Time to allow more trading options for domestic investors	
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Counter Point

Time to Allow More Trading Options for Domestic Investors

NARENDRA NATHAN

Indian stock exchanges are proactive and are introducing several strategy indices. However, Sebi is reluctant in allowing trading on most of them. And this is despite the fact that trading has already started on these products in foreign stock exchanges. For example, products based on NSE strategy indices are traded in Taiwan, Hong Kong, Korea and Japan. To increase the depth of Indian capital market, Sebi should allow the introduction of these products here also. After all, there is no purpose in denying this facility to domestic investors.

First step needed is long-duration derivative products on volatility indices. Though Sebi has allowed trading in volatility indices, it is still restricted to just three weekly contracts. That means, investors who want to take a long-term view on volatility are not allowed to do so. Once long-duration contracts are allowed, mutual funds can also launch index funds based on these products and help retail investors to participate in that.

Why investors should bother about volatility, you may ask. We all know that 'change is the only constant thing in life'. Similarly, for stock market investors, 'volatility' is the only thing that is constant. Though increase in volatility can happen due to sudden jump in prices, it usually happens when the market tanks. Since volatility index (also known as fear index) usually have negative correlation with the underlying index, investors use volatility index linked instruments to hedge against volatility. Many investors prefer to bet on implied volatility vis-à-vis realised volatility (ie actual volatility based on historical data).

Second, allow products based on inverse indices. Inverse indices are calculated as if the investor has a short position on that index and its value goes up if the underlying index comes down. Since mutual funds are not allowed take naked short position now, they are also not able to launch products based on them. So Sebi needs to take some pro-active action here. To benefit from short-term corrections in the market, investors have to sell and buy back later.

However, this is a costly proposition because of brokerage and also due to high bid-ask spread in several counters. Selling future is also problematic because investors have to go through bothera-

ANIRBAN BORA

IN INVESTORS' INTEREST

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use volatility index linked instruments to protect their portfolio. In addition to protecting their portfolio, some investors treat volatility itself as an asset class and diversify into it by taking some exposure to volatility index-linked instruments.

Volatility indices are calculated using two methods – expected volatility or actual volatility. The volatility index from NSE (India Vix) is based on expected volatility. Here the investors' perception about future volatility is measured by monitoring the bid – ask prices of Nifty option contracts. The volatility indices from BSE, on the other hand, are based on

tion of rolling over their bearish contracts.

Leveraged indices is the third variety and here, these indices are calculated based on the assumption that you are taking leveraged bets (ie return or loss will be magnified). Since these leveraged bets can be on long or short side, there will be two times normal index or two times inverse index. Since three-times leveraged products are already available in foreign stock and commodity exchanges, there is no reason why Sebi should block 2-times leverage products here.