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**A STUDY ON THE CONVERGENCE OF  
FUTURES AND CASH PRICES AT MATURITY : EXPERIENCE OF  
KLSE COMPOSITE INDEX FUTURES AND KLIBOR FUTURES**

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## **ABSTRACT**

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**KEYWORDS** : Price Convergence, Cash, Futures, Basis, KLSE Composite Index, KLIBOR, Fair Value, Overpriced, Underpriced, Arbitraging, Market Efficiency, Mispricing

The main objective of this project paper is to get better understanding on financial futures market activity with reference to the convergence of cash and futures price for KLSE Composite Index Futures and KLIBOR Futures. This study tries to determine the convergence of cash and futures price at maturity using the basis. From that, the efficiency of the market will be determined. Besides that, this study will explore on the arbitraging activity that exists due to mispricing. The theoretical model of fair value is applied on the monthly basis for Composite Index and quarterly basis for KLIBOR in order to establish an arbitrage opportunity. The data of Composite Index prices cover the period from 15 December 1995 to 31 December 1999 and for KLIBOR prices cover from 1996 to 1999.

The findings show that what the traders' experience in practice actually doesn't really correlate with the theory stated. This statement is made due to the value of basis between cash and futures whereby the cash and futures prices do not converge at all at

maturity. The price discrepancies between cash and futures give an opportunity to an arbitrageur to do arbitrage. This study conclude that the prices of cash and futures do not converge at maturity as what it is stated in the theory but the market is still efficient if the value of the basis falls in the stated range and there is also an arbitrage opportunity for an arbitrageur.

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