NPTEL

Course Name: Security Analysis and Portfolio Management

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Session 2: Markets for Investment and Construction of Indexes

1. What are the different investment alternatives provided by different financial markets?

Ans.

Marketable and Non-Marketable Assets:

- Marketable: Investor can manage and control, Less Liquid in Nature: All the Market Traded Securities
- Non-Marketable: No management but has Right, Highly Liquid: Bank Deposits, Post office Deposits, NSC etc.

Direct Vs. Indirect Investments:

- Direct Investment: Investor—(owns)---Portfolio--- (Dividend and Interest)---Income and Capital gain
- Indirect Investments: Investor—(owns)---Investment Company's Fund---(Dividend and Interest)---Income and Capital gain

Classification of Financial Markets:

- Nature of Claims: Debt Market, Equity Market
- Maturity of Claims: Money Market, Capital Market
- Seasoning of Claims: Primary Market, Secondary Market
- Timing of Delivery: Cash or Spot Market, Forward or Futures Market
- Organizational Structure: Exchange Traded Market, Over the Counter Market

2. What is the difference between Primary market and secondary market?

Ans.

Primary market

- The primary market is that part of the capital markets that deals with the issuance of new securities. Primary market provides opportunity to issuers of securities, Government as well as corporate, to raise resources to meet their requirements of investment and/or discharge some obligation.
- Equity Capital is raised in Primary Market. It can be raised through Public or primary Issue, Right Issue, Private Placement, Preferential Allotment
- The primary market is governed by the provisions of the Companies Act, 1956, which deals with issues, listing and allotment of securities. Additionally the SEBI - prescribes the eligibility and disclosure norms to be complied by the issuer, promoter for accessing the market.

Secondary Market

- Existing securities issued in the primary market are traded
- This market enables participants who held securities to adjust their holdings in response to changes in their assessment of risks and returns.
- It operates through over-the-counter (OTC) market and the exchange traded market.
- Operation of Secondary Market: Trading , Settlement
- Trading: Can be Open Outcry System and/or Screen-Based System.
  Under Open Outcry System traders shout and resort to signals on the trading floor of the exchange which consists of several trading posts for different securities. Buyers make their bids and sellers make their offers and bargains are closed at mutually agreed-upon prices. Under Screen-Based System Buyers and sellers place their orders on the computer. They can be limit order or best market price order. The computer constantly tries to match mutually compatible orders on price and time priority.
- Modern settlement system is an electronic delivery mechanism: It is facilitated by Depositories which is an institution which dematerializes physical certificates and effects transfer of ownership by electronic book entries. Settlement Procedure can be Weekly Settlement, Carry forward system (badla and undha badla), Rolling Settlement (T+1)

3. What is the meaning of margin trading and what are the major concepts associated with it?

Ans.

- Margin Trading: This is the part of a transaction value that a customer has equity in the transaction. Use of Margin: to buy more, to borrow money

  Concepts associated with margin:

- Initial margin: Amount Investor Puts up / value of transaction or It is the part of transaction's value the customer must pay to initiate the transaction with other part being borrowed from the broker.
- Maintenance Margin: The percentage of a security's value that must be on hand as equity.
- Margin Call: Demand from the broker for additional cash or securities as a result of the actual margin declining below the maintenance margin

4. Why stock market index is importance and what are the factors affecting construction of stock market index?

Ans.

A good Stock Index captures the movement of the well diversified and highly liquid stocks. It is the pulse rate of the economy. Index movements reflect the changing expectations of the stock market about future dividends of the corporate sector.

Importance of Stock Market Index

- To judge the performance of individual investor
- To measure the market rates of return
- To predict the market movements

Factors affecting the construction of stock market index

- Sample: It should be representative of total population
- Base year: It should be a normal year
- Weighting criteria
  - Equally Weighted Series
  - Price Weighted Series
  - Market value Weighted Series