

Learning Objective Unit No. 2

- ❑ Explain how macroeconomic factor affect the prices of stock
 - ❑ Analyze Industry Prospects
 - ❑ Identify the Qualitative factor that affect company prospects
 - ❑ Explain the difference between fundamental and technical analysis
 - ❑ Explain various Charting techniques
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Fundamental Analysis

“The right to happiness is
fundamental.”

[Anna Pavlov](#)

Definition

- Fundamental analysis is basically an attempt to analyze all the fundamentals and basic factors that affect risk and return of securities



Chemistry of Intrinsic value and market value

- Intrinsic value-In finance, **intrinsic value** refers to the value of a security which is intrinsic to or contained in the security itself. It is also frequently called **fundamental value**
- Significance of intrinsic value is that it helps to find out misplacement of values of securities.



Decisions on basis of I_v

- $I_v > M_p$ (buy the security)
- $I_v < M_p$ (Sell the security)



Process

- Economic Analysis
- Industry Analysis
- Company analysis



Economic Analysis



- Macro- economic factors
 - Global factors
 - Fiscal policy
 - Monetary policies
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Macro-economic factors

- ❑ Growth Rate and Gross Domestic Product-
- ❑ It is the measure of total production of final goods and services in the economy during specific period usually a year.
- ❑ Forecasting the GDP Growth Rate-
- ❑ Estimate most likely growth rate of three sectors
- ❑ Calculate the weighted average of three rates
- ❑ Note the weight of sector is being its

Industrial growth rate

- The higher the growth rate of industrial sector, *ceteris paribus* it is more favorable it is for stock market.
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Other factors

- Unemployment.
- Inflation rate & Price Level
- Growth in GDP
- Balance of Payments, Forex Reserves and Exchange rates
- Agriculture & Monsoon
- Savings & Investments
- Foreign exchange reserves
- Economic and Political policies
- Infrastructural facilities.
- Technological innovations.

Global Factors

- ❑ SWOT
- ❑ Profitability of the country
- ❑ Global competition in respect to exports



Fiscal Policies



- Policies which are concerned with the spending and tax initiatives of the government. It is the most direct tool to stimulate or dampen the economy.
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Monetary Policies

- ❑ Policies which are concerned with the manipulation of the money supply in the market. Monetary policy affects the economy mainly through its impact on interest.
- ❑ Bank Rate
- ❑ Reserve Requirement
- ❑ Direct credit controls



Analysis of Indian economy

- ❑ Monsoon
- ❑ Effect of mixed economy
- ❑ Monetary policies
- ❑ General business conditions
- ❑ Economic and political stability
- ❑ Debt on country



Technical Analysis

Technician has elected to study, not the mass of fundamentals, but certain abstractions, namely the market data alone. – John Magee.

What is technical analysis?

- It is a method of evaluating securities by analyzing the statistics generated by the market activity, such as past prices and volume. Technical analysis do not attempt to measure a securities intrinsic value, but instead use charts and other tools to identify patterns that can suggest future activity.
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Y Technical Analysis?

- For short term investment
 - Demand and supply in marketplace
 - Easy for technician to predict the trend
 - Concrete evidences for predictions
 - Basic Technical Assumptions-
 - The market Discounts everything
 - Price moves in trends
 - History trends repeat itself
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Dow Theory

- ❑ Originated by Charles Dow (one of the most oldest and famous technical tools)
 - ❑ According to Dow- "The market is considered to have three movements all going at the same time. The first is narrow from day-to-day. The second is short- swing, running from two-weeks to a month or more, the third is the main movement covering at least four years.
 - ❑ Primary trends
 - ❑ Secondary trends
 - ❑ Minor Trends
 - Dow-Jones Transportation Average.
 - Bullish Market- If both the averages are moving upwards.
 - Bearish Market- If both the averages are falling down
 - Uncertain Market- When both are showing odd movements
 - Signal to sell- If one average start falling after a period of rising stock prices
 - Signal to buy- if after a downfall in both the averages, one of the average shows upward trend.
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Criticism to Dow theory

- ❑ Not a theory it is an interpretation of known data.
 - ❑ It is not acceptable in its forecast.
 - ❑ It has poor predictive power.
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Tools of technical analysis

- Daily fluctuations or volatility
 - Floating stock and volume of trade
 - Price trends and volume trends
 - Rate of change of prices
 - Japanese candlestick approach
 - Dow theory
 - Elliot waves theory
 - Theory of gaps
 - Advance decline and spread in market.
 - Relative strength index.
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Tools and Techniques

- The technician for doing technical analysis-
 - Identify the trend
 - Recognize when one trend comes to an end and prices set off in the opposite direction
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Types of trend

- Uptrend
 - Downtrends
 - Sideways/Horizontal trends.
 - Trend Lengths-
 - I. Long- term trend
 - II. Intermediate trend
 - III. Short-term trend.
 - Trend lines
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Technical Analysis- Chart Types

□ Line Chart

- The most basic type of chart, Shows only closing price.
- Do not provide information like High, low, opening, closing Price
- Closing price is often considered as the most important price so line chart reflects only that.

□ Bar Charts

- These are easy to draw and easy to interpret.
- It shows high, low and closing price of

□ Candlestick charts-

- The drawing principle is same as that of the bar chart.
- ~~Candlesticks also rely heavily on the use of colors to explain what has happened during trading period.~~
- When the price of stock is up and closes above the opening trade, the candlestick is usually white or clear.
- If the stock has traded down for the period, then the candlestick will usually be black or red.
- If the stock's price has closed down above the previous days close but below the day's open, candlestick will usually be black or any color which is used for such situation by the site.
- Opening and closing at the same level – Doji Candlestick

Reference

- Investment Analysis and Portfolio Management By Prasanna Chandra
 - Investment Management By Bhalla
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