FUTURES

Futures. What is it?

Futures are a financial derivative known as a *forward contract*. A **futures contract** obligates the seller to provide a commodity or other asset to the buyer at an agreed-upon date. Futures are widely traded for commodities such as sugar, coffee, oil and wheat, as well as for financial instruments such as stock market indexes, government bonds and foreign currencies.

The earliest known futures contract is recorded by Aristotle in the story of Thales, an ancient Greek philosopher. Believing that the upcoming olive harvest would be especially bountiful, Thales entered into agreements with the owners of all the olive oil presses in the region. In exchange for a small deposit months ahead of the harvest, Thales obtained the right to lease the presses at market prices during the harvest. As it turned out, Thales was correct about the harvest, demand for oil presses boomed, and he made a great deal of money.

By the 12th century, **futures** contracts had become a staple of European trade fairs. At the time, traveling with large quantities of goods was time-consuming and dangerous. Fair vendors instead traveled with display samples and sold futures for larger quantities to be delivered at a later date. By the 17th century, futures contracts were common enough that widespread speculation in them drove the Dutch Tulip Mania, in which prices for tulip bulbs became exorbitant. Most money changing hands during the mania was, in fact, for futures on tulips, not for tulips themselves. In Japan, the first recorded rice futures date from 17th century Osaka. These futures offered the rice seller some protection from bad weather or acts of war. In the United States, the Chicago Board of Trade opened the first futures market in 1868, with contracts for wheat, pork bellies and copper.

By the early 1970s, trading in **futures and other derivatives** had exploded in volume. The pricing models developed by Fischer Black and Myron Scholes allowed investors and speculators to rapidly price futures and options on futures. To supply the demand for new types of futures, major exchanges expanded or opened across the globe, principally in Chicago, New York and London.

Exchanges play a vital role in **futures trading**. Each futures contract is characterized by a

number of factors, including the nature of the underlying asset, when it must be delivered, the currency of the transaction, at what point the contract stops trading, and the tick size, or minimum legal change in price. By standardizing these factors across a wide range of futures contracts, the exchanges create a large, predictable marketplace.

Futures trading is not without significant risk. Because futures contracts generally entail high levels of leverage, they have been at the heart of many market blowups. Nick Leeson and Barings Bank, Enron and Metallgesellshaft are just a few of the infamous names associated with futures-driven financial disasters. The most famous of all may well be Long Term Capital Management (LTCM); despite having both Fischer Black and Myron Scholes on their payroll, both Nobel Laureates, LTCM managed to lose so much money so rapidly that the Federal Reserve Bank of the United States was forced to intervene and arrange a bailout to prevent a meltdown of the entire financial system.

In the United States, futures transactions are regulated by the Commodity Futures Trading Commission

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Stock Futures

1. What are Stock Futures ?
2. How Stock Futures are priced ?
3. How are Stock Futures different from Stock Options ?
4. What are the opportunities offered by Stock Futures ?
5. How are Stock Futures settled ?
6. Can I square up my position ?
7. When I am required to pay initial margin to my broker ?

8. Do I have to pay mark to market margin ?

9. What are the profits and losses in case of a stock futures position ?

10. What is the market lot for stock futures ?

11. Why are the market lots different for different stocks ?

12. What are the different contract months available for trading ?

13. What is spread trading on BSE ?

14. As an investor, how do I start trading in Stock Futures ?

15. What securities can I submit to the broker as collateral ?

16. How does an investor who has the underlying stock, use stock futures when he anticipates a short-term fall in stock price ?

17. How can an investor benefit from a predicted rise or predicted fall in the price of a stock ?

18. What is pair trading ?

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1. What are Stock Futures ?

Stock Futures are financial contracts where the underlying asset is an individual stock. Stock Future contract is an agreement to buy or sell a specified quantity of underlying equity share for a future date at a price agreed upon between the buyer and seller. The contracts have standardized specifications like market lot, expiry day, and unit of price quotation, tick size and method of settlement.

2. How Stock Futures are priced ?

The theoretical price of a future contract is sum of the current spot price and cost of carry. However, the actual price of futures contract very much depends upon the demand and supply of the underlying stock. Generally, the futures prices are higher than the spot prices of the underlying stocks.

Futures Price = Spot Price + Cost of Carry

Cost of carry is the interest cost of a similar position in cash market and carried to maturity of the futures contract less any dividend expected till the expiry of the contract.

Example:

Spot Price of Stock "A" = 3000, Interest Rate = 12% p.a.

Futures Price of 1 month contract = 3000 + 3000*0.12*30/365

= 3000 + 30

= 3030

3. How are Stock Futures different from Stock Options ?

In stock options, the option buyer has the right and not the obligation, to buy or sell the underlying share. In case of stock futures, both the buyer and seller are obliged to buy/sell the underlying share.

Risk-return profile is symmetric in case of single stock futures whereas in case of stock options payoff is asymmetric.

Also, the price of stock futures is affected mainly by the prices of the underlying stock whereas in case of stock options, volatility of the underlying stock affect the price along with the prices of the underlying stock.

4 What are the opportunities offered by Stock Futures ?

Stock futures offer a variety of usage to the investors. Some of the key usages are mentioned below:

Investors can take long term view on the underlying stock using stock futures.

Stock futures offer high leverage. This means that one can take large position with less capital. For example, paying 20% initial margin one can take positionfor 100 i.e. 5 times the cash outflow.

Futures may look overpriced or under priced compared to the spot and can offer opportunities to arbitrage or earn risk-less profit. Single stock futures offer arbitrage opportunity between stock futures and the underlying cash market. It also provides arbitrage opportunity between synthetic futures (created through options) and single stock futures.

When used efficiently, single-stock futures can be an effective risk management tool. For instance, an investor with position in cash segment can minimize either market risk or price risk of the underlying stock by taking reverse position in an appropriate futures contract.

5 How are Stock Futures settled ?

Presently, Stock futures are settled in cash. The final settlement price is the closing price of the underlying stock.

6. Can I square up my position ?

The investor can square up his position at any time till the expiry. The investor can first buy and then sell stock futures to square up or can first sell and thenbuy stock futures to square up his position. E.g. a long (buy) position in December ACC futures, can be squared up by selling December ACC futures.

7. When I am required to pay initial margin to my broker ?

The initial margin needs to be paid to the broker on an up-front basis before taking the position.

8. Do I have to pay mark to market margin ?

Yes. The outstanding positions in stock futures are marked to market daily. The closing price of the respective futures contract is considered for marking to market. The notional loss / profit arising out of mark to market is paid / received on T+1 basis.

9. What are the profits and losses in case of a stock futures position ?

The profits and losses would depend upon the difference between the price at which the position is opened and the price at which it is closed.Let an investor have a long position of one November Stock "A" Futures @ 430. If the investor square up his position by selling November Stock "A" futures @ 450, the profit would be Rs. 20 per share. In case, the investor squares up his position by selling November Stock "A" futures @ 400, the loss would be Rs. 30 per share.

10. What is the market lot for stock futures ?

For market lot ands other details of the various stock futures available on the exchange, please visit the F&O List Section

11 Why are the market lots different for different stocks ?

According to L C Gupta Committee Report on Derivatives, at the time of introduction of Derivatives Contracts on any underlying the value of the contract should be at least Rs. 2 lakhs. This value of Rs. 2 lakhs is divided by the market price of the individual stock to arrive at the initial 'market lot' for it. It may be mentioned here that the only exception to this rule is the 'mini' contract on the Sensex (both futures and Options).

The market lots are reviewed twice a year and changes are made as per SEBI guidelines to re-align the market lots in cases where the value has increased / decreased drastically from the value at the time of introduction / previous review.

12. What are the different contract months available for trading ?

1, 2 and 3 months contracts are presently available for trading. However, in case of Sensex Options, SEBI has allowed the introduction of Long Dated Options or options with maturities of up to 3 years.

13 What is spread trading on BSE ?

One can trade in spread contracts on the Derivative Segment of BSE. Spreads are the contracts for differential price.This means that in case you want to buy a December contract and sell November contract,you can enter an order for Buy Nov Dec stating the difference you want to pay. This would mean that you are buying a December Contract & selling a November contract.

Similarly, you can enter an order for Sell Nov Dec stating the difference you want to receive. This would mean that you are selling a December Contract & buying a November Contract and receiving the difference.

14. As an investor, how do I start trading in Stock Futures ?

You need to first register yourself as a client with a Registered Broker by fulfilling all the KYC or Know Your Client rules. Then, sign up the client agreement form and risk disclosure document provided to you by your broker.

Deposit upfront the initial margin

Now start trading!!

15. What securities can I submit to the broker as collateral ?

You can pay initial margin in non-cash (bank guarantee, securities) form also. This is

an arrangement between you and your broker, as to which securities he/she is willing to accept. However, the mark-to-market loss incurred on a daily basis has to be settled in cash, only.

16. How does an investor who has the underlying stock, use stock futures when he anticipates a short-term fall in stock price ?

The holder of the physical stock can sell a future to avoid making a loss without having to sell the share. Any loss caused by the fall in the price of the stockis offset by gains made on the stock future position.

17. How can an investor benefit from a predicted rise or predicted fall in the price of a stock ?

An investor can benefit from a predicted rise in the price of a stock by buying futures. As the price of the futures rises, the investor will make a positive return. As the investor will have to pay only the margin (which forms a fraction of the notional value of contract), his return on investment will be higher than on an equivalent purchase of shares.

An investor can benefit from a predicted fall in the price of stock by selling futures. As the price of the future falls in line with the underlying stock, the investor will make a positive return.

18. What is pair trading ?

This trading strategy involves taking a position on the relative performance of two stocks. It is achieved by buying futures on the stock expected to perform well and selling futures on the stock anticipated to perform poorly. The overall gain or loss depends on the relative performance of the two stocks.

Similarly it is possible to take a position in the relative performance of a stock versus a market index. For example traders who would like to take only company specific risk could buy/ sell the relative index future.

What is the difference between Stocks and Futures

In some ways they are similar, but only minutely so. So let's consider some of the major differences between the two.

Most individuals have likely traded stocks at one time or another. Usually, it is to buy in order to 'own' a percentage of a particular company or to liquidate such partial ownership. They pick up a phone to call a broker or go online to purchase or sell. The order is facilitated through an 'exchange', such as the New York Stock Exchange for example.

Buying and selling Futures is similar in this respect. You can call a broker or go online to buy or sell Futures contracts. The order is then facilitated througha commodity exchange, such as the Chicago Merchatile Exchange for example. Yet while buying a stock gives you part ownership in a company or portfolio of companies (as in a fund), buying a Futures contract does not give you ownership of a commodity or product. Rather, you are simply entering into a contract to purchase the underlying commodity at a certain price at a future time, noted by the contract. For example, buying one May Wheat at 3.00 simply creates a contract between you and the seller (whom you need not know as this is taken care of via the exchange) that come May you will take delivery of 5000 bushels of Wheat at $3 per bushel, regardless of what the price of Wheat at market happens to be come May. As a speculator simply trading to make a profit from trading itself and with no interest in actually taking delivery of product, you will simply sell your contract prior to delivery at the going market price and the difference between your buy price and sell price is either your profit or loss.

When you buy a stock, you are part owner of a company. When you buy a **Futures contract**, you simply are **entering a contrac**t. With **stocks**, you will pay for the stock at the time of your purchase plus broker commissions. When buying a **futures contract**, you are simply entering the buy side of a contract and no monies is paid other than commissions to your broker.

Stock exchanges and **commodity exchanges** are both membership organizations established to act as middlemen between the buys and sells of all types of traders, from business entities to the individual small trader. The stock exchange act to bring capital from investors to the businesses that need that capital. They facilitate the transfer of property rights (ownership in the various companies offering stock).The commodity exchange act to bring people willing to assume risk for the opportunity to make a substantial amount of money for taking such risk.

This helps transfer the price risk associated with ownership of various commodities, such as Soybeans, or a service, like interest rates, from producers.

To buy stocks, you only need enough money in your account to purchase the stock outright plus commissions. Once you make the purchase, the money is removed immediately to make the purchase. With trading futures, since you are not actually purchasing anything but simply entering a contract to do so at a later time (which you will exit prior to avoid delivery), the broker will require a certain amount of margin (good faith deposit to cover any possible losses) in what is called a 'margin account'. Each commodity has a different minimum margin requirement depending on several factors. Your broker may use the exchange calculated margin or require a different margin of their own. If the value of the commodity were to decrease and you are on the buy side of the contract, then your contract has lost value and your broker will notify you if your unrealized losses exceeds have gone beyond your minimum margin requirement. This is called a 'margin call'. Naturally you would want to have more capital than simply the margin amount when trading futures to avoid these broker calls. The broker has the right (and likely will) liquidate your position if you are getting too close to not having enough to cover the losses in order to protect themselves.

With buying stocks outright, there is no potential for a margin call. You simply own the stock outright. So perhaps you may be wondering why anyone would bother buying futures contracts rather than stocks. The major answer is: **LEVERAGE.**

Leverage gives the trader the ability to control a large amount of money (or commodity worth a lot of money) with very little money. For example, if Live Cattle futures requires a minimum margin of $800 to trade a single contract, and a single contract represents 40,000 lbs at the current market price of say 75, you would be controlling $30,000 worth for a leverage of over 35:1. This is appealing to many traders and justifies the risk. What is that risk? Just as leverage can work in your favor, it can work against you at the very same ratio. Known as a 'two-edged sword'.

You can increase the leverage of trading stocks if you trade with a margin account. This usually allows you to purchase stocks on margin at the usual rate of 50%. So for every dollar you have you can purchase $2 worth of stock. The leverage is 2:1. How this works is that the broker is actually 'lending' you the other 50%. Of course by purchasing stock with margin you can lose more than you have due to the leverage. And in this case you can end up getting a 'margin call' from your broker if your stock losses too much value. But trading stocks comes no where close to the kind of leverage you get trading Futures.

When you look at these two trading vehicles, the bottom line comes to MARGIN and LEVERAGE.

Future Trading

Trading Stocks & Index Futures in the Indian Stock Market

Futures trading is a business that gives you everything you've ever wanted from a business of your own. Roberts (1991) calls it the world's perfect business. It offers the potential for unlimited earnings and real wealth. You can run it working at your own hours as well as continuing to do whatever you're doing now.

You can operate this business entirely on your own, and can start with very little capital. You won't have any employees, so you wouldn't need attorneys, accountants, or bookkeepers.

What's more, you'd never have collection problems because you won't have any "customers," and since there is no competition, you won't have to pay the high cost of advertising. You also won't need office space, warehousing, or a distribution system. All you need is a personal computer and you can conduct your business from anywhere in the world.... Interested?... read on!

What does Futures Trading apply to Indian Stocks & Indices

Futures Trading is a form of investment which involves speculating on the price of a security going up or down in the future.

A security could be a stock (RIL, TISCO, etc), stock index (NSE Nifty Index), commodity (Gold, Silver, etc), currency, etc.

Unlike other kinds of investments, such as stocks and bonds, when you trade futures, you do not actually buy anything or own anything. You are speculating on the future direction of the price in the security you are trading. This is like a bet on future price direction. The terms "buy" and "sell" merely indicate the direction you expect future prices will take.

If, for instance, you were speculating on the NSE Nifty Index, you would buy a futures contract if you thought the price would be going up in the future. You would sell a futures contract if you thought the price would go down. For every trade, there is always a buyer and a seller. Neither person has to own anything to participate. He must only deposit sufficient capital with a brokerage firm to insure that he will be able to pay the losses if his trades lose money.

What is a Futures Contract?

A futures contract is a standardized contract, traded on a futures exchange, to buy or sell a certain underlying instrument at a certain date in the future, at a specified price. The future date is called the delivery date or final settlement date. The pre-set price is called the futures price.

The price of the underlying asset on the delivery date is called the settlement price.

A futures contract gives the holder the obligation to buy or sell, which differs from an options contract, which gives the holder the right, but not the obligation. In other words, the owner of an options contract may or may not exercise the contract. Whereas in a futures contract, both parties of a "futures contract" must fulfill the contract on the settlement date.

In a futures contract the seller delivers the shares/commodity to the buyer, or, if it is a cash-settled future, as in the case of stock futures in India, cash is transferred from the futures trader who sustained a loss to the one who made a profit. To exit or close your position in an existing futures contract prior to the settlement date, the holder of a futures position has to offset his position by either selling a long position or buying back a short position, effectively closing out the futures position and its contract obligations.

The futures contract is a standardized forward contract, which is an agreement between two parties to buy or sell an asset (which can be of any kind) at a pre-agreed future point in time specified in the futures contract. Some key features of a futures contract are:

Standardization

A futures contract is highly standardized contract with the following details specified:

- The underlying asset or instrument. This could be anything from a barrel of crude oil, a kilo of Gold or a specific stock or share.

- The type of settlement, either cash settlement or physical settlement. Currently in India most stock futures are settled in cash.

- The amount and units of the underlying asset per contract. This can be the weight of a commodity like a kilo of Gold, a fixed number of barrels of oil, units of foreign currency, quantity of shares, etc.

- The currency in which the futures contract is quoted.

- The grade of the deliverable. In the case of bonds, this specifies which bonds can be delivered. In the case of physical commodities, this specifies not only the quality of the underlying goods but also the manner and location of delivery.

- The delivery month.

- The last trading date.

Trading in futures is regulated by the Securities & Exchange Board of India (SEBI). SEBI exists to guard against traders controlling the market in an illegal or unethical manner, and to prevent fraud in the futures market.

How does Futures Trading Work?

There are two basic categories of futures participants: hedgers and speculators.

In general, **hedgers** use futures for protection against adverse future price movements in the underlying cash commodity. The rationale of hedging is based upon the demonstrated tendency of cash prices and futures values to move in tandem.

Hedgers are very often businesses, or individuals, who at one point or another deal in the underlying cash commodity. Take, for instance, a major food processor who cans corn. If corn prices go up. he must pay the farmer or corn dealer more. For protection against higher corn prices, the processor can "hedge" his risk exposure by buying enough corn futures contracts to cover the amount of corn he expects to buy. Since cash and futures prices do tend to move in tandem, the futures position will profit if corn prices rise enough to offset cash corn losses.

Speculators are the second major group of futures players. These participants include independent traders and investors. For speculators, futures have important advantages over other investments:
If the trader's judgment is good. he can make more money in the futures market faster because futures prices tend, on average, to change more quickly than real estate or stock prices, for example. On the other hand, bad trading judgment in futures markets can cause greater losses than might be the case with other investments.
Futures are highly leveraged investments. The trader puts up a small fraction of the value of the underlying contract (usually 10%-25% and sometimes less) as margin, yet he can ride on the full value of the contract as it moves up and down. The money he puts up is not a down payment on the underlying contract, but a performance bond. The actual value of the contract is only exchanged on those rare occasions when delivery takes place. (Compare this to the stock investor who generally has to put up 100% of the value of his stocks.) Moreover the futures investor is not charged interest on the difference between the margin and the

full contract value.

Settling Futures Contracts in India

Futures contracts are usually not settled with physical delivery. The purchase or sale of an offsetting position can be used to settle an existing position, allowing the speculator or hedger to realize profits or losses from the original contract. At this point the margin balance is returned to the holder along with any additional gains, or the margin balance plus profit as a credit toward the holder's loss. Cash settlement is used for contracts like stock or index futures that obviously cannot result in delivery.

The purpose of the delivery option is to insure that the futures price and the cash price of good converge at the expiration date. If this were not true, the good would be available at two different prices at the same time. Traders could then make a risk-free profit by purchasing stocks in the market with the lower price and selling in the futures market with the higher price. That strategy is called arbitrage. It allows some traders to profit from very small differences in price at the time of expiration.

Advantages of Futures Trading in India

There are many inherent advantages of trading futures over other investment alternatives such as savings accounts, stocks, bonds, options, real estate and collectibles.

1. High Leverage. The primary attraction, of course, is the potential for large profits in a short period of time. The reason that futures trading can be so profitable is the high leverage. To 'own' a futures contract an investor only has to put up a small fraction of the value of the contract (usually around 10-20%) as 'margin'. In other words, the investor can trade a much larger amount of the security than if he bought it outright, so if he has predicted the market movement correctly, his profits will be multiplied (ten-fold on a 10% deposit). This is an excellent return compared to buying and taking physical delivery in stocks.

2. Profit in both bull & bear markets. In futures trading, it is as easy to sell (also referred to as going short) as it is to buy (also referred to as going long). By choosing correctly, you can make money whether prices go up or down. Therefore, trading in the futures markets offers the opportunity to profit from any potential economic scenario. Regardless of whether we have inflation or deflation, boom or depression, hurricanes, droughts, famines or freezes, there is always the potential for profit making opportunities.

3. Lower transaction cost. Another advantage of futures trading is much lower relative commissions. Your commission for trading a futures contract is one tenth of a percent (0.10-0.20%). Commissions on individual stocks are typically as much as one percent for

both buying and selling.

4. High liquidity. Most futures markets are very liquid, i.e. there are huge amounts of contracts traded every day. This ensures that market orders can be placed very quickly as there are always buyers and sellers for most contracts.

The Perfect Business

Trading commodity, stock or index futures, or any market you decide, is the absolute perfect business. But you must you learn how to trade correctly and how to control your own fear and greed while preserving your capital.

Futures trading is not like any other conventional business. Here are some major advantages for futures traders:

Low Startup Costs — only your computer
Low Overhead — work from home
No permits or licenses — no regulators
No set hours — trade when you want
No employees — no payroll, no forms, no hassle
No selling — no products or services
No inventory — no stock, inventory, no theft
No advertising — who needs it?
No steep learning curves — use our newsletter services
No worries about market direction — profit short or long anytime
No individual stock shocks — general market sentiment
No interest charges — you put up margin first
Low transaction fees — 0.10% of the contract value
No Real Estate - no tenants
No restrictions on markets to trade
No restrictions on time frames to trade
Inflation and recession proof
Total freedom to make all your own choices without someone looking over your shoulder or second guessing your every move

Once you understand the markets you can make money in up, down and sideways markets. The principles are all the same. Don't make this too hard. It is not rocket science.

You can generate constant cash flow today, with dedication and discipline and following our newsletter services.

Can we guarantee that you will be a successful trader?
We can guarantee that you will have the necessary information to make successful trades.

Futures Education

Getting Started in Futures Trading

By visiting TradingPicks.com Futures Education page, you've taken the first step in learning everything you need to know about futures trading, commodity futures trading and all the little things that will help you make your financial goals a reality. The pages on this site are specially designed to be educational and informative for both the beginner and the advanced trader. TradingPicks.com Futures Education page is your place to lean about everything futures trading.

Trading Facts

When getting started, it's important to know the facts. Knowing the facts about futures trading is crucial for people who work in one of the most adventurous corners of the business world. You are about to embark on a journey where the explorer must rely solely on his common sense and ingenuity, and face challenges that require intelligence, strength, and an adventuresome spirit. There are risks, but futures trading is a journey where the rewards justify the risks.

What is the Futures Market?

Futures markets have been described as continuous auction markets and as clearing houses for the latest information about supply and demand. They are the meeting places of buyers and sellers of an extensive list of commodities. Today, commodities that are sold include agricultural products (grains trading), metals (such as gold and silver), Energies trading (crude and petroleum), financial instruments, foreign currencies, stock indexes and more.

Successful Trading

For futures traders, one of the best suggestions they can take in order to be successful is to follow the trends. Many futures traders trade without a plan. Even if they have a plan, they second guess it and make the mistake of not sticking to it--especially if the trade is a loss. After several profitable trades, using futures trading facts, many speculators become fierce and radical, basing their trades on

hunches, and long shots rather than intelligible reasoning.

Successful futures traders are good businessmen and good money managers. Traders risk their capital, true, but those who are successful follow conservative and disciplined business practices. Money management is as important as being correct in the market.

When considering futures trading, people should not concern themselves with capital needed for daily sustenance. The capital recommended for futures trading is risk capital. Risk capital is money that, if lost, would not materially affect ones living standards. This is a very important concept to understand as you embark on your career in futures trading.

Who Trades?

Today's futures market has also become a major financial market. Participants in futures trading include mortgage bankers, farmers, and bond dealers, as well as grain merchants, food processors, savings and loan associations and individual spectators. Anyone buying or selling futures contracts should clearly understand that the risks of any given transaction may result in a futures trading loss.

While there are a number of steps that can be taken in an effort to limit the number of losses that a futures trader has, there are no guarantees that these steps will prove effective. Well informed futures traders should be familiar with available risk management possibilities. Just as different degrees of probable risk and reward vary, so may different futures contracts. A serious futures trader will want to employ the help of an experienced commodity trading advisor or broker to help them make the most of their opportunities.

Basic Rules for Futures Traders

Follow the trends. This is probably some of the hardest advice for a trader to follow because the personality of the typical futures trader is not "one of the crowd." Futures traders (and futures brokers) are highly individualistic; the markets seem to attract those who are. Very simply, it takes a special kind of person, not "one of the crowd," to earn enough risk capital to get involved in the futures markets. So the typical trader and the typical broker must guard against their natural instincts to be highly individualistic, to buck the trend.

Know why you are in the markets. To relieve boredom? To hit it big? When you can honestly answer this question, you may be on your way to successful futures trading.

Apply money management techniques to your trading.

Do not overtrade.

Take a position only when you know where your profit goal is and where you are going to get out if the market goes against you.

Trade with the trends, rather than trying to pick tops and bottoms.

Don't trade many markets with little capital.

Don't just trade the volatile contracts.

Calculate the risk/reward ratio before putting a trade on, then guard against the risk of holding it too long.

Establish your trading plans before the market opening to eliminate emotional reactions.
Decide on entry points, exit points, and objectives. Subject your decisions to only minor changes during the session. Profits are for those who act, not react. Don't change during the session unless you have a very good reason.

Follow your plan. Once a position is established and stops are selected, do not get out unless the stop is reached, or the fundamental reason for taking the position changes.

Use technical signals (charts) to maintain discipline − the vast majority of traders are not emotionally equipped to stay disciplined without some technical tools. Use discipline to eliminate impulse trading.

Have a disciplined, detailed trading plan for each trade; i.e., entry, objective, exit, with no changes unless hard data changes. Disciplined money management means intelligent trading allocation and risk management. The overall objective is end-of-year bottom line, not each individual trade.

When you have successful a trade, fight the natural tendency to give some of it back.

Use a disciplined trade selection system...an organized, systematic process to eliminate impulse or emotional trading.

Trade with a plan − not with hope, greed, or fear. Plan where you will get in the market, plan how much you will risk on the trade, and plan where you will take your profits.

Cut losses short. Most importantly, cut your losses short, let your profits run. It sounds simple, but it isn't. Let's look at some of the reasons many traders have a hard time "cuttings losses short." First, it's hard for any of us to admit we've made a mistake. Let's say a position starts going against you, and all your "good" reasons for putting the position on are still there. You say to yourself, "it's only a temporary set-back. After all (you reason), the more the position goes against me, the better chance it has to come back − the odds will catch up." Also, the reasons for entering the trade are still there. By now you've lost quite a bit; you sell yourself on giving it "one more day." It's easy to convince yourself because, by this time, you probably aren't thinking very clearly about the position. Besides, you've lost so much already, what's a little more? Panic sets in, and then comes the worst, the most devastating, the most fallacious reasoning of all, when you figure: "That contract doesn't expire for a few more months; things; are bound to turn around in the meantime."

"So it goes; so cut those losses short. In fact, many experienced traders say if a position still goes against you the second day in, get out. Cut those losses fast, before the losing position starts to infect you, before you "fall in love" with it. The easiest way is to inscribe across the front of your brain, "Cut my losses fast." Use stop loss orders, aim for a Rs. 5000 per contract loss limit...or whatever works for you, but do it.

Let profits run. Now to the "letting profits run" side of the equation. This is even harder because who knows when those profits will stop running? Well, of course, no one does, but there are some things to consider. First of all, be aware that there is an urge in all of us to want to win...even if it's only by a narrow margin. Most of us were raised that way. Win − even if it's only by one touchdown, one point, or one run. Following that philosophy almost assures you of losing in the futures markets because the nature of trading futures usually means that there are more losers than winners. The winners are often big, big, big winners, not "one run" winners. Here again, you have to fight human nature. Let's say you've had several losses (like most traders), and now one of your positions is developing into a pretty good winner. The temptation to close it out is universally overwhelming. You're sick about all those losses, and here's a chance to cash in on a pretty good winner. You don't want it to get away. Besides, it gives you a nice warm feeling to close out a winning position and tell yourself (and maybe even your friends) how smart you were (particularly if you're beginning to doubt

yourself because of all those past losers).

That kind of reasoning and emotionalism have no place in futures trading; therefore, the next time you are about to close out a winning position, ask yourself why. If the cold, calculating, sound reasons you used to put on the position are still there, you should strongly consider staying. Of course, you can use trailing stops to protect your profits, but if you are exiting a winning position out of fear...don't; out of greed...don't; out of ego... don't; out of impatience... don't; out of anxiety...don't; out of sound fundamental and/or technical reasoning...do.

"You can avoid the emotionalism, the second guessing, the wondering, the agonizing, if you have a sound trading plan (including price objectives, entry points, exit points, risk-reward ratios, stops, information about historical price levels, seasonal influences, government reports, prices of related markets, chart analysis, etc.) and follow it. Most traders don't want to bother, they like to "wing it." Perhaps they think a plan might take the fun out of it for them. If you're like that and trade futures for the fun of it, fine. If you're trying to make money without a plan − forget it. Trading a sound, smart plan is the answer to cutting your losses short and letting your profits run.

Do not overstay a good market. If you do, you are bound to overstay a bad one also.

Take your lumps. Just be sure they are little lumps. Very successful traders generally have more losing trades than winning trades. It's just that they don't leave any hang-ups about admitting they're wrong, and have the ability to close out losing positions quickly.

Trade all positions in futures on a performance basis. The position must give a profit by the end of the second day after the position is taken, or else get out.

Program your mind to accept many small losses. Program your mind to "sit still" for a few large gains.

Learn to trade from the short side. Most people would rather own something (go long) than owe something (go short). Markets can (and should) also be traded frown the short side.

Watch for divergences in related markets − is one market making a new high and another not following?

Recognize that fear, greed, ignorance, generosity, stupidity, impatience, self-delusion, etc., can cost you a lot more money than the market(s) going against you, and that there is no fundamental method to recognize these factors.

Learn the basics of futures trading. It's amazing how many people simply don't know what they're doing. They're bound to lose, unless they have a strong broker to guide them and keep them out of trouble.

Standing aside is a position. Patience is important.

Client and broker must have rapport. Chemistry between account executive and client is very important; the odds of picking the right Account Executive (AE) the first time are remote. Pick a broker who will protect you from yourself...greed, ego, fear, subconscious desire to lose (actually true with some traders). Ask someone who trades if they know a good futures broker. If you find one who has room for you, give him your account.

Sometimes, when things aren't going well and you're thinking about changing brokerage firms, think about just changing AEs instead. Phone the manager of the local office, let him describe some of the other AEs in the office, and see if any of them seem right enough to have a first meeting with. Don't worry about getting your account executive in trouble; the office certainly would rather have you switch AEs than to lose your business altogether.

Broker/client psychology must be in tune, or else the broker and client should part company early in the program. Client and broker should be in touch repeatedly, so when the time comes, both parties are mentally programmed to take the necessary action without delay.

Most people do not have the time or the experience to trade futures profitably, so choosing a broker is the most important step to profitable futures trading.

When you go stale, get out of the markets for a while. Trading futures is demanding, and can be draining − especially when you're losing. Step back; get away from it all to recharge your batteries.

Thrill seekers usually lose. If you're in futures simply for the thrill of gambling, you'll probably lose because, chances are, the money does not mean as much to you as the excitement. Just knowing this about yourself may cause you to be more prudent, which could improve your trading record. Have a business-like approach to the markets.

Anyone who is inclined to speculate in futures should look at speculation as a business, and treat it as such. Do not regard it as a pure gamble, as so many people do. If speculation is a business, anyone in that business should learn and understand it to the best of his ability.

Approach the markets with a reasonable time goal. When you open an account with a broker, don't just decide on the amount of money, decide on the length of time you should trade. This approach helps you conserve your equity, and helps avoid the Las Vegas approach of "Well, I'll trade till my stake runs out." Experience shows that many who have been at it over a long period of time end up making money.

Don't trade on rumors. If you have, ask yourself this: "Over the long run, have I made money or lost money trading on rumors? O.K. then, stop it.

Beware of all tips and inside information. Wait for the market's action to tell you if the information you've obtained is accurate, then take a position with the developing trend.

Don't trade unless you're well financed...so that market action, not financial condition, dictates your entry and exit from the market. If you don't start with enough money, you may not be able to hang in there if the market temporarily turns against you.

Be more careful if you're extra smart. Smart people very often put on a position a little too early. They see the potential for a price movement before it becomes actual. They become worn out or "tapped out," and aren't around when a big move finally gets under way. They were too busy trading to make money.

Never add to a losing position. Stay out of trouble, your first loss is your smallest loss.

Analyze your losses. Learn from your losses. They're expensive lessons; you paid for them. Most traders don't learn from their mistakes because they don't like to think about them.

Survive! In futures trading, the ones who stay around long enough to be there when those "big moves" come along are often successful.

If you're just getting into the markets, be a small trader for at least a year, then analyze your good trades and your bad ones. You can really learn more from your

bad ones.

Carry a notebook with you, and jot down interesting market information. Write down the market openings, price ranges, your fills, stop orders, and your own personal observations. Re-read your notes from time to time; use them to help analyze your performance.

"Rome was not built in a day," and no real movement of importance ends in one day. A speculator should have enough excess margin in his account to provide staying power so he can participate in big moves.

Take windfall profits (profits that have no sound reasons for occurring).

Periodically redefine the kind of capital you have in the markets. If your personal financial situation changes and the risk capital becomes necessary capital, don't wait for "just one more day" or "one more price tick," get out right away. If you don't, you'll most likely start trading with your heart instead of your head, and then you'll surely lose.

Always use stop orders, always...always... always.

What is Open Interest

Open Interest is the total number of outstanding contracts that are held by market participants at the end of the day.

It can also be defined as the total number of futures contracts or option contracts that have not yet been exercised (squared off), expired, or fulfilled by delivery.

Open interest applies primarily to the futures market. Open interest, or the total number of open contracts on a security, is often used to confirm trends and trend reversals for futures and options contracts.

Open interest measures the flow of money into the futures market. For each seller of a futures contract there must be a buyer of that contract. Thus a seller and a buyer combine to create only one contract.

Therefore, to determine the total open interest for any given market we need only to know the

totals from one side or the other, buyers or sellers, not the sum of both.

The open interest position that is reported each day represents the increase or decrease in the number of contracts for that day, and it is shown as a positive or negative number.

How to calculate Open Interest

Each trade completed on the exchange has an impact upon the level of open interest for that day.

For example, if both parties to the trade are initiating a new position (one new buyer and one new seller), open interest will increase by one contract.

If both traders are closing an existing or old position (one old buyer and one old seller) open interest will decline by one contract.

The third and final possibility is one old trader passing off his position to a new trader (one old buyer sells to one new buyer). In this case the open interest will not change.

Benefits of monitoring open interest

By monitoring the changes in the open interest figures at the end of each trading day, some conclusions about the day's activity can be drawn.

Increasing open interest means that new money is flowing into the marketplace. The result will be that the present trend (up, down or sideways) will continue.

Declining open interest means that the market is liquidating and implies that the prevailing price trend is coming to an end. A knowledge of open interest can prove useful toward the end of major market moves.

A leveling off of open interest following a sustained price advance is often an early warning of the end to an uptrending or bull market.

Open Interest - A confirming indicator

An increase in open interest along with an increase in price is said to confirm an upward trend. Similarly, an increase in open interest along with a decrease in price confirms a downward trend. An increase or decrease in prices while open interest remains flat or declining may indicate a possible trend reversal.

The relationship between the prevailing price trend and open interest can be summarized by the following table.

Price	Open Interest	Interpretation
Rising	Rising	Market is Strong
Rising	Falling	Market is Weakening
Falling	Rising	Market is Weak
Falling	Falling	Market is Strengthening

List of securities permitted for futures and option trading in India

Underlying	Symbol	Market Lot
BANK Nifty	BANKNIFTY	50
CNX IT	CNXIT	50
CNX Nifty Junior	JUNIOR	25
CNX 100	CNX100	50
S&P CNX Nifty	NIFTY	50
3I INFOTECH LTD.	3IINFOTECH	1350
Aban Offshore Ltd.	ABAN	200
ABB Ltd.	ABB	500
Aditya Birla Nuvo Limited	ABIRLANUVO	200
Adlabs Films Ltd	ADLABSFILM	450
AIA Engineering Limited	AIAENG	200
Allahabad Bank	ALBK	2450
Alok Industries Ltd.	ALOKTEXT	3350
Alstom Projects India Ltd	APIL	400
Ambuja Cements Ltd.	AMBUJACEM	2062
Amtek Auto Ltd.	AMTEKAUTO	600
Andhra Bank	ANDHRABANK	2300
Ansal Prop & Infra Ltd	ANSALINFRA	650
APTECH LIMITED	APTECHT	650

Arvind Mills Ltd.	ARVINDMILL	4300
Ashok Leyland Ltd	ASHOKLEY	4775
Associated Cement Co. Ltd.	ACC	375
Aurobindo Pharma Ltd.	AUROPHARMA	350
AXIS Bank Ltd.	AXISBANK	450
Bajaj Auto Ltd.	BAJAJAUTO	100
Bajaj Hindustan Ltd.	BAJAJHIND	1900
Ballarpur Industries Ltd.	BILT	1900
Balrampur Chini Mills Ltd.	BALRAMCHIN	4800
Bank of Baroda	BANKBARODA	1400
Bank of India	BANKINDIA	1900
Bata India Ltd.	BATAINDIA	1050
Bharat Earth Movers Ltd.	BEML	250
Bharat Electronics Ltd.	BEL	275
Bharat Forge Co Ltd	BHARATFORG	1000
Bharat Heavy Electricals Ltd.	BHEL	300
Bharat Petroleum Corporation Ltd.	BPCL	1100
Bharti Airtel Ltd	BHARTIARTL	500
BHUSHAN STEEL & STRIPS LT	BHUSANSTL	250
BIOCON LIMITED.	BIOCON	450
Birla Corporation Ltd	BIRLAJUTE	850
Bombay Dyeing & Mfg. Co Ltd.	BOMDYEING	300
Bombay Rayon Fashions Ltd	BRFL	1150
Bongaigaon Refinery Ltd.	BONGAIREFN	4500
Cairn India Limited	CAIRN	2500
Canara Bank	CANBK	1600
Central Bank of India	CENTRALBK	2000
Century Textiles Ltd	CENTURYTEX	425
CESC Ltd.	CESC	550
Chambal Fertilizers Ltd.	CHAMBLFERT	6900

Chennai Petroleum Corporation Ltd.	CHENNPETRO	1800
Cipla Ltd.	CIPLA	1250
CMC LTD.	CMC	200
Colgate Palmolive (I) Ltd.	COLGATE	1050
Corporation Bank	CORPBANK	1200
Crompton Greaves Ltd.	CROMPGREAV	1000
Cummins India Ltd	CUMMINSIND	950
Dabur India Ltd.	DABUR	2700
Deccan Aviation Limited	AIRDECCAN	1700
Dena Bank	DENABANK	5250
Divi's Laboratories Ltd.	DIVISLAB	310
DLF Limited	DLF	400
Dr. Reddy's Laboratories Ltd.	DRREDDY	400
Educomp Solutions Ltd	EDUCOMP	150
Escorts India Ltd.	ESCORTS	2400
Essar Oil Ltd.	ESSAROIL	5650
Everest Kanto Cylinder Ltd	EKC	1000
Federal Bank Ltd.	FEDERALBNK	1300
Financial Technologies (I) Ltd	FINANTECH	150
GAIL (India) Ltd.	GAIL	750
Gateway Distriparks Ltd.	GDL	2500
Glaxosmithkline Pharma Ltd.	GLAXO	300
GMR Infrastructure Ltd.	GMRINFRA	1000
Grasim Industries Ltd.	GRASIM	88
GTL Ltd.	GTL	1500
Gujarat Alkalies & Chem	GUJALKALI	1400
Gujarat Narmada Fertilizer Co. Ltd.	GNFC	2950
HAVELLS INDIA LIMITED	HAVELLS	400
HCL Technologies Ltd.	HCLTECH	650
HDFC Bank Ltd.	HDFCBANK	200
Hero Honda Motors Ltd.	HEROHONDA	400

Hindalco Industries Ltd.	HINDALCO	1595
Hinduja TMT Ltd.	HINDUJATMT	250
Hindustan Construction Co	HCC	1400
Hindustan Petroleum Corporation Ltd.	HINDPETRO	1300
Hindustan Unilever Ltd	HINDUNILVR	1000
Hotel Leela Ventures Ltd	HOTELEELA	3750
Housing Development and Infrastructure Ltd.	HDIL	400
Housing Development Finance Corporation Ltd.	HDFC	150
HTMT Global Solutions Ltd.	HTMTGLOBAL	250
ICICI Bank Ltd.	ICICIBANK	350
Idea Cellular Ltd.	IDEA	2700
IFCI Ltd.	IFCI	7875
I-FLEX Solutions Ltd.	I-FLEX	150
India Cements Ltd.	INDIACEM	1450
India Infoline Limited	INDIAINFO	500
Indian Bank	INDIANB	2200
Indian Hotels Co. Ltd.	INDHOTEL	1750
Indian Oil Corporation Ltd.	IOC	600
Indian Overseas Bank	IOB	2950
Indian Petrochemicals Corpn. Ltd.	IPCL	1100
Indusind Bank Ltd.	INDUSINDBK	3850
Industrial development bank of India Ltd.	IDBI	2400
Infosys Technologies Ltd.	INFOSYSTCH	100
Infrastructure Development Finance Company Ltd.	IDFC	2950
ITC Ltd.	ITC	2250
IVR Prime Urban Developers Ltd.	IVRPRIME	400

IVRCL Infrastructure & Projects Ltd.	IVRCLINFRA	500
J & K Bank Ltd.	J&KBANK	300
Jaiprakash Associates Ltd.	JPASSOCIAT	300
Jaiprakash Hydro-Power Ltd.	JPHYDRO	6250
Jet Airways (India) Ltd.	JETAIRWAYS	400
Jindal Stainless Ltd.	JSTAINLESS	2000
Jindal Steel & Power Ltd	JINDALSTEL	125
JSW Steel Ltd.	JSWSTEEL	550
Kesoram Industries Ltd	KESORAMIND	500
Kotak Mahindra Bank Ltd.	KOTAKBANK	550
LAKSHMI MACHINES LTD	LAXMIMACH	100
Lanco Infratech Ltd.	LITL	850
Larsen & Toubro Ltd.	LT	200
LIC Housing Finance Ltd	LICHSGFIN	1700
Lupin Ltd.	LUPIN	350
Mahanagar Telephone Nigam Ltd.	MTNL	1600
Maharashtra Seamless Ltd.	MAHSEAMLES	600
Mahindra & Mahindra Ltd.	M&M	312
Mahindra Gesco Developers	GESCOCORP	350
Mangalore Refinery and Petrochemicals Ltd.	MRPL	8900
Maruti Udyog Ltd.	MARUTI	400
Matrix Laboratories Ltd.	MATRIXLABS	1250
Moser-Baer (I) Ltd	MOSERBAER	825
Mphasis Ltd.	MPHASIS	800
Nagarjuna Constrn. Co. Ltd.	NAGARCONST	1000
Nagarjuna Fertiliser & Chemicals Ltd.	NAGARFERT	14000
National Aluminium Co. Ltd.	NATIONALUM	1150
National Thermal Power Corporation Ltd.	NTPC	1625

NDTV Ltd.	NDTV	1100
Neyveli Lignite Corporation Ltd.	NEYVELILIG	5900
Nicolas Piramal India Ltd	NICOLASPIR	1045
NIIT TECHNOLOGIES LTD.	NIITTECH	600
NUCLEUS SOFTWARE EXPORTS	NUCLEUS	550
Oil & Natural Gas Corp. Ltd.	ONGC	225
Omaxe Ltd.	OMAXE	650
Orchid Chemicals Ltd.	ORCHIDCHEM	1050
Oriental Bank of Commerce	ORIENTBANK	1200
Oswal Chem. & Fert. Ltd.	BINDALAGRO	4950
Pantaloon Retail (I) Ltd	PANTALOONR	500
Parsvnath Developers Ltd.	PARSVNATH	700
Patel Engineering Ltd.	PATELENG	500
Patni Computer Syst Ltd	PATNI	650
Peninsula Land Limited	PENINLAND	550
Petronet LNG Limited	PETRONET	4400
Polaris Software Lab Ltd.	POLARIS	1400
Power Finance Corporation Ltd.	PFC	2400
Praj Industries Ltd.	PRAJIND	2200
Punj Lloyd Ltd.	PUNJLLOYD	1500
Punjab National Bank	PNB	600
Puravankara Projects Ltd.	PURVA	500
Rajesh Exports Ltd	RAJESHEXPO	550
Ranbaxy Laboratories Ltd.	RANBAXY	800
Rel. Nat. Resources Ltd.	RNRL	7150
Reliance Capital Ltd	RELCAPITAL	550
Reliance Communications Ltd.	RCOM	700
Reliance Energy Ltd.	REL	550
Reliance Industries Ltd.	RELIANCE	150
Reliance Petroleum Ltd.	RPL	3350

Rolta India Ltd	ROLTA	450
S Kumars Nationwide Ltd	SKUMARSYNF	2600
SASKEN COMMU TECHNO LTD	SASKEN	550
Satyam Computer Services Ltd.	SATYAMCOMP	600
Sesa Goa Ltd.	SESAGOA	150
Shipping Corporation of India Ltd.	SCI	1600
Shree Cements Ltd	SHREECEM	200
Shree Renuka Sugars Ltd.	RENUKA	1000
Siemens Ltd	SIEMENS	188
Sobha Developers Ltd.	SOBHA	350
SRF Ltd.	SRF	1500
State Bank of India	SBIN	250
Steel Authority of India Ltd.	SAIL	2700
Sterling Biotech Ltd	STERLINBIO	1250
Sterlite Industries (I) Ltd	STER	438
Sterlite Optical Technology	STROPTICAL	1050
Strides Arcolab Ltd.	STAR	850
Sun Pharmaceuticals India Ltd.	SUNPHARMA	225
Sun TV Network Ltd.	SUNTV	500
Suzlon Energy Ltd.	SUZLON	200
Syndicate Bank	SYNDIBANK	3800
Tata Chemicals Ltd	TATACHEM	1350
Tata Consultancy Services Ltd	TCS	250
Tata Motors Ltd.	TATAMOTORS	412
Tata Power Co. Ltd.	TATAPOWER	400
Tata Steel Ltd.	TATASTEEL	675
Tata Tea Ltd.	TATATEA	550
Tata Teleserv(Maharastra)	TTML	10450
TECH MAHINDRA LIMITED	TECHM	200

The Great Eastern Shipping Co. Ltd.	GESHIP	1200
The Karnataka Bank Ltd.	KTKBANK	1250
Titan Industries Ltd.	TITAN	206
Triveni Engg. & Inds. Ltd.	TRIVENI	7700
TULIP IT SERVICES LTD	TULIP	250
TVS Motor Company Ltd.	TVSMOTOR	2950
Ultratech Cement Ltd.	ULTRACEMCO	200
Union Bank of India	UNIONBANK	2100
Unitech Ltd	UNITECH	900
United Phosphorous Ltd	UNIPHOS	700
United Spirits Ltd.	MCDOWELL-N	250
Videsh Sanchar Nigam Ltd	VSNL	525
Vijaya Bank	VIJAYABANK	6900
Voltas Ltd.	VOLTAS	3600
WELSPUN GUJ ST. RO. LTD.	WELGUJ	800
Wipro Ltd.	WIPRO	600
Wockhardt Ltd.	WOCKPHARMA	600
YES BANK LIMITED	YESBANK	1100
Zee Entertainment Enterprises Ltd.	ZEEL	700

The above list is as on 01.04.2008

Profit from Short selling the Indian Futures Markets

What differentiates futures traders for most ordinary investors is the fact that most of them are as likely to sell a market as they are to buy it. Unlike many equities strategies that focus only on advancing markets, in futures you can just as easily make money if prices are going up or down.

Have you ever been absolutely sure that a stock was going to decline and wanted to profit from its regrettable demise? Wouldn't it be nice to see your portfolio increase in value during a bear market? Both scenarios are possible. Many investors make money on a decline in an individual stock or during a bear market, thanks to an advanced investing technique called "short selling."

Short selling is neither terribly complex nor entirely simple. In other words, it's a concept that many investors have trouble understanding. In general, people think of investing as buying an asset, holding it while it appreciates in value, and then eventually selling to make a profit. Shorting is the opposite: an investor makes money only when a shorted security falls in value.

Most investors know the adage, "buy low, sell high." But, did you know that in the futures markets, the adage can also be turned around so you "sell high, buy low?" When you sell before a purchase, you are "selling short."

A short sale is made when prices are expected to drop, at which point you could offset the position with a buy, and claim a profit.

Why Short Sell?

There are two main motivations to short sell:

1. To trade
The most obvious reason to short is to profit from an overpriced or downward trending bear market.

2. To hedge
Very few investors short as an active investing strategy. The majority of investors use shorts to hedge. This means they are protecting other long positions with offsetting short positions.

Advantages of Short Selling Stock and Index Futures?

Make money in downtrends and bear markets when prices fall.
It may seem obvious, but what goes up must come down. If you think prices are due for a fall you can sell short to position yourself to gain from that drop.

Take a position with margin.

Futures positions tie up less money than stocks. Whether you're long or short, a position in single-stock futures requires margin equal to a certain % value of the contract's value.

Sell without owning.
In the futures markets, unlike the cash markets, you can sell stocks without actually owning or having them in your demat account. Shorting stock or index in futures have no such restrictions. Going short is just as easy as going long.

Sell at a better price.
Single-stock futures can sometimes be sold at a price higher than the actual stock itself. This happens because most single-stock futures trade at a premium to the stock price, called "basis."

How To Sell Short With Stock and Index Futures

For many investors the question is not whether to go short, but rather, how best to go about it. This is the easy part. When the time comes to position yourself for a downward move, simply place your order to sell. You can go to the market, work a limit order or enter a new position with a sell stop — just as you could with any buy order.

With futures, you're not selling the actual stock or index. Instead, you're entering into an agreement to deliver or close out your position before the contracts expiry date. Most investors simply buy back their short positions before the contracts expire.

And Finally...

Some people mistakenly believe that making profits on a short sale is unpatriotic, unethical or mean-spirited. But remember that for every buyer there is a seller taking the other side of the trade. That's what makes a market — two parties with different opinions about the future direction of the item being sold.

Unless a short sale involves fraud or manipulation, it is a routine valued aspect of liquid markets. After all, short-sellers will eventually be buyers — either to cover their short or to make delivery.

Why limit your opportunities with preconceived notions of what is or is not appropriate? If you think the market is due to rally, then buy. If you're bearish, then sell. And if you decide to take action on your bearish opinion, the short sale can get the job done nicely.

Why Trade NSE Nifty 50 & CNX IT Stock Index Futures

Why Trade NSE Nifty 50 & CNX IT Stock Index Futures?

Because it is difficult for most investors to select and invest only in the top performing stocks, investing in products that track stock indices, which provide exposure to the whole market or a sector of the market rather a few individual stocks has become increasing popular.

The advantage of indexing is available in mutual funds and exchange-traded funds. But, you should consider stock index futures instead for two main reasons:
flexibility and leverage.

Stock index futures have attracted many new traders, and for good reason. These innovative futures contracts can serve you in a number of ways, and be used with a variety of trading strategies and different financial objectives.

As you'll read later, the reasons to trade stock index futures are numerous and compelling. You can use them to take action on your opinion of the market, manage risk and gain exposure to various market sectors efficiently and cheaply.

TOP REASONS TO TRADE STOCK INDEX FUTURES

1. Add flexibility to your investment portfolio.
Stock index futures add flexibility to your portfolio as a hedging and trading instrument.

2. Create the possibility of speculative gains using leverage.
Because a relatively small amount of margin money controls a large amount of capital represented in a stock index contract, a small change in the index level might produce a profitable return on your investment if you're right about the market's direction.

3. Provide hedging or insurance protection for a stock portfolio in a falling market.
Although the stock market climbed steadily in 2003, it later became apparent that there is no guarantee that it will always do so. Even though you don't expect a fire in your house or an accident with your automobile, you buy insurance in case that should happen. You can also get "insurance" for your stock portfolio by using stock index futures to protect against the day a decline might come. And, unlike purchasing options as insurance, there is no time value erosion of the futures position.

4. Maintain your stock portfolio during stock market corrections.
You may not need "insurance" all of the time, but there are certain times when you would like

less exposure to stocks. Yet, you don't want to sell off part of a stock portfolio that has taken you a long time to put together and looks like a sound, long-term investment program.

5. Sell as easily as you can buy.

One of the major advantages of futures markets, in general, is that you can sell contracts as readily as you can buy them and the amount of margin required is the same. Mutual funds do not specialize in bear market approaches by short selling stocks but, and also it is not possible for individuals to short sell stocks in a falling market to make money.

6. Transfer risk quickly and efficiently.

Whether you are speculating, looking for insurance protection (hedging), or temporarily substituting futures for a later cash transaction, most stock index futures trades can be accomplished quickly and efficiently.

Many mutual funds require investors to wait until the end of the day to see at what price they were able to purchase or sell shares. With today's volatility, once-a-day pricing may not give you the maneuverability to take positions at exactly the time you want. Stock index futures give you the opportunity to get into or out of a position whenever you want.

How to Trade Gold Futures in India

The price of gold depends on a host of factors, which makes it very difficult to predict. In a fashion similar to shares, gold is an asset class by itself. In fact, in many villages and small towns of India, gold is preferred to bank deposits as a savings and investment instrument.

Till a year ago, to gain from price volatility, one would have to hoard and trade in gold physically. Not any more, however. With the commodity futures market operating in full swing, one has the option of not physically stocking gold to gain from its price movements.

Let us see how trading in futures is better than the option of hoarding gold. Firstly, there are several costs associated with the process of physically stocking gold. The costs include the cost of the gold itself, the cost of carrying, cost of physical storage, finance cost and last, but not the least, the safety element.

While futures might have some advantages, there is also a danger of losing big as your risks are also magnified and hence, one must tread carefully in this area.

In this context, if the going cost of gold is Rs 6000 per 10 grams, with an investment of Rs 6 lakh, one can buy 1kg of gold. Now, suppose, three months hence, when the going price of gold

is Rs 6,500 per 10 grams, the person decides to sell the gold. The gross profit made by the person is Rs 500 for every 10 grams and hence, for 1 kg, it stands at Rs 50,000. To arrive at the net profit, one would have to deduct the cost of financing; the cost of storage in a bank and transaction costs, including sales taxes.

Now, let's see what the same Rs 6 lakh can achieve in a futures market, assuming the same sequence of prices. In Indian exchanges, currently, futures contracts up to four months are available. Let's assume that three-month gold futures are trading at a little over the spot price, with the market expecting gold prices to remain stable over the next three-month period. Let this price be Rs 6050.

Since a futures contract is an obligation to buy or sell a specific quantity of the commodity, one does not have to pay for the entire value of the commodity. Buying futures obligates one to take delivery of the underlying commodity at a particular date in the future. This is also known as taking a long position.

To trade in gold futures, one has to go to a brokerage house and open a trading account. A trading account involves keeping an initial deposit of Rs 50,000 to Rs 1 lakh. Part of the money accounts for the margin money, which is required by the exchange when one enters trading.

For a high amount, however, the deposit amount is usually waived by the brokerage house. The whole investment is then generally treated as margin money. For commodity futures, there is usually a lot size or the minimum volume of the commodity of which one has to buy a futures contract.

Let's assume, for our case, the minimum lot size is 1 kg (lot sizes are usually 100gm or 1 kg). Thus, if the going futures rate is Rs 6,050 per 10 grams, the minimum value of a contract is Rs 6,05,000. The beauty of a futures contract is that to trade in them, one has to only invest the margin money. If we assume a flat 5% margin rate for the contract (margin rates vary from 5-10%), the margin money for a single lot is Rs 30,250. Add to that, a brokerage amount, which is usually .1% to .25% and some start-up charges. Applying these rates, which are prevalent in the market currently, a single lot of gold futures contract should come at around Rs 32,000.

Thus, with Rs 6 lakh, one can buy 19 lots of gold futures. One can , however, expect 'margin calls' from brokerage houses if the margin money falls short of the margin money required for trading in the exchange, determined at the end of the trading session each day.

Now, suppose that at the end of 3 months, the spot price of gold actually reaches Rs 6,500 per 10 grams.

The novelty of the futures market is that as long as there is sufficient liquidity in the markets,

the futures price always converges to the price of the under lying. Such is the leverage of futures, that with the same investment of Rs 6 lakh, one is actually commanding 19 lots of gold futures or in effect, 19 kgs of gold.

Thus, at the end of three months, assuming the above-mentioned course of events, on an investment of Rs 6 lakh, one can make a gross profit that is almost 17 times the profit made by physically stocking gold.

At the same time, the downside risk is also multiplied. To avoid the hassles of delivery, one must offset the futures contract just before the maturity date is reached. Delivery would entail gold certification and accreditation by an exchange-appointed assayer and increased transaction costs in general, as various taxes come into the reckoning.

The above example is about a case of taking a bullish view on the price of gold and hence, gaining from the price rise by buying futures. One can gain from a futures market even by having a bearish view on the price of gold. This aspect of gain is absent in the physical market for gold. If one believes that the spot price of gold is going to fall in the near future, all he needs to do is to sell gold futures.

While all this seems pretty rosy, there are some things to be kept in mind. Firstly, any transaction in the futures market is possible only if a counter-party to the buy or sell order that is placed, exists. For unusually large investments, the exchange may find it difficult to find a counter-party and so it may take some time to match it. Also, with any futures, there may be a problem in exiting from a position by buying or selling when one would like to.

Trading in Futures Derivatives (F&O)

Idea about futures derivatives

Future trading can be done on stocks as well as on Indices like IT index, Auto index, Pharma index etc

Stock future trading -
Let's first understand what the meaning of futures trading is. In simple language one future contract is group of stocks (one lot) which has to be bought with certain expiry period and has to be sold (squared off) within that expiry period.
Suppose if you buy futures of Wipro of one month expiry then you have to sell it within that one month period.
Important - Future contract get expires at every last Thursday of every month.

If you buy October month expiry future contract then you have to sell it within last Thursday

of October month. Likewise you can buy two months and three months expiry period future contract.
You can buy maximum of three month expiry period.
For example - suppose this is month of October then you have to buy till maximum month of December expiry and you have to sell it within last Thursday of December month. You can sell anytime between these periods.
Lot size (group of stocks in one future contract) varies from future to future contract.
For example Reliance Industries future lot size has 150 quantities of shares while a Tata Consultancy service has 250 shares.
In the same manner all futures have different lot sizes decided by SEBI (Securities Exchange Board of India).
The margin (in other words price of one lot size) varies on daily basis based on its stocks closing price.
Future trading can be done on selected stocks listed under Nifty and Jr. Nifty and not on all stocks.
The price of future contract is determined by its underlying stock.
Important - You can't buy future contract of expiry period of not more than 3 months.

Indices future trading

As you can do future trading on stocks likewise you can do trading on different indices like Nifty index, IT index, Auto index, Pharma index etc.

Successful trading in futures

Future or derivative trading is the process of buying or selling stock future or index future for a certain period of time and squaring off before the expiry date.
Expiry period can be of one month, two month and three month and not more then of three month.
Its not compulsion that you have to square off your positions on the expiry date or wait till the expiry period but in fact you can square off at any time even, at the same day, or you can hold as long as you want but remember to square off before expiry date.
Most of the times on 3rd month expiry future you may see very less trading volumes.
Generally most of the traders/investors trade or invest on current month future or second month future contract and you may see very low volumes on last month means third month expiry .
But on Nifty index contract or on other index contract you may see good trading volumes even on 3rd month expiry future also.
You can also buy and sell or sell and buy future contract on the same day of any expiry month.
This is called as day trading or intraday in futures.
Selling future contract before buying is called short selling. Short selling is allowed in futures trading.

Major Advantages of Futures Trading over Stock Trading

1) Margin is available -

In future trading you get margin to buy (but can hold only up to maximum of 3 months), while in stock trading you must have that much of amount in your account to buy.

For example - If you plan to buy stock XYZ at Rs. 100 and quantity 1000 shares then you have to pay 1 lakh rupees (RS 100 x1000 qty). But if you plan to buy XYZ future contract and that contract lot size has 1000 quantity of shares then instead of paying 1 lakh rupees you have to pay just 20% to 30% of whole amount which comes to 20 thousand to 30 thousand rupees.

In short in future trading you have to pay just 20% to 30% of the whole amount what you pay if you buy stock of that price. But limitation for this is your expiry period. Means if you bought future of one month expiry then you have to square off within that one month likewise you can buy maximum of three months expiry.

2) Possible to do short selling -

You can short sell futures- You can sell futures without buying them which is called short selling and later buy within your expiry period, to cover up your positions.

This is not possible in stocks. You can't sell stocks before buying them in delivery (you can do in intraday). You can short sell futures and can cover off within your expiry period.

For example - If expiry period of your future contract is of 1 month then you have time frame of one month to cover off your order like wise if your future expiry period is of two months then you have time frame of two months and this continues till three months and not more then three months.

In short selling of futures also you get margin as you get in buying of futures.

3) Brokerages are low -

Brokerages offered for future trading are less as compared to stock delivery trading.

Disadvantages of Future Trading over Stock Trading

1) Limitation on holding -

If you buy or sell a future contract then you have limitation of time frame to square off your position before expiry date.

For example - If you buy or sell future contract of one month expiry period then you have to square off your position before your expiry date of that month, so in this example you got one month period. So

likewise if you go for two month expiry period then you get 2 months and if you go for three month expiry then you will get 3 month expiry period to square off your position.

2) Level of Risk -

Due to margin facility in future trading you may earn huge profit by investing fewer amounts but at the contrary side if your trade goes wrong then you may have to suffer huge loss.

3) Limitation on stocks -

You can't do future trading on all stocks. You can only do on listed stocks on Nifty and Jr. Nifty.

Important points to Remember while doing future trading

1) First up all you have to decide whether you want to buy stock derivatives or index derivative. After this you have to select the expiry period. Once you buy certain expiry period then you have to sell (cover off) your order before that period.
Its no need to wait till the expiry period, you can even square off on the same day (if you are getting profit) or anytime whenever you feel to book profit, no compulsion to cover off your order on the last day of expiry.
2) Check out for Futures current market price.
3) Futures Lot Size (number of shares in that particular Lot).
4) Futures Lot price (this is the amount you must have in your account to buy one lot of future) also called as margin amount.
5) Selection of expiry period - you want to trade on expiry of one month, two month or last 3rd month.
6) No need to wait till expiry period can book profit wherever applicable.

Method of Short Selling

Short selling (selling before buying in future trading)
In future trading you can do short selling and buy (cover) later when price comes down from your selling price you can short sell stock future as well as index future. But again same restriction will apply and that is of expiry period.

Trading Stocks & Index Futures in the Indian Stock Market

Futures trading is a business that gives you everything you've ever wanted from a business of

your own. Roberts (1991) calls it the world's perfect business. It offers the potential for unlimited earnings and real wealth. You can run it working at your own hours as well as continuing to do whatever you're doing now.

You can operate this business entirely on your own, and can start with very little capital. You won't have any employees, so you wouldn't need attorneys, accountants, or bookkeepers.

What's more, you'd never have collection problems because you won't have any "customers," and since there is no competition, you won't have to pay the high cost of advertising. You also won't need office space, warehousing, or a distribution system. All you need is a personal computer and you can conduct your business from anywhere in the world.... Interested?... read on!

What does Futures Trading apply to Indian Stocks & Indices

Futures Trading is a form of investment which involves speculating on the price of a security going up or down in the future.

A security could be a stock (RIL, TISCO, etc), stock index (NSE Nifty Index), commodity (Gold, Silver, etc), currency, etc.

Unlike other kinds of investments, such as stocks and bonds, when you trade futures, you do not actually buy anything or own anything. You are speculating on the future direction of the price in the security you are trading. This is like a bet on future price direction. The terms "buy" and "sell" merely indicate the direction you expect future prices will take.

If, for instance, you were speculating on the NSE Nifty Index, you would buy a futures contract if you thought the price would be going up in the future. You would sell a futures contract if you thought the price would go down. For every trade, there is always a buyer and a seller. Neither person has to own anything to participate. He must only deposit sufficient capital with a brokerage firm to insure that he will be able to pay the losses if his trades lose money.

What is a Futures Contract?

A futures contract is a standardized contract, traded on a futures exchange, to buy or sell a certain underlying instrument at a certain date in the future, at a specified price. The future date is called the delivery date or final settlement date. The pre-set price is called the futures price. The price of the underlying asset on the delivery date is called the settlement price.

A futures contract gives the holder the obligation to buy or sell, which differs from an options contract, which gives the holder the right, but not the obligation. In other words, the owner of an options contract may or may not exercise the contract. Whereas in a futures

contract, both parties of a "futures contract" must fulfill the contract on the settlement date.

In a futures contract the seller delivers the shares/commodity to the buyer, or, if it is a cash-settled future, as in the case of stock futures in India, cash is transferred from the futures trader who sustained a loss to the one who made a profit. To exit or close your position in an existing futures contract prior to the settlement date, the holder of a futures position has to offset his position by either selling a long position or buying back a short position, effectively closing out the futures position and its contract obligations.

The futures contract is a standardized forward contract, which is an agreement between two parties to buy or sell an asset (which can be of any kind) at a pre-agreed future point in time specified in the futures contract. Some key features of a futures contract are:

Standardization

A futures contract is highly standardized contract with the following details specified:

· The underlying asset or instrument. This could be anything from a barrel of crude oil, a kilo of Gold or a specific stock or share.

· The type of settlement, either cash settlement or physical settlement. Currently in India most stock futures are settled in cash.

· The amount and units of the underlying asset per contract. This can be the weight of a commodity like a kilo of Gold, a fixed number of barrels of oil, units of foreign currency, quantity of shares, etc.

· The currency in which the futures contract is quoted.

· The grade of the deliverable. In the case of bonds, this specifies which bonds can be delivered. In the case of physical commodities, this specifies not only the quality of the underlying goods but also the manner and location of delivery.

· The delivery month.

- The last trading date.

Trading in futures is regulated by the Securities & Exchange Board of India (SEBI). SEBI exists to guard against traders controlling the market in an illegal or unethical manner, and to prevent fraud in the futures market.

How does Futures Trading Work?

There are two basic categories of futures participants: hedgers and speculators.

In general, **hedgers** use futures for protection against adverse future price movements in the underlying cash commodity. The rationale of hedging is based upon the demonstrated tendency of cash prices and futures values to move in tandem.

Hedgers are very often businesses, or individuals, who at one point or another deal in the underlying cash commodity. Take, for instance, a major food processor who cans corn. If corn prices go up. he must pay the farmer or corn dealer more. For protection against higher corn prices, the processor can "hedge" his risk exposure by buying enough corn futures contracts to cover the amount of corn he expects to buy. Since cash and futures prices do tend to move in tandem, the futures position will profit if corn prices rise enough to offset cash corn losses.

Speculators are the second major group of futures players. These participants include independent traders and investors. For speculators, futures have important advantages over other investments:

If the trader's judgment is good. he can make more money in the futures market faster because futures prices tend, on average, to change more quickly than real estate or stock prices, for example. On the other hand, bad trading judgment in futures markets can cause greater losses than might be the case with other investments.

Futures are highly leveraged investments. The trader puts up a small fraction of the value of the underlying contract (usually 10%-25% and sometimes less) as margin, yet he can ride on the full value of the contract as it moves up and down. The money he puts up is not a down payment on the underlying contract, but a performance bond. The actual value of the contract is only exchanged on those rare occasions when delivery takes place. (Compare this to the stock investor who generally has to put up 100% of the value of his stocks.) Moreover the futures investor is not charged interest on the difference between the margin and the full contract value.

Settling Futures Contracts in India

Futures contracts are usually not settled with physical delivery. The purchase or sale of an offsetting position can be used to settle an existing position, allowing the speculator or hedger to realize profits or losses from the original contract. At this point the margin balance is returned to the holder along with any additional gains, or the margin balance plus profit as a credit toward the holder's loss. Cash settlement is used for contracts like stock or index futures that obviously cannot result in delivery.

The purpose of the delivery option is to insure that the futures price and the cash price of good converge at the expiration date. If this were not true, the good would be available at two different prices at the same time. Traders could then make a risk-free profit by purchasing stocks in the market with the lower price and selling in the futures market with the higher price. That strategy is called arbitrage. It allows some traders to profit from very small differences in price at the time of expiration.

Advantages of Futures Trading in India

There are many inherent advantages of trading futures over other investment alternatives such as savings accounts, stocks, bonds, options, real estate and collectibles.

1. High Leverage. The primary attraction, of course, is the potential for large profits in a short period of time. The reason that futures trading can be so profitable is the high leverage. To 'own' a futures contract an investor only has to put up a small fraction of the value of the contract (usually around 10-20%) as 'margin'. In other words, the investor can trade a much larger amount of the security than if he bought it outright, so if he has predicted the market movement correctly, his profits will be multiplied (ten-fold on a 10% deposit). This is an excellent return compared to buying and taking physical delivery in stocks.

2. Profit in both bull & bear markets. In futures trading, it is as easy to sell (also referred to as going short) as it is to buy (also referred to as going long). By choosing correctly, you can make money whether prices go up or down. Therefore, trading in the futures markets offers the opportunity to profit from any potential economic scenario. Regardless of whether we have inflation or deflation, boom or depression, hurricanes, droughts, famines or freezes, there is always the potential for profit making opportunities.

3. Lower transaction cost. Another advantage of futures trading is much lower relative commissions. Your commission for trading a futures contract is one tenth of a percent (0.10-0.20%). Commissions on individual stocks are typically as much as one percent for both buying and selling.

4. High liquidity. Most futures markets are very liquid, i.e. there are huge amounts of contracts traded every day. This ensures that market orders can be placed very quickly as there are always buyers and sellers for most contracts.

Why Trade in Future Markets

The Perfect Business

Trading commodity, stock or index futures, or any market you decide, is the absolute perfect business. But you must you learn how to trade correctly and how to control your own fear and greed while preserving your capital.

Futures trading is not like any other conventional business. Here are some major advantages for futures traders:

Low Startup Costs — only your computer
Low Overhead — work from home
No permits or licenses — no regulators
No set hours — trade when you want
No employees — no payroll, no forms, no hassle
No selling — no products or services
No inventory — no stock, inventory, no theft
No advertising — who needs it?
No steep learning curves — use our newsletter services
No worries about market direction — profit short or long anytime
No individual stock shocks — general market sentiment
No interest charges — you put up margin first
Low transaction fees — 0.10% of the contract value
No Real Estate - no tenants
No restrictions on markets to trade
No restrictions on time frames to trade
Inflation and recession proof
Total freedom to make all your own choices without someone looking over your shoulder or second guessing your every move

Once you understand the markets you can make money in up, down and sideways markets. The principles are all the same. Don't make this too hard. It is not rocket science.

You can generate constant cash flow today, with dedication and discipline and following our newsletter services.

Can we guarantee that you will be a successful trader?
We can guarantee that you will have the necessary information to make successful trades.

Calculations

1. What are the profits and losses in case of a futures position ?
2. What happens to the profit or loss due to daily settlement ?
3. How does the Initial Margin affect the above profit or loss ?
4. What is a spread position ?
5. How are spread rates calculated ? Please illustrate with an example.
6. How do we calculate spreads in case of two way quotations ?
7. Please give a simple illustration to explain the mechanics of spread trading ?

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1 What are the profits and losses in case of a futures position ?

The profits and losses would depend upon the difference between the price at which the position is opened and the price at which it is closed. Let us take some examples.

Example 1

- Position - Long - Buy June Sensex Futures @ 15000
- Payoff -
  - Profit - if the futures price goes up
  - Loss - if the futures price goes down
- Calculation - The profit or loss would be equal to fifteen times the difference in the two rates.
  - If June Sensex Futures is sold @ 15500 there would be a profit of 500 points which is equal to Rs. 7500 (500*15).
  - However if the June Sensex However if the June Sensex Futures is sold @ 14700 , there would be a loss of 300 points which is equal to Rs. 4500 (300*15).

Example 2

- Position - Short - Sell June Sensex Futures @ 15500
- Payoff -
  - Profit - if the futures price goes down
  - Loss - if the futures price goes up
- Calculation - The profit or loss would be equal to fifteen times the difference in the two rates.
  - If June Sensex Futures is bought @ 15900 there would be a loss of 400 points which is equal to Rs. 6000 (400*15).
  - However if the June Sensex Futures is bought @ 15200, there would be a profit of 300 points which is equal to Rs. (300*15).

2 What happens to the profit or loss due to daily settlement ?

In case the position is not closed the same day, the daily settlement would alter the cash flows depending on the settlement price fixed by the exchange every day. However the net total of all the flows every day would always be equal to the profit or loss calculated above. Profit or loss would only depend upon the opening and closing price of the position, irrespective of how the rates have moved in the intervening days.

Let's take the illustration given in example 1 where a long position is opened at 15000 and closed at 15800 resulting in a profit of 800 points or Rs. 12000. Let's assume that the position was closed on the fifth day from the day it was taken. Let's also assume three different series of closing settlement prices on these days and look at the resultant cash flows.

Example 3

Daily closing settlement price

	Case 1	Case 2	Case 3
Day 1	14900	14800	14500
Day 2	15350	15300	15100
Day 3	15280	15400	14950
Day 4	14950	14700	15200
Position closed	15800	15800	15800

Case 1		Settlement Price	Calculation	Profit / Loss
Position opened	15000			
Day 1		14900	14900-15000	-100
Day 2		15350	15350-14900	450
Day 3		15280	15280 -15350	-70
Day 4		14950	14950 - 15280	-330

Position closed	15800		15800 - 14950	850
Net Profit/ Loss				800

Case2		Settlement Price	Calculation	Profit / Loss
Position opened	15000			
Day 1		14800	14800 - 15000	-200
Day 2		15300	15300-14800	500
Day 3		15400	15400-15300	100
Day 4		14700	14700 - 15400	-700
Position closed	15800		15800-14700	1100
Net Profit/ Loss				800

Case3		Settlement Price	Calculation	Profit / Loss
Position opened	15000			

Day 1		14500	14500 - 15000	-500
Day 2		15100	15100 -14500	600
Day 3		14950	14950 -15100	-150
Day 4		15200	15200 - 14950	250
Position closed	15800		15800 -15200	600
Net Profit/ Loss				800

In all the cases the net resultant is a profit of 800 points, which is the difference between the closing and opening price, irrespective of the daily settlement price and different MTM flows.

3 How does the Initial Margin affect the above profit or loss ?

The initial margin is only a security provided by the client through the clearing member to the exchange. It can be withdrawn in full after the position is closed. Therefore it does not affect the above calculation of profit or loss.

However there may be a funding cost / transaction cost in providing the security. This cost must be added to your total transaction costs to arrive at the true picture. Other items in transaction costs would include brokerage, stamp duty etc.

4 What is a spread position ?

A calendar spread is created by taking simultaneously two positions

1. A long position in a futures series expiring in any calendar month
2. A short position in the same futures as 1 above but for a series expiring in any month otherthan the 1 above.

Examples of Calendar Spreads

1. Long June Sensex Futures - Short July Sensex Futures.
2. Short July Sensex Futures - Long August Sensex Futures

A spread position must be closed by reversing both the legs simultaneously. The reversal of 1 above would be a sale of June Sensex Futures while simultaneously buying the July Sensex Futures.

5 How are spread rates calculated ? Please illustrate with an example.

The profit or loss in case of spreads depends only upon the difference between the rates for the two different calendar months. The real position is only of the differential - irrespective of the two rates.

Let's take an example.

Example 4 - assuming the futures are being traded at the following rates

	June		July		August	
	Bid	Ask	Bid	Ask	Bid	Ask
Rate	16200	16250	17000	17100	17500	17550

The spread calculations are as follows

Spread	Calculation	Rate
June - July	17000 - 16200	800
July -August	17500 - 17000	500
June - August	17500 - 16200	1300

6 How do we calculate spreads in case of two way quotations ?

In case the prices are quoted as bid and offer, the spreads would also have a two way quotation. While calculating use thumb rule that the spread rate calculated must have the maximum spread possible from the two given rates.

Example 5 - Lets assume the futures are being traded at the following rates

	June		July		August	
	Bid	Ask	Bid	Ask	Bid	Ask
Rate	16200	16250	17000	17100	17500	17550

The spreads would be calculated as follows.

Spread	Calculation	Rate	
June - July	17000 -16250 & 17100-16200	750	900
July - August	17500 -17100 & 17590-17000	400	590
June - August	17500 -16250 & 17590-16200	1250	1390

Another thumb rule to check the correctness of calculation is that the bid offer difference of the spread must be equal to the sum of the bid-offer differences of the two futures contract. For example the bid-offer difference for June-August spread is 140 points which is equal to the sum of the bid-offer difference of June Futures 50 points and August Futures 90 points.

7 Please give a simple illustration to explain the mechanics of spread trading ?

To illustrate lets assume that the market is in Contango i.e. the futures price is higher than the cash underlying price and the futures price of far month is higher than the futures price of the near month.

	June	July	August
Rates	15500	16200	17000

The spread calculations are as follows

Spread	Calculation	Rate
June - July	16200 - 15500	700
July - August	17000 - 16200	800
June - August	17000 - 15500	1500

Example 6

- Position -
  - Receiving the spread â€" Buy near month futures + Sell far month futures
  - Paying the spread â€" Sell near month futures + Buy far month futures
- Payoff -
  - Profit - Spread received > spread paid
  - Loss - Spread received< spread paid
- June- July spread is paid at 700 points . If June -July spread can be reversed at higher than

700 points it would result in profit. Assuming that the spread is reversed at 800 points a profit of 100 points or Rs1500 would result.

Open	Spread	Sell June	Buy July
Pay	700	15500	16200
Close		Buy June	Sell July
Receive	800	15500	16300
Profit	100	0	100

Please note that the spread profit depends only upon the differential received or paid, irrespective of the futures rates. In the above example let's take three cases where reversal is done at 900 points but with substantially different levels for June and July.

Case 1 -17000 and 17900

Open	Spread	Sell June	Buy July
Pay	700	15500	16200
Close		Buy June	Sell July
Receive	900	16550	17450
Profit	200	1050	1250

Case 2 - 16550 and 17450

Open	Spread	Sell June	Buy July
Pay	80	4600	4680
Close		Buy June	Sell July
Receive	900	16550	17450
Profit	200	1050	1250

Case 3 - 16000 and 16900

Open	Spread	Sell June	Buy July
Pay	700	15500	16200
Close		Buy June	Sell July
Receive	900	16000	16900
Profit	200	500	700

You would notice that the profit is always 200 points irrespective of the rates as the spread received is constant at 900 point