



Profitability of Futures w.r.t. SBI Bank: A Study

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ABSTRACT

Since 1991, India has implemented financial reengineering and new instruments as part of financial market reforms. One area in which innovation and growth are sluggish is the introduction of derivatives. The emergence and growth of the derivatives market in India are relatively recent developments. The volume and number of traded contracts in the derivatives market have grown exponentially since its inception in June 2000. Derivatives encompass a wide range of financial instruments, primarily consisting of options and futures. The price of the underlying asset and other relevant factors determine the value of these securities. They are worthless on their own and only have value because they give their owners the impression that they are the owners of some other financial assets or security. The purpose of this study is to investigate financial derivatives in relation to SBI Bank Ltd.

INTRODUCTION

The need of risk-averse economic players to protect themselves against uncertainty caused by fluctuations in asset values gave rise to the derivatives market, including forwards, futures, and options. Financial markets are defined by their tremendous volatility. Derivative products enable partial or total price risk transfer by locking in asset values. As risk management instruments, they frequently have minimal impact on changes in the pricing of the underlying assets. Derivatives, on the other hand, mitigate the impact of asset price volatility on risk-averse investors' cash flow and profitability by



locking in asset prices. Derivatives are risk-management instruments whose value is derived from an underlying asset. Underlying assets include indexes, shares, bonds, currencies, interest, and bullion. Banks, securities firms, corporations, and investors utilize derivatives to control risks, acquire lower-cost funding, and make a profit. In the future, derivatives are likely to rise even faster.

NEED FOR STUDY

The prominence of the derivative markets and their crucial role in the economy have grown recently. I've become interested in this field due to the rise in both domestic and foreign derivatives investments. By locking in asset values, derivative products allow for the partial or complete transfer of price risk. Given the rapid rise in trade volume in the derivatives market, investors will find great value in this analysis.

SCOPE OF STUDY

This study is restricted to "Derivatives," specifically focusing on futures and options within the Indian setting. A representative sample of the Inter-Connected Stock Exchange has been selected for the research. One cannot declare the study to be flawless. Any change might occur. The study's appraisal of the derivatives market is limited to the setting of India. The study is not predicated on the global view of derivatives markets, as seen in the CBOT, NASDAQ, and other places.

OBJECTIVES OF STUDY

- To examine how futures and options are traded.
- To determine the buyer and seller's and option writer's and holder's profit/loss position in futures transactions.

RESEARCH APPROACH

The primary and secondary sources of data used in the study are sources of information collecting. Primary data gathered in the form of questionnaires for certain reasons. Secondary data that is available online or through books, catalogues, etc.

LITERATURE REVIEW

Greeshma Francis (2019) "came to the conclusion that financial derivatives, because of their innovative nature and ability to disrupt the market, have a prominent place among all financial instruments



(products). Derivatives are a tool that enables the dealer to benefit while managing risk. Transferring risk from one person to another helps. One of the most prosperous emerging nations in terms of a thriving exchange-traded derivatives market is India. The introduction of equity derivatives into the Indian market has been a huge success. Globally, the rise of derivatives has outpaced that of its equivalent in recent years. The market for stock derivatives is significantly influencing how prices are discovered. Financial derivatives have been growing globally in India due to factors such as financial asset price volatility, global financial market integration, advanced risk management tools, financial engineering advancements, and risk management strategy choices."

In his 2014 study on futures, "Mohammed Rubani went into depth on how a futures contract is a special kind of financial contract, or derivative instrument, wherein two parties agree to transact a set of financial instruments or physical commodities for a certain price at a future date. When it comes to transaction costs, positions in futures markets may be taken considerably faster and for a lot less money than positions in the underlying spot markets. India is where financial instrument futures contracts first appeared. Index futures were introduced in June 2000, while individual futures contracts were introduced in 2001. The benefits of trading futures over other choices, such as savings accounts, equities, bonds, options, real estate, and collectibles, were highlighted in their study. strong liquidity, reduced transaction costs, profit in bull and bad markets, and high leverage."

"Ashutosh Vashishtha, Satish Kumar (2013) "highlighted that risk is a defining attribute of the majority of capital and commodities markets. Demand-supply dynamics cause fluctuations in the pricing of both agricultural and non-agricultural goods throughout time. The globalization and liberalization tsunami that has swept the globe over the last 20 years has resulted in a multiplication in the amount of international commerce and business. From Rs. 2365 crore in 2000–2001 to Rs. 11010482.20 crores in 2008–2009, the market turnover has increased. In only eight years, the volume of traded contracts and turnover in India's derivatives trading market had overtaken those of the cash segment. He finished by analyzing the historical foundations of derivative trading, the many kinds of derivative products, the evolution of regulations and policies, trends and growth, and the opportunities and difficulties facing the Indian derivative market going forward."

K. Soniya (2013) "emphasized the debut of the derivative market and noted that not all investors are aware that it is a recent development in India and that SEBI must take action to raise investor knowledge



of the derivative segment. The investor's profit or loss in the cash market is determined by the underlying asset's market price. The investor might make a huge profit or a sizable loss. On the other hand, the investor has minimal risk and enormous gains in the derivatives market. The main application of derivatives is for hedging. SEBI should amend several of its restrictions, such as contract size and FII involvement in the derivatives market, in order to expand the derivatives market in India."

DATA ANALYSIS

Evaluating futures' profit/loss position is the aim of this examination. Sample data from SBI Bank, HDFC Bank, and Axis Bank scrips were used for this study. The investigation took into account the banks' May 2018 contract, with a 3000 lot size. The analysis was conducted between May 1st, 2018 and May 25th, 2018.

Table-1: Market and Future Prices of SBI Bank

Date	Market Price	Futures Price	Open Interest	Number of Contracts
2-May-18	222	242.55	83166001	11370
3-May-18	242.9	243.35	82923001	11870
4-May-18	242.95	243	81693001	10939
5-May-18	247.5	247.1	82428001	13022
8-May-18	251.05	251.45	83877001	24083
9-May-18	249	249.15	85563001	10939
10-May-18	248.95	248.2	83529001	12387
11-May-18	251.35	251.2	81180001	10763
12-May-18	254.6	253.2	77517001	13539
15-May-18	249	247.75	78375001	18733
16-May-18	244.1	243.05	77610001	19542
17-May-18	243.7	243	77748001	10493
18-May-18	239.85	239.4	75999001	12389
19-May-18	245.45	245.6	73032001	19439
22-May-18	254.9	255.7	77448001	78061
23-May-18	264.2	263.8	77796001	61846



24-May-18	269.5	268.95	78693001	26461
25-May-18	267.95	268.65	73104001	18116

Sources: Primary Data

Interpretation: "One lot, or one thousand SBI futures, purchased on May 2, 2018, and sold on May 25, 2018, will result in a profit of Rs 241 - Rs 266.95, or Rs 25.95 per share. As a result, he will profit by Rs. 1650, or 0.55×1000 . He would make more money than he did at expiration if he sold the SBI futures on May 17 at a price of Rs 242.7. For the SBI futures, the trading week revealed high and low strike prices, also known as exercising prices. Price changes always have an effect on open interest and traded contracts. The cash market, the NIFTY index future, news about the underlying asset or sector (industry), engagement from FIIs, and other domestic and foreign events all have an impact on the futures market. At the conclusion of the contract period, SBI's closing price, which is Rs 266.95, is regarded as the settlement price."

Table-2, The first column explains the trading date, while the second column describes the SPOT market price in the cash sector on that day.

Table-2: Mark to Market Profit & Loss of SBI Futures

Date	Mark to Market	Date	Mark to Market
2-May-18	0	15-May-18	-5600
3-May-18	900	16-May-18	-4900
4-May-18	50	17-May-18	-400
5-May-18	4550	18-May-18	-3850
8-May-18	3550	19-May-18	5600
9-May-18	-2050	22-May-18	9450
10-May-18	-50	23-May-18	9300
11-May-18	2400	24-May-18	5300
12-May-18	3250	25-May-18	-1550

Sources: Primary Data

Graph-1: Price Movements of SBI Bank Spot & Futures

Sources: Primary Data

Interpretation: "SBI's future price is rising in tandem with the going rate. The buyer of a future makes money if the future's buy price is lower than the settlement price. The seller experiences losses if the futures selling price is lower than the settlement amount."

FINDINGS

- The study shows how successful hedging techniques are in reducing risk. It has discovered that danger is unavoidable. But can only be reduced to a minimum.
- Hedging, it has been discovered, offers a secure position on an underlying security. The other party bears the brunt of the loss. So, the risk and loss are covered by the hedging. Occasionally, the market's performance defies forecasts. Losses will result from this. As a result, the hedger has to think strategically and optimistically.
- The outcome of the employed strategy is significantly influenced by the hedger's prediction of the direction of the movement in the underlying security's price.
- It was discovered that every strategy used on historical data from the study's time period was able to significantly lower the loss resulting from price risk.
- The trader can counter position in a future contract and lower the degree of risk if he is unsure of the direction in which the profits of the present position will move.
- If the trader anticipates the market correctly, he may employ the approach to increase returns in an efficient manner.



- Anticipating tactics only for return enhancement is often a dangerous endeavor, as the position taker stands to lose more if the expectations regarding the market and underlying deliver poorly.

SUGGESTIONS

"Scripts from various sectors must make up a portfolio if an investor want to hedge using them since they are practical and accurately reflect the makeup of the securities market overall. The hedging instrument to lessen potential market risk losses. Loss reduction, not profit maximization, is its main goal. The gains from shares or futures will be deducted from the losses from shares or futures, as applicable. The return that a hedger receives is going to be less than that of a non-hedger. But compared to a hedger, the non-hedger bears a greater risk. The hedger must have both a positive and a strategic mindset. He ought to be aware of the movements and patterns in the market. If not, the tactics he uses result in losses for him. Much more knowledge of the stock market and investing trends is required, both in the present and the futures markets. In this sense, the operations of the NSE and BSE Training Institutes are concerning."

CONCLUSION

Many market chances arise from derivative trading, but investors must possess a thorough understanding of derivatives and know how to combine various products. An investor would be better off booking a profit than expecting to make more, as tiny movements in share prices, in contrast, might have a negative effect on the premium amount under futures and options. Because short positions have limited gains and an infinite loss responsibility, they should be managed carefully. Rather of hoping for enormous returns, investors should attempt to hedge their positions to reduce losses. Refrain from entering contracts when there is little liquidity.

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