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India VIX and its implications, a thread ■:



What is India VIX?

India Volatility Index ie India VIX is a measurement of expected volatility in the near term usually over the next 30 days in the Nifty50 index.

This indicates how much the index can move either side where higher vix means market tends to move steeply up or down and lower vix usually indicates a stable or a steady pace move.

How is it calculated?

India VIX uses the computation methodology of Chicago Board of Options Exchange (CBOE), with suitable amendments to adapt to the NIFTY options order book.

It considers the current month and next month OTM strike option best bid and ask quotes which are traded in the Futures and Options segment of NSE.

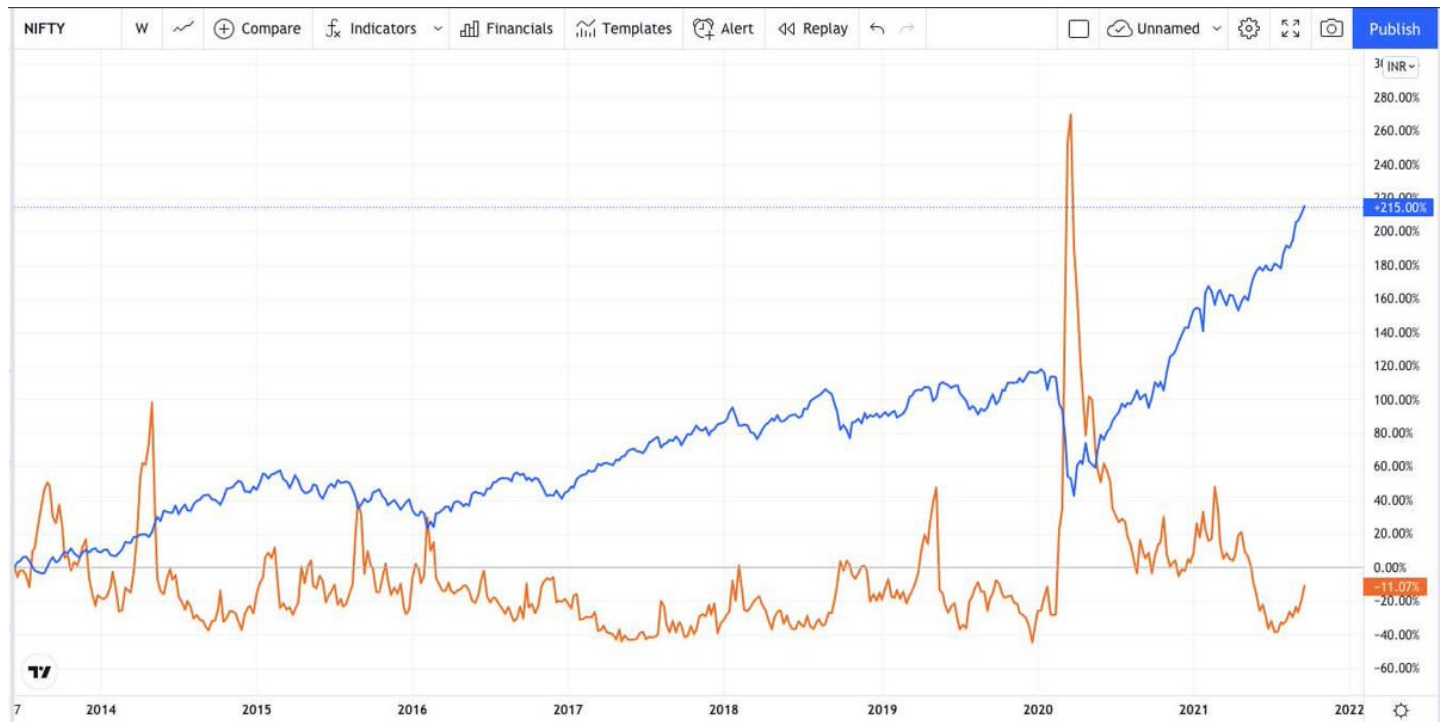
There are different factors considered here while calculating VIX:

1. Bid-Ask quotes
2. Time to expiry
3. Weightage
4. Risk free interest rates
5. Forward index level

At current level, Nifty is at 17850 and VIX is 16.9 so it indicates the volatility of 16.9% over the next year and for the next 30 days, the VIX of 16.9 is divided by square root of 12 ie 3.46 which comes to 4.88% move in Nifty.

Normally, a VIX level of 10-12 is considered as low whereas above 20 is considered as high. During the Covid-19 pandemic, India VIX even went above 80.

Here - orange = VIX and Blue = Nifty



Implications of VIX movement:

If the VIX is rising, it means that there is a higher probability of a far 'Out of the money' strike option expiring as 'At the money' or 'In the money'. Hence in this case, option premiums will be higher.

Lower VIX indicates stable market movement so the option premiums will be lower.

When VIX is rising, a net debit strategy can give good returns since it's a directional strategy while a net credit strategy when VIX is falling or low can give better returns as premiums are falling

VIX can also rise during the major financial events such as Union Budget, RBI policy or political events like state or general elections. Here the option premiums keep rising so option buying can give good returns.

And once this event concludes, VIX stabilises or falls so the option premiums can fall at a quick pace so here the option selling strategy can give good returns.