

# Financial Portfolio management: Overview and Decision Making in investment Process

Neelam Kapoor

Asst.Prof. B.Sc,MBA,UGC-NET

7-Laxmi Nivas Near Chaman Hotel Nayapura,Kota (Rajasthan)-324001, India

Email: [neelamklbc@gmail.com](mailto:neelamklbc@gmail.com)

## ABSTRACT:

*In the globalization era, Portfolio Management play an important role in investment of securities. portfolio management is both an art and a science. It is much more than the selection of securities from a catalog by a financial consultant or the application of a formula to a set of financial data input supplied by a security analyst. It is a dynamic decision-making process, one that is continuous any systematic but also one that requires large amounts of astute managerial judgment about the securities markets and the individual for whom portfolio is managed. portfolio management is a decisive element for the good performance of new product development and compliance with business objectives because it not only defines new product projects but also defines revisions, updates, and even decisions regarding the discontinuation of products that are produced and commercialized. This article proposes a framework with the specific objective of presenting an approach that could be useful to portfolio management. The framework proposed in this article presents a holistic perspective of portfolio management, suggesting the use of a set of formal management methods for not only evaluating product projects but also extending to organizational aspects and*

*including them in strategic planning and portfolio reviews.*

## KEYWORDS:

Portfolio Management; Risk; Securities; Financial Data; Investment; Diversification

## 1. INTRODUCTION :

A Portfolio Management refers to the science of analyzing the strengths, weaknesses, project, what is the goals of project, what is the resources of project to be implemented and opportunities and threats for performing wide range of activities related to the one's portfolio for maximizing the return at a given risk. Portfolio Management process start with raw inputs such as what is the how much capital is required for such project. After analyzing the factors investor evaluate the project or security in financial term such as Return of portfolio, risk of portfolio etc ,after that the organization according to organization strategy will chose the security or project.

Portfolio Management consists of two word i.e. Portfolio and Management. The meaning of this is as follows.

→Portfolio: Portfolio is group of financial assets such as shares, stock, bond, debt instruments, cash equivalent etc. A portfolio is planned to stabilize the risk of non-performance of various pools of investment.

→Management: Management is organization and coordination of the activities of an enterprise in accordance with well -defined policies and in achievement of its pre defined goal and objective.

Now lets comprehended the meaning of the term portfolio management.

→Portfolio Management : It guides the investor in a method of selecting the best available securities that will provide the expected rate of return for any given degree of risk and also to mitigate the risk . It is a strategic decision which is addressed by top level management.

Portfolio is combination of security such as Stocks Bonds and Money market Instruments.The process of blending together the broad Asset classes so as to obtain optimum return with minimum risk is called portfolio management. Diversification of investments helps to spread risk over many assets. Major tasks involved with Portfolio Management are as follows.

Taking decisions about investment mix and policy

Matching investments to objectives

Asset allocation for individuals and institution

Balancing risk against performance

## OBJECTIVES AND IMPORTANCE :-

The simple fact that securities carry differing degrees of expected risk leads most investors to the notion of holding more than one security at a time, in an attempt to spread risks by not putting all their eggs into one basket. Most investor hope that if they hold several assets, even if one goes bad, the others will provide some protection from an extreme loss.Portfolio Management routed through Diverfiction ,it efforts to spread and minimize risk take the form of diversification. The more traditional forms of diversification have concentrated upon holding a number of security types. It is most valuable objective of efficient portfolio would agree that a portfolio consisting of two stocks is probably less risk than one holding either stock alone.

**The objective of portfolio management is to invest in securities in such a way that one maximizes one's returns and minimizes risks in order to achieve one's investment objective.**

**A good portfolio should have multiple objectives and achieve a sound balance among them. Any one objective should not be given undue importance at the cost of others. Presented below are some important objectives of portfolio management.**

1. Security principal of investment: The first important objective of a portfolio, no matter who owns it, is to ensure that the investment is absolutely safe. Other considerations like income, growth, etc., only come into the picture after the safety of your investment is ensured
2. Consistency of Return : Once investment safety is guaranteed, the

portfolio should yield a steady current income. The current returns should at least match the opportunity cost of the funds of the investor. What we are referring to here current income by way of interest of dividends, not capital gains.

3. Capital Growth : A good portfolio should appreciate in value in order to protect the investor from any erosion in purchasing power due to inflation. In other words, a balanced portfolio must consist of certain investments, which tend to appreciate in real value after adjusting for inflation.
4. Marketability: A good portfolio consists of investment, which can be marketed without difficulty. If there are too many unlisted or inactive shares in your portfolio, you will face problems in encasing them, and switching from one investment to another. It is desirable to invest in companies listed on major stock exchanges, which are actively traded.
5. Liquidity: The portfolio should ensure that there are enough funds available at short notice to take care of the investor's liquidity requirements. It is desirable to keep a line of credit from a bank for use in case it becomes necessary to participate in right issues, or for any other personal needs.
6. Diversification of portfolio : Portfolio management is designed to reduce the risk of investment and provide optimum or highest return on

investment. The investor shall be aware of the fact that there is no such thing as a zero risk investment. More ever relatively low risk investment give correspondingly a lower return to their financial portfolio.

7. Favorable tax status : Since taxation is an important variable in total planning, a good portfolio should enable its owner to enjoy a favorable tax shelter. The portfolio should be developed considering not only income tax, but capital gains tax, and gift tax, as well. What a good portfolio aims at is tax planning, not tax evasion or tax avoidance.

**Investment safety or minimization of risks is one of the important objectives of portfolio management. There are many types of risks, which are associated with investment in equity stocks, including super stocks. Bear in mind that there is no such thing as a zero risk investment. More over, relatively low risk investment give correspondingly lower returns. You can try and minimize the overall risk or bring it to an acceptable level by developing a balanced and efficient portfolio. A good portfolio of growth stocks satisfies the entire objectives outline above.**

### 3. INVESTMENT PROCESS :

The selection of securities is made with a view to provide the investor the maximum yield for a given level of risk or ensure minimize risk for a given level of return. However, selection of securities is based upon the attitude of investor towards risk and other parameters. We can classify investor under three broad categories namely Risk averse, Risk Seeking and Risk Neutral.

1. Risk Averse: In this category we include those investor who demands maximum return a given for risk and they will take calculated risk.
2. Risk Seeking : In this category we include those investor who is willing to take more risk for given return and they will take high risk and called risk owner.
3. Risk Neutral : In this category we include those investor who is indifferent to risk and they will unknown about risk.

Prior to entering into an investment, our locally-based staff ensures that the potential investee meets the minimum standards of eligibility. We investigate the compatibility of the investee both in terms of development impact and from a financial strength perspective. Furthermore, environmental, social and corporate governance issues as well as client protection practices form an integral part in the investment screening, due diligence, audits, monitoring and reporting.

**Regardless of the attitude of an investor , in order to construct a portfolio we need to make investment in securities. This bring us the most crucial aspect of constructing a portfolio, i.e. investment process. The investment process describes how an investor should make decision with regard to the type of security ,how much to invest in such security and when to invest. The basic steps involved in**

**making an investment in securities are as follows.**

## **FINANCIAL INVESTMENT PROCESS**

1. Understand Your financial Health : This involves determining investors financial position objective and his attitude towards risk and return. Investor prepare a summary budget for investment and investor also make a financial tool plan for investment.
2. Understanding Financial Goals : This stage depends on financial goals of Investor. according to nature of portfolio and nature of investor, planner can choose best alternative investment.
3. Investment Plan : Investment plan is a road map of investment process. In this investor is to identify security after performing Economic, Industry and fundamental analysis of the security.
4. Portfolio Construction : Investor after analysis various factors construct portfolio of available securities. Investor is to ascertain assets i.e. securities in which investment is to be done and proportion of the same.
5. Portfolio Review and Re-balance : Periodic review of the portfolio to ensure that it fulfils the set out objectives and thus making changes. Investor for measure the final performance of the

portfolio in terms of risk and return and stated objectives.

#### 4. SCOPE OF PORTFOLIO MANAGEMENT :

1. Portfolio management is a continuous process. It is a dynamic activity. The following are the basic operations of a portfolio management.
2. Monitoring the performance of portfolio by incorporating the latest market conditions.
3. Identification of the investor's objective, constraints and preferences.
4. Making an evaluation of portfolio income (comparison with targets and achievement).
5. Making revision in the portfolio.
6. Implementation of the strategies in tune with investment objectives.

#### 5. ASSUMPTIONS OF PORTFOLIO THEORY :

1. **Investor are risk-averse :** This implies that instead of investing the entire wealth in a single asset or security the investors hold a well-diversified portfolio. A risk averse investor constitute a portfolio with a view to provide maximum yield for a given level of risk or to ensure minimum risk for a given level of return.

2. **Return of securities are normally distributed :** This implies that the mean and variance or standard deviation

**analysis is the foundation of the portfolio decisions.**

#### 6. APPROACHES IN PORTFOLIO CONSTRUCTION

:

**In the portfolio theory investor apply many tools and techniques for maximum benefits at lower risk. There are two approaches that followed by investor in portfolio construction**

##### 1. Traditional Approach :

**Traditional approach evaluates the entire financial plan of the individual. The traditional approach basically deals with two major decisions**

**\*Determining the objectives of the portfolio**

**\*Selection of securities to be included in the portfolio.**

→Steps in Traditional Approach

**1. Analysis of constraints: Investors analysis constraints that are as follows.**

**\*income Needs : Need for current income and need for constant income**

**\* Liquidity**

**\* Safety of the principal**

**\* Time horizon**

**\* Tax consideration**

**\*Temperament**

**2. Determination of objectives :**  
The common objectives are stated below

\*Current income

\*Growth in

\* Capital appreciation

\* Preservation of capital

### 3. Selection of portfolio :

\*Objectives

\*growth of income

\*Capital appreciation

\* Safety of principal

\* Risk and return analysis

### 4. Diversification

\*According to the investor's need for income and risk tolerance level portfolio is diversified

\*In the bond portfolio, the investor has to strike a balance between the short term and long term bonds .

### 2. Modern Approach :

**Modern approach gives more attention to the process of selecting the portfolio. The selection is based on the risk and return analysis. Returns includes the market return and dividend. Investor are assumed to be indifferent towards the form of return. The final steps is asset allocation process that is to choose the portfolio that meets the requirement of the investor. Investor can adopt passive approach or active approach towards the management of the portfolio. In the passive approach the investor would**

**maintain the percentage allocation of the asset classes and keep the security holding within its place over the established holding period. In the active approach the investor continuously assess the risk and return of the securities within the assets classes and changes them accordingly.**

**Portfolio risk can be reduced by the simplest kind of diversification. In the case of common stocks diversification reduces the unsystematic risk or unique risk. Analysts says that if 15 stocks are added in a portfolio of the investor , the unsystematic risk can be reduced to zero. But at the same time if the number exceed 15, additional risk reduction cannot be gained. But diversification cannot reduced systematic or undiversifiable risk.**

→**The Markowitz Model :**

Harry Markowitz published an article on portfolio selection in the journal of finance in march 1952.His publication indicated the importance of correlation among the different stocks return in the construction of a stock portfolio. After the publication of this paper, numerous investment firms and portfolio managers developed 'Markowitz algorithms' to minimize risk.

Markowitz Model of portfolio management have followings assumptions.

\*The individual investor estimates risk on the basis of variability of returns i.e the variance of the returns

\*Investor's decision is solely based on the expected return and variance of returns only

\*For a given level of risk, investor prefers higher return to lower return.

\*Likewise, for a given level of return investor prefers lower risk than higher risk.

## 7. TYPES OF PORTFOLIO :

Stock investors constantly hear the wisdom of diversification. The concept is to simply not put all of your eggs in one basket, which in turn helps mitigate risk, and generally leads to better performance or [return on investment](#). Diversifying your hard-earned dollars does make sense, but there are different ways of diversifying, and there are different portfolio types. We look at the following portfolio types and suggest how to get started building them: aggressive, defensive, income, speculative and hybrid. It is important to understand that building a portfolio will require research and some effort. Having said that, let's have a peek across our five portfolios to gain a better understanding of each.

### 1.The Aggressive Portfolio :

An [aggressive](#) portfolio or basket of stocks includes those stocks with high risk/high reward proposition. Stocks in the category typically have a high [beta](#), or sensitivity to the overall market. Higher beta stocks experience larger fluctuations relative to the overall market on a consistent basis. If your individual stock has a beta of 2.0, it will typically move twice as much in either direction to the overall market - hence, the high-risk, high-reward description. Most aggressive stocks are in the early stages of growth, and have a unique value proposition. Building an aggressive portfolio requires an investor who is willing to seek out such companies, because most of these names, with a few exceptions, are not going to be common household companies. Look online for companies with earnings growth that is rapidly accelerating, and have not been discovered by Wall Street. The most

common sectors to scrutinize would be technology, but many other firms in various sectors that are pursuing an aggressive growth strategy can be considered. As you might have gathered, risk management becomes very important when building and maintaining an aggressive portfolio. Keeping losses to a minimum and taking profit are keys to success in this type of portfolio.

### 2.The Defensive Portfolio:

[Defensive stocks](#) do not usually carry a high beta, and usually are fairly isolated from broad market movements. Cyclical stocks, on the other hand, are those that are most sensitive to the underlying economic "business cycle." For example, during recessionary times, companies that make the "basics" tend to do better than those that are focused on fads or luxuries. Despite how bad the economy is, companies that make products essential to everyday life will survive. Think of the essentials in your everyday life, and then find the companies that make these [consumerstaple](#) products. The opportunity of buying cyclical stocks is that they offer an extra level of protection against detrimental events. Just listen to the business stations and you will hear portfolios managers talking about "drugs," "defense" and "tobacco." These really are just baskets of stocks that these managers are recommending based upon where the business cycle is and where they think it is going. However, the products and services of these companies are in constant demand. A [defensive portfolio is prudent](#) for most investors. A lot of these companies offer a dividend as well which helps minimize downside capital losses.

### 3.The Income Portfolio :

An income portfolio focuses on making money through dividends or other types of

distributions to [stakeholders](#). These companies are somewhat like the safe defensive stocks but should offer higher yields. An income portfolio should generate positive cash flow. [Real estate investment trusts](#) (REITs) and [master limited partnerships](#) (MLP) are excellent sources of income producing investments. These companies return a great majority of their profits back to shareholders in exchange for favorable tax status. REITs are an easy way to invest in real estate without the hassles of owning real property. Keep in mind, however, that these stocks are also subject to the economic climate. REITs are groups of stocks that take a beating during an economic downturn, as building and buying activity dries up.

An income portfolio is a nice complement to most people's paycheck or other retirement income. Investors should be on the lookout for stocks that have fallen out of favor and have still maintained a high dividend policy. These are the companies that can not only supplement income but also provide capital gains. Utilities and other slow growth industries are an ideal place to start your search.

#### 4. The Speculative Portfolio :

A speculative portfolio is the closest to a pure gamble. A speculative portfolio presents more risk than any others discussed here. Finance gurus suggest that a maximum of 10% of one's investable assets be used to fund a speculative portfolio. Speculative "plays" could be [initial public offerings](#) (IPOs) or stocks that are rumored to be takeover targets. Technology or health care firms that are in the process of researching a breakthrough product, or a junior oil company which is about to release its [initial production](#) results, would also fall into this category.

Another classic speculative play is to make an investment decision based upon a rumor that the company is subject to a takeover. One could argue that the widespread popularity of [leveraged ETFs](#) in today's markets represent speculation. Again, these types of investments are alluring: picking the right one could lead to huge profits in a short amount of time. Speculation may be the one portfolio that, if done correctly, requires the most homework. Speculative stocks are typically trades, and not your classic "buy and hold" investment.

#### 5. The Hybrid Portfolio :

Building a hybrid type of portfolio means venturing into other investments, such as bonds, commodities, real estate and even art. Basically, there is a lot of flexibility in the hybrid portfolio approach. Traditionally, this type of portfolio would contain [blue chip](#) stocks and some high grade government or corporate bonds. REITs and MLPs may also be an investable theme for the balanced portfolio. A common fixed income investment strategy approach advocates buying bonds with various maturity dates, and is essentially a diversification approach within the bond asset class itself. Basically, a hybrid portfolio would include a mix of stocks and bonds in a relatively fixed allocation proportions. This type of approach offers diversification benefits across multiple asset classes as equities and fixed income securities tend to have a negative correlation with one another.



## 8. REFERENCES :

1. V Pattabhi Ram,SD Bala, Strategic Financial Management, Snow White ,New Delhi 2013,print
2. CA Ashis kalra, Strategic Financial Management, IGP publication, New Delhi 2013,Print
3. Dr JB Gupta, Strategic Financial Management, Taxmann's, New Delhi,2013,print
4. G Sekar,B Saravana Prasath, Strategic Financial Management,CCH,Haryana, 2013,Print
5. John l Teall,Westportconnectact,London,1999,Print
6. Keith Pilbeam,Finance and Financial Markets,Macmillan Business,1998,England Print
- 7.Larry Hariis,Oxford University Press,New Delhi,2011,Print
- 8.CA Rajat Mahan,Bharat,New delhi,2012,Print
- 9.Taxmann's,New Public Issue Guidelines,Taxmann,2009,Print
- 10.Mannual Of SEBI,Bharat,New Delhi,2014, Print
- 11.SEBI Mannual,Taxmann,New Delhi,2014,Print
- 12.Brain Cayle,Financial risk management,2001,Print
- 13.Dr RP Rustogi,Taxmann,New Delhi,2012,Print
- 14.My Khan,Pk jain,Financial Management,Tata Mcgraw hill Edu pvt ltd,New Delhi, Print
- 15.DK Singhal,Piyush Bihani, Strategic Financial Management,Parv Management Services Pvt Ltd 2011,Jaipur,Print