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MOTIVATING FACTORS FOR CONSUMERS TO PARTICIPATE IN DERIVATIVE MARKET IN HAINAN, CHINA

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ABSTRACT

Derivatives, which are valued using contracts that consider underlying factors, and risk hedging strategies have become more popular as a result of the liberalisation and deregulation of the world's financial markets. The majority of Chinese users of derivatives are hedgers; option traders include hedge funds, speculators, and arbitragers. The acceptance of derivatives and mutual funds has grown as a result of the entry of foreign investment institutions (FIIs) into the capital markets. Essential economic tasks that lessen financial market volatility include price discovery and risk management. The fast growth of China's financial derivatives markets may be attributed to many factors, including the rapid integration of financial markets, the emergence of information technology, and the rising significance of services to the Chinese economy. The purpose of research assessing participants' derivatives knowledge and use was to assess participants' derivatives knowledge and usage. According to the research, smaller investors often lack knowledge regarding derivatives; thus, regulators from the stock exchange, financial industry, and firms that deal in derivatives should work together to increase investor knowledge. Through securitization, market risks in underlying assets may be unbundled and repackaged, and the increasing use of derivatives for proactive corporate risk management has an influence on macroeconomic concerns and monetary policy.

KEYWORDS: Financial Development, Scale, Structure, And Mode of International Trade, Derivatives, Securities, Risk, Economics, Foreign Exchange, Financial Market.

INTRODUCTION

Due in large part to the financial industry's liberalisation and the emergence of several over the counter (OTC) and exchange-traded contracts, the use of derivative financial instruments for company risk management has grown significantly in recent years. Issues with monetary policy and macroeconomics are predicted to be impacted by this expansion. The financial market makes it possible to swap one kind of money for another and makes trading in commodities like gold and other precious metals easier. Financial markets are impacted by supply and demand, which results in the transfer of resources via price mechanisms such as interest rates. While investors may purchase and sell shares of stocks, bonds, and warrants on exchanges and other platforms, derivatives markets oversee the money-making, risk-transfer, and international trade facilitation functions via foreign exchange markets. Capital in the form of common stock shares is provided by the capital market, an institutional architecture that facilitates the borrowing and lending of long-term money inside the monetary system. It also facilitates trading in those shares. Bond markets encourage bond trading, whereas stock markets provide funding in the form of common stock shares. Investors have the option to acquire shares or common stock as a means of raising capital in both kinds of markets (Dr. Murlidhar Panga 2018). Due to the economy's growing globalisation, many businesses are now more susceptible to changes in the value of their own currencies. China's economy has grown significantly, with loans and savings rising to all-time highs. Over the last three decades, the ratio of total financial assets to GDP has climbed significantly, with a major contributing element being the growth in total financial assets. China's export sector, which has grown by 63 times since 1987, is one factor contributing to the country's economic development. Nevertheless, despite the industry's notable triumphs, China's export commerce growth rate has showed notable fluctuations and unfavourable changes in certain years. With a 7.5% rise in exports in 2016, the growth in exports was much larger than in 2015 and 1998. This suggests that China's export products are less competitive as a result of the external economic environment (Matthew 2020).

BACKGROUND OF THE STUDY

Sustainable development of a nation depends on investments such as stocks, bonds, debentures, insurance policies, and mutual fund shares. They increase the economy's competitiveness in the global market in addition to increasing output overall. But even though investing in the financial market would have a big influence on China's economic development, a lot of people there haven't started doing so yet. Retail investors, sometimes referred to as individual investors, put money into the stock market in the hopes of earning returns in the future. When they discuss their opinions about an asset, they are speaking about their own sentiments about it. Investor sentiment is very important in the stock market since it influences their choice of investment options based on their perspective on brokers, the stock market, and other options (Hardt, 2019). China's stock market is the oldest in the world, having been established in 1875 by 22 separate stockbrokers. Since then, the Chinese stock market has grown at previously unheard-of rates, emerging as a formidable competitor on the international scene. The growth of the economy is mostly fueled by the capital market, which includes primary and stock markets. The stock exchange gives investors access to a ready market for trading on a secondary market known as the stock exchange once shares or securities are issued on the main market. Through investing in diverse financial instruments, people may have a positive impact on the economic development of a nation (Feldman, 2013).

Problem Statement

No one has yet satisfactorily addressed the issue of whether or not it is possible for an individual to successfully anticipate financial markets over extended time periods and generate risk-free surplus trading gains over the market rate of return on an investment. It has always been difficult to gauge the stability and volatility of markets, but recent advances in complicated computer technologies have brought us closer than ever before. The Efficient Market Hypothesis holds that it is difficult to predict the future behaviour of prices in financial markets because these values are driven by random causes. They think that the level of noise in the markets is directly tied to the intrinsic volatility of the markets, making it impossible to earn more than the market's rate of return via trading without taking on too much risk. Behavioural economists claim that financial markets are predictable owing to investors making irrational judgements based on their emotions (Ramkumar, 2013). They argue that these trends may be recognised because of short-term market inefficiencies. Traditional financial market forecasting methods include both basic study and technical analysis. Yet questions persist about these strategies' efficacy, and their applicability in the realm of finance. Due to the ever-changing nature of the market, after a signal has been discovered and arbitrated, it may disappear unexpectedly. Research in this sector is impeded by the phenomena of favourable discoveries often being severely underreported to retain competitive advantage. Therefore, in order to ascertain whether or not it is possible to create risk-free surplus gains on markets over relatively lengthy durations, it is essential to perform extensive and open-ended examinations (Kahneman and Tversky, 1979).

Research Objectives

1. To compile a profile of retail traders who are involved in transactions using derivatives.

2. To understand the degree of knowledge and popularity of derivatives among capital market investors.
3. To determine the factors that motivate people to engage in the trading of derivatives.
4. To evaluate the perception of investors about the liquidity, return, and risk of different types of derivatives.
5. To ascertain the association between preference towards derivatives.

LITERATURE REVIEW

Conventional theories of international trade attribute trade flows to natural resources, geography, and technology. But these models do not consider the substantial financial resources when determining comparative advantage. Academics began to think about how growing currency values might affect global trade as they became more informed. Empirical study at the national, industrial, and corporate levels was sparked by Kletzer and Bardhan's (1987) introduction of the concept that credit was a driving force behind the growth of international trade. Stiglitz (2000) has recognised the informational efficiency of security pricing as a significant advancement in economic theory. Formally, the notion that securities prices properly reflect all relevant information is known as the Efficient Market Hypothesis (EMH). The random walk hypothesis is predicated on the notion that fluctuations in a security's price, or its returns, are random and unexpected. Future returns should only represent knowledge that is available in the future and should not be influenced by past, present, or any other kind of return, provided that information is dispersed across investors and over time. The assumption that returns on investments in securities should likewise be unexpected and unpredictable stems from the unpredictability of information. According to this school of thought, a security's price ought to represent a predicted return on investment that accounts for the security's risk. Investors in securities with such prices shouldn't be able to profit from assets that, when taking into consideration their exposure to risk, are anomalous, even if technical and/or fundamental analysis is used. Even if they use technical and/or basic analysis, this remains the case. To sum up, conventional theories of international trade emphasise technology, geographic location, and natural resources; yet they fail to consider the substantial financial resources that are involved in determining comparative advantage. Through an examination of pertinent published literature, researchers may draw comparisons between planned trials and previous testing, accounting for earlier research and contextualising the work that is now underway.

CONCEPTUAL FRAMEWORK

Research Design

Financial market players who trade Geogit securities, JRG security Ltd., and Hedge Equities are included in this study. Two hundred Chinese investors with extensive experience trading Geogit, JRG, or Hedge Equities are selected using a preset series of questions in order to create a sample that is meant to be representative of the whole community. All of these individuals have been chosen because they are typical of the Chinese investment scene. Primary data is analysed using several statistical approaches, such as chi-square analysis, percentages, likert scales, composite index, and many more. Ratios, percentages, correlation, and analysis of variance (ANOVA) are all prominent statistical methods that may be employed in the process of examining secondary data associated to derivative transactions.

RESULT

Test For Hypothesis

Table 1: Level of Income and Derivative Investment

Level of income	Invest in derivative	Not invest in derivative	Total
Below 10,000	108	20	128
Above 10,000	40	32	72
Total	148	52	200

Ho: There is no association between the preference towards derivatives and level of income.

Level of significance: 5%

Degree of freedom: 1

Calculated value: 4.98

Table value: 3.841

Ho ought to be disregarded on the grounds that the computed value of x2 is higher than the value of x2 shown in the table. This seems to indicate that there is a connection between a person's level of income and the number of derivatives they utilise. The amount of the respondent's annual income is a factor in whether or not they choose to invest in derivatives.

CONCLUSION

This research looks at how changes in the financial sector have affected the scale, composition, and dynamics of global trade. It shows that fast expansion in the financial industry may lead to increasing labour and land costs, higher export prices, and lower competitiveness. According to the findings, expanding the reach of the financial system should occur in tandem with economic growth (McKinsey, 2020). Since the exchange rate affects export trade growth, the government's approach to the rate should be fluid and responsive. China's export trade may benefit from a rise in the currency's value. China has to quicken the pace at which its financial reforms, capital market expansion, and direct financing are implemented. Direct financing is motivated by profit maximisation, whereas indirect financing is focused on limiting exposure to loss. China has to set up a multi-tiered financial system since indirect finance accounts for such a tiny share of the country's overall (Hyman, 2020).

LIMITATION OF THE STUDY

Derivatives' leveraged positions enable high-volume trading for low-resource traders for speculative and gambling objectives. Not only are gains compounded, but in the event that a sale falls through, losses are compounded as well. One may mostly attribute the growth of the derivatives market to speculation. Increased personal bankruptcies might result from people taking on more risk than they can afford due to derivatives leverage. In the derivatives market, one default might cause a great deal of harm. Derivatives were designed to reduce market risk, but as their usage has increased, so has this vulnerability. However, much of the technology’s application since then has been hypothetical. This is especially true for the OTC market. Regretfully, not all derivatives mitigate risk and function as planned. In a situation like this, leveraged investments might result in disastrous losses. Amidst allegations that derivatives trading has heightened market volatility, questions have been raised about the stability of the financial system (Hardt, 2019). Derivatives have increased market volatility by expanding slowly, putting both the participants and the stability of the market at risk. Although prices have lately shown symptoms of volatility, derivatives were created to help in the process of determining and stabilising prices. Still, given that these instruments are being utilised for speculation, the market is unstable right now. An additional element contributing to bigger swings is derivatives. Prices may stabilise if derivatives are used appropriately. The basis of the modern economic system is explicit trade. The practise of trade, and hence the use of money, seems advantageous at first glance: when two parties agree to exchange things, everyone benefits. This has been the most prevalent kind of social arrangement for at least the last 10,000 years. Here, the effects of wealth transfer across time are explained via a computer model. It has been a great advantage for us in the past, but as principles like equality and compassion have grown, it is no longer the greatest one. In addition, the ecosystem has suffered greatly as a result (Shafi, (2014).

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