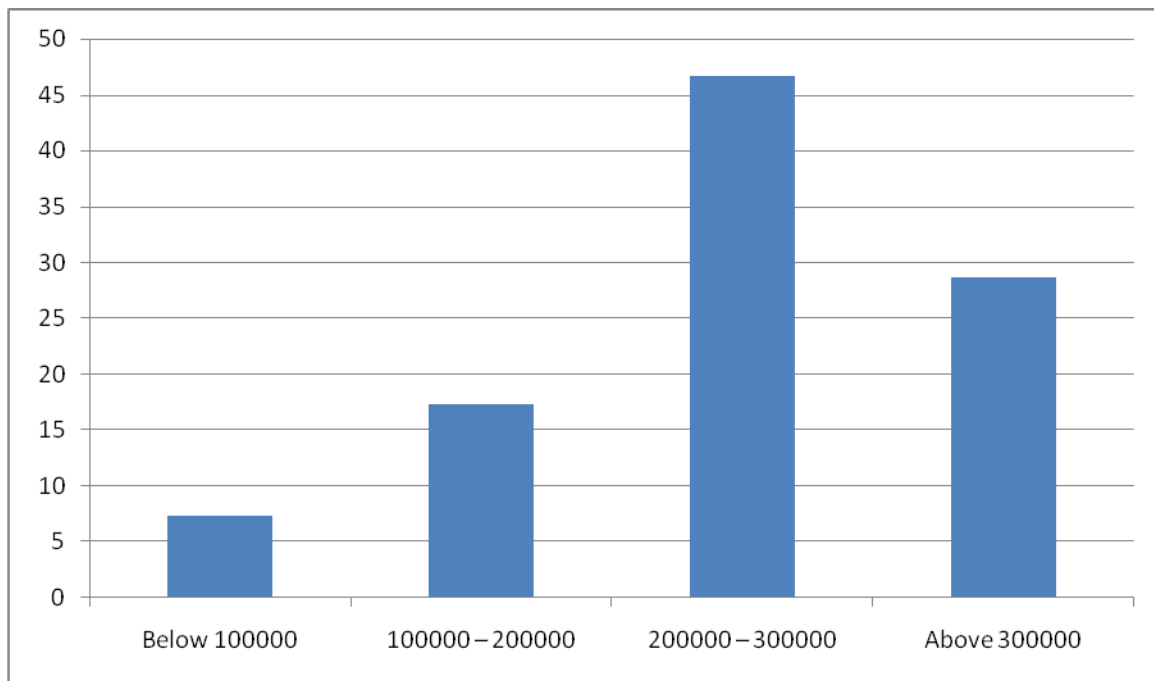
Source: primary data.

Interpretation: from the above table it is clear that 66% of respondents are graduates, very less 07% are under graduates.

Table no.2

Annual income of respondents

Annual income	No. of Respondents	Percentage (%)
Below 100000	11	7.33
100000 – 200000	26	17.33
200000 – 300000	70	46.67
Above 300000	43	28.67
Total	150	100%

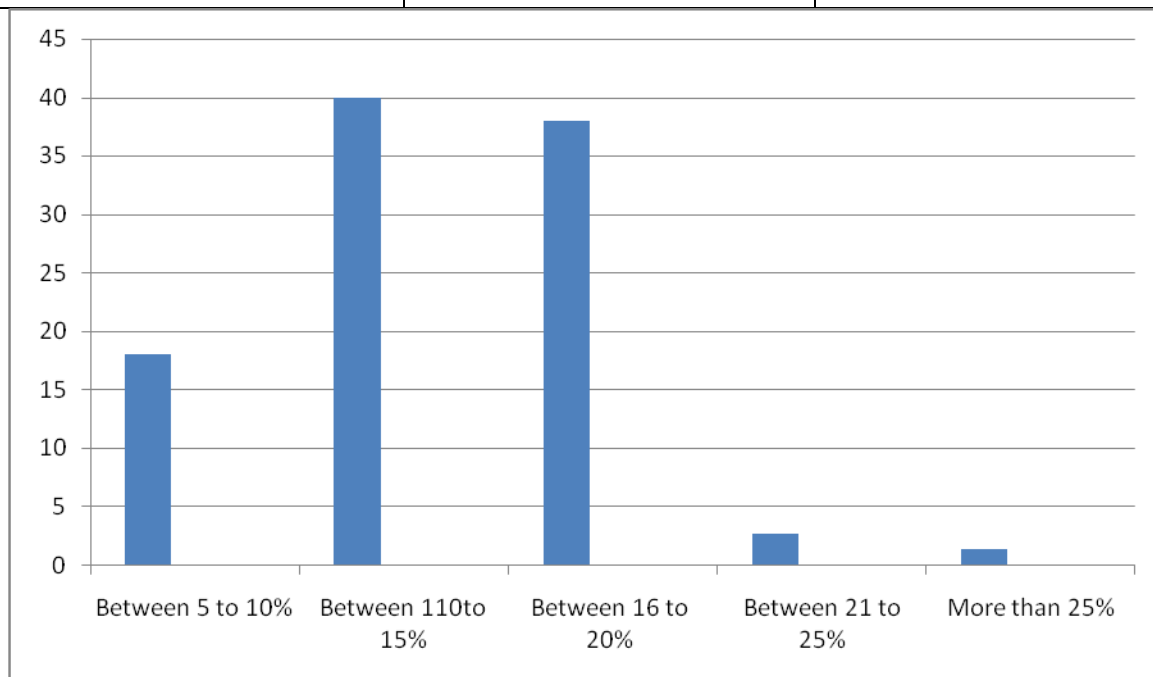


Interpretation: 46.67% of respondent's annual income is between 200000 – 300000 and followed by 28.67% respondent's income is above 300000.

Table no. 3

Percentage of income available for investment.

Savings for investment	No. of respondents	Percentage(%)
Between 5 to 10%	27	18
Between 11to 15%	60	40
Between 16 to 20%	57	38
Between 21 to 25%	04	2.67
More than 25%	02	1.33
Total	150	100%

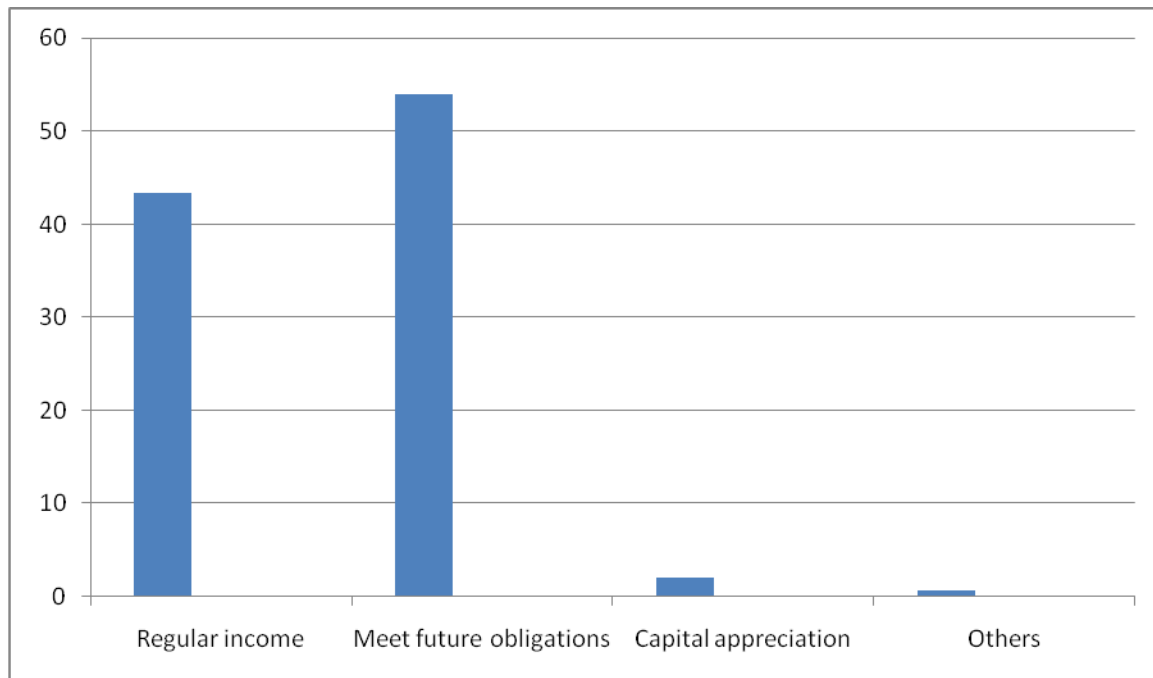


Interpretation: from the above 60% of respondents save 11 to 15% of their income for investment and only 1.33% of respondents save more than 25% their income for investments.

Table no. 4

Respondents purpose of the investment

Purpose of investment	No. of respondents	Percentage (%)
Regular income	65	43.33
Meet future obligations	81	54.00
Capital appreciation	03	2.00
Others	1	0.66
Total	150	100%

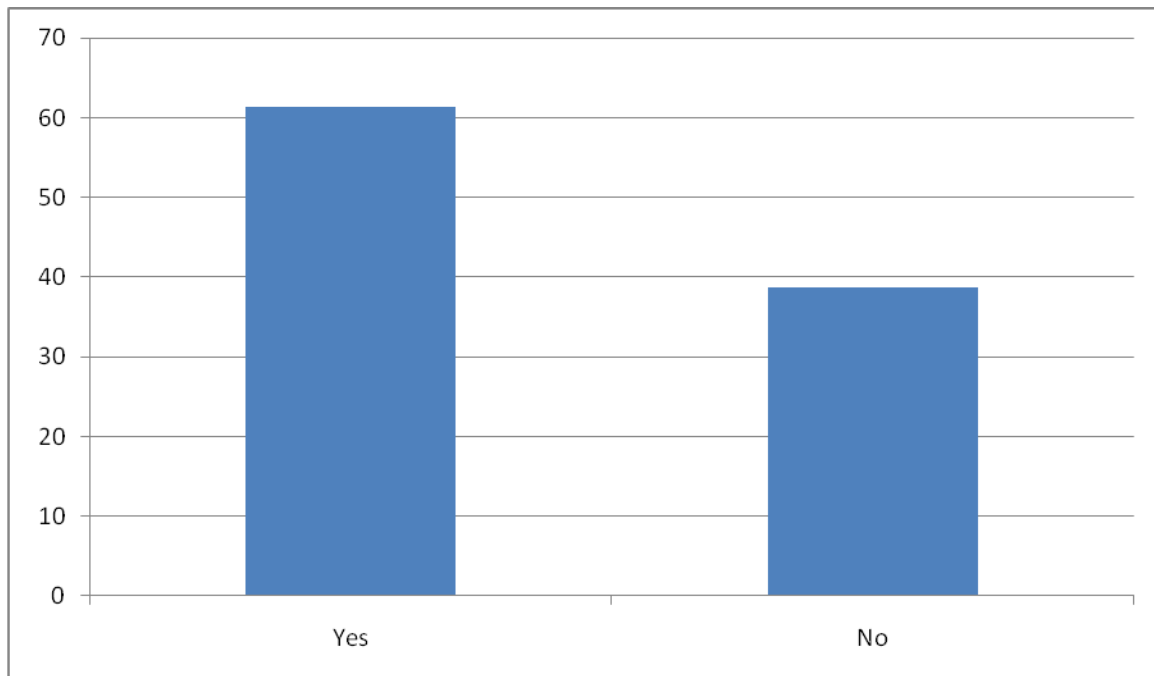


Interpretations: 54% of respondents investing to meet future obligations and 43.33 respondents are looking for regular income.

Table no. 5

Investment by respondents are invested in derivatives

Investment in derivatives	No. of Respondents	Percentage (%)
Yes	92	61.33
No	58	38.67
Total	150	100%

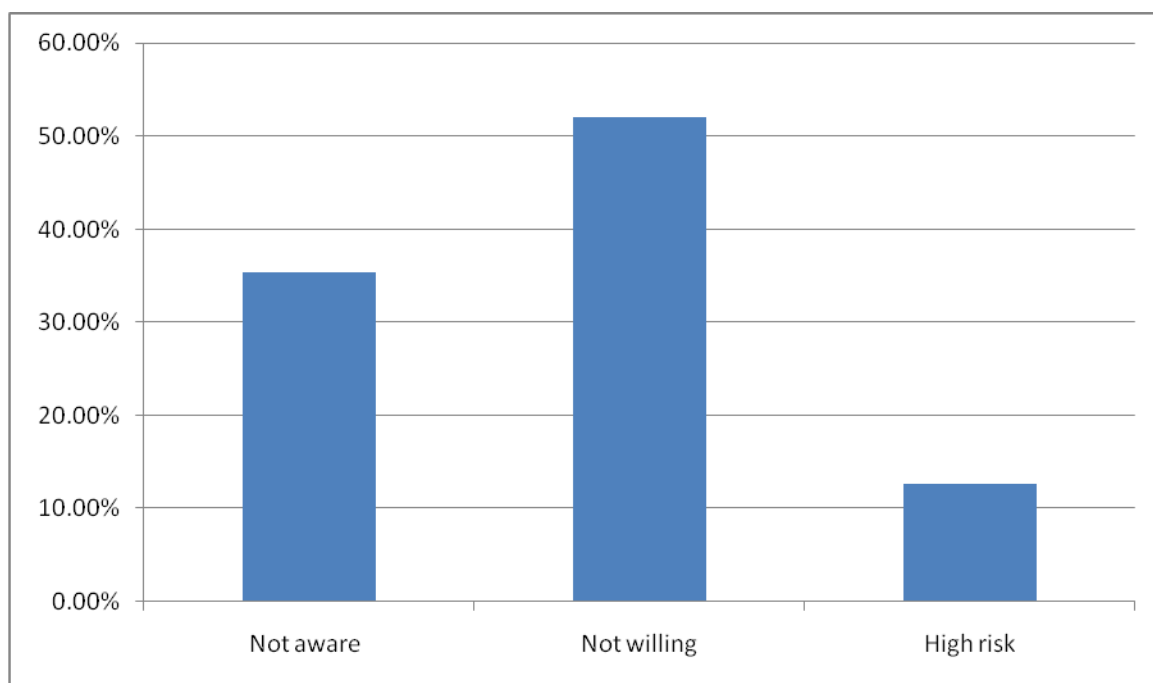


Interpretation: 61.33% of respondents are invested in derivatives and 38.67% of respondents are not invested in derivatives.

Table no. 6

Reasons for not investing derivatives.

Reasons	No. of respondents	Percentage (%)
Not aware	53	35.33%
Not willing	78	52.00%
High risk	19	12.67%
Total	150	100%

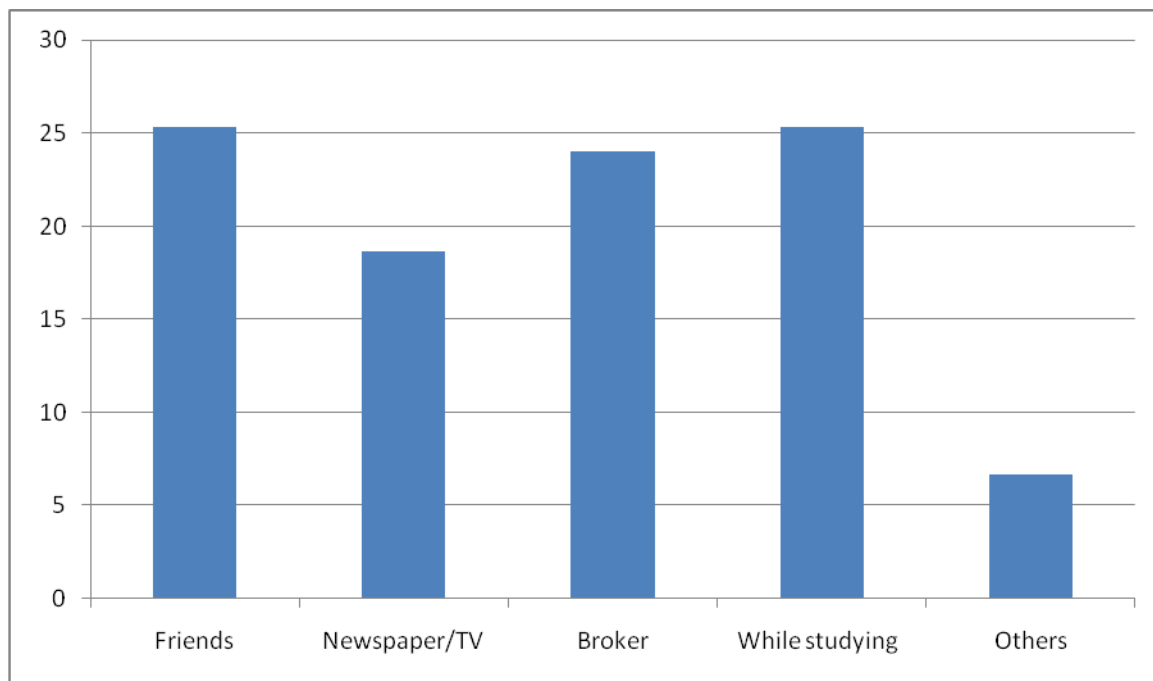


Interpretation: 52% of respondents are not willing to invest in derivatives, 12.67% of respondents are felt that derivatives are highly risky, 35.33% of respondents not aware of derivatives, so derivatives are highly risky and expected profit or loss is also high.

Table No. 07

Source of information about derivatives.

Source	No. of respondents	Percentage (%)
Friends	38	25.33
Newspaper/TV	28	18.67
Broker	36	24.00
While studying	38	25.33
Others	10	06.67
Total	150	100%

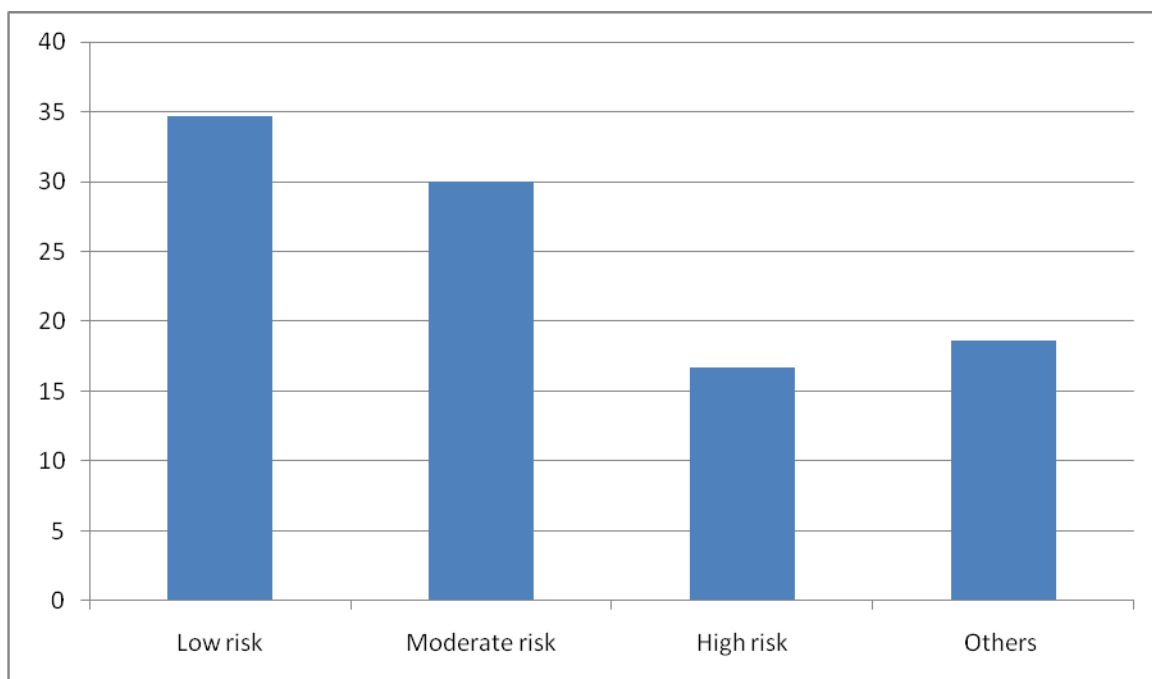


Interpretation: 25.33% of respondents know about derivatives from friends and while studying and 6.67% of respondents know about derivatives from others.

Table No. 08

Kind of risk investor perceive while investing in derivatives market.

Level of risk	No. of respondents	Percentage (%)
Low risk	52	34.67
Moderate risk	45	30.00
High risk	25	16.67
Others	28	18.66
Total	150	100%

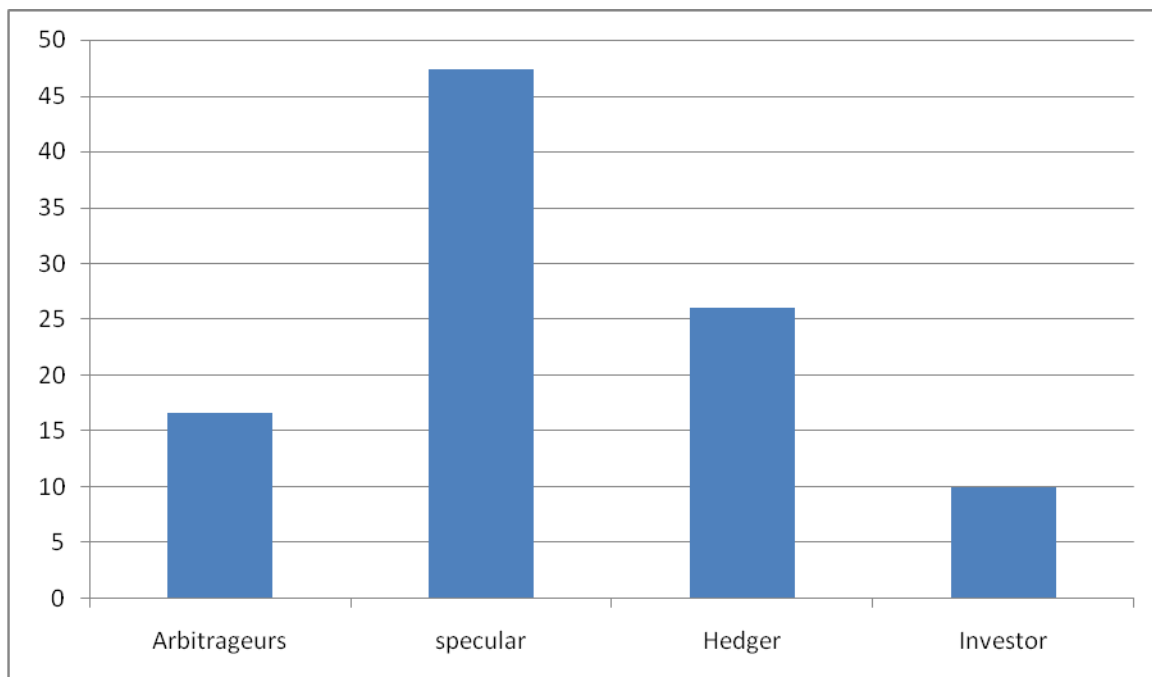


Interpretation: 34.67% of investors are taking low risk, 30% of investors are taking moderate risk, 16.67% of investors are taking high risk.

Table No. 09.

Investors participate as derivatives market as.

Participant as	No. of respondents	Percentage (%)
Arbitrageurs	25	16.67
specular	71	47.33
Hedger	39	26.00
Investor	15	10.00
Total	150	100%

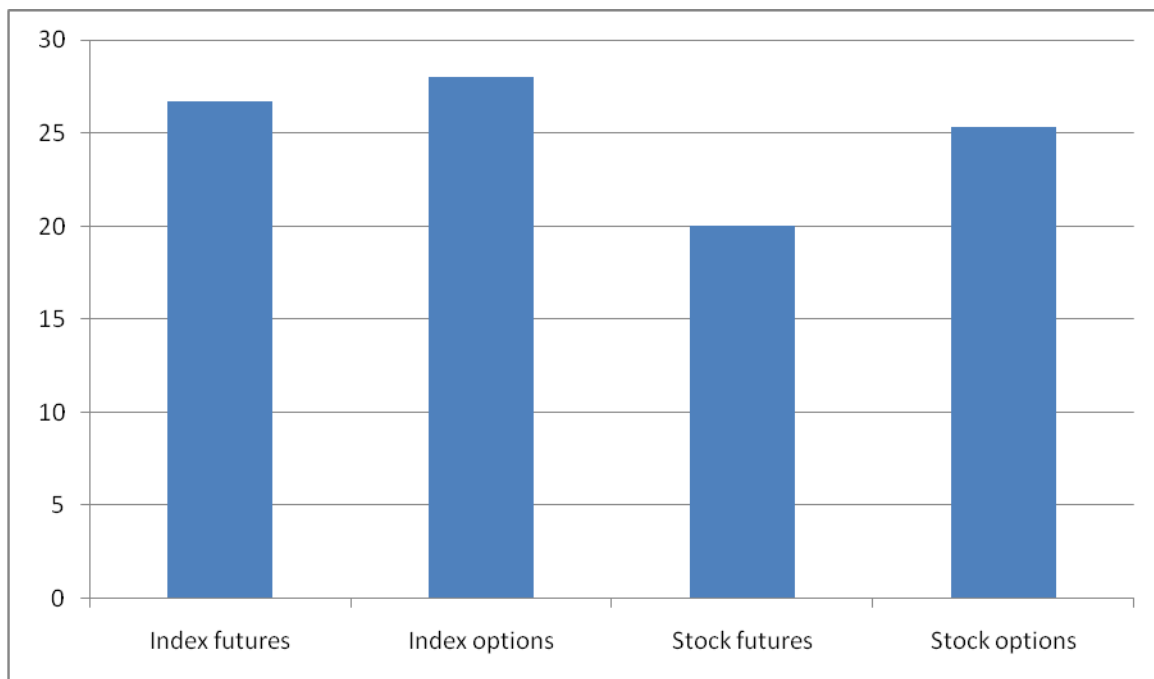


Interpretation: 47.33% of investors are speculators in derivatives market, 26% of investors are hedging for their investment, followed by 16.67% of investors are arbitrageurs.

Table No. 10.

Investors preference towards derivatives instruments (choose only one option)

Preference	No. of respondents	Percentage(%)
Index futures	40	26.67
Index options	42	28.00
Stock futures	30	20.00
Stock options	38	25.33
Total	150	100%

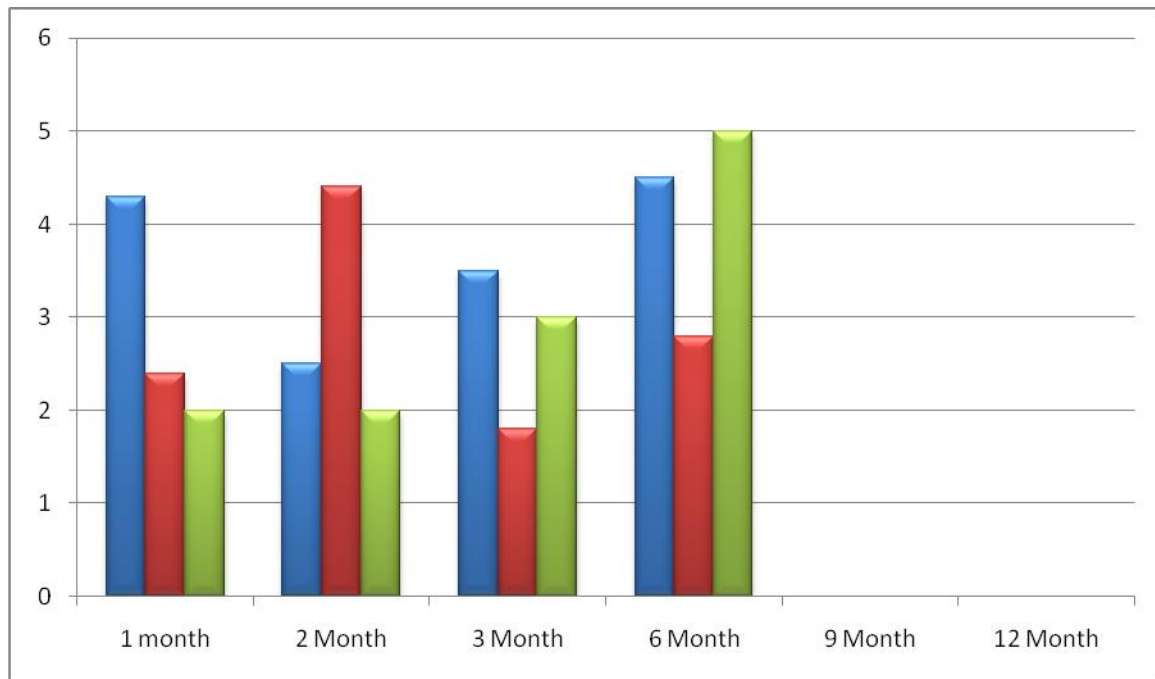


Interpretations: 28% of investors are more often invest in index options. And 26.67% are more often invest in index futures.

Table No. 11.

Time period choose for derivatives contracts by investors.

Time period	No. of respondents	Percentage (%)
1 month	11	7.33
2 Month	22	14.67
3 Month	44	29.33
6 Month	46	30.67
9 Month	11	7.33
12 Month	16	10.67
Total	150	100%

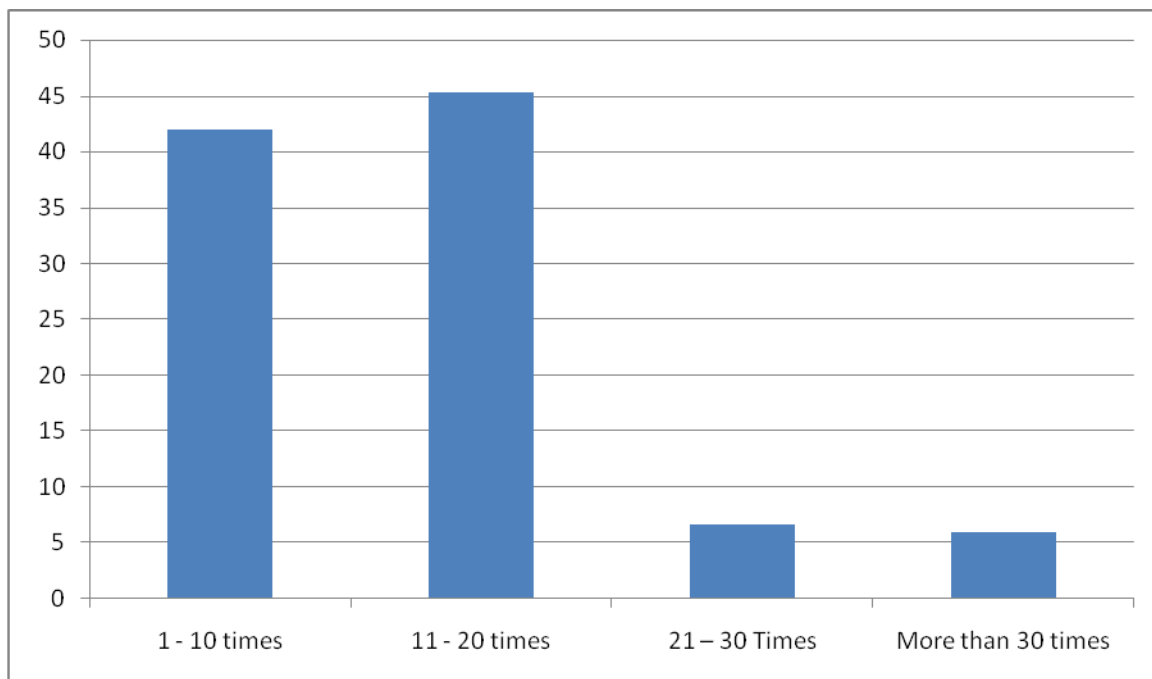


Interpretation: 30.67% of investors are taken 6 months positions, 29.33% of investors are taking 3 months positions.

Table No. 12

Frequency of investments in derivatives in a year.

Frequency	No. of respondents	Percentage (%)
1 - 10 times	63	42.00
11 - 20 times	68	45.33
21 – 30 Times	10	6.67
More than 30 times	09	6.00
Total	150	100%



Interpretations: 45.33% of investors invest in derivatives 11-20 times in a year, 6% of investors in derivatives very often (more than 30times in a year).

8. Findings from survey.

- 1) 66% of respondents are graduates. Very less 7% are under graduates.
- 2) 46.67% of respondents annual income is between 200000 – 300000 and followed by 28.67% of respondents income is above 300000.
- 3) 60% of respondents save 11 to 15% of their income for investments and only 1.33% of respondents save more than 25% of their income for investments.
- 4) 54% of respondents investing to meet future obligations and 43.33% respondents are looking for regular income.
- 5) 61.33% of respondents are invested in derivatives and 38.67% respondents are not invested in derivatives.
- 6) 52% of respondents are not willing to invest in derivatives, 12.67% of respondents are felt that derivatives are highly risky. 35.33% of respondents not aware of derivatives, so derivatives are highly risky and expected profit or loss is also high.
- 7) 25.33% of respondents know about derivatives from friends. And 25.33% of respondents know about derivatives while they are studying.
- 8) 34.67% of investors are taking low risk, and 30% of investors are taking moderate risk, 16.67% of investors are taking high risk.
- 9) 47.33% of investors are speculators in derivatives market, 26% of investors are hedging for their investments, followed by 16.67% of investors are arbitrageurs.
- 10) 28% of investors are more often invest in index options. And 26.67% are more often invest in index futures.
- 11) 29.33% of investors are taking 3 months positions. 30.67% of investors are taking 6 months positions.
- 12) 45.44% of investors invest in derivatives 11 – 20 times in a year. 6% of investors invest in derivatives very often (more than 30 times in a year).

9. Suggestions

There is a need to introduce more equity derivatives products in India and has long strides to take in terms of providing larger liquidity and depth to the bigger market players. Many respondents felt that it is right time to introduce the other complex products like exotic derivatives. In this study Derivatives market is risk and return game that's why the investor get risk. Due to absence of delivery based settlement, many investors may not be participating in the derivatives market. Also, this could bring one more type of product in the basket to be offered to the market at large. Hence, NSE may look at starting the physical delivery derivatives contracts to give further fillip to volume on its exchange in particular and the Indian equity derivatives market at large. Investors are more often invest in index options because of derivatives are highly risky. The study suggests that Government should look forward to setting up a super regulator who can take care of these various regulatory arbitrage/risk issues or there should be joint committee of all the regulatory bodies to look into such concerns of the market from overall perspective. This study can be used by the regulating authorities and broker houses to increase awareness among the investors about derivatives.

10. Conclusions

Now a days the investors know about the derivative market, so they are aware as derivative market offers more return, with the hedging of interest rate risk and exchange rate risk with maximum profits and minimum loss. Indian derivative markets have had a very good performance till date, to continue with this same growth individual investors have to be encouraged to enter into trades more often so that they help to drive the economy. In the study, it was found that derivatives are used as risk Hedging tool and the trend of the spot market affects the trading of Derivatives. It has been noticed that there has been awareness about derivatives trading amongst the derivatives in India since last few years. SEBI and government should take responsibility to create awareness among investors and need to educate individual investors through different seminars or training programs regarding the advantages and risk factors associated with derivative instruments. Respondents perceived that Market Risk and Credit risk are the two major risk observed in capital markets.

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