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A Study On Investor Insights For Financial Derivatives: Pros & Cons

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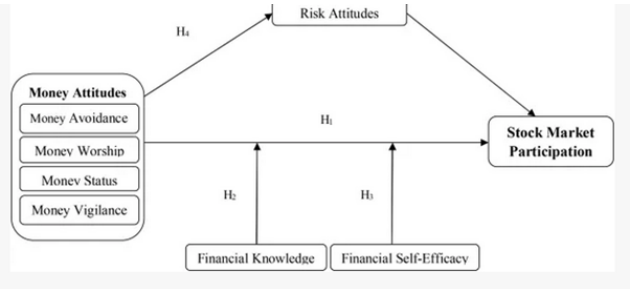
***Abstract* – Today's derivatives are based on a wide range of transactions and have a lot more applications. Even derivatives based on weather information, such how much rain fell or how many days had sunshine, exist. Derivatives come in a wide variety of forms that can be applied to risk management, speculation, and position leverage. With products that may accommodate almost every requirement or risk tolerance, the derivatives market is one that is still expanding. Derivative items fall into two categories: "lock" and "option." Lock products (such as futures, forwards, or swaps) obligate the parties to the terms of the contract from the beginning. On the other hand, option products (such as stock options) give the holder the right but not the responsibility to acquire or sell the underlying asset or security at a particular price on or before the option's expiration date. Futures, forwards, swaps, and options are the four most popular types of derivatives Advantages and disadvantages of investing in Index Derivative Market. Derivatives are new segment of secondary market operation in India; investors need to understand trade process and to make profit in derivatives market. Importance of investor has become increasing order because of Technological advancements in trading system, rapid growth of derivative market and new economic policy of 1991. Behaviour of investors tends to moves from savings to investment.**

Keywords: **Returns , Risk Factor, Market dynamics, Profit rate.**

I. INTRODUCTION

The Indian derivative market is a segment in the secondary market operations. Trading on derivatives is a type of financial contract between two or persons the value of which depends on another underlying asset or group of assets like stocks, commodities, bonds etc. Derivatives are commonly used by the investors to mitigate risks in the market, speculation, hedging and arbitrage. These are also known as contingent claims. Derivatives can be traded on an exchange or 'over-the-counter'. Prices of derivatives are derived from fluctuations in the underlying assets namely commodities and stocks indices and currency.

These are used for hedging risk and wealth maximization basing on the speculation in the market. Derivatives are not only used to partially or fully lockup risks in the financial markets and assets, but also gaining minimum capital appreciation or acquiring profits for risk investors. These are of four types – futures, forwards, swaps and options. The Financial Industry Regulatory Authority (FINRA) regulates the parties in derivative contracts. The National Futures Association (NFA) oversees the derivative markets and parties to derivative contracts. Indian investors started trading derivatives since 2000 starting with index futures at BSE and later on NSE Since then, derivatives market is onlooking remarkable growth in terms of value and number of contracts.



People have turned out to be increasingly active in stock markets, and participation has been advanced by the introduction of new monetary products and services. However, a portion of these products is hard to grasp, particularly for monetarily unsophisticated investors. Standard models of portfolio choice consider that knowledgeable investors make rational decisions to augment lifetime utility. There are various motivations to presume that one's choice about whether to put resources into stocks might be impacted by one's money attitudes that are created through social interaction, education, and experience.

II. LITERATURE

Klontz et al., (2023). Individuals have different attitudes regarding money, for example, some people like it a lot (money worship), others do not take interest in money (money avoidance), a few people want to increase their status through money (money status), and others consider money as a source of shame (money vigilance). Money avoidance refers to believing that money is bad, that wealthy individuals are greedy and that they do not deserve money. Individuals may avoid spending money on

even sensible or essential purchases. Individuals believing in the money worship dimension are convinced that more cash will solve the majority of their issues, that there will never be a sufficient amount, and that cash brings power and happiness.

Dr Bhavna (2024) the researchers enhanced their argumentation by demonstrating that financially educated people face lower costs for gathering and handling information and consequently face a more moderate financial threshold for stock market participation. It has been investigated that both knowledge and attitudes may change behavior and knowledge may bring variation in attitudes and similarly it may also bring change in behavior via attitudes which indicates that for most people knowledge and attitudes may be considered as complementary rather than a substitute.

III. Methodology

Objectives:

- To know the general public perception towards financial derivatives in general.
- To know various advantages in investing financial derivatives.
- To study investor satisfaction level in investing financial derivatives

Hypothesis:

- Ho1: There is no significant relationship between Experience of Investment and exposure of risk in Index Derivative Market.
- Ho2: There is no significant relationship between type of investor and level of satisfaction in Index Derivative Market.

Sample:

A Sample of 100 regular derivative investors opinion was captured by using a structured questionnaire to measure the study impact.

KMO and Bartlett's Test

KMO and Bartlett's Test		
Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		.692
Bartlett's Test of Sphericity	Approx. Chi-Square	7427.582
	df	66
	Sig.	.000

The KMO value is 0.692 >0.6. Bartlett's Test of Sphericity indicates a measure of the multivariate normality of set of variables (Sig. value is less than 0.00 indicates multivariate normal and acceptable for factor analysis).

The above table shows commonalities which indicate how much of the variance in the variables has been accounted for by the extracted factors. All items have been accounted for further analysis as its extraction value is more than 0.5.

Total Variance Explained

Component	Initial Eigenvalues			Extraction Sums of Squared Loadings			Rotation Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	4.833	40.272	40.272	4.833	40.272	40.272	3.728	31.066	31.066
2	2.200	18.334	58.607	2.200	18.334	58.607	2.125	17.712	48.779
3	1.810	15.086	73.693	1.810	15.086	73.693	2.079	17.322	66.101
4	1.239	10.327	84.020	1.239	10.327	84.020	1.990	16.580	82.681
5	1.102	9.187	93.207	1.102	9.187	93.207	1.263	10.525	93.207
6	.411	3.427	96.634						
7	.139	1.160	97.793						
8	.105	.872	98.666						
9	.058	.483	99.148						
10	.046	.382	99.530						
11	.037	.311	99.842						
12	.019	.158	100.000						

Extraction Method: Principal Component Analysis.

From the above table it is observed that 5 components or factors are having Eigen value more than 1, so only these 5 factors (value of component 1 = 4.83, component 2 = 2.2, component 3 = 1.8, component 4 = 1.23, and component 5 = 1.10) are considered for further analysis. Further, the extracted sum of squared holding % of variance depicts that the first factor accounts for 40.2% of the variance features from the stated observations, the second 18.33%, the third 15.08%, the fourth 10.32%, and the fifth 9.18%. Thus, 5 components are effective enough in representing all the characteristics or components highlighted by the stated 12 variables. The scree plot is a chart which represents the eigen values against all the components. It can be seen that the curve begins to flatten between components 6 and 7. Component 6 onwards has an eigen value is less than 1, so only five factors have been retained. The Table below shows the loadings (extracted values of each item under 5 variables) of the 12 variables on the 5 factors extracted. We have extracted 5 variables wherein the 12 items are

Rotated Component Matrix[a]					
	Component				
	1	2	3	4	5
Certainty Of Performance			.486		
High Liquidity				.972	
Low Margin Deposit				.972	
Transparency In Pricing			.915		

Obligatory Nature			.932		
The Holder Is Exposed To Risk	.917				
Too Much Volatility	.899				
Margin Deposit	.892				
High Contract Size	.886				
Lack Of Flexibility		.932			
Highly Standardized		.944			
Unfair Practices Of Brokers					.865
Extraction Method: Principal Component Analysis. Rotation Method: Varimax With Kaiser Normalization.					

divided into 5 variables according to the most important items which are similar responses in component 1 and simultaneously in components 2, 3, 4, and 5. The gap (empty spaces) on the table represents loadings that are less than 0.5, this makes reading the table easier. We suppressed all loadings less than 0.5.

The idea of rotation is to reduce the number of factors on which the variables under investigation have high loadings. The component having value minimum of 0.5 is considered for further analysis. But in the above table factor Volatility in derivative market is associated with equity market is having value of more than 0.5 in two components, so these factor can't be considered for further analysis. After interpreting all components in a similar fashion, we arrived at the following descriptions:

- Component 1 - "Instrument Behavior"
- Component 2 - "Instrument Standardization"
- Component 3 - "Pricing"
- Component 4 - "Initial Investment"
- Component 5 - "Brokerage"

Ho1: There is no significant relationship between Experience of Investment and exposure of risk in Index Derivative Market.

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.107[a]	.011	.009	.572

a. Predictors: (Constant), Experience in Investment in Derivatives

The R value represents the simple correlation and is 0.66, which indicates a moderate degree of correlation. The R2 value indicates percentage of total variation in the dependent variable, and the independent variable represents the Awareness of Derivative Market. In this case the R2 (0.43) which is greater than the adjusted R2 value (0.40).

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.890	1	1.890	5.770	.017[a]
	Residual	163.110	498	.328		
	Total	165.000	499			

a. Predictors: (Constant), Experience in Investment in Derivatives

b. Dependent Variable: Exposure of risk in Equity Index Market

For the Experience in Investment in Derivatives with Exposure of risk in Index Derivative Market, the significant value (p-value) is observed to be < 0.05 (p=0.000) and the differences in mean are statistically significant. Hence there is a significant relationship between the Experience of Investment and exposure of risk in Index Derivative Market.

Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	2.057	.070		29.317	.000
	Experience in Investment in Derivatives	-.057	.024	-.107	-2.402	.017

Coefficients						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.057	.070		29.317	.000
	Experience in Investment in Derivatives	-.057	.024	-.107	-2.402	.017
a. Dependent Variable: Exposure of risk in Index Derivative Market						

The Coefficients table provides necessary information to predict Exposure of risk in Index Derivative Market from Experience in Investment in Derivatives, as well as determine whether Experience in Investment in Derivatives contributes statistically significantly to the model (by looking at the "Sig." column).

Regression equation:
Exposure of risk in Index Derivative Market = 2.057 – 0.57 (Experience in Investment in Derivatives)

Ho2: There is no significant relationship between type of investor and level of satisfaction in Index Derivative Market.

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.133[a]	.018	.016	.596

a. Predictors: (Constant), Type of Investor

The R value represents the simple correlation and is 0.13, which indicates a low degree of correlation. The R2 value indicates percentage of total variation in the dependent variable, and the independent variable represents the Type of Investor. In this case the R2 (0.018) which is greater than the adjusted R2 value (0.016).

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	3.180	1	3.180	8.946	.003[a]
	Residual	177.020	498	.355		
	Total	180.200	499			

a. Predictors: (Constant), Type of Investor

b. Dependent Variable: Level of satisfaction in Index Derivative Market

For the Type of Investor with Level of satisfaction in Index Derivative Market, the significant value (p-value) is observed to be < 0.05 (p=0.003) and the differences in mean are statistically significant. Hence there is a significant relationship between the Type of Investor and Level of satisfaction in Index Derivative Market.

Coefficients						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.058	.071		56.875	.000
	Type of Investor	-.081	.027	-.133	-2.991	.003
a. Dependent Variable: Level of satisfaction in Index Derivative Market						

The Coefficients table provides necessary information to predict level of satisfaction in Index Derivative Market from Type of Investor, as well as determine whether Type of Investor contributes statistically significantly to the model (by looking at the "Sig." column).

Regression equation:
Level of satisfaction in Index Derivative Market = 4.058 - 0.081 (Type of Investor)

IV. DISCUSSION OF RESULTS

The study on investors' perceptions of investing in the derivatives market emphasises how crucial it is to comprehend investors' actions and choices in this market. It has been discovered that important issues for investors when investing in derivatives include a lack of comprehension, a sense of risk, and numerous factors impacting decision-making. The study also shows that investor perceptions have a big impact on the sustainability and growth of the derivatives market. Negative impressions or a lack of understanding may cause investor involvement to decline, trading volumes to decline, and market liquidity to possibly decline. On the other hand, additional activities for education and awareness could help investors understand the market better and possibly enhance participation, resulting in a market that is more alive and sustainable. The investors preference reason in

derivative investments is depends upon the investment objective such as Risk, Return, Safety and liquidity of the investment. Most of the investors enter into the Forward Contract investments is Return, Future Contract investments is Risk and Safety, Option Contract Investment is Future Needs and Investments in Swaps is Future Needs.

Now a days the investors know about the derivative market, so they are aware as derivative market offers more return, with the concept of hedging of interest rate risk and exchange rate risk with maximum profits and minimum loss investors such as professionals ha very high perceived interest in market. 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.

The study observe 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.

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