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Miscellaneous Concepts of the Stock Market-Part 2

LESSON 33 OF 33

RBI GRADE 'B'

Finance Section

Course- 5

"Indian Equity Market"

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RBI GRADE 'B': Finance Section

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Mahurat Trading

Every year, the stock market is open for a few hours on the first day of Diwali. A special trading session conducted for an hour on the auspicious occasion of Diwali. Usually this takes place in evening. Mahurat trading has been going on for over 100 years on the Bombay Stock Exchange. It marks the beginning of a new financial year called 'Samvat'.

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Top-down/ Bottom-up Approaches

- These are ways to select stocks from amongst the thousands listed on the exchange.
- The top-down approach first takes into consideration the macro-economy. You understand the trends and outlook for the overall economy. Using this, you choose a one or more industries that are expected to do well in the near future. This is because every industry reacts to overall economic conditions like inflation, interest rates, consumer demand and so on, in a different way. Select one amongst the industries after in-depth analysis. Next, you understand the workings of the industry, the players and competitors and other factors that affect the sector. Based on this, you select one of the companies in the industry.
- The bottom-up approach is just the opposite. You do not look at the economy or select an industry first, but concentrate on company fundamentals. You first understand what your priorities are – high growth or steady income through high dividends. Using appropriate ratios like the Price-to-Earnings ratio or the Dividend-yield, you select a bunch of stocks. Next, analyze each of these companies; find answers for questions like what factors drive profits? Is the company management efficient? Is the company heavily indebted? What is the future outlook? And so on. Based on the results, select the company that best fits your requirements. The bottom-up approach is most suited for weak market conditions. This is because, the underlying belief is that these companies will perform well even if the economy is poor. They are thus anomalies – companies that don’t follow the normal market trend.

Price-targets & Stop-loss Targets?

- As an investor, to maximize your profits, you need to get your pricing right – both when it comes to buying and selling. However, sometimes, prices fluctuate more than expected. So, it can become a little difficult to gauge whether to trade now or wait a little more. This is where stock recommendations help.
- Analysts put out price targets and stop-loss measures, which let you know how long you should hold a stock. A price target indicates that the price of share is unlikely to climb above the level. So, once the share price touches the target, you may look to sell it and pocket your profits. A stop loss, meanwhile, acts as a target on the lower end. It lets you know when to sell before the stock falls further and worsens your loss.

Insider Trading

- In your dealings with the stock world, you will often come across the term 'insider trading'. In simple words, the meaning of insider trading is 'the trading of shares based on knowledge not available to the rest of the world'. It is illegal to trade after receiving 'tips' of confidential securities information.
- This applies to corporate personnel as well as traders and brokers. This is why company management have to report their trades to the exchange. For example, when corporate officers, directors, or employees trade the company's stocks after learning of significant, confidential corporate developments, it is considered an illegal form of insider trading. This applies to employees of law, banking, brokerage and printing firms who were given such information to provide services to the corporation whose securities they traded. Even government employees, who trade after learning of such information, are considered to have broken the law on insider trading. It is a punitive offence.

Stock Quotes

You must have often seen a ticker on a business news channel on the TV or on the huge billboard outside the Bombay Stock Exchange, constantly showing a bunch of letters and numbers in green or red lettering. These are stock quotes. The bunch of letters you see is a stock symbol, while the numbers that follow signify the stock price.

- What are stock symbols?

A stock symbol is a unique code given to all companies listed on the exchange. Once you know the stock code or symbol of the company, you can easily obtain information about the company. This is important for investors who wish to conduct a financial analysis before purchasing a company's shares. For example, TCS stands for Tata Consultancy Services, while INFY stands for Infosys. Often, it is not possible to write the full name of a company. It would take up a lot of space on the ticker board or stock table. In such a case, the stock symbol comes handy and it is just 3-4 letters. For this reason, stock symbols are also referred to as ticker symbols.

PE (Price Earning) Ratio

Some stock tables and quotes also mention the PE ratio. This is the amount an investor pays for each rupee the company earns. It is calculated by dividing the stock price with the company's earnings per share. This is important because stock price is a market-assigned value. It largely depends on market sentiment about the stock, and hence may not be in synchronization with the share's internal value. The PE ratio, thus, helps give perspective about the share's value in comparison to the company's financial performance. A high PE ratio means the stock is costly, while a low PE ratio means the stock is cheaply available.

Trading Account

- When a company lists on the stock market, its shares become available for trading on the stock exchange. Earlier, the exchange had an open-outcry system. In the mid-90s, the stock exchanges adopted the electronic system. This means, all trades were conducted electronically. Simply put, you didn't have to go to the counter and place an order physically. You could do it through a computer, which would verify the details, the market price, and process the trade.
- For this reason, you need a special account through which you can conduct transactions. This is called the trading account. Without one, you cannot trade in the stock markets. You register for an online trading account with a stock broker or a firm. Each account comes with a unique trading ID, which is used for conducting transactions.
- A trading account is used to place buy or sell orders in the stock market. The demat account is used as a bank where shares bought are deposited in, and where shares sold are taken from

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