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   INTRODUCTION

   REVIEW OF LITERATURE

   NEED/IMPORTANCE OF THE STUDY

   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

   SCOPE FOR FURTHER RESEARCH

   ACKNOWLEDGMENTS

   REFERENCES

   APPENDIX/ANNEXURE

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- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
- Hunker, H.L. and A.J. Wright (1963), "Factors of Industrial Location in Ohio" Ohio State University, Nigeria.

CONTRIBUTIONS TO BOOKS

- Sharma T., Kwatra, G. (2008) Effectiveness of Social Advertising: A Study of Selected Campaigns, Corporate Social Responsibility, Edited by David Crowther & Nicholas Capaldi, Ashgate Research Companion to Corporate Social Responsibility, Chapter 15, pp 287-303.

JOURNAL AND OTHER ARTICLES

- Schemenner, R.W., Huber, J.C. and Cook, R.L. (1987), "Geographic Differences and the Location of New Manufacturing Facilities," Journal of Urban Economics, Vol. 21, No. 1, pp. 83-104.

CONFERENCE PAPERS

- Garg, Sambhav (2011): "Business Ethics" Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19–22 June.

UNPUBLISHED DISSERTATIONS AND THESES

- Kumar S. (2011): "Customer Value: A Comparative Study of Rural and Urban Customers," Thesis, Kurukshetra University, Kurukshetra.

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WEBSITES

- Garg, Bhavet (2011): Towards a New Natural Gas Policy, Political Weekly, Viewed on January 01, 2012 http://epw.in/user/viewabstract.jsp

A STUDY ON INVESTORS' PERCEPTION TOWARDS DERIVATIVE INSTRUMENTS AND MARKETS

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ABSTRACT

The history of derivatives may be new for developing countries but it is old for the 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 the nineteenth century with organized trading in cotton. Exchange traded financial derivatives were introduced in India since June 2000 at two major stock exchanges, NSE and BSE. There are various derivative instruments like Index Futures, Stock Futures, Index Options, Stock Options, Interest Rate Futures, Currency Options currently traded in these exchanges. But even after a decade the derivatives are actively engaged by professionals institutional investors. Many retail investors even today are not actively participating in the market because of lack of knowledge and complex nature of Instruments. This study is an attempt to know the retail investors perception and awareness about derivatives market and its instruments.

KEYWORDS
Derivatives, Derivatives Market, Institutional Investors, Investor Perception, Retail Investors.

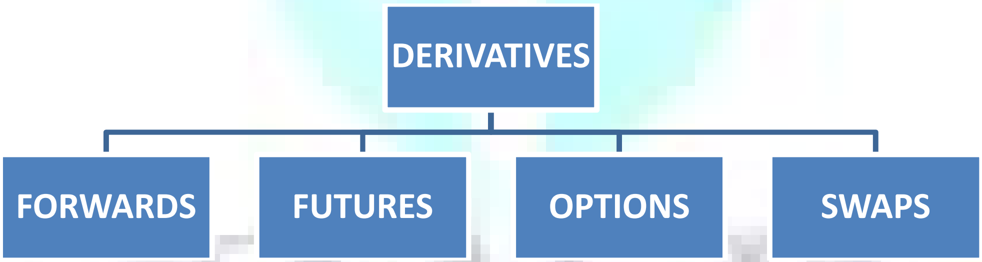
1. DERIVATIVE MARKETS

The emergence of the market for derivative products, most notably forwards, futures and can be traced back to the willingness of risk-averse economic agents to guard themselves against uncertainties arising out of fluctuations in asset prices. By their very nature, the financial markets are marked by a very high degree of volatility. Though the use of derivative products, it is possible to partially or fully transfer price risks by looking-in asset prices. As instruments of risk management, these generally do not influence the fluctuations in the underlying asset pries. However, by locking in asset prices, derivative products minimize the impact of fluctuations in asset prices on the profitability and cash flow situation of risk-averse investors.

A derivative is financial instrument whose value is 'derived' from another underlying security or a basket of securities. Traders can assume highly leveraged positions at low transaction costs using these extremely flexible instruments. Derivative products like index futures, stock futures, index options and stock options have become important instruments of price discovery portfolio diversification and risk hedging in stock markets all over the world in recent times.

2. DERIVATIVE INSTRUMENTS

DIAGRAM 1: TYPE OF DERIVATIVE INSTRUMENTS



Derivative contracts have several variants. The most common variants are forwards, futures, options and swaps. We take a brief look at various derivatives contracts that have come to be used.

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.

FUTURES: A futures contract is an agreement between two parties to buy or sell an asset at a certain time in the future at a certain price. Futures contracts are special types of forward contracts in the sense that the former are standardized exchange-traded contracts.

OPTIONS: Options are of two types – calls and puts. Calls give the buyer the right but not the obligation to buy a given quantity of the underlying asset, at a given price on or before a given future date. Puts give the buyer the right, but not the obligation to sell a given quantity of the underlying asset at a given price on or before a given date.

SWAPS: Swaps are private agreements between two parties to exchange cash flows in the future according to a prearranged formula. They can be regarded as portfolios of forward contracts. The two commonly used swaps are:

- Interest rate swaps: These entail swapping only the interest related cash flows between the parties in the same currency.
- Currency swaps: These entail swapping both principal and interest between the parties, with cash flows in one direction being in a different currency than those in the opposite directions.

3. THE PARTICIPANTS IN A DERIVATIVES MARKET

Hedgers use futures or options markets to reduce or eliminate the risk associated with price of an asset.

Speculators use futures and options contracts to get extra Leverage in betting on future movements in the price of an asset. They can increase both the potential gains and potential losses by usage of derivatives in a speculative venture.

Arbitrageurs are in business to take advantage of a discrepancy between prices in two different markets. If for example, they see the futures price of an asset getting out of line with the cash price, they will take offsetting positions in the two markets to lock in profit.

4. REVIEW OF LITERATURE

There are few studies have been conducted to examine the impact of derivative trading on Indian stock markets.

Thenmozhi (2002), in her study on the relationship between CNX Nifty futures and the CNX Nifty index finds that derivative trading has reduced the volatility in the cash segment.

Gupta (2002) concludes in his study that the overall volatility of the stock market has declined after the introduction of the index futures.

Bandivadekarand Ghosh (2003) conclude that while the, futures effect plays a definite role in the reduction of volatility in the case of S & P CNX Nifty, in the case of BSE Sensex where derivative turnover is considerably low, the effect is rather ambiguous.

Nath (2003) observed in a study examining the impact of derivative trading at individual stock level, the volatility has come down in the post-derivative trading period for most of the stock.

Dr. Avadhani, V.A (2007) in his work explains how Fiscal, Monetary and Credit policies tend to affect the performance of the financial instruments in the capital market (either directly or indirectly) it is observed that, where fiscal policy influence the demand and supply for shares and securities in the market, prevailing interest rate influence the cost of borrowing and investment which is influenced by the monetary policies of the government. Further the credit policy is found to be greatly influencing the liquidity positions in the markets.

Bredin, Don, O'reilly, Gerard and Stevenson, Simon (2011) in their study explain how monetary policy has become the main instrument in stabilization of inflationary trends.

Papadamou, Stephen and siriopoulous, costas (2012) in their study observed the behavior of the bank after implementation of new monetary policy that the bank goes for an instantaneous reduction in lending mortgage credit, considering real estate lending as a risky long term investment. Further, affecting the short term lending to households and loans and advances extended to firms together, due to the sluggish increase in the relevant lending rates leading to increased demand for funds and impacting the spending and investment activities of both individuals as well as the firms/business centers.

5. STATEMENT OF PROBLEM

The global liberalization 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 channel to invest with lower trading cost and it facilitates the investors to extend their settlement through the future contracts. They provide extra liquidity in stock market. In India, exchange traded financial derivatives were introduced in the year 2000. But even after 13 years the institutional investors are actively engaged in this market. Only limited retail investor's trade actively in this market. Hence this present study

6. OBJECTIVES OF STUDY

- To understand the concept of Derivatives and Derivative Trading.
- To analyze the perception of investors towards investment in derivative instruments and markets.
- To know different types of Financial Derivatives and their trading.

7. DATA AND METHODOLOGY

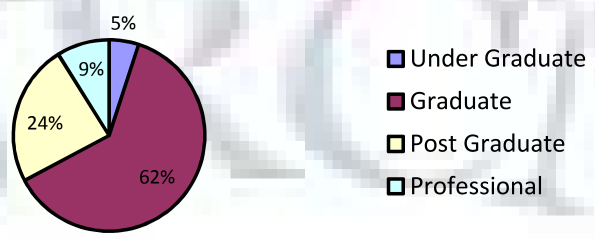
This study is based on primary data. The data was collected from the 180 retail investors from distinct parts of Bangalore. The respondent investors were selected using convenient sampling method. Questionnaire is used to collect the details about awareness and perception of retail investors about various derivative products available for trading in national stock markets. The data collected was analyzed by using sample statistical technologies like percentages and graphs. This study is limited to Bangalore city and it is subject to the views expressed by the respondents.

8. DATA ANALYSIS AND INTERPRETATION

TABLE 1: EDUCATION QUALIFICATION OF RESPONDENTS

Educational Qualification	No of Respondents	Percentage (%)
Under Graduate	9	5
Graduate	112	62.22
Post Graduate	43	23.89
Professional	16	8.89
Total	180	100

Source: *Primary data*

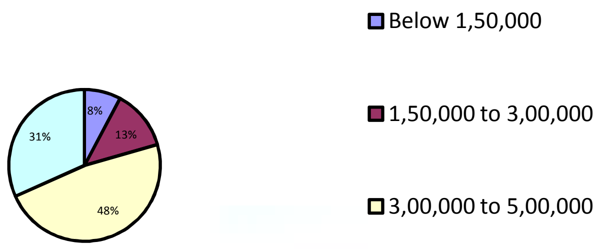


Interpretation: From the above table it is clear that 62% of respondents are Graduates, very less 5 % are Under Graduates

TABLE 2: ANNUAL INCOME OF RESPONDENTS

Annual Income	No of Respondents	Percentage (%)
Below 1,50,000	14	7.78
1,50,000 to 3,00,000	23	12.78
3,00,000 to 5,00,000	86	47.78
Above 5,00,000	57	31.66
Total	180	100

Source: *Primary data*



Interpretation: 47.78% of respondents' annual income is between 3,00,000 to 5,00,000 and followed by 31.66 % respondents income is above 5 lakhs

TABLE 3: PERCENTAGE OF INCOME AVAILABLE FOR INVESTMENT

Savings for Investments	No of Respondents	Percentage (%)
Between 5 to 10 %	23	12.78
Between 11 to 15 %	63	35
Between 16 to 20 %	82	45.55
Between 21 to 25 %	7	3.89
More than 25 %	5	2.78
Total	180	100

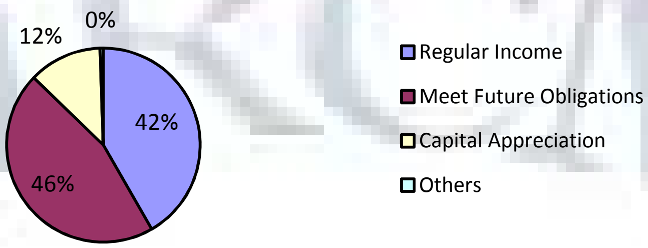
***Source:** Primary data*

Interpretation: From the above table 45.55% of respondents save 16 to 20 % of their income for investments and only 3% of respondents save more than 25% of their income for investments.

TABLE 4: RESPONDENTS' PURPOSE OF THE INVESTMENT

Purpose of Investment	No of Respondents	Percentage (%)
Regular Income	75	41.67
Meet future obligations	82	45.56
Capital Appreciation	22	12.22
Others	1	0.55
Total	180	100

***Source:** Primary data*

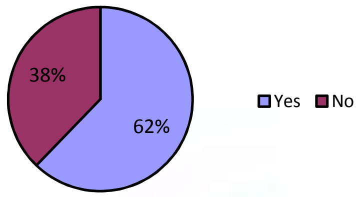


Interpretation: Nearly 46% of respondents investing to meet future obligations and 42% respondents are looking for regular income.

TABLE 5: INVESTMENT BY RESPONDENTS IN DERIVATIVES

Investment in Derivatives	No of Respondents	Percentage (%)
Yes	112	62.22
No	68	37.78
Total	180	100

***Source:** Primary data*

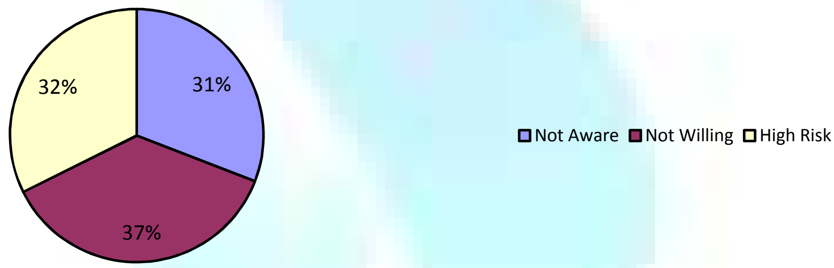


Interpretation: 62% of respondents are invested in derivatives, and 38% of respondents are not invested in derivatives.

TABLE 6: REASONS FOR NOT INVESTING IN DERIVATIVES

Reasons	No of Respondents	Percentage (%)
Not Aware	21	30.88
Not Willing	25	36.76
High Risk	22	32.35
Total	68	100

Source: *Primary data*

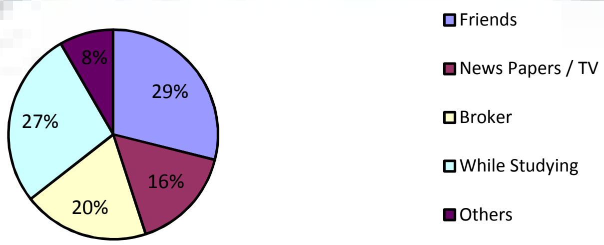


Interpretation: Nearly 36.76% of respondents are not willing to invest in derivatives, 32.35% of respondents are felt that derivatives are highly risky, 30.88% of respondents not aware of derivatives, so derivatives are highly risky and expected profit or loss is also high.

TABLE 7: SOURCE OF INFORMATION ABOUT DERIVATIVES

Source	No of Respondents	Percentage (%)
Friends	52	28.89
News Papers / TV	29	16.11
Broker	35	19.44
While Studying	49	27.22
Others	15	8.33
Total	180	100

Source: *Primary data*

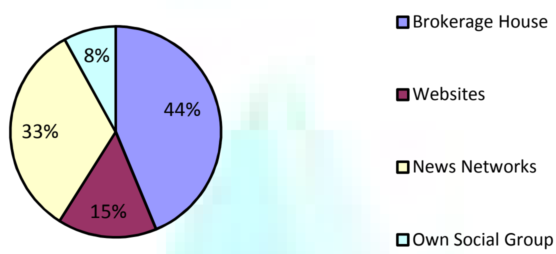


Interpretation: 30% of respondents know about derivatives from friends, and 27% of respondents know about derivatives while they are studying.

TABLE 8: SOURCE OF ADVISE BEFORE INVESTING IN DERIVATIVES MARKET

Source of Advice	No of Respondents	Percentage (%)
Brokerage House	49	43.75
Websites	17	15.17
News Networks	37	33.03
Own Social Group	9	8.03
Total	112	100

Source: *Primary data*

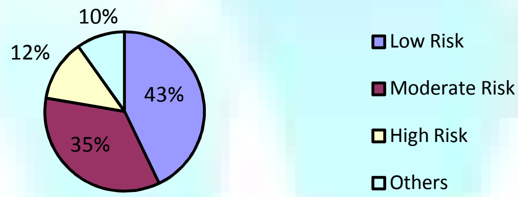


Interpretation: Nearly 44% of respondents are usually takes tips from Brokerage Houses, followed by 33% from News Networks and very less 8% of respondents take tips from own social groups, so derivatives are risky instruments that are the reason they are taking tips from Brokerage Houses and News Networks.

TABLE 9: KIND OF RISK INVESTOR PERCEIVE WHILE INVESTING IN DERIVATIVES MARKET

Level of Risk	No of Respondents	Percentage (%)
Low Risk	48	42.85
Moderate Risk	39	34.82
High Risk	14	12.50
Others	11	9.82
Total	112	100

Source: *Primary data*

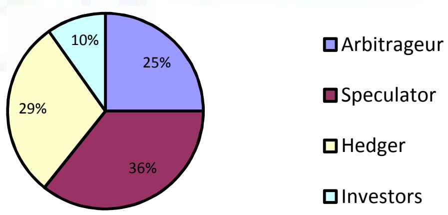


Interpretation: 42.85% of investors are taking low risk, and 34.82% of investors are taking moderate risk, 12.5% of investors are taking high risk.

TABLE 10: INVESTORS PARTICIPATE IN DERIVATIVES MARKET AS

Participant as	No of Respondents	Percentage (%)
Arbitrageur	28	25
Speculator	40	35.71
Hedger	33	29.46
Investor	11	9.82
Total	112	100

Source: *Primary data*

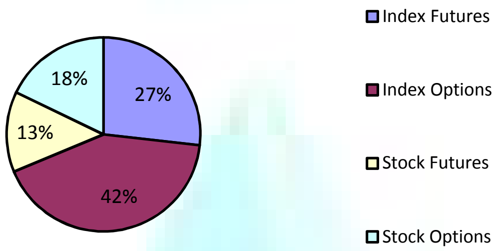


Interpretation: 36% of investors are speculators in derivatives market, 29% of investors are hedging for their investments, followed by 25% of investors are arbitrageurs.

TABLE 11: INVESTORS' PREFERENCE TOWARDS DERIVATIVE INSTRUMENTS (Choose only one option)

Preference	No of Respondents	Percentage (%)
Index Futures	30	26.78
Index Options	47	41.96
Stock Futures	15	13.39
Stock Options	20	17.85
Total	112	100

Source: *Primary data*

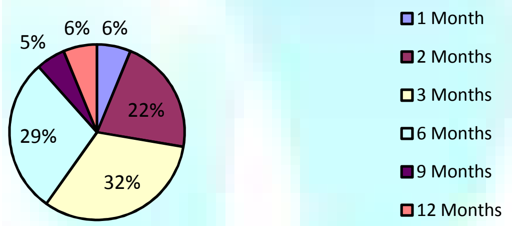


Interpretation: 42% of investors are more often invest in Index Options, and 27% are more often invest in Index Futures.

TABLE 12: TIME PERIOD CHOOSE FOR DERIVATIVE CONTRACTS BY INVESTORS

Time Period	No of Respondents	Percentage (%)
1 Month	7	6.25
2 Months	24	21.42
3 Months	36	32.14
6 Months	32	28.57
9 Months	6	5.35
12 Months	7	6.25
Total	180	100

Source: *Primary data*

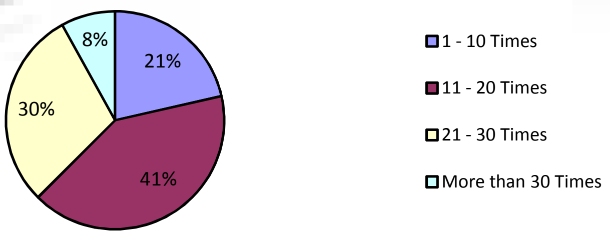


Interpretation: 32% of investors are taking 3 Months positions. 28.57% of investors are taking 6 Months Positions.

TABLE 13: FREQUENCY OF INVESTMENT IN DERIVATIVES IN A YEAR

Frequency	No of Respondents	Percentage (%)
1 - 10 Times	24	21.42
11 - 20 Times	46	41.07
21 - 30 Times	33	29.46
More than 30 Times	9	8.03
Total	112	100

Source: *Primary data*

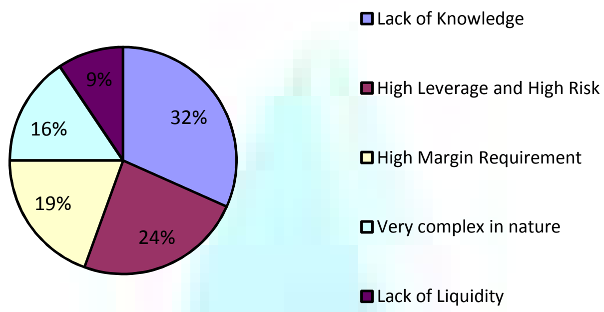


Interpretation: 42% of investors invest in derivatives 11 - 20 Times in a year. 8% of investors invest in derivatives very often (More than 30 Times in a year).

TABLE 14: TOP FIVE FACTORS HINDERING THE PERFORMANCE OF DERIVATIVES IN INDIAN STOCK MARKETS

Factor	No of Respondents	Percentage (%)
Lack of Knowledge	57	31.67
High leverage and high risk	43	23.89
High margin requirement	35	19.44
Very complex in nature	28	15.56
Lack of liquidity	17	9.44
Total	180	100

Source: *Primary data*



Interpretation: 32% of respondents have lack of knowledge about derivatives, 24% of respondents feel high leverage and high risk, 19% of respondents feel high margins required, 16% of respondents feel derivatives are very complex in nature.

9. FINDINGS FROM THE SURVEY

- 62% of respondents are Graduates, very less 5 % are Under Graduates
- 47.78% of respondents' annual income is between 3,00,000 to 5,00,000 and followed by 31.66 % respondents income is above 5 lakhs
- 45.55% of respondents save 16 to 20 % of their income for investments and only 3% of respondents save more than 25% of their income for investments.
- Nearly 46% of respondents investing to meet future obligations and 42% respondents are looking for regular income.
- 62% of respondents are invested in derivatives, and 38% of respondents are not invested in derivatives.
- Nearly 36.76% of respondents are not willing to invest in derivatives, 32.35% of respondents are felt that derivatives are highly risky, 30.88% of respondents not aware of derivatives, so derivatives are highly risky and expected profit or loss is also high.
- 30% of respondents know about derivatives from friends, and 27% of respondents know about derivatives while they are studying.
- Nearly 44% of respondents are usually takes tips from Brokerage Houses, followed by 33% from News Networks and very less 8% of respondents take tips from own social groups, so derivatives are risky instruments that's the reason they are taking tips from Brokerage Houses and News Networks.
- 42.85% of investors are taking low risk, and 34.82% of investors are taking moderate risk, 12.5% of investors are taking high risk.
- 36% of investors are speculators in derivatives market, 29% of investors are hedging for their investments, followed by 25% of investors are arbitrageurs.
- 42% of investors are more often invest in Index Options, and 27% are more often invest in Index Futures.
- 32% of investors are taking 3 Months positions. 28.57% of investors are taking 6 Months Positions.
- 42% of investors invest in derivatives 11 - 20 Times in a year. 8% of investors invest in derivatives very often (More than 30 Times in a year).
- 32% of respondents have lack of knowledge about derivatives, 24% of respondents feel high leverage and high risk, 19% of respondents feel high margins required, 16% of respondents feel derivatives are very complex in nature.

10. CONCLUSION

Even though most people look at derivatives with fear, they should understand the fact that derivatives help in shifting the risk to the other party. There are many myths that surround derivative market. All these can be done away with proper system in place.

Today institutional investors do most of the derivative transactions. It is very important that even individual investors participates in the derivative market actively and reap the benefits from it. 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.

After this study it is clear that derivative instruments and derivative markets are not so popular among individual investors. Only educated investors with the help of friends and brokers are investing in this market. The reasons for not investing in this market are lack of knowledge and very complex nature of instruments. Some people have a wrong perception about derivatives. Measures should taken to make sure that the investors get a right picture of the instruments and their risk factors.

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.

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