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EQUITY INVESTMENT STRATEGIES: A STUDY ON RETAIL INVESTORS IN INDIA

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ABSTRACT

This paper discussed the strategies adopted by retail investors for taking a decision regarding investment in equity securities. In the process, the theoretical aspects of investment decision making, investor preferences and perception are presented as a prelude to the empirical analysis. It is found from the study that information on several aspects required for trading in equity investments can be obtained from various resources. Retail investors lack of expertise and competency to employ sophisticated analytical tools to take their investment decisions. They adopt very simple and less time consuming strategies for arriving at a decision of investment in equity securities.

KEYWORDS: Retail Investors, Equity Investments and Investment strategies.

Introduction:

Retail investors require general information about the financial developments taking place in the economy, securities market behavior and specific information about the companies whose securities are under consideration for investment. They also require information relating to the new issues of the companies, investment advice and recommendation regarding the buying, holding and selling of certain security information about dividend, bonus, rights issues, record dates/book closures of their holdings etc. The information required is obtained from Financial Press, Stockbrokers' literature, Companies' publications and Advice and counseling by Investment advisers

Investors have to analyze and interpret the information provided in the financial press, stockbrokers' literature and companies' publications for taking a wise decision. All the investors do not possess the requisite knowledge and expertise to understand the information made available to them. Investors may burn their fingers when the investment information contained is misleading. Unscrupulous promoters and stockbrokers distort the facts and use flowery language to inspire the investors. As such, the investors have to observe caution before they take a decision, otherwise, they fall a prey for the tricks played by the vested interests.

Review of Literature:

Studies conducted previously on capital market developments, their trends and related to retail investors are studied under separate headings. Studies related to 'general financial behavior' investors like SEBI-NCAER Survey (2000) was carried out to estimate the number of households and the population of retail investors, Shanmugham (2001) studied their perception on various investment strategies, Rajeshwari T.R and Rama Moorthy V.E (2002) studied financial behavior and factors influencing fund/scheme selection investors, Manas Pandey (2004) examined the contribution of domestic saving in the growth of new issue market. NCAER and Max New York Life (2005) survey conducted on 'How India Earns, Spends and Saves' was for 2004-05, Louies M. Thompson Jr. (2007) focused on the importance of communicating with the individual investors, RBI Bulletin (2009) chapter VI examined the feasibility of directly estimating household savings through integrated income and expenditure surveys. S.Saravana Kumar (2010) studied investor preference of future and equity (cash) market.

Studies related various reforms taken place in the capital market like, Prof. V. Gangadhar & Yadagiri (1993) concluded that for the balanced and sound economic development a sound and strong capital market is a must, R. Nagaraj (1996) examined trends of the capital mobilization during the 1960-61 to 1992-93, L.M. Bhole & Shreeya Pattanaik (2002) discussed the working of Indian Stock Market (ISM) from both quantitative and qualitative perspectives, R. N. Agrawal (2003) supported the Levine and Zevos argument that well developed stock markets may be able to offer different kinds of financial services, M.T. Raju (2004) presented the SEBI's role over the past one decade in the strengthening and active functioning of stock exchanges and Hussein A. Hassan Al-Tamimi (2006) studied Factors Influencing Individual Investor Behavior

Objective of the Study:

- To review the strategies adopted by retail investors for taking a decision regarding investment in equity securities.

Methodology:

***Sources of Data*:**

This study is based entirely on primary data collected through a well designed structured questionnaire. The data was collected from investors spread over five selected major cities in the country viz., Bangalore, Chennai, Hyderabad, Mumbai and Warangal. Warangal is one of the rapidly growing city and my native place; hence I have selected Warangal as one of the cities to study. Admittedly, the sample does not represent the country's entire population but only "the universe of potential investors". Secondary data is also used to supplement the findings drawn from the primary data. The secondary data is collected from the various sources available like websites mainly SEBI, RBI, BSE and NSE, Magazines, Journals etc. wherever necessary.

Sample Design:

Retail investors from five cities namely Bangalore, Chennai, Hyderabad, Mumbai and Warangal, who have been operating for a period of two years or more are still performing during the period of the study are selected on the basis of convenient sample method. For an in depth study 100 literate retail investors have been selected from each city. And these retail investors are identified from the selected cities with the help of stock broking houses like Kotak Securities Ltd., ICICI Securities Pvt. Ltd., India Bulls Securities Ltd and Share Khan, etc

Data Analysis:

The data is analyzed by employing simple statistical tools like averages, mean standard deviation. Pie-charts and bar charts are also used to present the data wherever required.

Further standard deviation is also used to judge the homogeneity of the mean.

Investment Decision Making Process:

Generally an investment decision making process involves the following steps:

a. Specification of investment objective
b. Determination of investor risk tolerance
c. Evaluation of investment avenues
d. Execution of the investment decision

a) Specification of Investment Objective:

Any investor having investable surplus contemplates to employ the funds for investment in different kinds of assets. The asset to be acquired depends upon the investment objective of the investor. The objective varies from investor to investor and from time to time. It is largely influenced by a number of factors like the investors' age, education, income, preferences, perception of risk and liquidity, cash flow requirements, control desired over the asset transaction costs etc. Investor objectives in respect of his investment in equity securities can be stated as follows.

i. Fall of interest in other investment avenues
ii. To get quick and higher returns
iii. To make speculative profits
iv. To ensure liquidity for the investment
v. To ensure capital appreciation

Investors were asked to give the rankings for the reasons which are motivated to invest in capital market particularly equity. Five reasons are given to the investors and asked to give the ranks for the given reasons. The results are mentioned in the following Table 1

TABLE 1

Investors' Ranking of Reasons for Investment in Stocks

Reasons	**Number of investors giving ranks**				
	I	**II**	**III**	**IV**	**V**
Reasonable Rate of Interest	235	47	59	126	33
capital appreciation	105	148	97	96	54
Speculative Profits	86	122	111	37	144
Pride of ownership	43	56	123	134	144
Quick and Higher returns	31	127	110	107	125

Source: Primary Data

From the Table 1observed that, of the 500 respondents, I rank given the investors, nearly 50 percent were for 'Reasonable rate of interest' and 21 percent for 'capital appreciation' and 17 percent for 'Speculative Profits' of the stock market. Only around 9 percent of the investors invested in stocks for 'Pride of ownership of blue chip' stocks and 6 percent invested to 'Quick and Higher returns'.

Further, the ranks given by investors for various reasons were analyzed. The mean value of ranks and standard of deviation of the values from mean value were computed. Based on the mean value of the ranks the most preferred and least preferred reasons were identified. Table 2 presents the mean value and standard of deviation of the ranks.

TABLE 3.2

Mean and Standard Deviation of Investors Ranking Of Reasons for Investment in Stocks

Reasons	Mean	Standard Deviation
Reasonable Rate of Interest	3.97	1.249
Capital appreciation	3.39	1.090
Speculative Profits	3.03	1.205
Pride of Ownership	2.10	1.162
Quick and Higher returns	2.47	1.512

Source: Primary Data

Table reveals that the fall in interest rates for deposits to be the driving reasons for many investors to invest in the stock market. Investors investing to get quick and higher returns and pride of ownership are the least preferred reasons. In addition, it was found the second important reason is capital appreciation comparison to other forms of investments. Thus, it can be concluded that the overall fall in interest rates has forced the investors to invest in stock market to earn quick and higher returns. The standard deviation of investors' reasons for investment in stocks from mean value is less than one for first two reasons indicating the high degree of uniformity in the investors ranking as well as the homogeneity of the investors with respect to their reasons for investment in stocks.

b) Determination of Risk Tolerance:

The risk tolerance of investors differs from investor to investor. An investor may be a risk averter or a risk neutral or a risk taker. Risk averting investor does not accept risk associated with the investment and prefers investments carrying low degree of risk. Risk neutral investor assumes moderate risk and prefers diversification to neutralize the risks associated with his investments. Risk taking investor accepts higher risk and displays his preference for risky investments. The behavior of investors towards acceptance of risk is not consistent. As such, an investor has to assess his own ability to bear the risk of the proposed investment, before he attempts the evaluation of different investment avenues.

***c) Evaluation of investment avenues**:*

The investors have wide choice of financial instruments to select from and invest. Financial investment is one which is held as equity shares, preference shares, debentures, fixed deposits, tax saving bonds, Insurance, small savings, mutual fund schemes etc. These investments vary in terms of risk and return associated with them. For this study, Equity shares are considered as pre- requisite. Apart from Equity Shares, Mutual fund schemes, Tax

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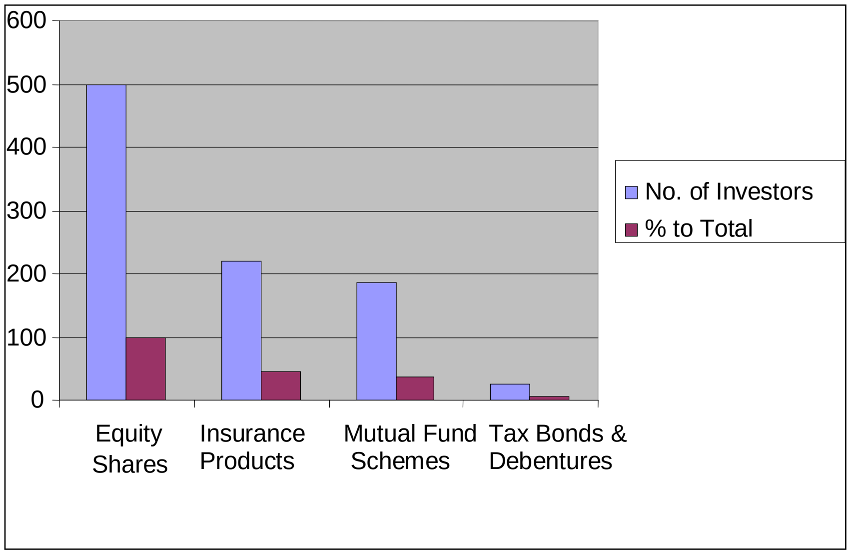
saving bonds and other Bonds and debentures are considered as investment types. These vary widely in terms of risk and return, in that equity shares at one extreme are of high risk and uncertain returns and tax saving bonds and debentures at the other extreme are with low risk and assured return. The investors' present holdings of the four listed types of investments are given in Figure 1

FIGURE 1
Investors Preference for Financial Assets



Source: Primary Data

Figure 1 throws light on the investments of investors. 100 percent of the investors hold equity shares, 43.8 percent of them have invested in Insurance products, and 37.4% in mutual funds and 4.8% of the investors have invested in tax saving bonds and debentures. This shows that this group of investors is primarily equity investors with some of them having invested in insurance products and mutual fund schemes. However, it seems that they are not that much interested in investing in tax saving bonds and debentures as only 4.8 percent of them have invested in those so far.

The above analysis explains that equity shares and mutual funds are largely attracted by the retail investors. They are remaining aloof from investing in other investment avenues. As such, measures have to be initiated to make these savings instruments more popular among the investing people by removing the legal constraints.

The return, risk and liquidity are more important among all the investment characteristics for evaluation of investment avenues. The larger the return an investor expects from an investment, the greater will be the risk and the lower the return he desires there from, the lower will be the magnitude of risk he assumes. Investor has to assess the risk at which the benefits accrue to him are maximum form the investment.

d) Execution of the Investment Decision:

The investment decision applicable to the present study refers to

a) The decision to purchase equity securities, or/and
b) The decision to sell equity securities

These decisions involve two aspects viz., a) what to purchase/sell? b) When to purchase /sell? The former aspect is about the selection of a security to be purchased or sold, and the latter is about the timing of affecting the particular deal.

After arriving at an investment decision, the investor places an order directly with the stock broker or through the sub-broker, with necessary instructions to purchase/sell certain security. The stock broker executes the investor's order as per the instructions for commission. The perceptions of investors on these questions have been answered in the coming discussions under the head of investment strategies.

Investment Strategies of Retail Investors:

A number of Theories, Models and Approaches like Fundamental Analysis, Technical Analysis, Random Walk and Efficient Market Theory are there in financial and investment literature, which help in taking profitable investment decisions. Analytical tools are largely used by institutional investors, professional investment advisers, large-size stock broking firms, security analysts and technical investors in arriving at investment decisions. Retail investors cannot take investment decisions by employing such sophisticated analytical tools because a majority of them are impatient, incompetent and they cannot spare sufficient time and funds for the purpose. The size of the investment they make in equity securities by each of the investors also does not demand for a lot of effort on their part. They spend more time for making money, but spend little time to manage their earnings and investments. A few of such investors evince interest Endeavour to perform the analyses required for taking investment decisions. Investment decisions of retail investors are also influenced by the mood of the securities market. Investment decision making is becoming more complicated and complex because of growth in the number of companies, non-availability of reliable information of their activities and manipulations and frauds that are taking place in the securities market. Retail investors adopt different, simple and less time consuming strategies for taking investment decisions, so that they can make at least satisfiable returns on their investments. They are described hereunder.

Strategy – I: Comparison of the Estimated Share Value with Its Current Market Price:

When an investor adopts this strategy to take an investment decision, a comparison of the estimated value of the share and its market price will be made. He estimates the value of the share on the basis of the P/E multiple and the EPS[1]. The P/E multiple of the industry or a predetermined standard P/E multiple is considered. Current EPS is collected from the financial publications. The estimated value of the share is obtained by multiplying the P/E multiple and the EPS.

Estimated Value of Share = P/E multiple X EPS

The current market price of the share is collected from the price quotations published in daily newspapers. Investor may consider either the high or the low or the weighted average price according to the investment decision he desires to make. If the investor intends to arrive at a 'buy decision', he considers 'high' market price of the share. In case he wants to take a 'sell decision' 'low' market price of the share is considered. Investor can also consider the weighted average price in case there is a significant daily price range and different

[1] Price-Earnings Ratio = Market Price of the Share/ Earnings per Share, Where EPS = Earnings available to equity share holders/ Number of outstanding equity shares.

volumes of scrips are traded at different floor prices.

Now the estimated share value is compared with the current market price and investment decision is taken as mentioned below.

a) If the estimated share value is less than the current market price to a market price to a marked extent, investor takes a decision to sell the share.

b) If the estimated share value is greater than the current market price significantly, investor takes a decision to buy the share.

c) If the estimated share value is hovering around the current market price closely, investor adopts 'wait and see' attitude and decides to hold the security.

Strategy – II: Averaging the Cost Price of Shares:

An investor expecting a fixed amount of investable surplus at different period of time utilizes the funds for the purchases of the shares of a company of his choice. The share is identified by observing the yearly price range published in daily newspapers. The company preferred depends upon the fancy he has taken A the market price of the share fluctuates from day to day on account of demand, supply and other factors the investor acquires the shares at different times. More number of shares are acquired when the market price is low and less number of shares are acquired when the market price is high. In this manner, the cost price of all the shares together is kept at the average level.

When the market price rises beyond the average cost price markedly, the investor takes a sell decision to realize profit on his investment in the security. Similarly, when the market price is moving up and down around the average cost price, the investor decides to hold the shares.

Strategy – III: Buying at Low and Selling at High:

The investor who adopts this strategy establishes price indicators to arrive at an investment decision. The strategy involves.

a) Obtaining the standard P/E multiple of the industry concerned, and
b) Determining two P/E multiples, one below and another above the standard P/E as price indicators.

These P/E multiples have to be determined in accordance with the investment objective of the investor. They work as signals for taking investment decision. When the current P/E multiple of the share of his choice falls to the predetermined, smaller P/E multiple, the investor takes a 'buy decision', and when it raises to the predetermined greater P/E multiple, he takes a 'sell decision'. This strategy is preferred by the investors making short-term investments.

Strategy – IV: Application of Beta Coefficient:

Investment decisions can be taken by employing Beta Coefficient. It measures the sensitivity of a share to the market movements. In other words, it describes the amount of change in the return on a share corresponding to a unit change in the market return. Beta coefficient is interpreted in the following manner.

Beta Coefficient	Interpretation
0	Indicates that the return on share is insensitive to market return
1	Indicates that the return on the share is same as that of the market return.
Greater than 1	Implies that the return on the share is greater than that of the market return by the number of times of the coefficient.
Less than 1	Describes that the return on the share is less than that of the market return by the number of times of the coefficient.
Positive	Indicates increase in the return
Negative	Indicates decrease in the return

a) When the market is bullish:

i. Investor takes a 'buy decision' in respect of shares with larger beta coefficients.

ii. Investor takes a 'sell decision' in respect of shares with smaller beta coefficients.

b) When the market is bearish:

i. Investor takes a 'buy decision' in respect of shares with smaller beta co-efficient.

ii. Investor takes a 'sell decision' in respect of shares with greater beta coefficients.

Strategy – V: Investor Perception of share Prices:

When an investor adopts this strategy to take his investment decision, he takes his own perception of the share price. In a rising market, the investor takes a 'buy decision' with the expectation that the price will further rise and the scrip acquired can be sold at a higher price at which profit can be booked. In a falling market, the investor takes a 'sell decision' with the hope that the price will further fall and the scrip on hand can be sold at a price at which potential loss can be reduced.

Strategy – VI: Average Up and Average Down of Price Decision:

The investor's strategy of this kind for taking investment decision is as follows.

i. In a rising market, the investor sells his share holdings in small quantities, so as to bring up the average price of all the shares put together.

ii. In a falling market, the investor buys shares in small quantities, so as to bring down the average price of all the shares taken together.

Strategy VII: Following Financial Publications:

Retail investors do not perform any kind of technical analysis for investment decision making. But, the investment guidance provided by the technical analysts in financial publications is taken as basis for making investment decision. The following criteria are followed:

a) Investor takes a 'buy decision' if the price rises above the neckline incase of 'inverse head and shoulders top' formation on the line chart.
b) Investor takes a 'sell decision' if the price falls below the neckline incase of 'head and shoulders top' formation on the line chart.

When moving average analysis is used in the technical analysis

a) Investor takes a 'buy decision' on perceiving the following trends
   i) Stock price line rises through the moving average line when the graph of the moving average line is flattening out.
   ii) Stock price line falls below the moving average line which is rising.
   iii) Stock price line which is above the moving average line, fall but begins to rise again before reaching the moving average line.
b) Investor takes a 'sell decision' on perceiving the following trends.
   Stock price line falls through the moving average line when the graph of the moving average line is flattening out. Stock price line rises above the moving average line which is falling. Stock price line, which is below the moving average line, rises but begins to fall again before reaching the moving average line[2]

Other Strategies of the Investors:

When the investor has perception of the return and risk characteristics of securities he takes a 'buy decision' in respect of the security known for high return and low risk. A 'sell decision' is taken in respect of the security known for low return and high risk.

Investor collects the ratings assigned for new issues of the companies from financial publication of choice. Then he takes a 'buy decision' of the securities assigned with the highest score.

In case of new issues of the companies, the information supplied in Memorandum accompanied with the application for the securities is analyzed and the quality of the issue is judged by the investor and decides himself either to subscribe for the issue or not.

Cautious and prudent investor takes investment decision on his own by judging the quality of a particular security. He collects the necessary information from the financial publications and discussions held with investor friends and sub-broker.

Lay and gullible investors take their investment decision on the basis of sub-brokers advice, market news, rumors and hearsay in the market.

Some investors take 'buy decisions' in respect of shares which are available at a very low price, with the hope that their prices are doubled or tripled in due course. The investment decisions of some investors are influenced by their sentiments and temperaments. If the investor is an optimist, he takes a 'buy decision' irrespective of the market movements. Similarly, if he is a pessimist, he takes a 'sell decision.

Now a day, investors are depending more on internet where he can get updated information from time to time. There are number of articles, analysis, columns and advices available on investment in securities in internet. Investors are taking this source as one of the important source to take decision.

An attempt is made to know what source of information they are following to invest in securities and to frame their own strategy. The following Table 3 presents the results.

[2] Prasanna Chandra, The investment Game- How toWin- Tata Mc Graw Hill Publishing Company Ltd. New Delhi, 1994, p.246

TABLE 3

Source of Information Used by Investors With Regard to Investment Strategy

Source	No. of Investors	% of Investors
Annual Reports including CG reports of the company	316	63.2
Advertisement of public issue of the company	297	59.4
Prospectus of the company	241	48.2
Interim financial results of the company	140	28
Analysis of New Issues by financial magazines	275	55
Share price quotations and volume of scrip of the company traded in a stock exchange	173	34.6
Brochures, pamphlets, booklets containing highlights of the issue and future prospects of the company and industry	40	8

Source: Primary Data

It is revealed from the table that investors have opted more than one source, majority of the investors are going with Annual Reports including Corporate Governance Reports of the company, next Advertisement of public issue, Analysis by financial magazines and Prospectus of the company were second, third and fourth places respectively. Twenty eight percent of the respondents are going through interim reports and only two percent of the respondents are going through brochures pamphlets, booklets containing highlights of the issue and future prospects of the company and industry.

The phase / stages of industry life cycle also influence the investment decision of the investors. As such, the investors' perception of the stages of the lifecycle of an industry in the purchase of equity securities has been examined. Results are mentioned in the following table 4

TABLE 4

Investors' Preference of the Phase of the Life Cycle of the Industry for Taking Investment Decision

Stage	No. of Investors	% of Investors
Pioneer	98	19.6
Expansion	157	31.4
Growth	166	33.2
Decline	69	13.8
Revival	10	2.0
Total	500	100.0

Source:Primary Data

Table reveals that nearly two third of the respondents are investing when the company is in expansion stage or in growth stage, nearly one fifth of the investors were shown to invest at pioneer stage, about 14% of the investors are investing at decline stage, this category of people may hope that the company will turnaround with good profits and only two percent of the respondents are investing at revival stage.

TABLE 5

Investors' Strategy on Selling Securities

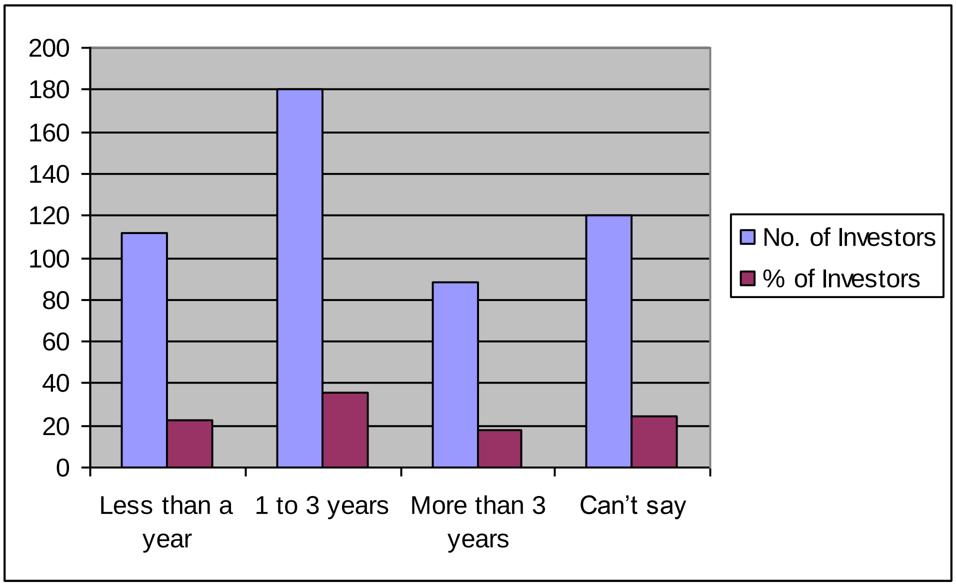
Investment Strategy Options	No. of Investors	% of investors
Sell the shares within the same day/few/days/months/ or in a year	60	12.0
As soon as price reaches my target	168	33.6
Keep revising the target as prices rises	129	25.8
Not interested in selling (Capital appreciation)	143	28.6
Total	500	100.0

Source: Primary Data

As part of knowing investment strategies it is required to know the time the investors wants to dispose the securities. The investment strategy of the investors in this regard is quite interesting. Table 5 shows, nearly one third have said that they sell the shares as soon as the price reaches their target. For them the period of holding is immaterial. One fourth of investors said they keep revising the target as price level rises. It is any body's guess at what time or price they will sell and these are the investors who usualy get trapped in times of unexpected turn of events. 28.6 percent of the investors were not interested in selling. They can be said to be the long-term investors. Only twelve percent of the investors have said they sell within a year and they are short-term investors or speculators.

Expected period of return is also one the important factor which influence investment strategy and it may differ among the investors. The investors' expectation on the period of return from stock market is given in the following Figure 2.

FIGURE 2: Expected Period of Returns on Investment In Stock Market



Source: Primary Data

Figure brings out that nearly two fifth of investors expect stock markets to gives higher returns over other forms of investments over a period of 1 to 3 years. Nearly 18 percent of investors expect it to give higher returns over a period of above three years and nearly 23 percent expect it to give within a year and nearly one fifth of the investors unable to express period of return. Thus, it can be said that investors on an overall basis expect the stock market to give higher returns in the long term spreading over a period of three years and above.

The investors' expectations regarding the period of returns were further classified and the basis of their age to know the impact of age on expectation about period of returns. The results are presented in the following table 6.

TABLE 6

Age -Wise Classification of Investors' Expectation about Period Returns

Age (in Years)	Period of Returns in Investment in Stock Market				Total
	Less than a Year	1 to 3 Years	More than 3 Years	Can't Say	
Up to35	53	75	24	59	211
36 to 50	39	55	40	16	150
51 to 60	10	50	14	24	98
61 and above	10	0	10	21	41
Total	**112**	**180**	**88**	**120**	**500**

Source: Primary Data

It can be seen from the table that the investors expecting the stock market to give better returns within a year and over a period of 1-3 years are dominated by the up to 35 year age group and investors' group expecting better returns over a period of more than 3 years is dominated by age group of 36-45 years. Thus it can be concluded that investors of above 35 years have long term orientation in their stock market investment

Conclusion:

Information on several aspects required for trading in equity investments can be obtained from various resources. Retail investors lack of expertise and competency to employ sophisticated analytical tools to take their investment decisions. They adopt very simple and less time consuming strategies for arriving at a decision of investment in equity securities. All the investors enquired being educated and aged, their personal judgment is found to be main inducement for taking an investment decision.

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