Once bitten twice shy during the bull run

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Vishal Dhawan

WITH THE Sensex hitting the 20,000-level and the wounds of the sharp fall of September 2008 still fresh in the minds of the investors, there is a distinct difference in the mood from the last time the markets hit 20,000-mark.

A large number of investors at the moment are paring equity exposures down to levels that are close to zero and waiting for an opportunity for the market to correct before they reinvest.

Equity valuations at this point do look to be aggressive vis-a-vis historical valuations. However, we believe that investors are taking a short-term view while making exit decisions from equities. Once bitten twice shy behaviour pattern is reasonable to expect, but the ability of investors and money managers to successfully time both their entries and exits is questionable.

In our experience, it is extremely likely that one ends up getting either one or both wrong. We have no reason to believe that it will be any different this time, with investors either exiting too early or re-entering too early.

Ask any investor about how he managed to liquidate all his portfolio at 21,000 on the Sensex last time and re-enter at below 10,000. The answers are unlikely to be a resounding Yes. We know of very few of such investors — institutional or retail.

So what should one do now? While there is no one size fits all solution to this, we think investors can look at the following options:

◗ Asset Allocation holds the key. We think asset allocation is a bit like work life balance — virtually everyone talks about it but very few actually implement it. Just like the benefits to a work life balance have been well documented, empirical evidence shows that asset allocation accounts for more than 90 per cent of portfolio return, with stock selection and market timing accounting for less than 10 per cent. If you have not devised your asset allocation strategy yet, treat it as an emergency so that you are in a position to clearly establish what your ideal equity exposure should be. Once you have done that, and if you are currently overweight on equities, please go ahead and sell. If all this sounds too complicated or time consuming for you, you can explore the option of using automatic asset allocation products in your portfolio or use the services of a financial planner.

◗ Move money from 100 per cent equity products to those that have lower equity levels. If higher equity markets are making you uncomfortable, pare down your equity exposure by moving to hybrid products that have a combination of stocks and bonds so that your equity exposure is reduced but not eliminated.

◗ Use this opportunity to clean up your portfolio — Empirical evidence proves that there are limited benefits of holding more than 15 stocks in a portfolio. With a large number of portfolios having got built through IPOs and small/mid cap stocks, it is a good time to cut.

(The writer is the founder of Plan Ahead Wealth Advisors Pvt. Ltd.)

smart investing

- ◗ Asset allocation is more important than stock selection and market timing.
- ◗ Move money from 100 per cent equity products to those that have lower equity levels such as hybrid products.
- ◗ There are limited benefits to holding more than 15 stocks in a portfolio. So it is good time to cut the portfolio.