Market Guide
In collaboration with SEC

Are you an informed investor?

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Knowledge empowers people. Similarly adequate knowledge about the stock market will strengthen your portfolio and enable you to maximize your returns. Adequate knowledge requires investors to be informed about all aspects of investing. Today's article will focus on certain areas of investing in the stock market that many investors are not familiar with.

Crossings

An equity market will attract various types of investors. Some of them deal with large-scale transactions. There are various strategic reasons for such investors to favour large-scale transactions. For an example, certain individuals might want to take over the ownership of a company, thus might intend to purchase a large portion of shares.

As our readers are aware, the local market is relatively small. Liquidity levels are also relatively low. In such a context, it might not be that easy to buy a large quantity of a given security from the market at once. Even if they do, a large order will have to be filled up with a large number of small quantities. This would increase transaction cost (brokerage) for the buyer and impact cost (this type of cost is used by large financial institution to determine the viability of a security that is purchased).

Thus authorities introduced ‘Crossings’ in the late 1990s to facilitate large-scale transactions with the aim of mitigating the aforementioned drawbacks.
A ‘Crossing’ is a large transaction executed on a separate board instead of the ‘Normal Board’ of the ATS. For an example, if there is an investor (local or foreign), who intends to buy a large quantity of a listed company, the investor might contact the major shareholders either directly, through a stock brokering firm or any other party and negotiate on the price and quantity. It is important to note that the price and quantity are pre-determined and the ‘Crossing Board’ is used to execute the transaction. Yet, it cannot be at a price below 5 percent of the closing price of the said security.

In the case of debt, the ‘Crossing’ cannot take place at a reference price less than 2 percent. Further on, in order for the transaction to be traded in the ‘Crossing Board’, the quantity should be more than 5 percent of the issued quantity of the listed company or the total value of the transaction should be greater than Rs.20 million. Orders placed on the ‘Crossing Board’ will not be visible in the normal market data displays; hence, will not put price pressure on other trading. The trade will be displayed as an execution. ‘Crossings’ on equity securities will not update the indices and closing price.

It is important for retail investors to pay attention to ‘Crossings’, especially if they have invested in that company. Information on ‘Crossings’ will be published on the Colombo Stock Exchange (CSE) website. If possible infer into the reason for such transactions and the investors involved in these transactions. A word of caution is given to our readers - never blindly enter/exit a stock simply because high-net-worth-investors were involved in the ‘Crossing’ transaction.

Default Board

Listed companies raise public money by issuing shares through an Initial Public Offering. Accordingly, the Securities and Exchange Commission of Sri Lanka (SEC) and the CSE are entrusted with the duty of safeguarding the interest of investors. Thus, they have imposed certain rules and best practices for listed entities to abide with.

If certain rules of the CSE are violated by the listed entity, such company will be transferred to the ‘Default Board’. The CSE may publicly reprimand the company and/or suspend trading of stocks for any period of time and/or delist the entity from the exchange. For an example, if a listed company fails to submit its annual report within five months of the financial year, the company would be transferred to the ‘Default Board’. Once it complies with the relevant provisions, it will be transferred back to the original board (Main Board or Diri Savi Board).

In the case of debt, there can be various reasons for it to be transferred to the Default Board. For an example, a company will be transferred to the Default Board if it fails to pay interest on the debt securities on the ‘due date’.

The securities shall be transferred out of the Default Board when it complies with the relevant listing rules. In the event the security continues to be on the Default Board for a period in excess of one month, the CSE in consultation with the SEC has the right to issue a press notice informing the public of the nature of the violation. If the securities continue to be on the Default Board for a period in excess of three months from the date of transferring the securities of the company to the Default Board, the CSE, at its discretion, may refer the matter to the SEC for necessary action.

The Default Board was introduced in the 1990s as a ‘red light’ for investors when investing in the stock market. It does not mean that investors should stop purchasing shares of a company that is on the Default Board. Instead, they have to be cautions when investing in such stocks. It is best to infer in to the reasons for the transfer and make calculated judgments prior to investing. We saw how certain investors blindly entered companies that were on the Default Board for serious violations of listing rules. As a result, many had to incur financial losses.

It is also important to note that companies are listed and traded only on the Main Board and Diri Savi Board. The Default Board is used only to transfer listed entities that violate listing rules.

Trading halts and suspensions Trading halts

A ‘Trading Halt’ is a temporary suspension in the trading of a particular security for a certain time period, usually in anticipation of a news announcement or to correct an order imbalance. A trading halt can also be imposed for purely regulatory reasons. A trading halt gives all investors equal opportunity to evaluate news and make buy, sell or hold decisions on that basis. The duration of a Trading Halt will be decided by the CSE or the SEC as the case may be and may be extended beyond one market day.

The CSE can at its discretion impose a Trading Halt on the securities of a listed entity in the following situations:

- Before an announcement of any price sensitive information of a listed company.
- To obtain a clarification from the company on a rumour/report regarding the company.
- When an unusual movement in price/volume of a security is noted.
- If it is necessary for the purpose of disseminating information.
- When directed by the SEC.

Suspensions

A stoppage in the trading of a security for an extended period of time is referred to as a suspension. This normally occurs when there is a lack of material financial information on the security. Once the security is suspended, shares of that security cannot be traded on the market until the suspension is lifted or lapses.

The CSE can at any time suspend the trading of securities of a listed entity if according to its opinion is faced with the following:

(i) The company is unable or unwilling to comply with or violates a listing rule

(ii) The CSE rules require the suspension

(iii)By operation of law the SEC may at its sole discretion direct the CSE to suspend the securities of any listed entity.

Circulars to shareholders Interim financial statements

Listed companies should give the CSE for public release, an interim financial statement prepared on a quarterly basis (financial statements), as soon as the figures have been approved by the board of directors of the company and in any event not later than 45 days from the end of the first, second and third quarters and two months from the end of the fourth quarter.

Most investors are in the habit of referring only the annual report. However, it is equally important to analyse interim financial statements as the information given is more up to date when compared to annual reports. Nevertheless, bear in mind that interim financial statements are not audited. Thus, you should be cautious when using these documents.

Annual reports

Listed entities are expected to send an annual report to all shareholders. Annual reports are often cumbersome but entail information that is required for investment decision-making. You can also read the annual reports by accessing the website of the CSE. When reading these reports it is advisable to pay attention to the following:

- Principal activities of the entity and its subsidiaries during the year and any changes therein.
- The names and the number of shares held by the 20 largest holders of voting and non-voting shares, the percentage of such shares held and the public holding percentage.
- Key financial statements.
- Relevant equity ratios (dividend per share. dividend payout, net asset value per share, market value per share) and debt ratios (debt/equity ratio, interest cover, quick asset ratio).
- Any changes in credit rating (for the entity or any other instrument issued by the entity), if applicable.
- Significant changes in the entity's or its subsidiaries' fixed assets.
- Relevant information if during the year the entity has raised funds either through a public issue, rights issue or private placement.
- Employee share option schemes and employee share purchase schemes.
- Disclosures pertaining to corporate governance.

- See more at: http://www.dailymirror.lk/89981/are-you-an-informed-investor#sthash.MBY1ZUPR.dpuf