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A STUDY ON THE PERCEPTION OF INVESTORS TOWARDS DERIVATIVES

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Abstract:

Investments are made with an expectation of return. Returns are always based on an important factor called risk. Investors may get a many questions while choosing an investment option, like, what are investment avenues? How much should I invest? Where to invest? And so on. All these questions generate a need for financial literacy. The investor's goal is to always earn a higher return at lower risk. But risk cannot be eliminated from investment. There are various hedging instruments to offset risk in shares and debentures, such as forward contracts, futures, and options. These are collectively known as derivatives. These contracts derive value from some underlying asset. The derivatives market plays a very crucial role in the capital market. The research objective is to study the perceptions of investors towards investment in derivatives. Derivatives offer investors effective tools for management of risk exposures and achieving investment objectives. This article aims to study the view point of investors while considering derivatives as a tool for investing. However, their complex nature and risk require in-depth knowledge to invest in derivatives. This study will reflect the behaviour of investors in balancing risk and return relationships. It will focus on the investor's behaviour while analysing various factors such as risk, return, stability, and liquidity of an investment. The derivatives investors ought to study the market trend, market regulations, market reforms, and several other factors that will affect their prudent decision to invest in the derivatives market.

Keywords: Derivatives, Risk, Return.

Introduction

The word 'derivative' comes from the word 'to derive'. Derivative has no independent value. Derivatives are financial contracts, whose value is derived from an underlying asset. Derivatives allow investors to speculate on price movements and hedge against risks. Currently, financial derivatives have become very popular capital market instrument and very frequently used in the

world of finance. When the price of the underlying asset changes the value of the derivative is also changed. Without an underlying asset, derivatives do not have any meaning. For example, value of a futures contract like gold contract derives from the value of the underlying asset i.e., gold. The prices in the derivatives market are driven by the spot or cash market price of that asset. The basic purpose of these instruments is to reduce financial risk and provide protection against future prices.

Products in Derivative market

There are 4 main types of derivative contracts, such as futures, options, forwards and swaps.

Forwards:

Forwards is a customised contract between the parties to buy or sell an asset at a predetermined price at a future date. Forwards are not standardised contracts.

Futures:

Futures contract are standardized and they traded on derivatives exchanges. A standardized contract means that the lot size and settlement dates are fixed by the derivatives exchanges.

Options:

An option is an agreement between two parties, where the buyer has a right, it does not give obligation. It gives a right to buy or sell pre-decided quantity and type of underlying asset.

Swaps:

In a swap contract, two parties agree to exchange assets which have a cash flow for a particular period. In this contract one of the asset will have uncertain variable factor like interest.

Literature review:

1. Nagaraju (2014) the research was on the topic "A study on Investor's perceptions towards derivative instruments and markets". This paper focused on perception towards Index options, Index futures, currency options etc. This study aim to create solution for inactive participation due to lack of awareness and complex nature of derivatives. Also, it focuses on the effect of savings on the investment options.

2.Anuradha and Daval (2008) the research was undertaken on "Futures Trading in pulses, benefits whom?" The motive of the study was to find out who is benefited by futures trading in agricultural commodities in India. The study concluded that farmers do not benefit from commodity investing.

3.Dr. Veena K.P. (2015) the study on "Investor Perception towards Trading in Equity Derivative Market: A Study at Angel Broking Pvt. Ltd., Mysore". This study shows that factors like fluctuations in asset price in stock market, collaboration of national domestic market with international markets, development of risk management tools have led to the growth in equity derivatives.

4. Mohammed Rubani (2017) the study on "A Study of Derivative Market in India". The study emphasis that derivative has no independent value. The value of derivative is derived from underlying cash asset. Derivative instruments are used to hedge risk. It also focuses on evolution of capital market. Trading in derivative instrument like futures serve as a tool of risk reduction for farmers, producers, investors, bankers, traders, etc.

Objectives:

1. To verify the overall level of awareness in investors regarding derivatives and their understanding of the concept.
2. To identify the factors influencing investor's perceptions towards derivatives, including risk perception, potential returns, complexity, and market volatility.
3. To analyze the extent to which past experiences of derivatives trading has affected current perceptions and willingness of investors to invest in derivatives.
4. To investigate the relationship between investor's perception of derivatives and their investment preferences, including asset allocation and risk tolerance.

Research Methodology:

Sample size: 100 people

Sampling method: Convenience sampling

Research method: survey

Tool for Data collection: Structured questionnaire circulated in the form of Google forms.

Sources of data: Primary data collected by survey

Analysis of data

Table no. 1

Age wise classification of the respondents

Gender	Number
Male	53
Female	47
Total	100

Note: Primary collection of data

Interpretation: The above table shows the gender wise classification of respondents. 53% respondents are male whereas 47% are female. Hence, we can see no significance difference based on gender.

Table no. 2

Percentage if Income available for Investment

Percentage of income available for Investment	Income available for Investment
Between 5% to 10%	42
Between 11% to 15%	14
Between 16% to 20%	16
Between 21% to 25%	9
more than 25%	19

Note: Primary collection of data

Interpretation: This table shows the different ranges of the percentage of income available for investment along with the corresponding number of instances. The majority of instances fall within the range of 5% to 10%. Between 11% to 15% and 16% to 20% have moderate representation. The least number of instances are within the range of 21% to 25%.

Table no. 3

Reasons for not investing into derivatives

Reason behind not investing into derivative market	Weight
High risk	28
Highly speculative	25
Lack of knowledge	43
Counter party risk	4

Note. Primary collection of data

Interpretation: The table evaluates that the Lack of knowledge has the highest weight at 43, indicating it is the most prominent reason for not investing in the derivative market. High risk follows with a weight of 28, suggesting significant concern among investors regarding the risk associated with derivatives. Highly speculative is another notable reason with a weight of 25, indicating apprehension towards the speculative nature of derivative investments. Counterparty risk has the lowest weight at 4, indicating comparatively less concern regarding counterparty risk. The data suggests that addressing the lack of knowledge and risk concerns are key factors in promoting investor participation in the derivative market.

Understanding and addressing these concerns can contribute to a more informed and confident investor base, potentially leading to increased participation and liquidity in derivative markets

Hypothesis

Data interpretation null hypothesis (H0) and alternative hypothesis (H1) for the perceptions of investors towards derivatives based on gender, education, and income:

Gender:

Null Hypothesis (H0): There is no significant difference in the risk perception of derivatives between male and female investors.

Alternative Hypothesis (H1): There is a significant difference in the risk perception of derivatives between male and female investors.

Contingency Tables

Contingency Tables

	What kind of risk do you perceive while investing in stock market?					
Gender	**Fear of being windup of a company**	**Loss on investment**	**Never ventured in stock market.**	**Slump in stock market**	**Uncertainty of returns**	**Total**
Female	7	0	0	7	35	49
Male	1	1	1	6	44	53
Total	8	1	1	13	79	102

Chi-Squared Tests

	Value	df	P
X^2	7.457	4	0.114
N	102		

Null Hypothesis accepted.

The calculated value (7.457) is less than the table value (9.488), accept the null hypothesis. The study reveals that there is no significance difference in the risk perception of derivatives between male and female investors.

Education:

Null Hypothesis (H0): There is no significant difference in the risk perception of derivatives among investors with different levels of education.

Alternative Hypothesis (H1): There is a significant difference in the risk perception of derivatives among investors with different levels of education.

Contingency Tables

Contingency Tables

Educational Qualification	What kind of risk do you perceive while investing in stock market?					Total
	Fear of being windup of a company	Loss on investment	Never ventured in stock market.	Slump in stock market	Uncertainty of returns	
Graduate	4	0	0	5	15	24
Post Graduate	0	1	1	2	29	33
Professional degree holder	2	0	0	3	13	18
Undergraduate	2	0	0	3	22	27
Total	8	1	1	13	79	102

Chi-Squared Tests

	Value	Df	P
X^2	13.343	12	0.345
N	102		

Null Hypothesis accepted.

The calculated value (13.343) is less than the table value (21.026), accept the null hypothesis. The study reveals that there is no significance difference in the risk perception of derivatives between different levels of education.

Income:

Null Hypothesis (H0): There is no significant difference in the risk perception of derivatives between investors with different income levels.

Alternative Hypothesis (H1): There is a significant difference in the risk perception of derivatives between investors with different income levels.

Contingency Tables

	What kind of risk do you perceive while investing in stock market?					
Income Range	**Fear of being windup of a company**	**Loss on investment**	**Never ventured in stock market.**	**Slump in stock market**	**Uncertainty of returns**	**Total**
1,50,000 - 3,00,000	2	1	0	3	18	24
3,00,000 - 5,00,000	1	0	0	2	12	15
Above 5,00,000	1	0	0	3	21	25
below 1,50,000	4	0	1	5	28	38
Total	8	1	1	13	79	102

Chi-Squared Tests

	Value	**Df**	**P**
X^2	6.048	12	0.914
N	102		

Null Hypothesis accepted.

The calculated value (6.048) is less than the table value (21.026), accept the null hypothesis. The study shows that there is no significance difference in the risk perception of derivatives between investors with different income levels.

Findings:

Based on the formulated null hypotheses (H0) and alternative hypotheses (H1) regarding investor's perceptions of derivatives based on gender, education, and income, conclusions can be drawn from the results of statistical analysis. Statistical analysis supports the null hypothesis (H0); it suggests that there is no major difference in the perception of derivatives between male and female investors

Conclusion:

Indian investors have a fair level of knowledge of the derivatives market and its concepts. This depicts that they are not entirely unfamiliar with derivatives but may not be experts either. Many investors try to avoid investing in derivatives due to their prediction of high level of risk. Derivatives are different than traditional investments such as stocks or bonds.

The decision to invest in derivatives is affected by various factors, and risk is indeed a important concern for many investors. Income, education, and gender don't serve as direct determinants for anyone who chooses to invest in derivatives. While these factors may indirectly influence investment decisions, they are not sole factors in determining one's investment choices. Other factors such as risk tolerance, financial goals, market knowledge, and personal preferences also play significant roles. Each individual's decision to invest in derivatives is multifaceted and influenced by a combination of all these factors.

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