INVESTING AT MARKET PEAKS

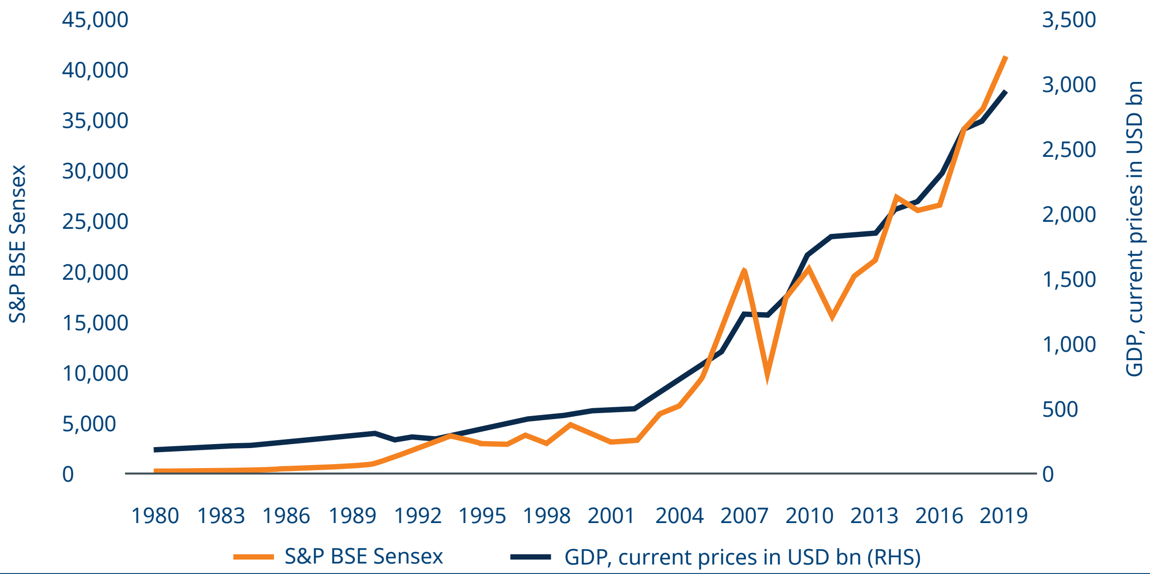
Don’t get deterred by peaks, equity investing is a long term game

The Indian stock market represented by the S&P BSE Sensex had a fairly good last quarter of 2019, crossing the 40,000 points by the year end and closing above 41,000 points in January. While the rising streak creates a pretty hunky dory picture of the market for investors, it might also have made them worried whether the index has peaked and will it start to decline now. With memories still fresh of the sharp decline they saw in 2008 after the Global Financial Crisis started, it is only natural that they have such a concern now. But there is one fact they tend to overlook – that the index value has doubled from 2008 peak of around 20,000 points for the Sensex. The lesson here is that markets usually reward investors who exhibit patience. This article is an attempt to break the myth that investors should not enter the market when it is at a peak. We also hold that the formula to generate greater wealth over the long term is not timing the market but rather investing in it systematically.

Market peaks are superseded in the long term

The capital markets have superseded every high in the long term. A look at the graphic will show you that many such pinnacles have come and gone in Indian stock market. The markets rise is in line with the economic growth. They are a barometer of the growth in a country’s gross domestic product (GDP). The growth is mirrored in the long-term movement of the market (see Chart 1). The graph makes it clear that investing in equities for the long term has been positive and that investors need not bother about the cyclical downturns in the market. Being one of the fastest developing economies, India certainly presents a case for this.

Chart 1: Capital markets mirror economic growth in the long term

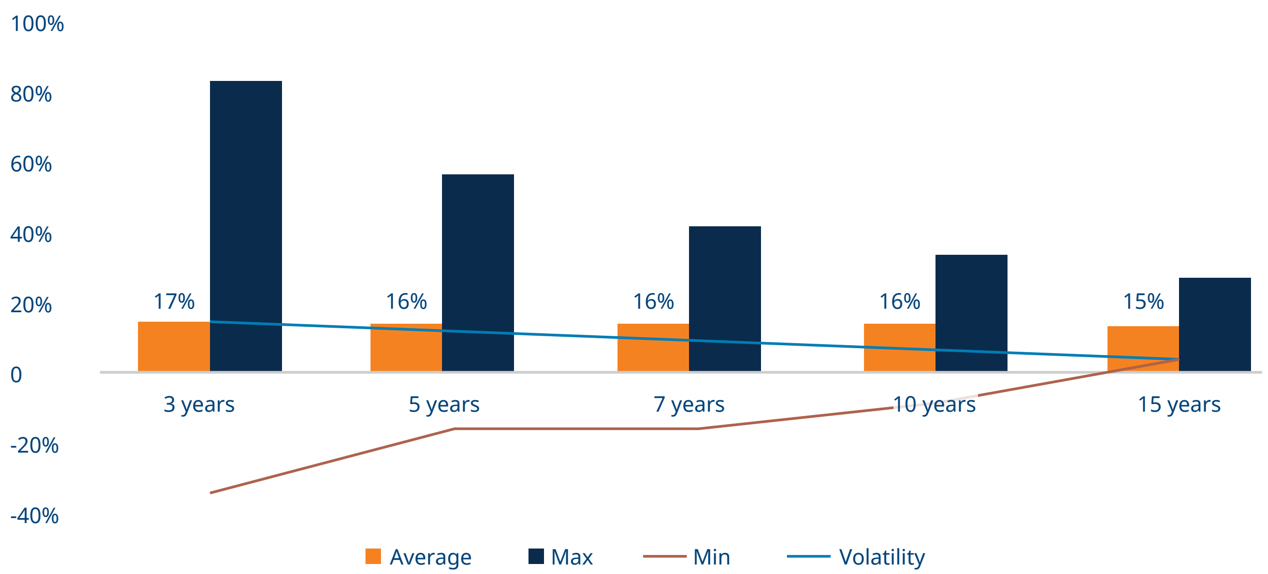


Source: BSE, IMF, Data as on December 31, 2019

Long-term investment is the most beneficial

That equity investment is a long-term game is a primary understanding any equity investor should have. Longer horizons tend to reduce the risks associated with timing the market. Analysis shows that equity has the ability to generate stable positive returns over the long term. For a fact, the S&P BSE Sensex has not given negative return in any 15-year period. Moreover, its volatility (denoted by standard deviation) is nearly 4% over such a horizon, much lower than nearly 17% over a three-year horizon.

Chart 2 – Returns stabilize, volatility reduces over the long term



Source: Data representation of S&P BSE Sensex, BSE, Data as on December 31, 2019

Case study: Long-term investing reaps benefits

Let us look at an actual case. Rahul had just started his job at the turn of the millennium and being a savvy professional, he decided to invest his savings of one year entirely – Rs 50,000– in the equity market. This was the time when the markets were at the peak due to the technology-fed Y2K rally.

But just as he invested, the markets fell drastically due to the dot-com bust. This experience instilled fear in him and he refrained from investing in the markets for the next few years. Rahul saw the 2003-2007 rally from the sidelines. When he finally mustered the courage to invest his savings of around Rs 5 Lakh in the market, the financial debt crisis unfolded and a lot of his money invested for the short term eroded.

Thereafter, he decided not to invest at market peaks. He kept away from the market until around 2013 when the market again started rising sharply on hopes of a strong government at the Centre. As his income had risen during the period, he had saved another 5 lakh and invested it entirely in the market.

So what do you think? Did Rahul make money after having timed the markets to perfection, or investing at peaks? Most would think no, but the answer is yes.

His invested money of Rs 10.5 lakh would have more than doubled to over Rs 23 lakhs at a compounded annualised growth rate of nearly 9% during the period. Markets herein referred is money invested in S&P BSE Sensex. Refer table below

Table 1: Long-term investing has reduced perils of market timing

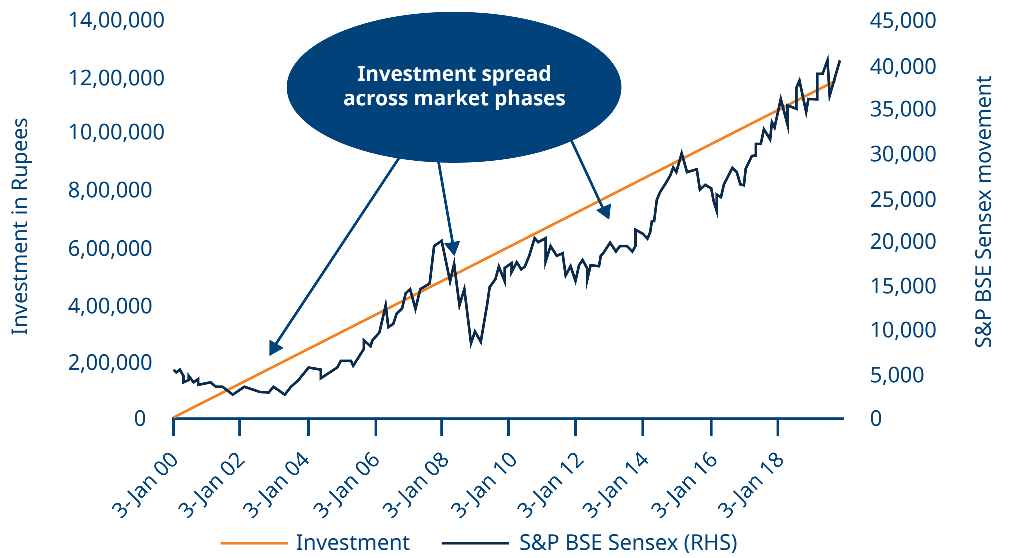
Period of investment	Amount invested
Y2K rally (12th Feb, 2000)	Rs 50,000
Global financial market rally (8th Jan, 2008)	Rs 5 Lakhs
Stable government at the Centre (31st Oct, 2013)	Rs 5 Lakhs
Total amount invested	10.5 Lakhs
Market value as of 31st Dec, 2019 (Assuming that money invested in S&P BSE Sensex)	Rs 23.10 Lakhs
Rate of return	8.80%

Systematic investing can yield better results

Instead of investing lump sum looking at the market trends and sentiments, if Rahul had invested systematically and in a measured manner over this period, would it have been better? The answer is an astounding 'yes'.

If Rahul would have invested Rs 5,000 per month from the time he started his haphazard investments, his total investments would have been around Rs 12 Lakh now, just about the same as what he did in the case study. However, his money would have grown to over half a crore. This is because by investing at regular intervals, he would have invested both in the highs and lows of the market – the former increasing the value of investments and the latter helping him accumulate more units.

Chart 3: Systematic investments helps spread money across market phases



Source: BSE

Table 2: Systematic long term investing is a winning solution

Total amount invested since 3rd January, 2000 in S&P BSE Sensex	**Rs 12 Lakhs**
Market value as of 31st December, 2019. (assuming that money was invested in S&P BSE sensex)	Rs 52. 90 Lakhs
SIP returns	13.15%

Past performance may or may not sustain in future.

Summing up

Investors thus should not get dissuaded by market peaks, instead when investing in equity, have a long term investment horizon and invest systematically in a disciplined manner so that you may to derive better returns from the asset class. As a British-born American investor, economist and investor says "The best way to measure your investing success is not by whether you're beating the market but by whether you've put in place a financial plan and a behavioral discipline that are likely to get you where you want to go."

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