Investment Management

(As per New Syllabus (CBCS) for Fifth Semester, BBA, Bangalore University w.e.f. 2014-2015)

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Investment Management is a study of individual securities and their properties and the risk and return faced by them. A capital market has many instruments available for an individual investor. He has to take a decision as to which investments would be useful for him. Most investors do not like risk but enjoy the benefits of returns. The art of combining high risk and low risk investments will provide the investor with good results. Therefore, an investor has to plan his portfolio by choosing the right type of securities and constantly review it to get a feedback. An investor is surrounded by different types of risks such as systematic and unsystematic risks present in the market. Although unsystematic risk can be reduced, it is unique and it affects a particular organization or industry and so it can be controlled if the problems surrounding it can be identified and steps taken to rectify the situation. Systematic risk is broad spectrum and cannot be reduced. So, the best solution is to diversify into different securities which may help in reducing risks but not completely eliminating it. The book explains the different kinds of risks that surround the investors and how they can be controlled.

Some techniques of investments are discussed in which different securities can be combined to get a high return. It explains different theories of portfolio management and guides an investor to take correct decisions in combining their securities. Investor should take his own decisions through fundamental analysis, technical analysis and feedback and review.

This book has explained the online or depository system of trading in shares and the broker’s method of purchasing and selling securities. It has also discussed developments in the stock market since SEBI was instituted. The Fundamental Analysis, Technical Analysis and Efficient Market Theory have explained the various approaches to investment.

The theories of Harry Markowitz, William Sharpe, Capital Asset Pricing Model (CAPM) and Arbitrage Pricing Theory have been discussed for analyzing and diversifying the portfolio of an individual.

This book is useful for students of business management, commerce, accounting and finance. It is comprehensive and simple to make it readable and easy for students to comprehend.

My acknowledgements to my publishers M/s Himalaya Publishing House Pvt. Ltd. for their continuing faith and trust in entrusting me with writing of this subject to publish as a book for students.

My special thanks are to Brajendra Kumar for always being patient, dutiful and helpful in assisting me in the preparation of the manuscript of this book.

I would like to thank my colleagues and students from various colleges for giving me suggestions.

Finally, I would like to thank all my students for continuously supporting me and giving me suggestions for incorporating the text in this book.

Dr. Preeti Singh
SYLLABUS

Objectives
1. To enable develop skills in analyzing various types of securities.
2. To develop necessary skills in students to design and revise a portfolio of securities.

Unit 1: Introduction to Investment Management 10 Hrs

Unit 2: Securities Analysis 14 Hrs

Unit 3: Portfolio Management 10 Hrs

Unit 4: Portfolio Management Strategies 12 Hrs

Unit 5: Mutual Funds 10 Hrs

Skill Development
● Seminars, Group Discussion and Case Studies on various aspects of syllabus.
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UNIT I
INTRODUCTION TO INVESTMENT MANAGEMENT

Chapter 1: Investment Management – An Introduction
Chapter 2: Risk and Return
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1.1 INTRODUCTION TO INVESTMENT MANAGEMENT

Money does not have any value unless it is invested. If a person has a large sum of money and he keeps it in his cupboard, it will not grow. It has to be invested in some financial asset to get a return. There can be no return without risk. It is within this framework of risk and return that investment has to be made. It is assumed that a person is risk averse and at the same time, he expects a good return on the money that he invests. Therefore, an investor has to trade-off between risk and return. This chapter is an introduction to the terms investment, speculation and gambling depicting its nature and scope. It also presents the media for investments and explains the investment process.

Investment is the commitment of funds with a long-term time framework, the objective being additional income to regular receipts and growth in the value of funds of an investor. Investment involves ‘waiting’ for a future reward in terms of income through regular interest, dividends, premiums, or appreciation in the value of the principal capital. The term ‘Investment’ is understood differently by economists and financial experts. Economists consider it as new and productive capital and financial experts emphasize on allocation and transfer of resources from one person to another. It is also different to the terms speculation and gambling and they differ in terms of risk, time framework and gains.
• It must be clearly established that investment involves long-term commitment.
• Financial and economic meaning of investment are different and must be understood in terms of use of capital.
• Investment speculation and gambling can be distinguished from each other through their risk, time period of commitment and gains.

Importance of Investments

Investments are important due to increase in life expectancy of a person, planning for retirement income, high planning for additional income due to high rates of taxation and inflationary pressure in an economy, the expectation of continuous stable income in the form of regular dividends, interests and other receipts. The following discussion provides an explanation of these issues.

1. Longer Life Expectancy

Investment decisions have become significant because statistics show that life expectancy has increased with good medical care. People usually retire between the ages of 60 and 65. The income shrinks at the time of retirement because the annual inflow of earnings from employment stops. If savings are invested at the right age and time, wealth increases if the principal sum is invested adequately in different saving schemes.

The importance of investment decisions is enhanced by the fact that there is an increasing number of women working in the organizations. Men and women are responsible for planning their own investments during their working life so that after retirement they are able to have a stable income through balanced investments.

2. Taxation

Taxation introduces an element of compulsion in a person’s savings. Every country has different tax saving schemes for bringing down taxation levels of a person. Since investments provide regular and stable income and also give relief in taxation, they are considered to be very important and useful if investments are made by proper planning.

3. Interest Rates

Interest rates vary according to the choice of investment outlet. Investors prefer safe investments with a good return. A risk-less security will bring low rates of return. Government securities are risk-free. However, market risk is high with high rates of return. Before allocations of any amount, the different types of securities must be analyzed to calculate their benefits and their disadvantages. The investor should make his portfolio with several kinds of investments. Stability of interest is as important as receiving a high rate of interest. This book is concerned with determining that the investor is getting an acceptable return commensurate with the risks that are taken.

4. Inflation

In a developing economy, there are rising prices and inflationary trends. A rise in prices has several problems coupled with a falling standard of living. Before funds are invested, they must be evaluated to find the right choice of investments to tide over inflationary situations. The investor will
look at different investment outlets and compare the rate of return/interest to cover the risk of inflation. Security and safety of capital is important. Therefore, he/she should invest in those securities that have an assured and regular return. An investor has to consider, the taxation benefit decides the safety of capital and its continuous return.

5. Income

Investment decisions are important due the general increase in employment opportunities and an understanding of investment channels for saving in India. New and well paying job opportunities are in sectors like software technology; business processing offices, call centres, exports, media, tourism, hospitality, manufacturing sector, banks, insurance and financial services. The employment opportunities gave rise to increasing incomes. Higher income has increased a demand for investments and earnings above the regular income of people. Investment outlets can be selected to make investments for supporting the regular income. Awareness of financial assets and real assets has led to the ability and willingness of working people to save and invest their funds for return in their lean period leading to the importance of investments.

6. Investment Outlets

The availability of a large number of investment outlets has made investments useful and important. Apart from putting aside savings in savings banks where interest is low, investors have the choice of a variety of instruments. The question to reason out is which is the most suitable channel? Which investment will give a balanced growth and stability of return? The investor in his choice of investment has the objective of a proper mix between high rate of return and stability of return to get the benefits of both types of investments.

Thus, the objectives of investment are to achieve a good rate of return in the future, reducing risk to get a good return, liquidity in time of emergencies, safety of funds by selecting the right avenues of investments and a hedge against inflation.

1.2 NATURE AND SCOPE OF INVESTMENT MANAGEMENT

Nature and scope of investment can be determined from the meaning of financial investments and how it is different from economic investment. It is also determined from the time period and the risk and its differences with speculation, gambling and arbitrage.

The nature of scope of investment management is:

- To understand the exact meaning of investment
- To find out different avenues of investment
- To maximize return and minimize risk
- To make a programme for investment through evaluating securities, constructing a portfolio and reviewing a portfolio
- To find out a time period for investments to take place
- To evaluate through various techniques to get the best return for the investor
Financial and Economic Meaning of Investment

Financial Investments are the allocation of monetary resources ranging from risk-free to risky investments and with the expectation of a good return that varies with risk. The investor has to aim at a trade-off between risk and return. The investors are the suppliers of ‘capital’ and in their view, investment is a commitment of a person’s funds to derive future income in the form of interest, dividends, rent, premiums, pension benefits or the appreciation of the value of their principal capital. To the financial investor, it is not important whether money is invested for a productive use or for the purchase of secondhand instruments such as existing shares and stocks listed on the stock exchanges. Most investments are considered to be transfers of financial assets from one person to another.

The economist understands the term ‘Investment’ as net additions to the economy’s capital stock which consists of goods and services that are used in the production of other goods and services. For them, the term investment implies the formation of new and productive capital in the form of new construction, new producers’ durable equipment such as plant and equipment, including inventories and human capital.

The financial and economic meaning of investment cannot be separated because the term draws a relationship with the economists and financial experts. Investment is a part of the savings of individuals which flow into the capital market either directly or through institutions; they may be divided in ‘new’ or ‘secondhand’ capital financing. Investors as ‘suppliers’ and ‘investor as ‘users’ of long-term funds find a meeting place in the market.

In this book, however, investment is used in its financial sense and investment will include those instruments and institutional media into which savings are placed.

Investment and Speculation

Investment is distinguished from speculation in three ways which are based on the factors of risk, time period and gains.

1. Risk

The term ‘risk’ has significance in the financial meaning of investment. Whatever amount is invested has the probability of incurring a gain or a loss in a financial transaction. Investment is not considered to involve high risk but it has limited risk and risk can be calculated through different techniques and the capital can be invested in avenues where the principal is safe. ‘Speculation’ is correlated with ‘high risk’ and short commitment. There are degrees of risk, and arbitrary judgements are made between high risk and low risk. An investor cannot have completely risk-free investments because there are certain non-controllable risks that cannot be calculated. The purchasing power risk or the fall in the real value of the interest and principal is beyond the control of a person. The money rate risk or the fall in market value, with the rise in interest rates also cannot be controlled.

These risks affect both the speculator and the investor. High risk and low risk are, therefore, general indicators to help an understanding between the terms investment and speculation.
2. Capital Gain

Speculation is buying low and selling high in a short time to make large capital gains. The motive in speculation is primarily to achieve profits through price changes. This can be distinguished from investment where securities are purchased by an investor through proper evaluation, analysis and review with the view of receiving a stable return over a long-term period of time.

3. Time

Time period explains the difference between investment and speculation. A fund allocation over a long-term period is called investment. A short-term holding is associated with trading for the ‘quick turn’ and is called speculation. The speculator is not interested in holding a security for current income but for high short-term gains.

The distinctions between investment and speculation help to identify the role of the investor and speculator. To summarize the above discussion:

1. The investor constantly evaluates the worth of a security through fundamental analysis, whereas the speculator is interested in market action and price movement.

2. There is a very fine line of division between investment and speculation. There are no established rules and laws that identify securities which are permanently for investment. There has to be a constant review of securities to find out whether it is a suitable investment for long-term or for quick turn of speculative profit. Long-term commitment becomes investment of the same security which if sold immediately on purchase only for profit becomes speculation.

3. Some financial experts have called investment ‘a well grounded and carefully planned speculation’, or good investment is a successful speculation. Speculation is planned short-term investment based on haunches and beliefs. Investment is planned, evaluated and analyzed long-term commitment of funds.

4. Speculation is to achieve high returns though risk of loss is high. Investments are for minimizing risk of investors with the expectation of high returns. Therefore, investment and speculation are a planning of risks.

5. A speculator expects high return for his investment and to make gains, he can commit his own funds as well as use borrowed funds. An investor is cautious by nature and usually uses his own funds for investing in securities.

The distinction between investment and speculation is given in Table 1.1.
**Table 1.1: Distinction between Investment and Speculation**

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<th><strong>Investment</strong></th>
<th><strong>Speculation</strong></th>
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<tr>
<td>Time Horizon</td>
<td>Long-term time framework beyond 12 months.</td>
<td>Short-term planning holding assets even for one day.</td>
</tr>
<tr>
<td>Risk</td>
<td>It has limited risk.</td>
<td>High Returns though risk of loss is high.</td>
</tr>
<tr>
<td>Return</td>
<td>It is consistent and moderate over a long period.</td>
<td>There are high profits and gains as well as high losses. It is not consistent.</td>
</tr>
<tr>
<td>Use of funds</td>
<td>The investor uses his own funds through savings.</td>
<td>Speculation is through own and borrowed funds.</td>
</tr>
<tr>
<td>Decisions</td>
<td>Safety, liquidity, profitability and stability considerations and performance of companies.</td>
<td>Market behavior information, judgments on movement in the stock market, haunches and beliefs.</td>
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**Investment and Gambling**

Gambling is artificial and unnecessary risk created for increased expected returns. The difference between investment and gambling is very clear. From the above discussion, it is established that **investment** is an attempt to carefully plan, evaluate and allocate funds in various investment outlets which offers safety of principal, moderate and continuous returns and long-term commitment.

Gambling is quite the opposite of investment. It connotes high risk and the expectation of high returns. It consists of uncertainty and high stakes for thrill and excitement. Typical examples of gambling are horse racing, game of cards, lottery, etc. Gambling is based on tips, rumors and haunches. It is unplanned, non-scientific and without knowledge of the exact nature of risk.

The distinctions between investment, speculation and gambling give us a basic idea of their nature, purpose and role.

**Investment and Arbitrage**

**Investment** is planned commitment of funds from a person’s savings into different outlets with the expectation of safe, stable and fare return. **Arbitrage** is the mechanism of minimizing risk through hedging and taking advantage of price differences in different markets. An arbitrage transaction is the simultaneous purchase of the same or similar security in two different markets. Short-term gains can be expected through such transactions. An investor can also be an arbitrageur if he buys and sells securities in more than one stock exchange to take advantage of the price differentials in such exchanges. Derivatives introduced in the Indian market have a great potential for arbitrage transactions. Arbitrage transactions help in enhancing efficiency and liquidity in the stock market and in increasing the volume of trade. Hedgers, speculators and arbitrageurs can minimize risks and make profits through the arbitrage process.

**1.3 TYPES OF REAL AND FINANCIAL ASSETS**

Real assets are tangible goods in possession of a person. Financial securities represent papers that are dependent on real assets for creating wealth.
1. Real Assets

Real assets are used to produce goods or services. They are tangible assets that have a physical form. Some examples of real assets are land and buildings, furniture, gold, silver, diamonds or artifacts. They may be marketable or non-marketable. They may also have the feature of being moveable or non-moveable.

2. Financial Assets

Financial assets are called *paper securities*. Some examples of these assets are shares, bonds, debentures, bills, loans, lease, derivatives and fixed deposits. Financial assets represent a claim by securities, on the income generated by real assets of some other parties. Such assets can be easily traded, as they are marketable and transferable. Financial assets are transactions between two or more parties. For example, if a person takes an insurance policy of ₹1,00,000 of Life Insurance Corporation, the contract is a liability of LIC but an asset of the person insuring himself because he has a claim over the insurance company to receive the principal sum with interest on the happening of an event or on the completion of a certain number of years.

<table>
<thead>
<tr>
<th>Table 1.2: Distinction between Real and Financial Assets</th>
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<tbody>
<tr>
<td>Real Assets</td>
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<tr>
<td>Land and building, furniture and machinery.</td>
</tr>
<tr>
<td>Tangible assets moveable, immoveable, marketable and non-marketable.</td>
</tr>
<tr>
<td>Theses assets are used for production of goods and services.</td>
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3. Commodity Assets

Commodities are a new form of investment in India. Examples of commodity assets are wheat, sugar, potatoes, rubber, coffee and other grains. Commodities are also in the form of metal like gold, silver, aluminum and copper. Cotton, crude oil and foreign currency are other examples of commodities. Importers and exporters invest in commodities to diversify their portfolios. Traders hedge or transact in commodities to make gains. A National Commodity and Derivatives Exchange Ltd. (NCDEX) has been set up in India in 2003 as a public limited company to transact in commodities.

The promoters of NCDEX were ICICI Bank Ltd., National Bank for Agriculture and Rural Development (NABARD), Life Insurance Corporation of India, Punjab National Bank, Canara Bank, CRISIL Ltd., Indian Farmers Fertilizer Cooperative Ltd. (IFFCO) and National Stock Exchange of India Ltd. (NSE). All these institutions subscribed to the equity shares of NCDEX.

The above explanations of the terms of investment have provided a background to the meaning of investment. This chapter now presents the importance of investments, opportunities conducive to investment, media available for investment, investment features and the process of investment.
1.4 INVESTMENT AVENUES

Many types of investment avenues or channels for making investments are available. A sound investment programme can be constructed if the investor familiarizes himself with the various alternative investments available. Investment media are of several kinds – some are simple and direct, others present complex problems of analysis and investigations. Some investments are appropriate for one type of investor and another may be suitable to another person.

The ultimate objective of the investor is to derive a variety of investments that meet this preference for risk and expected return. The investor will select the portfolio, which will maximize his utility. Securities present a wide range of risk-free instruments to highly speculative shares and debentures. From this broad spectrum, the investor will have to select those securities that maximize his utility. The investor, in other words, has an optimization problem. He has to choose the security, which will maximize his expected returns subject to certain considerations. The investment decision is an optimization problem but the objective function varies from investor to investor. It is not only the construction of a portfolio that will promise the highest expected return but it is the satisfaction of the need of the investor. For instance, one investor may face a situation when he requires extreme liquidity. He may also want safety of securities. Therefore, he will have to choose a security with low returns. Another investor would not mind high risk because he does not have financial problems but he would like a high return. Such an investor can put his savings in growth shares, as he is willing to accept the risk. Another important consideration is the temperament and psychology of the investor. Some investors are temperamentally suited to take risks; there are others who are not willing to invest in risky securities even if the return is high. One investor may prefer safe government bonds whereas another may be willing to invest in blue chip equity shares of the company.

Many alternative investments exist. These can be categorized in many ways. The investment alternatives/avenues are given below in Figure 1.1.

![Fig. 1.1: Investment Avenues](image-url)
The investment avenues have been categorized as direct and indirect investment alternatives/avenues. Direct investments are those where the individual makes his own choice and investment decision. Indirect investments are those in which the individual has no direct hold on the amount he invests. He contributes his savings to certain organizations like Life Insurance Corporation (LIC) or Unit Trust of India (UTI) and depends upon them to make investments on his and other people’s behalf. So, there is no direct responsibility or hold on the securities.

An individual also makes indirect investment for retirement benefits, in the form of provident funds and pension, life insurance policy, investment company securities and securities of mutual funds. Individuals have no control over these investments. They are entrusted to take care of the particular organization. In the organizations like Life Insurance Corporation or Unit Trust of India, provident funds are managed according to their investment policy by a group of trustees on behalf of the investor. The examples of indirect investment alternatives are an important and rapidly growing segment of our economy. In choosing specific investments, investors will need definite ideas regarding a number of features that their portfolio should have. To summarize:

- Direct investments are those where the individual has a direct hold on his investment decision.
- Indirect investments are those where the investor is dependent on another organization.

1. Risk-less vs. Risky Investments

Most investors are risk averse but they expect maximum return from their investments. Every investment must be analyzed because there is some risk in it. Only government securities are risk-less. The Indian investment scene has many schemes to offer to an individual. On an analysis of these schemes, it appears that the investor has a wide choice. A vast range of investments is in the government sector. These are mostly risk-free but low return yielding. Several incentives are attached to it. The private sector investments consist of equity and preference shares, debentures and financial engineering securities. These have the features of high risk. Ultimately, the investor must make his investment decisions.

The dilemma faced by the Indian investor is the reconciliation of profitability, liquidity and risk of investments. Government securities are risk-free and the investor is secured. However, to him, the return or yield is very important as he has limited resources and would like to plan an appreciation of the investments for his future requirements. Government securities give low returns and do not fulfil his objective of money appreciation.

Private sector securities are attractive, though risky. Reliance, Infosys, Wipro and Tatas give to the investor the expectation of future appreciation of investment by several times. The multinational and blue chip companies offer very high rates of return and also give bonus shares to their shareholders.

Real Estate and Gold have the advantage of eliminating the impact of inflation, since the price rises experienced by them have been very high. The Indian investor in this context cannot choose his investments very easily.
An investor can maximize returns with minimum risk involved if he carefully analyzes the information published in the prospectuses of private companies. Contents as the past performance, name of promoters and board of directors, the main activities, its business prospects and selling arrangements should be assessed before the investor decides to invest in the company.

From the point of view of an investor, convertible bonds may under proper conditions, prove an ideal combination of high yield, low risk and potential of capital appreciation.

2. Fixed and Variable Principal Securities

Fixed principal investments are classified as those whose principal amount and the terminal value are known with certainty. Cash has a definite and constant rupee value, whether it is deposited in a bank or kept in a cash box. It does not earn any return. Savings accounts have a fixed return; they differ only in terms of time period. The principal amount is fixed plus interest is earned on the deposit. Savings certificates are classified as national savings certificates, bank savings certificates and postal savings certificates. Government bonds, corporate bonds and debentures are sold having a fixed maturity value and a fixed rate of income overtime.

The variable principal securities differ from the fixed principal securities because their terminal values are not known with certainty. The price of preference shares is determined by demand and supply forces even though preference shareholders have a fixed return. Equity shares also have no fixed return or maturity date. Convertible securities such as convertible debentures or preference shares can convert themselves into equity shares according to certain prescribed conditions and thus have features of fixed principal securities supplemented by the possibility of a variable terminal value. Debentures, preference shares and equity shares are examples of securities sold by companies to investors to raise necessary funds. To summarize:

- Fixed securities terminal values are certain with fixed return and maturity dates.
- Variable principal securities terminal values are uncertain. Their price is determined by demand and supply mechanism.

3. Non-security Investments

‘Non-security Investments’ differ from securities in other categories. Real estate may be the ownership of a single home or include residential and commercial properties. The terminal value of real estate is uncertain but generally there is a price appreciation, whereas depreciation can be claimed in tax. Real estate is less liquid than corporate securities. Mortgages represent the financing of real estate. It has a periodic fixed income and the principal is recovered at a stated maturity date. Commodities are bought and sold in spot markets; contracts to buy and sell commodities at a future date are traded in future markets. Business ventures refer to direct ownership investments in new or growing business before firms sell securities on a public basis. Art, antiques and other valuables such as silver, fine China and jewels are also another type of specialized investments which offer aesthetic qualities also.
These features should be consistent with the investors’ objectives and in addition should have additional conveniences and advantages. The following features are suggested for a successful selection of investments.

4. Features of Investment Avenues

The features of an investment programme consists of safety of principal, liquidity, income stability, adequate income, purchasing power, stability, appreciation, freedom from management of investments, legality and transferability.

Safety of Principal

The investor, to be certain of the safety of principal, should carefully review the economic and industry trends before choosing the types of investment. To ensure safety of principal, the investor should consider diversification of assets. Adequate diversification involves mixing investment commitments by industry, geographically, by management, by financial type and by maturities. A proper combination of these factors would reduce the risk of loss. Diversification in proper investment programmes must be reasonably accomplished.

Liquidity

An investor requires a minimum amount of liquidity in his investments to meet emergencies. Liquidity will be ensured if the investor buys a proportion of readily saleable securities out of his total portfolio. He may, therefore, keep a small proportion of cash, fixed deposits and units which can be immediately made liquid. Investments like stocks and property or real estate cannot ensure immediate liquidity.

Income Stability

Regularity of income at a consistent rate is necessary in any investment pattern. Not only stability, it is also important to see that income is adequate after taxes. It is possible to find out some good securities which pay practically all their earnings in dividends.

Appreciation and Purchasing Power Stability

Investors should balance their portfolios to fight against any purchasing power instability. Investors should judge price level inflation, explore the possibility of gain and loss in the investments available to them, limitations of personal and family considerations. The investors should also try and forecast which securities will appreciate. A purchase of property at the right time will lead to appreciation in time. Growth stock will also appreciate over time. These, however, should be done through analysis and not as speculation or gamble.

Legality and Freedom from Care

All investments should be approved by law. Law relating to minors, estates, trusts, shares and insurance be studied. Illegal securities will bring out many problems for the investors. One way of being free from care is to invest in securities like Unit Trust of India, Life Insurance Corporation, mutual funds or savings certificates. The management of securities is then left to the care of the Trust who diversifies the investments according to safety, stability and liquidity with the consideration of
their investment policy. The identity of legal securities and investments in such securities will also help the investor in avoiding many problems.

**Tangibility**

Intangible securities have many times lost their value due to price level inflation, confiscatory laws or social collapse. Some investors prefer to keep a part of their wealth invested in tangible properties like building, machinery and land. It may, however, be considered that tangible property does not yield an income apart from the direct satisfaction of possession or property.

**Table 1.3: Features of Investment Avenues**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Risk</th>
<th>Return/Current Yield</th>
<th>Capital Appropriation</th>
<th>Liquidity/Marketability</th>
<th>Tax Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity Shares</td>
<td>High</td>
<td>Low</td>
<td>High</td>
<td>High</td>
<td>High</td>
</tr>
<tr>
<td>Debentures</td>
<td>Low</td>
<td>High</td>
<td>Very low</td>
<td>Very low</td>
<td>Nil</td>
</tr>
<tr>
<td>Bank Deposit</td>
<td>Low</td>
<td>Low</td>
<td>Nil</td>
<td>High</td>
<td>Nil</td>
</tr>
<tr>
<td>Public Provident Fund</td>
<td>Nil</td>
<td>Nil</td>
<td>Low</td>
<td>Low</td>
<td>Moderate</td>
</tr>
<tr>
<td>Life Insurance Policies</td>
<td>Nil</td>
<td>Nil</td>
<td>Low</td>
<td>Low</td>
<td>Moderate</td>
</tr>
<tr>
<td>Real Estate</td>
<td>Low</td>
<td>Low</td>
<td>High in Long-term</td>
<td>Moderate</td>
<td>Changes according to rules</td>
</tr>
<tr>
<td>Gold and Silver</td>
<td>Low</td>
<td>Nil</td>
<td>High in Long-term</td>
<td>Moderate</td>
<td>Nil</td>
</tr>
</tbody>
</table>

Investment is a study of employment of funds for the purpose of a return to the investor. It is of long-term horizon and it has to be planned through a proper process of evaluation. The investment process consists of different stages such as preparing an investment policy, making investment analysis, valuation of securities, portfolio construction and review.

**1.5 POINTS TO REMEMBER**

- Investment is employment of funds for achieving additional income and growth in value.
- Investment must be distinguished from speculation and gambling in terms of time horizon, risk, return and decision-making process. Investment is usually planned whereas speculation and gambling depend on immediate decisions with also the element of ‘luck’.
- Investments are transfers of financial assets from one person to another. They range from low risk to high risk.
- Investments are usually long-term and low risk. Speculation is high risk and high return and for short-term period of time.
- Investments may be financial claims or real and tangible assets like land and buildings, plant and machinery, gold, antiques, etc.
- Investment may be direct and indirect securities like shares and debentures. Investments in provident funds, pension funds and mutual funds are forms of indirect investments.
An investment programme should consist of safety of the principal amount, liquidity, income and purchasing power stability and appreciation.

The investment process consists of four stages. These are investment policy, investment analysis, valuation of securities, and portfolio construction and review.

1.6 QUESTIONS

1. Why do people invest? What are the factors which are favourable for making investments in an economy?

2. What is the meaning of investment? Discuss the different channels or alternatives available to an investor for making investments.

3. Describe the importance of an investment programme. What steps should an investor follow to make an investment?

4. Distinguish between investment, speculation and gambling. What is the usefulness of a sound investment plan?

5. Write notes on:
   (i) Commodity assets
   (ii) Process of investment
   (iii) Investment alternatives

6. Distinguish between:
   (i) Direct and indirect assets
   (ii) Real and financial assets
   (iii) Investment and arbitrage

7. Explain the nature and scope of investment management.

1.7 OBJECTIVE TYPE QUESTIONS

State whether the following statements are True (T) or False (F).

1. Investments are concerned with risk and return.

2. Investments involve long-term commitments.

3. Speculation brings about stable return for long-term period of time.

4. Speculation is considered with review and analysis and investments with capital gain.

5. Investments are based on portfolio construction, valuation, identification and analysis.

6. The variable investments consist of cash, bonds and savings certificates.

7. The investment objective is high risk and high return.

8. Arbitrage is a long-term investment.
9. The commodity investment is through saving bank.
10. Indirect securities consist of mutual fund and life insurance securities.


**Multiple Choice Questions**

1. Investment means ____________.
   (a) commitment of funds for future income
   (b) net additions to economy capital stock
   (c) short-term commitment of funds
   (d) capital gain

2. Speculation can be distinguished from investment in the following way:
   (a) Investment is high risk speculation is low risk.
   (b) Investment is short-term period of time speculation covers long-term period.
   (c) Investment is based on planning of funds for safety, liquidity, profitability, speculation on haunches and benefits.
   (d) Investment is your own funds, speculation consists of other people’s funds.

3. A gambler is one who makes planned investment and ____________.
   (a) believes in low risk
   (b) considers high risk and high profits
   (c) expects other people to plan his resources in one best security
   (d) buying government securities with safety of return

**Ans.:** 1. (a), 2. (c), 3. (b).

* * *