Measures for Rationalization and Strengthening the framework of Equity Derivatives Market

1. **Objective**

   1.1 This memorandum presents before the Board various measures that are being proposed for the rationalisation and strengthening of Equity Derivatives Market in India.

2. **Background**

   2.1 The Derivatives market in India has seen robust growth over time. Orderly growth, development and alignment of both cash and derivatives markets is important. Keeping this objective in mind, a proposed discussion paper was taken for consideration of the SEBI Board in its meeting held on June 03, 2017. The discussion paper undertook an assessment of the Indian derivatives market so as to evaluate whether there is a need to further strengthen the regulatory framework for derivatives in India. After due deliberations, the Board decided that stakeholders be consulted to ascertain their feedback.

3. **Discussion Paper/public consultation on Growth and Development of Derivative Market in India**

   3.1 As per the aforesaid Board decision, a discussion paper on “Growth & Development of Derivatives Market” and “Physical settlement in stock derivatives” was placed on the SEBI website for public consultation.

   3.2 In light of the public comments received and assessment thereof, discussion with the stock exchanges and market participants and further discussion in the Secondary Market Advisory Committee (SMAC) held on March 07, 2018, it is proposed that the measures stated in paragraph 4 below may be considered for further rationalisation and strengthening of Equity Derivatives Market in India.

4. Issues stated in the discussion paper and their assessment:

4.1 Whether there is a need to have compulsory physical settlement in stock derivatives contracts and whether physical settlement should be done in a phased manner starting with stock options followed by stock futures?

Feedback

4.1.1 On the issue of compulsory physical settlement:

4.1.1.1 Total 21 responses were received from market participants, out of which 12 participants felt that physical settlement should be made mandatory and 5 of them stated that the development of Securities Lending and Borrowing Mechanism would be a necessary pre-condition for physical settlement; revision of the eligibility criteria and physical settlement should only be permitted in very liquid stocks; etc.

4.1.1.2 Remaining participants suggested that physical settlement may increase cost and may not be required.

Our Comments

4.1.2 It may be brought out that final settlement price of cash settled equity derivatives contracts for stocks is based on the price in the underlying market i.e. the final settlement price of derivatives contract is based on the last half hour Volume Weightage Average Price (VWAP) of the relevant stock in the underlying cash market, on the date of expiry of the derivatives contract.

4.1.3 Towards this end, concerns have been raised that the settlement price for stock derivative may be amenable to possible mis-alignment due to low trading activity/ turnover in the underlying cash market and/or significant open interest (OI) held by certain group of investors (individuals and persons acting in concert (PACs) in such stocks.

4.1.4 In order to examine the alignment of cash and derivative segment, data was sought from the stock exchanges. Based on the data examined (sample of such stocks given as Annexure-1), it was observed that certain stocks had very high open interest held by individuals/ PACs and low liquidity in the cash market. Such a scenario provides considerable incentive for the individual/PAC to influence the settlement price of the derivatives contract by participating in the underlying cash market.

4.1.5 SMAC also took note of the recommendations of the L.C Gupta committee, constituted by SEBI, which laid down the principles for development and regulation of derivative markets in India. The L.C. Gupta committee had, inter alia, recommended in September, 2002 that “the positions which remain outstanding on the expiration date will have to be settled by physical delivery... However, when single stock derivatives were introduced in India, it was decided to use cash settlement to begin with because the exchanges did not then have the software, legal framework and administrative infrastructure for physical settlement. It was proposed that cash settlement would be replaced by physical settlement within a period of six months as the exchanges developed the capabilities to achieve physical settlement efficiently”.

4.1.6 Considering the above, SMAC was of the opinion that the probable mis-alignment between cash and derivative segment can be addressed if stock derivatives are physically settled as the closing price in the cash segment is not relevant for physical settled stock derivatives. Further, SMAC opined that a liquid and fully functional SLBM mechanism would complement physical settlement of stock derivatives.

4.1.7 Accordingly, SMAC recommended that adoption of physical settlement of stock derivatives should be carried out in a calibrated manner.

4.2 **Whether there is a need to review existing criteria for introduction of derivatives on stocks or derivatives on indices**

Feedback

4.2.1 On the issue of reviewing the existing criteria for introduction of derivatives:

4.2.1.1 Total 44 responses have been received from market participants out of which 32 respondents belong to institutional category and others are from individual investors.

4.2.1.2 Majority (68% of the respondents) suggested that there was a need to relook at the eligibility criteria for F&O stocks. It has been suggested that the criteria should be more stringent so as to reduce the number of stocks in derivatives.

4.2.1.3 Remaining participants responded that status quo may be maintained.

Our Comments

4.2.2 The revision in the existing entry criteria for introduction of derivatives on stocks was made in 2012. Given that market capitalization has moved up considerably since then, SMAC was of the opinion that the entry criteria be suitably revised to factor in the increase in the market capitalization.

4.2.3 Accordingly, SMAC felt that the exiting entry criteria with regard to market wide position limits (MWPL) and median quarter-sigma order size (MQSOS- a stock's quarter-sigma order size is defined as the order size in value terms required to cause a change in the stock price equal to one-quarter of a standard deviation) should be revised upwards from current level of Rs 300 crore and Rs. 10 lakh respectively to Rs. 500 crore and Rs. 25 lakh respectively.

4.2.4 To address the concerns that there may be mis-alignment between cash and derivatives due to low trading activity/turnover in the underlying cash market, SMAC opined that an additional criteria of liquidity in the cash market be also incorporated for considering introduction of stocks in derivatives. Accordingly, SMAC recommended an additional criterion of average daily ‘deliverable’ value in the cash market of INR 10 Crore.

4.2.5 Accordingly, it is proposed that any new stock would become eligible for derivatives if it meets the following norms:

- The stock is amongst the top 500 stocks in terms of average daily market capitalization and average daily traded value in the previous six months on a rolling basis. (same as the existing criteria for entry of stocks in derivative)
- The market wide position limit in the stock shall not be less than INR 500 crores on a rolling basis (existing INR 300 crores)

- The stock's median quarter-sigma order size over the last six months, on a rolling basis, shall not be less than INR 25 Lakh. (existing INR 10 Lakh)
- Average daily 'deliverable' value in the cash market is not less than INR 10 Crore in the previous six months on a rolling basis. (new/additional criteria proposed)

Above criteria are to be met for a continuous period of six months.

4.2.6 It may be noted that applying the enhanced criteria given at para 4.2.5 above to the existing position would result in significant number of stocks (69 stocks out of 208 stocks) moving out of derivative segment. Considering the recommendation of SMAC for introduction of physical settlement of stocks in derivatives in a calibrated manner, it is proposed that, to begin with;

- Stocks which are currently in derivatives and meet the current existing criteria (given at Annexure-2) but do not meet the enhanced criteria (given at para 4.2.5) would be physically settled. Such stocks, however, would have to meet the enhanced criteria within a period of one year from the specified date failing which they would exit out of derivatives. Or if the stock fails to meet any of the current existing criteria for a continuous period of three months, then it would exit out of derivatives. Stocks which are currently in derivatives and meet the enhanced criteria (given at para 4.2.5) shall be cash settled for the time being and would move to physical settlement in a phased manner. Stocks not satisfying any one of the enhanced criteria for a continuous period of three months shall move from cash settlement to physical settlement and after moving to physical settlement if the stock does not meet any of the current existing criteria for a continuous period of three months, then it would exit out of derivatives.

Proposal:

4.2.7 The proposals detailed above are summarized below:

4.2.7.1 Physical settlement for all stock derivatives shall be carried out in a calibrated manner.

4.2.7.2 Any new stock shall be introduced in derivative segment only if it satisfies the following enhanced eligibility norms:

- The stock is amongst the top 500 stocks in terms of average daily market capitalization and average daily traded value in the previous six months on a rolling basis. (same as the existing criteria for entry of stocks in derivative)
- The market wide position limit in the stock shall not be less than INR 500 crores on a rolling basis (existing INR 300 crores)
- The stock's median quarter-sigma order size over the last six months, on a rolling basis, shall not be less than INR 25 Lakh. (existing INR 10 Lakh)
- Average daily 'deliverable' value in the cash market is not less than INR 10 Crore in the previous six months on a rolling basis. (new/additional criteria proposed)

Above criteria are to be met for a continuous period of six months and would be reviewed in line with the market.

4.2.7.3 Stocks which are currently in derivatives and meet the current existing criteria but do not meet the enhanced criteria would be physically settled. Such stocks, however, would have to meet the enhanced criteria within a period of one year from the specified date to continue in the derivative segment. In the intervening one year period, if stocks fail to meet any of the current existing criteria for a continuous period of three months, failing which they would exit out of derivatives.

4.2.7.4 Stocks which are currently in derivatives and meet the enhanced criteria shall be cash settled for the time being and would move to physical settlement in a phased manner. The stocks not satisfying any one of the enhanced criteria for a continuous period of three months shall move from cash settlement to physical settlement and after moving to physical settlement if the stock does not meet any of the current existing criteria for a continuous period of three months, then it would exit out of derivatives.

4.3 **Ratio of turnover in derivatives to turnover in cash market is around 15 times. To what extent the drivers of this ratio in India are comparable with drivers in other markets.**

Feedback

4.3.1 Total 84 responses have been received on this issue, out of which 51 responses are from institutions including stock brokers and 30 responses are from individual investors.

4.3.2 The majority (74%) of the respondents felt that notional turnover has a multiplier effect due to the underlying price. Current notional reporting of turnover (in case of options) unduly inflates turnover of derivatives.

4.3.3 The remaining respondents (around 26%) did not express any concern over rising derivative to cash turnover; however, they have stated that cost of trading in cash segment is comparatively high in India and it should be reduced to enhance participation in cash segment.

4.3.4 A few respondents have expressed their concerns with regard to higher derivative turnover (T/O) compared to cash market.

Our Comments

4.3.5 Comparison of turnover ratio of derivate to cash market in India, with that of international markets, may not be an even comparison, single stock futures are not available in many jurisdictions and instead leveraged position similar to single stock futures are being taken through SLBM, Margin trading etc, which are reported as cash market turnover. Therefore, it is felt that due to nature of market structure and types of products, it would not be appropriate to compare our market with global markets.

4.3.6 The ratio of turnover in equity derivatives segment after taking into account only the premium paid for option contracts to turnover in equity cash segment, on an average, ranges between 2 to 4, while the same ratio based on notional turnover ranges between 12 to 15. This is broadly in line with the comparable statistics seen in different jurisdictions.

4.3.7 Internationally, there is no uniform practice of disseminating derivative turnover either on notional value or premium value. As per data made available by World Federation of Exchanges, option turnover is generally disseminated on the basis of notional value.

4.3.8 In 2015, SEBI advised exchanges to disseminate option turnover on premium basis along with notional values in order to increase transparency and provide additional information to market participants.

Proposal:

4.3.9 In view of the above, it is proposed that we may continue with the option turnover disclosures on premium along with notional value.

4.4 **Taking into account trading of individual investors in derivatives especially options, is there a need to introduce a product suitability framework in our market.**

Feedback

4.4.1 Total 66 responses have been received out of which 40 responses were received from institutional investors, including stock brokers. Remaining responses have been received from non-institutional investors.

4.4.2 Around half of the respondents, including institutions and non-institutions, are of the view that product suitability may not be required in light of the existing Risk disclosure documents that is mandated while on-boarding clients in F&O segment and requirement under SEBI (Stock-Brokers and Sub-Brokers) Regulations, 1992. The remaining respondents felt that there is need to have product suitability framework for derivatives.

Our Comments

4.4.3 Comparative analysis of the various jurisdictions indicate that certain jurisdictions have specific provisions for retail investors to qualify them for trading in derivatives. For instance, South Korea has "Qualified Retail Investor" Scheme. To prevent retail investors from making reckless investments and incurring huge losses in derivatives markets, South Korea has allowed only "qualified" retail investors to enter derivative market by establishing two stages of entry barriers'

- First stage - Retail investors who have completed prior education program and mock trading; and deposit at least KRW 30 million (i.e. Rs. 17.1 lakh approx.) as initial margin are allowed to trade simply-structured futures such as KOSPI200 futures or individual stock futures.
- Second stage - Retail investors with more than one-year trading experience allowed under the 1st stage and KRW 50 million of minimum margin (i.e. Rs 28.5 lakh approx.) will be allowed to trade complicatedly structured-futures and options such as V-KOSPI200 futures.

4.4.4 It is noted that internationally the product suitability framework has evolved taking into consideration the following:

- Minimum Income level/Net worth,
- Minimum educational qualification,
- Minimum experience in dealing in the market,
- Due diligence by stock brokers while dealing with clients in derivative market.

4.4.5 Current framework in India: Risk Disclosure Document:

- At the time of on-boarding of a client by a broker, it is mandatory that a broker executes a Risk Disclosure Document (RDD) and the same is included in the documentation related to client registration. The RDD has a separate detailed paragraph, which contains information about the risks involved in trading in the derivatives segment. Some of the statements which are given in the document are as follows:
  - The amount of margin is small relative to the value of the derivatives contract so the transactions are “leveraged” or “geared”.

- Trading in derivatives can be conducted with a relatively small amount of margin and there is a possibility of great profit or loss in comparison with the margin amount.
- Transactions in derivatives carry a high degree of risk.
- The losses may exceed the original margin amount.
- Risk of Option holders: An option holder runs the risk of losing the entire amount paid for the option in a relatively short period of time. This risk reflects the nature of an option as a wasting asset which becomes worthless when it expires. An option holder who neither sells his option in the secondary market nor exercises it prior to its expiration will necessarily lose his entire investment in the option. If the price of the underlying does not change in the anticipated direction before the option expires, to an extent sufficient to cover the cost of the option, the investor may lose all or a significant part of his investment in the option.
- Risks of Option Writers: If the price movement of the underlying is not in the anticipated direction, the option writer runs the risks of losing substantial amount. A spread position is not necessarily less risky than a simple 'long' or 'short' position. Combination transactions, such as option spreads, are more complex than buying or writing a single option. And it should be further noted that, as in any area of investing, a complexity not well understood is, in itself, a risk factor.

* Trading preferences: It is mandatory for the clients to provide their trading preference in terms of the exchanges and segments they want to trade (CIR/MIRSD/16/2011 dated August 22, 2011).
* Financial Details: It is mandatory for clients who opt to trade in derivatives segment to give their financial details i.e. their income

and the proof of income at the time of account opening. (CIR/MIRSD/16/2011 dated August 22, 2011).

- All dealers who operate in derivatives market have to pass relevant NISM examination or are required to undergo CPE training prescribed by NISM.

4.4.6 The regulatory framework in India has mainly evolved on the premise of disclosures. Such disclosures are required to be given at the time of on boarding of a client by a broker in terms of 'Rights and Obligations' document(s) and 'Risk Disclosure Document'. A client needs to confirm having read and understood the contents of the documents executed with the Stock Broker. In addition, SEBI (Stock-Brokers and Sub-Brokers) Regulations, 1992 also specify the code of conduct for stock brokers while dealing with clients.

4.4.7 Further, in the F&O segment of our market, it is mandatory for members to collect initial margins from respective clients on an upfront basis.

4.4.8 At the same time, however, a large proportion of individual investors trade in derivatives including writing of Options. Contribution of individual investors to the total turnover in the equity derivative segment was 25.67% during the FY 2016-17. Some of these individual investors may not be conversant with the risks associated with derivatives, even though they have been on boarded based on signing of the risk disclosure documents.

Proposal:

4.4.9 Considering that different jurisdictions have mandated specific product suitability norms for individual investors and it is important to maintain a balance with regard to providing opportunities and freedom to individual investors to express their views vis a vis risk associated with derivatives market**,** it is proposed that;

4.4.9.1 Individual investors may freely take exposure in the market (cash and derivatives) upto a computed exposure based on his disclosed income as per his ITR over a period of time. For any exposure beyond the computed exposure, the intermediary would be required to undertake rigorous due diligence and take appropriate documentation to satisfy the credit/exposure suitability of the individual investor.

4.4.9.2 Determination of the computed exposure and details of due diligence documents required shall be formulated in consultation with market participants.

4.5 **What are the global best practices and experience in international markets to align cash and derivative markets.**

Feedback

4.5.1 Total 50 responses have been received on this issue, out of which 32 responses are from institutions including stock brokers and 18 responses are from individual investors.

4.5.2 Market participants unanimously responded that a greater policy emphasis should be required to lower constraints on participation of financial institutions and developing weak or missing links between two markets such as the developing Securities Lending and Borrowing mechanism & Margin Trading framework to make it efficient and liquid. Further, identifying and removing divergences in trading costs between cash and derivative markets would be required to align these markets.

Our Comments

4.5.3 Almost all market participants who have responded felt that majority of markets globally have in place, well developed Securities Lending and Borrowing mechanism (SLBM) and suitable Margin Trading norms, both of which align the underlying cash market and the derivative markets.

4.5.4 With regard to the above suggestions, it is informed that SEBI has been taking various measures to develop underlying cash market. SLBM framework has been revised (17/10/2017) to make SLB products more suitable to the needs of the market participants. Margin Trading norms have been revised especially margin requirements were brought in line with that of derivative segment and certain other measures were also introduced to simplify the framework.

4.5.5 Further, market participants have also empathised that differentiating tax structure especially STT in cash and derivative market incentivises participants to trade in the derivatives as it is relatively cost effective to trade in derivatives. In this regard, the issue of STT on the cash market has been taken up with Government by SEBI.

4.5.6 It may be seen that the major suggestions (develop framework for SLBM and Margin Trading) by market participants to align the cash and derivative market have been implemented by amending the framework for SLBM and Margin Trading recently.

Proposal:

4.5.7 In view of the above, it is proposed that we may in due course analyse the market response to such changes and, if required, consider making modifications to SLBM/margin trading based on additional market feedback, at appropriate time.

4.6 **Considering the participants' profile, what measures would be required to create balanced participation in equity derivatives market.**

Feedback

4.6.1 Total 45 responses have been received out of which 31 responses were received from institutional investors, including stock brokers.

4.6.2 The majority suggested that the restrictions on domestic institutional investors such as insurance companies and mutual funds regarding participation in derivatives market may be relaxed. Certain other participants suggested introduction of longer tenure contracts.

Our Comments

4.6.3 Based on the suggestions received it is felt that various measures would be required in order to create a more balanced participation in derivatives. Therefore, there is need to relook at the regulatory restrictions placed on such domestic institutions especially in light of the fact that Indian markets already have a robust risk management framework in place.

4.6.4 As regard FPIs participation, it was opined by market participants that they may be trading in offshore exchanges, which are offering derivative products based on Indian indices, such as on SGX/Dubai etc. In light of recent development wherein SGX has introduced single stock futures on NIFTY stocks, exchanges (NSE, BSE and MSEI) have issued joint press release discontinuing their licensing arrangement with international exchange for trading of products based on Indian securities.

Proposal:

4.6.5 In view of the above, it is proposed that suggestions received to relook at the regulatory restrictions placed on such domestic institutions, may be taken up with the concerned sectoral regulators.

4.7 **Considering participants' profile, product mix and leverage in equity derivatives, what could be the guiding principles for setting minimum contract size and open position limits for equity derivatives.**

Feedback

4.7.1 Total 124 comments were received from market participants out of which 72 comments were received from non-institutions while 54 comments were received from institutional investors.

4.7.2 Majority market participants (80% respondents) stated that the contract size should not be increased and that rather it should be reduced. As regard position limits, the responses are fairly mixed.

Our Comments

4.7.3 In view of the contact size of various derivative products offered by international exchanges and based on the comments received, it appears that contract size should depend on the nature of the participation in the market. Large contract size are appropriate for markets dominated by large institutional participants, whereas in markets which have diverse participation across institutional and non-institutional investors, relatively smaller contract size is appropriate.

4.7.4 In many markets, mini derivatives contract, with lower lot sizes, exist alongside the primary derivative contracts. While this enables even smaller investors to participate, however, it causes a fragmentation of liquidity across products.

4.7.5 In view of foregoing, it is felt that introduction of mini contracts should not be encouraged.

4.7.6 In the discussion paper it was pointed out that Index option and stock options together dominate trading in derivatives and options account for 84% of trading volume in the derivatives market as per data for FY 2016-17.

4.7.7 In this regard, it may be noted that SEBI has recently prescribed that the market wide position limit for single stock futures and stock option contracts shall be linked to the free float market capitalization and shall be equal to 20% of the number of shares held by non-promoters in the relevant underlying security (i.e., free-float holding). Considering the investors profile in the Indian market, this limit is made applicable on aggregate open positions in all futures and all option contracts on a particular underlying stock.

Proposal:

4.7.8 In view of the above, it is proposed that:

4.7.8.1 Mini contracts may not be encouraged; and

4.7.8.2 Combined position limits product wise, i.e. combined limits for futures and for options, may continue.

4.8 **Whether there are any inefficiencies in the market that needs to be addressed.**

Feedback

4.8.1 Total 42 responses were received from market participants on this issue.

4.8.2 In this context, market participants have brought out inefficiencies related to taxes especially STT, excessive trading in out of money options and frequent breach of position limits, change in the methodology of calculation of closing price from VWAP to TWAP, etc.

Our Comments

4.8.3 It is noted that presently option sellers are charged 0.05% as STT on the premium amount. However, expiring in the money contracts attract STT at the rate of 0.125% on the notional value. As regard suggestions to reduce higher STT levy on exercise of the option, SEBI has permitted exchanges to provide a functionality to provide choice of ‘Exercise’ or ‘Do Not Exercise’, on the expiry day, for in-the-money (ITM) option contracts belonging to close to money (CTM) option series. Such functionality can be exercised by clients through stock brokers. The CTM option series are three ITM option series having strike prices immediately above settlement price (for put options) and three ITM option series having strike prices immediately below final settlement price (for call options). Therefore, with this framework in place in-the-money option holder belonging to close to money option series can express their willingness to exercise the option contract on expiry day.

4.8.4 In addition to the above, suggestion has also been received to change calculation methodology of closing price from volume weighted average price (VWAP) to time weighted price (TWAP). In this regard, the closing price in the cash market is calculated based on the volume weighted average price of trades executed in the last half hour of the trading hours. Few market participants have suggested that the VWAP is prone to manipulation as large trade in last half an hour could potentially change VWAP price. Therefore, instead of VWAP time weighted average price (TWAP) may be used.

4.8.5 Internationally, exchanges follow different practices for determining the closing price. Exchanges such as NYSE, NASDAQ and LSE follow closing call auction wherein close price is determined using call auction.

4.8.6 In India, the final settlement price of derivatives contract is based on the closing price of the relevant stock in the underlying cash market, on the expiry day of the derivatives contract. The perception of possible attempt to influence the closing price in cash market to gain in derivative segment would get mitigated with the proposed introduction of physical settlement.

Proposal:

4.8.7 In view of the above, it is proposed that we may continue with VWAP for arriving at settlement price of derivative contracts. However, improvements in calculation of settlement price may be separately examined in consultation with market participants taking into account the prevalent practices in different jurisdictions relating to methodology for calculation of settlement price.

4.9 **Whether there is any regulatory arbitrage that needs to be addressed**.

Feedback

4.9.1 Total 26 responses were received on this issue. The majority of respondents have raised the issue of taxes and regulatory arbitrage of trading of flagship indices in other jurisdictions.

4.9.2 Regulatory arbitrage in the equity derivatives market exists primarily in the form of competition from international markets that are increasingly focusing on introducing and trading India related products. Lot of trading in NIFTY futures is happening abroad especially on SGX. Any change in regulatory regime in India, there is always a constant fear that volumes shift abroad. SEBI can review the same and if possible disallow the listing of benchmark indices abroad to avoid such conflict.

Our Comments

4.9.3 The issue of taxes especially lower STT in options raised by certain market participants has already been dealt above.

4.9.4 The major concern expressed by market participants is related to trading of product based on the NIFTY and SENSEX. In this regard, acknowledging the concerns with respect to trading based on Indian indices in other markets, exchanges (NSE. BSE and MSEI) issued a joint press release dated February 10, 2018 stating that due to concerns of growing indices trading in other markets, existing licensing agreement with foreign counterparty will be discontinued. Therefore, with the said initiative of exchanges the concerns associated with trading in products based on the Indian indices may no longer remain.

4.10 **Taking into account the margin levied in the derivative segment and consequent leverage, is the present margin framework adequate. Is there a need to review trading and risk management framework for derivatives.**

Feedback

4.10.1 Total 59 responses have been received from market participants out of which, 41 respondents are from institutional category while 18 respondents are individual investors.

4.10.2 Almost 80% participant felt that there is need to review the margin framework for derivatives. Out of this, majority respondents are of the view that margins levied should be rationalised.

Our Comments

4.10.3 Market participants suggested to rationalise margin by allowing off-setting of margins across positions which materially reduce the risk. While certain other participants suggested to increase margin in the form of settlement margin (for those who have pay-in obligations), intra-day additional margin and also additional margins linked to leverage. Few participants suggested maintaining status quo on the risk management framework.

4.10.4 The performance of margin framework is measured by how well a clearing corporation can ensure that the markets continue to function with minimal counter-party defaults. By this simple measure, the present margin framework, which has been in place since 2002 for the equity derivatives markets, has functioned well. There have been no market failures even during the 2008 global market crash.

4.10.5 Study of global practices suggests that some of international exchanges/jurisdictions (CME and SGX-DC) do not permit cross margin benefits across markets i.e. underlying cash and derivative market. With a view to make our market more efficient, SEBI has already permitted cross margining for off-setting positions as per the following priority:-

- Index futures position and constituent stock futures position in derivatives segment.
- Index futures position in derivatives segment and constituent stock position in cash segment.
- Stock futures position in derivatives segment and the position in the corresponding underlying in cash segment.

Proposal:

4.10.6 The various aspects of risk management was also discussed in the Risk Management Review Committee (RMRC) on March 7, 2018. It was opined by the committee that further consultations with market participants on the existing framework of risk management in derivatives be carried out.

5. **Issues for deliberation by the Board**

The Board is requested to consider and deliberate the above issues. Board may also be requested to authorize the Chairman to make appropriate modifications in the existing framework for derivatives in terms of the decisions taken by the Board.

Annexure – 1

Table

Symbol	Average LHH CM Turnover (₹ Crores)	F&O LHH Expiry Day (₹ Cr)	Average Open Interest (OI) by Individuals or PACs (₹ Crores)	Ratio of OI/ Avg LHH CM
Scrip 1	2.73	12.92	1.56	0.57
Scrip 2	3.28	12.95	4.16	1.27
Scrip 3	4.22	12.89	5.53	1.31
Scrip 4	4.52	16.97	7.43	1.64
Scrip 5	5.01	13.33	5.31	1.06
Scrip 6	5.14	15.34	5.04	0.98
Scrip 7	5.32	22.51	9.10	1.71
Scrip 8	5.36	21.77	8.63	1.61
Scrip 9	5.72	25.70	12.00	2.10
Scrip 10	5.82	45.46	21.83	3.75

Source: NSE

Annexure – 2

Existing eligibility criteria for introduction of stock derivative

- The stock is amongst the top 500 stocks in terms of average daily market capitalization and average daily traded value in the previous six months on a rolling basis.
- The market wide position limit in the stock shall not be less than INR 300 crores on a rolling basis.
- The stock’s median quarter-sigma order size over the last six months, on a rolling basis, shall not be less than INR 10 Lakh.
