

INVESTMENT INSIGHT

Monthly Update



Oct 10, 2009

Editorial

There are two kinds of investors: those who don't know where the market is headed, and those who don't know what they don't know. In straight words nobody can predict interest rates, the future direction of the economy or the stock market as concluded by legendary fund manager Peter Lynch and seconded by Warren Buffet, the all time greatest investor. So true was their observation that it has been emphatically proved time and again as when voices in the market confidently predicted higher levels at 20000 Sensex in January 2008, market made the mockery of it and crashed to 8000. At 8000, when everyone was predicting 6000 Sensex, it took a sharp u-turn to 17000 in span of just 6 months. And now voices in the market are predicting 20000, so will it go there, is anybody's guess.

Despite failing numerous times, its human nature to always predict the future. The most interesting observation in recent times: when market plunged almost 60% and P/E reached 10, analysts were predicting it's overvalued as earnings will fall drastically in the subsequent quarters which will increase the P/E going forward. Now just after 6 months when market is trading at P/E of 22, it is said to be undervalued as future earnings are expected to increase according to new predictions by the same analyst group. Its surprising how in the span of just 6 months market which was said to be overvalued is suddenly undervalued after more than 100% rise from the March bottom. Well it seems this is just human psychology to follow the trend to feel comfortable. So, what we can assure of this is that nobody really knows the future earnings but are predicting by watching the trend. Therefore, earnings already declared are real and should be considered over expected future earnings.

So what should an investor do as future is so unpredictable?? Very simply, stop predicting it and stick to the basic. Warren buffet always says "Be fearful when others are greedy and be greedy when others are fearful". But this is hardly done by investors as emotions always overpower logic. Also sometimes inability to understand if markets are cheap enough to invest or expensive enough to withdraw money make investors do big mistake. By staying un-invested on sidelines when markets are cheap waiting for a so called bottom, investors miss a lifetime opportunity. Similarly inability to understand if markets are expensive enough to sell can result in loss of wealth in sudden market crash.

To win the battleground from emotional dominance and not to loose out in uselessly predicting the market one need to take goal oriented investment in the market. One should stay away from the voices in the market and do proper asset allocation and timely rebalance the portfolio to succeed the financial goals in life. This will imply one should have a long term time horizon for investment and should invest through SIP/STP to prevent the portfolio from wild swings and achieve satisfactory returns.

Wishing you and your family a very prosperous and joyous Diwali!

Happy Investing!