equaliFi ACADEMY

CIRA®

CERTIFIED INVESTMENT RESEARCH ANALYST®

Investments: Concepts & Features

Agenda

01 **Micro & Macro Economics Concept**
Introduction to Micro and Macro economics

02 **Financial Markets & Investments**
Introduction to Markets, Securities and Participants.

03 **Investment Process**
Introduction to the investment process followed as best practice

04 **Behavioral Finance & Investments**
Introduction and Application of Behavioral Finance in investment industry.

Micro & Macro Economics Concept

Key Learning Outcome

- Interest Rate
- Inflation
- Growth (GDP)
- Fiscal Deficit

Introduction

- The state of the economy and financial markets are interconnected.
- Financial markets bring together savers and users of capital.
- Savers defer consumption today for the future, saves their wealth (Capital), allows Governments and Corporates (Users) to use such capital for economic activities.
- This results in economic growth and employment.

Risk factor and Risk premium

Credit Risk Premium

Credit Risk Premium compensate the investor or bond holder for the probability of default of the issuer

Liquidity Risk Premium

The liquidity risk factor, compensate risk due to illiquidity.

Equity Risk Premium

Investor invest in the equity with systematic and unsystematic risk.

Other Risk Premium

The risk factor comprises risk related to people, processes, strategies etc.

Risk Free and Risky Asset Interest Rate

Risk Free Rate + **Risk Premium** = **Interest Rate for Risky Asset**

The Risk Free Rate means the rate of interest on Risk Free Asset (Treasury Bond)

Investor expects higher return for the credit, market and operational risk

The rate to compensate risk free rate + risk premium

Micro & Macro Economics Concept

Real and Nominal Interest Rate

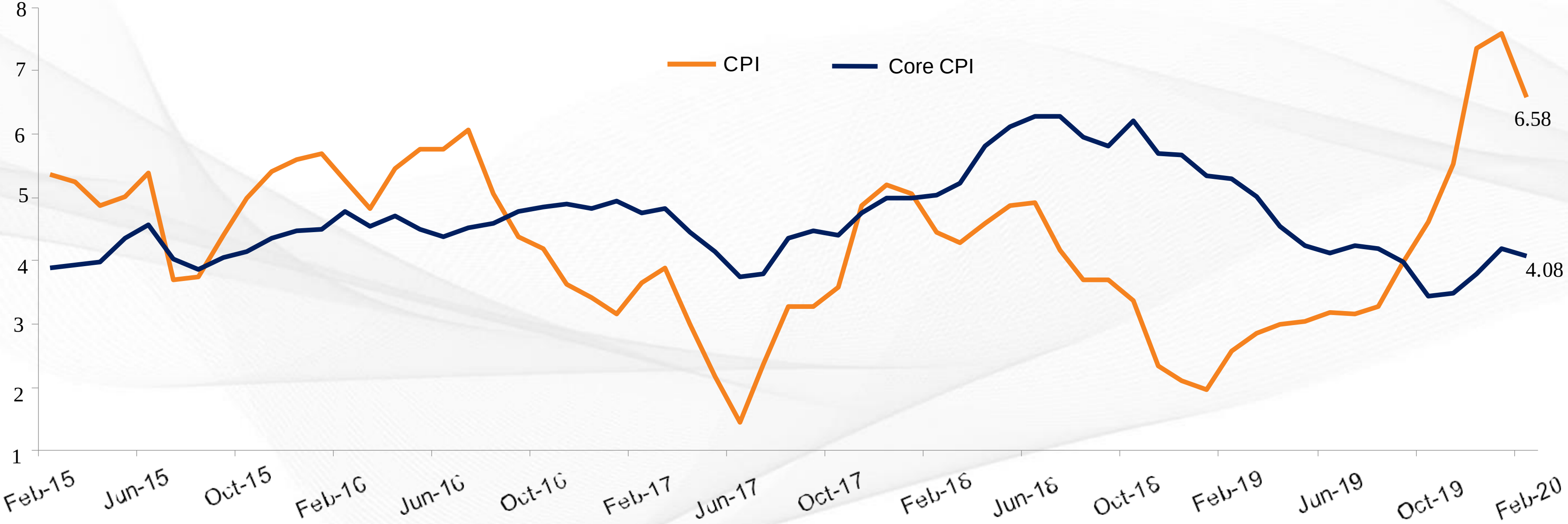
Nominal Interest Rate - Inflation = Real Interest Rate

A nominal interest rate includes inflation and other risk premia

Inflation is a general increase in the prices of goods and services in an economy

A real interest rate is the rate that adjusts for inflation and gives the real rate of bond or loan.

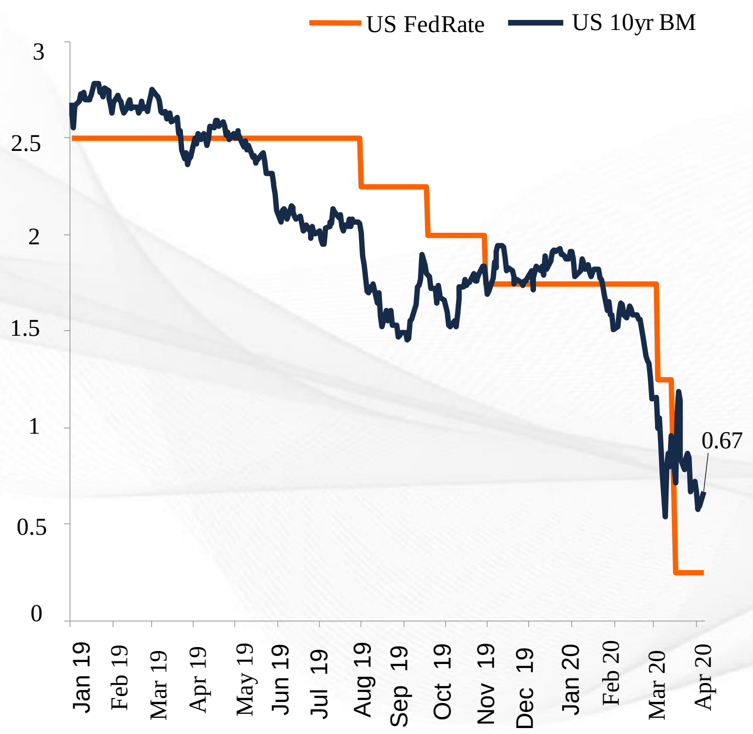
CPI Inflation

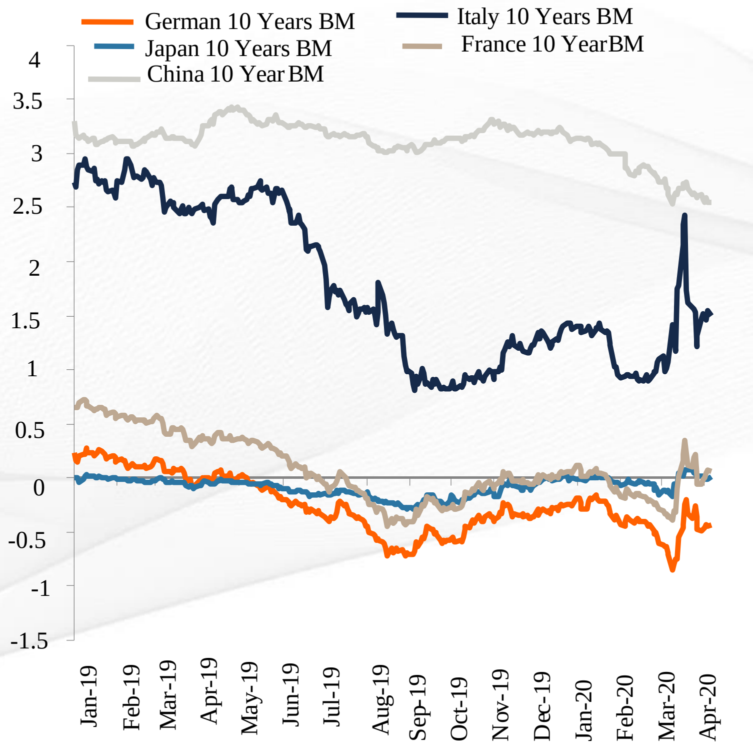


Source: RBI, Bloomberg, 31st March 2020

Financial Markets and Investments

Global Rates





Source: Bloomberg, Data as on 6th April 2020.

Financial Markets and Investments

RBI Repo Rate

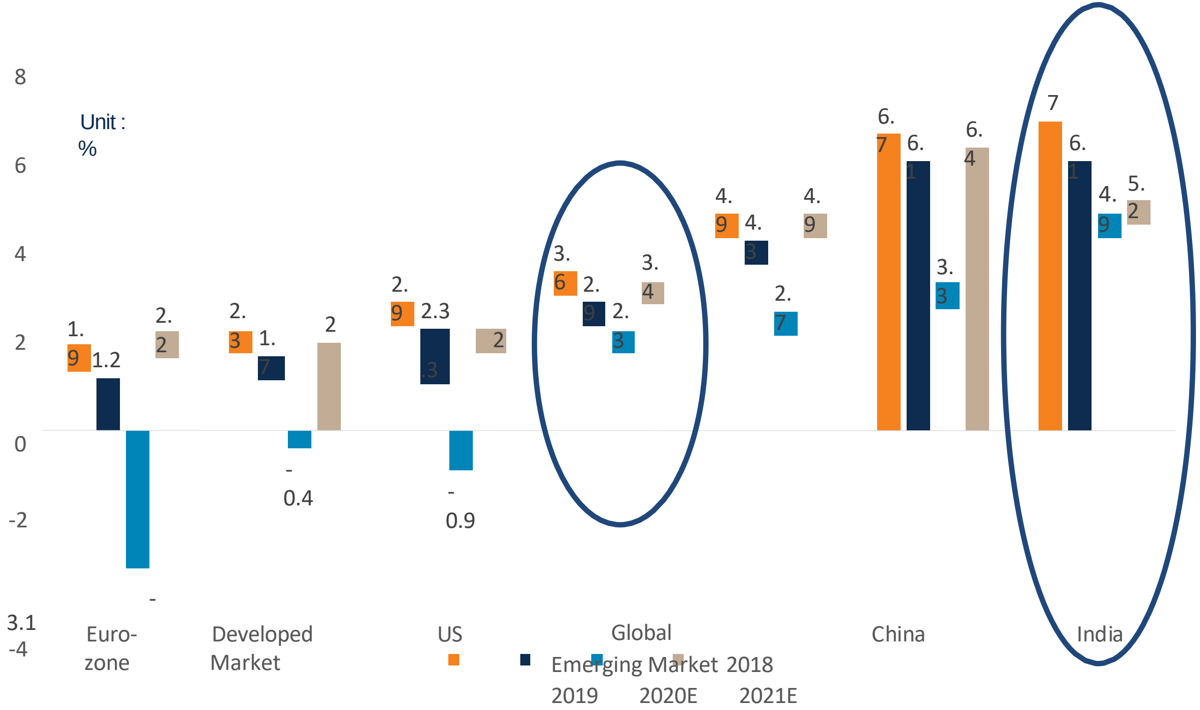
Change Date	Percentage
March 27 2020	4.400 %
October 04 2019	5.150 %
August 07 2019	5.400 %
June 06 2019	5.750 %
April 04 2019	6.000 %
February 07 2019	6.250 %
August 01 2018	6.500 %
June 06 2018	6.250 %
August 02 2017	6.000 %
October 04, 2016	6.250%

Economy Review 2020

	FY17	FY18	FY19	FY20E	FY21E
Real GDP Growth	8.2%	7.2%	6.8%	4.5%	5.0%
CPI Inflation	4.5%	3.6%	3.4%	4.0%	3.5%
Real Interest rate (Repo- CPI)	1.8%	2.5%	2.9%	2.1%	2.1%
Central Fiscal Deficit	3.5%	3.5%	3.5%	3.8%*	3.5%
Current Account Deficit	0.6%	1.8%	2.1%	2.0%**	2.0%**

Source: RBI, MOSPI, Bloomberg | * Budgeted for FY20, **as a % of GDP for 1QFY20 Data as on 31 st December 2020.

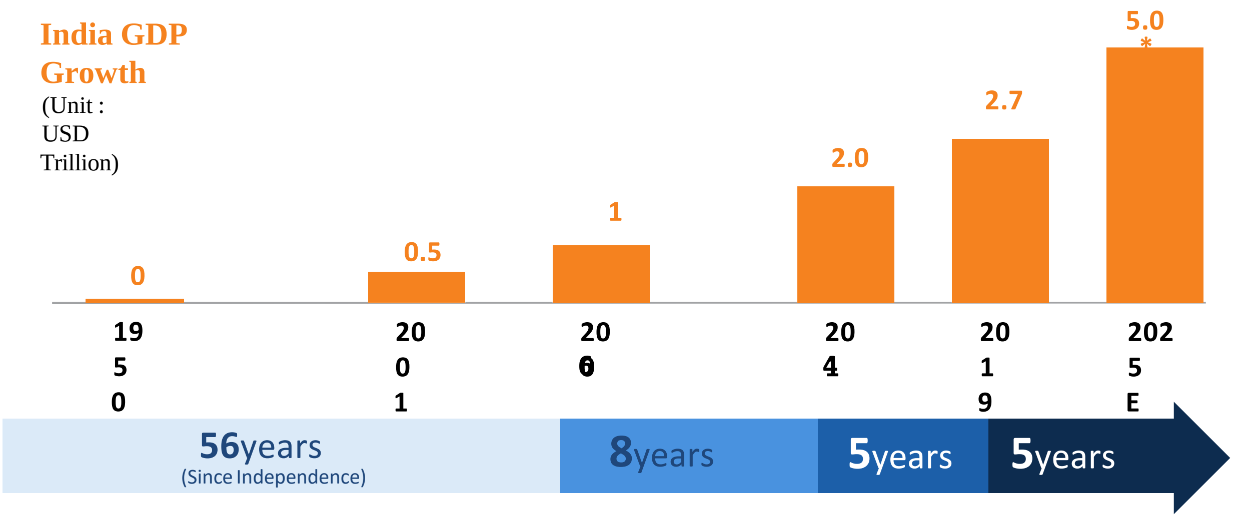
Global GDP Trends - IMF



Source: IMF, as on 31st March 2020. GDP Forecast for India is for 2018-19, 2019-20 & 2020 – 21 Fiscal Year. For the remaining geographies GDP forecast is for calendar year.

Financial Markets and Investments

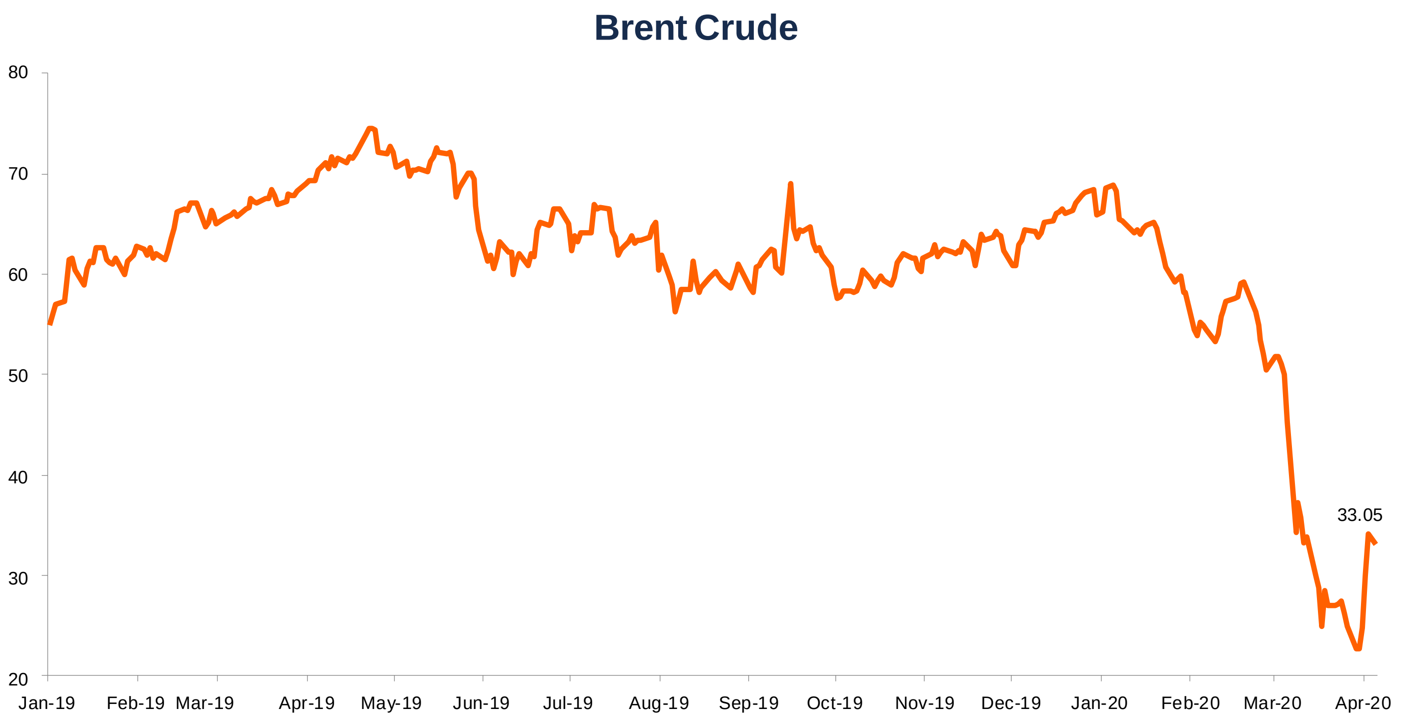
India a Huge Growth Opportunity



- 1st trillion took 56 years, 2nd – 8 years
- India's structural factors shouldhelp
- Efficiency gains through infrastructure, technology and reforms.

Source for above graphs: RBI, MOSPI, Bloomberg 31st Dec 2019 / * Based on the government's plan

Crude Oil

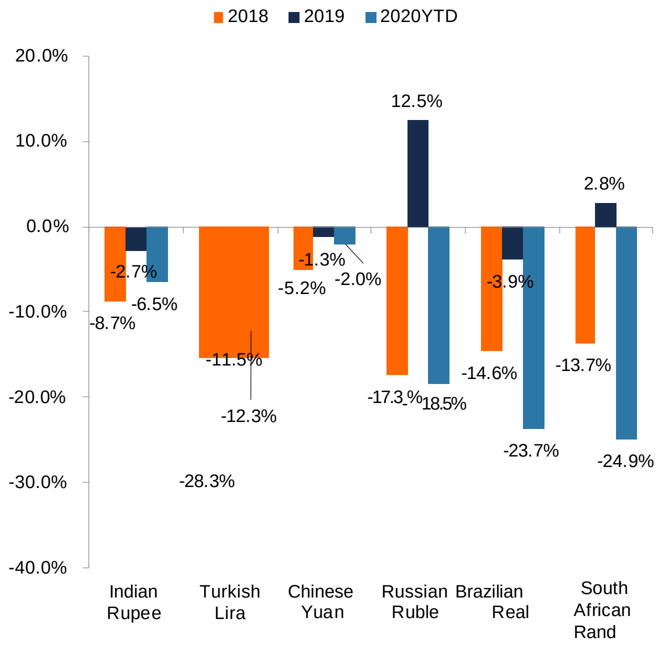


Source: Bloomberg, 6th April 2020.

Marae Asset Investment Managers (India) Pvt. Ltd.

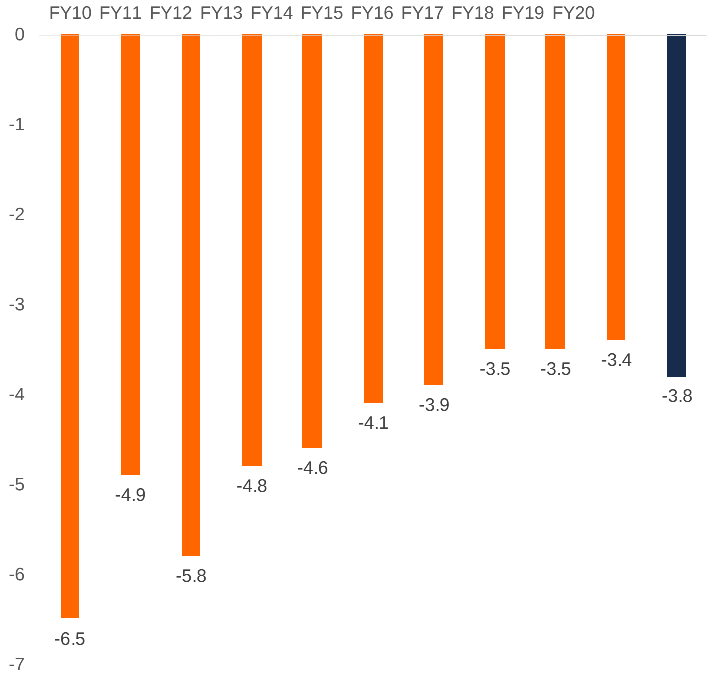
Fiscal Deficit a Challenge

Currencies Depreciation Continues in 2020 Again



Source: Bloomberg, 6th April 2020

Fiscal Deficit to GDP (%)



Financial Markets and Investments

Reforms

- IBC – December 2015
  - Resolution for stressed financial institutions
- MPC – June 2016
- RERA – May 2017
- GST – July 2017
- Corporate Tax – October 2019
  - Corporate tax rates cut to 22% from 30% (before surcharges).
- Privatization
  - Privatization of 5 PSU companies (including BPCL), IPO of LIC.
- Recapitalization and consolidation of PSU banks.
- Labor reforms- Industrial Relations Code, 2019

Source: Bloomberg

Financial Markets and Investments

Key Learning Outcome

- Markets: Debt, Equity, Money Market etc.
- Players, Platforms
- Exchange Traded Vs OTC
- Spot vs Forwards

Investment Vehicle

Historically, the three main asset classes have been equities (stocks), fixed **income** (bonds), and cash equivalent or money market instruments.
Currently, investment vehicle includes real estate, commodities, futures, other financial derivatives, and even cryptocurrencies to the asset class mix.

Regulated

Unregulated

Others

Debt

Commodities

Equity

Real estate

Crypto

Investment Avenues

- Non-Marketable Financial Assets
- Equity Shares
- Bonds
- Money Market
- Mutual Fund
- Life Insurance Policies
- Real Estate
- Precious Objects
- Financial Derivatives

Market Platforms & Players

- Issuers

- Central Government
- Local/ State Government
- Corporate

- Investors

- Banks
- Insurance
- Mutual Funds
- Provident Funds
- FIIs

- Intermediaries

- Exchanges
- Clearing Corporations
- Brokers
- Primary Dealers
- Investment Banks
- PDAI
- FIMMDA
- RBI
- SEBI
- IRDA

Investment Process

Key Learning Outcome

- Planning, Execution, Review & Feedback
- Evaluation: Return, Risk, Liquidity, Tax & Convenience

Investment Strategies

- **Active**

Active investment is a form of investment strategy that involves actively buying and selling assets in the hope of making profits and outperforming a benchmark or index.

- **Passive**

Passive investing is an investment strategy to maximize returns by minimizing buying and selling. Index investing in one common passive investing strategy whereby investors purchase a representative benchmark.

- **Trading & Investments**

Active trading is the act of buying and selling securities based on short-term movements to profit from the price movements on a short-term stock chart. The mentality associated with an active trading strategy differs from the long-term strategy.

Investment Management Process

Investment Objectives & Constraints		Strategic Asset Allocation		Security Selection Analysis		Execution	
Investment Policy Statement		Asset Allocation		Debt	Equity	Mode of Investment	
Goal		Equity		Credit Rating	Fundamental	Direct	
	Horizon		Bond	YTM			Mutual Fund
Liquidity		Commodity		Tax	Technical	PMS	
	Constraint		Alternatives	Liquidity			Alternative
Objective		Cash		Maturity	Behavioral	Other Vehicle	
Active	Passive	Asset type	Weight	Analysis	Selection	content	content

Investment Management Process

Performance Measurement

$$\text{Rate of Return} = \frac{\text{Annual Income} + (\text{End Value} - \text{Start Value})}{\text{Start Value}}$$

Example: Annual Income = Rs. 100, Start Value = 1000, End Value = 1030

Return = (100+(1030-1000))/1000 = 13%

Investment Management Process.. Cont.

Portfolio Review & Rebalancing-

It is therefore essential to review investments portfolio periodically.

Rebalancing is the process by which an investor restores their portfolio to its target allocation. Rebalancing brings portfolio back to the desired asset mix. This is done by reinvesting the profits that are taken out of some of the outperforming investments and putting them in underperforming assets.

Return: Arithmetic Average, Geometric Average, Internal Rate of Return

Risk Analysis

Beta, Duration

Appraisal Ratio

Sharpe ratio, Treynor ratio, M^2,

Style Analysis

Attribution Analysis

Portfolio Performance Evaluation

Investment Management Process

Behavioral Finance & Investments

Key Learning Outcome

- Behavioral Vs Traditional Finance
- Overcoming Behavioral Bias (Fear, Greed)

Introduction

- Behavioral Finance is the intersection of one's psychology and finance.

- It deep dives into irrational financial decisions. Behavioral Finance impacts the behavior of investors, analysts, advisors and other market players.

Financial Theory

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Traditional Financial Theory	Behavioral Finance Theory
Both the market and investors are perfectly rational	Investors are treated as “normal” not “rational”
Investors truly care about utilitarian characteristics	Investors are influenced by their own biases
Investors have perfect self-control	They actually have limits to their self- control
They are not confused by cognitive errors or information processing errors	Investors make cognitive & emotional errors that can lead to wrong decisions

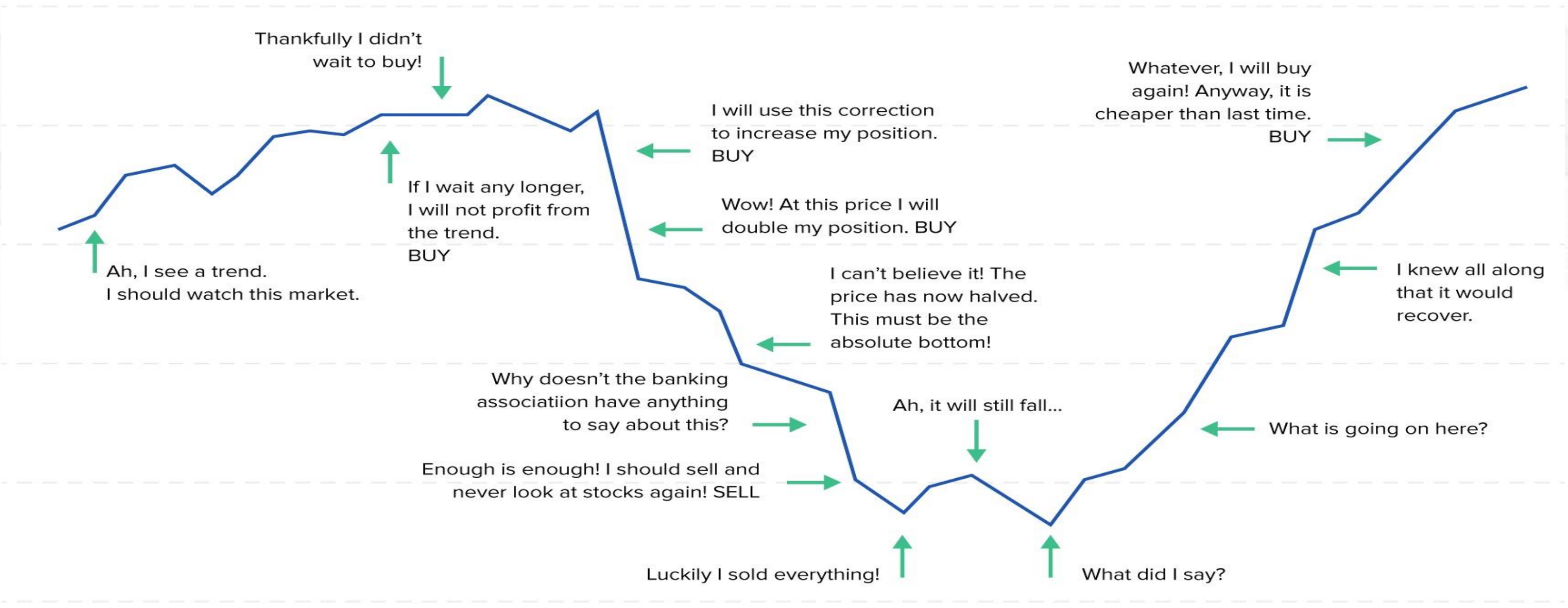
Common Behavioral Biases

- Overconfidence and illusion of control
- Self Attribution Bias
- Hindsight Bias
- Confirmation Bias
- Endowment Bias
- Representative Bias
- Framing Bias
- Anchoring Bias
- Loss Aversion
- Herding Mentality
- Status Quo Bias

"Behavioral biases are irrational beliefs or behaviors that can unconsciously influence our decision-making process. They are generally considered to be split into two subtypes- emotional biases and cognitive biases

Self-Transformation, Check & Change

Figure 1: Investment Process - Roller Coaster of Emotion



Source: Credit Suisse

Behavioral Finance & Investments

Self-Transformation, Check & Change

Anchoring Bias

- Acknowledge the anchor when making decisions.
- Understand, address, and remember the goal—not Wealth.
- Recognize that the ways choices are presented will affect the decision.

Status Quo Bias

- Stress-test portfolios/ Assets.
- Emotionally attached inappropriate assets?
- “Doing nothing” to goal-based Asset allocation

Recency Bias

Yesterday’s truth is not tomorrow’s
No pattern continues for ever.

Myopic Loss Aversion

- Financial losses are often locked in by panic selling.
- Keep a focus on the long term goals in order to drive success. affect the decision.

Self-Attribution Bias

- Review: where you made/ lost money.
- Look for patterns in poor unprofitable decisions.
- Learning from past mistakes and becoming smarter and more successful

Ambiguity Aversion

- Outcomes should drive your actions, not the fear of unknown.
- Goal-based planning is key to success.

Confirmation Bias

- Admit that different situations call for different expertise
- Seeking out confirmation of options is a way to “group think”

Overconfidence Bias

- Diversify portfolios.
- Excessive trading hazardous to wealth
- Review past trading/ investments to discover poor decisions, if any

Herding Bias

- Running with the crowd wont keep you from being wrong.
- By the time everyone is heading towards one direction, it is usually time to start heading the other way. affect the decision.

Thank You