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An analytical study of successful asset management

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Abstract

Different experts in finance have also documented that a specific and continuous strategy or style of the investors or fund managers also result into inefficiency of the stock market. Sharpe (1988, 1992) proposed "Style Analysis" as a factorial model which reflects mutual fund strategies without requiring data on the historical portfolio holdings. Sharpe opined in this model that it is style parameters of various fund managers which generates extra returns on a portfolio. Style plays a crucial role specially when a fund is managed by multi-managers and consistency in their styles directly influence the benefits expected from that fund. Furthermore, style consistency is critical in allowing a centralized manager to construct a blended portfolio with the ex ante desired risk-return properties. If growth (value) managers do not remain faithful to growth (value) stocks over time and roll their portfolio away from stocks belonging to their self-stated style specialization, then this is going to lead to an increase in the potentially diversifiable risk in the overall portfolio to the extent that their active positions correlate with other managers. This style drift could have adverse effects on the underlying fund's performance, risk and other fund attributes. In present time, the successful Asset Management Companies have developed investment strategies on a set of beliefs that narrate what is considered as 'Best Investment' by them.

Keywords: Blended portfolio, investors' behaviour, asset management, stocks, India

1. Introduction

The strong form of market efficiency hypothesis states that the current price fully incorporates all the existing information, both public and private (sometimes called inside information). The main difference between the semi-strong and strong efficiency hypotheses is that in the latter case, nobody should be able to systematically generate profits even if trading on information *not* publicly known at the time. In other words, the strong form of EMH states that a company's management (insiders) will not be able to systematically gain from inside information by buying company's shares ten minutes after they decided (but did not publicly announce) to pursue what they perceive to be a very profitable acquisition. Similarly, the members of the company's research department are not able to profit from the information about the new revolutionary discovery they completed half an hour ago. The rationale for strong-form market efficiency is that the market anticipates, in an unbiased manner, future developments and therefore, the stock price may have incorporated the information and evaluated in a much more objective and informative way than the insiders. Not surprisingly, though, empirical research in finance has found evidence that is inconsistent with the strong form of the EMH. For example, if the current market price is lower than the value justified by some piece of privately held information, the holders of that information will exploit the pricing anomaly by buying the shares. They will continue doing so until this excess demand for the shares has driven the price up to the level supported by their private information. At this point they will have no incentive to continue buying, so they will withdraw from the market and the price will stabilize at this new equilibrium level. This is called the strong form of the EMH. It is the most satisfying and compelling form of EMH in a theoretical sense, but it suffers from one big drawback in practice. It is difficult to confirm empirically, as the necessary research would be unlikely to win the cooperation of the relevant section of the financial community—insider dealers.

Share prices reflect all information, public and private, and no one can earn excess returns. If there are legal barriers to private information becoming public, as with insider trading laws, strong-form efficiency is possible, except in the case where the laws are universally agreed

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upon. To test for strong form efficiency, a market need not exist where investors can consistently earn deficit returns over a short period of time. Even if some money managers are not consistently observed to be beaten by the market, no refutation even of strong-form efficiency follows: with hundreds of thousands of fund managers worldwide, even a normal distribution of returns (as efficiency predicts) should not be expected to produce a few dozen "star" performers.

1.1 Strong Form Market Efficiency

The strong form market efficiency occurs if the stock price reflects all public and private information. This form is the most comprehensive case and testing EMH in strong form is very difficult, because private information is difficult to observe. In USA, there is an official document by the Security Exchange Commission (SEC), which contains an official summary of insider trading, giving a record of trading transactions by officers, directors and major stock holders using private information. If these trades result in abnormal return, then the market is not efficient in strong form. Testing of EMH in the strong form is conducted in different ways: first, testing the return that is earned by the insider, as defined in SEC documents; second, using indirect test by examining the return and trading volume prior to public announcement.

1.2 Trading by Insiders

Insiders are defined by the SEC as any manager, directors or owners who own at least 10 percent of a firm's shares. There are many restrictions on insider trading which prevent them from selling any stock before minimum holding period for at least six months and any profit made as a result of the violation of these restrictions must be returned to the company. Testing EMH in the strong form is performed by examining the market reaction to insiders trading as reported by SEC. Penman (1982) examines the insider trading around earning forecasting the announcement, by which they can achieve high abnormal return. Therefore, insiders do indeed have private information that is not impounded in the stock price.

2. Review of Literature

Santhapparaj and Reddy (2000) studied the weak form of market efficiency with the help of selected stock returns for the period January 1993 to December 1995. Out of 32 actively traded stocks, 20 stocks have been randomly selected from the Mumbai Stock Exchange official directory. It was found that out of 121 rank correlation coefficients, 78.52 percent were positive. For the monthly data, 16 coefficients were significant at 5 percent level and

none was negative. However, correlation coefficients based on the quarterly prices showed that only 39.40 percent (20 coefficients) have statistically significance at 10 percent, but none of the negative coefficients have statistical significant value. Therefore, it was identified that market was efficient in short period.

Choudhary (2000) investigated the stochastic structure of individual stock indices in seven countries: United States, United Kingdom, Canada, France, Germany, Japan and Italy. The Augmented Dickey-Fuller and KPSS unit root tests and Johansen's co integration tests were used to test the log of monthly stock indices from the period 1953 to 1989. He concluded that stock markets in seven countries are efficient during the sample period. Their result from both unit root tests showed that all seven series seem to contain a stochastic trend (unit root) and they are non-stationary in levels. The result of Johansen's co integration test showed no support for a stationary long-run relationship between the seven stock series. Absence of long-run multivariate relationships also provided evidence of efficient markets.

Chawla and Makkad (2001) analysed whether the Indian Stock Markets were efficient in weak form with the help of data on 49 scrips. The study was related to the period April 1996 to March 2000. The sample stocks were distributed among 9 industry groups. The study has noted that out of 166 correlations computed for various lags, 3 were positive in sign and 55 were negative in sign. Further that the highest and lowest percentage of positive rank correlation was for one month and one year lag period respectively. The percentage of positive rank correlation coefficients being 95.65, 54.54, 70.73 and 40 percent for one month, three months, six months and one year lag periods, respectively. But there was absence of any systematic pattern that emerges in the decline of positive rank correlation coefficients with the varying length of lag. The results of the study have also showed that the proposition regarding relative strength theory may be accepted for the one month lag period. But no substantial result was obtained for the relative strength hypothesis to hold good for lag period of three months and above.

3. Objective of the Study

The main objective of this research paper is to study validity of EMH in semi strong form in the Indian Stock Market through successful asset management.

4. Analysis and Interpretation

In this section of the research paper results and discussions are made as follows:-

Table 1: AARs & CAARs under Single Index Model (1999-2000)

DAYS	AARs	t stat for AARs	CAARs	t stat for CAARs
-20	0.989	0.896	0.989	0.896
-19	1.709	1.173	2.698	1.490
-18	-1.372	-0.917	1.326	0.566
-17	-0.364	-0.346	0.963	0.377
-16	-1.963	-1.537	-1.000	-0.350
-15	-1.968	-1.894s	-2.968	-0.979
-14	-1.655	-2.576**	-4.624	-1.516
-13	0.520	0.556	-4.104	-1.289
-12	0.521	0.363	-3.583	-1.030
-11	2.161	1.229	-1.422	-0.369
-10	0.703	0.393	-0.719	-0.171
-9	-0.732	-2.663**	-1.451	-0.352

-8	-0.110	-0.137	-1.561	-0.374
-7	2.119	1.750	0.558	0.128
-6	1.201	0.951	1.759	0.389
-5	3.010	2.995**	4.769	1.029
-4	-1.643	-1.247	3.126	0.649
-3	-1.339	-0.781	1.788	0.352
-2	-1.732	-1.638	0.056	0.011
-1	-2.668	-2.855**	-2.612	-0.496
0	1.285	0.682	-1.327	-0.239
1	-0.558	-0.273	-1.885	-0.322
2	-0.357	-0.352	-2.242	-0.377
3	0.582	0.387	-1.660	-0.271
4	-1.145	-0.579	-2.805	-0.438
5	2.223	1.838	-0.581	-0.089
6	0.526	0.266	-0.055	-0.008
7	0.451	0.389	0.396	0.058
8	0.587	0.561	0.983	0.142
9	-0.953	-1.202	0.030	0.004
10	-1.614	-1.063	-1.584	-0.222
11	-1.253	-1.271	-2.837	-0.395
12	1.233	1.031	-1.604	-0.220
13	-0.243	-0.160	-1.847	-0.248
14	-0.705	-0.416	-2.552	-0.335
15	-0.532	-0.398	-3.084	-0.399
16	0.973	1.646	-2.111	-0.273
17	-1.106	-0.881	-3.217	-0.411
18	-1.854	-1.565	-5.071	-0.640
19	0.608	0.503	-4.462	-0.557
20	0.239	0.186	-4.223	-0.521

Source: Data compiled from CMIE Prowess Database.

**Significant at 5 percent level of significance *Significant at 10 percent level of significance.

Table 2: AARs & CAARs under Single Index Model (2000-2001)

DAYS	AARs	t stat for AARs	CAARs	t stat for CAARs
-20	-1.433	-1.675	-1.433	-1.675
-19	-1.046	-0.802	-2.479	-1.624
-18	2.003	1.124	-0.477	-0.209
-17	0.615	1.168	0.138	0.062
-16	1.267	1.108	1.406	0.560
-15	1.110	1.611	2.516	0.978
-14	-1.029	-0.433	1.487	0.453
-13	0.456	0.360	1.943	0.553
-12	3.850	3.067**	5.792	1.552
-11	1.076	1.038	6.868	1.775
-10	-0.267	-0.451	6.601	1.707
-9	1.357	1.484	7.958	2.006
-8	0.009	0.013	7.967	1.987
-7	1.410	2.161*	9.377	2.322*
-6	-0.574	-0.393	8.804	2.058
-5	0.350	0.414	9.154	2.102
-4	0.363	0.256	9.517	2.084
-3	-2.618	-1.465	6.898	1.420
-2	0.217	0.130	7.115	1.392
-1	0.436	0.405	7.551	1.446
0	2.641	2.258*	10.192	1.904
1	0.606	0.667	10.798	1.991
2	-0.045	-0.050	10.753	1.959
3	-2.563	-2.378*	8.190	1.464
4	0.561	0.256	8.752	1.479
5	-3.805	-2.142*	4.946	0.804
6	2.826	1.730	7.772	1.224
7	0.241	0.707	8.013	1.272
8	1.192	0.850	9.204	1.427
9	0.273	0.216	9.478	1.441
10	2.035	0.837	11.513	1.667
11	1.955	1.588	13.469	1.920
12	-3.143	-3.497**	10.325	1.462
13	-0.638	-1.257	9.687	1.375

14	-0.301	-0.276	9.386	1.317
15	0.941	0.678	10.327	1.422
16	-2.977	-2.195*	7.350	0.995
17	0.381	0.464	7.731	1.042
18	0.260	0.116	7.991	1.040
19	3.387	1.778	11.378	1.442
20	-1.450	-2.524*	9.928	1.260

Source: Data compiled from CMIE Prowess Database.

**Significant at 5 percent level of significance. *Significant at 10 percent level of significance.

Table 3: AARs & CAARs under Single Index Model (2002-2003)

Days	AARs	t stat for AARs	CAARs	t stat for CAARs
-20	-0.090	-0.153	-0.090	-0.153
-19	-0.272	-0.523	-0.362	-0.462
-18	-0.727	-1.031	-1.089	-1.040
-17	0.500	0.731	-0.588	-0.471
-16	-0.423	-0.548	-1.011	-0.692
-15	3.123	3.109*	2.112	1.210
-14	0.591	0.443	2.703	1.275
-13	1.619	1.223	4.322	1.763
-12	-0.768	-0.428	3.553	1.221
-11	0.151	0.172	3.704	1.219
-10	-0.981	-2.891*	2.722	0.908
-9	1.436	1.699	4.158	1.335
-8	-0.689	-0.840	3.469	1.077
-7	-1.292	-4.006**	2.176	0.682
-6	0.281	0.341	2.457	0.746
-5	1.680	4.540**	4.137	1.261
-4	1.088	1.980	5.226	1.576
-3	-0.904	-1.477	4.322	1.283
-2	-0.002	-0.002	4.320	1.226
-1	-0.318	-0.227	4.002	1.068
0	1.394	0.513	5.396	1.269
1	-1.144	-0.488	4.252	0.914
2	-0.192	-0.119	4.061	0.831
3	-2.482	-3.361**	1.579	0.320
4	0.494	1.647	2.074	0.423
5	0.028	0.020	2.102	0.414
6	0.117	0.247	2.219	0.437
7	-1.181	-22.511**	1.038	0.208
8	-0.438	-0.873	0.600	0.120
9	-0.575	-1.846	0.025	0.005
10	1.104	0.677	1.130	0.218
11	-1.571	-2.674*	-0.441	-0.085
12	-0.408	-0.669	-0.849	-0.162
13	0.700	1.181	-0.149	-0.028
14	-0.040	-0.048	-0.189	-0.035
15	-0.432	-0.812	-0.620	-0.116
16	0.069	0.075	-0.551	-0.102
17	0.669	0.884	0.118	0.022
18	-1.011	-1.319	-0.893	-0.162
19	0.500	0.753	-0.393	-0.071
20	-0.076	-0.163	-0.468	-0.084

Source: Data compiled from CMIE Prowess Database.

**Significant at 5 percent level of significance. *Significant at 10 percent level of significance.

During 2000-2001, AAR occurred significant on the event day at 10 percent level. It is also found significant on t-7 day at 10 percent level and on t-12 day at 5 percent level. It is again found significant on 3rd, 5th, 16th and 20th days at 10 percent level and on 12th at 5 percent level in post-event window. CAAR is found positive throughout all the days in pre and post-event window except on 18th, 19th and 20th days in pre-event window. It is found significant on t-7 day at 10 percent level.

Positive AAR is found on the event day during 2002-2003, though it is not significant. AARs are found significant on t-

5 and t-7 at 10 percent level. It occurred significant on 10th and 15th days at 10 percent level in the estimation window. AARs are found significant on 3rd and 7th days at 5 percent level after the happening of the event and on 11th day at 10 percent level. Positive CAARs are found for 27 days before and after happening of the event. The cumulative average abnormal returns were found negative during -20 to -16 days and some depictions of negative CAARs were also found after happening of the event. But it is interesting to note that the chains of positive CAARs were continued after the occurrence of the event. The CAARs during all the days

of pre-event window and post-event window were found statistically insignificant and validated the null hypothesis of informational efficient market in India during the year.

Table 2 has reported the findings of average abnormal returns and cumulative average abnormal returns during 2002-2003. The negative sign of average abnormal returns during the estimation window and post event window indicated the under performance of the market around the bonus announcement day. During all the 20 days before and 4 days after the event, on the day of the event and t+12 to t+20 negative CAARs were found indicating lower actual returns of the securities from their expected returns. The investors must have over expected causing negative abnormal returns to them. During this period, there can be irrationality in the behaviour of market movement due to excessive positive rumours. The investors are in a hurry to earn abnormal returns; therefore, a general tendency of over expectations may be noticed in their investment behaviour. The AARs were found significant on t-17, t-18 and t-19 days at 5 percent level. It is found significant on t-13 day and t+12 day at 10 percent level. CAARs are found significant on t-15 to t-19 days at 5 percent level and on t-14 day at 10 percent level. It is also found significant on t-13 to t-10 days at 5 percent level and t-9 and t-8 days at 10 percent level. Furthermore, CAARs are not found significant continuously for 28 days from t-7 to t+20 days.

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