A STUDY ON PORTFOLIO MANAGEMENT WITH REFERENCE TO KARVY

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ABSTRACT

Portfolio Management is used to select a portfolio of new product development projects to achieve the following goals:

- Maximize the profitability or value of the portfolio
- Provide balance
- Support the strategy of the enterprise

Portfolio Management is the responsibility of the senior management team of an organization or business unit. This team, which might be called the Product Committee, meets regularly to manage the product pipeline and make decisions about the product portfolio. Often, this is the same group that conducts the stage-gate reviews in the organization.

A logical starting point is to create a product strategy - markets, customers, products, strategy approach, competitive emphasis, etc. The second step is to understand the budget or resources available to balance the portfolio against. Third, each project must be assessed for profitability (rewards), investment requirements (resources), risks, and other appropriate factors.

The weighting of the goals in making decisions about products varies from company. But organizations must balance these goals: risk vs. profitability, new products vs. improvements, strategy fit vs. reward, market vs. product line, long-term vs. short-term. Several types of techniques have been used to support the portfolio management process:

- Heuristic models
- Scoring techniques
- Visual or mapping techniques

The earliest Portfolio Management techniques optimized projects' profitability or financial returns using heuristic or mathematical models. However, this approach paid little attention to balance or aligning the portfolio to the organization's strategy. Scoring techniques weight and score criteria to take into account investment requirements, profitability, risk and strategic alignment. The shortcoming with this approach can be an over emphasis on financial measures and an inability to optimize the mix of projects.

I. INTRODUCTION

PORTFOLIO MANAGEMENT MEANING:

A portfolio is a collection of assets. The assets may be physical or financial like Shares, Bonds, Debentures, Preference Shares, etc. The individual investor or a fund manager would not like to put all his money in the shares of one company that would amount to great risk. He would therefore, follow the age old maxim that one should not put all the eggs into one basket. By doing so, he can achieve objective to maximize portfolio return and at the same time minimizing the portfolio risk by diversification.

- Portfolio management is the management of various financial assets which comprise the portfolio.

- Portfolio management is a decision – support system that is designed with a view to meet the multi-faced needs of investors.

- According to Securities and Exchange Board of India Portfolio Manager is defined as: “Portfolio means the total holdings of securities belonging to any person".

- **PORTFOLIO MANAGER** means any person who pursuant to a contract or arrangement with a client, advises or directs or undertakes on behalf of the client (whether as a discretionary portfolio manager or otherwise) the management or administration of a portfolio of securities or the funds of the client.
- **DISCRETIONARY PORTFOLIO MANAGER** means a portfolio manager who exercises or may, under a contract relating to portfolio management exercises any degree of discretion as to the investments or management of the portfolio of securities or the funds of the client.

FUNCTIONS OF PORTFOLIO MANAGEMENT:

- To frame the investment strategy and select an investment mix to achieve the desired investment objectives
- To provide a balanced portfolio which not only can hedge against the inflation but can also optimize returns with the associated degree of risk
- To make timely buying and selling of securities
- To maximize the after-tax return by investing in various tax saving investment instruments.

CHARACTERISTICS OF PORTFOLIO MANAGEMENT:

Individuals will benefit immensely by taking portfolio management services for the following reasons:

- Whatever may be the status of the capital market, over the long period capital markets have given an excellent return when compared to other forms of investment. The return from bank deposits, units, etc., is much less than from the stock market.
- The Indian Stock Markets are very complicated. Though there are thousands of companies that are listed only a few hundred which have the necessary liquidity. Even among these, only some have the growth prospects which are conducive for investment. It is impossible for any individual wishing to invest and sit down and analyze all these intricacies of the market unless he does nothing else.
- Even if an investor is able to understand the intricacies of the market and separate chaff from the grain the trading practices in India are so complicated that it is really a difficult task for an investor to trade in all the major exchanges of India, look after his deliveries and payments

NEED & IMPORTANCE OF STUDY:

Portfolio management has emerged as a separate academic discipline in India. Portfolio theory that deals with the rational investment decision-making process has now become an integral part of financial literature.

Investing in securities such as shares, debentures & bonds is profitable well as exciting. It is indeed rewarding but involves a great deal of risk & need artistic skill. Investing in financial securities is now considered to be one of the most risky avenues of investment. It is rare to find investors investing their entire savings in a single security. Instead, they tend to invest in a group of securities. Such group of securities is called as PORTFOLIO. Creation of portfolio helps to reduce risk without sacrificing returns. Portfolio management deals with the analysis of individual securities as well as with the theory & practice of optimally combining securities into portfolios.

The modern theory is of the view that by diversification, risk can be reduced. The investor can make diversification either by having a large number of shares of companies in different regions, in different industries or those producing different types of product lines. Modern theory believes in the perspective of combinations of securities under constraints of risk and return.

SCOPE OF STUDY:

This study covers the Markowitz model. The study covers the calculation of correlations between the different securities in order to find out at what percentage funds should be invested among the companies in the portfolio. Also the study includes the calculation of individual Standard Deviation of securities and ends at the calculation of weights of individual securities involved in the portfolio. These percentages help in allocating the funds available for investment based on risky portfolios.

OBJECTIVES OF THE STUDY:

- To study the investment pattern and its related risks & returns In **Karvy Stock Broking Limited**.
- To find out optimal portfolio of **Karvy Stock Broking Limited**, which gave optimal return at a minimize risk to the investor in **Karvy Stock Broking Limited**.
- To see whether the portfolio risk is less than individual risk on whose basis the portfolios are constituted
- To see whether the selected portfolios is yielding a satisfactory and constant return to the investor
- To understand, analyze and select the best portfolio

II. METHODOLOGY AND FRAMEWORK

DATA COLLECTION METHODS

The data collection methods include both the primary and secondary collection methods.

Primary collection methods:

This method includes the data collection from the personal discussion with the authorized clerks and members of the anjali financial services.

Secondary collection methods:

The secondary collection methods includes the lectures of the superintend of the department of market operations and so on., also the data collected from the news, magazines and different books issues of this study Superintend

LIMITATIONS OF THE STUDY

1. Construction of Portfolio is restricted to two companies based on Markowitz model.
2. Very few and randomly selected scripts / companies are analyzed from BSE listings.
3. Data collection was strictly confined to secondary source. No primary data is associated with the project.
4. Detailed study of the topic was not possible due to limited size of the project.
5. There was a constraint with regard to time allocation for the research study i.e. for a period of two months.

III. DISCRETIONARY PORTFOLIO MANAGEMENT SERVICE (DPMS):

In this type of service, the client parts with his money in favor of the manager, who in return, handles all the paper work, makes all the decisions and gives a good return on the investment and charges fees. In the Discretionary Portfolio Management Service, to maximize the yield, almost all portfolio managers park the funds in the money market securities such as overnight market, 18 days treasury bills and 90 days commercial bills. Normally, the return of such investment varies from 14 to 18 percent, depending on the call money rates prevailing at the time of investment.

NON-DISCRETIONARY PORTFOLIO MANAGEMENT SERVICE (NDPMS):

The manager functions as a counselor, but the investor is free to accept or reject the manager‘s advice; the paper work is also undertaken by manager for a service charge. The manager concentrates on stock market instruments with a portfolio tailor-made to the risk taking ability of the investor.

CRITERIA FOR PORTFOLIO DECISIONS:

In portfolio management emphasis is put on identifying the collective importance of all investor's holdings. The emphasis shifts from individual assets selection to a more balanced emphasis on diversification and risk-return interrelationships of individual assets within the portfolio. Individual securities are important only to the extent they affect the aggregate portfolio. In short, all decisions should focus on the impact which the decision will have on the aggregate portfolio of all the assets held.

- Portfolio strategy should be molded to the unique needs and characteristics of the portfolio‘s owner.
- Diversification across securities will reduce a portfolio‘s risk. If the risk and return are lower than the desired level, leverages (borrowing) can be used to achieve the desired level.
- Larger portfolio returns come only with larger portfolio risk. The most important decision to make is the amount of risk which is acceptable.
- The risk associated with a security type depends on when the investment will be liquidated. Risk is reduced by selecting securities with a payoff close to when the portfolio is to be liquidated.
- Competition for abnormal returns is extensive, so one has to be careful in evaluating the risk and return from securities. Imbalances do not last long and one has to act fast to profit from exceptional opportunities.

PORTFOLIO BUILDING:

Portfolio decisions for an individual investor are influenced by a wide variety of factors. Individuals differ greatly in their circumstances and therefore, a financial programme well suited to one individual may be inappropriate for another. Ideally, an individual‘s portfolio should be tailor-made to fit one‘s individual needs.

Investor‘s Characteristics:

An analysis of an individual‘s investment situation requires a study of personal characteristics such as age, health conditions, personal habits, family responsibilities, business or professional situation, and tax status, all of which affect the investor‘s willingness to assume risk.

Stage in the Life Cycle:

One of the most important factors affecting the individual‘s investment objective is his stage in the life cycle. A young person may put greater emphasis on growth and lesser emphasis on liquidity. He can afford to wait for realization of capital gains as his time horizon is large.

Family responsibilities:

The investor‘s marital status and his responsibilities towards other members of the family can have a large impact on his investment needs and goals.

Investor‘s experience:

The success of portfolio depends upon the investor‘s knowledge and experience in financial matters. If an investor has an aptitude for financial affairs, he may wish to be more aggressive in his investments.

Attitude towards Risk:

A person‘s psychological make-up and financial position dictate his ability to assume the risk. Different kinds of securities have different kinds of risks. The higher the risk, the greater the opportunity for higher gain or loss.

Liquidity Needs:

Liquidity needs vary considerably among individual investors. Investors with regular income from other sources may not worry much about instantaneous liquidity, but individuals who depend heavily upon investment for meeting their general or specific needs, must plan portfolio to match their liquidity needs. Liquidity can be obtained in two ways:

1. By allocating an appropriate percentage of the portfolio to bank deposits, and

2. By requiring that bonds and equities purchased be highly marketable.

Tax considerations:

Since different individuals, depending upon their incomes, are subjected to different marginal rates of taxes, tax considerations become most important factor in individual's portfolio strategy. There are differing tax treatments for investment in various kinds of assets.

Time Horizon:

In investment planning, time horizon becomes an important consideration. It is highly variable from individual to individual. Individuals in their young age have long time horizon for planning, they can smooth out and absorb the ups and downs of risky combination. Individuals who are old have smaller time horizon, they generally tend to avoid volatile portfolios.

IV. PORTFOLIO ANALYSIS:

Various groups of securities when held together behave in a different manner and give interest payments and dividends also, which are different to the analysis of individual securities. A combination of securities held together will give a beneficial result if they are grouped in a manner to secure higher return after taking into consideration the risk element.

There are two approaches in construction of the portfolio of securities. They are

- Traditional approach
- Modern approach

TRADITIONAL APPROACH:

Traditional approach was based on the fact that risk could be measured on each individual security through the process of finding out the standard deviation and that security should be chosen where the deviation was the lowest. Traditional approach believes that the market is inefficient and the fundamental analyst can take advantage of the situation. Traditional approach is a comprehensive financial plan for the individual. It takes into account the individual need such as housing, life insurance and pension plans. Traditional approach basically deals with two major decisions. They are

a) Determining the objectives of the portfolio

b) Selection of securities to be included in the portfolio

MODERN APPROACH:

Modern approach theory was brought out by Markowitz and Sharpe. It is the combination of securities to get the most efficient portfolio. Combination of securities can be made in many ways. Markowitz developed the theory of diversification through scientific reasoning and method. Modern portfolio theory believes in the maximization of return through a combination of securities. The modern approach discusses the relationship between different securities and then draws inter-relationships of risks between them. Markowitz gives more attention to the process of selecting the portfolio. It does not deal with the individual needs.

MARKOWITZ MODEL:

Markowitz model is a theoretical framework for analysis of risk and return and their relationships. He used statistical analysis for the measurement of risk and mathematical programming for selection of assets in a portfolio in an efficient manner. Markowitz apporach determines for the investor the efficient set of portfolio through three important variables i.e.

- Return
- Standard deviation
- Co-efficient of correlation

Markowitz model is also called as an "Full Covariance Model". Through this model the investor can find out the efficient set of portfolio by finding out the trade off between risk and return, between the limits of zero and infinity. According to this theory, the effects of one security purchase over the effects of the other security purchase are taken into consideration and then the results are evaluated. Most people agree that holding two stocks is less risky than holding one stock. For example, holding stocks from textile, banking and electronic companies is better than investing all the money on the textile company's stock.

Markowitz had given up the single stock portfolio and introduced diversification. The single stock portfolio would be preferable if the investor is perfectly certain that his expectation of highest return would turn out to be real. In the world of uncertainty, most of the risk adverse investors would like to join Markowitz rather than keeping a single stock, because diversification reduces the risk

V. CONCLUSIONS

In case of perfectly correlated securities or stocks, the risk can be reduced to a minimum point.

In case of negatively correlative securities the risk can be reduced to a zero.(which is company's risk) but the market risk prevails the same for the security or stock in the portfolio.

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