ETFs) or “short positions” funds (Short ETFs). Among investors – the funds of the “bear” market (Bear ETFs) can apply for such role, or as they are known, funds as the perspective and innovative investment and hedging instrument for the Ukrainian equity market and the prospects of their appearance.

Key words – bear market, equity market, exchange traded fund, inverse traded fund, volatility, short sale.

Ukrainian equity market ended the year 2012 as also the year 2011 in the «red zone»: the equity market indices decline reached almost 40 percent yearly. In terms of the Ukrainian equity market indices and trading volume of the leading Ukrainian stock exchanges the market is practically on its very low of 2008-2009 crisis years. Despite the global trends of equity markets recovery, the decline of the Ukrainian equity market continues in 2013.

Short periods of recovery and growth in the Ukrainian equity market used to change for a long time decline. Amid high volatility of national equity market the liquidity of national equity market has fall sharply (by the data of the «Ukrainian accounting service center in contracts in the financial markets» the current money assets deposited on the Ukrainian Exchange to meet commitments on the market transactions decreased from their maximum level – 330 million UAH in 2011 to the level of 34 million UAH by the end of August 2013). During 2011-2013 the number of Ukrainian «blue chips» became much shorter, the bulk of the exchange trading volume is now concentrated around 3-5 index blue chips of Ukrainian Exchange and the futures contracts on this index. The activity of the major groups of investors, both private and institutional remains low; with foreign investors are practically ceased operations.

The high level of uncertainty of the future prospects for Ukrainian equity market in terms of global and national financial instability makes the actual implementation in practice of Ukraine's equity market innovative financial instruments that would allow investors to obtain the desired level of investment return during long-term “bear market”. The crisis of the Ukrainian equity market during 2008-2013 years has shown that when the whole market is rapidly going down, the investor's portfolio should have investment instruments that can mitigate this decline; instruments that shall give “inversion effect” to the market trend and bring profits on the “bear market”.

In our opinion, inverse exchange-traded funds (Inverse ETFs) can apply for such role, or as they are known among investors – the funds of the “bear” market (Bear ETFs) or “short positions” funds) (Short ETFs).

Exchange-traded funds (ETFs) have gotten increasingly popular since they were introduced in 1993. Their value is based on a portfolio of investments, often referred to as a basket. In general, the basket consists of different stocks, but may also contain hard commodities, derivatives or other investments. ETFs trade throughout the day just like a stock and their value will fluctuate throughout the trading session.

In other words ETFs – are the investment funds whose securities are freely traded on the stock exchanges as listed securities. Typically, the ETF’s portfolio corresponds to the composition and structure of the selected index (benchmark) or a composite index that reflects the dynamics of a particular sector of the financial market and the market in general. For example, the net asset value (NAV) of the top - 10 ETF in global markets is over 350 billion USD. The average trading volume of shares of the world's largest ETF on the S&P500 index (NAV - 135 billion USD) «SPDR S&P500 ETF - SPY» is 20-25 billion USD per day. (Fig.1)

The main founders and ETF’s management companies are Barclays Capital Inc, Blackrock Fund Advisors, Emerging Global Shares, Deutsche Bank AG, Fidelity Management & Research Company, Pimco, State Street Bank and Trust Company, Russell Investment Group, UBS Global Asset Management, Vanguard Group Inc.

The ETFs that present the inverse return to yield of the benchmark index are usually called as the inverse exchange traded funds; they are also very popular and high liquid investment and hedging instruments among investors. Thus, the average daily trading volume of the inverse ETF for the S&P500 index - «ProShares UltraShort S&P500 ETF» is 1 billion USD. (Fig.2)
The purpose of these inverse ETFs is to generate profits during the price decline of the reference index or benchmark. This is achieved by the use of the "short sale" technology that means the inverse ETF to "sell" borrowed assets in the market to make the "short position" on the reference index or benchmark. Thus, buying shares of the inverse ETF, the investor receives additional hedging for his portfolio during the market decline and gets inverse profits. The inverse ETFs work the next way: for example inverse S&P 500 ETF – SDS seeks a daily percentage movement opposite that of the S&P, if the S&P 500 rises by 1%, the inverse ETF is designed to fall by 1%; and if the S&P falls by 1%, the inverse ETF should rise by 1%. Among the benefits of inverse ETF are low transaction costs and no costs for paying credit percent for the "short - position on the instruments of the spot market or derivative market rollover. Investing in these ETFs is similar to holding various short positions, or using a combination of advanced investment strategies to profit from falling prices. In addition, it is possible to buy inverse ETFs that focus on a specific sector, such as financials, energy or consumer staples. The strategy of portfolio hedging with the inverse ETF is very profitable in the bear market. Also, it should be reminded that simple short sales have the potential to expose an investor to unlimited losses, whether or not the sale involves a stock or ETF. The inverse ETFs, on the other hand, provide many of the same benefits as shorting, yet it exposes an investor only to the loss of the purchase price.

In the Ukrainian equity market there is first - run exchange traded fund - non-diversified closed-end investment fund "Ukrainian Exchange Index" (KUBI) managed by "Kinto" asset management company. The "KUBI" net asset value by the end of August 2013 – was about 2.5 mln.UAH).

Before 2011, when KUBI was founded Ukrainian investors had positive experience working with classical non-diversified closed-end index investment funds managed by "Amadeus" and "Foil" asset management companies.

The lack of the exchange traded funds legal regulation has caused the underdevelopment of the ETFs sector in the Ukrainian equity market. However the registered project of the law "About collective investment institutions» № 9615 from 19.12.2011 in the Parliament of Ukraine, which will become the law starting from the 1-st of January 2014 is expected to define the main characteristics of exchange-traded funds. Although it should be noted that the authors of the law have limited the description of the ETFs only by classic exchange funds that are based on stock indexes, stocks and precious metals. Many varieties of modern exchange traded funds, based on a wide variety of benchmarks (government securities, oil, grains, etc.) and technologies leveraged ETFs under the following conditions of the current law have not yet been legally regulated. New legal framework for their legal regulation is yet required.

At the end it should be noted that even with imperfect regulatory framework the inverse exchange-traded funds are possible in Ukrainian equity market and we can expect their appearance in the coming few years after the current reform of stock market infrastructure.

Conclusion

In this article, the nature and the properties of the exchange traded funds within the inverse exchange traded funds and the prospects of their appearance in the Ukrainian equity market have been highlighted.

References