CHAPTER-I
INTRODUCTION

1.1 General Background of the Study

Imbalance economic development of a country became barrier on the pace to economic prosperity .The imbalance economic development exist in the scattered money throughout the economy is not mobilized properly .It is clear that the overall development and prosperity of capital resources to productive sectors. To get rid from this problem a mechanism works in the country that is called financial market.

Financial market is concerned with accumulation and mobilizing of capital resources, which act as a life blood for any productive activities .Financial market plays as an active market where capital resources are transferred from savers to users, where savers let users to use their saving in expectation of multiplied returns from users in specific time period.

Investment is the sacrifice of certain present value for the uncertain future reward. It entails arriving at numerous decisions such as type, mix, amount, timing, grade etc of investment and disinvestment. Further, such decision-making has not only to be continuous but rational too. Broadly speaking, an investment decision is trade off between risk and return. All investment choices are made at points of time in accordance with the personal investment ends and in contemplation of an uncertain future. (Bhalla, 1999:3)

Investment should always insure two aspects , first ,the money should be available back when it is needed ,second ,the invested money should grow because a rupee's real value today is greater than a rupee's real value tomorrow in the world of inflation .Investment ,thus ,is simply concerned with the incensement of the investor's wealth (Cheney and Mosses ,1999 :13-14)

There many players in security market like institutional investors, individual investors, brokers, security dealers, market maker, investment banker, underwriter etc. Among these investors play a vital role providing best flow of capital in market. The investors search for the best alternative investment that can return a maximum future for their bright future.

Institutional investors and individual investors, both are equal important from the investment point of view. Institutional investors mobilize the financial resources from small saver to large units of industrial investors through collecting funds from small savers by issuing own securities and investing the pooled funds securities of industrial units.

Basically, institutional investors may play more significant role in the capital market of the country like Nepal. I t is because; the development of the capital market of Nepal is in infant stage. The knowledge and information about the stock market to the general people is very low. Therefore, they can not supply the sufficient funds in the capital market and their role in stock market is almost in significant.

1.1.1 Financial Instruments/Securities

A wide range of investment alternative is available to individual investors in the investment environment. Buying, common stocks, bonds of company, depositing money into bank account, buying a piece of land, gold or silver are examples of investment. Basically invested alternatives can be categorized into two groups;
Real assets or Non-financial assets.
Financial assets/Financial instruments.

Real assets can be tangible or intangible. Plant, machinery, office, factory, furniture and building, precious metals are example of tangible assets while technical know-how, technological collaborations, patents and copyrights are intangible assets. The firm requires number of real assets to carry on its business. Real assets are generally less liquid than financial assets. Returns on real assets are frequently more difficult to measure accurately.

Financial assets or instruments are pieces of paper representing an indirect claim to real assets held by someone else. These pieces of paper represents debt or equity commitments in the form of IOUs (written document providing evidence of debt) or stock certificates (Thapa, 2003:3).
In general, only a piece of paper represents the investor's right to certain prospectus or property and the conditions under which he or she may exercise those rights. This piece of paper, serving as evidence of property rights, is called a financial instrument. It may be transferred to another investor, and with it will go all its right and conditions. Thus, it is a

legal representation of the right to receive prospective future benefits under stated conditions (Alexander, et al. 2003:2-3). Some of the examples of financial instruments are common stocks, preferred stocks, bonds, convertibles, warrant, options, right and futures

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Government and private firms issue financial instruments. Government issued financial instrumentals to finance deficits in their budgets when revenues fall short of expenditures. Government instruments are almost invariably bond issues of various types. These bonds are issued by governments at all levels: federal, state and municipality. Because the federal government can print money ,its instruments are not subject to default. The instruments of the state and municipal governments, however, are only as sound as the abilities of these governments to raise revenue through taxation and other means. Private firms issue a wide variety of different types of financial instruments from bonds to common stocks. The quality of these issues is based in the quality of the earning power of the firms issuing them (Haugen, 1997:7).

Securities Exchange Act 2040 explains that "securities means shares, stock, bond, debenture, debenture stock issued by a corporate body or a certificate relating to unit saving scheme or group saving scheme issued by any corporate body in accordance with a prevailing laws or negotiable certificate of deposits or treasury bills issued by His Majesty's Government and it includes the securities issued under full guarantee of His majesty by the notification published in the Nepal Gazette or receipts relating to deposits of securities as well as right and interest relating to securities."

1.1.2 Financial Markets

Financial market is that market where money itself is traded –loaned or borrowed-in terms of different financial assets or instruments like stocks and bond (Ritter and Silber, 1993:25-26), i.e. financial instruments are traded in financial market. Financial market can be defined as a mechanism for bringing together buyers and sellers of financial assets in order to facilitate trading. It plays a significant role in bridging the gap between the deficit and surplus unit of society. Buy and sell orders that flow from investors' demand and supply pattern determines the prices of financial instruments which in turn will ultimately influence the allocation of resources throughout the economy.

A healthy economy is dependent on efficient transfers of funds from people who are net savers to firms and individuals who need capital-that is, the economy depends on efficient financial markets. Without efficient transfers of funds, the level of employment and productivity, and hence our standard of living would be much lower. So it is absolutely essential that our financial markets function efficiently (Western and Brigham,1996., 73-74).

Globalization of economies and market has been one of the major instruments of change. Due to globalization every sort of change occurring in one sector of the world affects the other. With the result of dynamic global changes and development, financial markets are rapidly responding. Therefore, now- a- day's financial market has become global phenomena and basic concern of financial and economic condition of any nation.
Financial market can be classified in various ways .The most common classification is:

- Primary market and secondary market
- Money market and capital market.

Primary Market

Securities available for the first time are offered through the primary securities markets. The issuers may be a brand-new company or that has been in business for many-many years. The securities offered might be a new type for the issuers or additional amount of securities used frequently in the past. The key is that the securities absorb new fund for the issuer, whereas in the secondary markets, existing securities are simply being transferred between parties and the issuer is not receiving new funds. After their purchase in the primary markets, securities are traded subsequently in the secondary market.

The primary market functions are operated by middlemen, called investment bankers. The investment bankers' principal activity is to bring seller and buyers together, thus creating a market. He normally buys the new issues from the issuer at an agreed upon price and hope to resell it to the investing public at a higher price or he does this on the basis of commission from the issuers for taking responsibility of selling the securities to the potential investors'. This act of investment banker is said to be underwriting of securities.

But all new issues are not underwritten; many issuers make direct sales to investor group, with only some investment banking securities provided for example, securities are often

sold directly to institutions. This is referred to private placement. The investment bankers may act only as a finder; that is, he locates the institutional buyers for a fee.

Secondary Market

The secondary market liquidates the shares and provides the opportunities between the seller of the securities and investors. So, the investors can buy or sell any securities of any business companies that are listed in the secondary market.

"After securities have been purchased from the primary market, they can be traded in the secondary market. The secondary market comprises the organized security exchange and a specialist facilitates the transaction. The major of all capital market transaction occur in the secondary market do not got to the organizational issuer instead to the initial owners (seller) of the securities "(NEPSE Annual report, 2001: 73).

So, secondary market is a security market where old securities are traded. In other word, once the securities have been issued in primary market, then they are traded in secondary market. The trading of stocks in secondary market is held of different business companies without their involvement .Investors can buy or sell any securities of any business companies that are listed in secondary market.

The basic economic function of secondary market is to provide marketability and liquidity for long-term investments, thereby the supply of equity and long-term debt capital for the financing of business companies. Once the investors purchase the security from the primary market, they need a place to sell those securities, which is called secondary market. "Once new issues have been purchase by investors, they change hands in the secondary markets. There are actually two broad segments of the secondary markets: the organized exchange and the over-their country (OTC) market (Fischer & Jordan, 2000:22).

a) Organized stock exchange

"The essential function of a stock is to provide active market place for corporate shares and other listed securities. The stock exchange plays an indispensable role in mobilizing funds in the capital market. The various virtues governing stock exchange include enhanced marketability of securities, rational allocation of invest able funds ,facilitate economic growth and wealth generation and proper maturity, liquidity and diversification of

investment. The growth of capital market through the vehicle of stock exchange has brought a flow of the information about various securities in additional to the sound listing criteria that prove worthwhile to the investors" (Shrestha, 1992:15).

Security exchange Center (SEC) was established in 1976 AD as an organized security exchange of Nepal with an objective of facilitating and promoting the growth of capital markets. Under the security Exchange Act 1983, the government converted SEC into Nepal stock exchange (NEPSE) in 1993. Its history began from the conversion in the stock exchange. It was the only capital markets institution undertaking the job of brokering, underwriting, managing public issue, market making for government bonds and other financial services. The basic objectives of NEPSE is to import free marketability and liquidity to the government and corporate securities by facilitating transaction in its trading floor through member, market intermediaries such as brokers, market etc.

b) Over the counter market

The name itself says that OTC was originated in the time when the securities were traded over the countries of different dealers. OTC is a market for those securities, which is not liter on the stock exchange. When the company first sells its securities to the public, the securities are traded in the ITC market. In modern days it has more to do in addition to place i.e. counter. OTC markets perform the works of both pray and secondary market. The securities traded over the canter range from most speculative common stocks. In past days, OTC markets were assumed to be more important for bonds than stocks. It includes all transactions of securities other than that taking place on the stock exchange. It is actually a group of security brokers.

Money market and Capital market

Money market is that financial market where funds are borrowed or loaned for short periods – usually less than a year. The main function of money market is to provide shot-term loans to business, government and household. Money markets activities includes primary and secondary markets activities in short-term negotiable instruments such as treasury bills, interbank deposits, commercial paper, certificates of deposit, banker's acceptance, repurchase agreements, and short-term municipal securities issued by non-financial corporations. The treasury bills, which are government securities, serve as a mechanism for non-inflationary financing of government deficits and can also support

monetary policy implementation. Other money market instruments are used to facilitate the supply of credit to larger corporations and to ease inter-bank financing.

Capital market is concerned with long-term finance. In the capital market, financial instruments with an original maturity of more than one year are traded. Equities or stock (ownership instruments), bonds, debentures, collateralized mortgage obligations, and derivatives are all capital market instruments. It consists of a series of channels through which the savings of the community are made available for industrial and commercial enterprises, and public authorities. It is concerned with those private savings, individuals as well as corporate, that are turned into investments through new capital issues and also new public loans floated by government and semi-government bodies (Kuchhal, 1976:283).
Capital market is the most important part of any financial market. An efficient capital market is an essential pre-requisite of economic development and the development of capital market in a country is dependent upon the availability of savings, proper organization of intermediary institutions to bring the investors and business ability together for mutual interests, regulation of investment, etc. With the rise of joint stock organization of production and distribution, the importance of capital market as a liaision between the investor and the entrepreneur has become paramount.

Capital market plays a significant role in mobilizing constant flow of saving and unutilized financial resources for expanding productive capacity of the countries. It provides the best investment opportunity to the investors. The major role of the capital market is to provide buying and selling opportunities of financial assets at competitive prices for the investors. In the capital market, demand comes from agriculture, industry, trade and government while supply comes from the individuals or corporate savings, institutional investors and the surplus of governments. The saving institutions like savings banks, investment trusts or investment companies, specialized financial corporations and stock exchanges are some of the important constituents of capital market (Kuchhal, 1976:283).

In theory, money market is different form the capital market. In practice, however, in most countries with efficient financial markets (that is, the money market and the capital market combined), the merchant banks are active in both. This is a simple function of the fact that a negotiable money market instrument for all practical purposes is simply a short-term

capital market instrument. Therefore, the techniques and facilities needed to operate in the money market are essentially the same as those needed to operate in the capital market.

Sidney Martin Robbins, in his article 'security' has picturised the brief history of the development of security market. It seems that the Stock Exchanges have got very old history for which we have to turn towards 12th century.

"Traders in European fairs in the middle ages found it convenient to use credit, which required the supporting documents of drafts, notes and bills of exchange. The French stock exchange may be traced as far back as the 12**th** century, when trading occurred in commercials bill of exchange. To regulate these incipient markets, Philip the fair (1268-1314) created the profession of courratier de change, the forerunner of the modern French stockbroker, or agent de change. Form similar roots in trade and commerce, the institutional beginnings of stock exchange appeared during the 16th and 17th centuries in other great trading centers throughout the world – Amsterdam, Great Britain, Denmark, Germany.

By the early 1600s, shares of the Dutch East India company were being traded in Amsterdam; in 1773, London stock dealers who had previously been meeting in coffeehouses moved into their own building; and by the 19th century, trading in securities on a formal basis was common in the industrialized nations.

The evolution of stock exchange continued. In great Britain, progress has for the most part been internal and voluntary; the London stock exchange has regulated its own activities. The French stock exchanges, in contrast are directly subject to law, and the operations of the agent stock change have been affected by nation's decrease. Securities markets in the United States began with speculative trading in issues of the new government. In 1791, the country's first stock exchange was established in Philadelphia, then the leading city in domestic and foreign trade (Robbins, 2003)"

1.2 Focus of the Study

Financial instrument is the vital instrument through which the government and corporate collect a fund for the development of the economy. This study has highlighted the several

kinds of financial instruments that are widely used in Nepalese business sphere. How these financial instruments play a vital role in Nepalese capital market is a major concern of this study. As there is great role of security market for national investment for greater return .There is a need of study of investors' behavior regarding how they make investment decisions. The study also focuses on how the investors do invest in the securities. In which instrument the investors prefer to invest in the security market is also the focus of the study.

This study aims to see how the governments as well as private securities are able to protect investors' interest and what type of benefits it provides to the investors regarding decisions making. Basically, the companies issue the common stocks and these stocks are transacted regularly in the NEPSE. Why Nepalese companies do not issue the debentures and preferred stocks in the Nepalese capital market is also the prime focus of the study.

1.3 Statement of the Problem

In the developed financial markets, there are many of financial instrument in use. Although our regulated capital market has crossed the history around two decades (since 1984), it seems ordinary shares are only the instrument through which company can go to the public for capital. The use of common stock alone covers 76.61% of total issues. It reveals, nobody has even though about other types of instruments. Nobody has made researched to see what the investors really think about other instruments, are the other instruments as well as preferences of investors really ineffective to be ignored totally, then why our market is unable to welcome other securities.

The Nepalese capital market is very lean to provide investment alternatives available in the world of financial market, very of few alternatives like common stock, preferred stock, corporate bonds and government bonds are very limited and the total market is dominated by common stocks. Likewise, the use of derivatives is almost nil and the use of municipal bonds was often heart but that had not been materialized yet.

If we see the scenario of government securities in Nepal, bonds are used in greater extent than treasury bills. Commercial banks are the major subscribers of treasury bills, which is the money market instrument of government. Similarly, government bonds are not trading

in the secondary market i.e. NEPSE. It shows that there is no freedom to the investors to buy and sell the government securities in the secondary market and it has made the investment market again limited.

Nepalese investors are not well informed and aware of features of different financial instruments. They lack proper knowledge and confidentiality because of which they are loosing their hard earnings. Institutional investors seem very passive in Nepalese capital market. The restrictions made on investors, especially institutional investors, by several directives are also preventing them from freely playing in the market with different instruments.

On the background, some of the main problems identified in the Nepalese capital market are

1. What is the reason behind the poor development of financial instruments in Nepal?
2. What are the investment alternatives available in the Nepalese capital market?
3. Which financial instrument, Nepalese investors preferred most?
4. What are the problems that the investors are facing to invest in securities in Nepalese Capital Market?

1.4 Objectives of the Study

The main objective of this study is to provide details about development of financial instruments in Nepalese capital market. The specific objectives of the study are:

- To analyze the development of Nepalese capital market.
- To analyze the different investment alternatives available in the Nepalese capital market
- To analyze the preference of the different investors of Nepal and to know what type of instruments the investors prefer the most.
- To identify the problems to invest in securities in Nepalese capital market.

Finally, the study aims to suggest and recommend to the concerned authorities with the help of major findings of the study.

1.5 Significance of the Study

A well- developed capital market presumes the existence of not only the investors – individual and institutional but mire significantly the existence of a network of specialized institutions and agencies that are always on the look out for investment in new ventures. This study provides guidelines to these agencies, which are looking for investment in new venture. It helps them to take correct investment decisions.

This study covers the analysis of the securities, which are common in the Nepalese Financial Market. It is analyzed that what factors affect the preference of investors. Actually, it focuses much more towards the investors and with regard in the NEPSE.

In the Nepalese capital market, common stock is the most interested instrument among all available financial instruments. The study efforts to detect the choice of financial instrument issued by the various sectors of economy. Therefore, the study has significance to the Nepalese companies who want to get the knowledge about the investor's preferences for the fund collection decision. This study is also important to the policy maker of the capital market as well.

This study has addressed those problems and issues, which are prevailing in Nepalese Capital Market. These problems and issues will surely act as an effective guideline to the new issuer to reach the potential investors. This study will also help prospective investors, financial intermediaries, investment bankers and other researcher in future giving them information about the Nepalese capital market and financial instruments available over there.

1.6 Limitations of the Study

This study is limited by the followings;

- Time is a major limitation of this study. As study is conducted for the partial fulfillment for the degree of Masters of Business study. Also, study is conducted within the Katmandu Valley only. So, the study area is also one of the limitations of this study.
- The study highly based on primary data. So, the reliability of data will heavily depend upon the responses of the respondents. Also the relevancy of the secondary data relies on published financial documents, annual reports, other related journals,

magazines and books of NEPSE, SEBO/N and NRB. So far as analytical tools are concerned, the limitations of analytical tools may creep in along with themselves.

- This study covers only 7 fiscal years.
- The scope of study is limited within the framework of financial instruments only, which are used in Nepalese Financial Market. Study has not considered other investment alternatives prevailing in the investment environment.
- Study deals more with capital market instruments than money market instruments. This study confines only the listed company's securities and partly government securities. So, it may not represent the population thought.
- In terms of investors, the study has focused on general investors (individual investors) rather than institutional investors due to limitation of time. Since the institutional investors are mostly guided by directives and mostly kept in legal boundaries, what matters more is directives rather than their independent thoughts. So, the study has focused more on general investors.
- The study highly depends on primary data collected from the individual investors selected randomly.

1.7. Organization of the Study

This is divided into 5 chapters. They are as follows:

Chapter I: Introduction:

The first chapter contains the introduction part of the study followed by overview of financial markets and financial instruments of Nepal. Focus of the study, statement of the problem, objective of the study, significance of the study and limitations of the study are also the content of this segment.

Chapter: 2: Literature Review

Second part of the study is literature review which contains of the review from the books, journals and thesis.

Chapter: 3: Research Methodology

The third chapter is research methodology and it contains research design, population and sample, sources and nature of data, procedure of sampling and data collection, data processing and presentation and data analysis tools.

Chapter: 4: Data Presentation and Analysis.

The fourth chapter is data presentation and analysis which contains presentation of data in various ways and its interpretation.

Chapter: 5: Summary, Conclusion and Recommendations

The whole study is summarized and concluded in this chapter. A list of suggestions and recommendations are also provided in this part of the study.

A list of bibliography and appendices are also presented after the end of chapter 5.

CHAPTER TWO
REVIEW OF LITERATURE

This chapter deals with the review relating to the area of Development of financial instruments in Nepalese capital market in more detail and theoretical way. Under this various books, journals, articles and previous research/dissertation has been consulted and reviewed.

2.1 Conceptual Framework

The investors always search for the better investment alternative that can maximize their wealth and ensure their better financial futures. Financial market with its wide range of security provides investors an investment alternative that can make their cash flow secure and build strong financial base. Investors invest in securities on the basis of public information that should provide every details of the company. Safeguarding investors wealth and their interest from unfair share trading practices should be the aim to enhance the awareness level of the investors in securities market.

2.1.1 Investment

Sharpe argued, "Investment in its broad sense means the sacrifice of current dollars for future dollars". The investment for future returns generally and automatically involves two attributes time and risk. The sacrifice of present wealth takes place in certainty but the reward or return is uncertain and hence bears a risk of uncertainty.

Investor always has to assume certain degree of risk due to risk. Thee are some securities which are less risky and have certainty of reward in future like in securities issued by the government, municipalities thought bonds, treasury bills etc.

Investors accumulate their earned incomes in form of saving but these saving are not an investment, it's rather defined as forgone consumption. The collected amount of rupee is not a capital unless it is invested in a productive process. The saving or collected earned incomes are used to produce more goods and services in country can be called investment. However we can categorize investment into two categories real and financial investments.

Real and financial investments

Real investment involves acquisition of tangible assets like lank, machinery, factories that involves direct flow of saving in to acquisition of assets or business.

Financial investment is indirect in nature; ones financial investment creates real investment for another. It is a form of investment involving contracts written in papers like shares, bonds etc. it is also known as papers assets.

In primitive economies or in stage of development most of investments are of real in nature. The investor finds only easy way to invest is in real investment. They are familiar and easy with buying real estate, bullion and are investing in business ventures directly or people just keep their money ideal by just saving.

But in present, due to well developed financial market people finds a way to put their money in to the highly rewarding investment. People can invest indirectly thought the purchasing of shares of the desired corporate house.

2.1.1.1 Types of Investors

There are various types of investors in the market. On the basis of information, individual investors and institutional investors are the most important investors in the financial market.

a. Individual investor

Individual owns a portfolio of securities and becomes investor. But the individual investors are part timer; they are the businessman, government worker, doctors, lawyer and even housewives, students and unemployed adults. When an individual buys a security, holds them and gets dividend or profit thought price appreciation, the cash flow becomes income to the people.

In Nepal it is hard to get a successful investor as they are in countable number. But we can get a very good example of successful investors in the neighboring country and well-known international icons like Warren buffet, John Templeton, Peter Lynch. Georgr Soros, David Dreman etc. The well-known Indian Investment Gurus Chandra Kant Sampat, Nemish Shah is people who took investment as their career.

The average investors in securities are part timer, with neither the ability nor time to evaluate a large (and often complex) flow of information. Most individual investors have a job apart from investing. Individuals have an opportunity cost in obtaining investment information, such as reading publication, tracking stocks prices, and building files on securities. This opportunities cost is the time and resources forgone that could have been used in other endeavors" (Jones, 1988:36).

b .Institutional Investors

Institutional investors are the active financial intermediaries involved in the securities market as professional investors. Generally, they are less restricted (bonded) in buying and selling of securities. They buy and sell the securities in bulk and have significant impact on the securities market in respect of resource mobilization, stock market price movement, market liquidity and so on. Especially, institutional investors do not hold securities in order to control over the management of the corporation instead they hold securities for financial benefits that may be generate from these investment in day to day transaction basis.

Institutional Investors and Changing Markets

The growth in size and institutional investors has produced increasing pressures on the security markets. The commission structure, membership requirements, and auction process of the organized exchanges have shown great incompatibility with the nature and needs of institutional investors.

The growing size and needs of institutional investors have increasingly come up against exchange rules, regulations and other rigidities (Fisher and Jordan, 2000:51). Since the late 1960s there have been a number of changes in the operation of the securities markets. These changes have been the result of competition within the securities industry and the result of external pressure from the Securities and Exchange Commission and congress. The broad classification of secondary securities market is occasionally divided into four categories of secondary markets. The first market represents the exchanges, second market represents over-the-counter trading; the third market represent the over-the-counter trading of shares that are listed on an exchange; and the fourth market represents direct trading between two investors (typically large institutional investors) without the brokerage firm acting as an intermediary (Fuller and Farrell, 1987:34)

2.1.2 Efficient Financial Market

Market efficiency means that the market price of a security represents the markets estimate to the value of that security. If the market is efficient, it uses all information available to it in setting a price. Investors who choose to hold a security are doing so because their information leads them to think that the security is worth at least its current market price. Those who do not purchase the stock interpret their information as a lower appraisal.

An efficient financial market exists security prices reflect all available public information about the economy, about financial markets, and about the specific company involved. The implication is that the market prices of individual securities adjust very rapidly to new information. As a result, security prices are said to fluctuate randomly about their "intrinsic" values. Expressed more formally, market efficiency means that the unanticipated portion of the return on a security is unpredictable and over a sufficient number of observations, does not differ systematically from zero. The unanticipated portion is simply the actual return less than which was expected based on some fundamental analysis (e.g.: its intrinsic value). Put differently, it is the surprise element.

Levels of market efficiency

Fama suggested three levels of market efficiency; weakly efficient market hypothesis, semi-strongly efficient market hypothesis and strongly efficient market hypothesis.

The first hypothesis is the weak market hypothesis. In this hypothesis, the type of information being considered is restricted to only historical prices. Investors should not be able to consistently earn abnormal profits by simply observing the historical prices of securities.

The semi-strong efficient market hypothesis states that all publicly available information must be already reflected in the stock prices. Such information includes in addition to past prices, fundamental data on the firms product line, quality of management, balance sheet earning forecasts and accounting practices etc. (Bhattarai, 2006: 353)

The strong efficient market hypothesis assumes that it reflects all information, both public and private.

This hypothesis claims that no one can earn a profit larger than what could be earned with a naïve buy and hold strategy by trading on short-term security price movements.

2.1.3 Financial Markets and Instruments

The major purpose of financial markets is to transfer funds from lenders to borrowers. They are the intermediary link in facilitating the flow of funds from savers to investors. By providing on institutional mechanism for mobilizing domestic savings and efficiently channeling them into productive investments they lower the cost of capital to investors and accelerate economic growth of the country. Financial markets are conduits through which those who do not spend all their income make their excess funds available to those who want to spend more than their income. (Ritter and silver, 1993:26). In this market, buyers and sellers of financial instruments come together. Business individuals and government units often need to raise funds. On other hand, some individuals and firms have income greater than their current expenditure, so they have funds available to invest. Interest of such both parties can be through the mechanism known as financial market. (Weston et al., 1996:30-31). Participants in the financial market commonly distinguish between the "Capital Market" and the "Money Market", former referring to borrowing and lending for long-term investment purposes, and the latter term generally referring to borrowing and lending for periods of a year or less (Vishwanath, 2000:322-323). Accordingly, a country's money market is often referred as its "market for short term funds", and its capital market, the "market for long term funds" (Kent, 1972:243)

2.1.3.1 Money Market Instruments

Money markets are used to facilitate the transfer of short-term funds to those with deficient funds. Money market deals with the short term financial needs. Here the investors find the instruments with the maturity of short period, usually less than a year. Such instruments with the maturity of short period, usually less than a year. Such instruments which have maturities within one year are referred to as money market securities/instruments.(Madura, 1998:38). They are less risky, easily marketable and carry low rates of return. Money market instruments/short term debt securities play a major role in the investment and borrowing activities of both financial and non-financial corporations. Individual investors with substantial funds may invest in such money market instruments directly or indirectly. Some money market instruments are negotiable and are traded in active secondary dealer,

markets; others are not some may be purchased by anyone with adequate funds, others only by particular type of institutions (Alexander, et a/2003: 303)

Money market instruments posses certain types of characteristics like;

They are all debt obligations; they have maturities ranging from one day to a full year.

They exhibit typically a high degree of safety of principal (they are subject to negligible interest rate risk, and issued by generally high credit standing borrowers like central bank), and they have high degree of liquidity (Santomero and Babbel, 1997:242-244)

Some popular instruments of money market are:

- Treasury bill
- Commercial Paper
- Certificates of deposit
- Banker's Acceptances
- Eurodollars.
- Repurchase Agreement.
- Short-term Municipal securities.
- Other instruments.

a) Treasury Bills

Treasury bills are short-term debt of the government which has maturity period of 91 days, 162 days or 364 days. These securities are issued in denominations of Rs 1000 and sold on a discount basis. The size of discount is determined in an auction, which will depend on the term of the bill and the prevailing market conditions. Treasury bills are issued in book-entry form; the buyer receiver a receipt at a time of purchase and the bill's face value at maturity. They do not carry coupon or stated interest so, they are called zero coupon bonds or deep discount bonds. The yield on Treasury bills is the difference between redemption value and purchase value. Treasury bills are considered as risk-free assets so that they have low yield to maturity and this yield is treated as interest income for tax purposes (Alexander, et al., 2003:348; shrestha, et al., 2003:72)

In U.S. security market, US Treasury issues treasury bills at regularly scheduled auctions to refinance maturing issues and to help finance current federal deficits. It also sells bills at irregular basis to smooth out the uneven flow of revenues from corporate and individual tax receipts. Persistent fedeial deficits have resulted in rapid growth in Treasury bills in

recent years. Congress first authorized them in 1929 (Cook, 1998:75). The federal Reserve Bank of New York, acting on behalf of the U.S. Treasury, auctions each new bill issue to dealers and other investors. The bills go to the bidders offering the highest price, there bye resulting in the lowest implied interest cost to the treasury. Because of the low risk and short maturity of these instruments, treasury bills are attractive instruments for many financial market participants. Individuals, corporations, state and local governments and money market mutual funds have large holdings. To individual and commercial investors, treasury bills constitute approximately one-forth of the total of all U.S. government marketable debts (santomero and Babbel, 1997:244-245).

In Nepal, NRB issues Treasury bills on behalf of the government to meet funding gap of the government to support various development programmes. According to the Economic survey 2005/2006 published by ministry of finance, Treasury bills during the FY 2005/06 increased by 22.05 percent totaling Rs. 62,970.3 million compared to Rs. 51,383.1 million during the corresponding period of F/Y 2004/05.

b. Commercial Paper

Commercial paper is a short-term unsecured promissory note issued by corporations and foreign governments. It is a low-cost alternative to bank loans for many large credit-worthy issuers. Issuers are able to efficiently raise large amount of funds quickly and without expensive securities exchange registrations. They sell paper, either directly or through independent dealers. Investors in the form of commercial paper earn competitive, market determined yields in notes whose maturity and amounts can be tailored to their specific needs (Hahn, 1998:105). The note is often additionally backed by unused bank lines of credit and /or a guarantee of a present corporation. These notes are issued for terms ranging from one day to one year (Hatch, 1983:84)

Commercial paper has a maturity period of up to 270 days. It is typically issued at a discount from face value, matures on a specific day, and is negotiable: Credit risk is perceived to be relatively low, and liquidity is also low. Accordingly investors tend to hold to maturity. Consequently, yields on commercial paper exceed those on Treasury obligations of similar maturities. Because of the advantages of commercial paper for both investors and issuers, commercial paper has become one of America's most important debt instruments. It is the second largest money market instrument, interims of outstanding

debt, behind T-bills. Money market funds are the largest investors in commercial paper. Insurers, banks, thrifts, non-official corporations, and state and local government bodies are also important investors in this instrument (Santomera and Babbel, 1997: 253-255)

In Nepal, no company has issued commercial paper so far. The company culture of efficiency is missing linkage to provide strong base for issue of commercial papers in Nepal. In other words, public confidence does not exist in Nepal to accept commercial paper (Shrestha, et al.. 2003:72-73)

C. Certificate of Deposit (CD)

A certificate of deposit is a document evidencing a time deposit placed with a depository institution. The certificate states.

- The amount of the deposit.
- The date on which it matures.
- The interest rate and
- The method under which the interest is calculated.

A CD can be legally negotiable or non-negotiable, depending on certain legal specifications of the CD. City bank of New York originated Negotiable CDs in 1961. A negotiable CD is a receipt from a commercial bank that can be sold by one investors to another investors who can in turn resell them. Negotiable CDs can therefore be easily traded in active secondary market. The depositor generally must hold Non-negotiable CDs until maturity. Most CDs feature a fixed interest rate to maturity; however some CDs have variable interest rates. CDs are issued both in bearer and registered firm. A bank tries to sell as many CDs as possible directly to investors. Because banks have limited capability to sell all their CDs directly to investors, however, they often sell some of their CDs to dealers who resell them to investors. In general, smaller banks and foreign banks make the greatest use of dealers when selling their CDs. Banks also frequently sell those CDs to dealers that are hard to sell directly to investors, such as longer-term CDs and variable rate CDs (Walter, 1998:90).

Like treasury bills, CDs are also sold at discount basis and repaid at par value. The difference between redemption value and purchase value amount is the holding period

return. CDs are highly liquid, almost risk-free and yield higher return than treasury bills, so they are popular form of short-term investment for companies and individual investors. In Nepal, only a few commercial banks issue CDs as capital market is not proving efficient and government regulations proved to be restrictive than liberal in facility commercial banks to play active role in capital market-(Shrestha, 2003:72)

d. Banker's Acceptances (BA)

A Banker acceptance was invented to suit the need of a party requiring temporary finance to facilitate and trading of specific goods. The party needing finance would approach investors for this temporary finance. The investors or lenders would then lend a certain amount to the borrower in exchange for a document stating that the debt would be paid back on a certain date in the short-term in future. The redemption of the loon would have to be guaranteed by a bank, called the acceptance by the bank making the arrangement. Thus, the name is "banker's acceptance" (Hatch, 1983:83)

It is, thus, simply a time draft drawn on and accepted by a bank. Before acceptance, the draft is not an obligation of the bank; it is merely on order by the drawer to the bank to pay a specified sum of money on a specified date to a named person or to the bearer of the draft. Upon acceptance, which occurs when an authorized bank employee stamps the draft "accepted" and sings it, the draft becomes a primary and unconditional liability of the bank. If the bank is well known and enjoys a good regulation, the accepted draft may be readily sold in an active market (La Roche, 1998:128). In exchange for guaranteeing the time draft, the accepting bank is given international trade documents, temporary title to the goods that are related to the transaction, and a commission for its services. Investors in BAs include commercial banks, foreign central banks, money market funds, and are issued with maturities ranging from one to six months (Santomero and Babble, 1997:255-256)

BAs have very active secondary market in America. The yields of BAs are slightly lower than those of commercial paper because BAs are less risky due to the borrower's pledge to pay, the collateral of goods and the guarantee of the accepting bank. Over the past 70 years, investors have not suffered any loses of principal. BAs are very popular in export-import business. Acceptance arising from imports into the United States accounted for 28 percent and those arising from the shortage of goods in or shipments of goods between

foreign countries accounted for 38 percent (Santomero and Babble, 1997:256, La Roche, 1998: 128-137).

e. Eurodollars.

In the world of international finance, large short-term CDs denominated in dollars and issued by banks outside the United States (most often in London) are known as Eurodollar CDs (or simply Euro CDs). Also available for investment are dollar denominated time deposits in banks outside the United States, known as Eurodollar deposits. A key distinction between Euro CDs and Eurodollar deposits is that Euro CDs are negotiable, meaning that they can be traded, whereas Eurodollar deposits are non-negotiable, meaning that they cannot be traded.

The demand and supply conditions for such instruments may differ from the conditions for other U.S. money market instruments, owing to restrictions imposed (or likely to be imposed) by the United states and other governments. However, enough commonality exists to keep interest rates from diverging too much from rates available on domestic alternatives. One difference from CDs issued by U.S. banks is that the Euro CDs do not have Federal deposit insurance (Alexander, et al, 2003: 345). Large corporations with international access invest on Eurodollars (Shrestha, et. al, 2003:73)

F. Repurchase Agreement (REPO)

Repurchase Agreement, the REPO is an agreement between two parities where by one party (Mostly the dealer of the government securities) sells securities to another party and agrees to buy the same securities at agreed higher prices at later date (Shrestha, 2003:73)

The terms repurchase agreement (REPO) and reverse repurchase agreement refer to a type of transaction in which a money market participant acquires immediately available funds by selling securities and simultaneously agreeing to repurchase the same or similar securities after a specified time at a given price, which typically includes interest at an agreed upon rate such a transaction is called a REPO where viewed from the perspective of the supplier of the securities (the party acquiring funds) and a reverse REPO or matched sale-purchase agreement. When described from the point of view of the supplier of fund. (Lumpkin, 1998: 59-61)

The security used may be a Treasury, Obligation, agency issue, mortgage-backed or Banker's acceptance, and the timing of the two transactions can be one day or several months apart. At the end of the period, the initial seller gets back the security and the purchaser gets back the yield implied by the difference. In the prices of purchase and repurchase is the REPO rate. The REPO rate charged to the initial seller depends on the nature of the under lying security (risk, liquidity and maturity) and the credit worthiness of the initial seller. The major players in the REPO market are banks, saving institutions and non-bank securities dealers. Investors such as banks, money market funds, and other non-financial firms who have funds to invest for short periods of time, take it as on attractive alternative to the Zero return received from idle balances in a checking account (Santomero and Babble, 1997: 256-257)

g. Short-term Municipal Securities.

Local governments or municipal governments often have temporary needs for cash to finance their own expenditures, to provide funds to some tax-exempt entities such as colleges and non-profit hospitals, and to a limited degree, to provide funds to private firms and individuals. To meet such needs, they often issue short-term municipal securities. There securities are issued in two forms: interest bearing notes and discount notes. The interest earnings and the capital gains in the case of municipal securities are generally exampled from the taxes, provided that the investor is a resident of the state or city that issues the debt instruments, Individuals, mutual funds, banks and other corporations are the major types of investors in municipal securities (Santomero and Babble, 1997: 248-250)

h. Other Instruments:

There are different other types of many market instruments used in different other countries. If use sees the American money market, besides above discoursed, federal funds, federal agency discount notes are very popular money market instruments.

2.1.4.2 Capital Market Instruments

Capital market provides a channel for the borrowing and lending of long-term funds. This is designed to finance long-term investments by business, governments and households. Trading of funds in the capital market makes possible the construction of huge establishments like: factories, school and highways. Financial instruments in the capital market have original maturities of more than one year. The principal suppliers and

demanders of funds in the capital market are more varied than in the money market (Rose, 2000).

Capital market consists of a series of channels through which the savings of the community are made available for industrial and commercial enterprises, and public authorities. In the capital market, demand comes from agriculture, industry, trade and government while supply comes from the individual or corporate savings, institutional investors and the surplus of governments. If comprises the savers – individuals and institutions – and bodies through which these savings are mobilized. The savings institutions like savings banks investment trusts or investment companies, specialized financial corporations and stock exchanges are some of the important constituents of capital market (Kuchhal, 1976:283)

The first step in studying capital market is to develop an understanding of the different classes of financial instruments. Some of the popular financial instruments that are traded in the capital market are:

- Equity or stocks (ownership instruments)
- Bond (Debt instruments)
- Derivative Securities.

a. Equity/Stock

Equities are often termed as – stocks or shares. Stocks represent part-ownership of a corporation. (Hatch, 1983:165). Holding a stock certificate means that holder owns the part of the corporation. Thus there are only corporate stocks, no government or state and local government stock, since individuals cannot own governments (at least not legally) (Ritter and silber, 1993:29). Equities or stocks are basically the contracts that establish an on going relationship between borrower and "lender" and almost always bundling some combination of "Control rights" and rights to be a "residual claimant". In the establishment of corporations of small and medium sizes, stock sales to the incorporators are usually the principal source of cash and other assests (Kent, 1972:264). The income that the stock holders receive is the dividend. Investment on equities is also known as – investment by way of proprietary interest. Such investment gives the investor a status of proprietor. He may be a sole proprietor, a partner, of a member of a joint stock company (Whyte, 1951:78).

People invest in equities because they want to make more income than they do in a savings account for the possibility of making more income, they assume more risk. There are several advantages and disadvantages of investing in stocks. The like; hood of dividends and price appreciation motivates most investors to consider common stocks. Many companies may declare relatively small cash dividends, perhaps with a return of only of 2 or 3 percent. But these companies may also offer a good chance for price appreciation over time. Equity investments also offer a high potential return. Greater than average returns are possible if one buys and sells the correct stocks. On the other hand, in equity investments risks of various types are also present. There is the financial risk that the company will go bankrupt. There is the liquidity risk that the price of a stock might be quite low when one wants to sell it. Along with them inflation risk also presents. In the period of high inflation, market prices of equity are depressed. Uncertainty of yield is another disadvantage of common stocks. Even a company with an excellent record of paying cash dividends might skip some dividends during market downturn. Since, many stocks vary in price with certain news events, world happenings and economic and political variables, investors need to be alert to current happenings in order to know when to sell quickly in order to reap profits or reduce losses (Garman et al., 1985: 490-492).

There are two main types of equity ownership prevalent in the market. They are:

- Common stock and
- Preferred stock

i) Common stock

Common stock is the first security of the corporation to be issued and, in the event of bankruptcy, the last to be retired. Common stock represents an ownership share in the firm; it has the lowest-priority claim on earnings and assests of all securities issued (Francis: 1991:50). It is the residual claimant of the earnings. The Chance of a common stockholder getting anything back from a bankrupt firm is minimal. They receive whatever is left after all the other claimholders have taken their rightful share. But, common stock has an unlimited potential for dividend payments and price appreciation payment of common dividend is purely discretion any on the part of the management. If the earnings are retained rather than distributed, stockholders do benefit in the sense that if the retained earnings are invested profitably, the firm will grow in size, and the stockholders will eventually capture the growth.

Thus, stockholders can expect to receive their income in the form of capital gains as well as dividends. Management controls the distribution of income between dividends and capital gains through its control over the fraction of earnings distributed as dividends. Firms that pay out a smaller fraction of their earnings as dividends can be expected to grow at a faster rate than firms that pay out a larger fraction.

The investor's risk is higher with common stock than with any other security a firm might issue. As a result of this risk, investors refuse to invest in common stocks unless they offer a role of return sufficiently high to induce the investors to assume the possible losses.

When investors buy common stock, they can obtain certificates as a proof of their part as owners of the firm if they so desire. A stock certificates state the number of shares purchased, their par value (If any), and the number of shares bought are noted in the stock record book of the transfer agent. As a result, there is little reason for most investors to have stock certificates prepared. The registrar checks to verify that the transfer agent made no errors.

Common Stockholders elect the board of directors and vote on major issues that affect the corporation because they are the owners of the corporation. But most stockholders are not interested in the voting power they possess and simply sign and return the proxies mailed to them by the company. A proxy allows a named person, usually a member of corporate management, to vote the shares of the proxy signer at the stockholders' meeting. The use of proxies usually allows management, which seldom owns a majority of votes, to vote its decisions into effect.

Authors like werrich, Garman, Eckert and Forgue have classified common stocks among – blue – chip stocks, income stocks, growth stocks, speculative stocks, cyclical stocks, and defensive stocks. Authors remark that such classification will aid when matching an investor's preferences with stock investment options.

- A blue-chip stock indicates a company with a well-regarded reputation and a long history both of good earnings and consistent cash dividends. An income stock has a

cash dividend that is higher than average because the company ha high earnings and chooses to regularly declare cash dividends.

- Stocks of companies that are lenders in their fields and have several consecutive years of above-average earnings are considered growth stock.
- A speculative stock has a spotty earnings record but has an apparent potential for substantial earnings at some times in the future even though such earnings may never be realized.

- A cyclical stock has a price that typically follows the general state of the economy and the various phases of the business cycle.
- Despite a general decline in economic activity, some companies maintain substantial earnings because their products are needed. These companies offer defensive stocks.(Garman et al, 1985:486-488; Weirich, 1983:395-398)

ii) Preferred Stock

Preferred stock is also a form of equity ownership. It is a hybrid of sorts between a fixed and a variable income security. It is occasionally referred to as a hybrid security since its characteristics lie some where between those of common stock and bond. Its claim isn't really fixed and definite in the sense that it can force the firm into bankruptcy if it isn't paid in full. On the other hand, its claim is limited in size to a specified amount. In general, the only leverage a preferred stockholder has over the firm is that no dividend can be paid on the common stock until the specified dividends have been paid on the preferred stock. Preferred stocks are usually perpetual securities having no maturity date, although there are expectations to this general rule. Preferred stocks are commonly callable, however. (Haugen, 1997:14-15). Preferred shareholders do not share in the profitability of a firm beyond the stated dividend rate, in this ground. It is rather curious why they are called preferred. But, they are superior in two areas.

1. Although they have no rights of dividends, if corporation allocates earnings to declare dividends, preferred shareholders must receive before common shareholders. In the event of forced liquidation, preferred shareholders have a claim on remaining assests up to the par value, as a priority over the common shareholders.

2. It seems that preferred stock is a hybrid security with characteristics of both common stocks and bonds. (Santomero and Babble, 1997: 344-345; Cowdell et al, 2001: 128; Hatch, 1983:206-208)

Preferred stockholder have a legal priority (or seniority) over common stockholders with respect to earnings and also with respect to assets in the event of liquidation. But, preferred stockholders are in a more risky (or junior) position relative to the corporate bondholders. Preferred stockholders generally receive a greater rate of return on their investment than bond holder's in compensation for the greater risk they bear. However, they generally receive a lesser rate of return than the common stockholder because they assume less risk. In terms of control, the preferred stockholder usually is in a better position than the bondholder assuming that the preferred stockholder has voting rights. (Francis, 1991: 55)
There are two basic types of preferred stocks, Cumulative and Non-cumulative.

- In the case of cumulative preferred stocks, if the from skips its dividend in any given year, no dividend can be paid on the common stock until that dividend and any other arrear dividends on the preferred have been paid in full.

- In the case of non-cumulative preferred stocks, if the firm skips the dividend on the preferred in any given year, it can pay dividends on the common as long as it pays the dividends on the preferred in the same year. a non-cumulative preferred has a very weak claim on the earnings of the firm (Haugen, 1997:15)

Besides, preferred stocks can be classified as participating or non-participating, callable or perpetual, convertible or non-convertible, term-preferred share etc.

A term – preferred share is a relatively recent Canadian phenomenon. The phrase is used to describe a particular type of share that has many of the characteristics of debt. A term-preferred share pays dividend and is preferred over the common shares as to assests but often has additional features. For example, the dividend is frequently set as a floating rate and is guaranteed by the company. Term-preferred shares are usually privately placed. (Hatch, 1983:209)

Probably 90 percent of all stock outstanding today is common stock since it has a broader appeal to investors than preferred stock. Since the yield is fixed, the price of preferred stock generally will not increase as the company becomes more profitable and successful. Thus, the typical preferred stock holder does not benefit from price appreciation as would a common stock holder. Instead, the price of preferred stock is based on prevailing interest rates (Garman et al; 1985:492-494). In Nepal only 5.44% of total outstanding stock is covered by preferred stocks.

b. Bond

A bond is a type of fixed income security by a borrowing entity in which the amount to be paid to the investors is specified in the investment contract or indenture. The inclusion of provision specifying the amount of income is a major distinguishing characteristic of bonds. In contrast, the board of directors determines the income from common stock cash dividend-periodically. A trustee (usually a large commercial bank) is appointed when the bond is issued to represent the collective interests of investors (Cheney and Moses,1999: 314)

Bond represents the debt instruments which represent borrowing. These are also known as contractual obligations since the creation of a debt is implemented by some form of contract fixing the rate of interest and defining the terms and conditions of repayment (Whyte, 1951:60). Bonds exist in a wide variety of forms – the corporate bonds (debentures), government bonds, municipal bonds etc. The firm which wants to raise a few million amount prints up fancy pieces of paper called bonds and try to sell them. Many individuals and financial institutions are interested in buying these papels. This paper states that the issuer (the borrower) promises to pay whoever owns the bond (the lender) certain interest payments at specified dates in the future. The paper also states when the bond will mature – the date when the loan will be paid off to whoever owns the bond at that time. Some bonds have an original maturity of only a few years, while others have twenty or thirty years. At times, perpetual bonds called consol have also been issued (Ritter and silber, 1993:28; Richards et al., 1984:375)

The differentiation made in bonds as notes and bonds are also seen, according to the maturity period. Notes have maturities of ten or less at issue date, whereas bond maturities exceed ten years at issue (Santomero and Babbel, 1997:269). The term to maturity is also

known as tenor. Corporate bonds are often known as debentures. Debenture holders have a prior claim on the assests of the company. The interest on debentures is a tax-deductible expense of the firm (Vishwanath, 2000: 314-315; Grinblatt and Titman, 2003:35-37).

The economic environment of the late 1970's and early 1980's resulted in some dramatic changes in the bond market and, consequently investors' attitudes towards bonds. Historically, investing in bonds was characterized as simply "buy and hold" or "clipping coupons" – a passive investment strategy that lacked the glamour of investing in other type of securities. Since the early 1980's however, double – digit inflation, monetary and fiscal policies, and international events have produced not only extremely high nominal interest rates but also considerable volatility in interest rates, which has resulted in fluctuating bond prices.

Predictably, there is a considerable debate about the future bond environment. On the one hand, some analysts view 1970s and 1980s as simply another page in history that will be remembered as unusual but not predictive; they believe the future will see a return to more passive bond portfolio management. On the other hand, some analysts believe the period was a good indication of future; they think that financial markets will be appropriate. Volatile markets encourage active management and call buy and hold strategies into question (Cheney and Moses, 1999: 316 – 319)

Types of bonds

There are different types of bonds such as:

- Corporate Bond
- Government Bond

(i) Corporate Bond

Corporate bond is a long-term promissory note issued by a business organization. Corporate bond has more default risk than government and municipal bonds and hence offer higher return too. They are traded in organized exchanges as well as over-the-counter market. Corporate bonds have not yet been popular investment alternative in Nepal. The only outstanding bond listed in NEPSE is the bond of Himalayan Bank Ltd (Thapa, 2002:256; Shrestha, et al. , 2003:8)

When corporate bonds are issued, they are backed by an indenture in which the firm promises to the bond trustee that it will comply with certain provisions. Among these are the payment of the scheduled interest and principal. There may also be restrictions on the amounts of dividends that can be paid to stockholders. There may be restrictions on the use of the proceeds of the bond issue, guarantees on the acquisition of insurance and restrictions on investments by the firm in the capital market (Haugen, 1997:13).
A Corporate bond comes in a wide variety of forms:

Mortgage bonds represent debt that is secured by a pledge of specific property. In the event of default, the bondholders are entitled to obtain the property in question and to sell it to satisfy their claims on the firm. In addition to the property itself, the holders of mortgage bonds have an unsecured claim on the corporations. Mortgage bondholders are usually protected by terms included in the bond indenture.

Collateral Trust Bonds are backed by other securities that are usually held by the trustee. A common situation of this sort arises when a security of a subsidiary firm are pledge as collateral by the parent firm.

Equipment obligations, also known as equipment trust certificates are backed by specific pieces of equipment like railroad cars and commercial aircrafts. If necessary, the equipment can be readily sold and delivered to a new owner. The legal arrangement used to facilitate the issuance of such bond can be very complex. The most popular procedure uses the "Philadelphia Plan" in which the trustee initially holds the equipment and issues obligations and then leases the equipment to a corporation. Money received from a lessee is subsequently used to make interest and principal payments to the holders of the obligations. Ultimately, if all payments are made on schedule, the leasing corporation takes title to the equipment.

Debentures are general obligations of the issuing corporations and thus represent unsecured credit. To protect the holders of such bonds, the indenture will usually limit the future issuance of secured debt as well as any additional unsecured debt.

(ii) Government Bond

The securities issued by the government for the collection of the fund is called government bond. Actually government raises fund from market to conduct regular activities to conduct development programs, to recover the deficit budget etc.

In Nepal, Nepal Rastra Bank has been actively issuing various government securities with the main aims of tackling the deficit budget. In Nepal, the government to fulfill its needs issues following security.

Treasury Bills

Treasury bills are the short-term instruments of the government. It normally matures in 91 days while some mature in 364 days. Thus, treasury bills are issued to meet short-term financial requirement of the government. Treasury bills are sold to the bidders in the order that one who bids with the expectation of low interest rate. Nepal government initiated the process of selling treasury bills to banks, financial institutions and individuals since 2018 and thought an auction process since 2045.

Development Bond

By, the word it is clear that it is issued by the government for the purpose of development works. It matures normally in five or more years. In the year 2062 Nepal government has issued 10 year development bond. It has fixed and minimum interest rate. The payments of the interest are paid on semiannual basis. The income from these bonds is taxable. It is open to all as the individual willing to purchase can purchase it. Nepal government initiated the process of selling development bond since 2020.

National saving Bond

It is also long-term bond and it normally bears maturity period of five years. It has fixed interest rate payable semiannually. These bonds are normally tax-free bonds and having high interest rates. The main holder of these bonds are general pubic because it is focused to the individual investors but also other organization and financial institution can purchase it. Nepal government initiated the process of selling National saving bond since 2040.

Special bond

Special bond is issued on special occasion when government fall sort of funds. The government issues special bonds to those parties to whom the government has to make payments. Instead of paying cash, the government issues special bonds as a substitute of cash repayment and extends the period of payments. Nepal government initiated the process of selling special bond since 2023.

Public saving Card

It is also a long-term debt instrument, which normally matures in five years. The characteristic of the public saving card is same as the other long-term bonds. It has also fixed interest rate and payable semiannually. It can be purchased only by Nepalese citizens. It is also a taxable government bond. Nepal government initiated the process of selling public saving card since 2059.

C.Derivative securities

Derivatives are given their name as derivatives because their value is derived from the underlying assest with which they are associated. These instruments provide investors with the confidence that a degree of liquidity is maintained.

Derivatives are financial contracts whose price relates to the price of a particular assest. It means the value of derivative securities, if not all; a part of their value is derived from the value of another security. For example, the value of a call option is derived from the value of the common stock against which the call option is written; the value of a commodity futures contract is derived from the value of a commodity, which must be delivered in the future. There are wide range of derivatives, which are used mainly for managing financial risk (Fuller and Farrell, 1987:16). Derivate securities are important investment alternatives in developed market, but they are not available in Nepal. A few important derivate securities from the point of view of investors are:

丿 Option

An option is a contract between two people where in one person grants the other person the right, but not the obligation to buy or sell a specified assest at a specified (Predetermined) price on or before a set expiration date. Between any two parties involved in the contract, the party receiving the right to buy or sell a specific assest is called an option buyer and the person giving the right to sell or buy the assest is called an option seller or option writer.

An option is probably the most popular derivative security in the world of investment. It is derivative because it derives its value from an underlying security such as a stock, a bond etc.

Some options are traded in the organized exchanges and are known as 'exchange traded options' others are traded in the over the counter (OTC) market and are known as 'OTC options' or 'off exchange options'. An option is the result of private negotiations of two parties where as exchange traded options are initiated and further traded or organized exchanges. Exchange traded options are standardized as to the amount and price of the underlying assest (Gautam and Thapa, 2061:7.1)

The two most basic types of option contracts are known as calls and puts. A call option is an option contract it gives the buyer the right to buy a specific number of shares on or before a specific future date at a stated price from the option writer. A second type of option contract for stocks is the put option. It gives the buyer the right to sell a specific number of shares of a specific company to the option writer at a specific selling price on or before a specified future date at a stated striking price. (Bhattarai, 2006:390)

Cap, Floors and Collars

A cap is a call option on interest rates, often with multiple exercise dates. A floor is a put option on interest rates, often with multiple exercise dates. Collar is a position taken simultaneously in a cap and a floor (Saunders, 1997: 506)

Warrants, Rights and Convertibles.

- **Warrants**

A warrant is a long-term option that gives the holder the right to purchase a stated number of shares of the company's stock at a specified price within stipulated period of time. Generally, warrants are distributed with debt and preferred stock, and they are used to induce investors to buy long-term debt or preferred stock with a lower coupon rate than would otherwise be required.

Generally, warrants are used by small, rapidly growing firms as "sweeteners" when they sell debt or preferred stock. Company can reduce coupon rate and avoid some restrictions by attaching warrant with the security. Moreover, some time large firms use bonds with

warrants to collect heavy amount. A bond with warrants has characteristics of both debt and equity. It is a hybrid security that provides the financial manager with an opportunity to expand the firm's mix of securities and thus to appeal to a broader group of investors.

⁾ Rights.

Growing corporations frequently need to raise additional capital. They do this by issuing bonds and or selling new shares of stock. If additional stock is sold, stakeholders of most corporations will experience dilution of their ownership position. The issuing corporation offer prefers selling shares to current stockholders because it is less expensive. A right is a legal instrument offered to a stock holder to purchase a proportionate number of shares of new company stock at a specific price during a limited time period. Rights have intrinsic financial value because they are normally offered at a price some what lower than the current market value of the stock. Consequently, a market exists for the buying and selling of rights, and once again we inter the world of the speculator. An especially, attractive speculative investment is using margin to buy rights with the hope that the value will rise (Garman et al, 1985: 620).

⁾ Convertibles

Convertibility is a feature attached to a security. It is an option to the buyer of security with such attachment. Convertible securities are such financial instruments which can be converted into a stated number of common stocks of the issuing company on or before the expiration date. These are the hybrid securities including the feature of bond or preferred stock and common stock. Convertible securities are issued by companies to raise long-term funds. The interest rate or dividend rate on such convertibles will be lower than that of the non-convertible because of its conversion feature. By doing so the issuing company reduces its cost of financing as well as makes the security easily saleable in the market.

Bonds and preferred stocks both may have the conversion features. Moreover, a company can issue convertible bonds and convertible preferred stocks. Bonds with convertible features are called convertible bonds and preferred stocks with these features are called convertible preferred stocks. (Bhattari, 2006:429)

As a rule, convertible securities are callable. The purpose of the call provision is not to redeem the convertible bonds or preferred stock but to force conversion of the issue when

the conversion value of the security is well above the call price. In practice, few convertibles are ever redeemed

2.2 Investment Objectives and Preferences of Investors

People invest for one or more of four general reasons: (i) to increase income, (ii)to have funds available during retirement years, (iii)to achieve specific financial goals and (iv)to gain a feeling of financial security. Getting ahead through investments requires willingness, ability and discipline. Willingness involves understanding your own motivations. People report these kinds of reasons for investing:

I have too much money just sitting in the bank

I want to get rich quickly.

I want to get rich slowly.

I want to buy a Mercedes-Benz automobile.

I want to retire with a secure income.

My parents have to depend on me financially after their retirement.

My children should not have to support me in my old age, and many more like these.

'Ability' has to do with knowing alternative investments, finding investment funds and making intelligent investment decisions. And,' discipline' describes the courage to act responsibly in financial matters (Garman, 1985:446-447).

The economists John Maynard Keynes, writing in his famous 1936 General Theory, identified three reasons for holding financial assests

Precautionary -saving for rainy days.

Transactionary -to accumulate day -to- day needs.

Speculative- moving between money and non-monetary assists in anticipation of financial returns.

More recently, the monetarist Milton Friedman proposed his portfolio theory as to why people hold different financial assests. This suggests that people will satisfy their cash demands before considering any other assests. They will then fulfill their needs for highly liquid accounts, then less liquid but potentially higher return assests(Cowdell et al.,2001:2).While making savings and investments, people are driven by various stumali.These vary according to personal need and preferences, as well as factors such as attitude to risk, liquidity requirements, life cycle hypothesis etc.(Cowdell et al.,2001:3).

This is essentially the problem of equating the requirements of the investor with the suitability of the investment. The requirements of different investor may vary greatly. They may be determined by the urgency of absolute need, or they have latitude enjoyed by those wants are satisfied. More often than not the actual requirements will lie somewhere between these two extremes. They may be capable of precise definition, but usually, there will be some uncertainty. The problem will be easiest when the requirements can be met by choosing from wide range of investments. It will be most difficult when full achievement is hardly possible or when it is a question of selecting the investments which, though falling short of complete fulfillment of purpose, yet come nearest to attaining what is required. One very important thing to note is that it is the requirements of the investor which should make the pace. There is the body which has to be clothed (Whyte, 1951:163).

Investors, a buyer of financial products, expect to obtain three characteristics from the financial instruments. They are the expected return, security and liquidity (Blake, 2000:57).The principal objective in making investments is to earn a return that compensates investor for the risk of the investment. To be more specific, the investment objectives are related to the

- Safety
- Growth of principal
- Regular return
- Liquidity (Stevenson and Jennings 1984:3-5)

a. Safety

Many investors equate the objective of safety of principle with the purpose of high quality investment instruments. Saving accounts, certificates of deposit and saving bonds all have a virtually guaranteed return of principal. While these types of investments may help keep the amount of the portfolio reasonably constant, inflation may reduce its purchasing power. Hence, investors often seek to keep the portfolio safe in terms of purchasing power by seeking enough growth to offset changes in the cost of living. For the pension funds, investment on safety instruments is more desirable. The safe investment made by Mexican companies -90% of their pension funds money is invested in government bonds-has made Mexico's future pensioners more fortunate. But in Britain and America, pensions funds are

suffering from chronic shortfalls, for them 90% investment on government bond is too high.(The Economist, April 26th 2003:77)

b. Growth of principal

Price appreciation of principal in addition to the secured principal is also one significant objective of investors. When an investment is purchased with the hope of earning a capital gain at the time of sale, the investment objective is growth, which is the primary reason most individuals invest. A crucial task for the investor is to balance the desire for safety of principal with the desire for growth in a manner, consistent with his or her personal preferences.

C. Regular Income

Investors may realize investment income either in the form of regular income or capital appreciation. Under some circumstances regular income is either necessary or highly desirable. It can be the objective to those who must produce a fixed amount of income from investments for living expenses. A retired individual often needs a high level of current regular income to be able to supplement income from social security or other pension plans. Current income may often be desirable if the individual or institution owing the investment is in a very low or zero marginal tax bracket. A marginal tax bracket is the tax rate that applies to the last currency earned by the tax payer. The idea here is that income in the form of capital appreciation is in a more favorable tax position than current income received in the form of dividends or interest. Hence, individuals in high marginal tax brackets may prefer capital appreciation and individuals and institutions with low or zero tax brackets may prefer current income. The need of regular income varies greately, depending upon such factors as the age, wealth and non-investment income of the investor.Bonds, preferred stocks, and other investments with current yields are traditional income investments.

d. Liquidity

Liquidity is the ability to turn an investment into cash quickly at a value close to the original amount of the investment. Only high quality investments with short maturities would qualify as being liquid under this strict definition. Another definition of liquidity introduces marketability aspects land defines liquidity as the ability to turn an investment into cash quickly at a price close to the last transaction of that assest.Under this definition,

many more investments would qualify as being liquid, since we ignored the safety-of-principal component that says we must sell at a price close to the cost of investment. In investment planning it is important to allow for a certain degree of liquidity so that if cash is needed unexpectedly, an investment would not have to be sold for a loss in order to raise the funds (Stevenson and Jennings, 1984:3-5; Weirich, 1983:336-338)

2.3 Review of Related Studies

2.3.1 International Journals

R.R. Garside, 1998

In this project report, Garside have described – "At one level, capital markets are simple enough. The primary market is where companies raise capital by issuing securities, basically either shares or bonds. The secondary market is where those same securities are traded. Those definitions are simple and there is nothing very complex about the mechanisms for issuing, trading or setting. Sometimes, the term capital market is extended to cover long-term bank loans to companies. But at another level, the capital markets are more complex because when they function properly, they are the very hubs of a free market economy. In them, all economic currents and forces meet and interact.

"A healthy capital market is democratic and egalitarian. It shows no respect for class or caste. It does not acknowledge hierarchy. When the price of share falls, it falls for all those who hold it. Financial analyst may have decorated in math but some of the best traders of equities future and options have been near a university."

Mark Grinblatt and Matti Keloharju, 2001

Grinblatt and Keloharju have conducted a study to monitor buys, sells and holds of individuals and institutions in the Finish Stock Market on a daily basis. They have tried to explore the motivations for trade. With the variety of tests, the study lists several factors like: past returns, reference price effects, volatility, life cycle, size of holding period capital gain or loss, and tax effects which motivate the individual and institutional investors to decide on buying and selling. These all are determinants of investment decisions.

Past returns are the most important factor for less sophisticated investors – households general government and not-profit institutions; they are more predisposed to sell than to

buy stocks with large past returns. Such investors tend to be contrarians and foreign investors are opposite, they show momentum behavior.

Life cycle consideration also account for investment decisions. Investors tend to sell (Primarily inherited stock) early in life, purchase stock in the prime earning years of middle age, and then sell stocks in old age. The youngest investors buy more. Investors begin net sales of stocks at an old age that is latter in life. So far as volatility is concerned, high volatility increase the propensity of households to buy rather than sell a stock.

Luis M. Viceira, 2001

Luis M. Viceira has made a study in relation to portfolio choices and income. The paper examines how risky labour income and retirement affect optimal portfolio choices. "With idiosyncratic labour income risk, the optimal allocation of stocks is ambiguously larger for employed investors than for retired investors, consistent with the typical recommendations of investment advisors. Increasing idiosyncratic labour income risk raises investors' willingness to save and reduces their stock portfolio allocation towards the level of retired investors. With time variation in investment opportunities, retirement and death play an instrumental role as events that exogenously fix the individual's investment horizon. When future level income is certain, it is optimal for employed investors to hold proportionally more stocks in their portfolio than it is for retired investors" (Viceira, 2001:433)

This paper shows, employed investors have an additional source of income, they can afford more aggressive portfolio than retired investors. Financial advisors typically recommend that their customers invest more in stocks than in safe assets when they are working, and shift their investment towards safe assets when they are retired.

Michael S. Rashes, 2001

Rashes had conducted a study to find out how the confusion of investors affects the stock market. As per the confusion of investors, three possibilities are identified – incorrect order entry; failure to utilize all available information and ticker symbol confusion. This paper basically focuses on the ticker symbol confusion of MCI Communication (MCIC) and Massmutual Corporate Investors (MCI). Here, Rashes have illustrated that as many as one percent of the MCIC trades those investors intend to make incorrectly result in MCI

transactions. This happened due to the investors' confusion between a well-known stock and a lesser-known one that have little in common besides their similar ticker symbols.

This paper examines the noise traders, who actively trade on the basis of incomplete or premature information. Some investors are also found failed to condition their portfolio decisions and the complete information set. This paper finds that genuine shifts in sentiments due to misunderstanding of information about a single stock can lead to deviations of security prices from fundamental values.

Dimitri Vayanos, 2001

Vayanos has illustrated strategic trading of strategic traders in a noisy market. Large traders, such as dealer, mutual funds and pension funds, play an important role in financial market. He assumes, trading motives for large traders are generally of two types – informational and allocation. Informational motives arise from private information about asset payoffs and allocation motives are risk sharing, portfolio rebalancing and liquidity. Large traders or investors are assumed to be risk averter instead of risk neutral. This paper reveals that the strategic traders like large traders often play with their stocks, termed as market manipulation. They go changing their holdings as per the inside information. Likewise they sell the stocks with the inside information that price will fall because of negative earnings announcements and they will again repurchase the stock when the price falls. These are also known as 'round trip transactions'.

Kent Daniel, David Hirshleifer and Avanidhar Subrahamanyam

A study made by Daniel, Hirshleifer and Subrahamanyam have concluded that securities market under overreactions based on two well known psychological biases – investor over confidence about the precision on private information and biased self attribution, which cause asymmetric shifts in investor's confidence as a function to their investment outcomes. According to them, over confidence implies negative long-term auto correlation, excess volatility and when managerial actions are correlated with stock miss pricing, public event based return predictability. Biased self attribution add positive short lag auto correlation 'momentum', short run earning 'drift' but negative correlation between future returns and long-term past stock market and accounting performance.

2.3.2 Related Articles Reviewed

Organized Stock exchange in Nepal had made a history of ten years. Although it is not sufficient to make a history Nepal Stock Exchange has faced all types of possible happenings. The big bullish period, the long bearish period, the unprecedented market capitalization, the quite fair market driven by innocent and honest market intermediaries, the quite unfair market driven by ~ll1fair practices, the rumor driven market, the big changes in ownership of joint venture banks, the addition and subtraction in the listed companies, etc are some key events in the history of Nepalese capital market. Though, the concept of secondary market was developed especially for the promotion of portfolio management of big business houses and big investors, the concept has failed in our country due to restrictions on their participation in the market **Agrawal, 2004:** 68-69.

Jagdish Agrawal - CA as well as Broker of stock market - has remarked "If we talk about the size of the market we can compare it with a person suffering from a disease, due to which his height has stopped increasing but he is gaining in weight (Agrawal, 2000)

In one critically written article, **Atma Ram Ghimire** had remarked -

“The components of the market are lame and weak and perhaps work for vested interest. The Securities Board the supreme body this market gave the permission to Taragaon Regency Hotel to increase the number shares issued from 8 million to 12 million units after the public oversubscribed the initial after. despite the advise from experts not to do no. To repeat the same mistake, the Board gave almost similar permission to Hotel Radisson and now public investors are again cheated. The board has thus repeatedly supported companies in their activities that lead to cheating the investors. There have been so called market makers in the stock market but they did not appear when the market was booming with unnatural growth. Neither are they in sight now when the market is crashing. Why cannot the board cancel the license the recalcitrant market makers and issue new ones Why in a liberal and market economy is the license/quota system being followed It should be open the all - brokers. market makers, and stock dealers. Just fix straight and transparent requirements like 5 million capitals. Master's degree in economics management accountancy and whatever but not something based on 'HAKIMKO BIBEKMA I (the judicious will of the decision maker).

The broker Organizations are real private, and run a one-man show. Invest of them do not have real education and knowledge about the market. They do not have analysts or

advisors to make suggestions to the investors. Their primary motto is to make transactions and earn commission. They have not paid a single rupee from the earning they have made from this market for its promotion. They have not even spent on their basic office automation and systematic transaction recording. One of the reasons of such aloofness is the security provided by NEPSE and Board hakims, denying other qua/tiled institutions a free entity into the market.

The general public has invested recklessly. They just believe what one broker or the investor says about scrip. They must study (be informed) about the company before making they must receive the financial information before they make investment and act mtiullafly. This will avoid the typical crashes the market experienced in the past which were largely created by unnatural activities on the institutions and individuals concerned"(Ghimire, 2001)

When we see the share market, more than 90 percent of the transactions that take place 111 the share market relate to the securities of the financial institutions. We can count the active industrial and trading sector units on our finger. This shows that the securities market in Nepal is essentially the financial sector securities market. This also implies that the financial sector has transformed itself into the most dynamic and also the most attractive sector of investment in Nepal. So credit of current position of public interest in share investment actually goes to bank and financial sectors. But challenge in this regard is that the industrial and trade sector have not been able to fulfills the expedition of the invester (Shrestha, 2004:77). *"it is because of the better performance of the financial sector that, public interest in share investment has highly increased."* Says Madan Raj Joshi, General Manager of Nepal Stock Exchange Ltd. However, the investment has been confined to selective companies only. There is a genuine cause behind this Majority of the manufacturing and processing companies and trading firms have become unable to fulfill the general investors' expectations, Neither they have become able to give return to the investors nor to disseminate information in time.

Navaraj pokharel, who recently completed two years' term as president of Nepal stock Brookes association, says the market was rumor driven in the past but it is now more or less information driven. As dissemination of information is mandatory to commercial bank and financial companies, credibility of such companies has increased. Besides, they have

been providing lucrative returns including bonus shares and right issues to the investors. The result, more pressure on shares of banks and financial institutions. This has raised a big question in the capital market circle: Will the capital market survive only on financial sector's performance? Stock market officials as well as investors and share brokers agree that the capital market of the country may not survive or sustain relying only on the financial sector. If something amiss happened, it may crash leading the economy to crisis. East Asian crisis is the latest example (Shrestha, 2001). Finance companies, in general, have provided better return to investors by way of dividend, bonus share and right share, Comparatively, it is much leaper to invest in finance companies than in banks in relative prices and cheaper than insurance companies in terms of return on investment. Capital gain is not that much impressive in finance company stocks in comparison to banking sector (Ghimire, 2001a.)

On the other hand, if we see the scenario of instruments Equity issuance formed a significant portion of total issue in the capital market since fiscal year 1993/94 till fiscal year 2002/03, which accounted for more than 76% of public issues. The issuance of such curatives is a viable opportunity for risk-bearing investors who wish to take greater risk r higher return. The risk-averse investors on the other hand would seek to invest on crudities like bonds issued by corporations and government, debentures, preference shares c. which would provide them fixed return over a period of time with very *little* on *their investment. The corporate bonds/debentures* of only four institutions viz. Sri *Ram Sugar M ills Ltd., Bottlers Nepal* Ltd., Himalayan Bank Ltd., and recently that of Nepal 'Investment market Ltd. have been issued in the capital market till date. Of these debentures, those of) Bottlers Nepal and Sri Ram Sugar Mills have already matured. This speaks for the need to raise the issuance of more viable risk-averse investment opportunities to cater for that theory of investors Vaidya and Parajuli, 2004: 88-89).

The serious weakness facing Nepal's stock market is the low participation of investors in curatives transaction. Majority of the investors participating in the exchange are from Katmandu valley. Since there is only one stock exchange in the country and it is located the capital, and there is no other alternative available, participation of the investors from side the valley is very low. A ray of hope has been aroused by the Tenth Five-year Plan lich targets to increase the investor participation in the securities transaction and to have minimum of 3% of total population investing in the share capital of the organized sector

Terries. For this the government has brought out the concept of regional exchange. But is worth noting that the concept of regional exchange was there also in the Ninth Five year Plan. As nothing noticeable was done towards this direction during the Ninth Plan period, doubts; re raised also at the possibility of implementing the program in the 10^{th} period. For investors who want to invest through the primary market, it is not so great a problem even if they art living far away from the stock exchange as they can easily apply for the shares through different financial institutions which have their offices scattered around the country. But in the real sense, this is not enough for the involvement of the people in the securities transaction and investment in share capital of the organized sector enterprises. It is important to facilitate the participation of such people in the secondary market as well (Bhattarai, 2003).

It is obvious that investors or general savers are main wheels of securities market to run. Both individual and institutional investors mean a lot to security market. But, in our context we lack the active institutional investors. Despite the lack of intuitional investors, think stock market in Nepal has good confidence of the general investors his is proved by the response that the public offering by some companies received during the recent past. The public has the interest and capacity to subscribe the shares in primary market. Shree investment Finance company Ltd., Janaki Finance Company, Gorkha Insurance, Sri Lanka Merchant Finance Limited, SBI (fight shares), Himalayan Bank (debenture), Everest Bank (Preference share) etc. were offered to the public and all of them were oversubscribed (Ghimire, 2002).

2.3.3 Review of Unpublished Masters' Degree Thesis

Study of Mr. Prasad Dangol

Mr. Prasad Dangol(2004) had conducted a study on "A study on Investors' perception in Nepalese Stock Market". The study had the following objectives:

- To examine the impact on the stock market as per the change of investors' perception.
- To examine whether investors' perception leads to growth of the stock market.
- In order to achieve the objective Mr. Dangol used the secondary data as well as primary data in the form of questionnaire. And the data collected has analyzed by

using the different test and ultimately following major findings has been detected which are as follows:

The interests of investors have been decreasing continuously towards to stock market. Regarding the revenue from the disposal of the stocks, 30.37% of individual and 55% of institutional investors reinvested on other shares/stocks. And the remaining individual investors invested on other sectors after selling their stocks such as bank deposits, business, Government bond and others. The remaining institutional investors invested on other sectors after selling their stocks such as bank deposit, invested on business and others.

The revenue dividends and capital gains from stocks were not also 100% reinvested on stocks. It was seen that 52.59% individual and 55% institutional investors' perceptions indicated that they did reinvest the dividends and capital gains in stock, 7.41% individual and 5% institutional investors indicated that their reinvestment depended on others situations. The remaining 40% of both types of investors indicated that they did not reinvest the dividend and capital gains in stock.

The fluctuation of the stock price is the cause of the investors' perception. Actually, changing perception of investors' continuously pushes the price of the stock up and down. From the one sample runs test it was found that banks, manufacturing and others sectors have a negative trend in response to their share price. Similarly finance and insurance sectors have a positive trend in response to their share price. In aggregate, it was found that the NEPSE index has a negative growth. It indicated that the perception of the investors' led the growth of the stock market.

Study of Mr. Badri Subedi

Mr. Badri Subedi(2003) had conducted a study on *"Investors Awareness in the securities Market in Nepal"*. The study had the following objectives:

- To examine the popularity of the securities among the general public.
- To find out whether the investors are adequately aware or not in the share trading.
- To trace out the investors attitude towards the share investment in comparison to investment in other sectors.

To achieve the objectives of this study, descriptive and analytical deign has been used. Some financial and statistical tools have been applied to examine facts and descriptive techniques have been adopted to evaluate awareness of investors in Nepalese security market and by analyzing following findings has been drawn out:

Out of the total investors 24.54 percent investors responded that there are better opportunities for investors in non-securities sectors while 75.46 percent responded here were better opportunities for Nepalese investors in securities sectors. Among these respondents, who chose securities market as better sector for investors, responded the banking, finance, insurance, manufacturing, hotel, trading and other factors are suitable for investment in ranking. Likewise, the respondents, who chose on-securities sector as better sector for investors respondent the bank fixed deposit, fixed asset, business venture and other sectors are suitable for investment in ranking. They specified the nursing home and educational institutes.

8.05 percent of the respondents said that they are satisfied with the present vaiability of the information about the securities while 81.95 percent of the respondents showed their dissatisfaction about the present situation of the availability of the adequate information.

Companies are found unable to meet the target level as described in the prospectus as 14 percent of the investors said that listed companies are able to meet the target as mentioned in their prospectus while 86 percent of them said that they are not able to meet the target as mentioned in the prospectus.

The regulatory activities of the regulatory authorities were found inefficient as 32 percent of the respondents responded that the regulatory activities are efficient while 68 percent of them opposed the response.

The status of grievances handling of the different institutions involved in share trading activities could not be considered satisfactory as 12.5 percent of the total respondents are found satisfied with the performance of the different institutions in handling the grievances of investors while 87.5 percent of them showed their dissatisfaction.

Most of the investors were found dissatisfied with the return they are presently getting from the stock investment as 23.61 percent of the total investors were found satisfied while 76.39 percent were found dissatisfied.

Friends and other sectors were found to be highly inspiring source to get the idea to invest in share while investors education programme and brokers were found to be less inspiring sources to make investment in shares.

The regulatory aspect of NEPSE is found at low to maintain the fair share trading activities as 29.17 percent of investors were found satisfied with the regulatory activities while 70.83 percent of them were found dissatisfied with the regulatory activities.

The dividend and capital appreciation were found most inspiring factors for investors to invest in shares while social status and participation in AGM were found less inspiring factors whereas marketability was found to be moderately considerable factors.

The level of investors awareness in the securities market was found at low and moderate level as responded by most of the investors while it is at very low and very high level as responded by very few investors.

The rumor and whim is found highly and moderately responsible in influencing the decision of the investors in share investment as responded by most of the investors whereas it is at low and very low responsible as per some of the investors.

Study of Mr. Santosh Upadhyaya

Mr. Santosh Upadhyaya(2004) has conducted a study on *"Investors Preference & Financial Instruments"*. The study has the following specific objectives:

- To study the preferences of the investors in the financial instrument.
- To assess investors' awareness regarding the investment decisions in selecting securities.
- To analyze the investment trend in the security market of Nepal.

Mr. Upadhyaya has used different research variable in the questionnaire and this has been tested through the statistical tools and finally he draw the following major findings:

The market capitalization of the different financial securities showed the common stock had the largest chunk of trading in the market. Hence, it can be said that Nepalese investors are trading common stocks. Likewise, the stocks of banking sectors had the largest chunk

of trading in the market, which proved that the preference of investors is on common stock of banking system.

The majority of the Nepalese investors preferred the equity share for investment; they preferred government securities after common stocks. The stocks and preferred stocks were least preferred.

The investors preferred the banking sector for investment.

The majority of the respondents stated that the investors do not make risk return analysis before making investment decision.

Nepalese investors' main objective of investment was profit.

It investors were not satisfied with their return from investment decision I securities as the respondents were asked whether they were satisfied or not on return from their investment decision in securities.

Major portion of the Investor were not aware regarding their investment in the Nepalese security market.

Major portion of the respondents stated that dividends/returns were the main influencing factors for preferences of investors.

The majority of the respondents of the different groups stated that the Nepalese investors were not getting sufficient and timely information from the companies. With respect to the rules and regulation of government, it was found that the existing rules and regulations were not sufficient to protect the investor’s investment in the security market.

Study of Mr. Santosh Upadhyaya

Bhatta (2001) conducted a study on the topic "Dynamic of Stock Market in Nepal". The main objectives of the study are to analyze the trend of Nepalese stock market. His study finds out that investors are interested to invest their resources in the shares of corporate sector. Hence it is necessary to develop the entrepreneurship and encourage the entrepreneurs to start the productive venture as soon as possible. Management capability of the entrepreneurs is a key for better performance of the firms. Government should launch programs to enhance management capability of the entrepreneurs, which may contribute to raise the return from the investment.

Development of manufacturing sector is the backbone of an economy, which in turn assists to foster banking, finance and insurance sectors. Unfortunately, the manufacturing sector does not have a good performance in Nepalese economy. Almost all firms in this sector

have sustained a loss. The secondary aspect of the stock market is also not functioning well in Nepal. There is almost no liquidity in the stock market for shares except that of banking and some finance and insurance sectors.

Although it has become late to take steps to overcome such problems of the Nepalese stock market in order to make it active and supportive, the stock market has good prospect for the resources mobilization to finance productive enterprises in Nepalese economy.

Study of Mr.S.K.Koirala

Koirala (2001) made a study regarding *"Government securities as internal debt of Nepal"*. For meeting the ever-widening budgetary deficit, government has to resort to internal borrowing. Internal public debt has been playing a significant role in the formation of financial resource for development expenditure as well as in the growth of money and capital market. It can be in the form of real and unreal borrowing. The unreal borrowing includes the government bonds and treasury bills held by Rastra Bank and Commercial Banks. The real borrowing includes the bonds and the treasury bills held by individual, groups and other institutions, and this can decrease the inflation since it reduces the purchasing power of the investors. Koirala states that the internal debt increased with an average annual growth rate of 13.3%.

The investors' interests were found to be affected by their occupation. The businessman, students and the retired persons are less interested to purchase the government securities but the civil servant and permanent employee of organized bodies are more interested to purchase the government securities. On the contrary, level of education found to be irrelevant factor. It does not affect to the interest towards the government securities. It means all level of people from the viewpoint of education is equally interested to purchase government securities. But, the background of education seems as an important factor. Those people whose academic background is economics, finance, management and commerce are more aware than the people with other background. Koirala, in his study states that higher income group people are less interested to purchase the government securities. The test regarding awareness resulted that the people from urban area are more aware than the people from rural area regarding government securities.

Koirala declares that the bonds and securities must be of different types so that they may suit the preference of people from the different segment of society, either rich or poor. Bonds can be varied in terms of interest rates, maturity and denominations. To attract people towards the government bonds, it is essential that some special bonds might be issued for development work with a particular locality. This will motivate other localities also. Maturities of bonds are recommended not to exceed 7 years, due to declining real value of assets because of increasing rate of inflation.

Study of Mr.S.K.Koirala

Paudel (2002) studied about the *"Government Securities Practices in Nepal"*. It finds out that the interest of investors on government security and their educational background is completely independent. Both the educated and uneducated people are equally interested on government securities. The study also draws the conclusion – both poor and rich people are interested to government securities. Those who are unable and unskilled to exploit market and start their own enterprises are investing in government securities; those who have studied the business related subjects are more aware of various categories of government securities; and people in rural area are less aware of the government securities.

In addition, Paudel states that T-bills are most welcomed security in comparison to other government securities. His study found that 50% of the respondents were aware of the government securities since few years ago only. 59.1% respondent told that they prefer government securities due to tax freeness and risk freeness. Large investors thought to invest idle cash in government securities and only few of them used loan in order to purchase the government securities.

Study of Mr.Ishwor Pahari

Pahari (2003) had conducted *"A study about the debt market in Nepal"*. He points out the fact that the government securities in terms of bonds and corporate securities in terms of equity are issuing and growing regularly since 1993. However other types of securities like preference shares and debentures are not growing properly. His study also looks towards inflation – the relationship between inflation rates with government borrowing is positive. Positive relationship was also found between government securities (national saving certificates and government bonds) are market interest rate. But market interest rate is adversely influence by T-bill rates.

Survey of investors made by Pahari shows that majority of respondent preferred common stocks for the investment. Government securities got the second priority and corporate debt securities got the third, whereas majority of respondents companies gave the first priority to the government debts. Majority of respondents were found willing to invest in banking sector debt securities. Pahari also found that majority of investors felt that the government securities should also be traded on NEPSE floor. Study finds that the government securities market is unsystematic. Nepalese investors were found to believe that 'common stocks are marketable than debentures' as a motive of issuing common stock in place of debentures, yet they also pointed that 'default in payment of interest and principal' also makes the debentures unattractive. Regarding foreign investors, Pahari asserts that the majority of respondents were in favor of welcoming the foreign investors. Respondents also agreed that the Nepalese debt securities market lacks adequate infrastructures and facilities; infrastructure indicated trading mechanism, rules and regulations, and credit rating agencies.

2.4 Research Gap

Many studies have been reviewed in the previous section but no researches have made study about the development of financial instruments in the Nepalese capital market. Prasad Dangol (2004)made a research about investors' perception in Nepalese stock market,Badri Subedi(2003) about investors awareness in the Nepalese securities market,Santosh Upadhyaya (2004) about preferences of Nepalese investors in selecting financial instruments, Bharat Prasad Bhatta (2001) made a research about dynamic of stock market in Nepal, S.K. Koirala (2001) about government securities as internal debt, Ram Prasad Poudel (2002) about government securities practices in Nepal and Ishwor Pahari (2003) about Nepalese debt market, All these materials found in different studies are of fragmented nature. Some of them are related to the investors' behavior, some with their psychology and some with their decisions. However, none of the study is directly related with the development of financial instruments in the Nepalese capital market. This shows a clear research gap about the study.

CHAPTER -III

RESEARCH METHODOLOGY

3.1 Introduction

Research and methodology is a systematic way to solve the research problem. In other words, research methodology describes the methods and process applied in the entire aspects of the study. Research methodology refers to the various sequential steps (along with a rational of each step) to be adopted by a researcher in studying a problem with certain objectives in view. Thus overall approach to the research is presented in this chapter .This chapter consists of research design, sample size and selection process, data collection procedure and data processing techniques and tools.

3.2 Research Design

Research design is a plan, structure and strategy of investigation conceived so as to obtain answer to research question and to control variances. It is a definite procedure and techniques which guides to the study and provide ways for research viability. This study describes and explores the development of financial instruments in Nepalese capital market .The current status of financial instruments is well explained with the proper analysis of past data .Therefore this is historical type of research design.

3.3 Population and Sample

The entire number of financial instruments available in the Nepalese capital market and the investors of such instruments are the population for the research study. Survey is conducted on different places like NEPSE floor, broker's offices, and several other places .Seven year data from the period of 2000/2001 - 2006/07 of four commercial banks and four finance companies were taken as a sample for the study of secondary data. Name of sampled companies selected for the study are listed below.

- Nepal Investment Bank Ltd.
- NABIL Bank Ltd.

- Himalayan Bank Ltd.
- Standard Chartered Bank Nepal Ltd.
- Goodwill Finance Company.
- Nepal Merchant Banking and Finance Company.
- Katmandu Finance Company
- People's Finance

3.4 Sources of Data

This research is based upon the secondary data for the historical performance assessment and the primary data for the qualitative assessment of information .The required data are collected from various secondary sources like SEBO/N reports, NEPSE reports, annual report of selected listed companies, economic survey published by Ministry of Finance and economic indicator published by NRB. Apart from this, primary data collection methods are used to know about the development of financial instruments in Nepalese capital market .Primary data in this research is received from filling the questionnaire.

Thus, both primary and secondary sources are used for the data collection. The study heavily depends upon the secondary sources of data.

3.5 Data Collection Techniques

To collect the primary data, questionnaire survey has been done along with some interview and observations .Structured questionnaires are used in this regard and some unstructured interviews are also taken as per necessity the queries related to the failure and success of securities, weakness existed in the primary and secondary markets have been asked. Questionnaires were distributed to those individuals who have a knowledge and experience about capital market. A survey was conducted on the floor of different commercial banks and broker's office within a period of three days. Participants of the questionnaire survey are the staffs and clients of the banks who were available during survey period. Similarly, discussions, interviews and informal talks were also held with investors, brokers and analysts to know much about their psychology.

As for secondary data collection , different reports ,bulletins ,journals, articles and other publications published by relevant sources like NRB, NEPSE , SEBO/N etc are used along with the annual reports of sampled institutes.

3.6 Data Processing and Analysis Techniques

Analysis is the systematic and careful examination of available fact so that certain conclusions can be drawn and inferences are made .For the purpose of processing and analysis of the data; different relevant statistical tools and computer software programme(SPSS) is used. The study has used the mix of statistical tools from simple percentage analysis to the hypothesis testing tools as per the requirements and their suitability. The statistical tools that are applied in this study are:

a. Arithmetic Mean: Arithmetic mean of a given set of observations is their sum divided by the number of observations. In such a case all the items are equally important. Simple arithmetic mean is used in this study as per the necessity for analysis.

$$\text{Mean}(\bar{x})\ X\frac{X}{N}$$

Where,

∑X= sum of all values of the variable ″X″

N= number of observations

X= variables involved

b. Standard Deviation: The standard deviation usually denoted by the letter sigma (ō). Karl Pearson suffused it as a widely used measure of desperation and is defined as the positive square root of the arithmetic mean of the squares of the deviation of the give observations from their arithmetic mean of a set of value. It is also known as root mean square deviation. Standard deviation, in this study, has been used to measure the degree of fluctuation of problems to invest in securities and that of other variables as per the necessity of the analysis.

$$\text{Standard Deviation } (\pm)\ X\frac{(X-\bar{X})^2}{N}$$

c. Percentage Analysis

The percentage analysis is done to compare the two or more data from general information .It is used as a method to divide the opinions of related sectors into two or more sectors.

d. Chi-square test χ^2

Chi- square has been used to check whether there is any association between two independent variables as well as to check the uniform distribution of variables. It is calculated as:

$$¡^2 X \sum_{iXl}^{r} \sum_{jXl}^{c} \frac{(o_{ij} Z E_{ij})^2}{E_{ij}}$$

Where,

$¡^2$ = Chi-square statistic

r = Number of rows

c = Number of columns

O_{ij}= Observed number of categorized in the i^{th} row of the j^{th} column

E_{ij} = Number of case expected in the i^{th} row of the j^{th} column = $E_{ij} = \frac{RiCj}{N}$

e. Subscription Ratio

Subscription Ratio is calculated to see the subscription scenario in the primary issues. Basically this tool has been used to see sector-wise subscriptions to find out which sector has better subscription.

$$\text{Subscription ratio } X \frac{\text{Number of shares applied}}{\text{Number of shares issued}}$$

f. Growth Rates

Growth Rates are used to see how the investment on government securities and common stocks are growing in commercial banks and finance companies. This helps to reflect the investments made on different financial instruments available in the Nepalese capital market.

$$\text{Growth rates } X\frac{V_1 - V_0}{V_0} x100$$

g. T-test for Significance of Correlation Coefficient:

T-distribution is commonly called student's t-distribution and is used when the sample size is less than 30, given a random sample from a bi vitiate normal population. When hypothesis is tested that the correlation coefficient of the population is zero, i.e. the variables in population are uncorrelated, the following t-test is applied; which is applied in this study.

If the calculated value of t' exceeds $t_{0.05}$ for (n-2) d.f.; we say that the values of 'r' is significant at 5% level. If 't' $<t_{0.05}$ the data are consistent with the hypothesis of an uncorrelated population.

i. Variables

Variables are the characteristics of persons, things, groups', programmes etc. A variable is thus a symbol to which numbers or values are assigned. Small size of market ,poor corporate results, poor regulatory infrastructure, low level of investor's knowledge in security market, poor performance of national economy are the variables of this study.

Graphs

Pie charts are used to show the sector wise coverage in total trading volumes.

Line chart are used to show the trend of issues of instruments.

CHAPTER-IV

DATA PRESENTATION AND ANALYSIS

This chapter puts forward the analysis of secondary data primary data along with their results and interpretations. This chapter starts with the analysis of secondary data concerned with the issuance of financial instruments, subscription ratios, trading volume, NEPSE Index, citizen investment scheme, and institutional investor, followed by the analysis of primary data collected through questionnaire survey. Several relevant tools and tests have been used for analysis of primary statistics.

4.1 Development of Nepalese Capital Market

Although the history of financial instruments in Nepal begins with the issue made by Biratnagar Jute Mills, it got further development only after the restoration of democracy and Liberalization policy. Between 1984 and 1990, 42 companies were listed, out of which more than 25 companies had some form of government ownership. Government's privatization policy also enabled new industrial companies to enter the stock market. Of the total public issues approved in 1994 and 1995, 28.4%was issues of privatized companies. The growth of the stock market has mainly been due to the liberalization and the resulting growth of the financial sector (commercial banks and finance companies) rather than that of the industrial sector.

Stock market in Nepal has been growing gradually both in terms of turnover as well as the capital investment. In the F/Y 2006/07, 44 companies have listed their securities amounting to Rs.3794.65 million in NEPSE. The securities listed consists of ordinary shares, right shares, bonus shares and debentures of the 44 companies listing securities in NEPSE, 10 are new companies. At the end of this F/Y, number of listed companies in NEPSE reached 144.

Table 4.1

Listed companies by the end of the F/Y 2006/07

S.N.	Sector	No. of Listed Company	Paid up Value (Rs. in Million)	Trading (Rs. in Million)	Market Capitalization Value (Rs. in Million)
1.	Commercial Banks	15	8522.73	2696.28	68694.36
2.	Development Banks	22	816.91	82.76	1577.45
3.	Finance Company	55	2564.81	305.85	5000.04
4.	Insurance Company	16	1256.70	129.90	4952.19
5	Hotel	4	1552.88	19.77	2344.21
6	Manufacturing and Processing Company	21	2756.96	17.19	5472.11
7	Trading Company	5	76.64	15.80	764.44
8	Other Company	6	2460.92	183.88	8008.94
	Total	**144**	**20008.55**	**3451.43**	**96813.74**

Source: SEBO Annual Report, 2006/07

Out of 144 listed companies, NEPSE classified 56 companies (38.4 percent) consisting of 11 commercial banks development banks,27 finance companies, 10 insurance companies and 1 manufacturing and processing company under group "A" and the rest under group "B", as per the provision of securities Listing Bye-laws,1996".As per the provision of this bye laws those listed companies which have profit track record for the last three years, book value higher than paid up value, submitted its financial statement to NEPSE within six months after the expiry of F/Y, paid up capital exceeding Rs.20 million , have at least 1000 general Shareholders falls on Category "A". The Current Figures, as per the SEBO Annual Report 2006/07, show that the total amount of Securities traded in this F/Y is RS. 3451.43 million and the total paid up value of the listed securities reached Rs.20008.55 at the end of this F/Y. In the last F/Y, total amount of securities traded was Rs.4507.68 million and the paid up value of the listed securities was 16771.85 million .By the end of this F/Y the market capitalization value of the listed securities reached to Rs.96813.74 million. In the last F/Y, this value was Rs.61365.89 million. During this year, the highest value of market capitalization was Rs.96813.74 million and the lowest was Rs. 61630.90

million. The percentage contribution of market capitalization on GDP is estimated to be 17.35

NEPSE Index

By the end of this fiscal year 2006/07, the price index of the listed securities (NEPSE Index) remained at 386.83 points, which is 100.16 points higher than that of the last Fiscal years' index 286.67 points. In this fiscal year, the highest index of 388.49 was noted on May 15, 2007 and the lowest index of 287.90 points was noted on June 17, 2007. The ups and downs in the NEPSE index during this fiscal year are shown in the table below

Table 4.2

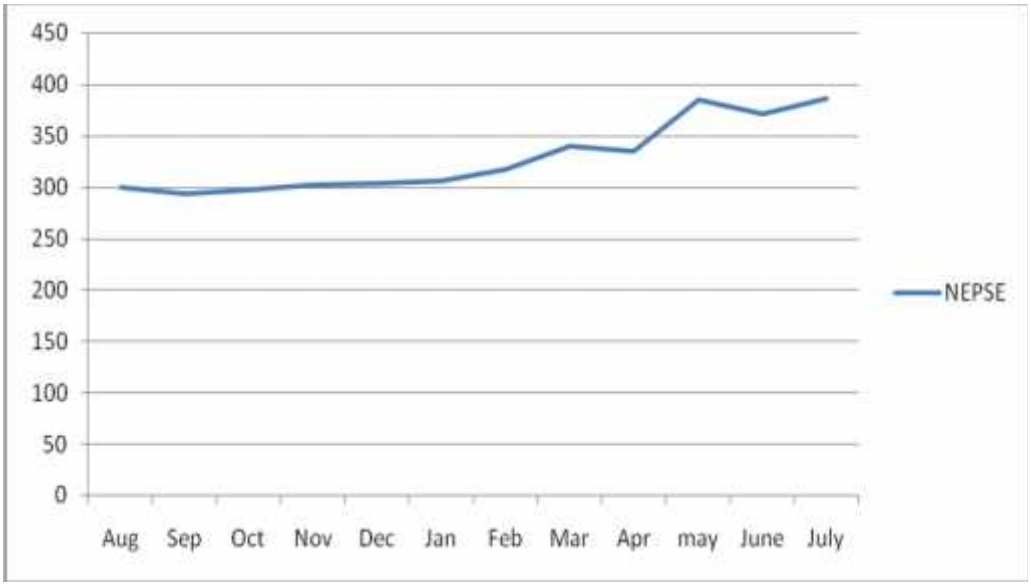
NEPSE Index for the F/Y 2006/07

Month	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	may	June	July
NEPSE Index	300.05	293.35	297.34	302.39	303.12	305.50	317.79	339.79	334.77	385.89	372.01	386.83

Source: SEBO Journal, Volume III

Figure 4.1

NEPSE Index for the F/Y 2006/07



4.1.1 Scenario of Nepalese Financial Market

4.1.1.1 Primary Market Scenario

Table 4.3

Trend of Primary Market

(Rs. In million)

S.N	**Headings**	**Fiscal year**						
		2000/01	**2001/02**	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2006/07**
1	Issue Approval	630.3	493.4	1579.9	696.6	1090.4	1672.3	2443.3
	a. ordinary shares	412.5	278.7	319.5	394.3	657.5	377.5	579.8
	b.Right Shares	124.6	131.8	621.9	162.2	70.0	949.3	1013.5
	c.Preferential shares	-	-	140.0	-	-	-	-
	d.Debentures	-	-	360.0	-	300.0	300.0	850.0
	e.Mutual fund	-	-	-	100.0	-	-	-
	f.Units	93.2	82.9	138.5	40.1	62.9	45.5	142.9
2.	Number of companies Making public issues	9	9	12	18	14	14	34

Source: Economic survey 2006/07

The government and public limited companies issue securities. General public, profit and non-profit organizations are the buyers/investors of securities and finance companies licensed to carry out merchant banking activities in Nepal. Development of primary market in Nepal started after the establishment of securities Exchange Centre in 1976. Despite some positive indications, the primary market is still in infancy stage. The type of securities issued, and the volume of issue is still insignificant (Shrestha et al., 2003:29-30)

In FY 2006/07, 34 corporate entities have been authorized to mobilize capital from the primary stock market for a total amount of Rs 2443.3 million by issuing stock of ordinary and preferential shares and debentures. Such authorized amount was higher by 46.10 percent compared to the same period of FY 2005/06. In the same period of previous fiscal year, there were 14 such entities authorized to mobilize capital of Rs 1672.3 million through ordinary and preferential shares and mutual fund.

4.1.1.2 Secondary Market Scenario

Table 4.4

Trend of Secondary Market

(Rs. In million)

	Fiscal Year						
Headings	**2000/01**	**2001/02**	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2000/01**
Value of shares traded	1157.0	2344.2	1540.6	575.8	2144.3	4507.7	34541.4
No of shares transacted "000"	7674	4989	6005	2428	6468	18434	12221.93
Transactions(No.)	29136	46095	42028	69163	85533	106246	97374
Market capitalization	43123.3	46349.4	34703.8	35240.4	41424.8	61365.9	96813.7
Traded value as a percent of market capitalization	2.68	5.06	4.44	1.63	5.18	7.34	3.56
Market capitalization as a percent of GDP	11.77	10.50	7.55	7.16	7.72	10.41	14.98 #
Paid- up value of listed stocks	7347.4	8165.2	229685.0	12560.00	13404.9	16771.9	20008.6
No. of listed entities	110	115	96*	108	114	125	135
No. of transacted companies	69	67	69	81	92	102	110
NEPSE Index (point)	360.7	348.40	227.50	204.86	222.04	283.67	386.86

Percentage computed on the basis of estimated GDP

*25 companies deleted

Source: Economic Survey, 2006/07

The role of secondary market is more in focus than that of primary market in securities market. It is mainly due to the fact that secondary market provides liquidity to the securities and ensures continuous price formation. The continuous price formation process reduces sudden jump in the price of the securities in the market. NEPSE is the only organized exchange to carry out secondary market operation of corporate securities in Nepal (Shrestha et al., 2003:30-31).

In the fiscal year 2006/07, number of such listed in the stock exchange has totaled 135.The number of such listed entities was 125 during the corresponding period of FY 2005/06. In the review period of FY 2006/07, market capitalization increased by 57.76% and reached to Rs 9681.37 million compared to 61366.59 million during the corresponding period of FY 2005/06.

Cash transaction in the NEPSE during the review period of FY 2006/07 decreased by 21.43 percent totaling Rs 3451.4 million with 12.22 million shares in comparison to 18.43 million shares worth Rs 4507.7 million transferred during the same period of FY 2005/06. Number of transactions decreased by 8.35% in the fiscal year 2006/07 to total 97374 as compared to 106246 transactions in the corresponding period of the previous fiscal year.

NEPSE index increased by 100.19 percent point from 286.67 point to 386.86 points in the FY 2006/07 compared to the same period of FY 2005/06.

4.1.2 Primary Subscription of Securities

As per the provision of securities legislation, a company should issue its securities to the public within two months after getting issue approval from SEBO. During the period of last seven years (2000/2001-2006/07, total 102 companies issue their securities to the public amounting to Rs 6206 million, among which 48 are finance companies and 13 are commercial banks. (Details are presented in Appendix no.2)

From the analysis, it is found that the number of issuing finance companies is greater than the issuing commercial banks. But, the issues made by commercial banks are highly oversubscribed in the primary market. This shows that investors want to make investment in commercial banks rather than finance companies. Most of the securities issued by manufacturing and processing companies are found to be under-subscribed

In this F/Y 2006/07,18 companies consisting of 5 commercial banks, 4 development banks, 7 finance companies and 1 other company issue their securities to the public amounting to Rs 2443.28 million. In the last F/Y, 14 companies had issued securities amounting to Rs.1476.82 million. This shows that the issue of securities to the public follows the

increasing trend. Total amount of securities issued to the public in a last 7 years is shown in a table below:

Table 4.5

Issue of Securities to the Public

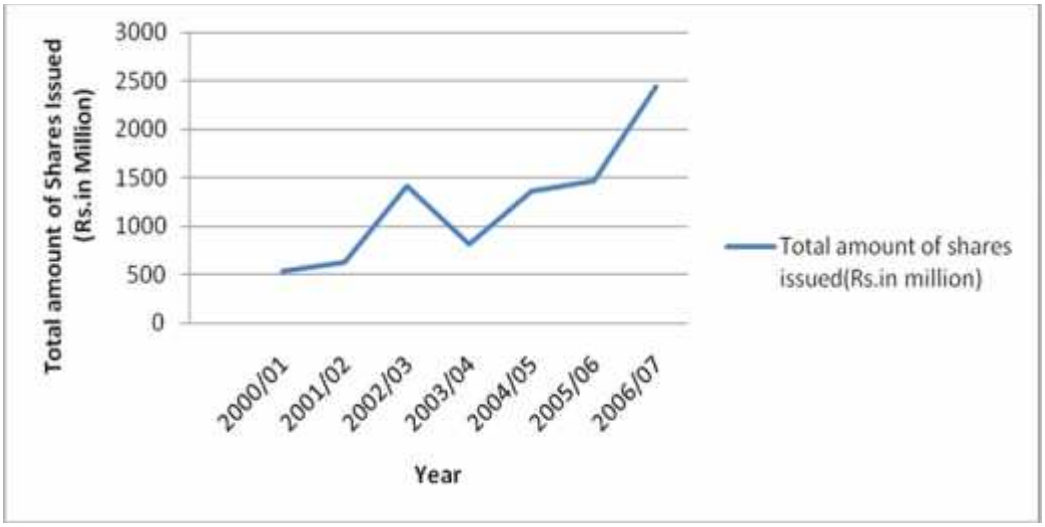
Year	Total No. of shares issued	Total amount of shares issued (Rs.in million)
2000/01	5370600	537.06
2001/02	6342900	634.29
2002/03	14166500	1416.65
2003/04	8137400	813.74
2004/05	13634245	1363.4245
2005/06	14768200	1476.82
2006/07	2443280	2443.28
Total	**62419845**	**62419.845**

Source: SEBO/N Annual Report (For the period of 2000/01-2006/07)

The above table can be clearly explained with the help of trend line below. It shows that the issue of securities to the issue of securities to the public follows the increasing trend except in the F/Y 2003/04. This depicts that public are slowly being attracted towards the securities, and due to the changing scenario of the economy, there is still a hope of increasing this trend.

Figure 4.2

Securities Issued to he Public in a Last Seven Years



4.1.3 Trading Volumes

During the course of our study, we have also analyzed the sector-wise trading volumes of different financial instruments in the NEPSE floor. The trading volumes of different securities by the different investment sectors are presented in the table below:

Table 4.6

Trading Volume of Securities on the Basis of Investment Sectors

Amount of Trading Volumes

Year	Commercial banks	Development banks	Insurance	Finance	Mfg.& Processing	Hotels	Trading	Others	Total
2000/01	877.65	0.00	82.22	60.95	73.83	26.72	12.20	23.21	1156.7
2001/02	1922.28	0.00	38.64	254.61	67.19	22.34	4.46	26.39	2335.9
2002/03	1151.35	23.54	28.45	70.60	21.44	138.44	4.25	2.56	1540.6
2003/04	332.51	25.90	64.59	129.69	4.00	6.80	11.84	0.66	575.9
2004/05	863.41	32.33	36.86	165.09	1031.62	2.84	11.83	0.29	2144.2
2005/06	4021.83	22.01	67.62	216.37	114.90	4.48	7.99	52.48	4507.6
2006/07	2696.28	82.76	129.90	305.85	17.19	19.77	15.80	183.88	3451.43
Total	**11865.31**	**186.54**	**448.28**	**1303.16**	**1330.17**	**221.39**	**68.37**	**289.47**	
Percentage (Amount)									
2000/01	75.87	0.00	7.11	5.27	6.38	2.31	1.05	2.01	100.00
2001/02	82.29	0.00	1.65	10.90	2.88	0.96	0.19	1.13	100.00
2002/03	74.73	1.53	1.85	11.07	1.39	8.99	0.28	0.17	100.00
2003/04	57.73	4.50	11.21	22.52	0.69	1.18	2.06	0.11	100.00
2004/05	40.20	1.50	1.70	7.70	48.10	0.10	0.50	0.00	99.8
2005/06	89.20	0.40	1.50	4.80	2.30	0.20	0.10	1.10	99.6
2006/07	78.12	2.40	8.86	3.76	0.57	0.50	0.46	5.33	100
Total	**498.14**	**10.33**	**26.77**	**66.02**	**62.31**	**14.24**	**4.64**	**9.85**	

Source: SEBO/N Annual Report (For the period of 2000/01-2006/07)

Table No.4.6 depicts that the commercial banks covers the greater percentage of trading activities than other sectors. During a period of last seven years, commercial bank alone makes a transaction amounting to Rs. 11865.31 million. Coverage of commercial bank is

always more than 40% in total trading volumes. Due to sudden increase in the trading volume of manufacturing and processing company in a F/Y 2004/05, it takes place a second position. In this period, it covered around 48% of total volume. A year ago it was just 0.69% but with a gradual increment, it reached to 48%. The trading of financial companies was also used to be good till 2003/04 with 22.52% of total trading volume in that period. But, from the F/Y 2004/05 onwards, the trading volume of finance companies and insurance companies had fallen tremendously. Development bank as a separate sector has got its existence only from F/Y 2002/03 and its trading volume is growing in a good pace. The trading of hotels has trembled very much in FY 2004/05.Manufacturing and processing companies are also not doing well; their share in total trading volume is reducing.

4.1.4 Assessment of Disclosure Standards in Nepalese Stock Market

The tenth plan document (2002-2007) of HMG/N has clearly stated that the government is committed to create opportunity for number of people to reap benefits from the return obtained by directing investment in income generating portfolio of assests. This objective can be fulfilled only by the rational and accountable behavior focused towards the compliance of the disclosure standards by the key players in the capital market. Disclosure standard implies to any kind of reliable information disclosed to the users of information especially to shareholders and other interested investors. This helps to understand the performance of companies that affect the capital market as a result of primary and secondary market activities. The act of disclosing helps the public to have rational judgment through the process of analysis and evaluation of performance necessary for making decisions.

Whatever the fund raised from the public needs to be expended in accordance with legitimate authority. If not, any illegality and inadequacies in a system of management and accounting disclosure standards can undermine the public confidence that ultimately affects the stock market in one way or the other. In our country, despite continuous efforts to improve the quality and contents of disclosure standards, many inconsistencies still exist due to restraint and reluctant attitude of management towards adequate disclosure of information to the public. The presentation, quality and contents of the disclosure are still not proving satisfactory to win the confidence of investing public.

Table 4.7

Table Showing Compliance of Disclosure

Fiscal Year	Listed Companies	Companies Submitting Annual Report	Disclosure Status (%)
1999/00	110	61	55.46
2000/01	115	67	58.26
2001/02	96	68	70.83
2002/03	108	66	61.11
2003/04	114	71	62.28
2004/05	125	86	68.80
2005/06	135	95	70.37
2006/07	144	97	76.22

Source: SEBO/N Annual Report (For the period of 2000/01-2006/07)

The seven years data reveals that the listed companies increased from 110 in 2000/01 to 144 during 2006/07 but due to de-listing it decreased to 96 in 2001/02 .The compliance of disclosure is 70.83% of listed companies and in some years it had dropped to 55.46%. For the F/Y 2006/07, 95 companies out of 135 submitted their annual reports to the board .These companies consist of 14 commercial banks, 5 development banks, 43 finance companies, 10 insurance companies' hotels, 12 manufacturing and processing companies trading companies and 2 other company. However, taking disclosure status of the listed companies finance companies top the list since more than 93% of finance companies submit the annual report timely to the concerned authorities , then followed by commercial banks providing disclosure varying from 83% to 90% . Insurance companies come under third ranking of the disclosure status from 72% to 82%.Hotels and others provide disclosure from 50% to 80% and among all trading sector has the lowest disclosure status from 18% to 30%.

4.2 Analysis of Investment Alternatives

4.2.1 Corporate Securities

Table 4.8

Issue of Corporate Securities

Fiscal year	Ordinary shares	Right Shares	Common Stock*	Preference Shares	Debenture	Mutual Fund/Unit Scheme	Total
2000/01	412.46	124.6	537.06	0	0	93.25	630.31
2001/02	118.5	365.79	484.29	0	0	82.91	567.2
2002/03	378.76	387.87	766.63	140	360	138.48	1405.11
2003/04	551.5	162.24	713.74	0	0	140.09	853.83
2004/05	755	429.92	1184.92	0	300	62.28	1547.2
2005/06	300.89	669.42	970.31	0	300	45..49	1315.8
2006/07	579.83	1013.45	1593.28	0	850	60.4	4096.96
Total	3096.94	3153.29	6250.23	220	1810	622.81	8903.04
Percentage	34.78%	35.42%	70.20%	2.87%	20.33%	7%	100%
Rank			1	4	2	3	

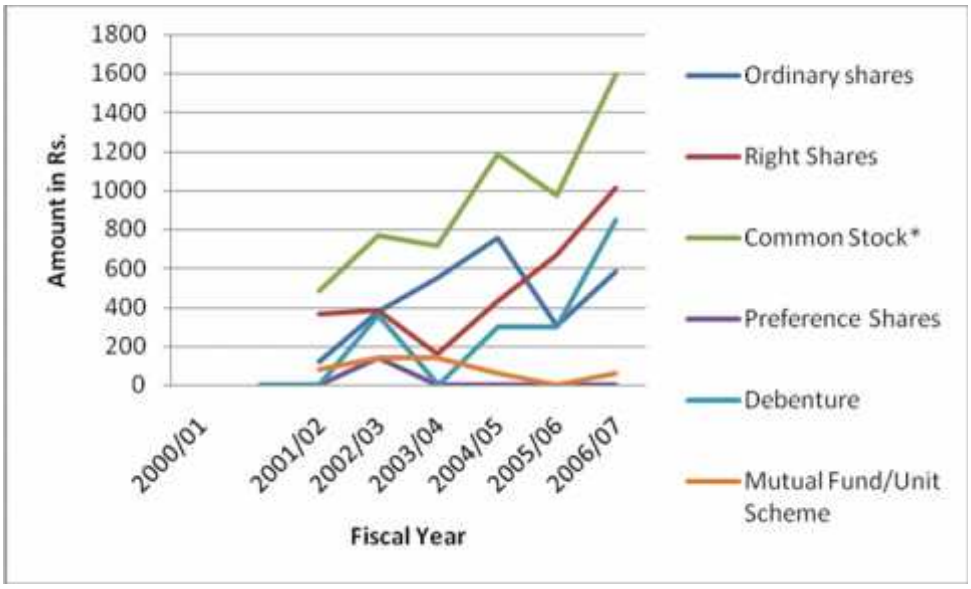
*It includes both ordinary share and right share

Source: SEBO/N Annual Report 2006/07

The table 4.8 shows the amount of different corporate securities that are issued in different time periods (from fiscal year 2000/01-2006/07) in Nepalese capital market. The total amount figures to Rs. 8903.04 millions during this time period of 7 years. It shows that the common stock dominate the total market. Right shares have the largest share in the total market i.e. 35.42%, and then come ordinary shares, debentures, mutual funds and preference share. These instruments are ranked in terms of their coverage in total amount of public issue. The above trend shows that the issue of debentures and mutual funds slowly emerge from 2000/01 in the market but preference share is still not that very popular in the Nepalese capital market

Figure 4.3

Trend of Corporate Issues



The above line shows the trends of issues of corporate securities in the capital market of Nepal since 2000/01.Only a line representing common stock follows an increasing trend, whereas others have very ups and downs as frequently reach the zero limits.

On this basis, we can conclude that common stocks are the most widely used corporate security. Similarly, preference share is a least used financial instrument in the Nepalese financial market. It means that capital market of Nepal is heavily dependent upon the equity instruments. Financing from other instruments is still very small compared to equity instruments. Issuance of just four types of securities reveals that our capital market t is really very poor on the matter of varieties of corporate securities. Nepalese capital market is fully dependent upon these traditional types of securities. Financial or securities innovation is lacking in Nepal's capital market.

4.2.2 Government Securities

Table 4.9

Issue of Government Securities

(Rs.in million)

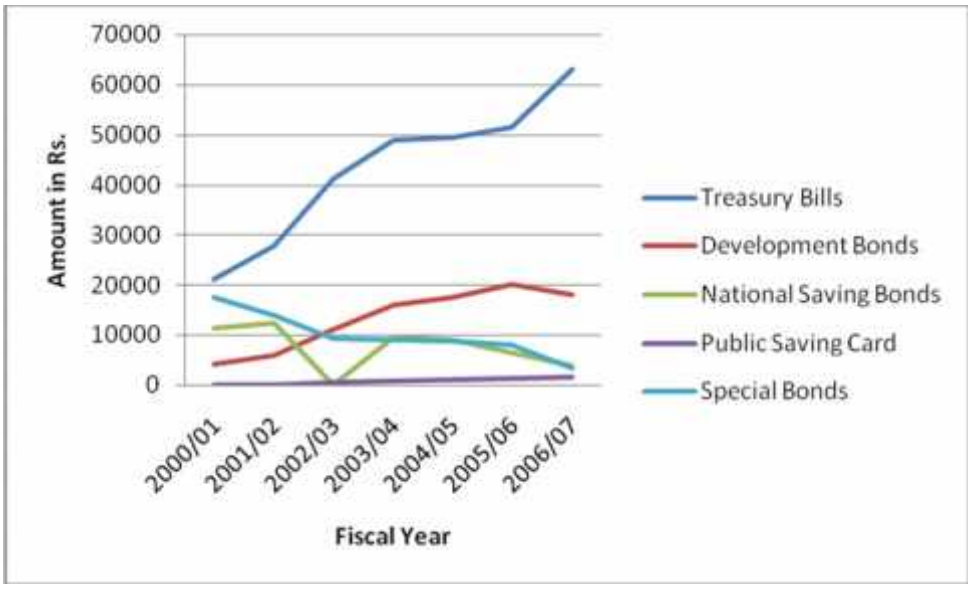
Fiscal year	Treasury Bills	Development Bonds	National Saving Bonds	Public Saving Card	Special Bonds	Total
2000/01	21026.90	4262.20	11526.50	0.00	17541.40	54357
2001/02	27610.80	5962.30	12476.40	0.00	13994.30	60043.80
2002/03	41106.50	11090.70	11536+.10	628.10	9259.30	73620.70
2003/04	48860.70	16059.20	9629.80	931.10	9164.50	84645.30
2004/05	49429.60	17549.20	9029.80	1178.90	8946.20	86133.70
2005/06	51383.10	19999.20	6576.80	1428.90	8176.30	87564.30
2006/07	62970.3	17959.2	3876.8	1678.9	3469.8	89954.9
Total	**302387.9**	**92882**	**64652.2**	**5845.9**	**70551.8**	**536319.7**
Percentage	**56.38%**	**17.31%**	**12.05%**	**1.09%**	**13.15%**	**100%**
Rank	**1**	**2**	**4**	**5**	**3**	

Source:NRB Quarterly Economic Bulletin, Mid July 2007 and Economic Survey,2006/07

If we see the scenario of government securities, treasury bills are widely issued during the period of last seven years with the coverage of 56.38% out of total government securities issued. Similarly, special bonds, national saving bonds and development bonds are also issued to some extent by the government which covers 13.15%, 12.05% and 17.31%. The table shows that public saving cards were issued for the first time in 2002. Though its contribution in total amount is very little i.e. 1.09%, its use is increasing tremendously.

Figure 4.4

Trend of Government Issues



The above line chart displays the trends of issuance of various government securities. In the figure, we can see that the Treasury bill is the only instrument which follows the rapid increasing trend. Development bonds are also growing, but in a very slow pace. Special bonds and national saving bonds start following decreasing trend since 2000/2001 and 2006/07. Public saving card's line is in very low level. From the above figure, we can conclude that Treasury bills are most widely used government securities and the public saving cards are newly introduced instruments-bills are mostly used by institutional investors as it helps them to increase their liquidity.

4.2.3 Collective Investment Scheme

4.2.3.1 Citizen Unit Scheme

SEBO had permitted Citizen Investment Trust (CIT) to operate the Citizen Unit Scheme in the F/Y 1994/95. The objective of the scheme is to collect capital from the small and medium savers to make investment in a professional and efficient way and distribute the returns earned thereon .This is an open-ended scheme with the face value of Rs. 100 per unit. CIT itself has been performing the function of selling and repurchasing the unit of the scheme. It has been regularly reporting SEBO on the performance of the scheme. The performance of Citizen Unit Scheme in a last seven years is shown in a table below:

Table 4.10

Performance of Citizen Unit Scheme

(Rs. in Million)

S.N	Particulars	Fiscal year						
		2000/01	**2001/02**	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2006/07**
1.	Total amount of units sold	187.37	336.78	645.26	837.47	1003.87	1215.62	1486.34
2.	Total amount of units repurchased	44.12	110.63	280.62	432.15	536.27	702.53	829.01
3.	Investment	143.88	236.40	371.50	414.43	447.54	531.40	645.14
	a)Government Bond	30.85	59.65	119.50	188.00	186.50	176.00	169.80
	b)Bank Deposit(Fixed)	68.50	100.00	130.00	96.50	125.00	108.00	310.00
	c)Share/Debenture	2.03	6.75	10.05	15.43	19.53	31.40	28.34
	d)Loan & advances	42.50	70.00	111.50	114.50	116.50	216.00	137.00
4.	Net Income	16.71	19.98	35.26	37.40	36.44	42.12	50.31
5.	Dividends (%)	11	9	8.5	8	7	7	7
6.	Number of unit holders	4601	6270	8299	9087	9871	10813	2840

Source: SEBO Annual Report

As reported by CIT, by the end of the F/Y 2006/07, it sold units amounting to Rs.1486.34 million and repurchased the units amounting to Rs. 829.01 million. By the end of this F/Y, its total investment is Rs .645.14 million and the profit of the scheme in this F/Y is Rs.50.31 million. This profit increases at the rate of 19.44 %in compare to last fiscal year. The total number of participants of the scheme reached to 2840, which increases by 9.54% from last year this shows that people are being attracted to the scheme. It distributed 7% dividend to its unit holders during this period.

4.2.3.2 NCM Mutual Fund, 2059

SEBO approved for the operation of NMC mutual Fund, 2003/04. The total amount of the mutual fund is Rs.100.00 million. It is an Close ended fund and its maturity period is 10 years. Each units of the fund has a par value of Rs.10. the scheme is listed in

the NEPSE.NIDC capital Markets Ltd.is the fund manager of this scheme and Nepal Industrial Development Corporation is the trustee .

As reported by the NIDC Capital Markets – the fund manager, total investment fund reached to Rs.210.71 million by the end of this F/Y and the net assests value reached to 189.14 million. The performance of the fund in the last three years is given in the table below.

Table 4.11

Performance of the NCM Mutual Fund

S.N	Particulars	Fiscal year			
		2003/04	**2004/05**	**2005/06**	**2006/07**
1.	Investment	110.32	123.41	156.49	210.71
	a) Shares and debentures	84.43	95.88	127.95	183.53
	b) Government Bonds	10.00	10.00	10.00	10.00
	c) Bank(Special Deposit)	15.89	8.83	18.54	13.68
2.	Net Income	2.14	9.50	9.19	13.89
	a)Dividend in shares	1.62	2.16	1.82	2.82
	b)Interest in Government Bonds and Debentures	0.03	0.77	0.69	0.81
	c)Bank Interest	0.49	0.61	0.34	0.54
	d)Income from sale of shares	-	5.96	6.34	9.71
3.	Net Assets Value	105.69	118.02	144.93	189.14
4.	Outstanding Units (Units in '000')	10,000	10,000	10,000	10,000
5.	Net Assests Value per unit	10.57	11.80	14.49	18.91
6.	Number of unit holder	2882	2882	2559	2481
	a)Institutional	9	19	20	20
	b)Individual	2863	2863	2539	2461
7.	Dividend (%)	5	5	5	6-7%

Source: Annual Report of SEBO

4.2.4 Investment Made by Different Financial Institutions

Study has explored the institutional investment made by different commercial banks and finance companies towards corporate securities and government securities.

4.2.4.1 Investment of Commercial Banks in Government and Corporate Securities

Table 4.12

Table Showing Total Investment of Commercial Banks

(Rs. in million)

	Fiscal Year							
	2000/01	**2001/02**	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2006/07**	**Average growth rate**
Investment in government securities								
Nepal Investment Bank	0.00	300.00	224.40	400.00	2001.10	1948.50	2522.3	99.46%
NABIL Bank Ltd.	1233.82	2732.96	4120.29	3588.77	3672.63	2413.94	2301.46	20.46%
Standard chartered Bank	3338.67	4811.01	5784.72	6722.83	7948.22	7203.07	8635.87	18.21%
Himalayan Bank Ltd.	2112.88	2224.3	3047.75	3998.87	3431.73	5469.73	5144.3	18.79%
Total	**6685.37**	**10068.27**	**13177.16**	**14710.47**	**17053.59**	**17035.24**	**18603.93**	**11719.14**
Average	**1671.34**	**2517.06**	**3294.29**	**3677.61**	**4263.39**	**4258.81**	**4650.98**	**3476.21**
Growth Rate		**50.60%**	**30.87%**	**11.63%**	**15.92%**	**-0.10%**	**9.20%**	**19.68%**
Investment in Corporate securities								
Nepal Investment Bank Ltd.	12.69	12.69	13.89	13.89	13.89	17.74	17.74	6.19%
NABIL Bank Ltd.	16.12	18.82	22.22	22.22	22.22	440.28	104.19	306.74%
Standard Chartered Bank Ltd.	11019	11.19	11.19	11.19	11.19	13.35	15.3	5.65%
Himalayan Bank Ltd.	9.46	10.69	34.27	34.27	34.27	39.91	39.90	41.61%
Total	**49.49**	**53.39**	**81.57**	**81.57**	**81.57**	**511.28**	**177.13**	**148**
Average	**12.37**	**13.34**	**20.39**	**20.39**	**20.39**	**127.82**	**44.28**	**36.99**
Growth Rate		**7.84%**	**52.84%**	**0%**	**0%**	**526.87%**	**65.35%**	**87.03%**

Source: Annual Report of Sample Banks

Table No. 4.11 depicts the total investments made by different commercials bank (samples taken) in government securities and corporate securities, average of them, growth rates along with the average growth rates of individual banks during a period of 2000/01 to 2006/07. During this period, average amount of investments made on government securities is Rs. 3476.21 million whereas average investment made in corporate securities is Rs. 36.99 million. This obviously shows the huge investment is made towards government than corporate securities. But, considering the growth rate, average growth rate of investment in corporate securities (87.03%) is higher than that of investment in government securities (19.68 %). This may be because of tremendous increase in investment towards corporate securities during this fiscal year, 2006/07. In this fiscal year, investment in corporate securities is haphazardly increases by 526.51 %. This shows that the banking sectors are increasing their investment towards corporate securities.

If we see individually, average growth rate of investment in government securities is greater than investment in corporate securities in case of two sample banks (Nepal Investment Bank, Standard chartered Bank. But, in case of NABIL Bank and Himalayan Bank average growth rate of investment in corporate securities is greater in Government securities (Details of calculation are presented in Appendix No.3)

4.2.4.2 Investment of Finance companies in Government securities and corporate securities

Table 4.13

Table Showing Total Investment of Finance Companies

(Rs. in million)

	2000/01	**2001/02**	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2006/07**	Average growth rate
Investment in Government securities								
Goodwill Finance Co Ltd.	27.64	37.70	41.82	46.5	25.95	35.48	25.6	3.86%
Nepal Merchant Banking and Finance co Ltd.	208.39	208.39	320.19	449.3	724.15	487.88	440.83	18.81%
Katmandu Finance Co Ltd.	4.90	4.90	1.75	1.75	1.75	0.00	0.00	-27.38%
People's Finance Co Ltd.	9.00	9.00	9.00	5.00	0.00	0.00	0.00	-24.07%
Total	249.93	259.99	372.75	502.55	751.8	523.36	466.43	446.68
Average	62.48	65	93.19	125.63	187.95	130.82	116.60	111.67
Growth Rate		4.03%	43.36%	34.81	49.60%	-30.39%	-10.45	15.16%
Investment in Corporate Securities								
Goodwill Finance co ltd	13.25	24.45	23.93	22.04	11.86	7.39	7.07	-13.71%
Nepal Merchant Banking and Finance co Ltd.	2.59	1.74	19.14	17.39	17.79	6.19	6.19	149.18%
Katmandu Finance Co Ltd.	1.59	4.24	4.96	4.94	4.98	1.72	1.54	18.02%
People's Finance Co Ltd.	2.00	2.00	2.00	11.12	11.14	3.09	3.09	63.98%
Total	19.43	32.43	50.03	55.49	45.77	18.39	17.89	34.20
Average	4.85	8.10	12.5	13.87	11.44	4.59	4.47	8.54
Growth Rate		67.01%	54.32%	10.96	-17.80%	-59.87%	-2.614%	8.66%

Source: Annual Report of Sample Finance Co.

As previous, the above table shows the scenario of finance companies (sample companies) towards investment in government securities and corporate securities. Table depicts that average amount of investment made towards governments securities (Rs.111.67 million) is

higher than corporate securities (Rs.8.54 million). Hence, we can conclude that both sectors, commercial banks and finance companies, make huge amount of investment towards government securities.

Incase of finance companies, total average growth rate towards government securities is 15.16 %, which is higher than that of corporate securities (8.66 %). But, if we consider the individual samples, all samples except that of Goodwill Finance; average growth rate of investment in corporate securities is more than investment in governments securities. (Calculation details are presented in Appendix No.3). Finally, we can conclude that finance companies are increasing their investment towards corporate securities.

Primary Data Analysis

Questionnaire survey was made with investors of different nature randomly, including male, female less informed, well informed, employed, unemployed investors and so on. The total number of subjects or cases is .58. Details of descriptive statistic are shown in appendix no.5)

Gender and age

Among 58 selected investors 69%of investors were male investors and 31.9% were female investors. As per the age 9% were below 30 and rest was 30 and above.

Education

On the basis of education, investors are categorized into there groups- undergraduate, graduate and post graduate and above. Among them, majority of investors 51.7% were graduate, 32.8% of respondent core postgraduate and above and remaining 15.5% were undergraduate.

Employment status

Considering employment status, majority of investors i.e. 63.79% were found to be jobholders. It means that they are regular earners.18.96% of respondents were found to very self-employed. They were also there regular earners. Around 12.06% were unemployed which means that they do not have regular such of income and very few were

fund to be retired i.e. 5.17%. They do not have current regular income source except pensions and provident funds.

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Category

Regarding the question asked to the investors abut category, 41.1% of replied that they are informed investors likewise 13.85 of respondents answered that they are well-informed 12% were found analyst of processional investors and rest belong to informed category. During the survey it was fond that most of investors who were found in NEPSE floor and bookers offers were well informed and professional.

For the collection of primary data, it is done on the basic of major investment alternative, available, financial instruments and investor's attitude towards awareness, whim, risk and return and so on.

4.3 Major Investment Alternatives Available in the Nepalese Capital Market

For this study, corporate securities government securities real estate and bullion are taken as a major investment alternative that is prevailing in the Nepalese investment environment. Table below shows the major investment alternative and their frequencies as well as percentage.

Table 4.14

Major Investment Alternatives Available in the Nepalese Capital Market

Investment alternative	**Frequency**	**Percentage**
Corporative securities	31	53.4
Government Securities	13	22.4
Real estate	8	13.8
Bullion	6	10.3
Total	**58**	**100.0**

Sources: Field Survey, 2007

The above table depicts that majority of the investor's i.e. 53.4% like to invest in corporate securities; where as 22.4% of investors would like to invest in government securities only 13.8% of the investors prefer real estate and 10.3% of the investors prefer bullion.

On this basis we can say that corporate securities and government securities are major investment alternatives where as real estate and billion is not a major one. The corporate securities is widely used in the Nepalese capital market because of the reasons also like back interest rates are going down, government bonds are rarely available and the bullion market is not systematically organized.

4.3.1 Preference over Financial Instruments

Study had considered common stock, preference shares, government bonds, debentures, mutual funds and treasury bills as the major financial instruments. Since these are the major instruments that prevail in the Nepalese financial market. Among the survey made with 58 investors, there preferences towards different financial investments were shown in the table below;

Table 4.15

Preference over Financial Instruments

Financial Investment	**Frequency**	**Percentage**
Common Stock	22	37.9
Government bonds	11	19.0
Performance share	9	15.8
Debenture	7	12.1
Mutual Funds	5	8.6
Treasury Bills	4	6.9
Total	**58**	**100**

Sources: Field Survey, 2007

In the above table it is clearly given the respondents view regarding the different financial instrument. Majority of the respondents 37.9% stated that the Nepalese investors preferred to invest in common stock 19.05 of the respondents stated that the preference of investors is on government bond, 15.5% of respondents stated tat the investors prefer to invest in

preference share 12.1% of respondents preferred to invest in debenture where as 8.6% investors prefer mutual fund and 6.9% investors prefer treasury bills.

On analyzing all these aspects we can conclude that most of the investors gives that preference toward the common stock and after that they go for the government bond next most of them prefer preference share, then after debenture and they least prefer the mutual funds and treasury bill.

4.3.2 Preference over Investment Sectors

SEBON and NEPSE have categorized that listed companies in 8 sectors as commercial banks, finance companies, insurance companies development banks, manufacturing and processing trading, hotels and others. For this study also, same sectors of investment are considered to see which sector the investors prefer most to invest.

Table 4.16

Preference over Investment Sectors

Investment Sector	**Frequency**	**Percentage**
Commercial Banks	31	53.4
Financial companies	10	17.2
Insurance companies	7	12.1
Development banks	5	8.6
Manufacturing and processing companies	2	3.4
Trading companies	2	3.4
Hotels	1	1.7
Total	**58**	**100**

Sources: Field Survey, 2007

We can see from the above table that the majority of the opinions (53.4%) supported commercial bank, 17.2 % respondents stated that Nepalese investor prefer finance companies. Than 12.1% respondents prefer insurance companies, 8.6% investors prefer development banks and 3.4% of respondent stated that the investors prefer to invest in manufacturing and processing companies and trading companies .We can also see that only 1.7% of the investors prefer the hotel sector.

On analyzing all these aspects we can conclude that commercial banks, finance companies and insurance companies are found to be the most preferred sectors whereas the manufacturing and processing, trading and hotels are the less preferred sectors. Among them commercial banks are most preferred and hotels are least preferred sectors for investment.

4.3.3 Consideration for Corporate Security Investment

As per the survey made with the investors different factors were considered while making an investment decisions to buy corporate securities. Different factors, their frequencies and their percent were shows in the table below;

Table 4.17

Consideration for Corporate Security Investment

Factor	**Frequency**	**Percentage**
Companies goodwill	28	48.3
Forecasted profit	18	31.0
Friends and relatives motivated them	8	13.8
Advertisement appealed	3	5.2
Because most of people are buying it	1	1.7
Total	**58**	**100**

Sources: Field Survey, 2007

Here most of the investors (48.3%) said that company's goodwill is the most impotent which guides their investment decisions. Whereas 31.0% investors consider forecasted profit before investing in corporate securities 13.8% of investor said that they just buy the corporate securities because of the friends and relatives.

On analyzing all these aspect we can conclude that most of the investors consider company's goodwill before investing in corporate securities.

4.3.4 Preference on Stock Investment

Survey made with 58 investors shows that following result towards preference of investor's stock investment.

Table 4.18

Preference of Investors over Stock Investment Stock

Stock investment factors	Frequency	Percentage
Dividend	14	24.1
Capital gain	29	50.0
Bonus share	9	15.5
Representation in board	2	3.4
voting right	4	6.9
Total	**58**	**100**

Sources: Field Survey, 2007

We can see from the above table that the maximum frequency lies on capital prefer capital gain on their stock investment. Dividend is the next preferred factor of stock investment with 24.1% response, and then only come bonus share with 15.5% response. Very few investors 3.4% consider representation in board as the preferred factor of share invests. Where as 6.9% of investor preferred voting rights as the factor of stock invest high preference toward capital gain from the investors perform the increment of the share price as a factor of stock investment.

4.3.5 Awareness of Financial Instruments

Among the 58 randomly selected general investors, only 12% were found to be professional investors who are really informed and aware as well as they do the analysis while making investments, 13.8% said that they are well informed about financial market. Around 31.03% of investors said that they are less informed type of investors .A large segment of investors 43.1% said that they are neither less informed nor well informed. They are informed just to a satisfactory level. It shows how much Nepalese investors are aware of financial instruments. Only 15 among 58 said that they are really much informed. This scenario depicts that majority of investors are not well informed and much aware. (Details in Appendix)

4.3.5.1 Education and Market Information

In the samples taken, majority of investors were found informed but not well informed and also significant portion said that they are less informed. A test has been made to see if the

awareness of market information varies with the level of education. Theoretically, it can be said that highly educated person has much knowledge of market. To test it chi-square test has been made for the variables like education and categories of investors.

Null Hypothesis (Ho) = the variables, level of education and market information has no association.

Alternate Hypothesis (H_1) =the two variables have significant association.

Table 4.19

Level of Education and Market Information

	Types of Investors				
Level of education	**Less informed**	**Informed**	**Well informed**	**Analysts professional**	**Total**
Undergraduate	3	4	1	1	9
Graduate	10	15	3	2	30
Post-Graduate	5	6	4	4	19
Total	18	25	8	7	

Sources: Field Survey, 2007

Tabulated value of chi-square (χ^2) at 5% level of significance for 6 d.f is 12.59.As per the calculation made in appendix no.12 calculated value of chi-square (χ^2) at 5% level of significance for 6.d.f is 4.1915.Since the table value exceeds the calculated value, null hypothesis is accepted. It means that there is not any association between level of education and market information only to be highly educated can't make a person well informed investors.

4.3.5.2 Awareness of Financial Derivatives

Table 4.20

Knowledge and Attitude Towards Financial Derivatives

Do you know about financial derivatives?

If yes which one do you know?

			Derivatives	**Frequency**
Yes	24	41.37%	Future	2
			Options	5
			Warrants	6
			Convertibles	11
			Do your want to invest on them?	Yes No 18 6
No	34	58.63		
Total	**58**	**100%**		

Sources: Field Survey, 2007

As shown in the above table, majority of investors 58.63% were found to be unaware of financial derivatives. Only 41.37% of investors were found to be aware of financial derivatives. Among them most of them know about convertibles since it had got the largest frequency of 11, options and warrants are found to be almost equally popular. Only few investors (i.e. 2) know about future. Among those who know about financial derivatives were asked whether they want to invest on them if they got opportunity, for that questions among 24 investors 18 of them said yes where as remaining 6 investors said they just know about derivative but don't want to invest on them.

a) Educational and Knowledge of financial derivatives.

Since 58.63% of investors were unaware of financial derivatives, whether the education of investors affect the knowledge of derivatives or not has been explored on the basis of chi-square test.

Null Hypothesis (Ho) = there is no relations between the level of education and knowledge of derivatives.

Alternate Hypothesis (H_1) = Relationship exist between the level of education and knowledge of derivatives.

Table 4.21

Education and Knowledge of financial derivatives.

Level of education	**Know about datives?**		
	Yes	No	Total
Undergraduate	2	7	9
Graduate	9	21	30
Post-graduate and above	13	6	19
Total	**24**	**34**	

Sources: Field Survey, 2007

Tabulated value of chi-square at 5% level of significance for 2.d.f is 5.99. As per the calculation made on Appendix no.13 calculated value of chi-square is 8.6075. Since calculated value exceeds the table value, null hypothesis is rejected. It means that there is association between level of education and knowledge of derivatives. Most of the investors with high level of education were aware of derivatives.

4.3.6 Attitude toward Government Securities

Survey made with 58 investors shows the following result towards investment on government securities

Table 4.22

Investment on Government Security

	Frequency	**Percentage**
Investors who have invested in government securities	40	68.96
Investors who have not invested in government securities	18	31.03
Total	**58**	**100**
For those who have invested in government securities, what factors made them invest on it?		
Marketability	5	12.5
No risk/Safety	32	80
NRB Notices	2	5
Friends and relatives	1	2.5
Whim and rumor	0	0
Total	**40**	**100**

Sources: Field Survey, 2007

Result show that 80% of the investors have invested on government securities because of safety or no - risk, 12.5% have invested because of the liquidity of the government securities, only few investors have invested on government securities just by studying NRB notices (5%) and through friends and relatives(2.5%).However, nobody said they were affected by the whim and rumor.

4.3.7 Consideration for Investment Decision.

As per the survey made with the investors different factors were considered while making an investment decisions. Different factors their frequencies and percent were shown in the table below;

Table 4.23

Consideration for Investment Decision

Factors	**Frequency**	**Percentage**
Company's track-record /goodwill	18	31.0
Forecasted profit	11	19.0
Management term and promoted	7	12.1
Environment factors	5	8.6
Expected risk level	9	15.5
Taxation	3	5.2
Inflection	2	3.4
Liquidity and maturity	3	5.2
Total	**58**	**100**

Sources: Field Survey, 2007

Studying the frequency as well as percentage, we can say that company's track record is that factor which majority of investors consider before making investment decisions. Then comes forecasted profit as second major consideration and the factors like management team and promoters comes in third place of consideration.

All above mentioned factors are very crucial factors while making decision of investment. So, good investors must consider all these factors before making investment.

4.3.8 Attitude Toward Re Investment

Table 4.24

Attitude Towards Re Investment

		Frequency	**Percentage**
Re-investment	Purchase more securities of more kind	18	31.0
	Purchase some other kind of securities	25	43.1
	Total	**43**	**74.1**
No-reinvestment	Spend on durables	6	10.3
	Save it safely	9	15.5
	Total	**15**	**25.8**

Sources: Field Survey, 2007

The above table depicts that majority of the investors i.e. 74.1% want to re invest their return, where as 25.8% of investors just want to save the return safely or spend the returns to buy some durables.

Among those who want to re-invest, 25 investors (43.1% of re- investors) want to purchase some other types of securities, or want to invest on some investment opportunities. However, 18 investors (31.0% or re- investors) want to purchase the same kind of securities from which they have gained. It means that most of the investors want to diversify their portfolio by selecting some other investment instruments .But during the course of survey investor said the decision to select which instrument fully depends upon the market scenario.

4.4 Problems to Invest in Securities in Nepalese's Security Market

There are number of problems that the investors are facing in the Nepalese security market. The securities market in Nepal is still at a nascent stage and has failed to show impact on the overall national economy. Small market size has made it vulnerable to manipulation and price rigging. The market lacks sectoral diversification of performing listed companies, access to secondary trading services is limited, transparency and efficiency of the issuer and market is not sufficient, capacity of the regulator, exchange and the players is limited, the market is featured by active individual investors and the institutional

investors are conspicuously absent. The market infrastructures supporting the trading, clearing and settlement are not sufficient.

The opinion given by the respondents regarding the problems to invest in securities is given below. The means score above the average level indicates that those problems may be regarded as the basic problem to invest in Nepalese security market and vice versa.

4.4.1 Small Size of Market

Table 4.25

Small Size of Market

Variable	**N**	**Mean**	**Std. deviation**
Low quality of public issue of share	58	4.4310	1.12565
Lack of one window policy in public issue	58	4.3621	1.61446
No diversity in issue companies	58	4.1897	1.54984
Use of outdated technology in securities trading and clearing and settlement system	58	5.0345	1.16928
No choice of instruments	58	5.0000	1.12390
Low involvement of institutional investors in the market.	58	4.1552	1.37396
Long time gap between public issue and listing	58	3.9138	0.91188
Slow speed of privatization	58	3.9138	0.91188
Average mean		**4.48**	

Sources: Field Survey, 2007

One Sample Test

Text value -4

Variable	**t**	**df**	**Sig. (2tailed)**	**Mean difference**	**95 % confidence interval of the difference**	
					Lower	**upper**
Low quantity of public issue of share	2.916	57	0.005	0.4310	0.1351	0.7270
Lack of one window policy in pubic issue	3.732	57	000	.75856	3115	1.1657
Use of outdated technology in securities trading and clearing and settlement system	-.407	57	0.686	-0.2862	-.5107	.3383
No choice of instruments	6.738	57	.000	1.0345	.7270	1.3419
Low involvement of institutional investors in the market	6.776	57	.000	1.000	.7045	1.2955
Long time gap between public issue and listing	.860	57	.393	.1552	-2061	.5164
Slow speed of privatization	3.024	57	.004	.3621	.1223	.6018

Above table shows the clear picture of descriptive result for all the variables. The mean score of overall items appeared as above average position (i.e. 4.48 presented in table 4.25). It signifies that small size of market may be the major problem to invest in securities. There was no choice of instruments as well as low involvement of institutional investor in the market because the average of this variable was found above average positing (i. e. 5.0345 and 5.000 respectively). Similarly the mean score of slow speed of privatization appeared as 3.9138 which signify that the respondents slightly agree that it is the problem to invest. In other situation, the position/ size of the market was found average because the mean score of remaining other variable was found in average position.

In the same way, the standard deviation of the entire variable except slow speed of privatization was found above the average (i.e.>1).It means that the responses were found highly fluctuation in these cases. In terms of low speed of privatization the respondents found low fluctuated.

An issue appeared whether difference found among variables are significant or not. To resolve this problem on sample's' test has been conducted among those variable. The result of high mean difference and significant' statistics refers statistically different. The result showed high 't' statistics in the variable of 'low involvement of institutional investors in the market, and ' No choice of instrument', moderate in 'lack of one window policy in public issue' and 'slow speed of privatization' and low in remaining other variables. The result showed that the variable having high and moderate's' value were found statistically significant at more than 99 percent level of confidence.

4.4.2 Poor Corporate Results

Table 4.26

Poor Corporate Results

Variable	**N**	**Mean**	**Std. deviation**
Poor performance of listed companies from manufacturing and trading sector.	58	4.5862	1.18521
Poor corporate governance practice	58	3.9483	1.36911
Inadequate accounting and auditing practice of issuer and listed companies.	58	3.4828	1.52455
Low level of professionalism in financial forecasting and underwriting practice.	58	3.3103	1.64591
Poor performance of privatized enterprises.	58	3.4138	1.31168
Inadequate disclosure practice of issuer and listed companies	58	3.7414	1.11702
Average mean		**3.7471**	

One Sample Test

Test Value = 4

Variable	**t**	**Df**	**Sig. (2tailed)**	**Mean difference**	**95 % confidence interval of the difference**	
					Lower	upper
Poor performance of listed companies from manufacturing and trading sector	3.767	57	0.000	-.5862	.2746	.8978
Poor corporate governance practice	-.288	57	.775	-.0017	-.4117	.3083
Inadequate accounting and auditing practice of issuer and listed companies.	-2.584	57	012	.5172	-.9181	-.1165
Low level of professionalism in financial forecasting and underwriting practice	-3.191	57	.002	-.6897	-1.1224	-.2569
Poor performance of privatized enterprises.	-3.404	57	.001	-.5862	-.9311	-2413
Inadequate disclosure practice of issued and listed companies.	-1.763	57	.083	-2586	-.5523	.351

The above table shows the clear picture of descriptive result of the entire variable. The mean score of over all item appeared as average position (i.e 3.7471 presented in tables 4.26). It signifies that poor corporate results may be the average problem to invest in securities. There was poor performance of listed companies from manufacturing and trading sector. The average of this variable was fond above average (i.e. 4.5862)

Similarly, most of the respondents slightly disagree that low level of professionalism in financial forecasting and underwriting practice is the problem that the investors are facing in the Nepalese security market because the mean score of the variable stood as 3.3103. In other situation, the mean score was found average.

In the same way, the standard deviation of all the variables was found above the average (i.e.>1). It means that the responses were found highly fluctuated in these cases.

An issue appeared whether difference found among variables are significant or not. To resolve this problem, one sample‘t’ test has been conducted among these variables .The result of high mean difference and significant 't'statistics refers statistically different.

The result should moderate’t’ statistics in the variable of poor performance of listed companies from manufacturing and trading sector and low in remaining other variables.

4.4.3 Poor Regulatory Infrastructure

Table 4.27

Descriptive Statistics of Poor Regulatory Infrastructure

Variable	**N**	**Mean**	**Std. Deviation**
Investors protection mechanism is not adequately developed	58	3.6362	1.42699
Inadequacy in legal infrastructure on securities market.	58	3.2069	1.43586
Improper handling of investor’s grievances	58	4.9138	1.60355
Inadequacy in accounting and auditing system and legislation.	58	4.1379	1.69051
Negative impact of Nepal Rastra Banks directives.	58	3.4483	1.48882
Average mean		**3.8686**	

One-Sample Test

Test Value =4

Variable	t	d.f	Sig. (2 tailed)	Mean difference	95% confidence interval of the difference	
					Lower	Upper
Investors protection mechanism is not adequately developed	-2.208	57	0.031	-0.4138	-.789	-.0386
Inadequacy in legal infrastructure on securities market	4.207	57	.000	-0.7931	-1.1706	-0.4156
Improper handling of investors grievances	4.340	57	.000	0.9138	0.4922	1.3354
Inadequacy in accounting and auditing system and legislation	.621	57	.537	0.1379	-0.3066	0.5824
Negative impact of Nepal Rastra Bank's Directives	-2.822	57	.007	-0.5517	-.9432	-0.1603

Table 4.27 shows the clear picture of descriptive results of the entire variable. The mean score of overall items appeared as average position. . It signifies that poor regulatory infrastructure may be the problem to invest in securities. Investor's grievances were not properly handled by the issuer and listed companies because the mean of this variable was found above average i.e. 4.9138. There was also inadequacy in accounting and auditing system and legislation because the mean of these variables also appeared above average i.e. 4.1379. Most of the respondents disagree that inadequacy in legal infrastructure on securities market may be the problem to invest in securities because the mean score of the variable is 3.2069. The mean score of remaining other variables was found in average position.

In the same way, the standard deviation of all the variables was found above the average (i.e.>1). It means that the responses were found highly fluctuated in theses cases.

An issue appeared whether difference found among variables are significant or not. To resolve this problem one sample't' test has been conducted among these variables. The result of high mean difference and significant' statistics refers statistically different. The

result showed high't' statistics in the variable of improper handling of investor's grievances and inadequacy in legal infrastructure on securities market and low in remaining other variables.

4.4.4 Low Level of Investor's Knowledge in Security Market

Table 4.28

Descriptive Analysis of Low Level of Investor's Knowledge in Security Market

Variable	**N**	**Mean**	**Std. Deviation**
Insufficient educative and awareness activities relating to securities market.	58	3.9483	1.34324
Investors are not aware and educated on risk and return aspect of securities market.	58	3.9655	1.31076
Absence of investment advisory and management companies.	58	4.3966	1.15378
Average mean		**4.1034**	

One-Sample Test

Test Value = 4

Variable	**t**	**d.f**	**Sig. (2_tailed)**	**Mean difference**	**95% confidence interval of the difference**	
					Lower	Upper
Insufficient educative and awareness activities relating to securities market.	-0.293	57	0.770	-0.0517	-0.4049	0.3015
Investors are not aware and educated on risk and return aspect of securities market.	-0.200	57	0.842	-0.0345	-0.3791	0.3102
Absence of investment advisory and management companies.	2.618	57	0.011	-0.3966	0.0932	0.6999

As shown in the table no 4.28 the mean score of overall items appeared above average position i.e. 4.1034. It signifies that low level of investor's knowledge in security market may be the basic problem to invest in securities. The respondents were highly agreed that there is absence of investment advisory and management companies in Nepalese security market because the mean score of this variable was found above average (i.e. 4.3966). Respondents also agree that investors are not aware and educated on risk and return aspect of securities market as well as there is insufficient educative and awareness activities relating to securities market.

In the same way the standard derivation of all the variables was found above the average (i.e. >1). It means that the responses were found highly fluctuated in these cases. An issue appeared whether difference found among variables are significant or not. To resolve this problem, one sample 't' test has been conducted among these variables. The result of high mean difference and significant 't' statistics refers statistically different.

The result shows high 't' statistic in the variable of absence of investment advisory and management companies and low in remaining other variables .The result show that the variables having high 't' value were found statistically significant that more than 99 percent level of confidence.

4.4. 5 Poor Performance of National Economy

Table 4.29

Descriptive Analysis of Poor Performance of National Economy

Variable	**N**	**Mean**	**Std. Deviation**
Low level of saving and investment in the economy.	58	3.4310	1.14113
Bank oriented financing pattern	58	3.0690	1.49692
Low level of per capita income	58	3.8793	1.29882
Industrial slackness and security problems	58	4.0172	0.92701
Average mean		**3.59**	

One-Sample Test

Test Value=4

Variable	T	d.f	Sig.(2taied)	Mean difference	95% confidence interval of the difference	
					Lower	Upper
Low level of saving and investment in the economy.	2.877	57	0.006	.4310	.1310	.7311
Bank oriented financing pattern	.351	57	.727	.0690	-.3246	.4626
Low level of per capita income	5.156	57	.000	.8793	.5376	1.2206
Industrial slackness and security problems	8.367	57	.000	1.0172	.7735	1.2610

Table no 4.29 shows the clear picture of descriptive results of the entire variable. The mean score of overall items appeared as average position (i.e. 3.59 presented in table 4.29). It signifies that poor performance of national economy may not be the major problem to invest in securities.

The respondents were highly agreed that there is industrial slackness and security problems because the average of these variables was found above average (i.e. 4.0172). The mean score of remaining other variables was found in average position.

In the same way the standard derivation of all the variables except industrial slackness and security problems was found above the average (i.e.> 1). It means that the responses were fond highly fluctuated in these cases,. In terms of industrial slackness and security problems the respondents found low fluctuated.

An issue appeared whether difference found among variables are significant or not. To resolve this problem, one sample‘t’ test has been conducted among these variables. The result of high mean difference and significant't' statistics refers statistically different.

The result showed high‘t’ statistics in the variable of industrial slackness and security problems and low level of per capita income, moderate in low level of saving and investment in the economy and low in bank oriented financing pattern.

4.5 Major Findings

Some of the summarized major findings of the study are:

1. Financial Instruments in Nepal

The issuance of corporate securities made since 2000/01 shows that 70.20% of total issues is covered by common stock .Since it has highest coverage in total corporate issues, it means common stock is the most widely used corporate security. Whereas preference shares and debentures are in low limits. In comparison to them, mutual fund and unit schemes are used significantly.

Government issues shows that T-bills are the mostly used government security which covers around 56.38% of total issues. It is the money market instruments and is not targeted for individual investors .Development bonds and special bond have also significant coverage in total issues of 17.31% 13.15% respectively .Public saving card has appeared as a new concept and is growing in a good phase.

2. Major Investment alternatives and investor' preferences

While conducting survey with 58 randomly selected investors, corporate securities, government securities, real estate and bullion are considered as major investment alternatives available in the Nepalese capital market. Among them, corporate securities are found to be widely used alternatives. But the alternatives like real estate and bullion are not that much preferred by Nepalese investors.

3. Investment Sectors and investors preferences

Result showed that investors want to invest most of their savings on banking and financial sectors in comparison to other sectors like: manufacturing and processing, trading, hotel and others. Commercial banks, finance companies and insurance companies were found to be the most profitable and safe sectors.

Analysis of subscription ratios has also showed that the issues of financial institutes are highly over-subscribed. On the contrary, issues made by manufacturing and processing companies suffer from under-subscription. It depicts that in the primary market also, most of the savings were invested in the banking sector takes an important place than other sectors.

4. Financial instruments and investors preferences

To focus more on financial instruments only ,the alternatives like Real estate and bullion were dropped and different financial instruments that are prevailing in the Nepalese capital market were presented to the investors to see what they prefer most .Here, common stock appeared as the most popular financial instruments. Responses toward T-bills were found very low.However, government bonds appeared as the second most popular financial instruments. As per the issuance also, Nepalese capital market heavily depends upon common stock. The issuance of other instruments in comparison to common stock is very poor. It means that the capital market of Nepal lacks the choices. Financial innovation is really lacking in Nepalese financial market.

5. Consideration for Corporate security investment.

Majority of the respondents stated that company's goodwill is the most important factor which guides their investment decisions.

6. Stock investment and investor's preferences

Capital gain was found to be the most preferred factor of stock investment. Dividend appeared as the second preferred objective of stick investment.

7. Government Securities and investor's preferences

More than 30% respondents have never invested on government securities. Majority of those who have invested said that they have invested because of safety

8. Awareness of financial instruments

Nepalese financial market is lacking well-informed and professional investors. Most of the investors are educated but education has not to do much with the knowledge of capital market and financial securities. They do not conduct detail analysis before making investment on financial instruments. While interviewing, investors said that before investing, they should consider several important factors like companies track record, promoters of the company, forecasted profit, environmental factors and others. But in practice, our market is totally guided by whim and rumor.So, at the time of making decision, whim and rumor affects much. Awareness towards the derivatives is found to be very poor in the Nepalese capital market.58.61% of respondents said that they have not ever heard about derivatives. Only some educated and professional investors were found to

be aware of derivatives. Most of them know about convertibles and only few investors know about future.25% of investors said that also they have an idea about derivatives; they do not want to take risk by investing on them. The knowledge of options, futures, Swaps are lacking in Nepalese capital market

Around 74% of investors said that they re-invest the returns they gain. But remaining 25.8% will consider buying some durables or saving the return safely if they gain from investment.

9. Problems to invest in securities in Nepalese Security market

The respondents were asked to give their opinion regarding the problems to invest in securities in Nepalese security market .Among the problems. Small size of market and low level of investor's knowledge in security market were found to be the major problems that the investors are facing to invest in securities. Under small size of market, there was no choices of instruments as well as there low involvement of institutional investors in the market.Similarly,under poor corporate results, majority of investors strongly agreed that there was poor performance of listed companies from manufacturing and trading sector. In the same way, under poor regulatory infrastructure, majority of investors strongly agree that investor's grievances were not properly handled. Under low level of investor's knowledge in security market there was absent of investment advisory and management companies.

Similarly, under poor performance of National Economy, most of the respondents strongly agreed that there was an industrial slackness and security problem.

CHAPTER-V

SUMMARY, CONCLUSION & RECOMMENDATIONS

5.1 Summary

The history of securities market begins with the flotation of shares to the general public by Biratnagar Jute Mills ltd. in 1936. However, the development of securities market could not be a national policy for a long time. The then industrial policy of Nepal led to the development of securities market with the establishments of securities Marketing Centre (SMC) IN 1976.Before the establishment of SMC, there were no institutional arrangements to undertake and to manage the new issues of securities. IPO s had to be made as per the Provision of Companies Act, 1936, which were not adequate and relevant. The Act had not even incorporate security.

SMC started secondary trading of securities in 1981, which was restricted to government bonds till 1983, the concept of well- structured secondary market had not evolved in Nepal No separate Act existed to regulate the trading of securities the securities exchange Act, 1983 was enacted in 1983 .The act restricted the exchange of unlisted shares. The SEC was the only institution at that time managing and operating primary and secondary markets of long-term government and corporate securities.

A need to develop different institutional mechanisms relating to securities market was strongly felt to avoid potential conflict of interest between the services provided. The first amendment in the Securities Exchange Act, 1983 in 1993 paved the way for the restructuring of securities market in Nepal, which led to the establishment of Securities Board of Nepal (SEBO) IN 1993 with a mandate to regulate and develop the securities market.SEBO started to register securities and grant approval for issuing securities to the public in 1993.The first amendment in the act also led to conversion of SEC into Nepal Stock Exchange (NEPSE) in 1993 with the objective of operating and managing secondary transactions of securities. The initial efforts led to the opening of full-fledge stock exchange in January 13, 1994.

The second amendment Securities Exchange Act 1983 was made in 1997. This amendment made provision for registering securities businesspersons in SEBO.As per the provision of second amendment SEBO provided the license to the securities businesspersons in 1997. The amendment made mandatory provisions for the listed companies to submit annual and semiannual reports to the SEBO. This amendment also required securities businesspersons to submit annual reports incorporating the securities transactions carried out by them to SEBO.

Currently , there are 23 stockbrokers, 2 securities dealers, 9 issue managers, l stocks exchange and 135 listed companies in the Nepalese securities market. Till now , the companies like banks, finance, insurance, hotels, manufacturing, trading, aviation etc have entered into security market but the companies from construction, information technology, etc have not entered yet. Ordinary shares, right shares, preference shares, debentures, and mutual funds are major corporate securities of Nepalese capital market. Common stock appears as the most widely used corporate securities. To turn towards the government securities, there areT-bills, and IMF promissory notes The participation of mutual fund in the securities market as institutional investors is limited to only two - Citizen investment Scheme (operated from 1994/95)and NCM Mutual Fund (operated from 2002/03).

Looking towards the public issue, during the period of last seven years(2000/01 to 2006/07), total 102 companies issue their securities to the public among which most are finance companies. But the issues made by commercial banks are highly oversubscribed in the primary market. Most of the securities issued by manufacturing and processing companies are found to be under-subscribed. This indicates that investors want to hold the securities of commercial bank than companies from other sectors.

Nepalese financial market consists of varied types of investors, those who are completely unaware of market and those who are professional players of security market. However, the institutional investor seems very much passive in secondary market though their participation in IPO's are very significant .In such scenario, this study was conducted with an objective to explore the developmental position of different financial instruments in the Nepalese capital market. Specifically, the objectives of the study are set as: to analyze the development of Nepalese capital market, to analyze the different investment alternatives

available in the Nepalese capital market, to analyze the preference of the different investors of Nepal and to know what type of instruments the investors prefer the most and to identify the problems to invest in securities in Nepalese capital market. Responses of 58 randomly selected investors are taken for the study. The time period for this study is from 2000/01 to 2006/07.

5.2 Conclusion

Capital plays a vital role in the economic development of a country. Nepal being one of the least developed countries in the world has to make every possible endeavor to efficiently mobilize the available capital. the need for securities market development in Nepal has been an accepted reality ; however it is still at a nascent stage. The economic liberalization ,which really started to gain momentum after the establishment of several joint venture commercial banks in the mid-eighties, ushered to establish full-fledge NEPSE and SEBO to trade and regulate securities law and the its underlying regulations to make the capital market more vibrant and dynamic ,the effort have not yielded the desired results. With the current stock trading turnover of about Rs3541.43 million market representation severely titled towards the banking sectors (around 89%),almost non-existence institutional investors, underdeveloped bond and derivative markets coupled with serious governance issues, our market is far from appealing to potential investors.

History of securities market shows that only four types of securities (common stock, preference shares, debentures, mutual funds) were being issued in Nepal at varying period of time. Nepalese security market is completely dominated by equity shares. Investors do not have many choices, so they are pouring their investments on those equity investments. There are very less number of professional investors, whom we can count easily. The awareness level of those professional investors is really good, but those investors who do not have much information about the market, makes investment just because of influence of friends and relatives. They even don't know how the transfer of share ownership takes place and what its process is. The awareness level of general investors is really poor. They just follow the whim of the market. Those who do not know about the financial market and investment scenario prefer real estate and bullion where their capital gets stuck for the long time in a hope of rise in their price. Such investment will not help in the capital mobilization of the economy. Institutional investors are very passive in Nepal. Commercial

banks, finance companies, insurance companies, pension funds, investment trusts etc.are the major institutional investors of any economy. But our country all of those are not actively taking part in the capital market, especially in secondary market. Institutional investor such as CIT has very low participation in Nepalese security and Employee Provident Fund has no participation at all. The participation of Mutual fund in the securities as institutional investors is limited to only two-NCM Mutual Fund and Citizen Investment scheme. Similarly, listed companies as institutional investors have stake in an average below one percent in the primary market. It seems stock market liquidity needs improved seriously. The market will have better liquidity if the securities are available to the price takers and the price reflects all relevant information. Nepalese security market is performing poorly in both these aspects. The consequence is very low market participation.

The efficient services of market intermediaries, awareness campaigns for investors, conductive and realistic policies of regulating authorities, legal inadequacy, double taxation on dividend and capital gain tax, poor corporate governance practices, poor disclosure practices high cost of public issue, high transaction cost and so on are the major felt need in this regard.

5.3 Recommendations

With the study of findings of research and the literatures reviewed, finally some suggestive measures can be forwarded to the concerned parties.

- Investors tend to avoid securities market because they do not have options to invest in securities according to their risk-return preference (K.C. 2004). The diversity n more development securities market instruments attracts the investors of various risk-return preferences thereby promoting the size of market and liquidity. Ordinary share is a risky instrument whereas preference share, mutual fund and debentures are low risk instruments. In the context of Nepalese market, there is less opportunity for risk averter and risk neutral investor as the market is dominated by ordinary share, which is most risky instruments. Market is not conductive to knowledgeable investors as there are no derivative instruments like warrants, options, future, swaps, etc. to match with their preferences and expectations. Government securities (bond) market is unsystematic as

the buying and selling of government securities is not based on demand and supply. Corporate bond market is also in the initial stage of development. Thus, the market is not encouraging to attract the large number of potential investors.

- Systematizing the government securities market and attracting institutional investors in the market could partly solve the problem of low diversity in securities market instruments. The systematic market for government securities also provides benchmark in setting interest rate for corporate debentures. To systematize government securities market, government securities should be transacted thought the NEPSE. Privatization bond, development bend, municipal bond and securitization activities should be promoted to increase the market for fixed income instruments. Institutional investors should be encouraged to enter into the market with suitable fiscal and other incentives as they could stimulate demand for debentures. Incentives should also be provided to the companies raising funds by issuing derivatives.

- Institutional investors are more informed than individual investors and have more incentive to monitor performance and keep management up to the mark. Institutional investors help stabilize price of securities and maintain confidence of retail investors in the market. But, the involvement of institutional investors is very low in Nepal. To address this problem, government should take initiative in establishing a clear regulatory provision that requires the Employee provident Find and Citizen Investment trust investing certain portion of funds in the securities market along with some provisions of fiscal and other incentives. Some flexibility in the directives should be brought to attract the institutional investors in the market of financial instruments.

- The securities market provides liquidity to the issued securities. The BAFIO, 2004 requires every financial institution to offer at least 30% share of issued capital to the general public Similarly, Insurance Board also requires every insurance company with its registered office in Nepal to offer at least 20% of its issued capital to general public. However, in case of companies from other sectors, there is no mandatory provision for the issuance of securities. The liquidity in the market can be promoted by increasing public flotation of shares. Amending the legal provisions governing financial institutions and insurance companies that require the increase percentage of public flotation could do this. In addition, mandatory provision should be made for the

companies from other sectors to float certain percent of their shares to the public. The government should also be committed to achieve its goal set in the tenth plan to increase the public ownership in the corporate bodies. The pace of privatization of public corporations should also be increase by making use of the securities markets mechanism in the process.

- Study shows that large portion of investors is unaware of market mechanism. Due to this they are investing their big chunk of capital towards unproductive alternatives like real estate and bullion. If awareness level of investors can be improved more savings can be pulled towards financial instruments. Awareness programs and campaigns should be launched for this. This will also help to increase the number of smart investors who will not just gamble on the basis of rumor and whim.

- A separate body that effectively council and give investment related information to the current as well as prospective investors should be formed. Specialized firms, consultancy or forum to provide financial assistance and advices to the investors are really needed for the betterment of the investor's investment decision.

- Regulating authorities like SEBO should work for the well being of the investors with the pro-investors policies. They should not be simply watching the malpractices of listed companies. Investors are the main pillars of the capital market. Without the trust of investors, no capital market can sustain. So, to win the trust of investors, regulating authorities should act on the best interest of investors.

- The regulating authorities should try to bring the investors in the main streamline so as to increase their trust and participation in financial system. Representatives from the investors in regulating mechanism can be one strong move in this regard. Regulating authorities should act as the facilitators rather than the interveners.

- Dividend is the most inspiring aspects for the investment on the ordinary shares of the companies. Stocks with larger ratio of dividend per share to book value per share have higher liquidity, lower leverage, higher earnings, higher assets turnover and higher interest coverage (Pradhan & adhikari, 2004). Nepalese shareholders are not indifferent

towards payment or non-payment of dividends as dividend payout affects the price of a common stock. Despite the important aspect of dividend to encourage the investment in the security market, it is taxed twice. First it is taxed at the corporate level and when it comes to the hands of the investors then also it is taxed. This discourages the investment in ordinary share. In view of resent level of securities market development, there should not be double taxation on dividend.

- Capital gain tax can divert securities market investment to the commodity and bullion markets. In the provision of present capital gain tax, tax is imposed on capital gains from the trading of securities but there is no clarity regarding the write off of capital losses incurred and there is also a problem of establishing net gains in the trading of securities. So the provision of capital gain tax should be rationalized in view of present initial stage of securities market development.

- Generally, companies with the poor governance practices hesitate to issue securities. Issuing companies with poor corporate governance practices from manufacturing and processing, trading and hotel sectors, which issued securities in the past had very poor performance and could not provide any returns to the investors. As a result, investors hesitate to subscribe public issues from manufacturing and processing, trading and hotel sectors and due to this the companies from these sectors face difficulties in raising fund from the market. Hence, concerned authorities must be aware to improve corporate governance practices in the country and rehabilitate the companies from manufacturing and processing, and trading sectors. For this, regulator should prescribe codes on corporate governance and should make mandatory provisions to follow.

- A good disclosure practice is essential to bring transparency in the securities market. Inadequate disclosure practices and poor transparency discourage potential investors from investing in the security market. In order to secure investors' confidence and commitments, a flow of information is a must as investors can make informed decisions in securities market only with adequate information. Informed decisions of investors not only help to stabilize price of securities but also help to attract additional investors in the market. So, to curb he problem of poor disclosure practice, regulatory provisions relating to securities market should be strengthened, as present securities laws do not

provide sufficient power to the regulators to enforce better disclosure practice of the listed companies.

- Cost of public issue (i.e. underwriting cost, advertising, printing and other expenses, collection and refund charges, and issue management commission) is relatively high in Nepal compared to neighboring countries. Among the cost components, collection and refund charges is highest due to over-subscription of issue. Hence, public issue process should be made simple by adopting one window policy that ultimately reduces cost of public issue.

- Cost relating to secondary trading of securities is taken here as transactions cost. Lower the transaction cost higher the return to the investors on securities trading and vice versa. Competitive transaction cost is an incentive to increase volume of share trading. Low transaction cost helps to stabilize securities market by reducing volatility I pricing thereby provide investors a safer place in invest.

- The securities market in Nepal is underdeveloped where procedural or opportunity cost is significantly higher that explicit cost. The development of on-line trading system of securities will provide trading facility to greater number of investors who have access to web. The reduction in transaction time and increasing ease of trade execution should lead to higher volume of securities trading and lower transaction cost.

Appendix No.1

Questionnaire Survey

Dear Respondents

These questions are designed to analyze the development of different financial instruments like: share, debentures etc. The data provided by you will be used only for the research study as a partial fulfillment of MBS degree. I assure you, your responses and views will be completely confidential. Your correction information in this regard will help to explore actual scenarios in this context.

So I cordially request you to kindly answer the questions below.

Binod Thapa
Researcher
Nepal Commerce Campus

Respondents Profile

Sex – Male …….. Female ……

Education -	Less than Graduation	…….
	Graduate	…….
	Post Graduate and above	…….

Status :	Unemployed	……	Job Holder	……..
	Retired	……	Self Employed	……..

1. Please tick that, which appropriately describes you.

a. Less informed investor
b. Informed investor
c. Well informed investor
d. Analyst/Professor

Response toward Financial instrument.

1. Which do you think is a major investment alternative available in the Nepalese capital market

a. Corporate Securities
b. Government Securities
c. Real Estate
d. Bullion

2. In which of the following financial instrument do you prefer to invest?

a. Common Stock
b. Government Bond
c. Preference Share
d. Debenture
e. Mutual Funds
f. Treasury Bills

3. Which one of the following investment sectors do the investors prefer ot make investment?

a. Commerical Banks
b. Finance Companies
c. Insurance Companies
d. Development Banks
e. Manufacturing and processing companies
f. Trading companies
g. Hotels

4. Have you heard about derivatives like future, option, warrants, etc?

a Yes
b. No

If yes, which ones?

a. Future
b. Options
c. Warrants

d. Convertibles

5. What made you buy corporate securities?
   a. Company's goodwill
   b. Companies broadcast profit
   c. Friends and relatives
   d. Advertisements appealed you
   e. Because most of people are buying it.

6. What do you prefer in your share investment?
   a. Dividend
   b. Capital gain
   c. Bonus Share
   d. Representation on Bond
   e. Voting rights

7. If you have invested in Government securities, then what made you buy government securities?
   a. Marketability
   b. No risk/Safety
   c. Friends and relatives
   d. NRB Notice
   e. Because most of the people buy.

8. Suppose you gained a lot from your present investments then what will you do with your return?
   a. Purchase more securities of same kind
   b. Purchase some other types of securities
   c. Spend on durable
   d. Save if safely

9. In your opinion, what investor should consider most before investment decision?
   a. Company track record/goodwill
   b. Forecasted profit
   c. Management team and promoters
   d. Environment factors (political scenario, national plans and policies,international trends, etc)
   e. Expected risk level
   f. Inflation
   h. Liquidity and Maturity

10. Please read the following statement and circle at the appropriate number that comes closet to your opinion.

S. no.	**Particular**	**Strongly Disagree**	**Disagree**	**Slightly disagree**	**Slightly Agree**	**Agree**	**Strongly Agree**
1	**Small size of the market**						
a.	Low quality of public issue of share	1	2	3	4	5	6

b.	Lack of one window policy in pubic issue	1	2	3	4	5	6
c.	M\no diversity in issue companies	1	2	3	4	5	6
d.	Use of outdated technology in securities trading and clearing and settlement system	1	2	3	4	5	6
e.	No choice of instruments	1	2	3	4	5	6
f.	Low involvement of institutional investors in the market	1	2	3	4	5	6
g.	Long time gap between public issue and listing	1	2	3	4	5	6
h.	Slow speed of privatization	1	2	3	4	5	6
2.	**Poor Corporate Results**						
A	Poor Performance of listed companies from manufacturing and trading sector	1	2	3	4	5	6
b.	Poor corporate governance practice	1	2	3	4	5	6
c.	Inadequate accounting and auditing practice of issuer and listed companies	1	2	3	4	5	6
d.	Low level of professionalism in financial forecasting and under writing practice	1	2	3	4	5	6
e.	Poor performance of privatize enterprises	1	2	3	4	5	6
f.	Inadequate disclose practice of issuer and listed companies	1	2	3	4	5	6
3	**Poor regulatory infrastructure**						
A	Investor Protection mechanism is not adequately developed	1	2	3	4	5	6
B	Inadequacy in legal infrastructure on securities market	1	2	3	4	5	6
C	Improper handing of investor grievances	1	2	3	4	5	6
D	Inadequacy in accounting	1	2	3	4	5	6

	and auditing system and legalization						
E	Negative impact if Nepal Rastra Bank' s directives	1	2	3	4	5	6
4.	Low level of investors knowledge in securities market	1	2	3	4	5	6
A	Insufficient educative and awareness activities relating to the securities market	1	2	3	4	5	6
B	Investors are not aware and educated on risk and return aspect of securities market t	1	2	3	4	5	6
C	Absence of investment advisory and management companies	1	2	3	4	5	6
5	**Poor Performance of National economy**						
A	Low level of saving and investment in the economy	1	2	3	4	5	6
B	Bank oriented financing pattern	1	2	3	4	5	6
C	Low level of per capita income	1	2	3	4	5	6
D	Industrial slackness and security problems	1	2	3	4	5	6

Appendix No.2

Calculation of Subscription Ratios

Name of Issuing company	Securities	Public Flotation (Rs. In Million)	No. Of shares Issued	No. of shares applied	Over-subscription (Times)	Subscription (%)	Under-Subscription (%)
F/Y 1999/00 (2056/057)							
Alliance Insurance Co. Ltd.	Equity	20.00	200000			62.63	
Taragaon Regency Hotels	Equity	120.00	1200000	2965460	2.47	247.12	
Taragaon regency Hotels	Pref.	80.00	800000	1081380	1.35	135.17	
Pokhara Finance Ltd.	Equity	8.00	80000	212600	2.66	265.75	
Nepal Share Market Ltd.	Right	30.00	300000				

Total		258.00	2580000				
F/y 2000/2001 (2057/058)							
Universal Finance & Capital Market Ltd.	Equity	3.26	32600	147300	4.52	451.84	
Nepal Industrial & Comm. Bank Ltd.	Equity	175.00	1750000	14278639	8.16	815.92	
Nepal Merchant Banking & Finance Ltd.	Equity	50.00	500000	(Not Issued)			
Necon Air Ltd.	Right	89.60	896000	853980		95.31	4.69
Lumbini Finance & Leasing Co. Ltd.	Equity	24.00	240000	2775100	11.56	1156.29	
Paschimanchal Finance co. Ltd.	Equity	20.00	200000	259300	1.30	129.65	
Ace Finance Co. Ltd.	Right	15.00	150000	150000	1.00	100.00	
Sanarmatha Ins. Co. Ltd.	Equity	10.20	102000	3388610	33.22	3322.17	
Oriental Hotels Ltd. (Radisson)	Equity	150.00	1500000	9429027	6.29	628.60	
Total		**537.06**	**5370600**				
F/Y 2001/02 (2058/059)							
Siddhartha Finance Ltd.		8.00	80000	1417500	17.72	1771.88	
Nepal merchant Banking & Finance Ltd.		50.00	500000	23525457	47.05	4705.09	
Alpic Everest Finance Ltd.		5.00	50000	2108810	42.18	4217.62	
Nepal Bangladesh Finance & leasing co. Ltd.		7.50	75000	2442840	32.57	3257.12	
Narayani Finance Ltd.	Right	12.58	125800	153497	1.22	122.02	
Nepal Bank of Ceylon Ltd.		150.00	1500000	(Not Issued)			
Everest Bank Ltd.	Right	119.21	1192100			27.17	
Neal Devt. Bank Ltd.		48.00	480000	13950476	29.06	2906.35	
Bank of Katmandu Ltd.	Right	234.00	2340000	2300314		98.30	1.709
Total		634.29	6342900				
F/Y 2002/03 (2059/060)							
Himalayan Distillery Ltd (Publication)	Equity	173.48	1734800	183430		10.57	89.43
Himalayan Distillery Ltd. (Underwriters)	Equity	173.48	1734800	1551170		89.43	1057
Nepal Housing & Merchant Finance Ltd.	Equity	15.00	150000			100.00	
Union Finance Co. Ltd.	Equity	24.00	240000	2107980	8.78	873.39	
Development Credit Bank Ltd.	Equity	48.00	480000	6766630		1409.71	
Ace Finance Ltd.	Right	45.00	450000			100.00	
Nepal SBI Bank Ltd.	Right	287.87	2878700			97.26	
NIDC Capital Market Ltd.	Right	40.00	400000			95.00	
Nepal Bank of Ceylon Ltd.	Equity	150.00	1500000	(Not Issued)			
United Finance Ltd.	Equity	24.00	240000			1055.73	
Himalayan Bank Ltd.	Deb.	360.00	3600000				
Nepal Life Insurance co. Ltd.	Equity	50.00	500000			756.08	
Nirdhan Utthan Bank Ltd.	Equity	3.30	33000			388.12	
Everest Bank Ltd.	Pre.	140.00	1400000			141.68	
Int'l Leasing & Finance Co.	Equity	30.00	300000	6512000		2170.67	
Gorkha finance Ltd.	Equity	10.00	100000			864.45	
Shree Investment &	Equity	16.00	160000	22042		13.78	86.22

finace Co. Ltd.							
Total		**1416.65**	**14166500**				
F/Y 2003/04 (2060/061)							
Life Insurance Corporation (Nepal) Ltd.	Equity	50.00	500000	8717214	17.43	1743.44	
Nepal Srilanka merchant Bank Ltd.	Equity	40.00	400000	2461650	6.15	615.41	
NCM Mutual Fund	Fund	100.00	1000000				
Nepal Investment Bank	Right	57.24	572400			97.42	
Janaki Finance Co. Ltd.	Equity	8.00	80000	1263380	15.79	1583.89	
Central Finance Co. Ltd.	Equity	8.00	80000	681930	8.52	852.41	
Nabadurga Finance Co. Ltd.	Equity	8.00	80000	1161240	14.52	1451.55	
Premier Finance Co. Ltd.	Equity	8.00	80000	821090	10.26	1026.36	
Machhapurchhre Bank Ltd.	Equity	165.00	1650000	3272825	1.98	198.35	
Nepal Share Market and Finance Ltd.	Right	60.00	600000			85.35	
Mahalaxmi Finance Ltd.	Right	25.00	250000				
NB Insurance Co. Ltd.	Equity	20.00	200000	265420	1.33	132.69	
Peoples Finance Ltd.	Right	20.00	200000			56.69	
Butwal Finance Ltd.	Equity	20.00	200000	1607470	8.04	803.74	
OM Finance Ltd.	Equity	8.00	80000	1314260	1.43	1637.83	
Laxmi Bank Ltd.	Equity	192.50	1925000	4838550	2.51	251.35	
Standard Finance Co. Ltd.	Equity	24.00	240000	870090	3.63	362.54	
Total		**813.74**	**8137400**				
F/Y 2004/05 (2061/062)							
Alpic Everest Finance Ltd.	Right	20.00	200000			100.51	
Nepal Investment Bank	Deb.	300.00	3000000			102.28	
Cosmic Merchant Banking & Finance Ltd.	Equity	24.00	240000	1722780	7.18	717.83	
Kumari Bank Ltd.	Equity	150.00	1500000	12170299	8.11	811.35	
Siddhartha Finance Co. Ltd.	Right	20.00	200000			88.84	
Fewa Finance Co. Ltd.	Equity	8.00	80000	1884000	2355	2355.00	
Nepal Credit & commerce Bank Ltd.	Equity	210.00	2100000	2564140	1.22	122.10	
Prudential Insurance Co. Ltd.	Equity	20.000	200000	1913620	9.57	956.81	
NB Finance & Leasing Co. Ltd.	Right	30.00	300000			66.84	
Paschimanchal Bikas Bank	Equity	6.00	60000	1192800	19.88	2023.28	
Chhimek Bikas Bank	Equity	3.00	30000	41780	1.39	139.27	
Laxmi Bank	Equity	192.50	1925000	4831750	2.51	251.35	
Kish Merchant Banking	Equity	20.00	200000	360000	1.80	179.60	
Nepal Bangladesh Bank	Right	359.9245	3599245			95.26	
Total		**1363.4245**	**13634245**				
F/Y 2005/06 (2062/063)							
Nepal Bangladesh Bank Ltd.	Right	359.92	3599200			95.26	
National Hydropower Co. Ltd.	Equity	140.00	1400000			21.55	
World Merchant Banking & Finance Ltd.	Equity	24.00	240000	2316000	9.65	965.17	
Annarpurna Finance Co. Ltd.	Right	20.00	200000			97.33	

Birjung Finance Ltd.	Equity	24.00	240000	1689600	7.04	704.48	
Deprosc Development Bank Ltd.	Equity	3.48	34800	90132	2.59	259.34	
Everest bank Ltd.	Deb.	300.00	3000000			100.00	
Nirdhan Utthan Bank Ltd.	Right	15.00	150000			65.92	
Nepal SBI bank Ltd.	Right	215.93	2159300			96.50	
Nepal Investment Bank Ltd.	Right	295.29	2952900			99.04	
Everest Finance Ltd.	Equity	8.00	80000	432000	5.40	540.46	
Capital Merchant Banking & Finance Ltd.	Equity	28.00	280000	565600	2.02	202.49	
National Finance Ltd.	Right	43.20	432000			97.06	
Total		1476.82	14768200				
F/Y2006/07(2063/064)							
Chilime Hydro Power Co.Ltd.	Equity	237.41	2374100	12084169	5.09	509.84	
Development credit Bank Ltd.	Right Share	80.00	800000	766960		95.87	4.13
Prudential Bittiya Santha Ltd.	Equity	24.50	245000	276850	1.13	113.34	
Siddhartha Bank Ltd.	Equity	150.00	1500000	27975000	18.65	1865.33	
Bank of Kathmandu Ltd.	Debenture	200.00	2000000	2660000	1.33	133.31	
Srijana Finance Ltd.	Equity	4.00	40000	48400	1.21	121.08	
Kumari Bank Ltd.	Right Share	125.00	1250000	1912500	1.53	153.46	
Gandaki Development Financial Institution Ltd.	Equity	15.00	150000	595500	3.97	397.51	
Fewa Finance Co.Ltd.	Right Share	30.00	300000	292200		97.40	2.6
Business Development Financial Institution Ltd.	Equity	12.00	120000	2625600	21.88	2188.34	
Om Finance Co Ltd.	Right Share	30.00	300000	298980		99.66	0.34
Royal Merchant Banking &Fin Ltd.	Equity	17.50	175000	495250	2.83	283.30	
Goodwill Finance Ltd.	Right Share	25.00	250000	237400		94.96	5.04
Janaki Finance Co.Ltd	Right Share	10.00	100000	98330		98.33	1.67
Central Finance Ltd.	Right Share	12.00	120000	117984		98.32	1.68
Taragaun Regency Hotels Ltd.	Right Share	446.45	4464500	2564855		57.45	42.55
Bhajuratna Finance &Saving Co. Ltd.	Equity	10.50	105000	289800	2.76	274.36	
Guheswori Merchant Banking &Finance Ltd.	Equity	20.00	200000	426000	2.13	213.54	
Siddhartha Bikash Bank Ltd.	Equity	20.00	200000	444000	2.22	222.43	
IME Financial Institution Ltd.	Equity	17.50	175000	801500	4.58	458.46	
Shikhar Insurance Co.Ltd	Equity	25.00	250000	10937500	43.75	4375.86	
Bhrikuti Development Bank Ltd.	Equity	6.42	64200	137388	2.14	214.42	
Machhapuchere Bank Ltd.	Right Share	165.00	1650000	21235500	12.87	87.13	
Kist Merchant Banking &Finance Ltd.	Right Share	50.00	500000	10995000	21.99	78.01	
Nepal Share Markets &Finance Ltd.	Right Share	40.00	400000	363760		90.94	9.06

Nepal Investment Bank Ltd.	Debenture	250.00	2500000			100.00	
Nepal Industrial &Commercial Bank Ltd.	Debenture	200.00	2000000			100.00	
Patan Finance Ltd.	Equity	20.00	200000	232000	1.16	116.06	
Nepal SBI BankLtd	Debenture	200.00	2000000	2020000	1.01	101.20	
Total		**2443.28**	**24432800**				

Source: SEBO Annual Report, 2006/ 2007 and other information provided by SEBO

Appendix No. 3
Investment made by commercial Banks on government securities and common stocks and their growth rates.

Randomly Selected Commercial Banks	**2000/01**	**2001/02**	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2006/07**	Average Growth Rates
Nepal Investment Bank Ltd.	0.00	300.00	224.40	400.00	2001.10	1948.50	2522.3	
Government Securities	.	.	.	.	.	.	.	
Growth in Govt. Securities	.	1.1667	-0.252	0.7825	4.0028	0.00263	0.2944	0.9946
Shares, Debentures and Bonds,	12.69	12.69	13.89	13.89	13.89	.	17.74	
Growth in shares	.	0	0.0946	0	0	0.2772	0	0.0619
Other investments.	0.00	1657.58	1583.87	1291.35	1847.49	1967.95	3062.8	
Total Investment	**12.69**	**1970.27**	**1822.16**	**1705.24**	**3862.48**	**3934.19**	**5602.8**	
NABIL Bank Ltd.								
Government Securities	1233.82	2732.96	4120.29	3588.77	3672.63	2413.94	2301.46	0.2046
Growth in govt. Securities		1.215	0.5076	-0.129	0.0234	-0.3427	-0.0465	
Shares, debentures and bonds	16.12	18.82	22.22	22.22	22.22	440.28	104.19	3.0764
Growth in shares.		0.1675	0.1807	0	0	18.82	-0.7633	
Other investments.	1	4952.53	4057	2420.18	2141.22	1415.44	3772.8	
Total Investment	**1250.94**	**7704.31**	**8199.51**	**6031.17**	**5836.07**	**4269.66**	**6178.5**	
Standard Chartered Bank								
Government Securities	3338.67	4811.01	5784.72	6722.83	7948.22	7203.07	8635.87	
Growth in Govt. Securities		0.4409	0.2024	0.1622	0.1823	-0.0938	0.1989	0.1821
Shares, Debentures and Bonds,	11.19	11.19	11.19	11.19	11.19	13.35	15.3	
Growth in shares		0	0	0	0	0.193	0.1460	0.0565
Other investments.	0	4736.97	3.479.96	3623.66	3400.92	2486.14	4187.3	
Total Investment	**3349.86**	**9559.17**	**9275.88**	**10357.68**	**11360.33**	**9702.56**	12838.5	
Himalayan Bank								
Government Securities	2112.88	2224.3	3047.75	3998.87	3431.73	5469.73	5144.3	
Growth in govt. Securities		0.0527	0.3702	0.3121	-0.1418	0.5939	-0.0594	0.1879
Shares, debentures and bonds	9.46	10.69	34.27	34.27	34.27	39.91	39.91	
Growth in shares.		0.1264	2.2057	0	0	0.1646		0.4161
Other investments.	94.04	1848.17	6075.09	6142.3	5826.11	6182.7	5704.83	
Total Investments	**2216.41**	**4083.16**	**9157.11**	**10175.44**	**9292.11**	**11692.34**	**10889.03**	

Appendix No. 4
Investment made by Finance Companies on Government securities and common stock and their growth rates.

Randomly Selected Finance Companies	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	Average Growth Rates
Goodwill Finance Co. Ltd.								
Government Securities	27.64	37.70	41.82	46.5	25.95	35.48	25.6	
Growth in Govt. Securities		0.3640	0.1093	0.1119	-0.4419	0.3672	-0.2784	0.0386
Shares, Debentures and Bonds,	13.25	24.45	23.93	22.04	11.86	7.39	7.07	
Growth in shares		0.8653	-0.0213	-0.0790	-0.4619	-0.3769	-0.0433	-0.1371
Other investments.	2.55	0.60	3.00	8.40	0.03	0.03	15.23	
Total Investment	**43.44**	**62.75**	**68.75**	**76.94**	**37.84**	**42.90**	**47.9**	
Nepal Merchant Banking & Finance co. Ltd.								
Government Securities	208.39	208.39	320.19	449.3	724.15	487.88	440.83	
Growth in govt. Securities		0.0000	0.5365	0.4032	0.6117	-0.3263	-0.0964	0.1881
Shares, debentures and bonds	2.59	1.74	19.14	17.39	17.79	6.19	6.19	
Growth in shares.		-0.3282	10.0000	-0.0914	0.0230	-0.6521	0	1.4918
Other investments.	120.11	208.74	171.4	187.64	253.81	20.2	325.73	
Total Investments	**331.09**	**418.87**	**510.73**	**654.33**	**995.75**	**514.27**	**772.75**	
Kathmandu Finance Co. Ltd.								
Government Securities	4.90	4.90	1.75	1.75	1.75	0.00	0.00	
Growth in Govt. Securities		0.0000	-0.6429	0.0000	0.0000	-1.0000		-0.2738
Shares, Debentures and Bonds,	1.59	4.24	4.96	4.94	4.98	1.72	1.54	
Growth in shares		1.6667	0.1698	-0.0048	0.0089	-0.6546	-0.1046	0.1802
Other investments.	9.40	14.00	20.50	13.5	14.50	29.50	75.7	
Total Investment	**15.89**	**23.14**	**27.21**	**20.19**	**21.23**	**31.22**	**77.28s**	
Peoples Finance Co. Ltd.								
Government Securities	9.00	9.00	9.00	5.00	0.00	0.00	0.00	
Growth in govt. Securities		0.0000	0.0000	-0.4444	-1.0000	0	0	-0.2407
Shares, debentures and bonds	2.00	2.00	2.00	11.12	11.14	3.09	3.09	
Growth in shares.		0.0000	0.0000	4.5600	0.0018	-0.7226	0	0.6398
Other investments.	21.56	30.94	32.12	24.00	7.00	5.00	5.00	
Total Investments	**32.56**	**41.94**	**43.12**	**40.12**	**18.14**	**8.09**	**8.09**	

Appendix No. 5
Primary Data - Descriptive Statistics.

Gender		
Male	40	69.0%
Female	18	31.0%
Age		
Below 30	19	32.8%
30 and above	39	67.3%
Education		
Under-graduate	9	15.5%
Graduate	30	51.7%
Post-graduate and above	19	32.8%
Employment status		
Unemployed	7	12.06%
Job Holder	37	63.79%
Self Employed	11	18.96%
Retired	3	5.17%
Category		
Less - informed	18	31.03%
Informed	25	43.1%
well - informed	8	13.8%
Analyst / Professional	7	12%

Appendix No.6

Frequency table showing major investment alternatives in Nepalese capital market.

Investment alternative	Frequency	Percent
Corporate Securities	31	53.2
Government Securities	13	22.4
Real estate	8	13.8
Bullion	6	10.3
Total	**58**	**100.00**

Appendix. No. 7

Frequency table showing major financial instruments in Nepalese capital market.

Financial Instruments	Frequency	Percent
Common Stock	22	37.9
Government Bond	11	19.0
Preference Share	9	15.5
Debenture	7	12.1
Mutual funds	5	8.6
Treasury Bills	4	6.9
Total	**58**	**100.00**

Appendix No.8

Frequency table showing Preference of investors over Investment Sectors

Investment Sector	Frequency	Percentage
Commercial Banks	31	53.4
Financial companies	10	17.2
Insurance companies	7	12.1
Development banks	5	8.6
Manufacturing and processing companies	2	3.4
Trading companies	2	3.4
Hotels	1	1.7
Total	**58**	**100**

Appendix No.9

Consideration for corporate security investment

Factor	Frequency	Percentage
Companies goodwill	28	48.3
Forecasted profit	18	31.0
Friends and relatives motivated them	8	13.8
Advertisement appealed	3	5.2
Because most of people are buying it	1	1.7
Total	**58**	**100**

Appendix No.10

Preference of investors over stock investment stock

Stock investment factors	Frequency	Percentage
Dividend	14	24.1
Capital gain	29	50.0
Bonus share	9	15.5
Representation in board	2	3.4
voting right	4	6.9
Total	**58**	**100**

Appendix No.11

Frequency table showing investment on government security

Marketability	5	12.5
No risk/Safety	32	80
NRB Notices	2	5
Friends and relatives	1	2.5
Whim and rumor	0	0
Total	**40**	**100**

Appendix No.12

Calculation of Chi-square

Observed Frequency (0)	Expected frequency(E)=$\frac{R \times C}{N}$	(0-E)	$(0-E)^2$	$\frac{(0-E)^2}{E}$
3	$\frac{9 \times 18}{}$ =2.793	0.207	0.0428	0.015

	58			
4	$\frac{9\times25}{58}$ =3.879	0.1221	0.464	0.000377
1	$\frac{9\times8}{58}$ =1.24	-0.24	0.0576	0.0464
1	$\frac{9\times7}{58}$ =1.08	-0.08	0.00064	0.0005925
10	$\frac{30\times18}{58}$ =9.31	0.69	0.4761	0.0511
15	$\frac{30\times25}{58}$ =12.93	2.07	4.761	0.331
3	$\frac{30\times8}{58}$ = 4.13	-1.13	1.2769	0.309
2	$\frac{30\times7}{58}$=3.62	-1.62	2.6244	0.72
5	$\frac{19\times18}{58}$ =5.89	-0.89	0.7921	0.1344
6	$\frac{19\times25}{58}$ =8.18	-2.18	4.7524	0.580
4	$\frac{19\times8}{58}$=2.62	1.38	1.9044	0.7268
4	$\frac{19\times7}{58}$ =2.29	1.71	2.92	1.2768
				χ^2=4.1915

Degree of freedom = (r-1) (c-1)
= (3-1) (4-1)
= 2×3 = 6

Appendix No. 13

Calculation of Chi-Square

Observed Frequency (0)	Expected frequency(E)=$\frac{R\times C}{N}$	(0-E)	$(0-E)^2$	$\frac{(0-E)^2}{E}$
2	$\frac{9\times24}{58}$=3.724	-1.724	2.972	0.798
7	$\frac{9\times34}{58}$ =5.2754	1.724	2.55	0.4848

9	$\frac{30\times24}{58}=12.4137$	-3.4137	11.65	0.9388
12	$\frac{30\times34}{58}=17.5862$	3.41	11.653	0.66
13	$\frac{19\times24}{58}=7.862$	5.137	26.38	3.356
6	$\frac{19\times34}{58}=11.137$	-5.137	26.39	2.370
				$\chi^2=8.6075$

Degree of freedom = (r-1) (c-1)
= (3-1) (2-1)
= 2×1
= 2

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