Share Trading

Strategy — GICS, indexes, sectors

Introduction

When looking for feasible investing alternatives, it can be useful to focus on the stocks within specific market sectors. Conversely, there might be a good reason to ignore the stocks in a specific sector.

For example, if the economy is such that several key retail companies are suffering, then it might be reasonable to conclude that many stocks in the retail sector could be at risk of poor company performance. Investing in these stocks might be a high-risk in the short term.

Therefore, it can be very useful to understand how similar companies are classified (that is, by market *sectors*), and how to identify similar companies.

This Article in Brainy's series on Share Trading (number ST-6250) explains the idea of industry *sectors*, and the *Global Industry Classification Standard* (GICS) coding system. It provides a discussion about comparing the share price of a company to both it's own sector index, and to similar companies. It also explains how to find out which companies are classified together within GICS *sectors*.

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What are market indexes?

Market *indexes* are entities that allow investors to gain an insight into the performance of an entire *asset class*, or a segment of that asset class. Some indexes group together the companies with a somewhat similar market capitalisation, while other indexes group together the companies which operate in similar industries. So, each index comprises a list of companies that make up the index, and the index is assigned an overall value so that a price chart of the index can be produced.

Many investors use an index to compare the performance of any one company to it's peers in the same class. Indexes can also be used as the underlying entity for various financial instruments (such as CFDs) and to benchmark the performance of portfolios designed to replicate the performance of a given asset class. By trading index futures, options, warrants, CFDs, and the index-tracking Exchange Traded Funds (ETFs) an investor could gain exposure to the performance of the index or could even hedge an existing portfolio.

Key features of indexes

The market indexes are designed to be broad measures of performance of a particular asset class, or a subset of an asset class. So that indexes are widely adopted, the methodology used to create an index is often published so that stakeholders can gain an understanding of the underlying philosophy behind the index and it's calculation. Also, indexes are sometimes designed to be investable. This means that constituent securities must be relatively easily tradeable so that index tracking portfolios can be created (hence listing rules such as those related to liquidity). For more details refer to the Standard & Poor's web site[1].

Types of indexes

There are several broad types of indices[2]:

- Capitalisation indices
- Sector indices
- Residential property indices
- Fixed income indices
- Strategy indices
- Volatility indices.

In this Article below we will only concentrate on the first two index types in this list.

1 Standard & Poor's — www.standardandpoors.com/indices/main/en/us
2 More detail about types at: www.asx.com.au/products/types-of-indices.htm

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