INVESTMENT MANAGEMENT

Chapter One

Introduction to Investment Management

Unit Introduction

"An investment operation is one which, upon thorough analysis, promises safety of principal and an adequate return. Operations not meeting these requirements are speculative."

- By Graham and Qadd's Security Analysis

"Investment Management is the process of managing money, including investments, budgeting, banking, and taxes, also called money management."

Investment management is the major factor that contributes to managing a variety of equities, including stock holdings, bond funds, and other investments, including property investment, to meet specific financial objectives for the benefit of shareholders. Investment management is also known as wealth management or portfolio management. Investors can be institutions, including insurance firms, pension plans, corporations, charitable organizations, educational facilities, or investment firms. Investments can be made directly through financing or, more commonly, through mutual fund schemes, including mutual funds, marketplace funds, or real estate investment trusts (REITs) (Singh, 2012).

The administration of investment funds is frequently referred to as "asset management." Still, the more general phrase "capital management" could refer to any institutional investments in addition to capital management for individual investors. When discussing their activities within the framework of "private banking," investment firms specializing in advising or discretionary managing on account of private companies (who are typically wealthy) may frequently refer to their operations as managing money or portfolio management. When managing a client's wealth, financial planners adopt a more comprehensive perspective, allocating funds to various asset management techniques (Avadhani, 2010).

The phrase "fund manager" can relate to either a company that offers investment advisory services or even the individual who leads fund management choices within U.S. inside the United Kingdom, the term "investment adviser" is used instead (Bhalla, 2008).

Based on research conducted by the Boston Consulting Group, the value of assets handled professionally for fees hit an all-time high of $62.4 trillion in 2012 after being unchanged since 2007. It was then anticipated that this value would reach $70.2 trillion the following year.

The five largest investment firms are responsible for managing 22.7 % of such assets that third parties own. Nevertheless, according to the Herfindahl-Hirschmann Index, the market penetration in 2018 was assessed to be 173.4, indicating that the sector is not overly concentrated (Vishwanath & Krishnamurti, 2009).

Learning Objective

At the end of this chapter, students will be able to:

1. Define Investment Management
2. Explain the characteristics of investment
3. Discuss Investment activity
4. Discuss factors influencing investment

Key Terms

1. Investment
2. Investment activity
3. Speculation
4. Gambling
5. Investor

1.1. Meaning and Concept of Investment

In finance and economics, "investment" refers to several closely related concepts.

Investment according to Theoretical Economics

Production of capital goods—items that are not utilized but rather utilized in further production—is an investment.

Examples of this

1. Building
2. A railroad
3. Land clearance by a factory
4. Putting oneself through college (Barton & Oliveros, 2019).

Investment according to Finance Term

Investment is the acquisition of assets. As An Example

1. Purchasing bonds and stocks
2. Real estate investment
3. Mortgages (Leontiev, 2020).

Then, these assets can provide a future income source and value appreciation (i.e., investing in real estate).

Investment, according to Oxford Dictionary

Investment refers to financial investment.

Investment from an Individual Point of View

Investments are financial commitments of some kind. For example (Gaillard, 2009).

1.2. Characteristics of Investment

The term "investment" refers to putting money into marketable and tangible capital instruments. Massive investments include risk, return, safety, liquidity, marketability, concealability, capital growth, purchasing power, stability, and benefits (Barua & Sharma, 2010).

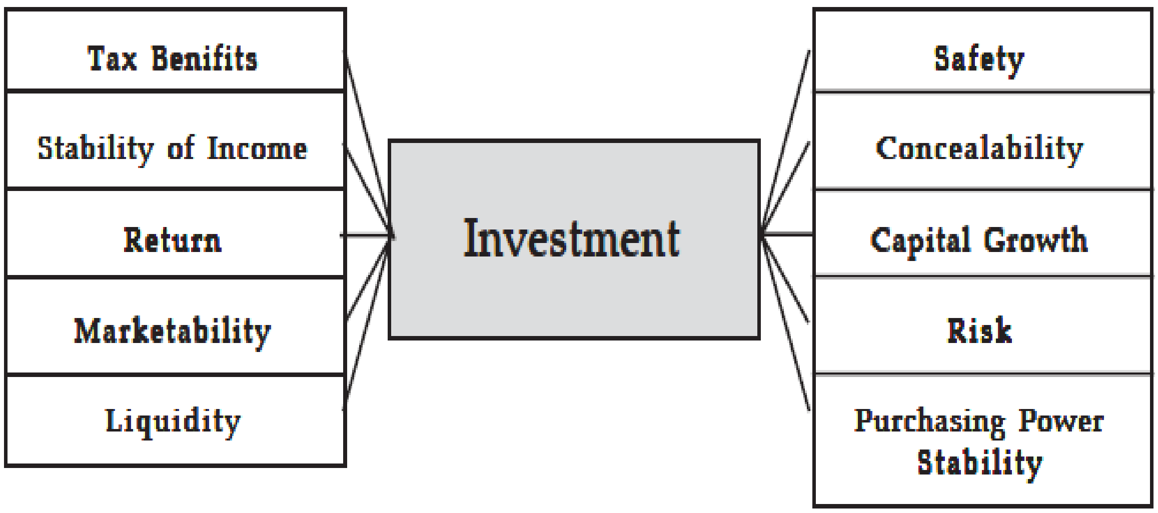

Figure 1.1. Characteristics of Investment (Source: Oreilly.com, Creative Commons License).

Did you know?

Features of an investment programme consist of the following factors:

1. Safety of principal amount
2. Liquidity of the investment
3. Income stability of the investment
4. Appreciation and purchasing power stability of the investor investment
5. Legality and freedom from care about the investment
6. Tangibility of the investment

Figure 1.1 shows the following list of significant qualities of investments:

1. Risk
2. Return
3. Safety
4. Liquidity
5. Marketability
6. Concealability
7. Capital growth
8. Purchasing power stability
9. Stability of income
10. Tax benefits (Wei & Yao, 2015).

Risk

Risk is the possibility of losing the capital of an investment. Among an investment's key qualities, it.

The following variables affect risk:

1. As a result of the extended investment time of maturity, an investor would assume greater risk.
2. Governmental and semi-government entities are producing less risky securities.
3. According to the protected and set interest paid on debt instruments with fixed deposits, the hazard of the aforesaid investment is lower. Consider debentures (Merolla et al., 2014).
4. According to their unsecured status, variable return, and owning nature, ownership instruments like equities or parameters to determine to carry a higher risk.

5. When comparing ownership investment to borrowed capital, the risk of level of returns unpredictability is higher.
6. The tax regulations would affect the return upon risk (Jorion, 2000).

Return

Return is the term for the anticipated rate of return on investment.

One crucial aspect of return investment. Return is indeed the primary element that affects the investor's investing patterns. Investors seek investments with a high return on investment (Fullan, 2000).

Safety

The preservation of an investor's initial investment and anticipated rate of return is referred to as safety.

One of the fundamental components of investment is protection. Investors seek security for their money. Capital guarantees returns without financial loss or a long period to keep it. Government bonds are the choice of the investor who desires lower-risk investments. Private securities are preferred by investors who want a higher rate of return since they offer less security (Dekker, 2014).

Liquidity

A liquid investment is prepared to be converted into cash. In those other terms, it is instantly accessible in cash. Liquidity is the ability of an investment to be quickly realized, sold, or placed on the market. The return could be poor when liquidity is strong. Consider UTI units. Any investor often favors assets with liquidity, security of funds with low risk, and maximizing return on investment (Brunnermeier, 2009).

Marketability

Marketability is the ability to acquire and sell securities on an open market. Marketability refers to an asset's ability to be transferred or sold. Securities that can be sold more quickly than those not registered are listed on a stock exchange. Shareholders of limited public corporations can be transferred more readily than privately owned firms.

Concealability

Another crucial aspect of an investment is its capacity to remain undetectable. In addition, for an investment to be protected against societal unrest, government asset seizures, or excessive taxes, it needs to be easy to conceal and leave no trace of the money it has brought in through usage or sale. Since they combine great value with tiny mass and are easily transferrable, gold or precious gems have long been valued for these purposes (Longstaff, 1995).

Capital Growth

Capital growth is the term for investment development. Currently, capital growth has emerged as a key characteristic of investments. It acknowledges the link between strong corporate and industrial growth and high capital appreciation. Investors and advisors always look for "growth stocks" purchased at the appropriate moment and in the correct industry (Le Forestier et al., 2022).

Purchasing Power Stability

It is a reference to a market's purchasing power. Investments now need to have buying power consistency as among their key characteristics. Investments always imply committing current funds to get larger future income (MacLean & Ziemba, 2011).

Stability of Income

It speaks of a consistent investment return. Revenue stability is one of the Investment's key distinguishing characteristics. Just as primary security requires a distinct approach, income stability does too. Each investor takes into account the stability of their financial income as well as the stability of their buying power (Taylor, 2006).

Tax Benefits

The investment's last distinguishing quality is tax advantages. Tax advantages relate to designing an investment plan while taking one's status into account, which might be expensive for the investor. In reality, there are two issues:

a. One who is interested in the profits the investment generates.
b. The cost of taxable income upon the revenue is another (Gennetian et al ., 2018).

1.3. Need and Importance of Investments

An investment is just a significant and practical element in the framework of the modern world. Some elements are crucial. They are listed as follows:

1. More longevity or retirement planning
2. Taxes that are being increased
3. High rates of interest
4. High inflation rate
5. Higher-income
6. Accessibility to a wide range of investment opportunities (Эшов, 2020).

Longer Life Expectancy

Given that most Indians retire between the ages of 56 and 60, investment choices have become more important. They want to save money as a result. Savings on their own do not lead to a rise in wealth; rather, savings should be invested effectively so that the primary income will last longer throughout retirement. An extended life expectancy is a factor in successful savings and additional investment activities that support investment choices (De la Croix & Licandro, 1999).

Increasing Rates of Taxation

As tax rates are raised, the emphasis will be on helping taxpayers save money. A taxpayer's tax liability is impacted by their investments in provident funds, pension funds, Unit Trust of India, health insurance, unit-linked insurance providers, National Savings Certifications, developmental bonds, postal service cumulative direct investments, etc. (Hartman, 2002).

Interest Rates

One of the crucial components of a wise investment strategy is the interest rate. The rate of interest varies depending on the type of investment. Risk level and safety investments might alter over time. They could vary due to the various benefit plans that the organizations provide. Factors besides a high-interest rate may well favor the outlet for investment. Obtaining high-interest rates depends on the interest rate's current stability (Black, 1995).

Inflation

The issue of inflation now persists. It has an impact on price increases. A declining level of living is accompanied and linked by several issues. Investors' thorough examination of inflation will thus postpone subsequent investment processes. The investor is sure to verify the investment's safety and the safety of the principal amount. First, both are essential from the perspective of the interest earned from assets (Guth, 2000).

Income

Another crucial component of an investment is revenue. Whenever the government offers jobs to the jobless citizens of the nation, the end consequence is income assurance rather than saving more money. The capacity and desire of working-class people to save but also invest their money has increased due to higher salaries and much more investment opportunities (Ferrer-i-Carbonell, 2005).

Investment Channels

Due to the nation's advancement and growth, many different investment channels have now increased economic success. Investment pathways signify a person's willingness to invest in various products, such as unit trust programs, corporate shares, provident funds, health insurance, and corporation fixed deposit accounts (Asongu, 2013).

1.4. Investment Activity

Purchases, sales of capital instruments, and tangible assets, including marketable investments on secondary and primary markets, are all considered investments. The process of putting money or savings towards purchasing new assets or continuing to create current ones are referred to as investing. The activity with investments is shown in Figure 1.2. As a result, investment activity involves the purchase of assets such as:

1. Financial Assets
2. Physical Assets
3. Assets may be sold in secondary and primary markets (Tyebjee & Bruno, 1984).

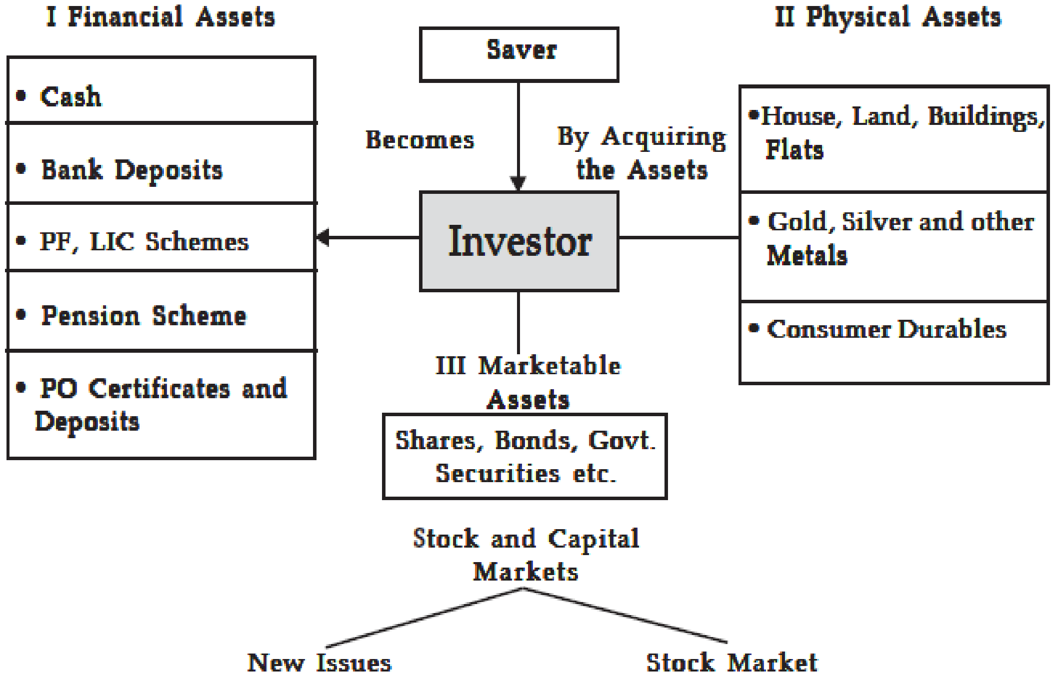

Figure 1.2. Investment Profession (Source: Vecteezy.com, Creative Commons License).

Financial Assets are:

1. Cash
2. Bank Deposits
3. P.F.
4. LIC Schemes
5. Pension Scheme
6. Certificates and Deposits from the Post Office (Karolyi & Stulz, 2003).

Physical Assets are:

1. Buildings, Land, Homes, and Apartments
2. Metals like gold, silver, and others
3. Consumer Durables

Marketable Assets are:

1. Shares
2. Bonds
3. Government Securities
4. M.F. Schemes
5. UTI Units etc.

The use of money or savings towards purchasing new assets or the continued creation of current ones is referred to as investing (Musa & Ahmad, 2012).

1.5. Investment for Consumption and Business

Two parts of the income are separated, namely:

a. Consumption
b. Investment

Money that is not spent is kept and invested. Investments in consumer durable goods, automobiles, silver, and gold are also beneficial for current and future usage. However, investments often encourage more spending in the future since they increase future revenue or capital gains. Some corporate investments are put to use in commerce, transportation, as well as other services. Professionals like physicians, attorneys, and dealers spend money to invest in their businesses, resulting in increased income consumption (Balta & Ruscher, 2013).

Importance of Financial and Physical Investment

Savers often prefer physical assets that are less efficient and rarely provide revenue. These investments include buying non-durable and durable everyday items, gold, silver, vehicles, antiquities, or "curios." These include meeting the immediate demands of the customer in terms of comfort, extravagance, social standing, ego-building, etc. If they are located in desirable or commercial regions, few can generate revenue through renting these to others and occasionally even capital growth. Similarly, without providing a consistent source of income, silver, gold, and other metals, jewels, and antiquities may show capital growth. Some investments, such as gold, diamonds, jewelry, etc., are made for social prestige and status (Schmitt-Grohé & Uribe, 2011).

1.6. Factors Influencing Investment

The investment includes the purchase of tangible, monetary, and marketable resources. Regulatory safeguards, a strong currency, the presence of banking firms to promote saving, and modes of corporate organization are all elements that impact investor decisions over which investment opportunities to pursue (Obamuyi, 2013).

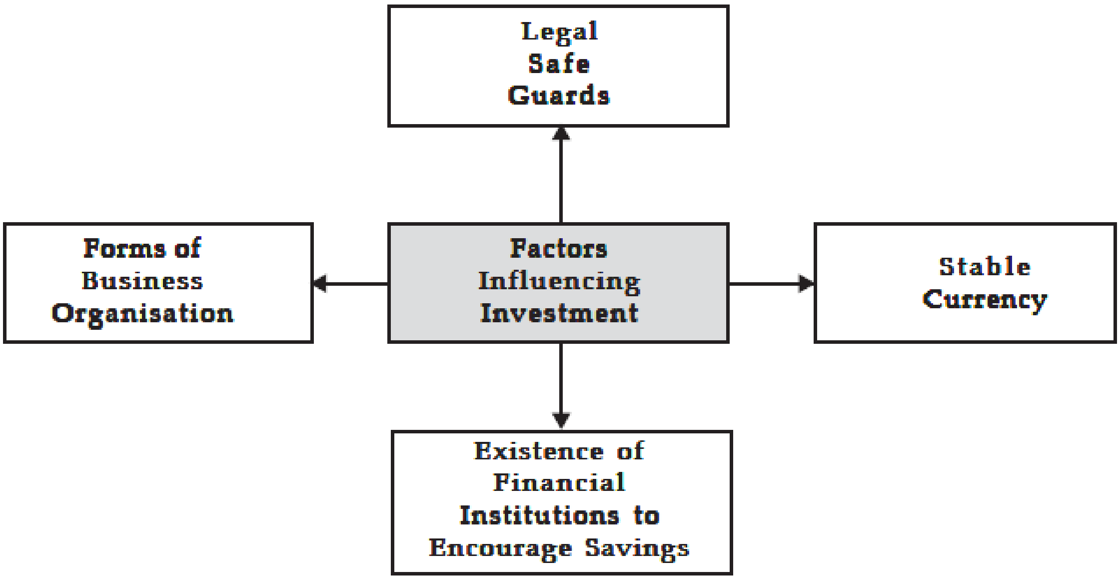

Figure 1.3. Investment Influencing Factors (Source: Wang Bo., Creative Commons License).

Remember:

An investing must have a well-organized monetary system including clear planning and appropriate policies.

Figure 1.3 depicts the following investment-influencing factors:

a. Legal safeguards
b. Stable currency
c. Financial institutions exist to promote saving
d. Form of business organization (Dash, 2010).

Legal Safeguards

A strong government carries appropriate legal protections that promote investment and savings growth. Investors would be eager to put their money into the market. They want the government to guarantee and defend their property ownership (Wamae, 2013).

Investors in India are in a unique position.

1. Free enterprise
2. Government control

India's economy is diverse. To attain the advantages of both socialist/communist and capitalist types of governance without even any drawbacks, it promotes the mixture of the government service, which itself is managed either by the government, as well as the private industry, that is allowed free to function (Mutswenje, 2009).

A Stable Currency

An investing must have a well-organized monetary system, including clear planning and appropriate policies. Most assets, including bank deposits, health insurance, and stocks, are paid in a set amount of domestic currency. A financial system that is appropriate and well-organized would influence the investment channels. As a result, the monetary policy shouldn't encourage intense inflationary forces or be ready for a deflationary model. They are both undesirable. As a result,

a. Investment buying power is ruined by price inflation.
b. Deflation is similarly harmful since it tends to decrease the nominal values of inventory, equipment, and buildings in addition to land and other fixed assets.

In addition to providing investor protection, prudent and well-planned fiscal and financial management supports proper control, effective governance, economic well-being, and a well-regulated, growth-oriented securities market (Wamae, 2013).

Existence of Financial Institutions to Encourage Savings

Availability of financial firms that promote saving and guide it toward productive investment through the expansion of an investment industry in most nations, banking firms are typically present.

1. Commercial Banks
2. Life Insurance Companies
3. Investment Companies.

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1. Industrial Development Bank of India (IDBI) (Shideler & Kraybill, 2009).
2. Industrial Credit Investment Corporation of India (ICICI)
3. Industrial Finance Corporation of India (IFCI)
4. State Financial Corporations
5. National Bank of Agriculture and Rural Development (NABARD)
6. Commercial Banks
7. Co-operative Banks
8. Life Insurance Corporation

9. Unit Trust of India
10. Development Banks

These financial organizations provide various programs to promote investing and saving. (Mwangi, 2011).

1.7. Forms of Business Organization

1. Company
2. Sole Trading Concern
3. Partnership Firms
4. HUF

These are several configurations of a business. The type of corporate organization that is always present facilitates saving and investing. The ideal business organization for investment is a public limited company (Chilver, 1984).

For the following purposes, limited public businesses are particularly beneficial to investors:

1. Limited Liability of Shareholders
2. Perpetual Life and Transferability
3. Divisibility of Stock and Shares
4. The capacity to go on with business regardless of the membership
5. It ensures the stability and durability of corporate operations.

Due to the following factors, investors cannot benefit from a sole proprietorship, partnerships, or Hindu undivided families:

1. Owners, investors, and members are subject to unlimited responsibility (Tulsian, 2002).
2. It causes the organization to have a limited lifespan.

Investors are still not prepared to invest under such circumstances since their investments are neither safe nor secure.

The public limited liability corporation is a well-liked financial vehicle. Investors are drawn to publicly traded companies for the reasons listed below. As follows:

i. Liquidity
ii. Convenience
iii. Longevity
iv. Stable return (Rutten, 2003).

1.8. The Investment Process/Stages

Investment method is referred to as investment strategy, financial analysis, securities evaluation, and appropriate portfolio creation (Pashkevich et al., 2022).

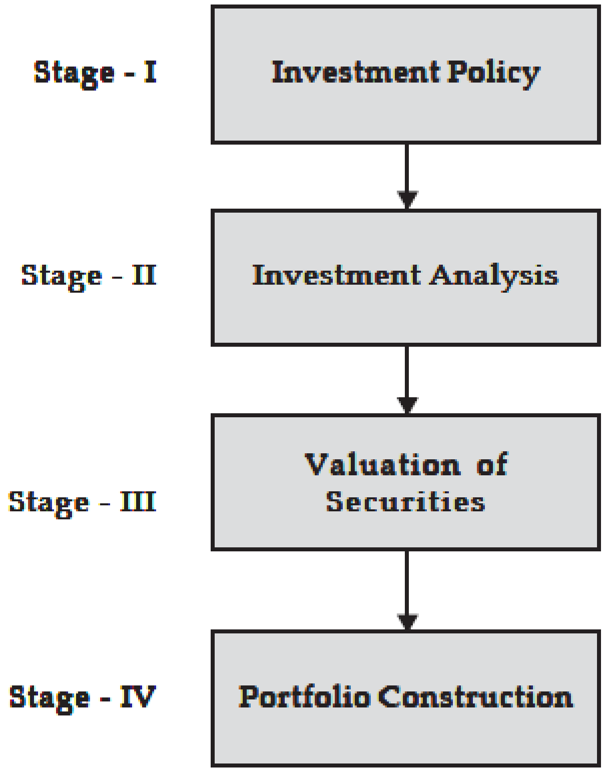

Figure 1.4.The Investment Process/Stages (Source: Investmentpedia.org, Creative Commons License).

Figure 1.4 shows the steps of the investing process. The steps of the investing process are described below:

a. Investment Policy
b. Investment Analysis
c. Valuation of Securities
d. Portfolio Construction (Rochford & Rudelius, 1997).

Investment Policy

The first step in the investment decision is the investment policy. The following characteristics of an investor are determined:

i. Calculating Investable Wealth
ii. Making Portfolio Objectives Sense
iii. Identification of Potential Investment Assets

iv. Examining the Qualities of Investment Assets

v. Wealth Distribution Among Asset Types (Villegas-Navarro et al ., 2001).

Investment Analysis

The second step in the investment strategy is investment analysis. The following criteria are used in the investor examination of the investment:

1. Stock Analysis of Equity
2. Examination of Industries
3. Examination of Industries
4. Analysis of Stocks in Quantitative Form
5. Examining the Economy
6. Analysis of Debentures and Bonds
7. Analysis of Yield Structure
8. Consideration of Debentures
9. Quantitative Analysis of Debentures
10. Other Asset Analysis
11. Qualitative Analysis
12. Quantitative Analysis (Lichtenthaler, 2008).

Valuation of Securities

The third step in the investing process is the evaluation of securities. This phase entails

i. Valuation of Stocks

ii. Valuation of Debentures and Bonds

iii. Valuation of Other Assets (Cherep, 2019).

Portfolio Construction

The process of building a portfolio comes last during the investment strategy. As listed below, it includes the following areas:

1. Determination of Diversification Level
2. Consideration of Investment Timing
3. Selection of Investment Assets
4. Investable Wealth Distribution to Investment Assets
5. Evaluation of Portfolio for Feedback (Sormunen & Laitinen, 2012).

1.9. Sources of Investment Risk

The Oxford Dictionary defines risk as "the chance of encountering danger or of incurring injury or loss," among other definitions. This fits the meaning that most investors associate with the phrase. Investors frequently recognize five categories of investing dangers. As follows:

i. Business and Financial Risk
ii. Interest Rate Risk
iii. Purchasing Power Risk
iv. Social/Regulatory Risk
v. Other Risk (Bechtel, 2009).

Business and Financial Risk

In reality, business risk and investment risk are two different categories of danger. Naturally, they are connected. Operational risk is another name for business risk. Operational risk is related to how the business entity conducts its daily business. Debt and preference shares put money at risk (Fixed cost securities). Several variables, including those listed below, may contribute to financial and business risk:

1. Heightened Competition
2. The emergence of New Technologies
3. Development of Substitute Products
4. Shifts in Consumer Preferences
5. Inadequate Supply of Essential Inputs
6. Changes in Government Policies
7. Poor Business Performance (Javid & Seneviratne, 2000).

Interest Rate Risk

Another type of investment risk is interest rates. Shareholders are exposed to risk due to alterations in the interest rates on securities. Existing fixed-income assets' marketing prices decrease when interest rates rise and vice versa. This occurs because a consumer of such a fixed economic security will not purchase it when its principal amount or face value is lower than the current interest rate on a comparable asset.

Market Risk

Prices of assets, especially share capital, are likely to fluctuate even when the business sector's earning potential and also the structure of the levels are more or less unchanged. This variation has several causes (Drury et al., 2013).

Following is a list of the primary causes:

1. The altering investor psyche.
2. There are times when investors' outlooks turn optimistic, and their time horizons for investing grow.
3. Unexpected wars, election years, political activity, prominent person's sickness or death, market speculation, and corporate exodus are all significant psychological aspects of the market.

These factors cause practically all common equity values to decrease as uncertainty and fear permeate the market (Benaroch, 2001).

Purchasing Power Risk

The main risk that investors confront is buying power risk. Traders choose assets whose market values fluctuate with consumer spending to offset rising living expenses. They'll discover that their overall wealth has decreased if they don't. Inflation eliminates investors' economic influence over products and services. All investors must, in essence, be interested in the ongoing control their people investing has had on products and services (Wang & Yang, 2016).

Other Risks

Investments in foreign assets are typically subject to other kinds of hazards. Risks related to the financial value and political climate are involved. Investors that purchase foreign securities do so at several dangers. The following is a list of them:

1. A change in the foreign government and repudiation of outstanding debt
2. Nationalization of businesses, and firms, that is, seizure by the government
3. The foreign state or company's desire but incapacity to manage its debt (Hashemizadeh et al ., 2021).