

Equity or Derivatives? Analyzing Investor Perspectives and Preferences

Mr. Javier Martinez^{*1} & Dr. Lucia Gomez²

^{1&2}Department of Architecture, Polytechnic University of Valencia, Valencia, Spain

ABSTRACT

In India most of the investment avenues are termed to be risky by the investors. The major feature of investment as perceived by the investors is income stability, principal amount, liquidity, easy transferability and approval. There are a number of investment avenues available in India such as share, silver, real estate, gold, Life Insurance, Bank, postal savings, etc. The desired level of Return and the tolerance for risk help in deciding the choice of the investor. The investment may differ from provident fund, national saving certificate, chit funds, insurance schemes, company fixed deposits, government securities, bonds, equity, mutual fund schemes and derivatives. It can be concluded that every investor wants to save extra, be added risk directs to more profit. This is the major reason why the perception of the investor changes when it comes to the investment in equity and derivatives. There is lot confusion in the investment patterns and the investment avenues to be decided between equity and derivatives. The present research study aims to compare the perception of investors towards derivatives and equity.

KEYWORDS: equity, derivatives, investment, risk and saving.

I. INTRODUCTION

The financial market in any country is the backbone of economic scheme. The financial market trends to help in the allotment of share capital in the sectors of an economy (Vashishtha & Kumar, 2010). The allocation of capital helps in keeping a significant environment for investment and savings. The financial system in India is more dynamic than the real system as it tends to react to the changing needs of the economy. There are a number of investment avenues in the financial system of India. There are some investment avenues that tend to provide high returns and there are some that do not tend to provide high returns. In addition to that the risk associated with investment avenues is always fluctuating. Some avenues are very risky while some are not very risky (Acharya & Richardson, 2009). These are the two major factors that affect the perception of the investors with respect to the investment in equity and derivatives. Investment is termed as a perfect investment, when the investment is able to satisfy the needs of the investors. This is the major reason why the starting point of a perfect investment looks through the needs of the investors (Sathya, 2015).

Equity and derivatives are the two investment avenues for people in India when it comes to taking investment decision. Equity refers to the difference between the value of Assets and liabilities. If liabilities are more than assets then equity can also be negative (Allayannis & Weston, 2001). Shareholders equity denotes the equity of a company that is divided among shareholders of preferred stock. The value of capital stock also depends upon the economic prospects of the corporation. On the other hand derivative refers to the security with the price that depends upon the underlying assets (Saravana, 2010). It is also asserted that derivatives derive the value from other sources or assets. The underlying assets from which derivative derive their value are commodities, bonds, currencies, stocks, market indexes and interest rates. The present research study aims to compare the perception of investors with respect to equity and derivatives. The research study would be undertaken by collecting primary data from the investors of Indore.

II. RESEARCH OBJECTIVES

The objectives of present research study are as under:

- To compare and study the factors that affect the choice of investors while selecting equity and derivatives.
- To compare and study the perception of investors towards equity and derivatives.

III. PROBLEM STATEMENT

The significance of a study with respect to the perception of investors for investment avenues does not need an emphasis. The manner in which an investor perceives Investment Avenue and the factors that influence the perception levels of the investors are major problems relating to the investment decision making. The manner in which an investor perceives and mitigates risk in an investment avenue is also a very important aspect in investment decisions. The perception of investors with respect to equity and derivatives of Investment Avenue

is also a significant matter of concern. Along with that different demographic factor like income level, age, gender, experience, occupation and investment patterns also influenced the perception of investors with respect to equity and derivatives. These are the major factors that make it very important to conduct the research study to compare the perception of investors with respect to equity and derivatives.

IV. SCOPE OF THE STUDY

The present study would cover the behaviour of investors towards equity and derivatives in Indore city. It would analyse the demographic factors of the investors and discuss the manner in which the decisions are taken by these investors in Indore city.

Hypothesis of the study

Ho1: there is no significant difference in the investment patterns of the investors between equity and derivatives on the basis of gender.

Ha1: there is a significant difference in the investment pattern of the investor between equity and derivatives on the basis of gender.

V. REVIEW OF LITERATURE

A study was conducted to ascertain the preference of investors and their requirement towards derivative investment that was based on convenience sampling (Bandivadekar & Ghosh, 2003). It was identified that the investors mostly preferred equity schemes while making investment into mutual funds. In addition to that a research study was also conducted to analyse the effect of a number of demographic factors on the attitude of investors towards equity and derivatives. The study revealed that out of 250 respondents, 71 respondents had positive attitude and 117 respondents had neutral attitude while 62 respondents had a negative attitude towards derivatives (Sarangdevot & Rathore, 2014). Study denoted that most of the investor was still confused about derivative and they could not form any attitude or behaviour towards the investment in derivatives. It was also observed that most of the respondents had lack of awareness about various aspects of derivatives (Chawla, 2014).

A research study conducted to identify and evaluate the factors that influence the perception of investors towards investment in the capital market in India on the basis of descriptive study (Sahadevan, 2002). It was identified that occupation is a factor that has the most significant impact on the investment pattern of the investors. This has impact on risk and uncertainty in future and option, cash market and size of investment in future and option. In addition to that age was another factor that had influential role on future and options and cash market (Karthikeyan, 2014). These are the two variables that were found to be very influencing for the behaviour of investors. Investors have huge scope for capital appreciation and current earnings in the emerging market.

To study the investment pattern and level of awareness of the investors a research study was conducted on a sample of 150 respondents. So that a pre test questionnaire was used (Sah & Omkarnath, 2005). It was identified that most of the investor were aware about the investment in equity and its benefits. It further identified that people belonging to the age group 19-55 years were the major individuals taking investment decisions for equity. Along with that the income group was 30,000-70,000 and above (Kathuria & Singhania, 2010). It is also identified that tax benefits and the diversification of portfolio for the major factors that attracted investors towards investment in equity.

Research study also analyse the impact of various demographic factors like gender, age, occupation, education, savings and income to study the attitude of retail investors towards equity and derivatives (Sah & Omkarnath, 2005). It was identified that the investors had positive attitude towards investment in equity and derivatives. It was also identified that most of the investors prefer to invest in equity rather than derivatives (Kumar & Pandey, 2009). Two major reasons associated with this were to get maximum return on minimum risk. Along with that safety was also a significant factor that affected the decision making of the investors. With reference of investors about different investment avenues and the knowledge about risk in investment was also analysed through structured questionnaire (Nelson et al., 2005).

It is identified that the perception of investors has changed due to the number of driving factors for the growth of derivative market. The major driving factor that is driving the growth of derivative market in Indian economy is the improvement in communication facilities (Nath, 2003). Due to the enhanced communication facilities more and more investors are looking forward to invest in derivatives. Along with that the long term investment and savings are also the major factors that have contributed in boosting up the number of investors taking decision to invest in derivative. It is also identified that the volume of derivative contracts has increased

only because of these two factors (Bhatt & Bhatt, 2012). It is also argued that derivatives have enhanced the investor's interest towards taking more risk because of Greater Returns. It is also identified that this is the factor that has also increased entrepreneurship in India (Roztock & Weistroffer, 2004).

The researchers have identified that derivative markets are more standardized and regulated and this is something that provides a controlled environment and it also relates with the fact that high risk results into higher Returns (Kuemmerle, 1999). The investors get motivated because they going to get higher returns by taking higher risk. But also results into earning more profit because of derivatives. This is also significant reason why commodity derivative to play a crucial role in the price risks management of the communities (Reddy & Sebastin, 2008). There are different forms of derivatives that are forward, future, swaps and options that are widely used in India.

VI. RESEARCH METHODOLOGY

The present research study is conducted as a descriptive research study by taking into consideration the literature. It will also be conducted through survey method to collect the information from the investors in Indore city. For doing that a structured questionnaire was prepared using different variables. The researcher has used simple random technique for collecting primary and secondary data.

Sampling

A sample of 200 respondents belonging to Indore city would be taken on random basis for the present research study.

Data analysis tools

A number of statistical and mathematical tools are present but the present research study is based on Chi square. SPSS software is used to run the statistical test.

VII. DATA ANALYSIS

The hypothesis of the present research study was tested using Chi-square test of goodness of fit. Given below is the case processing summary of 200 participants of the study that consists of both males as well as females. The second table represents gender and the investment avenues that they prefer (equity, derivatives or both). The third table denotes chi-square test and the P-value.

Case Processing Summary

	Cases					
	Valid		Missing		Total	
	N	Percent	N	Percent	N	Percent
gender * investment	200	100.0%	0	0.0%	200	100.0%

**Table 1: Case Processing Summary
gender * investment Crosstabulation**

			investment			Total
			equity	derivative	both	
gender	Male	Count	48	32	48	128.0
		Expected Count	48.2	32.6	48.2	371.0
		% within gender	19.7%	12.9%	67.4%	100.0%
	female	Count	21	18	33	72
		Expected Count	21.8	18.4	33.8	72.0
		% within gender	22.3%	12.7%	65.1%	100.0%
Total	Count		69	50	81	200
	Expected Count		69.0	50.0	81.0	200.0
	% within gender		20.8%	12.8%	66.4%	100.0%

**Table 2: Cross tabulation
Chi-Square Tests**

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	.201 ^a	2	.712
Likelihood Ratio	.200	2	.718
Linear-by-Linear Association	.190	1	.442
N of Valid Cases	200		

a. 0 cells (0.0%) have expected count less than 5. The minimum expected count is 37.44.

Table 3: Chi square test

Symmetric Measures

		Value	Approx. Sig.
Nominal by Nominal	Phi	.032	.717
	Cramer's V	.032	.717
N of Valid Cases		200	

a. Not assuming the null hypothesis.

b. Using the asymptotic standard error assuming the null hypothesis.

As per the decision rule to assess if the test is significant or not (for Alpha=.05)

The P value is more than or equal to .05 in this implies that the test is not significant. This further implies that there is no significant difference in the investment patterns between the equity and derivatives between males and females.

Table 4: Symmetric Measures

Factors influencing derivatives selection

Factors	No. of respondents
Complexity	110
Suitable only for big investors	119
Unsafe and risky	132
Low brokerage fees	23
Less speculative	120
Sufficient protection measures	131
Role of SEBI	129

Factors influencing equity selection

Factors	No. of respondents
Easy and traditional	154
Comfort	139
Safe and less risky	168
High brokerage fee	29
More speculative	32
Sufficient protection measures	124
Role of SEBI	147

It is identified from the above table that there are so many factors that influence the selection of equity and derivatives. It is further identified that the reason why investors choose derivatives is that it is less speculative. This is the only and most significant reason behind choosing derivatives. In addition to that the investors also opined that there are sufficient protection measures taken by the regulatory bodies for derivatives. It is also a major reason why investors choose this. SEBI also plays a very important role in derivatives. This makes investors protected. This is also the reason why investors choose derivatives.

It is identified from the above table that there are so many factors that influence the selection of equity. It is further identified that the reason why investors choose equity is that it is easy and traditional. This is the most significant reason behind choosing equity. Investors also choose equity because it is comfortable and anyone can easily invest in it. Another reason behind investing in equity is that it is safe and less risky. In addition to that the investors also opined that there are sufficient protection measures taken by the regulatory bodies for equity. It is also a major reason why investors choose this. SEBI also plays a very important role in equity. This makes investors protected. This is also the reason why investors choose equity.

VIII. CONCLUSION

The analysis suggests that equity is better option for the investors as compared to that of the derivatives. There are a number of favourable factors identified from the study that support that equity is better option than derivatives for taking investment decision. There are various favourable factors that make the investment in equity easier for the investors and due to that the investors prefer to invest in equity. It is also identified that investors found derivatives more risky than equity.

The research has achieved the objectives set in the beginning. It has identified the factors that affect the choice of investors while selecting equity and derivatives as mentioned above. In addition to that the research study has also identified the perception of the investors towards equity and derivatives. It is analysed that there is no difference in the perception of the investors towards equity and derivatives.

IX. REFERENCES

- [1] Acharya, V. & Richardson, M., 2009. Derivatives: The Ultimate Financial Innovation. New York.
- [2] Allayannis, G. & Weston, J., 2001. The use of foreign currency derivatives and firm market value. The review of financial studies .
- [3] Bandivadekar, S. & Ghosh, S., 2003. Derivatives and Volatility on Indian Stock Markets. RBI Occasional Papers, 24(3), pp.12-28.
- [4] Bhatt, K. & Bhatt, K., 2012. Effects of Investor Occupation and Education on Choice of Investment: An Empirical Study in India. International Journal of Management, 29(4).
- [5] Chawla, D., 2014. An Empirical Analysis of Factors Influencing Investment in Mutual Funds in India. Global Business Review, 15(3), pp.493-503.
- [6] Karthikeyan, S., 2014. Investors Perception towards Investment. International Journal of Informative and Futuristic Research, 1(9), pp.55-67.
- [7] Kathuria, L. & Singhanian, K., 2010. Investor Knowledge and Investment Practices of Private Sector Bank Employees. The Indian Journal of Commerce, 63(3), p.79.
- [8] Kuemmerle, W., 1999. The Drivers of Foreign Direct Investment into Research and Development: An Empirical Investigation. Journal of International Business Studies .
- [9] Kumar, B. & Pandey, A., 2009. Role of Indian Commodity Derivatives Market in Hedging Price Risk: Estimation of Constant and Dynamic Hedge Ratio and Hedging Effectiveness. 22 Asralian Finance and Banking Conference 2009.
- [10] Nath, G.C., 2003. Behaviour of stock market volatility after derivatives. NSE Working Paper.
- [11] Nelson, J., Moffitt, J. & Graves, J., 2005. The impact of hedging on the market value of equity. Journal of Corporate Finance.
- [12] Reddy, Y.V. & Sebastin, A., 2008. Interaction between Equity and Derivatives Markets in India: An Entropy Approach. ICFAI Journal of Derivatives markets, 5(1), pp.18-32.
- [13] Roztock, N. & Weistroffer, H.R., 2004. Evaluating information technology investments in emerging economies using activity-based costing. Electronic Journal of Information Systems in Developing countries.
- [14] Sahadevan, K.G., 2002. Derivatives and Risk Management: A Study of Agricultural Commodity Futures in India. Research Project Report, Indian Institute of Management, Lucknow.
- [15] Sah, A.N. & Omkarnath, G., 2005. Causal Relationship between Futures Contracts and Volatility of the Spot Market: A Case of S&P CNX Nifty and Nifty Futures. ICFAI Journal of Derivatives Markets, 2(2), pp.64-71.
- [16] Sarangdevot, S. & Rathore, Y., 2014. Growth & Future of Derivatives in India: A Study. Int'l Journal of Computing, Communications & Instrumentation Engg. (IJCCIE) .
- [17] Saravana, S., 2010. An Analysis of Investor Preference Towards Equity and Derivatives. The Indian Journal of Commerce, 63(3), p.71.
- [18] Sathya, S., 2015. A Comparative Study on Equity, Commodity, Currency Derivatives in India - Evidence from Future Market with special reference to BSE Ltd, Mumbai.