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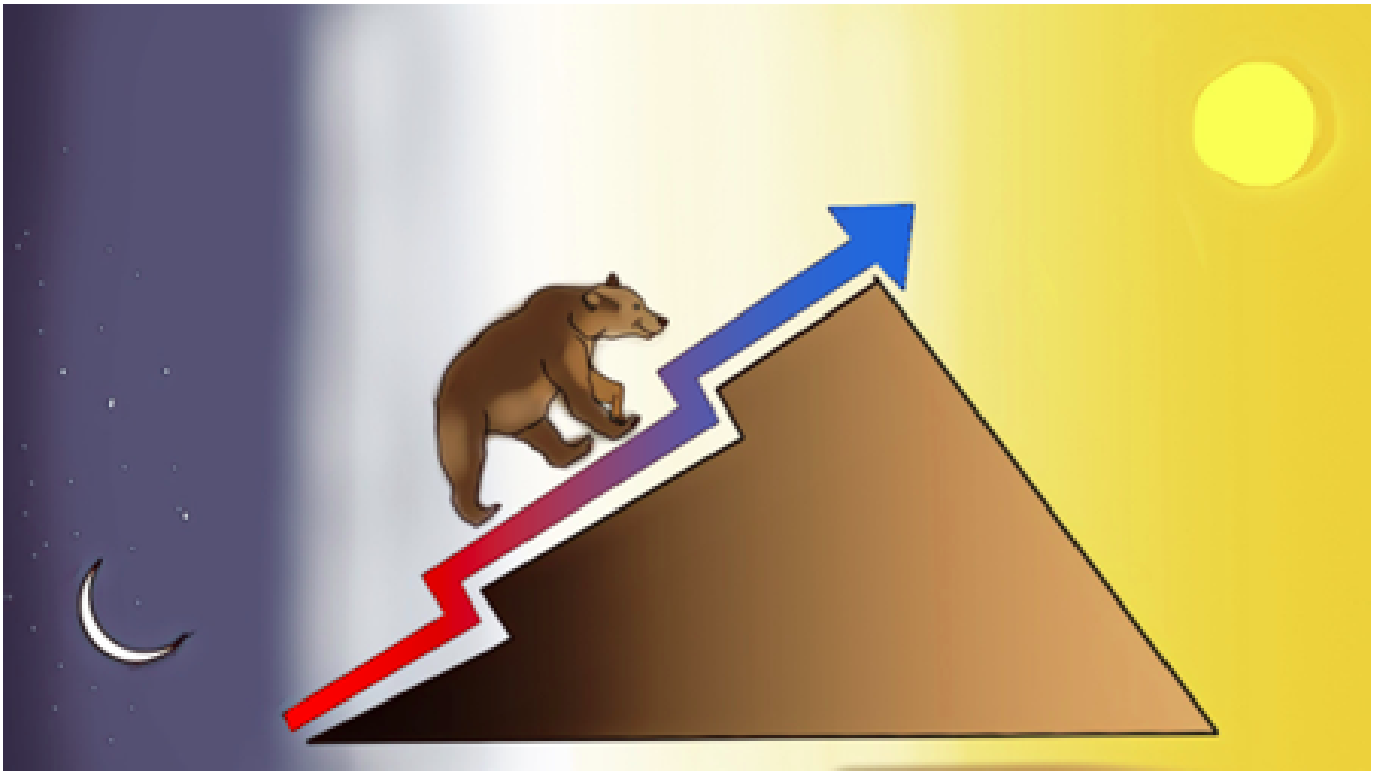
EDWARD INVESTMENT MANAGEMENT

A NOTE FOR INVESTORS: WADING THROUGH THE MARKETS



“Short Termism” is a foe of the sensible investor

With the ongoing outbreak of coronavirus amidst a backdrop of economic slowdown the markets have plummeted significantly since February 2020 creating a 2008 crisis like situation, it gives investors a reason to ponder over instinctive “short termism” and to harness the ability to look beyond such sharp yet brief disruptions. The just concluded quarter may not have been so kind to our portfolios and was no less than a roller coaster ride, descending from the top in a free fall. Consequently, the mood looks glum and it is understandable that the investor wants hand holding in times like these to navigate through the uncertainty. Such fierce bear markets can be agonising but have the ability to make enormous amounts of wealth for the ones who “bear” through it all. If tamed well bear can be your best mate!It must be kept in mind that there’s always light at the end of the tunnel

In the markets, an investor faces both risk and volatility, and should not confuse between the two. The difference must be understood, while risk is the possibility of a permanent loss of capital, volatility is the gyrations in the stock prices and not the value of the businesses. Risk should be avoided whereas volatility should be used to exploit opportunities in the markets to buy good businesses at cheap prices. Due to the present scenario an investor might misunderstand volatility and uncertainty for risk but it must be noted that some of the counters we never thought in the past couple of years would plunge to such attractive levels have rebounded as god sent gifts. The ongoing situation might've pushed our economy back by three to four quarters but it has provided us with an opportunity to start over and bottom fish chunks of worthwhile businesses, which can create substantial value in the long run. It is a good time to take advantage of the opportunities that have surfaced due to this crisis while keeping our return expectations under check in the short term. Equity as an asset class must always be treated as a long term engagement with at least five years of exposure in the markets. For all practical purposes, an asset manager acts as an intermediary between an investor and a business owner to compound the investor's wealth. An asset manager as well as a business owner must be allowed time to implement his strategies and manoeuvre through short term niggles, corrections, crashes, bear markets, companies going bust, some country's economy heading for a slowdown or black swan events like the recent outbreak of coronavirus. Investing in a business could be compared to real estate, we buy property for its rental yield as a source of income or with an expectation of significant capital appreciation. In equities, the rental yield is the dividend yield and the capital appreciation is the appreciation in the stock price over time.

In today's day and age when the world is interlinked, the global markets are driven by the flow of money across the world, therefore this makes sure that an investor is not immune to a falling market in some other part of the world. Such convolutions are a characteristic of the markets, from optimism to pessimism, booms and busts will continue to take place. What will remain is, good businesses running profitably, witnessing huge gains and making investors enormous amounts of wealth, IN THE LONG RUN. So, as an investor one should try to look for a "margin of safety" while buying businesses that would ensure a good night's sleep. There will be times when the margin of safety is further expanded, with value getting cheaper making it even more attractive, just like buying a dollar for 50 cents, after this fall we are now buying even for 20 cents in some cases. The buying must persist if the research and conviction point in that direction. We continue to deploy cash in the businesses we already own in a staggered manner.

Over 30% fall in the index till now from its peak is healthy and essential for a cooling down of the markets. The famous Warren Buffet quote, "Unless you can watch your stock holding decline by 50% without becoming panic-stricken, you should not be in the stock market" must be recollected and assimilated during these times. One should be ready to witness a sizeable fall even from the current levels. Coronavirus just played the role of a catalyst, there is not much to worry about even if it falls further as excesses have built up over the last few years.

This can be concluded from the US rally which started in March 2009 with the S&P 500 rising more than 4 times, reaching 3380 from 760 in ten years without any major corrections. India has been witnessing a similar trend since 2014 with the NIFTY50 doubling in six years from 6,000 to 12,000 odd levels. In between a lot has happened, demonetisation (November 2016), GST (July 2017), IL&FS crisis (September 2018), DHFL going bust, Jet Airways collapse (May 2019), financial stress in the telecom sector, PMC bank and YES bank crisis, the ongoing slowdown with peak unemployment in 45 years, almost all major economic indicators gone for a toss and the most recent being the coronavirus outbreak. This is where margin of safety, diversification in the portfolio, asset allocation, capital protection, and cash calls come into play to mitigate the risks. The recovery curve for the markets could be V shaped or a long drawn U, hence, staying on course is most important. Looking for and buying fundamentally strong survivors which can possibly weather the storm and come out strong would ultimately be the businesses translating into wealth.

Certain industries or businesses are facing a crisis due to a number of reasons, global or domestic issues, resulting in decimation of businesses causing destruction of competition and consolidation of industries. Thus, it could be a perfect opportunity to look for market share gains and focus on businesses which come out as strong players in those industries. Also, in the current scenario, the identification of sectors with “pent up” demand must be done, spaces which could be immune to loss of sales in the medium term, leading to profits in the forthcoming quarters.

To look on the positive side, the markets have also seen a fair share of good days with the corporate tax rate cut introduced in September 2019. The drastic fall in oil prices and global interest rates coming down in response to this global health emergency could also be a huge breather for the corporate sector in the future. India could use the shutdown on Chinese industry to its advantage to expand its share in global manufacturing which is presently dominated by China, leading to long term benefits for the economy.

The lesson to be learnt from the past is that such disasters affect growth in the short term but markets emerge out of such short lived jolts hence, patience is an important virtue in the markets. We must remember the pendulum swings from over optimism to extreme pessimism, stocks will fall in panic situations like these but the best way to tackle through all of this is to avoid “short termism” which can turn out to be worse than COVID-19 itself.

It is the perfect time to curate a shopping list and wait for the fat pitch.

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