The Exponent Group of Journals For Shares And Stock Market

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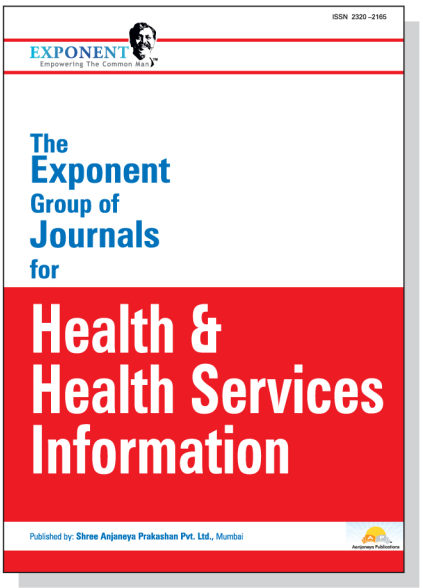
* All correspondence may be addressed to:-

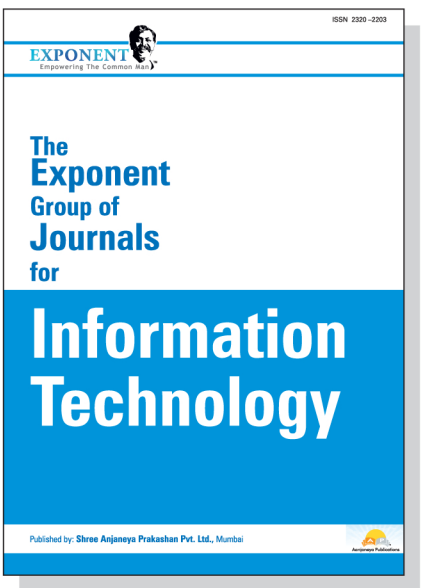
Editors Desk, Exponent Group of Journals
Email: editor.exponentjr@gmail.com, exponent.jr@gmail.com

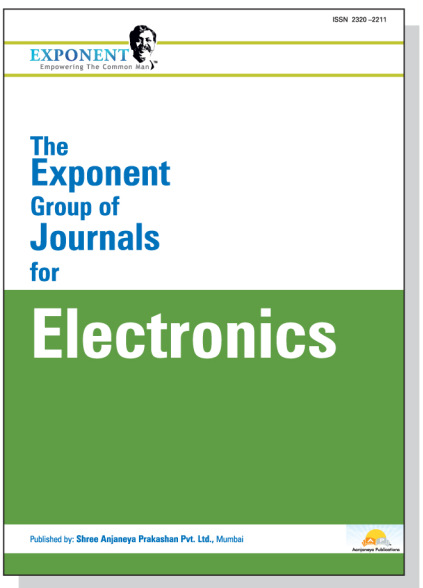
The EXPONENT GROUP OF JOURNALS

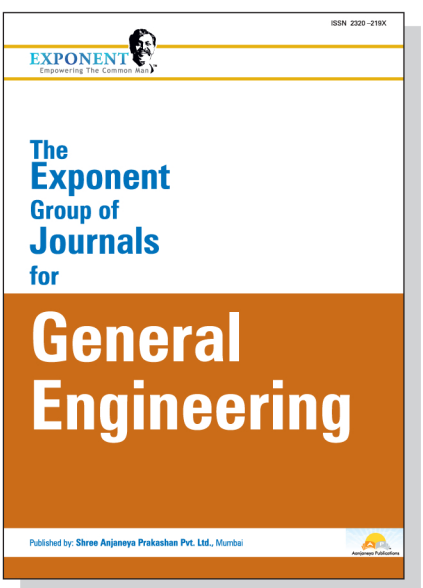
Empowering The Common Man

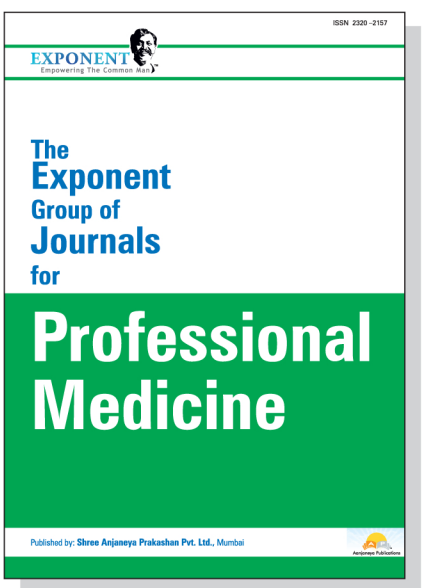
The Exponent Group of Journals

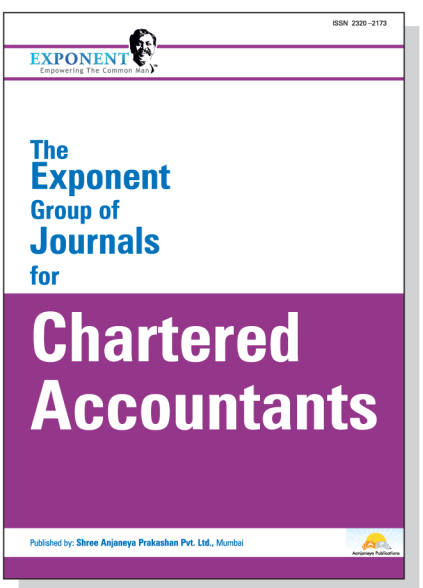












Editorial

- Sanket Pradhan

Email: sanket.pradhan@gmail.com

We all talk about the stock markets, SENSEX, NIFTY. There are numerous discussions going on – why did the market go up or when can I buy or what do I buy and many many more questions. But how many of us really know the Stock Market or even for that matter what is a stock or a share. May be very few. The main object of this edition is to given some basic insights on the stock market and then also discuss the stock indexes. We have started with these series and we will elaborate more in the editions to come.

We also will be discussing on the economic outlook for India and just give our perspective of how the Indian Markets may behave in the days to come. We will also be discussing on BREXIT.

The people of Britain voted for a British exit, or Brexit, from the EU in a historic referendum on Thursday June 23. The outcome prompted jubilant celebrations among Eurosceptics around theEuropean Continent and sent shockwaves through the global economy.After the declaration of the result, the pound fell to its lowest level since 1985 and David Cameron resigned as Prime Minister.Mrs May has said that she will trigger Article 50 - the step that starts the timer on two years of Brexit talks - by the end of March 2017.This means that Britain is scheduled to leave the EU by March 2019.

The Brexit victory sent economic shockwaves through global markets and Britain lost its top AAA credit rating. The Bank of England has cut interest rates and taken other emergency steps to help stop the UK from slipping into recession. There is ongoing uncertainty over what will happen once Britain leaves the EU because it has to make new trade agreements with the rest of the world.

This all has a humongous impact on the world economy and also on the global markets. We will discuss this in detail on our article on Brexit.

Hope you find all these informative. Request that you please do share your feedback on the email addresses mentioned.

Happy Reading !!!!

Basics About Stock Market

- Sanjay Thakkar

E-mail: sanjaydssl@yahoo.com

No one likes to lose money. Moreover, the pain threshold of some is greater than it is with others. If you're considering an investment in the stock market and the thought of a loss upsets you, you probably shouldn't invest. However, when you invest there are several things you should know to increase your chances of winning. That's the subject of this article. Although there are numerous details and caveats, this article will help you understand the basics of how the stock market works and why stocks react as they do. We'll also discuss some things that every investor should know. Let's dispense with the mystery and take a look behind the veil.

The stock market is a complex system where shares of publicly-traded companies are issued, bought and sold. To some it is a nebulous, dark chasm where people gamble. Actually, it is not gambling at all. Why? Let's say you put Rs100 on one roll of the dice. If you win, you win RsX. If you lose, you lose the entire Rs 100. When you invest in stocks, you will win Rs X or lose RsY. It's rare to lose it all, unless of course you invest in a company that goes bust. You could say that the stock market is a group of people pitting their expertise against one another. We'll touch on that in the next section.

The stock market is a collection of millions of investors with diametrically opposing views. This is because when one investor sells a particular security, someone else must be willing to buy it. Since both investors cannot be correct, it is an adversarial system. In short, one investor will profit and the other will suffer loss. Therefore, it's important to become well versed on the investment you are considering.

There are many factors that determine whether stock prices rise or fall. These include the media, the opinions of well-known investors, natural disasters, political and social unrest, risk, supply and demand, and the lack of or abundance of suitable alternatives. The compilation of these factors, plus all relevant information that has been disseminated, creates a certain type of sentiment (i.e. bullish and bearish) and a corresponding number of buyers and sellers. If there are more sellers than buyers, stock prices will tend to fall. Conversely, when there are more buyers than sellers, stock prices tend to rise.

Let's assume stock prices have been rising for several years. Investors realize that a correction will come and stock prices will tumble. What we don't understand is what will trigger the selloff or exactly when it will occur. Therefore, some investors will sit on the sidelines holding cash, waiting for the opportune time to get in. Those who are willing to assume the risk may jump in because the return on cash is so low and it hurts to earn zero while watching stocks move higher. This begs a couple of key questions. If you're on the sidelines, how will you know when to get in? If you're already in, how will you know when it's time to get out? If the stock market was predictable, these questions could easily be answered. However, it is not. There are actually three issues an investor should consider. The first is understanding the point at which stock prices are fairly valued. The second issue is the event that will cause a downturn. The final issue is understanding the human decision-making process. Let's briefly look at these.

Stock Valuation

The actual price of a stock is determined by market activity. When making the decision to buy or sell, the investor will often compare a stock's actual price to its fair value. For example, if a stock is trading at Rs30 per share and its fair value is Rs35, it may be worth purchasing. Conversely, if it trades at Rs 30 but its fair value is Rs25, the stock would be considered overvalued and the investor would be wise to avoid it. What is a stock's fair value and how do you calculate it? Ideally, it would be based on some standardized formula. However, there are many ways to derive this figure. One method is to combine the value of a company's assets on its balance sheet, minus depreciation and liabilities. Another is to determine

its intrinsic value, which is the net present value of a company's future earnings. We have briefly discussed two methods. There are a number of others. Because the methods yield a slightly different result, it's sometimes difficult to know if a stock is overvalued, undervalued, or fairly valued. And even if it is overvalued, that doesn't mean investors will suddenly sell and the price will fall. Actually, a stock can remain overvalued for quite some time. This is also why it can be problematic to make buy/sell decisions based on where the price of the stock is in relation to some moving average.

Triggering Event

Knowing which event will cause a trend reversal is analogous to seeing around the corner of a solid brick building. Need I say more?

The Human Decision Process

This is the most interesting of the three. Inside every individual there is a logical and an emotional component. We may analyze a situation using our logical side but when it's time to act, we refer to our emotions. For example, when purchasing a car, we might research the engine, fuel efficiency, amenities, or other items. But when it's time to decide, we often ask other types of questions. Such as, how do I look in the driver's seat? Does the car match my image? When making investment decisions, since there is an investor on the other side ready to buy what you're selling or selling what you want to buy, you must be able to process the relevant data and make a good decision. However, it's impossible to know everything you would need to know and process it without any bias. For these and other reasons, we will make a sub-par decision at times. This will occur even with the most analytical individuals.

The two most important decisions an investor will make are when to buy and when to sell. The best time to buy is when others are pessimistic. The best time to sell is when others are actively optimistic. When buying, remember that the prospect of a high return is greater if you buy after its price has fallen rather than after it has risen. But caution should be exercised. For example, after the stock of fictitious Company X declined by 30%, 40% or more, the first question to ask is why. Why did the stock fall as it did? Did other stocks in the same industry experience a decline? If so, was it as severe? Did the entire stock market fall? If the broader market or other stocks in the same industry/sector performed relatively well, there may be a problem specific to Company X. It's best to adopt a buy/sell discipline and adhere to it. Benjamin Graham, the father of value investing, once said, "The buyer of common stocks must assure himself that he is not making his purchase at a time when the general market level is a definitely high one, as judged by established standards of common-stock values." His reference was to what we discussed as fair value under the section Stock Valuation above.

Summary

The stock market is a complicated place for which the novice investor is not particularly well suited. Avoid the "hot tip" talk around the water cooler or in the lunchroom. Stock prices rise and fall for reasons which can be complex. Since the only sure bottom is zero, when you invest, consider adding protection (i.e. stop orders, options, etc.). To avoid disaster, be sure the company you're buying is worth owning. Unless you love risk, you may wish to avoid putting too much of your money in one stock.

It takes years to become well versed on the financial markets and on stocks in general. You may want to find someone you trust and seek their guidance. It may seem like an unnecessary expense but heading into unfamiliar territory alone can often cost us more than we expect.

Indian Economic Outlook (Q1 FY 2016-17)

- Rohan Takalkar

E-mail: rtakalkar17@gmail.com

Economic Data

Index of Industrial Production (IIP) for the month of May came in at 1.2% versus a contraction of (-) 1.35% in April. Data for April has been revised from an initial estimated contraction of (-) 0.8%. The cumulative growth for the period April-May 2016over the corresponding period of the previous year stands at (-) 0.1% compared to 2.8% growth in the year-ago period .Based on uptick from the excise duty collections, we continue to believe that the IIP would improve significantly going forward; India's retail inflation held at a 22-month high. Consumer prices rose 5.77 % in June from a year earlier after a 5.76% increase in May. Wholesale inflation, as measured by the wholesale price index (WPI), rose to 1.62% in June from 0.79% in May. India's Gross Domestic Product (GDP) rose to 7.9% Year on Year (Y-O-Y) in Q4 FY16 in relation to 7.2% in Q3 FY16 and 6.7% in Q4 FY15. The recovery was attributed to household consumption as the same surged to 8.3% in contrast to 6.6% in Q4FY15, while investment dwindled to 2.4% in relation to a raise of 7.3% in Q4FY15. India's foreign exchange reserves tumbled $3bn to $360.7bn in the last week of June On April 8, Indian foreign exchange reached a historical high of $359bn after a jump of $4.2bn in a week. Since then this has been the highest fall in the reserves.

Equity Markets

The domestic market closed higher on Thursday, erasing their losses suffered on Friday after Brexit referundem. Hopes of a good monsoon and a recovery in earnings have boosted the market, with the broader NSE Nifty surging more than 7% in the April-June quarter, its strongest since April-June 2014. The Sensex ended up 259 points at 27,000. The Nifty ended up 84 points at 8,288, the highest closing level since October 23, 2015. For the month of June the FIIs were net buyers of stock worth Rs.1,670 crore;, sectors like Infra, Banks, Autos and Realty outperformed the key benchmark indices, whereas sectors like Pharma, Telecom, Energy, Metals and Utilities underperformed as per market sentiments and expectations. The Monsoon session of the Parliament is expected to begin in the second half of July 2016 within a positive sentiment on the passing of the GST bill. This could spiral growth even further for the government as well as for the Indian equity markets.

Fixed Income Market

The Interbank Lending rate declined by 15 bps at 7% as RBI infused Rs 800.9 Billion ($11.9 billion) thought open market debt purchases which reduced the short term borrowing costs.While average banking system liquidity was in surplus Rs 373 billion till july 8. compared to Rs 157 Billion previous week.The loans grew at 9.4% in 12 months through june 24 lowest 10 years ,also 10 year Government bonds fell 5 basis points at 7.33%, RBI has bought back 700 billion Government Securities (G-Secs).

Outlook

The recent rally in Indian markets is driven largely by a global risk-on trade, assisted by some India specific factors. A possible delay in the US rate hike cycle, forecast of a good monsoon and relatively better earnings outcome were a few of the key factors.

Global growth remains weak with little evidence of demand improvement despite several years of easy monetary policies by most large central banks. Any risk emanating on the global front can affect FII flows that have been a key driver of markets. As far as India is concerned, the capex cycle is yet to show relevant recovery as the asset quality travails of the Indian banks are not yet over. However, despite this uncertainty in the short term, we believe that the medium term outlook of the Indian economy and consequently the equity markets is quite positive. Indian market valuations are at 17x FY17 earnings, which we believe is an attractive good number, given that a cyclical recovery is expected in the near future. We continue to remain optimistic from a medium to long term point of view, despite our short term concerns.Bond markets have been quite balanced in spite of the significant addition for the demand for Government Securities (G-Secs) in the form of OMO purchases by the Reserve Bank of India (RBI). Banks have also been quite reluctant to replace the Government Securities (G-Secs) sold by them in the Open Market Operation (OMO) auctions. Hence, the OMO purchases from RBI have only substituted the Banks' demand for G-Secs and have not added to the demand side.The uptick in inflation has also pushed out the possibility of a near term rate cut which in turn has raised the bar for a future rate cut. A period of sustained low inflation is anticipated which may spiral rate cuts in the near future.

On the liquidity front, RBI's OMOs plus seasonal factors have helped diminish the liquidity deficit in the banking system. It is expected that liquidity will improve further on seasonal factors and the system is likely to be in a surplus mode in the coming months. An improvement in liquidity and lower probability of near term rate cuts will lead to further rise in the yield curve i.e. short end yields are likely to soften while the longer term yields are likely to stay flat or harden. In a flat to a rise yield curve environment, it is expected that interest accruals will form a larger portion of the Bond portfolio returns than duration plays.

Indian Stock Markets - Moving Ahead

- Madhumita Ghosh

E-mail: ghoshmadhumita@hotmail.com

The markets had been through a roller coaster ride in the last few days due to domestic and global concerns. Britains exit from the European Union had led to volatility in currency markets. The British sterling pond crashed 8% and touched the lowest level in 30 years. The dollar thus appreciated and this led to weakness in emerging market currencies. Weakness in currency and uncertainty in global economic outlook has impacted the Indian markets in the last few sessions. In the domestic side exit of Raghuram Rajan was also a domestic concern which however did not impact the market significantly

The Indian economy at this juncture stands out in terms of economic fundamentals and strong growth story. However this growth is constrained significantly due to stress in banking sector . The banks reeling under high NPA pressure has become shy towards forwarding credits. The silverline is that debt burden on high debt companies have decreased considerably and thus India Inc's balance sheet is improving. Banks are writing off bad loans or restructuring loans. One time blow should clean the sector in the coming months. Being the yardstick banking would then contribute towards speeding up the economic growth. Amongst the emerging markets India is well positioned in terms of economy corporate performance , low commodity prices and stable government.

The need of the hour is quick announcement and implementation of sound reforms and policies. The global environment will remain uncertain for sometisme and put pressure on other economies. Policy making in this dynamic and challenging global environment would require lot of thinking and prudency to help India move forward despite such hurdles.

Cabinet clearing the 7th commission, GST bill , mining policy and good monsoons should provide positive direction to the market. It should auger well for sectors having rural theme, consumer durable being the biggest beneficiary. Auto, FMCG, Logistics, entertainment would also benefit.

The positive triggers would continue to accelerate the market despite challenges and help Nifty to cross 8500 level in short to medium term. The small and midcaps is expected to perform better than the large caps.

Brexit

- Rohan Takalkar

Email: rtakalkar17@gmail.com

What is Brexit?

The people of Britain voted for a British exit, or Brexit, from the EU in a historic referendum on Thursday June 23.

The outcome has prompted jubilant celebrations among Eurosceptics around the Continent and sent shockwaves through the global economy.

After the declaration of the result, the pound fell to its lowest level since 1985 and David Cameron resigned as Prime Minister of this country.

Mr. Cameron said: "I will do everything I can as Prime Minister to steady the ship over the coming weeks and months. But I do not think it would be right for me to try to be the captain that steers our country to its next destination."

The new Prime Minister Theresa May has already set out Britain's positions in meetings with the leaders of France, Germany and other key European nations.

Mrs. May has declared that "Brexit means Brexit" but she has delayed triggering Article 50 until sometime next year. The use of Article 50 starts the timer on two years of exit talks before the UK is expelled from the political bloc.

The Brexit vote has sparked calls for a second Scottish independence referendum because of majority of Scots voted to remain in the EU during the referendum.

Spain's Government has also called for joint control of Gibraltar and Sinn Fein is demanding a vote to unite Ireland and Northern Ireland.

Jeremy Corbyn is now standing in a leadership contest against MP Owen Smith after mass resignations from his cabinet due to his lukewarm support for the EU.

Leading Brexiteer Nigel Farage resigned as the leader of Ukip on Monday July 4 and said that he had achieved his life goal of getting Britain out of the EU.

What does Brexit mean for the economy?

The Brexit victory sent economic shockwaves through global markets and UK stocks had their worst drop since the finanical crisis.

Emergency steps are now being taken to calm the economic turmoil after the pound fell to its lowest level since 1985. Britain has lost its top AAA credit rating.

There is ongoing uncertainty over what will happen when Britain leaves the EU because it has to make new trade agreements with the rest of the world.

Bank of England Governor Mark Carney said: "Some market and economic volatility can be expected as this process unfolds. But we are well prepared for this."

Mr. Carney has announced an interest rate cut and other measures aimed at saving the country from slipping into recession.

Supporters of Brexit argue that EU countries have every incentive keep trading with the UK, which is a large importer of goods and services.

But Europhiles worry that foreign companies will be less likely to invest here and could relocate their headquarters if Britain loses access to the EU's

single market.

Neil Woodford, head of investment at Woodford Investment Management, said could see to an extent why the Brexit vote had been seen as an "existential shock' to the economy.But he said: "The reality is very different in my view. I don't think there's going to be a recession in the UK." WILL OUR ECONOMY RECOVER?

Mr. Farage has also said the Brexit vote is good news for exporters who have struggled with the high value of the pound.

Now Britain has voted to leave the EU, it will no longer have to contribute billions of pounds a year towards the European Union's budget.

During the referendum campaign, Eurosceptics slammed a Confederation of British Industry report that claimed that Brexit would cause a £100billion "shock" to the UK economy.

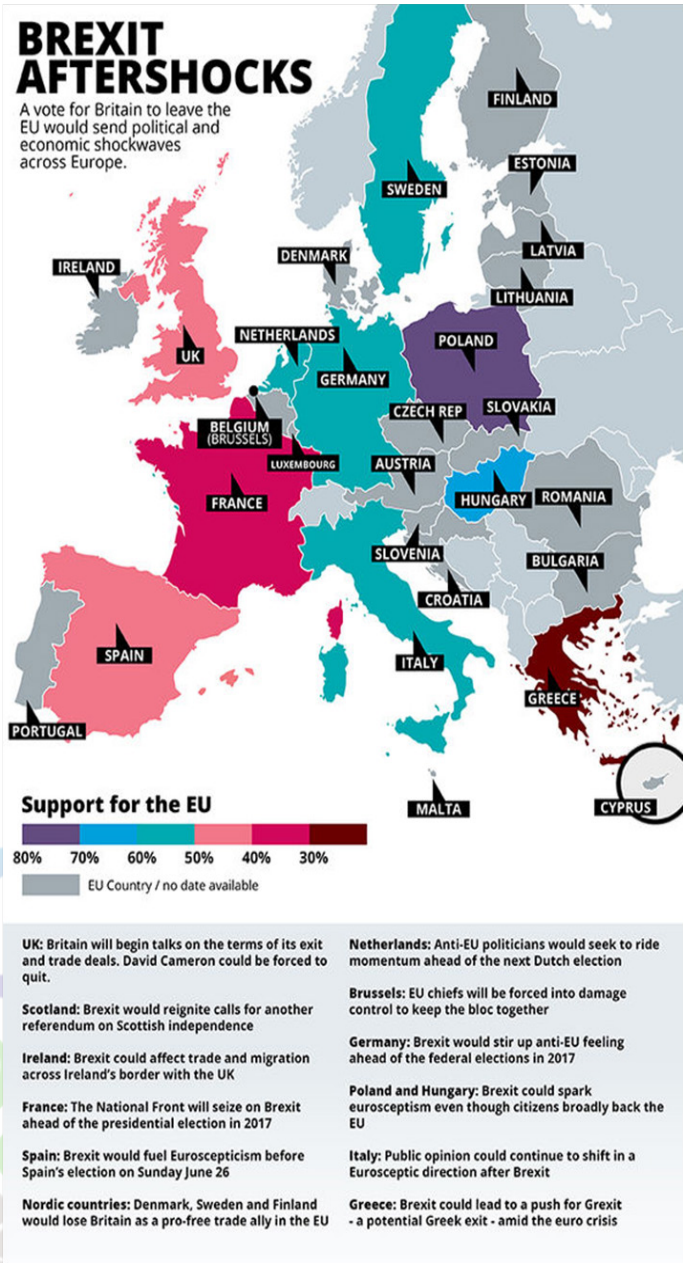
What will happen to immigration when Britain leaves the EU?

Eurosceptics say Brexit will allow Britain to take back control of its borders in order to curb immigration and increase security.

Britain will no longer have to accept 'free movement of people' from Europe, which Brexiteers say puts pressure on public services such as the NHS and schools.

Brexit campaigners have said that Britain will be free to impose an 'Australian-style points system' to better manage immigration and fill skill shortages here.

But the Remain campaign believes that Brexit will hit the British economy, which relies on the free movement of EU migrant workers such as health professionals.



Brexit sent political shockwaves around Europe

Some Europhiles have also said that Brexit will compromise the UK's ability to fight cross-border crime and terrorism.

Mr Cameron even said he suspects that ISIS leader Abu Bakr al-Baghdadi "would be happy" when Britain leaves the EU.

What will happen to Britain's place in the world?

Brexit campaigner believe that British voters have taken a once-in-a-lifetime opportunity to restore Britain's sovereignty.

Eurosceptics see EU institutions as inherently un-

democratic and argue that laws that affect the UK should not be decided by bureaucrats in Brussels.

Mr. Johnson argues that the EU has greatly eroded the public's ability to elect politicians to pass laws that matter to them.

In his victory speech, the former London mayor said that the British people will now be able to "settle their own destiny" outside the EU.

IMPACT ON INDIA

It would be prudent to say that it will drastically affect Indian financial market with respect to capital flows from EU. For the past few years European growth has slowed down and hasn't increased capital exports to India Substantially. It would definitely see a fall in Indian business operated in EU and UK. Brexit could cause fall in capital flows into UK from rest of Europe. Since UK already has high current account deficit reduced capital flows might affect its currency and economic growth , weakening of its currency might affect exports from rest of Europe into UK and thereby economic growth of European Union. Hence, whole euro could see some slip on growth and hence Indian businesses operating in Europe."

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Indices

- Sanket Pradhan

Email: sanket.pradhan@gmail.com

What is an Index?

You may often hear people speaking that the 'market' fell one day, or that the 'market' jumped. However, if you read the stock table, you will realize that not all stocks rose or fell. There were some which moved in the opposite direction. Then, what does the 'market' mean?

It means an index.

An Index is used to give information about the price movements of products in the financial, commodities or any other markets. Financial indexes are constructed to measure price movements of stocks, bonds, T-bills and other forms of investments. Stock market indexes are meant to capture the overall behavior of equity markets. A stock market index is created by selecting a group of stocks that are representative of the whole market or a specified sector or segment of the market. An Index is calculated with reference to a base period and a base index value.
Stock market indexes are useful for a variety of reasons.

Some of them are:

- They provide a historical comparison of returns on money invested in the stock market against other forms of investments such as gold or debt.
- They can be used as a standard against which to compare the performance of an equity fund.In It is a lead indicator of the performance of the overall economy or a sector of the economy.
- Stock indexes reflect highly up to date information
- Modern financial applications such as Index Funds, Index Futures, Index Options play an important role in financial investments and risk management

From among the stocks listed on the exchange, some similar stocks are selected and grouped together to form an index. This classification may be on the basis of the industry the companies belong to, the size of the company, market capitalization or some other basis. For example, the BSE Sensex is an index consisting of 30 stocks. Similarly, the BSE 500 is an index consisting of 500 stocks.

The values of the grouped stocks are used to calculate the value of the index. Any change in the price of the stocks leads to a change in the index value. An index is thus indicative of the changes in the market. Some of the important indices in India are:

- Benchmark indices – BSE Sensex and NSE Nifty
- Sectoral indices like BSE Bankex and CNX IT
- Market capitalization-based indices like the BSE Smallcap and BSE Midcap
- Broad-market indices like BSE 100 and BSE 500

WHY DO WE NEED INDICES?

Indices are an important part of the stock market. Here's why we need stock indices:

Sorting:

In a share market, there are thousands of companies listed. How do you differentiate between all of those and pick one or two to buy? How do you sort them out? It is a classic case of a pin in a stack of hay. This is where indices come into the picture. Companies and their shares are classified into indices based on key characteristics like size of company, sector or industry they belong to, and so on.

Representation

Indices act as a representative of the entire market or a certain segment of the market. In India, the BSE Sensex and the NSE Nifty are considered the benchmark indices. They are considered to represent the overall market performance. Similarly, an index formed of IT stocks is supposed to represent all stocks of companies from the industry.

Comparison

An index makes it easy for an investor to compare performance. An index can be used as a benchmark to compare against. For example, in India the Sensex is often used as a benchmark. So, to find if a stock has outperformed the market, you simply compare the price trends of the index and the stock. On the other hand, an index can also be used to compare a set of stocks against a benchmark or another index. For example, on a given day, the benchmark index like Sensex may jump 200 points, but this rally may not extend to a certain segment of stocks like IT. Then, the fall in the value of index representing IT stocks could be used for comparison rather than each individual stocks. This also helps investors identify market trends easily.

Reflection

Investor sentiment is a very important aspect of stock market movements. This is because, if sentiment is positive, there will be demand for a stock. This will subsequently lead to a rise in prices. It is very difficult to gauge investor sentiment correctly. Indices help reflect investor's mood – not just for the overall market, but even sector-wise and across company sizes. You can simply compare an index with a benchmark to see if has underperformed or outperformed. This will, in turn, reflect investor sentiment.

Passive investment

Many investors prefer to invest in a portfolio of securities that closely resembles an index. This is called passive investment. An index portfolio helps investors cut down cost of research and stock selection. They rely on the index for stock selection. As a result, portfolio returns will match that of the index. For example, if Sensex gave 8% returns in one month, an investor's portfolio that resembles the Sensex is also likely to give the same amount of returns. Indices are also used to construct mutual funds and exchange-traded funds (ETFs).

HOW ARE STOCK INDICESFORMED ?

An index consists of similar stocks. This could be on the basis of industry, company size, market capitalization or another parameter. Once the stocks are selected, the index value is calculated. This could be a simple average of the prices of the components. In India, the free-float market capitalization is commonly used instead of prices to calculate the value of an index.

The two most common kinds of indices are – Price-weighted and market capitalization-weighted index.

What is stock weightage?

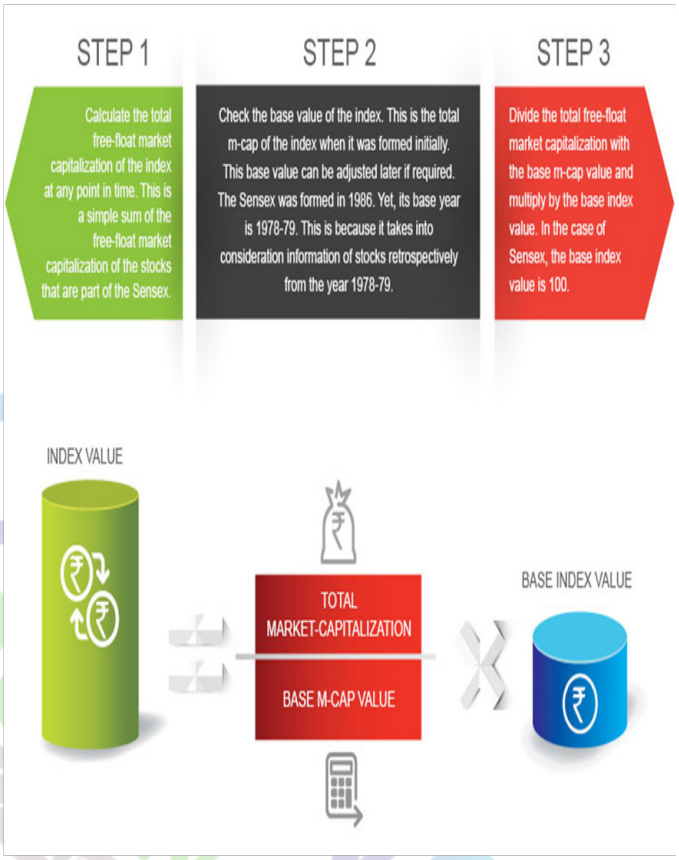
Every stock has a different price. So, a 1% change in one stock may not equal a similar change in another stock's price. So, the index value cannot be a simple total of the prices of all the stocks. Here is where the concept of stock weightage comes into play. Each stock in an index has a particular weightage depending on its price or market capitalization. This is the amount of impact a change in the stock's price has on index value.

Market-cap weightage Market capitalization is the total market value of a company's stock. This is calculated by multiplying the share price of a stock with the total number of stocks floated by the company. It thus takes into consideration both the size and the price of the stock. In an index using market-cap weightage, stocks are given weightage on the basis of their market capitalization in comparison with the total market-capitalization of the index. For example, if stock A has a market capitalization of Rs. 10,000 while the index it is part of has a total m-cap of Rs. 1,00,000, then its weightage will be 10%. Similarly, another stock with a market-cap of Rs. 50,000, will have a weightage of 50%. The point to remember is that market capitalization changes every day as the stock price fluctuates. For this reason, a stock's weightage too changes every day. However, it is usually a marginal change. Also, the market capitalization-weightage method gives more importance to companies with higher m-caps. In India, most indices use free-float market capitalization. In this method, instead of using the total shares listed by a company to calculate market capitalization, only the amount of shares publicly available for trading are used. As a result, free-float market capitalization is a smaller figure than market capitalization.

Price weightage In this method, an index value is calculated on the basis of the company's stock price, and not market capitalization. Stocks with higher prices have greater weightages in the index than stocks with lower prices. The Dow Jones Industrial Average in the US and the Nikkei 225 in Japan are examples of price-weighted indices. There are also other kinds of weightages like equal-value weightage or fundamental weightage. However, they are rarely used by public indices.

HOW IS INDEX VALUE CALCULATED?

An index's value depends on whether it is a price-weighted index or market cap-weighted. Let us take the example of the BSE Sensex to understand how an index is calculated.



WHAT NEXT?

Now, we have understood the basics of a stock market indices. So let us move on to the different types of indices in the next edition.