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A Conceptual Study of Portfolio Management

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Abstract

Investment is an activity that commits funds in any financial form in the present with an expectation of receiving additional return in the future. The expectations bring with it a probability that the quantum of return may vary from a minimum to a maximum. This possibility of variation in the actual return is known as investment risk. Thus, every investment involves a return and risk. Investment is an activity that is undertaken by those who have savings. Savings can be defined as the excess of income over expenditure. An investor earns/expects to earn additional monetary value from the mode of investment that could be in the form of financial assets. The unique goals and circumstances of the investors must also be considered some investors are more risk averse than others. mutual fund have developed particular to optimize their portfolio holding.

I.INTRODUCTION

Portfolio management refers to the management or administration of a portfolio of securities to protect and enhance the value of the underlying investment. It is the management of various securities share bonds etc and other assets eg real estate to meet specified investment goals for the investor.it helps to reduce risk without sacrificing return. it involves a proper investment decision with regards to what to buy and sell.it involves proper money management. It is known as investment management. Portfolio management involves deciding what asset to purchase how many to purchase, when to purchase them, and what asset to divest. These decisions always involve some sort of performance measurement, most typically expected return on the portfolio, and the risk associated with this return i.e standard deviation of the return typically the expected return from portfolio of different asset bundles is compared. Portfolio management involves maintaining a proper combination of securities which comprise the investors portfolio in a manner that they give maximum return with minimum risk. This requires framing of proper investment policy. Investment policy means formation of guidelines for allocation of available funds among the various types of securities including variation in such proportion under changing environment. This requires proper mix between different securities in a manner that it can maximize the return with minimum risk to the investors. Broadly speaking investors are those individuals who save money and invest in the market in order to get return over it. They are not much educated expert and they do not have time to carry out detailed study. they have their business life, family life, as well as social life and the time left out is very much limited to study for investment purpose on the other hand institutional investors are companies mutual fund, investment banking, stock broking and life insurance company who have surplus fund which needs to be invested profitably. These investors have time and resources to carry out detailed research for the purpose of investing.

Challenges of Indian Investment Industry:

The investing story in India has not been always that smooth. Pitfalls are sure to co-exist. The main hurdle on India's growth now is its infrastructure. On the other hand, infrastructure is India's biggest opportunity as well. The fiscal deficit of India also poses a big threat to the investment industry in India. For an emerging economy like India, it is recommended that an investor always balances the unique risks against the potential for high long-term growth. Accordingly, the decision for investment should be made. Of late, the Indian economy is turning out to be extremely conducive in terms of domestic and foreign investments. India Investments has been the major propelling force towards India's attainment of self-sustained growth by way of rapid industrialization. The pioneers of the investment industry have been Foreign Direct Investment (FDI) and Investments made by NRIs. Foreign Direct Investments in India has been gearing up momentum every passing day. So, to view an economy which is entirely open to the global markets, the investment industry in India should be groomed in a manner that the maximum returns are achieved. It is advisable that the investment industry's potential should neither be overestimated nor underestimated. We should know how to deal with the complexities of the investment industry and grow along with it.

Function of Portfolio management

- To frame the investment strategy and select an investment mix to achieve the desired investment objectives.
- To make timely buying and selling of securities.
- To maximise the after-tax return by investing in various tax saving 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 analyse 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.

Importance of Portfolio management

- Emergence of institutional investing on behalf of individuals. A number of financial institutions, mutual funds and other agencies are undertaking the task of investing money of small investors, on their behalf.
- Growth in the number and size of investible funds – a large part of household savings is being directed towards financial assets.
- Increased market volatility – risk and return parameters of financial assets are continuously changing because of frequent changes in government's industrial and fiscal policies, economic uncertainty and instability.
- Greater use of computers for processing mass of data.

- Professionalization of the field and increasing use of analytical methods e.g. quantitative techniques in the investment decision – making
- Larger direct and indirect costs of errors or shortfalls in meeting portfolio objectives – increased competition and greater scrutiny by investors.

Steps in portfolio management

Step1: Specification and qualification of investor objectives, constraints, and preferences in the form of an investment policy statement.

Step 2: Determination and qualification of capital market expectations for the economy, market sectors, industries and individual securities.

Step 3: Allocation of assets and determination of appropriate portfolio strategies for each asset class and selection of individual securities.

Step 4: Performance measurement and evaluation to ensure attainment of investor objectives.

Step 5: Monitoring portfolio factors and responding to changes in investor objectives, constrains and / or capital market expectations.

Step 6: Rebalancing the portfolio, when necessary, by repeating the asset allocation, portfolio strategy and security selection.

Risk And Expected Return

There is a positive relationship between the amount of risk and the amount of expected return i.e., the greater the risk, the larger the expected return and larger the chances of substantial loss. One of the most difficult problems for an investor is to estimate the highest level of risk he is able to assume.

1. Risk is measured along the horizontal axis and increases from the left to right.
2. Expected rate of return is measured on the vertical axis and rises from bottom to top.
3. The line from 0 to R (f) is called the rate of return or risk less investments commonly associated with the yield on government securities.
4. The diagonal line form R (f) to E(r) illustrates the concept of expected rate of return increasing as level of risk increases.

Evaluation of Portfolio:

Portfolio manager evaluates his portfolio performance and identifies the sources of strengths and weakness. The evaluation of the portfolio provides feedback about the performance to evolve better management strategy. Even though evaluation of portfolio performance is considered to be the last stage of investment process, it is a continuous process. There are number of situations in which an evaluation becomes necessary and important.

i. Self-Valuation: An individual may want to evaluate how well he has done. This is a part of the process of refining his skills and improving his performance over a period of time.

ii. Evaluation of Managers*:* A mutual fund or similar organization might want to evaluate its managers. A mutual fund may have several managers each running a separate fund or sub-fund. It is often necessary to compare the performance of these managers.

iii. Evaluation of Mutual Funds: An investor may want to evaluate the various mutual funds operating in the country to decide which, if any, of these should be chosen for investment. A similar need arises in the case of individuals or organisations who engage external agencies for portfolio advisory services.

iv. Evaluation of Groups: Academics or researchers may want to evaluate the performance of a whole group of investors and compare it with another group of investors who use different techniques or who have different skills or access to different information.

Portfolio Revision

The portfolio which is once selected has to be continuously reviewed over a period of time and then revised depending on the objectives of the investor. The care taken in construction of portfolio should be extended to the review and revision of the portfolio. Fluctuations that occur in the equity prices cause substantial gain or loss to the investors. The investor should have competence and skill in the revision of the portfolio. The portfolio management process needs frequent changes in the composition of stocks and bonds. In securities, the type of securities to be held should be revised according to the portfolio policy. An investor purchases stock according to his objectives and return risk framework. The prices of stock that he purchases fluctuate, each stock having its own cycle of fluctuations. These price fluctuations may be related to economic activity in a country or due to other changed circumstances in the market is able to forecast these changes by developing a framework for the future through If an investor careful analysis of the behavior and movement of stock prices is in a position to make higher profit than if he was to simply buy securities and hold them through the process of diversification. Mechanical methods are adopted to earn better profit through proper timing. The investor uses formula plans to help him in making decisions for the future by exploiting the fluctuations in prices.

II.CONCLUSION

Portfolio can be constructed with the help of traditional approach and modern approach. The main objectives of portfolio management is to keep the investors in investing in various securities. So, the risk is to be minimized and to get higher yield of return. In traditional approach the constraints, investors need for current income and constant income are analysed. Investors prefer safe and secured investment avenues. The investors had been facing various risk in their investment like depression phase in market, fall in sensex/ nifty, inflation, fluctuations in interest rates, global turnaround and recession. It can be concluded that inflation period has impact on the savings as it increases the expenses and also affects the overall economy/market. Thus, inflation acts as risk involved in investment portfolio.

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