Security Analysis

Meaning of Security Analysis

Security analysis is the systematic process of **evaluating securities** such as shares, bonds, debentures, and other financial instruments in order to determine their **intrinsic value**, risk, and expected return. The main objective of security analysis is to help investors make **sound investment decisions** by identifying undervalued and overvalued securities.

According to **Graham and Dodd**,

"Security analysis is the analysis of value of securities with a view to investment."

It involves the study of **economic conditions, industry performance, and company-specific factors** to assess whether a security is worth investing in.

Objectives of Security Analysis

The primary objectives of security analysis are:

1. To estimate the **intrinsic value** of a security.
2. To identify **profitable investment opportunities**.
3. To assess the **risk and return** associated with securities.
4. To help investors select a **balanced and diversified portfolio**.
5. To minimize investment risk and maximize returns.

Importance of Security Analysis

1. Helps investors avoid speculative decisions.
2. Provides a scientific basis for investment decisions.
3. Assists in selecting suitable securities according to investor goals.
4. Helps in timing the purchase and sale of securities.
5. Promotes efficient allocation of capital in the economy.

Types / Approaches of Security Analysis

Security analysis is generally classified into two major approaches:

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1. Fundamental Analysis

Fundamental analysis evaluates a security by examining the **basic economic, industry, and company-specific factors** that affect its value.

(a) Economic Analysis

This involves the study of macro-economic factors such as:

- National income and growth rate
- Inflation and interest rates
- Fiscal and monetary policies
- Industrial production
- Balance of payments

Economic conditions influence corporate earnings and investor sentiment.

(b) Industry Analysis

Industry analysis examines the **performance and prospects of a particular industry**, including:

- Nature and growth of the industry
- Demand–supply conditions
- Level of competition
- Government policies
- Technological changes

(c) Company Analysis

Company analysis focuses on the **financial and operational performance** of a specific firm. It includes:

- Management efficiency
- Product line and market share
- Profitability and growth prospects
- Capital structure
- Financial statements analysis (ratio analysis, cash flow analysis)

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2. Technical Analysis

Technical analysis studies **past market data** such as price movements, volume of trading, and market trends to predict future price behavior.

Features of Technical Analysis:

- Based on charts and statistical indicators
- Assumes market prices reflect all information
- Focuses on timing of buy and sell decisions

Tools of Technical Analysis:

- Line charts, bar charts, and candlestick charts
- Moving averages
- Support and resistance levels
- Relative Strength Index (RSI)

Difference Between Fundamental and Technical Analysis

Basis	Fundamental Analysis	Technical Analysis
Focus	Intrinsic value	Price trends
Time horizon	Long-term	Short-term
Data used	Economic & financial data	Market data
Objective	Identify undervalued securities	Predict price movement

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Limitations of Security Analysis

1. Depends on availability and accuracy of information.
2. Cannot eliminate risk completely.
3. Time-consuming and requires expertise.
4. Market sentiments and speculation may distort prices.
5. Sudden economic or political changes can affect results.

Role of Security Analysis in Investment Decisions

Security analysis guides investors in:

- Selecting appropriate securities,

- Managing risk through diversification,
- Planning long-term and short-term investment strategies,
- Achieving financial goals efficiently.

Security analysis is an essential tool for rational investment decision-making. By carefully evaluating securities through fundamental and technical approaches, investors can reduce uncertainty and improve the chances of earning stable returns. Though it has certain limitations, security analysis remains the backbone of professional investment management and capital market efficiency.