The Power of the Ordinary

How good old Grandma's tales can help us navigate the stock market

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Dear Investor,

Have you ever wondered what happened to the simple and straightforward way of living, and longed for the days when life was less complicated?

One of the greatest weaknesses of the modern age is that we have developed a tendency to make things more complicated than what is warranted. In the process, we generate a maelstrom of data and information and tend to get drowned in it.

The stock market is a living example of this.

The primary cause for this behaviour, we think, is the misplaced belief that in order to succeed in the stock market, one needs to do something "extraordinary", or that there is no place for the routine, the ordinary, or the average, in the stock market.

Nothing could be farther from the truth.

Maybe **some** investors have managed to do extraordinary things, but it is absurd to believe that a majority of investors is capable of doing this. Usually, the majority isn't above the average.

Does that mean that those of us who are not above average are condemned to get a poor return from the stock market?

Not at all.

Being average does not mean that the benefits of the stock market should be denied to us. If the fate of the world's largest democracy can be decided by the ordinary people, can the same ordinary people not create a decent return for themselves?

It does not need extraordinary intelligence to benefit from the stock market. It needs the lessons we have learnt when we were kids.

Let us rewind to the times when we were regaled by the tales told by our grandmother.

The grandmother in the family is not known for her breathtaking intelligence, or her ability to analyze the whole world. But her fables and parables had truths that were universal and permanently relevant.

She had seen the world, not through the eyes of an "educated" person who tries to alter the world, but through the eyes of an observer who has experienced what is sustainable and what is not.

In all her stories, in all her parables, the following truths always emerged:

(a) Pay attention to the foundation before building the structure

(b) Don't take shortcuts

(c) You shall reap what you sow

(d) Never envy another's success

(e) Everything in life comes to a full circle.

It is remarkable that these are the 5 most important lessons anyone can teach us about equity investing.

Pay attention to the foundation before building the structure

Before attempting an investment plan in equity, let us ask ourselves the following questions. These questions can be answered only by the individual investor himself/herself, and there is no one-size fits all plan that suits everybody.

(i) Have I made adequate provisions for my household expenses before investing in equity?

(ii) Am I investing in equity only that part of the money that I can really spare for a few years?

(iii) Am I investing my own money or am I borrowing to invest? (borrowing to invest in the stock market is not recommended in most cases)

(iv) What is the goal that I seek to achieve with my investment plan?

(v) Do I have the temperament to withstand fluctuations in the stock prices that are inevitable? If so, to what extent?

(vi) Most importantly, can I do it myself? If not, which manager should I choose?

Don't take shortcuts

Old Grandma was right. **MONEY DOES NOT GROW ON TREES.** There is no investment plan in equity that can guarantee a rate of return. There is simply no point in getting excited about the stock market only when the market is booming, and then staying away from it when the market is not going through a bullish phase. Patience and perseverance are far more important ingredients of success than intelligence or insider information.

That said, equity investment is a very good way to participate in the growth of the economy. But equity markets don't move up (or down) in a straight line. There will be fluctuations. But these fluctuations need not, and will not create panic if (a) the investor is adequately diversified (b) if the portfolio is built with companies with a strong business model and financials and (c) when the price paid per share is not exorbitantly expensive.

In order to benefit from the equity market, an investor must agree to the following 3 conditions:

(a) The investor must believe that the future of the economy is good, and there is a good prospect for growth over the next several years

(b) He/she must believe that the companies that function more efficiently will generate a higher return to investors than others that don't.

(c) He/she must accept that fluctuations in share prices will always be there, and that the market prices of shares neither go up or go down in a straight line. The short term price movement of the stock is a function of literally hundreds of variables, but in the long term, the performance of the company is what drives the stock price.

If the investor does not have the time to do equity investing on his/her own, then the Systematic Investment Plan (SIP) in a mutual fund is probably the best way in which he/she can invest. It is simple, it is convenient, and it takes away the emotion from investing. Just take care to choose at least 2 or 3 SIPS in products that are different from each other.

The best thing for you to do (if you don't have the time to do investing on your own) is to choose 3 or 4 mutual funds that are different from each other. Please take the help of your advisor in choosing a good large-cap fund, a good mid-cap/diversified fund, and a good balanced fund. These three together should, in our opinion, meet at least 80% of your equity investment needs.

Satisfy yourself with the help of your advisor that these funds have been consistent in their approach to investment, and have a portfolio without any major irritant.

After choosing these funds with care, just invest the same amount every month – month after month after month. For an SIP to work best, an investor should continue with the plan at least for a full cycle. i.e., if you start an SIP

during a bull market, you should continue with it at least until the next bull market. The worst thing that you can do is to stop an SIP when the market starts falling.

The SIP route is a boring way to invest, but we assure you – you will not find a better method.

Also, the investor is well advised to stay away from investment plans that sound too complicated; if you don't understand it, don't invest in it.

Please remember that the returns from an investment plan are not proportional to the extent of complication it carries. In other words, a simple investment product is just as capable of delivering the same quantity of returns as a plan that is highly complex.

There may be others who understand complicated products. By all means let them invest. You will find that a simple, uncomplicated investment plan can give you a very decent return, provided you are willing to give it some time to perform. Your investment advisor is the best person to guide you in this.

You shall reap what you sow.

The law of Karma works very well indeed in the stock market. If you choose to buy shares without adequate study (simply because it was recommended as a tip), or when you buy companies of dubious quality, it is extremely unlikely that you would consistently make money using this technique. Such things may work once in a while, if you are lucky. But luck does not continue indefinitely.

Please spend some time discussing the investment plan with your advisor. Do it at length before starting to invest, and after the start, spend at least one day every six months in reviewing it.

Never envy another's success

Let's dispassionately look at this. Often, the biggest cause of disappointment about our stock market performance is not that we made a poor return – it is that somebody else made more money.

If somebody has achieved better returns than us, the following can be the reasons:

(a) Maybe he/she is a better investor

(b) Maybe his/her set of companies did well during this time period, and maybe our set of companies would do better next year

(c) Maybe the asset allocation worked in their favour during this period, which may correct next year

As the great Benjamin Graham has said – ***"Investing isn't about beating others at their game. It's about controlling yourself at your own game"***

Everything in life comes to a full circle

There are times when one sector is extremely popular. The same sector would become completely neglected a few years later.

Sometimes mid-caps will be unpopular – they can become enormously popular a few years later, and become unpopular again.

PSUs were popular in the mid 2000s. They turned unpopular in the late 2000s.

FMCGs were unpopular in the mid 2000s. They turned enormously popular after 2009-10.

The important thing for us to do is to adequately diversify.

Let's just remember old Grandma's tales, and the lessons they teach. They are invaluable tools, and they are reminders that being ordinary does not in any way stop us from achieving a satisfactory return from the stock market.

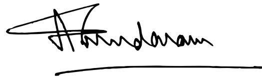
Getting a satisfactory return from the stock market is within everybody's reach. All of us can earn a good return from the stock market if we are disciplined and patient enough. But our problems will start when we abandon what is "good" in search of something that is "the best".

Once again, to quote the great Benjamin Graham ***"to achieve satisfactory investment results is easier than most people realize; to achieve superior results is harder than it looks".***

On behalf of DHFL Pramerica AMC, we wish you and your family all the very best in the ensuing New Year 2017.

Warm regards,

Yours sincerely,



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26th December 2016.