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STUDY ON DERIVATIVES WITH REFERENCE TO SHAREKHAN

1 .SUSMITHA, 2.Dr. B. RENUKA

[1]MBA STUDENT SCHOLAR, TKR COLLEGE OF ENGINEERING&TECHNOLOGY, HYDERABAD,TELANGANA,INDIA
[2]ASSISTANT PROFESSOR ,TKR COLLEGE OF ENGINEERING&TECHNOLOGY, HYDERABAD,TELANGANA,INDIA

ABSTRACT: To understand the concept and to know about derivatives market in India.To study about futures and options market and analyze the operations.To analyze profit/loss position of futures buyer and seller and also the option writer and option holder.To study various trends in derivatives market.To increase the integration of financial market with the international market.Derivatives are mainly introduced for the purpose of reducing the risk through transferring, spreading.

KEY WORDS: PARTICIPANTS IN THE DERIVATIVE MARKETS, TYPES OF DERIVATIVES, .INDUSTRY PROFILE, DATA ANALYSIS AND INTERPRETATION

I.INTRODUCTION

1.1.STUDY ON DERIVATIVES WITH REFERENCE TO SHAREKHAN

The only stock exchange operating in the 19[Th] century were those of Bombay set up in 1875 and Ahmedabad set up in 1894. These were organized as voluntary non-profit-making association of brokers to regulate and protect their interests. Before the control of securities trading became a central subject contract act of 1925 used to regulate trading in securities. Under this act, The Bombay stock exchange was recognized in 1927 and Ahmedabad in 1937.The turnover of the stock exchange has been tremendously increasing from last 10 years. The number of trades and the number of investors, who are participating, have increased. The investors are willing to reduce their risk, so they are seeking for the risk management tools.

Prior to SEBI abolishing the BADLA system, the investors had this system as a source of reducing the risk, as it has many problems like no strong margining system, unclear expiration date and generating counter party risk. In view of this problem SEBI abolished the BADLA system.

1.2. DEFINITION:

Derivative is a product whose value is derived from the value of an underlying asset in a contractual manner. The underlying asset can be equity, forex, commodity or any other asset.

1.3.PARTICIPANTS IN THE DERIVATIVE MARKETS:

The following three broad categories of participants:

A. HEDGERS:

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

B. SPECULATORS:

Speculators wish to bet on future movements in the price of an asset. Futures and options contracts can give them an extra leverage; that is, they can increase both the potential gains and potential losses in a speculative venture.

C. A**RBITRAGERS**:

Arbitrageurs are in business to take 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 position in the two markets to lock in a profit.

1.4. TYPES OF DERIVATIVES:

The following are the various types of derivatives. They are:

A. 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.

B. FUTURES:

A futures contract is an agreement between two parties to buy or sell an asset at a certain time in the at a certain price.

C. 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 give future date. Puts give the seller 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.

D. WARRANTS:

Options generally have lives of up to one year; the majority of options traded on options exchanges having a maximum maturity of nine months. Longer-dated options are called warrants and are generally traded over-the counter.

1.5. ELIGIBILITY OF ANY STOCK TO ENTER IN DERIVATIVES MARKET

- Non promoter holding (free float capitalization) not less than Rs.750crores from last 6 months.
- Daily Average Trading value not less than 5 crores in last 6 months.
- At least 90% of Trading days in last 6 months.
- Non-Promoters Holding at least 30%.
- BETA not more than 4 (previous last 6 months)

II.REVIEW OF LITERATURE

2.1. AnjumSiddiqui (2007)- Financial contracts, risk and performance of Islamic banking.

The purpose of this paper is to focus on various modes of Islamic finance and examines their risk and other characteristics by conducting a selective literature review.

2.2. **Jabir Ali(2008)** - Efficiency in agricultural commodity futures markets in India.

In line with the ongoing global and domestic reforms in agriculture and allied sectors, the Indian Government is reducing its direct market intervention and encouraging private participation based on market forces. This has led to increased exposure of agricultural produce to price and other market risks, which consequently emphasize the importance of futures markets for price discovery and price risk management. The

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purpose of this paper is to analyze the efficiency of agricultural commodity markets by assessing the relationships between futures prices and spot market prices of major agricultural commodities in India.

2.3. **GeoffroyEnjolras(2010)** - Combining participating insurance and financial policies.

The purpose of this paper is to examine a new insurance policy against natural disasters.

2.4. **Md. MahmudulAlam(2018)** - The Islamic Shariah principles for investment in stock market.

Because of chronic financial crises experienced during past several decades repeatedly and a failure to protect investors' rights as a result, the world is looking for an alternative form of stock market for quite some time so that interests of all relevant stakeholders can be safeguarded. At the same time, from the perspectives of devout Muslims, the current form of stock market restricts a Muslim to make investments in the market because of several unsatisfying provisions from the viewpoint of the Islamic law known as Shariah. This study aims to provide the criteria under which conditions of the Islamic Shariah permit making investments in the stock market. Hand in hand with that primary discussion, it has been eluded briefly why the Islamic Shariah principles offer a better alternative against conventional practices of the stock market.

2.5. Jing Chi, Martin Young(2005)- Developing a Financial Derivatives Market in China

While China is currently moving toward the full development of its own financial derivatives markets, to date, China's experience with these has been a negative one. This paper examines the importance to China of developing a fully integrated financial derivatives market from both the economic and financial market perspectives. It examines the best way forward for derivative trading, both markets based and over-the-counter, and the types of products best suited to both, given the current state of the Chinese financial markets. Consideration is given to market structure, regulation, trading and settlement systems and international cooperation.

III. INDUSTRY PROFILE&COMPANY PROFILE

3.1.INDUSTRY PROFILE

The Indian stock market turned out to be among the world's best performers in 2016-17 with the Bombay Stock Exchange (BSE) Sensex rising 29% from 21,140 on January 1 to 27,312 on December 19. Most market players believe this stellar run will continue in 2016 on the back of reforms, strong foreign fund inflows, revival of manufacturing, improvement in the macro-economic situation and rise in corporate earnings growth.

3.1.1.Attractive Valuations

Despite the sharp rise, the valuation of the Indian stock market is still attractive. On

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December 12, the Sensex was trading at a price-to-earnings (PE) ratio of 18.5, marginally lower than the five-year average of 18.77. One reason is that the return on equity of BSE 200 companies is bottoming out. "Revival of growth of Indian companies, which were facing tough times for the past five years, is still at a nascent stage. Nifty 50 companies can see 16-17% earnings growth in the next one year.

Stocks that respond to interest rate moves, coupled with select debt schemes, are likely to be the winners in 2016, with the Reserve Bank of India expected to start easing its monetary policy.

Fund managers said economic prospects have improved, but the New Year may be tougher for equity investors to make money as valuations of many stocks are rich after the broad-based rally in 2015. Concern over interest rate hike in the US and weak global crude oil prices may also keep investors on.

India is among the top-performing emerging markets in 2015. So far in 2015, the Sensex has gained 34%. Smaller companies have fared even better, with the BSE Mid Cap index surging 56% and the BSE Small Cap Index jumping 75%.

Market participants consider probable interest rate cuts by the Reserve Bank of India (RBI) as the biggest trigger for the economy and the markets. The extent of monetary policy easing would determine the strength of rally in shares of the so-called interest rate-sensitive sectors such as banks, auto, real estate andbonds. Fund managers said debt funds could offer good returns in the coming year as a fall in interest rates could lead to an appreciation in bond prices. With wholesale price inflation coming at nil for November, expectations of interest rate cuts as early as in the March quarter are high. "Short term rates can fall more than long-term rates. We expect consumer inflation to be in the range of 5-5.5%, and expect RBI to cut interest rates by 50 basis points in 2015," said DhawalDalal, executive V-P and head (fixed income), DSP BlackRock Mutual Fund. If interest rates fall by 50 basis points, investors could see a 5% capital appreciation on their long-term gilt fund portfolio.

"Gold's under-performance was mainly due to prices falling in dollar terms amid anticipated tapering over last several months combined with FII investment in Indian stocks.

3.2 COMPANY PROFILE

SHARE KHAN, a professionally managed Investment advisory services company, developed in the year 1985 by three young entrepreneurs with an intension to Minimization of Risk and Maximization of Return in the field of Indian Capital markets by extensive research work.

As a sub member of NSE, BSE, MCX, NCDEX, NSDL and CDSL, which are pioneers in the respective operations, SHARE KHAN is having more than 500 branches in all over India.

Share khan, India’s leading stock broker is the retail arm of SSKI, an organization with over eighty years of experience in the stock market with more than 280 share shops in

120 cities and big towns, and premier online trading destination www.sharekhan.com. Share khan offers the trade execution facilities for cash as well as derivatives, on BSE and NSE depository services, commodities trading on the MCX (Multi Commodity Exchange of India Ltd) and NCDEX (National Commodity and Derivative Exchange) and most importantly, investment advice tempered by eighty years of broking experience.

Share khan provides the facility to trade in commodities through Share khan Commodities Pvt. Ltd – a wholly owned subsidiary of its parent SSKI. Share khan is the member of two major commodity exchanges MCX and NCDEX.

3.2.1. Features of Share khan company:

- You get freedom for paper work
- There are instant credit and money transfer facilities
- You can trade from any net enabled PC
- Timely advice and research reports
- Peal time portfolio tracking
- Information about price alerts.

3.2.2.SHARE KHAN IS IN MAERKET BECAUSE OF:

- Investor care is of paramount importance at SHARE KHAN
- SHARE KHAN offers large avenues of investment solutions for all classes of investors under one roof.
- SHARE KHAN Experience is one of prized possession. SHARE KHAN has an experience of more than 20 years wherein grown phenomenally.
- One of the most competitive brokerage structure.
- Hassle free trading experience.
- Timely advice along with research support to the clients through SMS and Emails on Equities, Derivatives, Commodities, IPOs and Mutual Funds.
- VALUE FOR INVESTOR'S TRUST
- INTEGRITY AND HONESTY

IV.DATA ANALYSIS AND INTERPRETATION

4.1. OBSERVATIONS AND FINDINGS

- The future price of M/S. DLF INDIA LTD moving along with the market price.
- If the buy price of the future is less than the settlement price, than the buyer of a future gets profit.
- If the selling price of the future is less than the settlement price, than the seller incur the losses.

4.2.Using Index Options

There are potentially innumerable ways of trading on the index options market. However, we shall look at eight basic modes of trading on the index futures market:

4.3.Hedging

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H5 Have portfolio, buy puts

4.4.Speculation

S3 Bullish index, buy Nifty calls or sell Nifty puts

S4 Bearish index, sell Nifty calls or buy Nifty puts

S5 Anticipate volatility, buy a call and a put at same strike

S6 Bull spreads, buy a call and sell another

S7 Bear spreads, sell a call and buy another

Arbitrage

A3 Put-call parity with spot-options arbitrage

A4 Arbitrage beyond option price bounds[1]

4.5. Strategies formulated

The simplest starting point of a Strategy could be having a clear view about the market or a scrip. There could be strategies of an advanced nature that are independent of views, but it would be correct to say that most investors create strategies based on views.

4.6.If I have a bullish view

The following strategies are possible:

- Buy a Future
- Buy a Call Option
- Sell a Put Option
- Create a Bull Spread using Calls
- Create a Bull Spread using Puts

OBSERVATIONS AND FINDINGS

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CONCLUSION:

- ➢ In derivative segment the profit/loss of the option writer purely depends on the fluctuations of the underlying asset.
- ➢ Derivatives market is an innovation to cash market. Approximately its daily turnover reaches to the equal stage of cash market. The average daily turnover of the NSE derivative segments.
- ➢ In cash market the profit/loss of the investor depend the market price of the underlying asset. The investor may incur huge profits or he may incur huge profits or he may incur huge loss. But in derivatives segment the investor the investor enjoys huge profits with limited downside.
- ➢ In cash market the investor has to pay the total money, but in derivatives the investor has to pay premiums or margins, which are some percentage of total money.

SCOPE OF THE STUDY

a.In India, all attempts are being made to introduce derivative instruments in capital market. In the forex market there are higher chances of introducing derivatives on a large scale.

b. In fact, the necessary groundwork for the introduction of derivatives in forex market was prepared by a high-level expert committee appointed by RBI.

c.Now derivatives has been introduced in India in the form of options and futures. Since, derivatives are permitted legally, one can use them to insulate his equity portfolio against the vagaries of the market

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STUDENT PROFILE

GUIDE PROFILE
Dr. B. RENUKA,
M.COM.MBA.MHRM
ASST.PROFESSOR IN MBA DEPARTMENT
TKR COLLEGE OF ENGINEERING &TECHNOLOGY,
HYDERABAD, TELANGANA.
INDIA.

V .SUSMITHA SHE IS COMPLETED HER MBA DEGREE FROM VISHWA VIKAS DEGREE COLLEGE AT NAGARKURNOOL, AND PURSUING MBA IN TKR COLLEGE OF ENGINEERING AND TECHNOLOGY,HYDERABAD,TELANGANA,INDIA.