

### ALL ABOUT FREE FLOAT OF A COMPANY:

It is Important to view free float?



In finance, the **free float** of a company is defined as those shares that are readily available for trading. The concept of free float is particularly important for assigning a weight to a listed company in the calculation of an index.

In practice the number of readily available shares is calculated by subtracting the number of restricted shares from the total number of shares in issue for a particular company. The definition of restricted shares varies depending on the particular index being calculated.

In general the definition for restricted shares include some or all of the following categories:

- Promoters holdings,
- Government holdings.
- Directors holdings.
- Strategic holdings.
- Shares listed on a different exchange.

- Share holdings larger than a certain percentage (e.g. 5%).

**Calculated as:**

$$\text{FFM} = \text{Share Price} \times (\# \text{ Shares Outstanding} - \text{Locked In Shares})$$

### ***Free-Float Methodology***

The free-float method is seen as a better way of calculating market capitalization because it provides a more accurate reflection of market movements. When using a free-float methodology, the resulting market capitalization is smaller than what would result from a full-market capitalization method.

## **Free float: indicator of a stock's liquidity, helps decide its price**

The outstanding shares of a listed company are like an elephant's tusks. The more they grow, the more impressive they look. But what's the use of keeping a long knife if you can't use it in your day-to-day life? Similarly, a large number of outstanding shares in itself can't be of much use to investors unless it also leads to an increase in what we call "free float".

In our day-to-day analysis of different factors affecting the market, we often forget that "free float" also plays a crucial role in deciding the price of a stock.

**Johnny:** OK! "Free float" plays an important role. But can you first explain, Jinny, what exactly a free float is?

**Jinny:** Free float is that portion of the outstanding shares of a listed company that is actually available for day-to-day trading by investors. Normally, all outstanding shares are not available for trading. For example, a listed company may have 10 million outstanding shares, of which only six million may actually be available for trading.

The six million shares would be referred to as free float in market terminology. But you may ask, where did the remaining shares go? The remaining shares certainly didn't vanish into thin air. They may be lying with the promoters of the company or some other strategic investor interested in the management of the company or some other long-term institutional investor, who may not be interested in day-to-day trading.

The shares which are not available for day-to-day trading are called "restricted shares". The decision for not trading the restricted shares by promoters or strategic investors may be voluntary sometimes, but many times, restricted shares are actually forbidden from trading due to a "lock-in period" imposed by some legal requirement.

**Johnny:** So it all boils down to how much free float a company has. Is there any method by which we can estimate the free float of a company?

**Jinny:** Many websites provide market information about listed companies which also contains their shareholding pattern and free float. You can yourself estimate the free float of any listed company, but for that you need to pay closer attention to its annual report, which discloses the shareholding pattern of promoters, strategic investors and others.

For an up-to-date estimate, you can also check the quarterly shareholding pattern submitted by listed companies to stock exchanges. It would be better if you keep a watch on public announcements made by companies from time to time, regarding investments or disinvestments by promoters or strategic shareholders.

Once you know how many shares are lying with long-term investors, you can subtract that from the total outstanding shares of a company to arrive at its free float. Collecting all this information no doubt requires effort, but the major challenge lies in identifying long-term investors.

Other than promoters and self-declared strategic investors, how would you know a particular investor is maintaining his holding due to some long-term business strategy and not for trading? To arrive at a reasonable conclusion, use a few rules.

Shareholding of government or state agencies in any company is considered to be of long term. Likewise, shareholding acquired through private placement or any acquisition requiring disclosure and open offer under the takeover code could be considered to be long term.

Investment made under the foreign direct investment, or FDI, category and equity held by associate or group companies can also be considered to be long term.

**Johnny:** So, estimating free float really requires more effort than doing two plus two. But tell me, Jinny, why is free float considered that important?

**Jinny:** It is important to know about the free float of a listed company because it's an indicator of a stock's liquidity. A more liquid stock can be traded at a lower cost and in less time. A lower free float is a sign of low liquidity, which affects both buyers and sellers.

The more the number of shares available for trading, the more buyers and sellers are able to take part in the market. A small free float means that a lower number of shares is actually available for trading, which makes it much more difficult to match buyers and sellers at their chosen price and time.

For this reason, many investors avoid illiquid stocks. Sometimes buyers are not able to find enough sellers, and sometimes sellers are not able to find enough buyers. Such a situation may lead to price volatility.

Scarcity of shares may, in fact, artificially push up the prices. A small free float means that even a small rise in demand may push up the prices.

It would take much less pull to affect the price of a few thousands shares than it would take to affect millions. A dangerous situation for both buyers and sellers because once the demand ceases, the

prices fall back with equal rapidity. So those interested in buying a stock having a small free float must keep this aspect in mind.

**Johnny:** Thanks for your words of caution, Jinny. Shallow waters may hold nasty surprises.

**What:** The “free float” of a listed company denotes shares that are actually available for day-to-day trading.

**How:** Free float can be estimated by analyzing the shareholding pattern, as published in the annual report or quarterly information submitted to stock exchanges and announcements made from time to time.

**Why:** Free float has an impact on prices because it affects stock liquidity.

Financial Services	Free Float
Icici bank	102291.35
Hdfc bank	68203.57
Housing development finance pvt.ltd	68193.84
State bank of india	52927.35
Axis bank	28343.92
Infra Dev.fin.co.ltd	15371.85
Punjab national bank	13109.18
Kotak mahindra bank	12036.69
Reliance capital	8745.3

Metals	Free Float
Tata Steel	41899.29
Sterlite Industries (India) Ltd	34201.05
Jindal Steel & Power Ltd.	28260.9
Hindalco Industries Ltd	22971.42
Steel Authority of India	13316.15

Energy Services	Free Float
Reliance industries	184465.57
Oil & natural gas corporation	35067.42
Tata power co ltd	21837.53
Ntpc ltd	18130.51
Gail india ltd	18108.88
Reliance infrastructre ltd	15741.41
cairn india	13241.69
reliance power ltd	5734.66
Power grid corporation of india ltd	6178.4
Bharat Petroleum	6565.42

Automobile	Free Float
Mahindra & Mahindra Ltd	21452.45
Tata Motors Ltd	21053.23
Maruti Suzuki India Ltd.	17923.53
Hero Honda Motors Ltd	17566.29

Construction	Free Float
Larsen & Turbo Ltd.	94665.12
DLF Ltd.	12250.02
Unitech. Ltd.	10765.06

Pharma	Free Float
Cipla Ltd	16755.51
Sun Pharmaceutical Industries Ltd	13522.92
Ranbaxy Laboratoreis Ltd	6896.97

Telecom	Free Float
Bharti Airtel Ltd.	37153.36
Idea Cellular Ltd.	11568.23
Reliance Communications Ltd.	11418.41

Cement	FreeFloat
JaiPrakash Associates Ltd.	17366
Ambuja Cements Ltd.	9762.18
Acc Ltd.	9485.3

Consumer goods	Free float
ITC	68429.94
Hindustan Unilever Ltd.	23598.08

Industrial manufacture	Free Float
Bharat Heavy Electricals Ltd.	39962.24
Siemens Ltd.	11140.51
ABB Ltd.	8463.59
Suzlon Energy Ltd.	5292.18

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