

# A Study on Stock Selection Behaviour of Individual Investors based on Nifty 50 Holdings

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## ABSTRACT

Investment decisions are the result of investment analysis which involves a thorough analysis of information disclosed by companies. Stock investments are more sensitive to information (both quantitative and qualitative). Individual investors' preference for specific stock over available stocks depends largely on the financial information of a company. Investors attach different levels of importance to each attribute of a stock while selecting stocks for investment. The present study is an attempt to identify the preferred stock attributes of retail investors based on shareholding in Nifty fifty stocks for the quarter ending March 2018. The study is based on secondary data and the data sources include NSE and other stock analysis websites and online research articles. From the analysis, the study found that FMCG is the most preferred sector and retail investors display high preference for low risk, low leverage and high valued stocks. Further, retail investor investment found high in stocks with low promoter holding and high domestic institutional holding. Understanding the stock selection behaviour of individual investors is of high importance to regulators and stock market analysts as it helps them to identify the areas that need to be focused more for increased investment from individual investors that result in stock market development thereby economic growth.

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## 1. Introduction

In long run, the economic well being of an individual is determined by the kind of investments he or she made. The investment decisions of an individual are largely guided by the investment objectives. Individuals in general seek for low risk and high return investments. Stock investment has the better potential to deliver high inflation adjusted returns compared to other asset classes over a longer period of time. However, to enjoy such returns, a thorough analysis should be made by the investor on the stock fundamentals and technical aspects. A critical review of information furnished by companies helps an investor in understanding its long-run return prospects. Stock investments are more sensitive to information (both quantitative and qualitative). Quantitative information includes information relating to financial performance of a firm. On the other hand, qualitative information includes information relating to environment, CSR and corporate governance factors. The performance of stock market depends on the investor response to information.

The availability of so much of information and many options in the present investment market, selecting a good stock can be a daunting task for an average investor but it is must to create long term wealth. Though predicting the stock performance is not so easy, but it can be better assessed by the financial indicators presented in the annual reports of companies. Dutta, Bandopadhyay, and Sengupta (2012) investigated the influence of financial ratios on the performance of actively traded stocks in Indian stock market. The study concluded that financial ratios are helpful in predicting the outperforming shares.

Investors attach different levels of importance to each financial ratio while picking stocks. The criteria for stock selection differ with the category of investor. Aggressive investors seek for capital appreciation, while conservative investors look for capital preservation. Further, with respect to reference time period, some investors look at recent performance and go for investment whereas other investors consider long term performance of the stock before making investment. There exist another class of investors who do not analyze publicly available information but make stock investments just based on advices of stock brokers, family and friends. Understanding the investment decision making process and preferred stock attributes of individual investors is of utmost significance as it not only helps in stock market development but also helps in fueling country's economic growth.

## 2. Review of Literature

Investment decision making involves analyzing various investment opportunities that demands information. Information disclosed by companies has significant impact on prices of the stock and there by impacts the investor stock selection. Bogdan DIMA and Otilia SARAMAT (2013) investigated the impact of publicly available information on market value of Romanian companies stocks listed on Bucharest Stock Exchange and found that information has value relevance in stocks' market value. The Stock investment decisions are majorly guided by the financial information disclosed by the companies. The financial statements and ratios have profound impact on stock selection behaviour of investors. Joshua Aron, G. Namusonge & Maurice Sakwa (2014) studied the impact of financial information on share investment in Kenya and concluded that retail investors of Kenya attach much

significance to financial information before making share investment. Gunathilaka C (2014) also investigated the influence of various stock attributes on stock selection decision of retail investors' of Colombo Stock Exchange and found that financial information followed by broker advice have significant impact on equity selection decision of retail investors Srilanka. Besides financial information, non-financial information also gaining prevalence in stock market investment analysis. Imran Ali and Kashif Ur Rehman (2013) examined the stock selection behaviour of small investors in Pakistan. The study adopted Structural Equation Modelling (SEM) and identified stock attributes such as dividend and yields, firm's industry, price trends and volatility, firm's market status, source of recommendation, firm's reputation, CSR, Firm's visibility in media have significant and positive influence on individual investors' equity investment decisions.

### 3. Objective and Scope of the Study

The primary objective of the present study is to identify the preferred stock attributes of retail investor based on shareholding in Nifty 50 stocks. The study considered only retail investors (investments upto 2 Lakhs) category under individual investors segment. The present research limited its scope to finding the preferred financial attributes of retail equity investors.

### 4. Research Methodology

The study is based on secondary data. The data sources include National Stock Exchange website and other stock analysis websites and online research articles. The study made analysis from data collected for the period March 2018.

### 5. Data Analysis

**Table - 1**  
**Sector Preference of Retail Investors**

Sector	Average Retail Share Holding (%)
Automobile	6.3
Chemicals	8.6
Communication	0.46
Construction	9.66
Energy	3.1
Financial	5.8
FMCG	9.9
Healthcare	8
Metals	8.1
Services	1.8
Technology	4

Source: NSE

**Table - 2**  
**Shareholding Structure Analysis**

Range	Category	Average Retail Share Holding (%)
<b>A. Promoter Holding</b>		
	i) No Promoter Holding	9.2
Low	ii) Promoter Holding < 25%	5.6
Medium	iii) Promoter Holding 25% - 50%	7
High	iv) Promoter Holding > 50%	4.3
<b>B. FII Holding</b>		
Low	i) FII Holding < 20%	5.8
Medium	ii) FII Holding 20 - 40%	6.1
High	iii) FII Holding > 40%	4.9
<b>C. DII Holding</b>		
Low	i) DII Holding < 10%	5
Medium	ii) DII Holding 10 - 20%	5.3
High	iii) DII Holding > 20%	7.6

Source: NSE

**Table - 3**  
**Preferred Valuation Ratios of Retail Investors**

Range	Valuation Ratios	Average Retail Share Holding (%)
<b>A. Free Float Market Capitalisation<sup>1</sup></b>		
Low	i) M'Cap < 50000 Cr	5.2
Medium	ii) M'Cap : 50000 - 100000 Cr	5.4
High	iii) M'Cap > 100000 Cr	7.5
<b>B. Price-Earnings (PE) Ratio<sup>2</sup></b>		
Low	i) PE < 25	5
Medium	ii) PE : 25 - 50	6.2
High	iii) PE > 50	6.9
<b>C. Price-Book (PB) Ratio<sup>2</sup></b>		
Low	i) PB < 5	5.5
Medium	ii) PB : 5 - 10	5.5
High	iii) PB > 10	8.1

Source: 1. NSE Fact Book 2018 & 2. Value research online

**Table – 4**  
**Dividend and Risk Preference**

Range	Dividend & Risk Factors	Average Retail Share Holding (%)
<b>Dividend Yield<sup>1</sup></b>		
Low	i) Dividend Yield < 1%	6
Medium	ii) Dividend Yield : 1 - 3%	7
High	iii) Dividend Yield > 3%	2.9
<b>Standard Deviation of Daily Returns (%)<sup>2</sup></b>		
Low	i) Std.Dev < 1%	6.3
Medium	ii) Std.Dev 1 – 2%	5.8
High	iii) Std. Dev > 2%	4.9

Source: 1. Value Research Online & 2. NSE Fact Book 2018

**Table – 5**  
**Capital Structure Analysis**

Range	Total Debt to Equity Ratio	Average Retail Share Holding (%)
	i) Debt to Equity Ratio = 0	5.5
Low	ii) Debt to Equity Ratio < 0.5	7.2
Medium	iii) Debt to Equity Ratio: 0.5 - 1	3.9
High	iv) Debt to Equity Ratio > 1	4.9

Source: RediffMoney

Note: The Categorization and labeling as Low, Medium and High for all the above tables are based on Author convenience

## 6. Findings

1. FMCG Sector is the most preferred and Communication is the least preferred sector by retail investors.
2. From the shareholder structure analysis, it is found that small investors prefer to invest in those companies with no or less holding by promoters followed by average FII holding and high DII holdings.
3. With respect to free float market capitalization, individual investors prefer to invest in high market capitalization companies. Firms with Price to Earnings ratio (PE) greater than 50 found high retail investors holding that indicate growth stocks are more appealing to retail investors. Fundamentally strong companies i.e., Price-Book ratio with greater than 10 attracted high retail investments.
4. In general, retail investors are risk averse or very little risk takers. Accordingly, stocks with less return

volatility bagged high retail investments. The preference for low dividend yield stocks shows that income stocks are less appealing to retail investors.

5. With respect to leverage, retail investments found high in low leveraged companies i.e., companies with low debt to equity enjoyed comparatively high retail investor investments.

## 7. Conclusion

Financial characteristics significantly influence stock market participation in India, Bennet.E., & Selvam. M. (2013). However the extent of influence of various financial characteristics will not be same for all investors. Hence a proper analysis of factors influencing stock selection behaviour of small investors is essential as it provide valuable insights to stock market regulator and analysts that help them to discover the areas that need serious attention for much more investments from retail investors.

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