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ANALYSING INVESTOR PERSPECTIVES ON FINANCIAL DERIVATIVES IN THE INDIAN MARKET: A LOCALIZED STUDY IN BANGALORE

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Abstract: **To gain insight into perceptions, participation barriers, and market risks, the research paper "Analysing Investor Perspectives on Financial Derivatives in the Indian Market: A Localised Study in Bangalore" examines investor perceptions of financial derivatives. The study investigates factors influencing traders and non-traders in the Indian market using a thorough methodology involving primary and secondary data sources, including structured surveys and secondary data analysis. Based on an analysis of 100 participants using both descriptive and inferential statistics, the paper provides insights into the attitudes and behaviours of investors, with a focus on Bangalore. The research advances knowledge of financial derivatives in the Indian context by assisting in investor decision-making and fostering stability.**

Keywords: **Financial derivatives, Investor perspectives, Participation barriers**

I. BACKGROUND

Derivatives are essential to risk management, speculation, and portfolio diversification in today's financial market. Due to changing regulations and heightened investor participation, their usage has increased in India, where exchanges transact over Rs. 20,000,000 crores annually. But a lot of individual investors have never dealt with derivatives before, usually because of false beliefs and misconceptions that paint them as difficult and dangerous. To overcome this, focused investor education initiatives are necessary to debunk misconceptions, advance comprehension, and provide investors the power to make wise choices. Reducing this knowledge gap can improve the Indian capital market's resilience, liquidity, efficiency, and participation.

1.1 Introduction

For centuries, derivatives have been a cornerstone of modern finance, financial instruments whose value is based on an underlying asset. They include stocks, foreign exchange, commodities, and interest rates from derivatives' inception. Derivative contracts provide market participants with various tools and strategies ranging from pure speculation to portfolio diversification and the ability to hedge future movements in assets prices. The investment decision aims to acquire a required rate of return with minimum risk. In this context, several instruments, practices, and strategies have been formulated and made more significant in the recent past. As the boundaries for international trade and business have opened, world trade has taken a momentum in the last decade. The world has entered a new phase of global integration and liberalisation. The world-wide assumption of capital markets has increased the financial risk arising out of the frequent changes in the interest rates, currency exchange rate, and stock prices. To address the risk associated with these volatile variables and the increasing interdependence of the capital markets across nations, risk management techniques have also evolved through the development of instruments that reduce risk. Financial derivatives are these new, widely used instruments that not only lower financial risk but also present new opportunities for high-risk investors.

II. REVIEW OF LITERATURE

• Bhatt, B. K., & Chauhan, M. A. A. (2014). THE STUDY OF INVESTOR'S PERCEPTION TOWARDS DERIVATIVES AS AN INVESTMENT AVENUE. Kadakia International Journal of Research in Multidiscipline, 1(3), 127-137 Through India's equity derivatives market exceeding traditional equity turnover, this study examines how investors see derivatives as essential tools for risk management. Retail investors' insights shed light on elements that influence investment decisions, such as risk management, hedging tactics, and market volatility. To optimise derivative benefits and handle complexity in the Indian market, one must comprehend these dynamics.

• Selvaraj, N. (2021). Traders Perception and Awareness on

Financial Derivatives in Indian Stock Market. International Journal of Business Management and Finance Research, 4(1), 19-31.
India started implementing structural reforms with the 1991 Economic Policy. Particularly when it comes to derivatives, traders give priority to minimising risk and maximising profits. In times of market volatility, derivatives present chances to increase returns and control risks. Despite the Reserve Bank of India's efforts, the public still has little knowledge about derivatives. This research seeks to bridge the knowledge gap between the advantages of derivatives and the necessary skills for their successful use in the Indian market by evaluating public awareness and making recommendations for improving adoption and awareness by brokerage firms and regulators.
• Ganai, K. A., Chisti, K. A., Malik, I. A., & Showkat, N. (2023). A Systematic Review of Empirical Literature with Reference to Financial Derivatives. Education Quarterly Reviews, 6(1).
The study emphasises on how the market volatility of the 1970s led to the emergence of financial derivatives, such as forwards, futures, and options. Derivatives, which were originally motivated by changes in interest rates and exchange rates, became essential for risk transfer. They overtook commodity futures by the middle of the 1980s and accounted for two thirds of derivative transactions. Equity derivatives became very popular all over the world. These developments highlight the role that derivatives play in risk management and market stability, as well as the necessity of future innovation and adaptation to keep up with changing consumer demands.
• Veena, K. P., & Mahadeva Murthy, C. (2015). Investor perceptions towards trading in equity derivative market: A study at Angel Broking Pvt Ltd, Mysore city. *Global Journal for Research Analysis, 4*(Issue no 2277-8160), Volume 4.
This study investigates how risk-averse investors looking for protection against volatile asset prices drive the use of derivatives, which are essential for risk management. It highlights systemic risks that have an impact on the larger financial
market as it looks at the traits, motivations, and difficulties faced by investors in equity derivatives.

III. RESEARCH METHADOLOGY:

3.1 Statement of the problem

The study aims to perform a comprehensive analysis of financial derivatives in the Indian market, focusing on investor perceptions, market impact, risk analysis, factors influencing participation, and concerns. Finding out how investors view derivatives, what influences their choices, what risks are involved, why some choose not to participate, and how derivatives affect the market are all things that this study aims to investigate. The purpose of the research is to clarify these uncertainties and provide significant additional knowledge about how financial derivatives work within the Indian financial system.

3.2 Research gap:

This study aims to fill a significant research gap about the factors influencing investor behaviour and the role of financial derivatives in the Indian market. Presently, there is a lack of information specifically about India because most published works focus on international perspectives. By carefully examining investor views, concerns, and decision-making processes regarding financial derivatives in India, this research seeks to close this knowledge gap and offer investors, policymakers, and market practitioners' insightful information. Furthermore, since the dynamics of this area have not yet been thoroughly examined in the literature, the research will provide unique insights that are peculiar to the Bangalore region.

3.3 Research objectives

- To assess the investors' perceptions on financial derivatives
- To identify the factors influencing individuals to refrain from engaging in derivative trading.
- To analyse risk associated with derivatives in the Indian market.

3.4 Scope of the study

This study examines the perspectives of investors on financial derivatives, examining their functions in risk mitigation, conjecture, and market fluctuations. It explores market segmentation, regulatory impact, investor awareness, and international influences. Understanding investor behaviour will help with the creation of specialized financial products and educational programs, according to the study's goals. It aims to encourage the effective and responsible use of derivatives within the financial system by learning more about investors' perceptions of them. The research tackles the complexities surrounding derivative instruments in the Indian market by using a multifaceted approach. In the end, it aims to provide policymakers, market players, and academia with important knowledge, promoting a more knowledgeable and stable derivatives landscape.

3.5 Sources of data

Primary and secondary methods were employed in the collection of data for the study. Whereas secondary data came from reports from a variety of sources, including company websites, online activities, seminars, textbooks, articles, journals, and research papers, primary data came from distributing questionnaires to investors in Bangalore. The research examined 8 million traders and non-traders in the Indian market, with a convenience sample of 100 participants chosen for the study. Investor perceptions were summarised by descriptive statistics, and

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relationships between variables were examined by inferential statistics, especially chi-square tests.

3.6 Limitations of the study

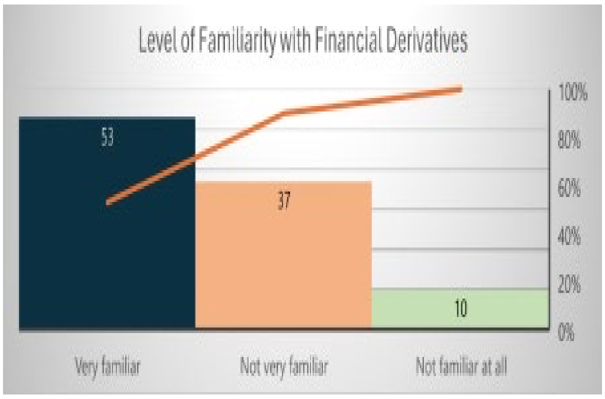
• The study's limited sample representation makes it more difficult to generalise the findings to larger investor populations.
• The responses of survey participants may be influenced by their perspectives, which negatively impact the validity of the findings.
• The opinions of respondents may have an impact on their survey responses, which compromises the validity of the results.
• Uncertainty resulting from unforeseen or external market fluctuations does compromise the stability and reliability of the study's conclusions.

IV. ANALYSIS AND DISCUSSION

Title of the table 4.0.1: Level of familiarity with financial Derivatives

Options	Responses	percentage
Very familiar	53	53%
Not very familiar	37	37%
Not familiar at all	10	10%
Total	100	100%

GRAPH 4.0.1 LEVEL OF FAMILIARITY WITH FINANCIAL DERIVATIVES

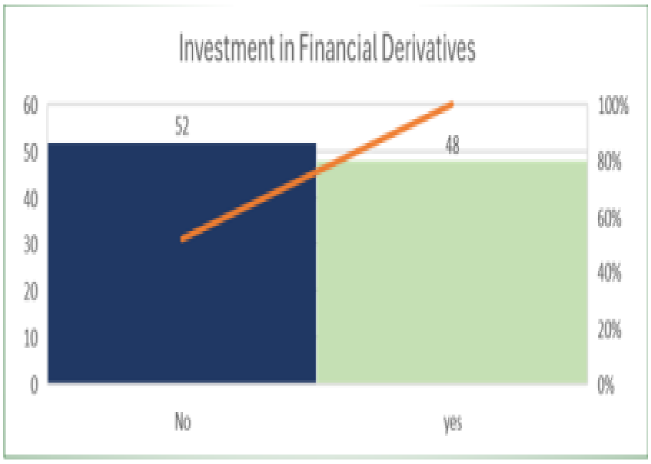


ANALYSIS AND INTEERPRETATION
According to the data, respondents' familiarity with financial derivatives varies: 53% respond they are "very familiar," 37% respond with they are "not very familiar," and 10% respond with they are "not familiar at all." This implies that different comprehension levels may affect how derivatives are perceived and decided. To guarantee that all surveyed population segments make informed decisions, it is imperative that efforts be made to improve education and awareness.

TITLE OF THE TABLE 4.0.2: INVESTMENT IN FINANCIAL DERIVATIVES

Options	Responses	percentage
yes	48	48%
No	52	52%
Total	100	100%

GRAPH 4.0.2: INVESTMENT IN FINANCIAL DERIVATIVES



ANALYSIS AND INTERPRETATION
The nearly equal distribution of respondents' opinions regarding derivative investments reveals a wide range of opinions about these products. Approximately 48% have made investments, demonstrating their confidence in their use for returns or risk management. Complexity or perceived risk are two possible deterrents for the remaining 52%. This emphasises how important it is to launch campaigns to close the knowledge gap and promote greater involvement in the derivatives market.

TITLE OF THE TABLE 4.0.3: BARRIERS TO DERIVATIVE INVESTMENT

Options	Responses	percentage

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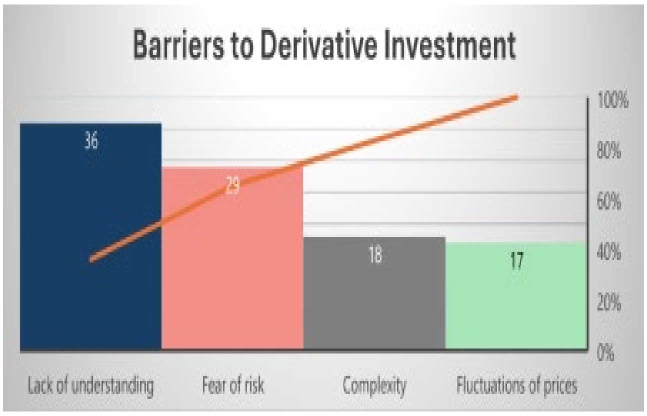
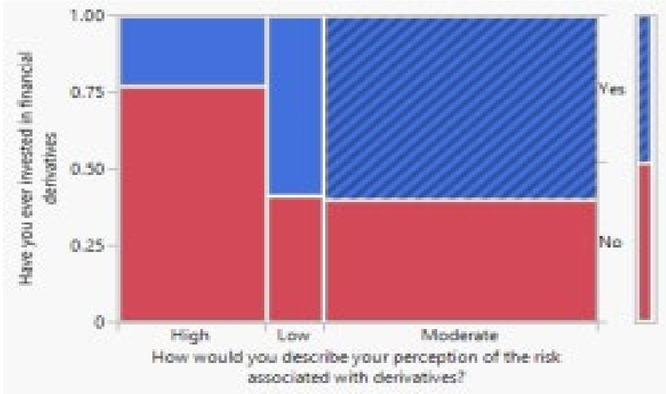
Lack of understanding	36	36%
Fear of risk	29	29%
Complexity	18	18%
Fluctuations of prices	17	17%
Total	100	100%

GRAPH 4.0.3: BARRIERS TO DERIVATIVE INVESTMENT



ANALYSIS AND INTERPRETATION
According to the data, respondents' the highest reasons for not investing in financial derivatives are "fear of risk" (29%) and "lack of understanding" (36%). Furthermore, "Complexity" (18%) and "Price fluctuations" (17%) are mentioned as contributing factors. These results highlight important obstacles to investing in derivatives, such as risk aversion and knowledge gaps. Reducing these worries with risk management techniques and education may make it easier for more people to participate in the derivatives market.

4.1 Hypothesis
Null Hypothesis (H0): There is no significant relationship between investors' perceptions of financial derivatives and their level of involvement in derivative trading.
II. Alternative Hypothesis (H1): There is a significant relationship between investors' perceptions of financial derivatives and their level of involvement in derivative trading.
• The degree of participation in trading derivatives is the Dependent variable. • Perspectives of financial derivatives held by investors are an independent variable. Mosaic plot



Tests

N	DEGREE OF FREEDOM	-LOG LIKE	RSQUARE(U)
100	2	6.0841397	0.0879

TEST	CHI-SQUARE	PROB>CHISQ
LIKELIHOOD	12.168	0.0023*
PEARSON	11.637	0.0030*

Interpretation
The results demonstrate a significant relationship between investors' perceptions of financial derivatives and their involvement in derivative trading, as indicated by the rejection of the null hypothesis. Both the likelihood ratio test ($p = 0.0023$) and Pearson chi-square test ($p = 0.0030$) show strong evidence against the null hypothesis, with p-values less than 0.05. This suggests that investors' attitudes towards the risks and benefits of derivatives significantly influence their willingness to trade them. Understanding and managing these perceptions are crucial for effective investment strategies.

Hypothesis 2:
I. Null Hypothesis (H0): There is no significant influence of various factors, including risk aversion, lack of knowledge, and regulatory concerns, on individuals' decisions to refrain from engaging in derivative trading.
II. Alternative Hypothesis (H1): There is a significant influence of various factors, including risk aversion, lack of knowledge, and regulatory concerns, on individuals' decisions to refrain from engaging in derivative trading.
• Trading derivatives is a Dependent variable.
• Variables including regulatory concerns, knowledge of

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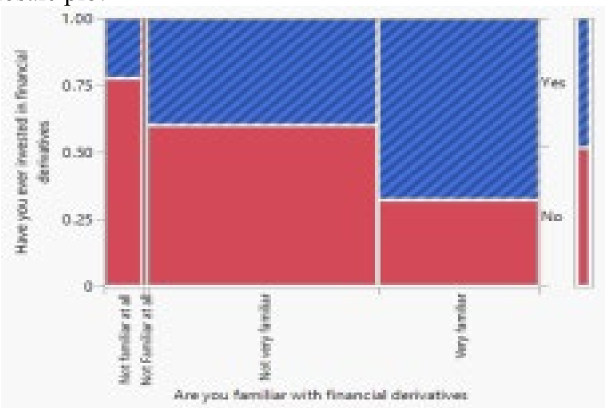
derivatives, and risk aversion are independent variable.
Mosaic plot



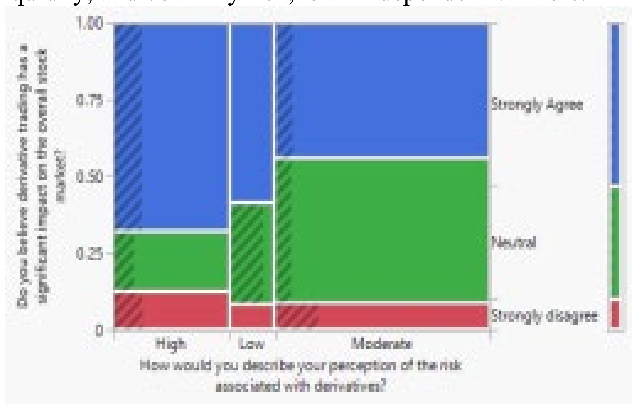
Tests

N	DEGREE OF FREEDOM	-LOG LIKE	RSQUARE(U)
100	3	5.5672022	0.0804

TEST	CHI-SQUARE	PROB>CHISQ
LIKELIHOOD	11.134	0.0110*
PEARSON	10.485	0.0149*

INTERPRETATION
The results indicate a significant relationship between these factors and individuals' decisions, as evidenced by the likelihood ratio test (p = 0.0110) and Pearson chi-square test (p = 0.0149), both yielding p-values less than 0.05. Therefore, we reject the null hypothesis, suggesting that factors such as regulatory concerns, knowledge of derivatives, and risk aversion do have a significant influence on individuals' decisions to refrain from engaging in derivative trading.
This underscores the importance of considering multiple factors in understanding individuals' behaviours in derivative markets and developing effective strategies to address their concerns.

Hypothesis 3
I. Null Hypothesis (H0): There is no significant relationship between the risk associated with derivatives and their prevalence in the Indian market.
II. Alternative Hypothesis (H1): There is a significant relationship between the risk associated with derivatives and their prevalence in the Indian market.
• The proportion of derivatives (trading volume, number of contracts, market share) in the Indian market is dependent variable.
• Risk related to derivatives, such as market, counterparty, liquidity, and volatility risk, is an independent variable.



Tests

N	DEGREE OF FREEDOM	-LOG LIKE	RSQUARE(U)
100	4	3.6392626	0.0389

TEST	CHI-SQUARE	PROB>CHISQ
LIKELIHOOD	7.279	0.1219*
PEARSON	6.923	0.1400*

INTERPRETATION
The analysis aimed to explore the relationship between the risk associated with derivatives and their prevalence in the Indian market. However, the results show no significant evidence of a relationship. Both the likelihood ratio test (p = 0.1219) and Pearson chi-square test (p = 0.1400) yielded p-values greater than 0.05, indicating no clear link between risk and prevalence. Therefore, we fail to reject the null hypothesis, suggesting that the perceived risk associated with derivatives does not significantly impact their prevalence in the Indian market based on the variables examined.

V. CONCLUSION

In conclusion, the research provides valuable insights into investor perceptions and behaviours in the derivatives market, highlighting the factors influencing investment decisions. Despite misconceptions, many retail investors view derivatives as suitable for individual investment, guided by factors such as awareness, guidance, and strategic considerations. Demographic factors like age and income level play significant roles in investors' propensity to engage in derivative trading. Understanding these dynamics, along with factors like hedging funds, risk control, and market volatility, is crucial for stakeholders to enhance investor confidence and optimize investment outcomes.

VI. REFERENCES

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