Timing the market

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Volatility in the equity market has drawn many investors away from the equity market. However, the expanding IPO market has seen a number of different kinds of businesses getting listed on NSE and BSE enabling investors to hold a well-diversified portfolio. Now, diversification does help in hedging the portfolio against unsystematic risk, that is, business risk, but one cannot hedge oneself against systematic risk, that is, the market risk.

Let us dig deeper and analyse how the NIFTY has fared in terms of volatility from 1997-98 to 2017-18. I was analysing the equity market data for the past 20 years and observed that the volatility has only gone down in the recent years. If you compare the 52-week high/low of the NIFTY, the average volatility in the last 5 years was around 29% as compared to 20 years back, in 1997-1998 when it was 40%. This implies a marked improvement in terms maturity of the Indian Equity Market and almost in line with the US market where the average volatility is around 24%. It would, thus, be fair to assume that investing in Indian equity market has become *less risky* as it was, say, 20 years ago. These numbers are significant because it reflects the confidence of investors on the Indian equity market, that has grown in the recent past.

Now before you draw conclusions that Indian equity is now turning into a flower bed with higher returns and lower volatility, let me share with you some numbers on how the midcaps have fared so far… NIFTY Midcap rose 34.85% in FY17 and then further rose 27% and hit a lifetime high at 21840.85 on 15th of January, 2018 since FY17. Nifty Midcap has since corrected 19% when it hit a year low of 17700.90 on 17th July, 2018. This translates into a volatility of more than 36% in FY17 and 28% in FY18. It is interesting to see how volatility itself is so volatile when it comes to NIFTY Midcap.

One can argue that if you had invested Rs. 100 in NIFTY Midcap on 1st April, 2016 and exited on 15th Jan, 2018 when NIFTY Midcap hit its lifetime high, you would have earned an absolute return of 71.26% (CAGR 35%). It is easy to calculate such returns while doing a post facto analysis as actually earning that return is possible only if one has the supernatural power of perfectly timing the market. Because, if you chose to remain invested, you would have lost 23% already till 31st July, 2018 since its lifetime high. Taking a closer look reveals that there are plenty of stocks that have corrected more than 50% and hit fresh 52-week lows this year in FY19. That is the sort of wonder that timing the market does.

The current market scenario is eerily similar to year 2008 when the market crashed to record lows. As per statistics, only 54 percent of the total stocks are trading above their 200-day daily moving average (DMAs), which is the second lowest in a decade. During the 2008 highs, 52 percent of stocks traded above their 200 DMAs. With nearing elections and global trade wars, the market continues to remain volatile. The initial crash of Feb 2018 was triggered by the budget instigating mass sell offs by foreign investors which has been eventually balanced by huge buys by domestic buyers. Further, stellar performances from large caps have helped the NIFTY touch fresh highs post Q1 of FY19

So, the question is, does investing in equity give you a desired return after having taken all the risk? Does the return justify the Risk-Return relationship?

While it is impossible to time the market perfectly, it is undeniable that experience does help to a certain extent. Experience together with knowledge helps in identifying growth stocks and value stocks, that beats the NIFTY when held for a longer period of time.

In addition, an in-depth fundamental analysis of companies is very important before purchasing a stake in the same. Also, one should put prime focus on the quality of management, their vision, enthusiasm and passion to drive their companies to new highs. In an era of rising bank frauds and corporate frauds, corporate governance reports give us an insight into the morale values of the management so as to judge, how diligent they might be in order to stay away from unfair trade practices. These factors have significant implications in the long run, if an investor plans on to hold a stock for a very long term, say 10 years or more. Reduced volatility gives investors more comfort in investing a larger proportion of their wealth in equities for the long term, for the high net-worth individuals, both Indians and NRIs.

Like, as Warren Buffet says, "*Our favourite holding period is forever*."

Personally, I do not bet on timing the market and do my share of research before buying stake in a company. I believe, timing the market is rather gambling. While we do have modern tools for technical analysis of the market, but only to bet better. You win or you lose.