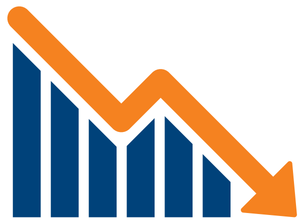
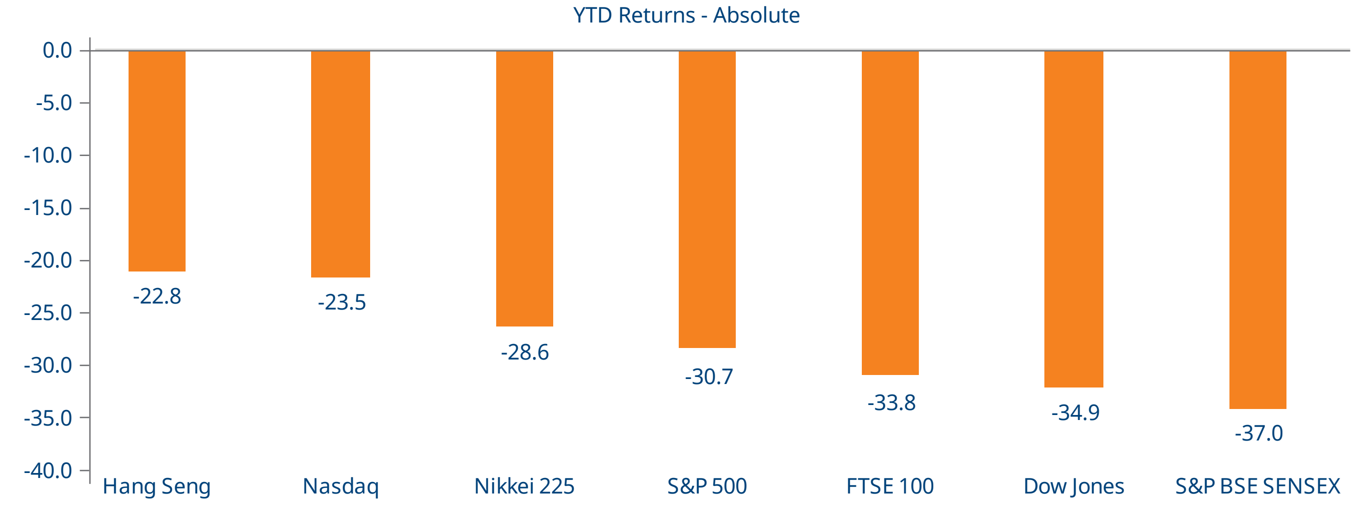
An Investor Education Initiative
MIRAE ASSET
Mutual Fund
by Mirae Asset Knowledge Academy

HOW TO INVEST IN VOLATILE MARKET?

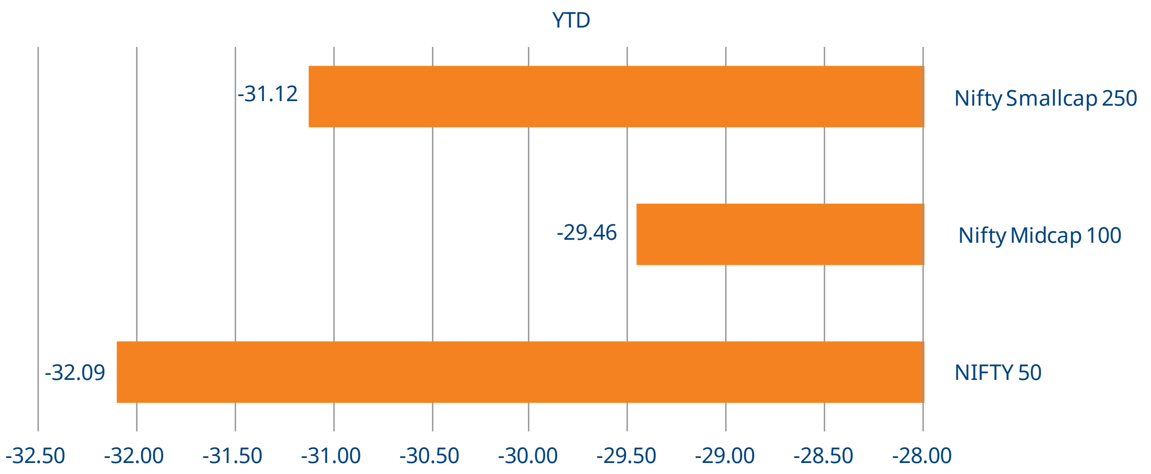
The last one month may have been scary for many investors especially those who are facing a full blown bear market for the first time. In the last one month, Nifty 50 has fallen 32% and is trading below 8000. The last time we saw Nifty below 8000 was back in 2017. We are not alone in this situation. The rapid spread of Coronavirus around the world has badly affected market sentiments. Most of the major stock indices including Dow Jones, S&P 500, Nikkei, FTSE, DAX, etc have fallen nearly 20% by more than 30%.





Source: Yahoo Finance. Note that, even though Hang Seng fell 14% in last one month, it had fallen 10% in January when Coronavirus was mostly limited to China. Data as on 15th Feb 2020 to 19th Mar 2020.

Over the past 5 years, we have seen bouts of high volatility but it was limited to particular market segments. In 2015 – 16 correction, large caps were affected the most but midcap funds gave positive returns. In 2018 – 19 correction, mid and small caps were affected but large cap funds were able to give stable returns. In a full blown bear market, all market segments are affected but you should know that we have seen this several times in the past.

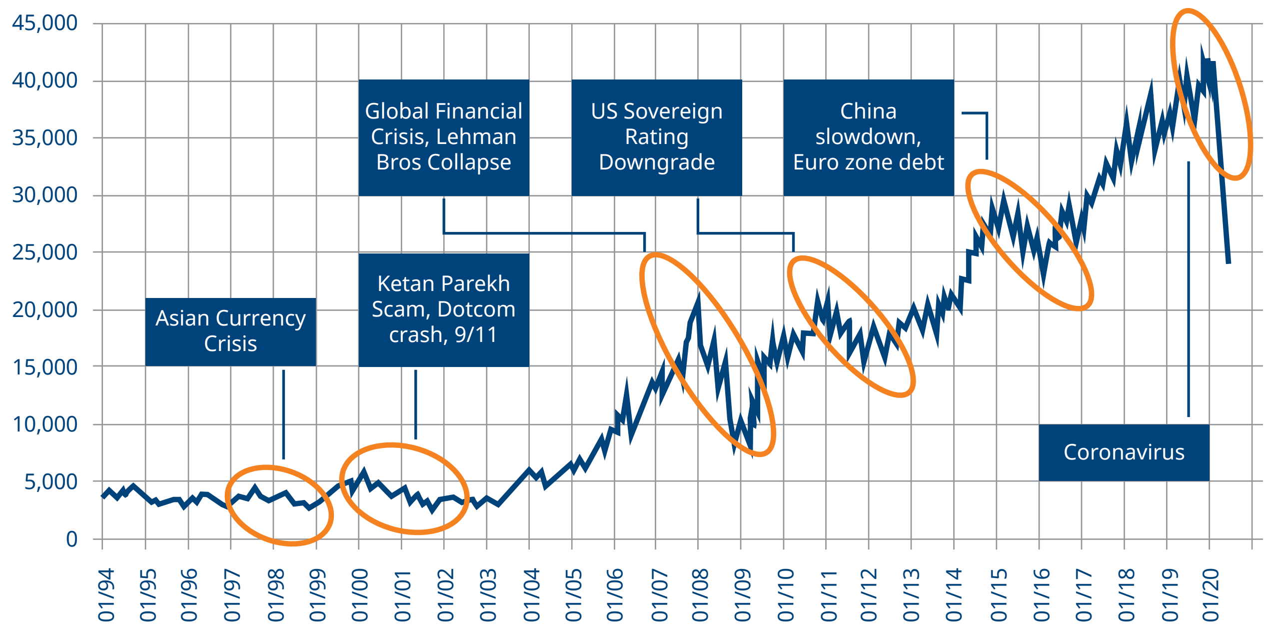


Source: National Stock Exchange. Data as on 15th Feb 2020 to 15th Mar 2020.

History of Indian stock market

Many investors are experiencing this situation for the first time, but if you go back into the history of Indian stock market, you will see that we have seen bigger corrections than the one we are see right now. The chart below shows the price history of Sensex and the major corrections over the last 25 years. We had 5 major corrections (ranging from 20% to 60%) during this period, not including the crash after NDA lost 2004 election (because the market recovered very quickly).

Sensex 25 year price history



Source: Bombay Stock Exchange. Data as on 1st Jan 1994 to 18th Mar 2020.

The chart above shows that equity as an asset class can be extremely volatile in the near to moderate term but at the same time can create wealth in the long term irrespective of market cycles. Over the last 25 years, the Sensex has multiplied nearly 10 times, despite several economic downturns and severe financial crises. In this article, we will discuss how to invest in volatile market.

Do not panic – be patient

It is understandable that you may feel stressed when your investments plummet in value. It is after all, your hard earned money. But if you panic, you may make wrong decisions which will impact your financial interests in the long term. Losses in equity funds are notional if you remain invested – they are likely to eventually recover. If you panic and sell, you will make your loss permanent. You should understand that while price destruction in bear markets can be severe, they do not last very long. Further, the recoveries from bear market bottoms in the past have been quite sharp. Simply being patient and not panicking in bear markets can be enormously beneficial for your financial interests.

Bear Market Period	Length of Bear Market	% Correction from peak	% recovery from bottom in 1 year
1998 – 1999	9 months	-39%	40%
2000 – 2001	20 months	-34%	16%
2008 – 2009	14 months	-60%	109%
2011 – 2012	9 months	-28%	18%
2015 - 2016	11 months	-22%	26%

Source: Advisorkhoj Research

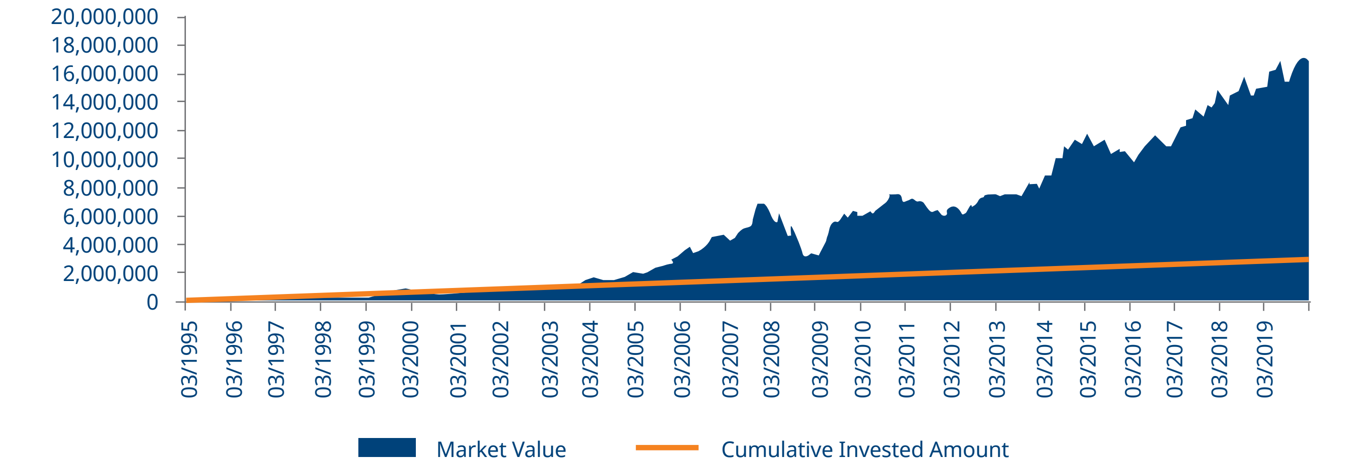
Remain disciplined – invest systematically

Volatility is part and parcel of equity as an asset class. Systematic investing is the best form of financial discipline and it may reap rich rewards during bear markets through rupee cost averaging as you will be investing systematically at low valuations. If you stop your SIPs in volatile market, you will not be able to take full advantage of Rupee Cost Averaging. The table below shows the value of Rs 10,000 monthly SIP investments made for 1 – 2 years during bear market periods, after 5 years. As shown in the table below, you can be deprived of substantial amounts of profits in the long term if you stop your SIPs. In fact, bear markets are the best times for your SIP as you can get very high profits from the investments made during that period.

SIP Period	Cumulative Investments	Investment Value – 5 years later
Apr 1998 - Apr 1999	1,20,000	2,28,383
Feb 2000 - Feb 2002	2,40,000	9,28,068
Jan 2008 - Jan 2009	1,20,000	1,86,010
Nov 2010 - Nov 2011	1,20,000	2,36,208

Source: Advisorkhoj Research. Data as on 1st Apr 1998 to 31st Nov 2016.

The chart below shows the returns of Rs 10,000 monthly SIP made in the Sensex over the past 25 years. With a cumulative investment of Rs 30 lakhs you could have accumulated a corpus of nearly Rs 1.7 crores, despite several market crashes and severe global crises e.g. Asian currency crisis, dotcom bubble, 9/11, SARS, global financial crisis in 2008, Eurozone debt crisis etc, apart from local risk factors.



Source: Advisorkhoj Research. Data as on 1st Mar 1995 to 1st Mar 2020

Use simple & smart strategy to buy on dips – STP

Many investors may have lump sum funds available for investments but may feel scared to invest or may want to time the market. Investors should understand that market bottoms are almost impossible to predict. If you are worried about volatility then you can use mutual fund Systematic Transfer Plan (STP), whereby you invest your lump sum money in a low risk debt mutual fund e.g. liquid fund and then transfer funds systematically to an equity fund of your choice over a period of time e.g. 3 months, 6 months, 1 year etc depending on your outlook on volatility. By investing through the STP mode, you can take advantage of volatility through Rupee Cost Averaging and also aim to benefit from liquid fund returns which may be higher than savings bank interest rate.

We will show the benefits of STP for the 3 major corrections i.e. 2000, 2008 and 2011. Let us assume you invested Rs 3 lakhs lump sum in a liquid fund and transferred Rs 25,000 every month to Sensex for one year. After the end of the STP period, you switched the remaining balance of the liquid fund to Sensex. Let us further assume liquid fund returns are equal to 1 year bank FD interest rates. The table shows the investment values of such STPs after 5 years. You can take advantage of smart investment options to maximize the returns of your bear market investments while minimizing risks at the same time.

SIP Period	Cumulative Investments through 1 year STP	Investment Value – 5 years later
Feb 2000 - Feb 2001	3,00,000	6,72,503
Jan 2008 - Jan 2009	3,00,000	4,40,942
Nov 2010 - Nov 2011	3,00,000	5,73,761

Source: Advisorkhoj Research. Data as on 1st Feb 2000 to 31st Nov 2016.

Summary

Equity as an asset class is intrinsically volatile. However, there are periods where investors can face extreme volatility which can test their patience. We are going through such a period now and we do not know how long it will last. However, investors should understand the difference between risk and volatility.

- You are likely to make a loss in this market if you redeem but if you remain invested, for a long period of time and follow a market will eventually recover and you can get good returns.
- Systematic investing is likely to help you benefit from volatility.
- You should be patient, continue your SIPs and take advantage of STP if you have lump sum funds.
- Most importantly, you should avoid being affected by rumours and remain focused on your financial goals.
- The age old virtues of patience and discipline taught by your parents will be your biggest friends in difficult times.