Third Edition

Security Analysis and Portfolio Management

S. Kevin

This new edition of the book explains in detail the two phases of wealth creation through investment in securities. The first phase *Security Analysis* deals with the selection of securities for investment. The book begins with an introduction to the investment process and a familiarization of the securities market environment and the trading system in India followed by different dimensions of the risk involved in investment. The different methods of security analysis such as Fundamental analysis (including economy, industry and company analysis), Technical Analysis and Random Walk Theory (including Efficient Market Hypothesis) are explained in different chapters. The valuation of securities such as equity shares and bonds is illustrated with examples.

The second phase *Portfolio Management* includes different processes such as portfolio analysis, portfolio selection, portfolio revision and portfolio evaluation. These processes are explained in different chapters. Pricing theories such as Capital Asset Pricing Model (CAPM), Arbitrage Pricing Theory (APT), and Fama French Three Factor Model are explained with suitable examples. The book provides an introduction (in four chapters) to Financial Derivatives (Futures and Options) used for hedging the risk in investment. Behavioural Finance—the new investment theory—is also discussed in this edition. Each chapter of the book is supported with examples, review questions and practice exercises to facilitate learning of concepts and theories.

The book is intended to serve as a basic textbook for the students of finance, commerce and management. It will also be useful to the students pursuing professional courses such as chartered accountancy (CA), cost and management accountancy (CMA), and chartered financial analysis (CFA). The professionals in the field of investment will find this book to be of immense value in enhancing their knowledge.

NEW TO THIS EDITION

- A new chapter on Behavioural Finance – The New Investment Theory
- A new section on Fama French Three Factor Model
- Revisions in different chapters

THE AUTHOR

S. KEVIN (Ph.D.) has over 40 years of experience in teaching Commerce and Management courses at the postgraduate level. He served as Professor of Commerce and Pro-Vice-Chancellor at the University of Kerala. He also served as the Director of TKM Institute of Management and the Director and Dean of Management Studies at Bishop Jerome Institute, Kollam (Kerala). His areas of specialization are financial management, investment management, international finance, and derivatives. He has published several research articles in scholarly research journals such as Finance India, Productivity, Economic and Political Weekly of India, Decision, Yojana, International Journal of Management and Systems, etc. He has published three more books for the students of finance – all published by PHI Learning.

Other books by the author

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Third Edition

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To
My beloved parents
Stephen *and* ***Mary***

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PREFACE

Security Analysis and Portfolio Management are the two different phases of wealth creation through investment in securities. Security Analysis helps to select the securities that have good potential for growth. These securities are identified with the help of different types of analysis such as Fundamental analysis (of Economy, Industry and Company), Technical analysis and Market efficiency analysis (based on Efficient Market Hypothesis). These securities can be purchased from the securities market which comprises of primary market and secondary market (stock exchanges). Investment in these securities is expected to generate positive return in the future; but, as the future is uncertain, there is an element of risk in such investment. Thus, return and risk are two interrelated features of investment in securities.

Wealth creation requires that the investor should maximize the return from investment and minimize the risk involved in it. One of the methods of minimizing risk is diversification of investment which can be done through the creation of a portfolio of different types of securities. An investor can design an optimal portfolio that will not only minimize the risk but also maximize the return. Portfolio Management is the process of designing and creating an optimal portfolio, revising such portfolio periodically to ensure that it continues to be optimal and finally evaluating the performance of the portfolio. Capital Asset Pricing Model (CAPM) and Arbitrage Pricing Theory (APT) help in the estimation of the expected return of a portfolio which is a critical input for determining the success of portfolio management.

An alternative method of risk reduction in investment is the use of derivative instruments which are of recent origin. Forwards, Futures, Options and Swaps are the basic derivative instruments used for the purpose. The risk involved in the trading of an asset for investment purpose can be hedged (minimized) with the use of derivative instruments which is a novel practice in the financial markets.

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