Abstract

Risk is the most predominant and inherent characteristics of stock investment and management of risk has become a great concern for all those who associate with the stock market. However derivatives are the instruments which would help to transfer market risk and provides protection against losses resulting from unforeseen price changes. Derivatives are specialized contracts which are also employed for a variety of purposes including reduction of funding costs by borrowers, enhancing the yield on assets, modifying the payment structure of assets correspond to investors market view etc. In Indian context; derivatives have already underwent several regulations and deregulations for more than four decades. In 1990 the country felt Balance of Payment Crisis and subsequent liberalization and deregulation of various markets triggered the need for strong risk management products. The authorities began to think seriously and SEBI appointed a committee under the chairmanship of L.C Gupta in 1996 to develop appropriate regulatory framework for derivative trading in India. Based on the L.C. Gupta committee recommendations; derivative trading formally commenced in India on June 2000. From the date of inception onwards a remarkable growth was reported for derivative trading in India even though the laws strictly demands that derivatives can be used only for hedging purpose.

In South Kerala; investors (especially LNI’s) hesitated to operate with derivatives as themselves considers derivative investments are highly risky. This conservative attitude was developed as a result of lack of awareness about derivatives; and even the experienced investors were not that much supported from technical and financial levels. Even though a sizeable volume was traded by retail investors with derivatives; in majority of the cases their investment resulted in losses. This clearly signals that the real profit was enjoyed by organized participants like institutional investors and High Net worth Individuals (HNI’s).

In view of the above the research problem entitled “CUSTOMER PREFERENCE TOWARDS FINANCIAL DERIVATIVES WITH REFERENCE TO SOUTH KERALA MARKET” was formulated. This research will address the issue from the dimensions of the growth and development of financial derivatives in India, various demographic and behavioural factors influencing the preference of retail
investors in South Kerala, the present level of support offered by various stakeholders and also develops a suitable model for trading with derivatives. A macro level analysis on the trading volume of financial derivatives for the past twelve years has been analyzed to get a broader outlook on the growth and development of this segment. This research work is arrived out of primary data collected from 1020 retail investors and 200 experts working in stock trading field. Data analysis shows that the major portion of the retail investors came to know about derivatives through broking firms; this indicates that the intermediaries can play a predominant role among retail investors for influencing their investment decision and range of investment. The retail investors in South Kerala are too conservative especially with respect to the fund allocation towards derivatives; and their fund allocation is highly influenced by previous trading experience. Moreover the investors’ are considering derivatives as a speculation tool rather than a risk management tool. This work also will provide a detailed picture of investors attitude towards derivatives, motive and de-motives behind derivative investment, investors opinion on broking firms and intermediaries, their post investment behaviour etc. The opinion of experts’ working in stock trading field was examined to evaluate the effectiveness of support rendered by different stakeholders for derivative trading. Based on the experts opinion; the top level executives expressed some concern with respect to the service offered by staffs working with different firms; and they are not satisfied with the staff level support for derivative trading from the magnitudes of qualification of the staff, quality of service offered etc. This work will also examine the experts preferred strategies for attracting customers towards derivatives, managing customer base, their contract selection mechanism etc. After incorporating possible strategies a business model was developed for trading with derivatives.

*Keywords:* Financial derivatives, Customer preference, Role of intermediaries, Strategic business model for derivative trading.