A Study of Retail Investors Behavior and level of Awareness about Equity Futures and Options

Shrikrishna K S

4th Semester MBA, VVCE, Mysore

Rakesh H M

Assistant Professor, Dept. of MBA, VVCE, Mysore

Abstract

The investor plays a very important role in the stock market because of their big share of savings in the country. The Regulators of the stock market never can ignore the behavior of retail investor. This study aims to understand the behavior of retails investor and their level of awareness about equity futures and options. A survey is conducted to collect data relating to the above subject. Primary data is collected from a sample of 50 retail investors of Mysore City, Karnataka, India. The study also attempts to find the factors affecting the investment behavior ofsuch as their awareness level, duration of investment etc.

Keywords: Investors Behavior, Retail Investors, Awareness level, Futures and Options.

Introduction

The Indian financial market has undergone great changes during the last two decades. One of the most significant changes is the introduction of derivatives in the year 2000. In March 1998, the L.C. Gupta Committee (LCGC) submitted its report recommending that, the introduction of the derivatives markets. The Committee strongly favours the introduction of financial derivatives in order to provide the facility for hedging in the most cost – efficient way against market risk. Even after fourteen years from introduction of derivatives, market participants especially small-retail investors are not familiar with the concept of derivatives. Still they have misconceptions about derivatives. Indeed, they feared derivatives due to lack of knowledge about them and their use. Access to risk-management instruments paper, a small attempt is made to identify the myths of derivatives. At present total turnover of derivatives business in India is around Rs. 200, 00,000 crores p.a. both in National Stock Exchange and Bombay Stock Exchange.

Before coming to the theme of the topic in elaborative way, better to know the meaning of financial derivatives. A financial derivative has an underlying asset, that is, a financial derivative is evolved to hedge the risk involved in dealing in a particular financial asset such as a share or a foreign currency, interest rate etc,. Hence, the value of a financial derivative is derived from the underlying asset, and that is why it known as a derivative security. Financial derivatives are designed to provide protection to participants in financial markets against adverse movements in the pricesof the underlying assets. They facilitate the exchange of financial assets in future at prices determined in the present. Financial derivatives include forwards, futures, swaps and options and the underlying assets to which they relative include stocks, bonds, foreign currencies, interest rates and stock market indices. Standardized derivative contracts (e.g. futures and options) are traded or transacted on organized exchanges and these are known as exchange-traded derivatives. Other derivative contracts that are privately negotiated between parties (e.g. forwards) are known as Over-the-counter derivatives as they are not transacted on organized exchanges but are privately traded. Forward contracts are commitments entered into by two parties to exchange a specific amount of money for a particular good or service at a specified future time.

Today's sophisticated international markets have helped in the rapid growth of derivative instruments. In the hands of knowledgeable investors, derivatives can derive profit from:

- Changes in interest rates and equity markets around the world
- Currency exchange rate shifts
- Changes in global supply and demand for commodities such as agricultural products, precious and industrial metals, and energy products such as oil and natural gas

Adding some of the wide variety of derivative instruments available to a traditional portfolio of investments can provide global diversification in financial instruments and currencies, help hedge against inflation and deflation, and generate returns that are not correlated with more traditional investments

Literature review

Dr. ArifurRehman Shaikh, Dr. Anil B. Kalkundarikar conducted a research on, “ANALYSIS OF RETAIL INVESTOR’S BEHAVIOUR IN BELGAUM DISTRICT, KARNATAKA STATE” (July 2011). This research observed that 0.096 point change in knowledge boosts investors return expectation by 1 point. Investors having extensive knowledge has the return expectation of multifold when compared to other knowledge categories. The primary rational behind this phenomenon is that small investors put small investments in long range investments with rational expectation; on the other hand the investors with extensive knowledge use their awareness to read the market trend and swap their investments to achieve optimum returns.

Dr. Shaik Abdul Majeeb Pasha conducted a research on, "RETAIL INVESTORS' PERCEPTION ON FINANCIAL DERIVATIVES IN INDIA" **(2013).** The research concludes that thederivatives offer a proven method of breaking risk into component pieces and managing those components independently. Almost every investor has unique risk profile inherent in his investment portfolio and that can be better managed through derivatives trading.

Dr. Giridhar K.V, Mr. Krishna M.M. (Feb 2014),"A STUDY ON COMMODITY DERIVATIVES: AN AVENUE FOR INVESTMENT" The research concludes that apart from other products more products like Commodity Options need to be introduced. This will further help deepen the market & would help in increasing the popularity of such exchanges. This will finally lead to a wider investor base & lesser power in the hands of ruthless traders & speculators.

Dr. T. N. Murty and P.V.S.H Sastry, "INVESTMENT PERCEPTION OF SMALL INVESTORS - A SCIENTIFIC ANALYSIS"The research concludes that it is better to bring the government or regulatory bodies like SEBI lot of awareness and encourage in retail investors in equities to become greater part of development of economic system for making investment on long term basis.

Gaurav Agrawal and Dr.Mini Jain, "INVESTOR'S PREFERENCE TOWARDS MUTUAL FUND IN COMPARISON TO OTHER INVESTMENT AVENUES" After analyzing & interpreting the data received from the respondents, it may be concluded that maximum investors are aware about Banks & LIC investment avenues only. More than 80% investors are aware about Mutual Funds, Real Estate, and NSC investment avenues.

ShanmngaSundaram V examined (2011)"THE IMPACT OF BEHAVIOURAL DIMENSIONS OF INVESTORS IN CAPITAL MARKET"and concluded that investors decisions are influenced by psychological factors as well as behavioural dimensions and this psychological effect is created by the fear of losing money due to sudden decline in the stock indices, greed and lack of confidence about their decision making capability.

Lovric M (2008),“INDIVIDUAL INVESTOR BEHAVIOUR IN WHICH INVESTMENT DECISION ARE SEEN IN AN INTERACTIVE PROCESS OF INTERACTIONS BETWEEN THE INVESTOR AND THE INVESTMENT ENVIRONMENT”and they suggested that this conceptual model can be used to build stylized representation of individual investors and further studied using the paradigm of agent based artificial financial markets.

Steven C Blank,“RESEARCH ON FUTURES MARKETS: ISSUES, APPROACHES AND EMPIRICAL FINDINGS” and they concluded that increased contact between academic and industry analysts in forums such as those sponsored by the futures exchanges can serve as an “arbitrage” process to keep research progressing efficiently in useful directions.

Bharathidasan, Institute of Management, (School of Excellence of Bharathidasan University), Tiruchirapalli, “A STUDY ON INVESTORS PREFERENCES TOWARDS VARIOUS INVESTMENT AVENUES IN CAPITAL MARKET WITH SPECIAL REFERENCE TO DERIVATIVES” finally concluded that the awareness about the various uses of derivatives can help investors to reduce risk and increase profits. Though the stock market is subjected to high risk, by using derivatives the loss can be minimized to an extent.
R. Dixon, R.K. Bhandari, “DERIVATIVES, RISK AND REGULATION: CHAOS OR CONFIDENCE?” concludesthat there has been an extraordinary increase in the use of financial derivatives in the capital markets. Consequently derivative instruments can have a significant impact on financial institutions, individual investors and even national economies.

Objectives of the study

1. To test level of awareness among retail investors with regard to futures and options
2. To identify the objectives of investments in equity futures and options
3. To assess the perception on behavior of investors towards equity futures and options

Limitations of the study

- The views of respondents will be subjected to their bias and prejudice.

- The research does not cover the entire population of all the branches of ING VYSYA BANK customers, it only concentrates on the customers of IngVysya Bank of Kuvempu Nagar Branch Mysore due to the limitation of time and resources.
- The findings of this study would be based on sample size, so they cannot be generalized.
- Study will be made only in Mysore.
- The research period is very short. Therefore, time constraint could be a limiting factor

Research methodology

Sample source

The research is purely done on the retail investors who have invested their funds in one or the other financial instrument. So the sample source of the study is Retail Investors.

Sample size

The sample size we have taken is ***50*** retail investors who have invested in any financial instruments in Mysore city. The sample size taken is very small when compared to the actual population but the 50 respondents are selected randomly and there will be no bias in choosing the respondents or sample size.

Sampling technique

Non-probability sampling, it represents a group of sampling techniques that help researchers to select units from a population that they are interested in studying.So under this research the sample is taken out of the retail investors who are directly related to our study.

Sampling Method:

*Purposive Sampling,*It is also known as judgmental sampling, selective sampling or subjective sampling, is a type of non-probability sampling technique where the units that are investigated are based on the judgment of the researcher. The main goal of purposive sampling is to focus on particular characteristics of a population that are of interest, which will best enable to answer research question.

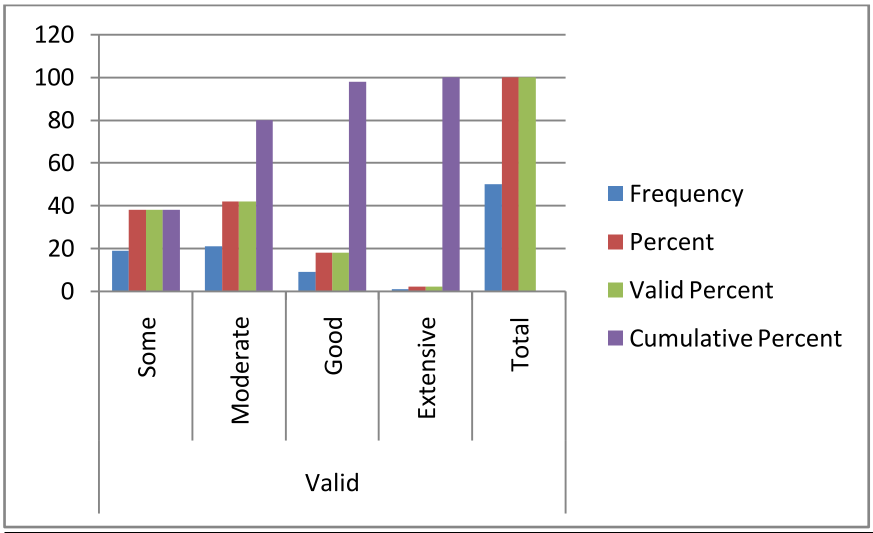
Data collection method

The research is based on primary data and the primary data is collected through Questionnaire method. A questionnaire has been structured to get needed information from respondents. Questionnaires have been termed differently, including surveys, schedules, indexes or indicators, profiles, studies, scales, inventories, etc.

Data analysis and Interpretation

Table 1:Level of Investment knowledge					
		Frequency	Percent	Valid Percent	Cumulative Percent
	Some	19	38.0	38.0	38.0
	Moderate	21	42.0	42.0	80.0
	Good	9	18.0	18.0	98.0
	Extensive	1	2.0	2.0	100.0
	Total	50	100.0	100.0	

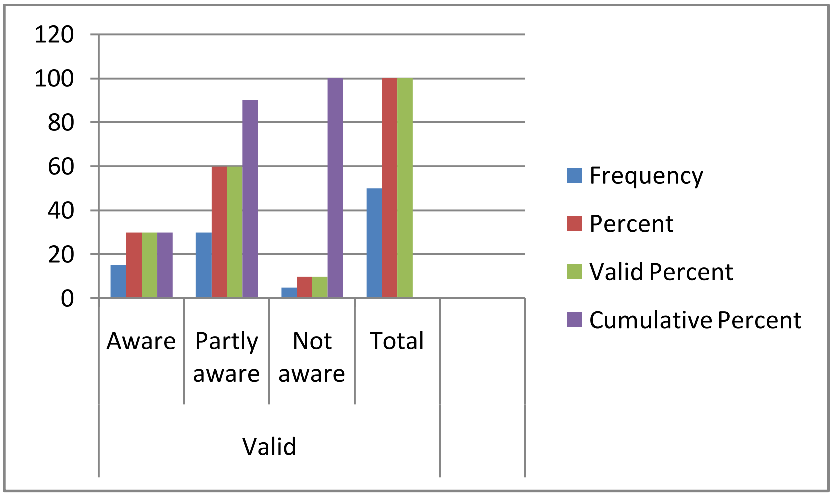
Graph 1:Level of Investment knowledge



Out of 50 respondents (retail investors) it has been proved that, 38% of people have 'Some' knowledge, 42% of people have 'Moderate' knowledge and 18% of people have 'Extensive' knowledge. This analysis shows that majority of investors have 'Moderate' knowledge about Investment i.e., 42%. The statistics of level of investment knowledge is represented in the above diagram.

Table 2: Level of Awareness about Derivatives					
		Frequency	Percent	Valid Percent	Cumulative Percent
	Aware	15	30	30	30
	Partly aware	30	60	60	90
	Not aware	5	10	10	100
	Total	50	100	100	

Graph 2:Level of Awareness about Derivatives

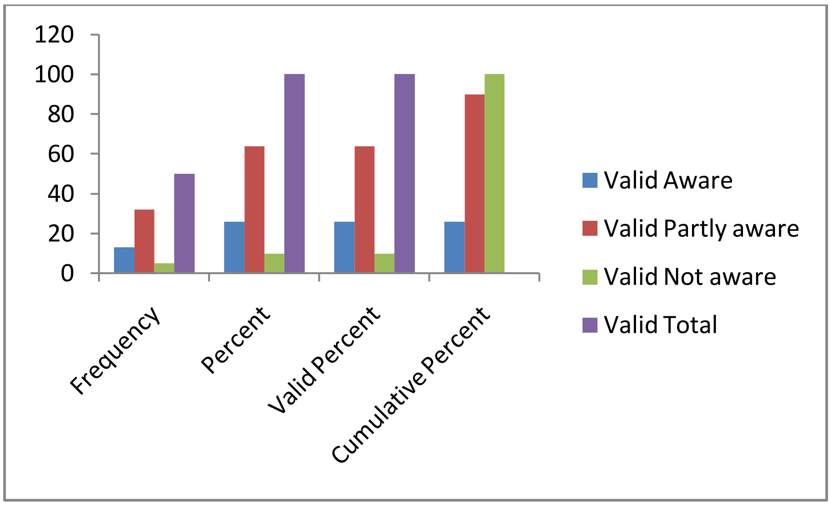


Derivative is one of the emerging investment opportunity and many retail investors are not aware about derivatives. The research reveals that out of 50 respondents 30% have awareness about derivatives, 60% are partly aware and 10% of investors are doing have awareness about the concept of derivatives. This statistics is represented in the above graph.

Table 3: Awareness about Equity Futures and Options

		Frequency	Percent	Valid Percent	Cumulative Percent
	Aware	13	26	26	26
	Partly aware	32	64	64	90
	Not aware	5	10	10	100
	Total	50	100	100	

Graph 3:Awareness about Equity Futures and Options

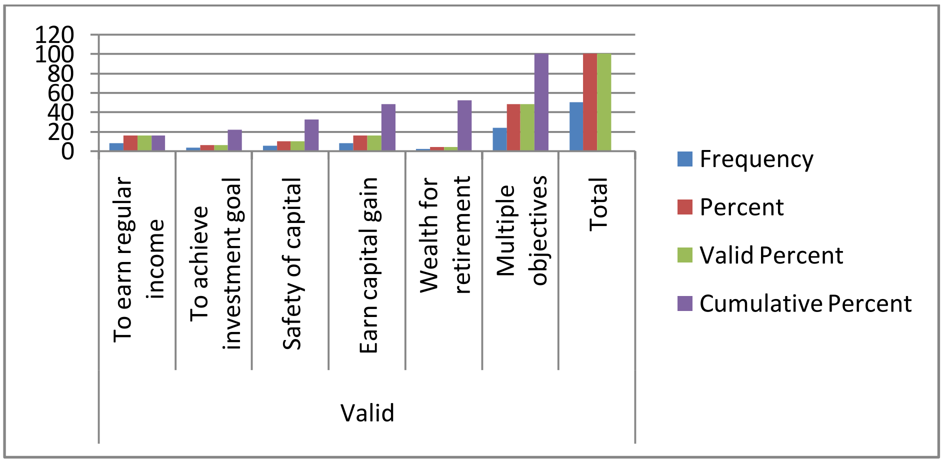


Equity future and option is one of the components of Derivative market. Many of the investors are not even hear the concept of equity future and option. Out of 50 respondents we came to know that 26% are aware about equity futures and options, 64% are partly aware and 10% are not aware about that. This statistics is represented in the above graph.

Table 4:Objectives of investment in Equity Futures and Options

		Frequency	Percent	Valid Percent	Cumulative Percent
	To earn regular income	8	16	16	16
	To achieve investment goal	3	6	6	22
	Safety of capital	5	10	10	32
	Earn capital gain	8	16	16	48
	Wealth for retirement	2	4	4	52
	Multiple objectives	24	48	48	100
	Total	50	100	100	

Graph 4:Objectives of investment in Equity Futures and Options

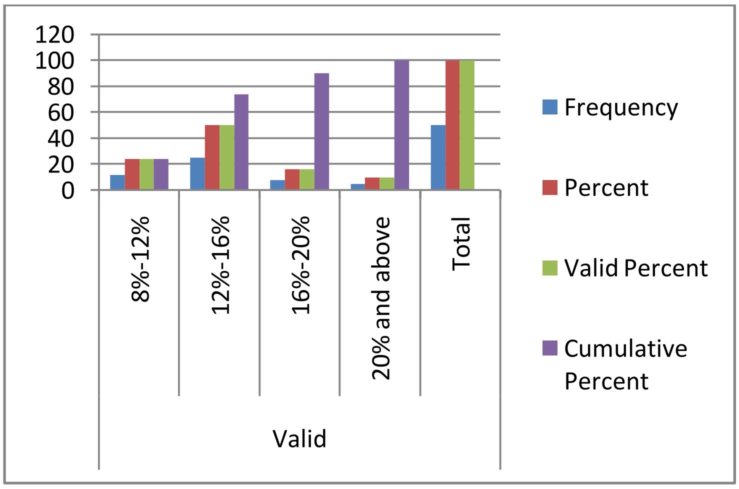


The objectives of investment differ from investor to investor and investment to other investment. So under this research we have taken 6 different objectives to know the major objectives of the investment. The analysis proved that out of 50 respondents 16% of investors invest for the purpose of earning regular income, 6% of the investors invest for the purpose of achieving their investment goal, 10% of investors objective is to safe guard their investment, 16% of investors objective is to earn capital gain in the long term, 4% of investors are investing for the purpose of their retirement benefits and the majority of investors i.e., 48% of investors have multiple objectives in their investment.

Table 5:Expected rate of return on investment perannum

	Frequency	%	Valid Percent	Cumulative Percent
8%-12%	12	24	24	24
12%-16%	25	50	50	74
16%-20%	8	16	16	90
20% and above	5	10	10	100
Total	50	100	100	

Graph 5:Expected rate of return on investment per annum



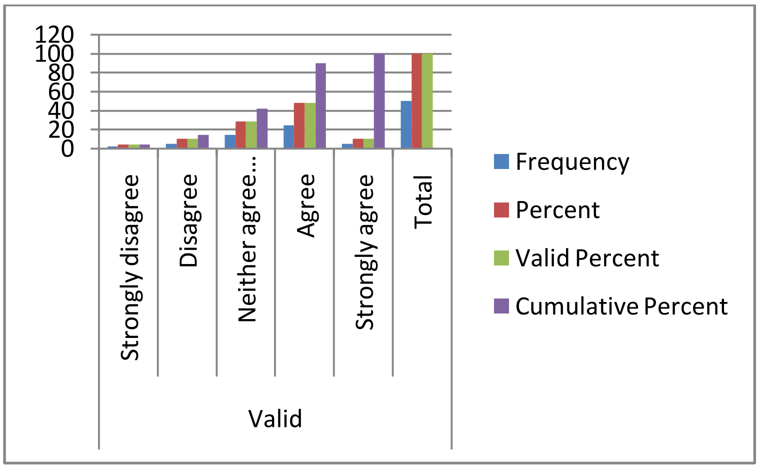
The expectation of returns on investment differs from investors to investors, some investors will give more importance to the rate of return, and some give more importance to safety of the investment. So the return expectation of different investors are analyzed and the result is that, out of 50 respondents 24% investors expect 8-12% return per annum, 50% of investors expect 12-16% return per annum, 16% of the investors expect 16-20% return per annum and 10% investors expect more than 20% return per annum. This statistics is graphically represented in the above diagram.

Table 6:Derivatives are the emerging investment opportunities of present scenario

		Frequency	Percent	Valid Percent	Cumulative Percent
	Strongly disagree	2	4	4	4
		5	10	10	14

Disagree				
Neither agree nor disagree	14	28	28	42
Agree	24	48	48	90
Strongly agree	5	10	10	100
Total	50	100	100	

Graph 6: Derivatives are the emerging investment opportunities of present scenario

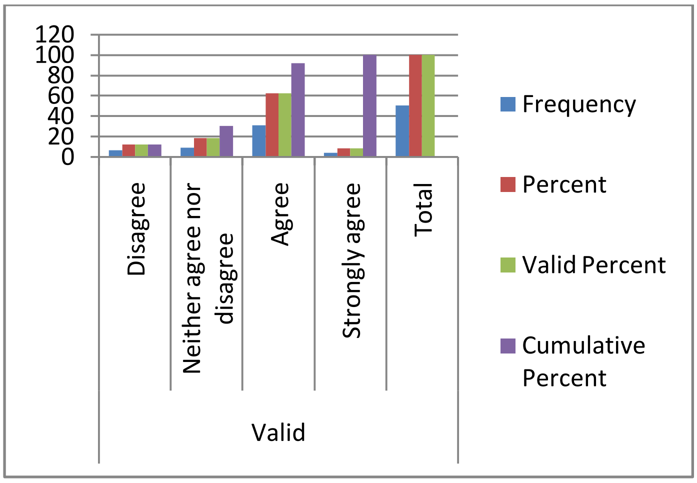


Derivative is one of the investment opportunities where many of the investors are not even aware about the derivatives. In past 1 decade the derivatives have become very popular in the financial market. So for the statement, "Derivatives are the emerging investment opportunities of present scenario" out of 50 respondents 4% of investors strongly agree, 10% of investors disagree, 28% of investors neither agree nor disagree, 48% agree and 10% strongly agree. This is represented in the above graph.

Table 7: Equity Futures and Options are way to reduce the risk in investment				
	Frequency	**Percent**	**Valid Percent**	**Cumulative Percent**
Disagree	6	12	12	12
Neither agree nor disagree	9	18	18	30
Agree	31	62	62	92

Strongly agree	4	8	8	100
Total	50	100	100	

Graph 7: Equity Futures and Options are best way to reduce the risk in investment

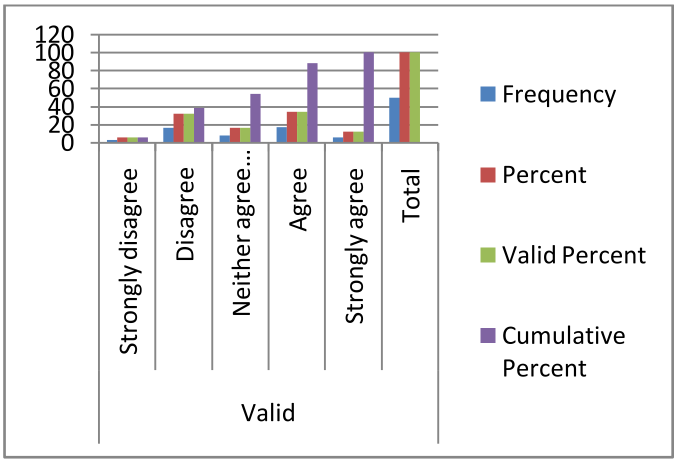


The above table and graph represent the opinion of the retail investors towards the equity futures and options whether it is the best way of reducing the risk in investment. Out of 50 respondents 12% disagree that equity futures and options are the best way to reduce the risk of investment. 18% of the respondents neither agree nor disagree, 62% agreed and 8% strongly agreed. So, maximum respondents agreed that equity futures and options are the best way to reduce risk in investment.

Table 8:The risk avoiders are interested towards Equity Futures and Options

		Frequency	Percent	Valid Percent	Cumulative Percent
	Strongly disagree	3	6	6	6
	Disagree	16	32	32	38
	Neither agree nor disagree	8	16	16	54
	Agree	17	34	34	88
	Strongly agree	6	12	12	100
	Total	50	100	100	

Graph 8:The risk avoiders are interested towards Equity Futures and Options

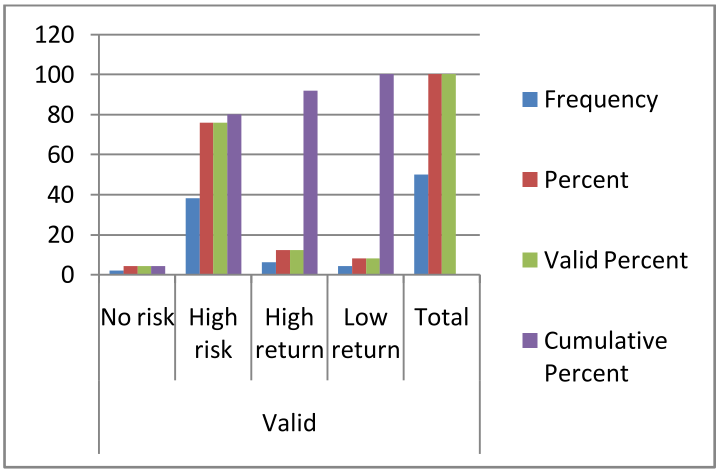


Out of 50 respondents 6% strongly agreed that only the risk avoiders are interested towards equity futures and options, 32% disagree, 16% neither agree nor disagree, 34% agree and 12% of respondents strongly agreed. So, maximum investors agreed that only the risk avoiders are interested towards equity futures and options.

Table 9:Kind of investment the Equity Futures and Options are.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No risk	2	4	4	4
	High risk	38	76	76	80
	High return	6	12	12	92
	Low return	4	8	8	100
	Total	50	100	100	

Graph 9:Kind of investment the Equity Futures and Options are.

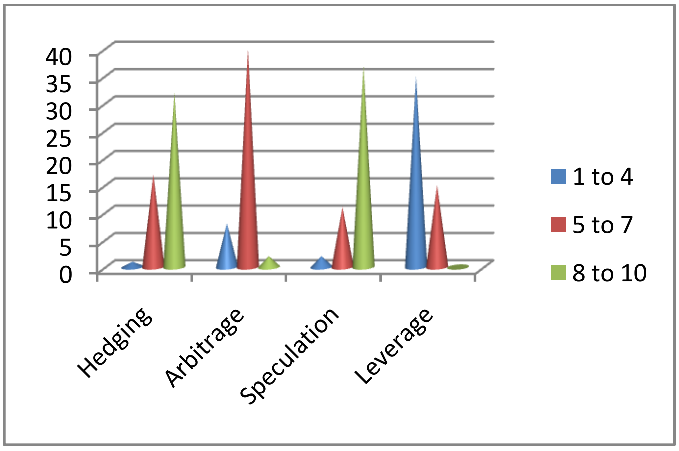


According to 4% of the retail investors equity futures and options are no risk investment, 76% told that it is a high risk investment, 12% said that it is a high return investment and 8% of the respondents told that the equity futures and options are low return investment. Majority of the population presumes that equity futures and options are high risk investment.

Table 10:Showing the feature of Derivatives

	Hedging	Arbitrage	Speculation	Leverage
1 to 4	1	8	2	35
5 to 7	17	40	11	15
8 to 10	32	2	37	0

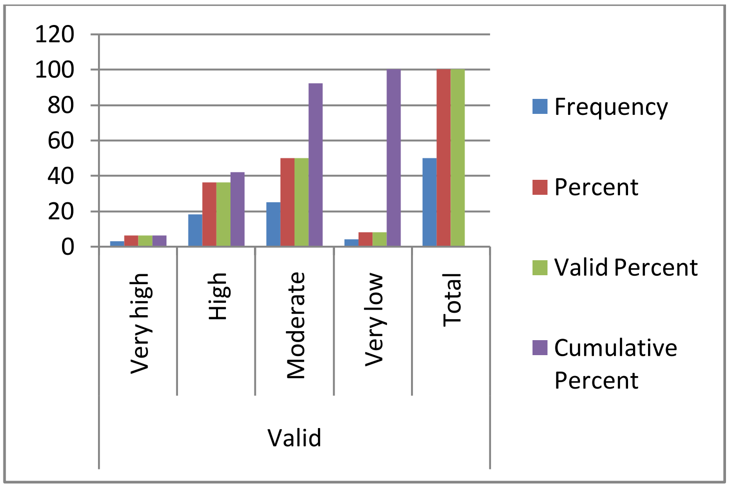
Graph 10:Showing feature of Derivatives



The above table and graph shows that the rating given by the investors out of 10 point scaling. There is only 1 investor, who rated below 4 as derivatives are used for hedging, 17 rated 5 to 7 and 32 rated 8 to 10. Majority rated 5 to 7 points for arbitrage. Majority rated 8 to 10 points for speculation and many investors will not use derivatives for leverage.

Table 11:Liquidity perception regarding Equity Futures and Options				
	Frequency	**Percent**	**Valid Percent**	**Cumulative Percent**
Very high	3	6	6	6
High	18	36	36	42
Moderate	25	50	50	92
Very low	4	8	8	100
Total	50	100	100	

Graph 11:Liquidity perception regarding Equity Futures and Options

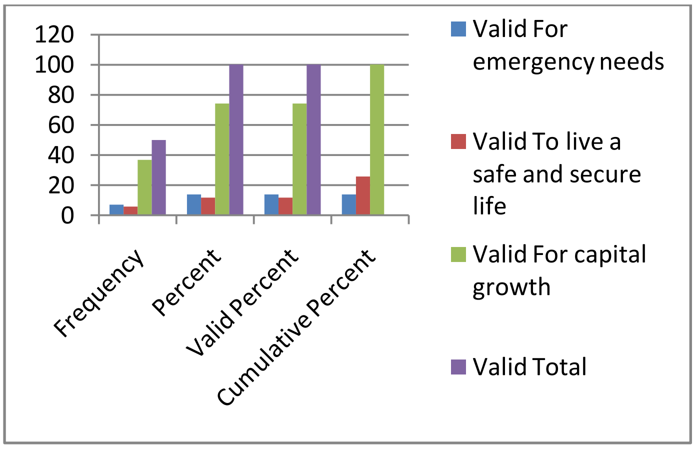


Liquidity is one of the important factors to be considered while deciding about the investment. So the investor looks the level of liquidity in investing on any investment option. Out of 50 respondents 6% said that the level of liquidity is very high in equity futures and options, 36% feels that liquidity is high, 50% believe that liquidity will be moderate and 8% say that the level of liquidity is very low in equity futures and options.

Table: 12Reasons for Investment					
		Frequency	**Percent**	**Valid Percent**	**Cumulative Percent**
	For emergency needs	7	14	14	14
	To live a safe and secure life	6	12	12	26

	For capital growth	37	74	74	100
	Total	50	100	100	

Graph 12:Reasons for Investment

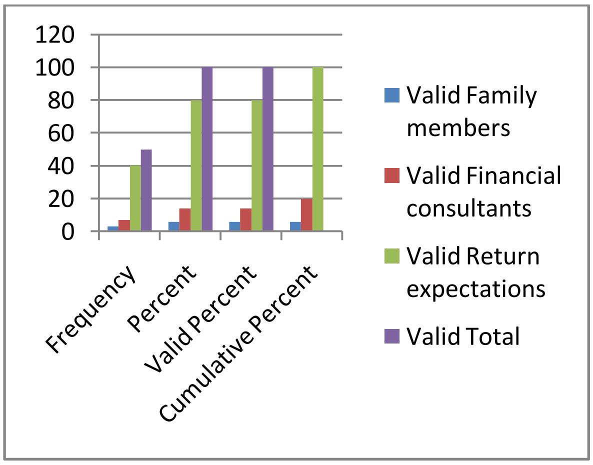


The purpose of investing in different investment alternatives will differ from person to person; the reasons of investing of different investors are represented in the above diagram and table. 14% of the respondents invest for the purpose of emergency needs, 12% of the respondents invest to live a safe and secured life and 74% for the purpose of capital growth. So majority of the investors are interested to invest for the purpose of capital growth.

Table 13:Factors affecting Investment behavior

		Frequency	Percent	Valid Percent	Cumulative Percent
	Family members	3	6	6	6
	Financial consultants	7	14	14	20
	Return expectations	40	80	80	100
	Total	50	100	100	

Graph 13:Factors affecting Investment behavior

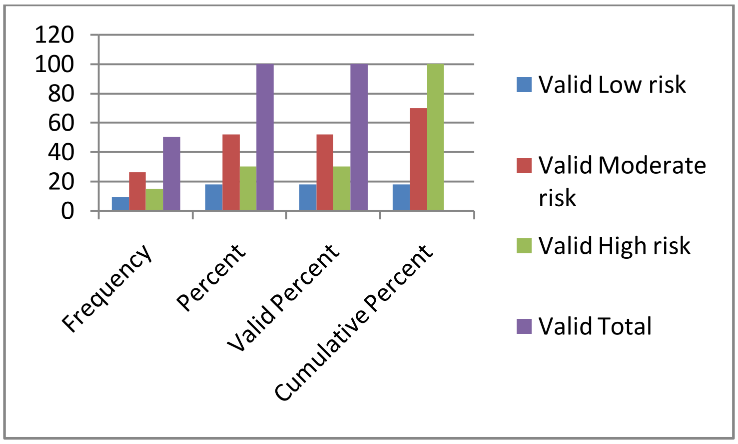


The behavior of the investors will be affected by multiple factor; it differs from one person to another. 6% of the respondents told that the main factor the influence on the investment is family members, 14% told that the investment behavior affected by financial consultants and 80% told that the investment will be affected by the return expectation of the investors.

Table 14:Risk level of investors in Equity Futures and Options

		Frequency	Percent	Valid Percent	Cumulative Percent
	Low risk	9	18	18	18
	Moderate risk	26	52	52	70
	High risk	15	30	30	100
	Total	50	100	100	

Graph 14:Risk level of investors in Equity Futures and Options

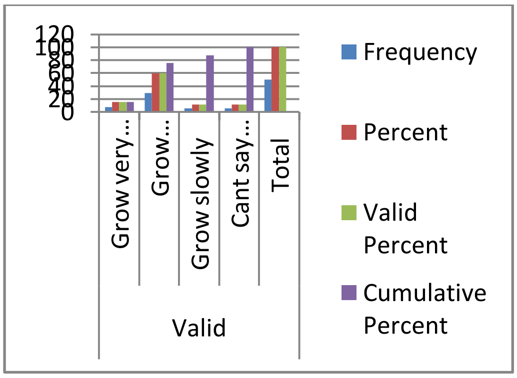


Out of 50 respondents 18% told that investors risk level in equity futures and options is low, 52% told that risk is moderate and 30% feel that risk is high in equity futures and options.

Table 15:Perceptions towards Derivative trading in India

	Frequency	Percent	Valid Percent	Cumulative Percent
Grow very fast	8	16	16	16
Grow moderately	30	60	60	76
Grow slowly	6	12	12	88
Can't say anything	6	12	12	100
Total	50	100	100	

Graph 15:Perceptions towards Derivative trading in India



As derivative is the recent development in the Indian financial market, the perceptions towards the derivatives among retail investors are different. Out of 50 respondents 16% perceived that the derivatives market will grow very fast, 60% feel that grow moderately, 12% feel that grow slowly and 12% told that can't say anything about the derivatives.

Table 16

Sl No	Factors	Variance	Skewness	Std error	Kurtosis	Std error
1	**Level of Investment knowledge**	.627	.555	.337	-.403	.662
2	**Awareness about Derivatives**	.449	.592	.337	1.043	.662
3	**Awareness about Equity Futures and Options**	.341	.025	.337	-.113	.662
4	**Objectives of investment in Equity Futures and Options**	3.72	-.641	.337	-1.118	.662
5	**Expected rate of return on investment per annum**	.802	.645	.337	-.101	.662

6	**Derivatives are the emerging investment opportunities of present scenario**	.908	-.737	.337	.475	.662
7	**Equity Futures and Options are best way to reduce the risk in investment**	.637	-.802	.337	.250	.662
8	**Only the risk avoiders are interested towards Equity Futures and Options**	1.38	-.048	.337	-1.145	.662
9	**According to you Equity Futures and Options are ………………. Investment**	.431	1.510	.337	2.424	.662
10	**What is the liquidity perception regarding Equity Futures and Options**	.834	.862	.337	1.576	.662
11	**Reasons for Investment**	.531	-1.518	.337	.707	.662
12	**Factors affecting Investment behavior**	.907	-1.745	.337	1.468	.662
13	**Risk level of investors in Equity Futures and Options**	.475	-.160	.337	-.826	.662
14	**Perceptions towards Derivative trading in India**	.735	.810	.337	.315	.662

Findings of the study

- Retail investors have moderate knowledge about investment.
- Majority of retail investors have moderate knowledge about derivatives.
- Majority of the retail investors are partly aware of equity futures and options.
- The retail investors invest their funds not for single objective but for multiple objectives.
- Average return expectation on the investment is 12-16%.
- Derivatives are the emerging investment opportunity in present scenario.
- To reduce risk equity futures and options are best alternative.
- Equity Futures and Options are attracted by the risk avoiders.
- Equity Futures and Options are high risk investment.
- The level of liquidity is moderate in Equity Futures and Options.
- The main intention of investment is for capital growth.
- The main factor that affects investor’s behavior is return expectation.
- Moderate risk is there in Equity Futures and Options.
- Derivative will grow moderately in future.

Conclusion

The most important issue in efficient market theory is that it is not possible to outperform the market over the long-term. An efficient capital market is characterized by the fact that information is available to all investors or market participants, so stock prices always incorporate and reflect all relevant information. Due to this issue, the price of a stock should reflect the knowledge and expectations of all investors or market participants.

Behavioural finance with regard to investor behaviour is creating a revolution in financial theory. The combination of financial theory with other social sciences resulted in the appearance of behavioural finance. This is a relatively young and promising field of modern finance which has future registering remarkable progress in the last decades. It analysis the investor edge of investment decision making process and awareness about equity futures and options.

The study reveals that the respondents assimilate the objectives of saving, the factors influencing the saving and the sources of information for decision making. The annual income and the annual saving are given importance of consideration by the respondents, because the level of income decides the level of savings. The investors are partly aware about the equity futures and options and finally they feel that market movements affect the investment pattern of investor

References

- Analysis of Retail investor’s Behavior in Belgaum District, Karnataka State, by Dr. ArifurRehman Shaikh, Dr. Anil B Kalkundarikar on July 2011.
- Retail investors perception on financial derivatives in India, by Dr. Shaik Abdul Majeeb Pasha on 2013
- A study on commodity derivatives: an avenue for investment, by Dr. Giridhar K.V, Mr. Krishna M.M
- Investment perception of small investors - a scientific analysis, byDr. T. N. Murty and P.V.S.H Sastry
- Investor’s preference towards mutual fund in comparison to other investment avenues, byGaurav Agrawal and Dr.Mini Jain.

- The impact of behavioral dimensions of investors in capital market, byShanmngaSundaram V on 2011.
- Individual investor behavior in which investment decision are seen in an interactive process of interactions between the investor and the investment environment, by Lovric M on 2008.
- Research on futures markets: issues, approaches and empirical findings, bySteven C Blank
- Investment property portfolio management and financial derivatives, byPatrick McAllister, John R. Mansfield.Management’s disclosure of hedging activity: an empirical investigation of analysts and investors reactions, byJennifer Reynolds Moehrle