

Derivatives on

GLOBAL INDICES

Trade in global markets through NSE

DIRECTIONAL OVERVIEW



Presenting future contracts on S&P 500® and DJIA indices

S&P 500 and DJIA indices are two of the world's most followed indices and are considered as the barometers of U.S. market. These indices have displayed historic resilience in holistically capturing the movements of the U.S. market. NSE which has been a pioneer in the introduction of innovative and investor friendly products is introducing rupee denominated future contracts on S&P 500 and DJIA indices. This is the first time in the world that futures contracts on S&P 500 index are being introduced and listed on an exchange outside of their home country, USA.

Indices

S&P 500®

S&P 500 is a free-float capitalization-weighted index of 500 leading companies of the U.S. economy and is widely regarded as the best single gauge of the U.S. equities market. Although the S&P 500 focuses on the large cap segment of the market, with approximately 75% coverage of U.S. equities, it is still widely considered as an ideal proxy for the total market. S&P 500 is maintained by Standard & Poor's and was introduced in 1957.

DJIA

Dow Jones Industrial Average (DJIA) is a price weighted index first published in the 1896. DJIA Index includes 30 large and liquid blue chips stocks traded on U.S. exchanges. The Dow® represents roughly 28% of the float-adjusted market capitalization of the U.S. stock market. Being composed mainly of blue-chip stocks having a leadership position in the U.S. market the Dow® doesn't literally "represents" the entire U.S. market rather, it is a blue-chip index representing the leading companies in the industries driving the U.S. stock market. As a result, its performance is highly correlated with broad-based U.S. indices like S&P 500.

Background

Indian Investors are currently permitted to invest in foreign assets subject to the limits stipulated by the Reserve Bank of India. The transaction costs in respect of direct investment transactions could be higher and are subjected to foreign currency risks apart from the equity market risks. Futures on S&P 500 and DJIA currently being introduced by NSE shall enable investors desirous of taking exposures to U.S. market to do so, without taking any foreign currency risk as they are rupee denominated contracts. Besides, these contracts enable those invested in the U.S. markets to hedge their equity exposure. They also provide a mechanism to those investors who want to hedge their Indian portfolios from foreign event risk. They can also be used as a hedging tool by investors having a high exposure to stocks in sectors whose financial performance depends significantly on the prospect of the U.S. economy. Further, these contracts traded together provide new opportunities of using trading strategies like Gap trading and Simultaneous trading by taking advantage of good positive correlation between the indices.



About this Booklet

This booklet is developed to acquaint the members with the contract specifications of the future contracts on S&P 500 and DJIA and also to give them an overview of the utility of these contracts for expressing directional view on S&P 500 and DJIA indices and for short-term trading interest.

Contract Specifications

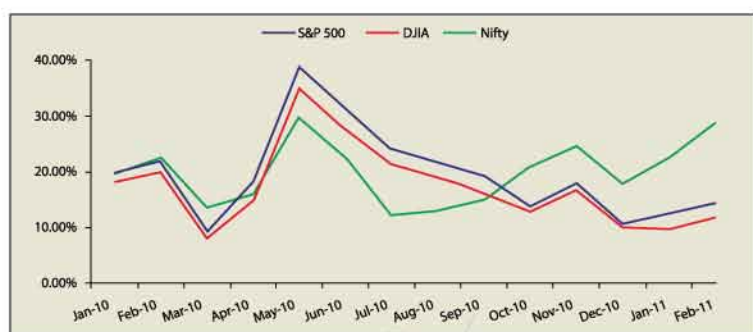
| | S&P 500 Index futures | DJIA Index futures |
|----------------------------|---|---|
| Ticker Symbol | S&P500 | DJIA |
| Contract Size | 250 units | 25 units |
| Notional value | Contract size multiplied by the index level (For example : if the current index value is 1000 then the notional value would be $1000 \times 250 = \text{Rs. } 2,50,000$) | Contract size multiplied by the index level (For example: if the current index value is 10000 then the notional value would be $10000 \times 25 = \text{Rs. } 2,50,000$) |
| Tick Size | 0.25 | 2.50 |
| Trading Hours | As in equity derivative segment | |
| Expiry Date | 3rd Friday of the respective contract month. In case third Friday is a holiday in USA or in India the contract shall expire on the preceding business day | |
| Contract months | Three serial monthly contracts and following three quarterly expiry contracts in the Mar-Jun-Sep-Dec cycle | |
| Daily Settlement Price | Last half hour's weighted average price | |
| Final Settlement Price | All open positions at close of last day of trading shall be settled to the Special Opening Quotation (SOQ) of the S&P 500 and DJIA Index on the date of expiry. (http://www.cmegroup.com/trading/equity-index/files/SOQ.pdf) | |
| Final Settlement Procedure | Final settlement will be Cash settled in INR based on final settlement price | |
| Final Settlement day | All open positions on expiry date shall be settled on the next working day of the expiry day (T+1) | |
| Position Limits | The Trading Member/Mutual Funds position limits as well as the disclosure requirement for clients is same as applicable in case of domestic stock index derivatives | |

Using S&P 500 and DJIA index futures

Futures contracts on S&P 500 and DJIA indices are actively traded at Chicago Mercantile Exchange (CME) and are very liquid. Close to close volatility and intra-day Hi-Lo in these indices are comparable to that observed in Nifty.

Comparison of volatility

The graph provided below depicts the month wise volatility (annualized) observed in S&P 500, DJIA and Nifty indices over the past few months.



Intraday High/Low variation

Intra-day high/low variation of S&P 500 and DJIA indices are comparable to that of Nifty index. This may be observed from the table below which provides the Intra-day high/low variation of S&P 500, DJIA and Nifty Indices for the period from January 2010 to February 2011.

| Index | Average | Max | Min |
|---------|---------|--------|-------|
| S&P 500 | 1.31% | 9.55% | 0.29% |
| DJIA | 1.79% | 11.63% | 0.68% |
| NIFTY | 1.51% | 3.63% | 0.48% |

Using S&P 500 and DJIA index futures

Traders may use futures on S&P 500 and DJIA indices to express their views about the direction of U.S. markets and benefit from the same. The strategies which may be employed based on the trader's view of the market's movement are as follows:

Bullish View

Presume that a hypothetical trader is tracking the home sales report for taking a view on U.S. economy and that he expects a rise in home sales number for the month of February 2009. The report for same is expected in month of March 2009. To express his view, the trader goes long on DJIA futures by buying 1 future contract of March month

| | Mar 02, 2009 | Mar 23, 2009 |
|--------------|--------------|--------------|
| DJIA futures | 6763.30 | 7775.85 |

Presume that the trader's view was correct and the U.S. market reacted positively on March 23, 2009 on positive home sales report for February 2009. DJIA closed up 7% on March 23, 2009. If the trader decides to book profit by closing his positions he would make a profit of Rs. 25,314.

| | Long DJIA Position (Lot Size 25) |
|--|----------------------------------|
| Value of position on Mar 02, 2009 (in Rs.) | 1,69,082.50 |
| Value of position on Mar 23, 2009 (in Rs.) | 1,94,396.25 |
| Margin Cost (Assumed at 10%)/ Investment amount (in Rs.) | 16,908.25 |
| P&L (in Rs.) | 25,313.75 |
| Return on investment | 150% |

Bearish View

Presume that on Jan 02, 2009 a trader is bearish on U.S. economy and expects disappointing numbers for the fourth quarter. He feels the S&P 500 is trading at a premium. To express his view, the trader goes short on S&P 500 futures by selling 1 future contract.

| | Jan 02, 2009 | Jan 20, 2009 |
|-----------------|--------------|--------------|
| S&P 500 futures | 931.80 | 805.25 |

Presume that the traders view turns out to be correct and U.S. market reacted negatively on Jan 20, 2009 after banking and technology companies announced massive quarterly losses and poor forecast numbers. S&P 500 falls sharply and closes 5 % down. If the trader decides to book profit by closing his positions he would make a profit of Rs. 31,638.

| | Short S&P 500 Position (Lot Size 250) |
|--|---|
| Value of position on Jan 02, 2009 (in Rs.) | 2,32,950.00 |
| Value of position on Jan 20, 2009 (in Rs.) | 2,01,312.50 |
| Margin Cost (Assumed at 10%)/ Investment amount (in Rs.) | 23,295.00 |
| P&L (in Rs.) | 31,637.50 |
| Return on investment | 136% |

Important Macroeconomic indicators

S&P 500 and DJIA are dependent upon several macro-economic factors. Tracking some key indicators may help a trader to make an informed directional decision. Given below are some of these factors:

ADP Employment Report - It is a monthly report which helps to sense the growth prospect in the job market. If job growth is positive, then interest rates are likely to rise - bond and stock prices may fall. In contrast, when job growth is slow or negative, then interest rates are likely to decline - boosting up bond and stock prices in the process.

Housing Market Index - This report provides a gauge of the demand for housing and thereby the economic momentum. Growth in new home sales points towards greater consumption capacity of consumers. This report is published on monthly basis.

Consumer Price Index - The consumer price index is the most widely followed monthly indicator of inflation. Low inflation may promise low interest rates and therefore may be a boost to the market.

Producer Price Index - Producer price index measures prices of consumer goods and capital equipment. When PPI decreases it indicates low inflation and thereby low interest rates.

Industrial Production - Healthy Industrial production growth reflects the growth in the economy and therefore may be a boost to the market.

Trading S&P 500 and DJIA futures at NSE

Members shall not need any change to their existing hardware, software or network and Investors may use their existing relationship with their trading members to trade these products. The derivative contracts on these two indices provide multiple advantages as outlined below:

- **Simplicity:** The contracts shall be traded during Indian time and under the domestic regulatory set up

- **No currency risk:** The contracts are rupee denominated. Hence there shall be no currency risk associated in trading them
- **Ease of Access:** The instruments would be introduced in the existing equity derivatives segment. The existing trading, clearing and risk management infrastructure could be used without any additional cost
- **Opportunities:** Futures contracts on these indices will enable Indian investors to participate in international financial markets and bringing diversification in their investment portfolios
- **Security:** Settlement Guarantee currently available in F&O segment shall be automatically extended to these products as well

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