Outlook for equities

- Good investments are typically made in challenging times and seldom in good times
- 1 year forward P/E's have corrected from ~25X to ~12X, between January 2008 till date; these are significantly lower than long term averages
- In a year's time, 1 year forward P/E of Sensex at current levels, should be ~11X. P/E's in India, even in crisis situations have not fallen below 10 – 11x
- An 8.50% yield on 10 year G-sec's corresponds to a P/E of ~ 12x. In 1 year, P/E's of equities should be lower than bond P/E's at current index levels. This points to under-valuation of equities vis-à-vis bonds
- In view of the above, risk reward appears favourable over 1 year and longer periods

All data pertaining to equity markets and G-Sec's above is as on Dec 30, 2011

HDFC MUTUAL FUND

How to earn more from equities ?

- Equity prices and returns are volatile over short to medium periods
- In the long run, however, returns from equities are surprisingly predictable;

  Equity returns = Earnings growth + dividends

For details please refer next slide

- Whenever past returns from equities are less than earnings growth, future returns should be more and vice-a-versa

Period ending March 31	Rolling 5 year returns of Sensex (%p.a.)	Rolling returns over next 5 years of Sensex (% p.a.)
1992 - 1997*	-5%	1%
1994 - 1999	0%	8%
1996 - 2001	1%	26%
1997 - 2002	1%	30%
1998 - 2003	-5%	39%
2000 - 2005	5%	22%
2007 - 2012	3%	?

As an illustration, in last 20 years when returns over 5 years have been less than 5% p.a., subsequent 5 year returns have been strong

- Given the low returns of last 5 years and the low P/E multiples, returns over next 5 years should be a combination of earning growth & P/E expansion

* In 1992, P/E's were ~ over 40 times and inspite of –ve 5 year returns, P/E's in 1997 were still around 25 times. Currently P/E's are 12 times based on one year forward (March 2013) earnings

Past Performance of the Sensex may or may not be sustained in future. The above table is for illustration purposes only and should not be construed as an investment advice. It does not in any manner imply or suggest current or future performance of any HDFC Mutual Fund Scheme(s).

Sensex Rolling Returns

Short term returns in equities are volatile; hence equity investments should be made with a long term horizon

No.	Year ending March	BSE Sensex on 31/03/XX	Rolling 1 year returns	Rolling 5 year returns	Rolling 10 year returns	Rolling 15 year returns
0	Mar-79	100				
1	Mar-80	129	29%			
2	Mar-81	173	35%			
3	Mar-82	218	26%			
4	Mar-83	212	-3%			
5	Mar-84	245	16%	20%		
6	Mar-85	354	44%	22%		
7	Mar-86	574	62%	27%		
8	Mar-87	510	-11%	19%		
9	Mar-88	398	-22%	13%		
10	Mar-89	714	79%	24%	22%	
11	Mar-90	781	9%	17%	20%	
12	Mar-91	1168	50%	15%	21%	
13	Mar-92	4285	267%	53%	35%	
14	Mar-93	2281	-47%	42%	27%	
15	Mar-94	3779	66%	40%	31%	27%
16	Mar-95	3261	-14%	33%	25%	24%
17	Mar-96	3367	3%	24%	19%	22%
18	Mar-97	3361	0%	-5%	21%	20%
19	Mar-98	3893	16%	11%	26%	21%
20	Mar-99	3740	-4%	0%	18%	20%
21	Mar-00	5001	34%	9%	20%	19%
22	Mar-01	3604	-28%	1%	12%	13%
23	Mar-02	3469	-4%	1%	-2%	14%
24	Mar-03	3049	-12%	-5%	3%	15%
25	Mar-04	5591	83%	8%	4%	15%
26	Mar-05	6493	16%	5%	7%	15%
27	Mar-06	11280	74%	26%	13%	16%
28	Mar-07	13072	16%	30%	15%	8%
29	Mar-08	15644	20%	39%	15%	14%
30	Mar-09	9709	-38%	12%	10%	6%
31	Mar-10	17528	81%	22%	13%	12%
32	Mar-11	19445	11%	12%	18%	12%
33	Mar-12*	15455	-21%	3%	16%	11%
	Probability of loss		12/33	3/29	1/24	0/19

Sensex /Equities are a great compounding machine Rs. 100 = Rs. 16,000 over 32 years

Long term returns are *less* volatile; risk in equities *reduces* as holding period increases

As holding period increases, chances of loss reduces

Past Performance of the SENSEX may or may not be sustained in the future. * Assume Index at current level (Dec 30, 2011) for Mar-12 for illustrative purpose. Returns for periods more than 1 year are shown on a compounded annualised basis. **Note:** The base year of SENSEX is 1978-79 and the base value is 100. Please visit www.bseindia.com for the SENSEX calculation methodology

Why is it a good time to start / increase SIPs ?

- Index has given low returns over the last 5 years (2.31% CAGR* for BSE Sensex)
- P/E's have thus corrected significantly and are currently at ~12X based on March 2013 earnings versus the long term average P/E of ~17X **
- Future returns should thus be both from earnings growth and increase in PE's
- Equities are a unique asset :

  In a growing economy, generally, the lower the past returns than earnings growth, the higher should be the future returns and vice versa
- In view of the above, we recommend continuing / enhancing / starting SIPs as a prudent strategy for equity investments

* As on Dec 30, 2011 ** Source: CLSA

Summary

- Indian economy is a long term growth economy and is likely to be the 5th largest in the world by 2020
- The current challenges facing us are mostly internal and the economy should do well again, when these are overcome
- Low P/E's of today represent an opportunity for the long term investor
- Good investments are made in bad times and seldom in good times
- Key risks are spike in oil prices and lack of serious effort to curtail fiscal deficit
- Allocation to equities should be increased in a phased manner with a medium to long term view

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