



Budget



PRE-BUDGET DERIVATIVE STRATEGIES -2021

Jan 24, 2021

DERIVATIVE STRATEGY – BUDGET 2021



The Budget session of Parliament will commence on January 29th and finance minister Nirmala Sitharaman will present the Union Budget on February 1st.

Nirmala Sitharaman earlier hinted that Hundred years of India wouldn't have seen a budget being made post a pandemic like this and therefore Budget announcement could be an extremely important event for Indian markets.

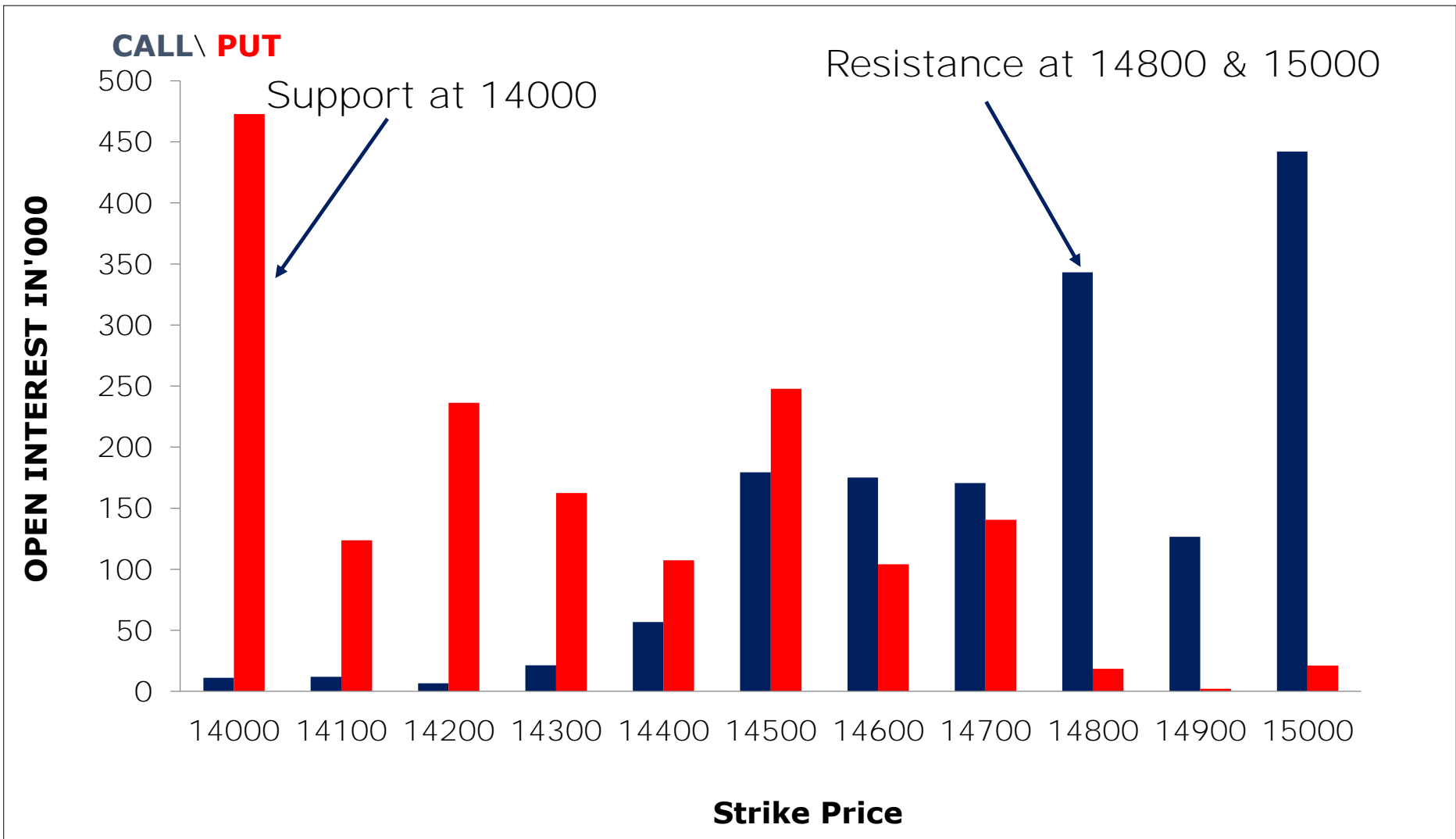
Depending on the budgetary announcements, Nifty may swing wildly on either side.

Moreover our markets have almost doubled from the March lows within the span of last ten months.

For investors who are fully invested, it is advisable to hedge your portfolio (full or part) ahead of such big events. This can be done by buying Index Put Options.

However one should understand that hedging is like an Insurance, which comes with some cost.

NIFTY OPTION OPEN INTEREST DISTRIBUTION (04 FEB EXPIRY)

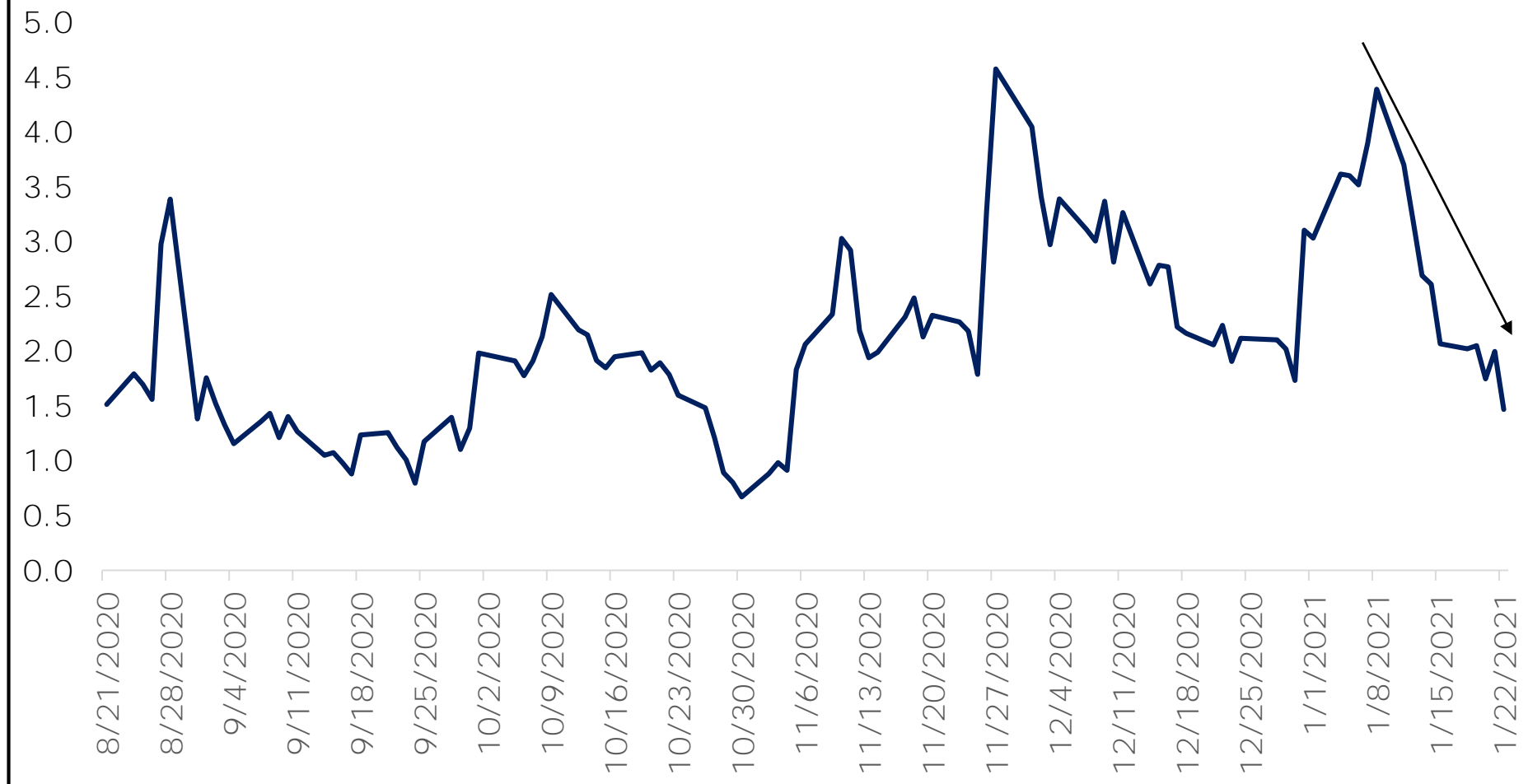


FII's REDUCING LONGS IN THE INDEX FUTURES

LONG TO SHORT RATIO - LOWEST SINCE 04 NOV 2020



FII's INDEX FUTLONG TO SHORT RATIO FELL TO 1.5 FROM 4



HISTORY SUGGESTS NIFTY IVs FALL ON THE BUDGET DAY



BUDGET DATE (A)	ONE DAY BEFORE BUDGET (B)	ON BUDGET (C)	CHANGE BASIS(%) (D=B-C)	One month before budget (E)	CHANGE BASIS (%) (F=E-C)	One month After budget (F)	CHANGE BASIS (%) (G=F-C)
28-Feb-15	19.68	16.99	-2.69	21.28	-4.29	14.00	-2.99
29-Feb-16	20.36	19.10	-1.26	16.49	2.61	17.98	-1.12
01-Feb-17	16.55	14.03	-2.52	14.85	-0.82	13.14	-0.89
01-Feb-18	15.19	13.15	-2.04	12.29	0.86	12.70	-0.45
01-Feb-19	16.85	14.76	-2.09	14.92	-0.16	14.04	-0.72
05-Jul-19	14.18	12.39	-1.79	13.36	-0.97	15.97	3.58
01-Feb-20	16.76	16.35	-0.41	10.33	6.02	24.30	7.95
AVERAGE			-1.83		0.46		0.77

HISTORY SUGGESTS BANK NIFTY IVs FALL ON THE BUDGET DAY



BUDGET DATE (A)	ONE DAY BEFORE BUDGET (B)	ON BUDGET (C)	CHANGE BASIS(%) (D=B-C)	One month before budget (E)	CHANGE BASIS (%) (F=E-C)	One month After budget (F)	CHANGE BASIS (%) (G=F-C)
28-Feb-15	27.80	24.65	-3.15	25.24	-0.59	20.03	-4.62
29-Feb-16	26.63	24.84	-1.79	22.95	1.89	24.09	-0.75
01-Feb-17	20.72	18.76	-1.96	19.85	-1.09	16.02	-2.74
01-Feb-18	18.12	15.85	-2.27	13.25	2.6	16.3	0.45
01-Feb-19	17.05	15.47	-1.58	14.58	0.89	13.54	-1.93
05-Jul-19	16.93	14.03	-2.90	15.59	-1.56	20.02	5.99
01-Feb-20	21.88	20.22	-1.66	13	7.22	25.7	5.48
AVERAGE			-2.19		1.34		0.27



For Investors who understand derivatives (its risks and rewards) and would like to hedge before announcement of budget.

There are lot of expectations from the Union budget 2021 and therefore there could be lot of volatility depending on the announcements from the budget.

Therefore for those who hold large portfolios, it is advisable to hedge (full or part) through buying Put Options. Here the simplest thing to do is to buy a Nifty Put.

STRATEGY : Buy NIFTY 14300 PUT AT Rs 211 (04 FEB EXPIRY). Lot size 75. Contract value Rs 1072500

The quantity of Put options that need to be bought will vary depending on the size and composition of the portfolio. Investors need to ascertain the beta of their portfolio.

- 1) Large cap Portfolio** – The beta of the diversified large cap stock portfolio is likely to be around 1. Assuming the size of the portfolio is Rs 1 Cr, one need to buy 9 lots of Nifty 14300 Put options.
- 2) Mid cap & Small cap Portfolio** – The beta of the diversified Small-cap stock portfolio is likely to be 1.10 (Last 5 years beta-Source Bloomberg). Assuming the size of the portfolio is Rs 1 Cr, one need to buy 10 lot of Nifty 14300 Put options.

Depending on the composition of the portfolio, the cost of hedging Rs. 1 cr portfolio will be approximately Rs. 1.42 lakhs to Rs. 1.58 lakhs (1.9% to 2.1% of portfolio value).

DERIVATIVE STRATEGY – FOR CONSERVATIVE TRADERS

Strategy : Short Iron Butterfly

We are suggesting short Iron Butterfly strategy for conservative traders.

It has been observed from past 7 years data that IV drops significantly on the budget day (Refer slide 5 & 6). Moreover Option data suggest we may move in the range of 14000-14800 till 04 Feb Expiry. Therefore we are suggesting following strategy to take benefit of it. It is four-part strategy consisting of a bull Put spread and a bear Call spread.

STRATEGY : SHORT IRON BUTTERFLY SPREAD

NIFTY(CMP 14372) Lot size 75 EXPIRY 04 FEB

Leg 1 : Sell 1 Lot NIFTY 14400 Call at Rs 257.1.

Leg 2 : Sell 1 Lot NIFTY 14400 Put at Rs 254.1.

Leg 3 : Buy 1 Lot NIFTY 14800 Call at Rs 96.7.

Leg 4 : Buy 1 Lot NIFTY 14000 Put at Rs 110.85.

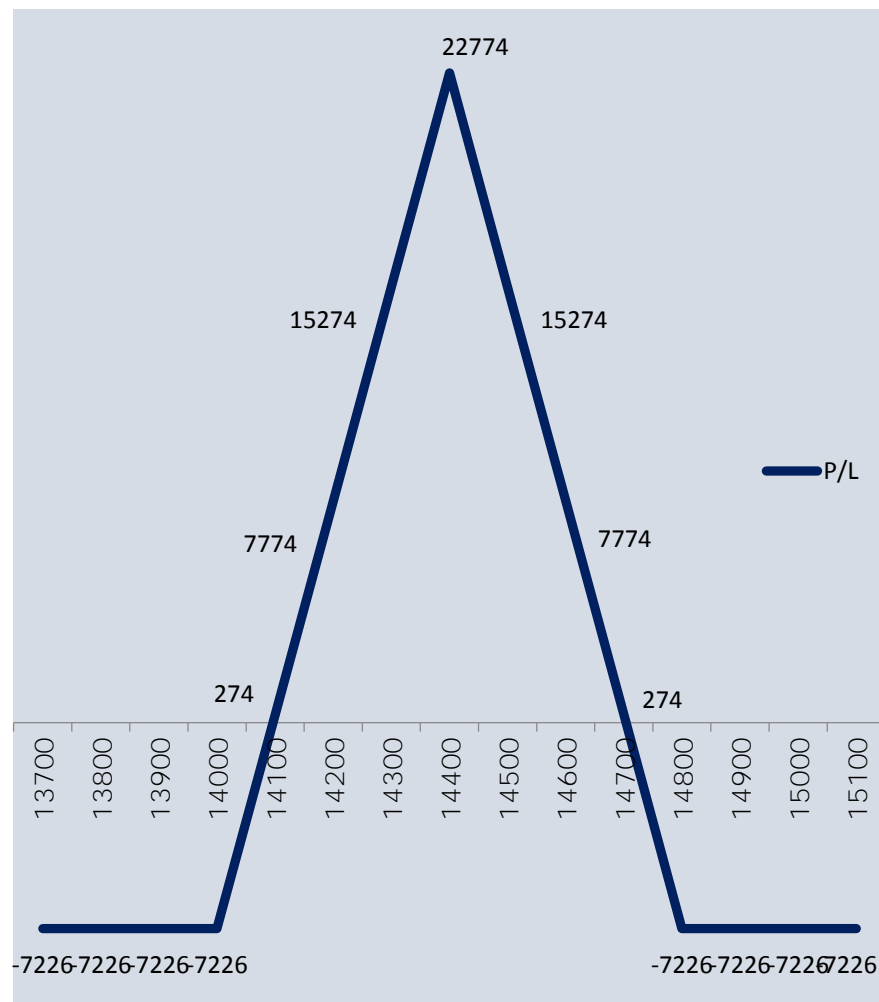
Total cost of the Strategy Rs 7226

Maximum Profit of Rs 22774, If Nifty closes at Rs 14400 on 04 Feb Expiry

Upper Breakeven Point : 14703. Lower Breakeven Point : 14097

Approx Margin requirement : Rs 85000

PAYOFF DIAGRAM



DERIVATIVE STRATEGY – FOR AGGRESSIVE TRADERS

Strategy : Long Butterfly With Puts

We are suggesting long Butterfly strategy for aggressive traders.

Few derivative Indicators (Refer Slide Number 7) suggest downside from hereon. Option data suggest on the downside Nifty May find strong support around 14000 levels. Therefore we are suggesting following strategy. A long butterfly spread with puts is a three-part strategy that is created by buying one put at a higher strike price, selling two puts with a lower strike price and buying one put with an even lower strike price.

STRATEGY : LONG BUTTERFLY SPREAD WITH PUTS

NIFTY(CMP 14372) Lot size 75 EXPIRY 04 FEB

Leg 1 : Buy 1 Lot NIFTY 14400 Put at Rs 254.1

Leg 2 : Sell 2 Lot NIFTY 14000 Put at Rs 110.85

Leg 3 : Buy 1 Lot NIFTY 13600 Put at Rs 38.85.

Breakeven Points 13671 & 14329

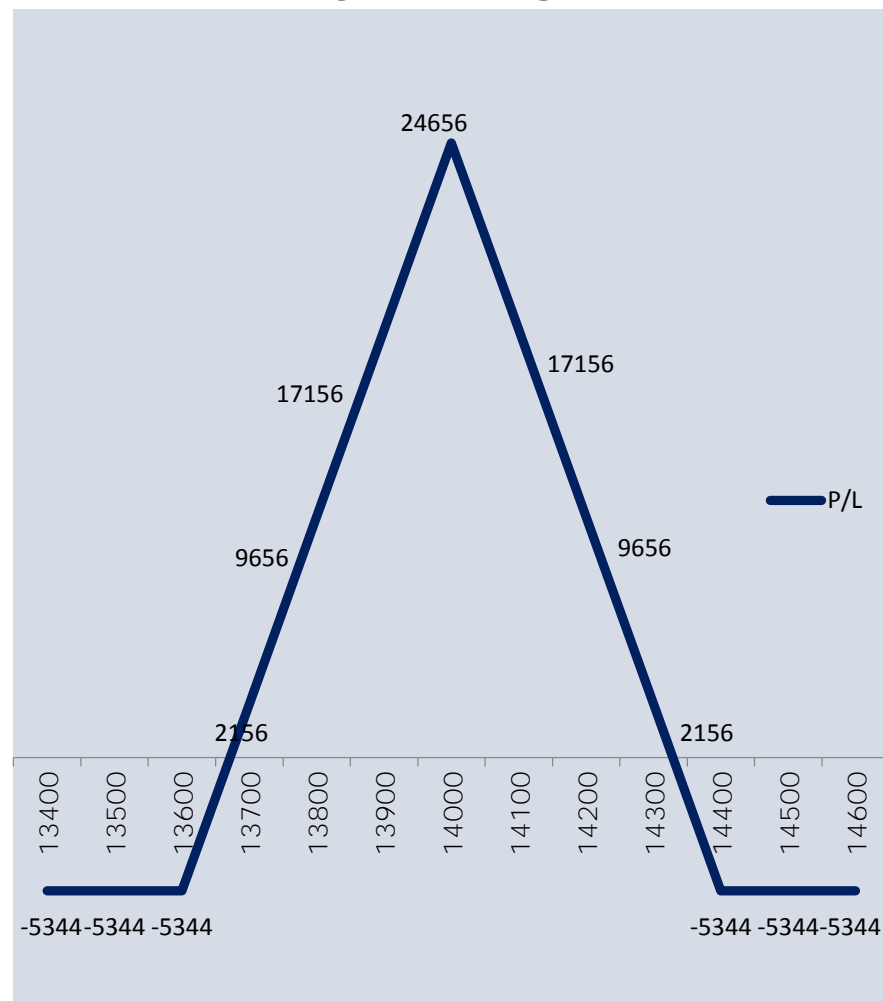
Maximum Profit of Rs 24656 at Rs 14000

Maximum loss of Rs 5344

- 1) If Nifty closes at or below 13600
- 2) If Nifty closes at or above 14400

Approx Margin requirement : Rs 43116

PAYOFF DIAGRAM



HEDGE MTF STOCKS USING PUT BEAR SPREAD STRATEGY



Script	EXPIRY	LOT		Strikes	PREMIUM	Strikes	PREMIUM	MAX LOSS PER LOT QTY	MAX PROFIT PER LOT QTY
			CMP	(TO BUY)	(TO BUY)	(TO SELL)	(TO SELL)		
BHARTIARTL	25-Feb	1851	577	570	27.45	540	16.65	19991	35539
BAJFINANCE	25-Feb	250	4967	4900	224	4600	110	28500	46500
DRREDDY	25-Feb	125	5034	5000	209	4700	91	14750	22750
RELIANCE	25-Feb	250	2050	2000	69	1900	32	9250	15750
KOTAKBANK	25-Feb	400	1831	1800	73	1700	37	14400	25600

Creating Put spreads may attract margins (relatively low - due to hedge positions). Hedging against MTF portfolio can also be done by using Nifty Options, but individual stocks may react differently to Budget announcements..

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