PGIM
India Mutual Fund

# Don’t throw the baby out with the bath water!

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**Ajit Menon**
CEO

That proverb best explains what to guard against as investors. Investing has always been and will always remain first about buying into good businesses. Dire headlines on index levels distract from this. While fear is predominant at this time and the daily dose of bad news exaggerates negativity, it is important to step back and look at this in the context we are in. The corona virus pandemic has brought in sharp corrections in the equity markets. Most commentaries tend to equate this crisis with Global Financial crisis of 2008 and experts of all hues have been sifting through many other crises past to make a judgement about where this could be headed in terms of investment outcomes.

It is first and foremost a humanitarian crisis unlike many instances of the past where some other market forces were at play. Through various interactions I have realised that most of us are looking for the answer to one question, which is, when will it all end and when will some semblance of normalcy resume? Truth is that none of us are in a position to take any data based view on how the pandemic plays out and if further extensions to the lockdown will be required to comprehensively get over this humanitarian crisis. Difficult to say what the final impact will be on the economy and on livelihoods. With a reported 75% of working people in India being self-employed and or casual workers, yes it will impact the poor much more and will also impact the middle class.

Having said that, as investors what are the answers to some of the questions as mentioned above. To best answer that it may be first pertinent to ask a few more relevant questions. What defines you as an individual? Are you a saver or an investor or a speculator? Do you mostly play defensive or aggressive? And importantly, are you more of an optimist or a pessimist? If you are an optimist like me and believe that sooner or later the world will come out of this crisis, then there are plenty of things going right for you. For starters, equity market valuations are at a historic low. On Market cap to GDP basis Indian markets are at 52%, which is closer to 2008 levels. On Price to Book the markets are trading below the 10 year average. All that jargon simply means that you are probably getting good businesses cheap relative to their intrinsic value. Central banks are acting in tandem taking several steps on the monetary front to ease the pain. Various governments including our own are also finding fiscal alternatives to support consumers and corporates alike with, I suspect, more to come. Our own studies at PGIM global for events over the past 68 years have shown that both equity and fixed income markets normalise in a 7 to 9 month period from large drawdowns. These data points should just help us at best define probabilities for the current situation.

It is also worth noting that such difficult periods in history have resulted in high incidences of human innovation across sectors. This has borne out in periods after both the world wars and the depression. My personal optimism comes from the fact that the Equity asset class is the only asset class perhaps best placed to capture the coming innovation wave compared to money in the bank, in fixed income, in real estate, commodities and frankly anything else other than being the innovator yourself.

Being an optimist I am naturally biased here I should say against pessimists as pessimism tends to lead one to take actions that could crystalize losses by selling out. It is difficult to catch the bottom in markets anyway. Perhaps being neither a pessimist or an optimist and rather being a realist is the best option and more matured investors who stick to a process and their asset allocation with a simple strategy of investing pre-dominantly in diversified equity funds and high quality fixed income funds will always have the last laugh. Nevertheless, in the current context we would advise one to stay invested and not redeem in a panic. While it is difficult to say if things will normalise next month, next quarter or in the same seven to nine month time frame observed earlier, historically, it has been noted that whenever there is a pullback rally in the market, it is strongest in the first year. Please consult your advisor before taking any action on the portfolio. It is important to note that quality businesses have a higher probability of an early come back making the process of stock selection or portfolio selection very important. Our focus on picking companies with positive operating cash flows, high ROE and low leverage stand us in very good stead in the equity space in the current context.

Volatility is an embedded feature of markets and this has increased in recent times for various factors. Rising inequality in many countries (especially the developed ones), around the world and elected governments reacting with steep regulations and reforms, climate change and its impact, geopolitical shifts between US, China, Russia and others that redefine trade and logistics, technology and the higher incidence of things like Algorithm based trading that exaggerates both down moves and up moves in markets. The only proven method to tackle volatility is to diversify across as many asset classes as possible including gold, real estate, currency, commodities etc. Maintaining a diversified portfolio across cycles is the mantra. PGIM through its more than 145 year old history has seen many a turbulent times and emerged stronger every time and we remain confident that this time it will be no different.

To conclude, at this point, we think that this is a humanitarian crisis first and what matters most is that everybody remains safe and healthy. Stay at home and stay safe. Together we will overcome this challenge too. Keep the faith... and the baby safe !

Happy investing

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