Why equity?

A far-off investment goal can ride out market lows

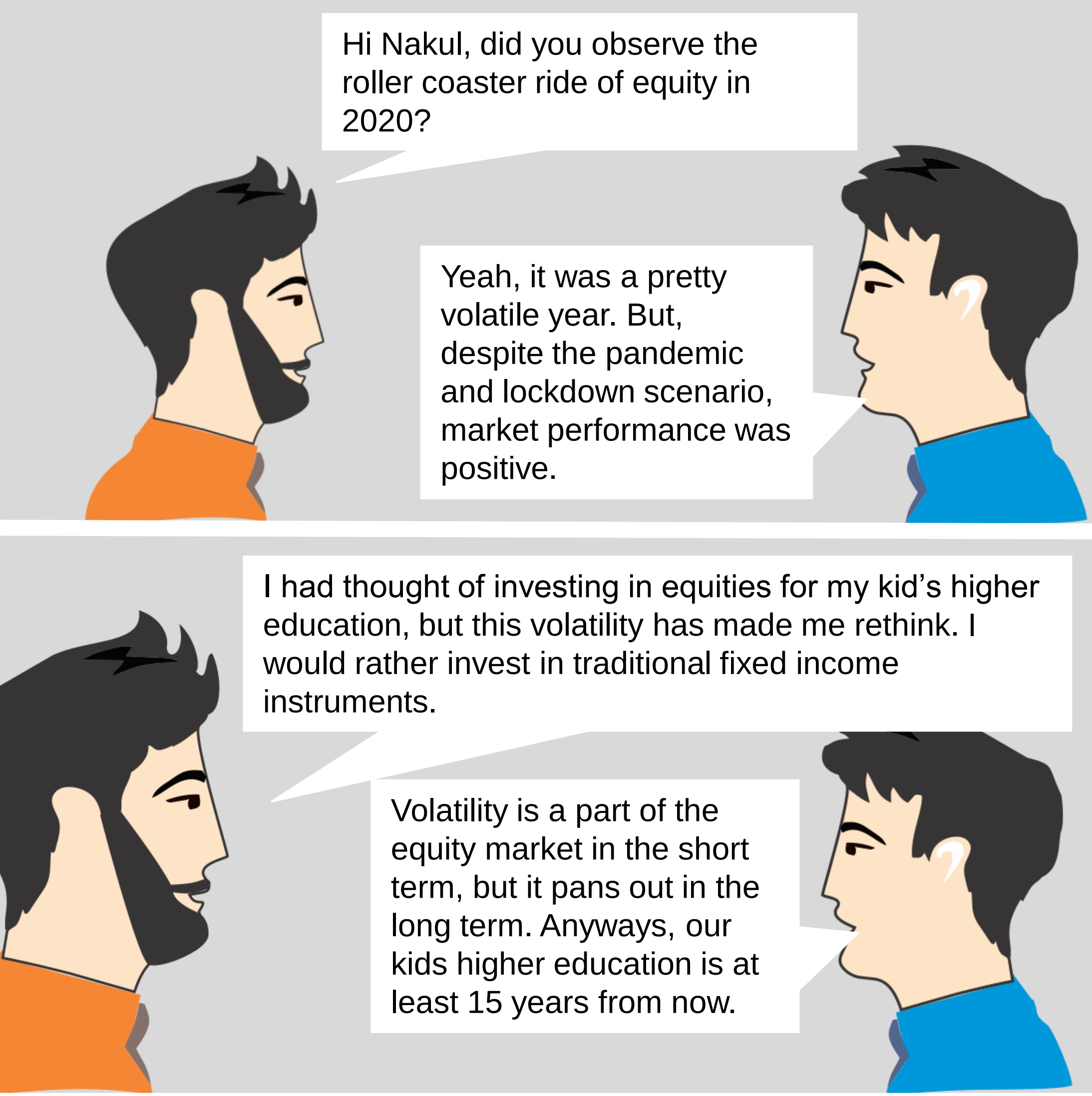
HSBC
Global Asset
Management

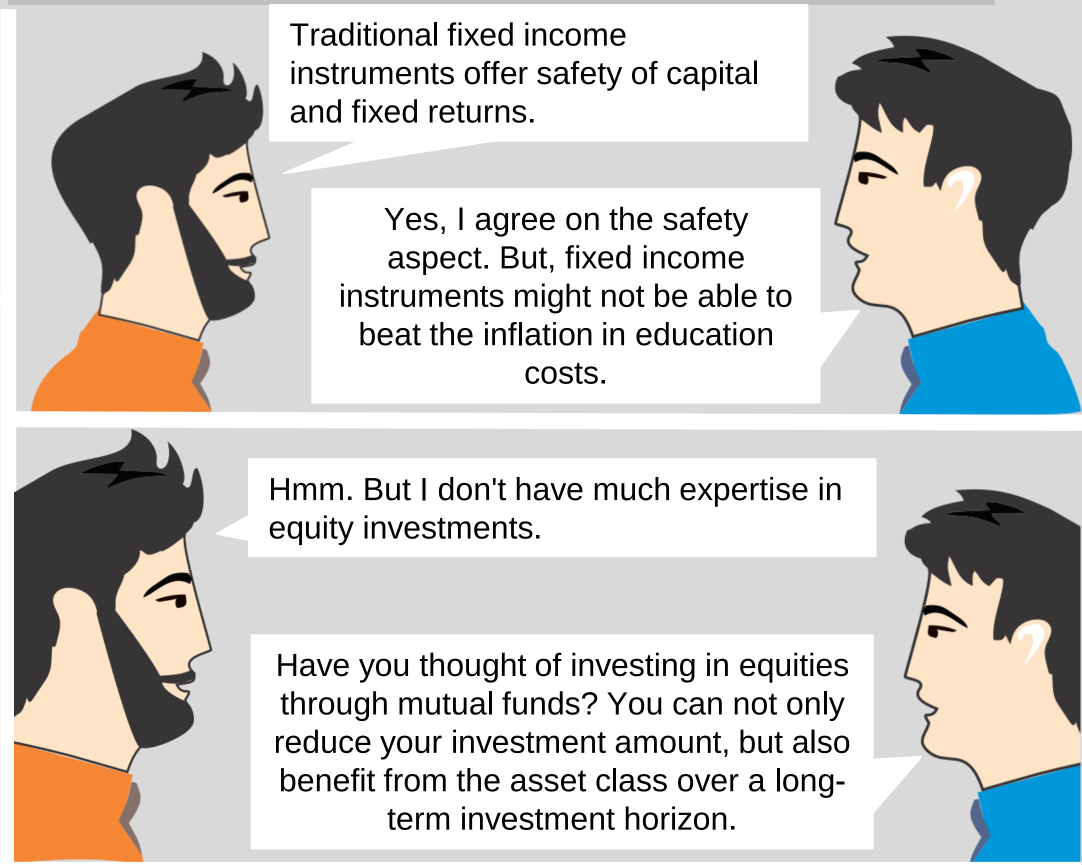
January 2021

Why make equities a part of your investment portfolio?

Let’s look at a conversation between Rahul and Nakul

Rahul and Nakul are old friends meeting after a long time. They discuss about equity market movement in 2020 and their plans to invest for their kids’ higher education.





Systematic investments in equity provide optimum results for investors over the long term

Inherent volatility in equity investments pans out over long term

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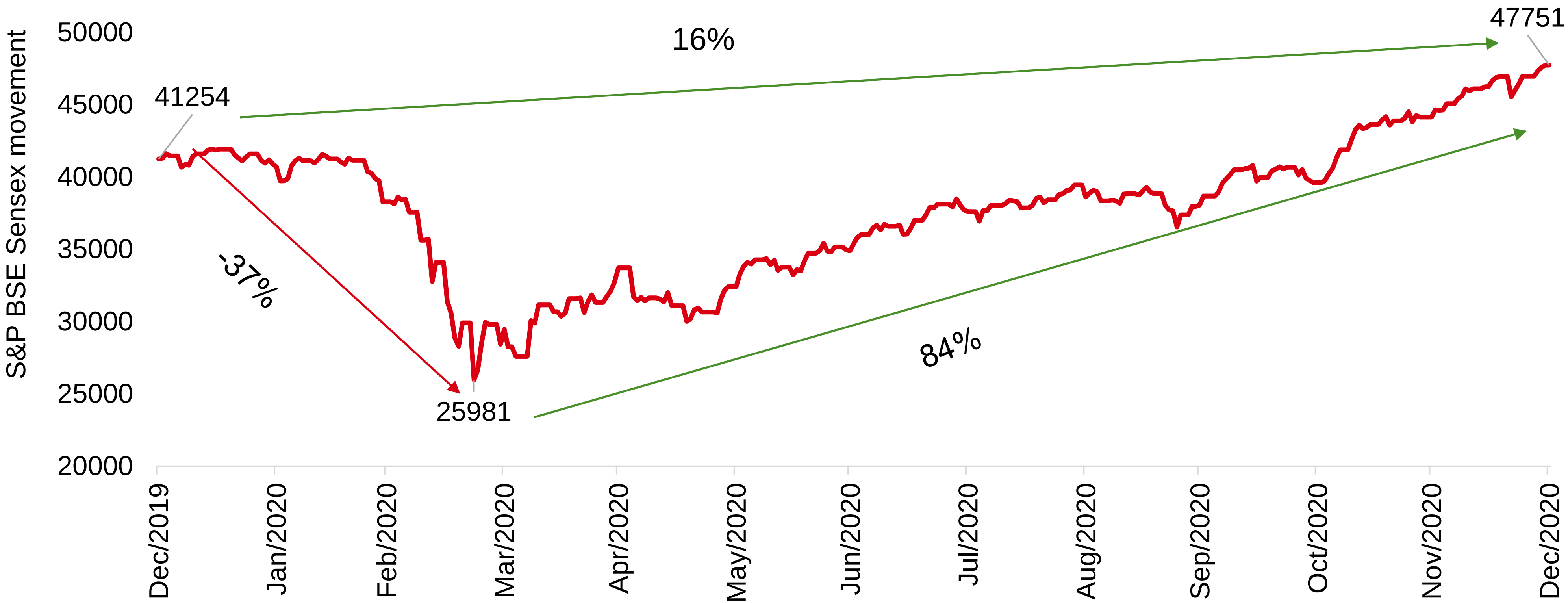
Roller coaster ride for equities in 2020, but market at record high



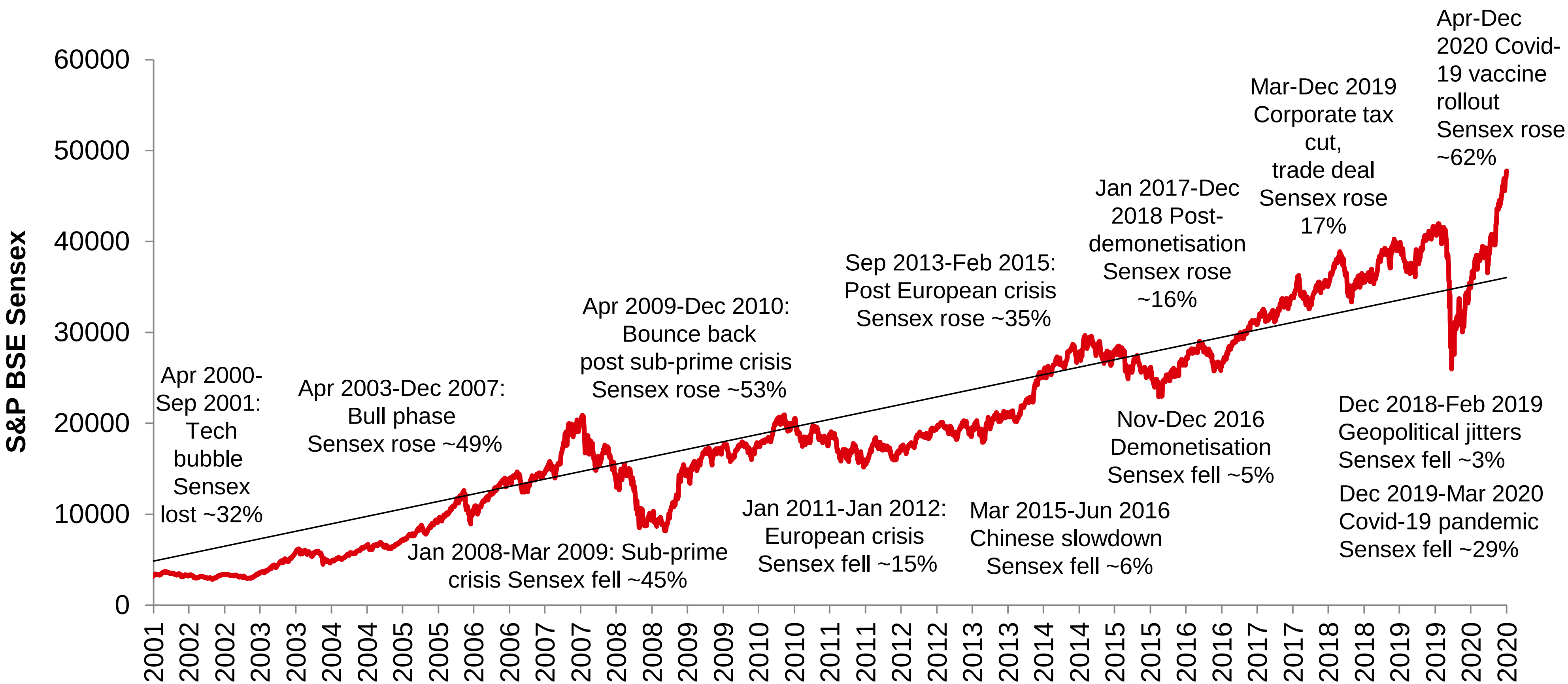
Covid-19 and lockdown worries dragged down equities in Q1 2020; S&P BSE Sensex fell 37% from the end of Dec 2019, but recovered 84% in the rest 9 months to close at 16% for the year

Source: CRISIL, BSE, S&P BSE Sensex

Note: Past performance may or may not sustain, past performance does not guarantee future performance

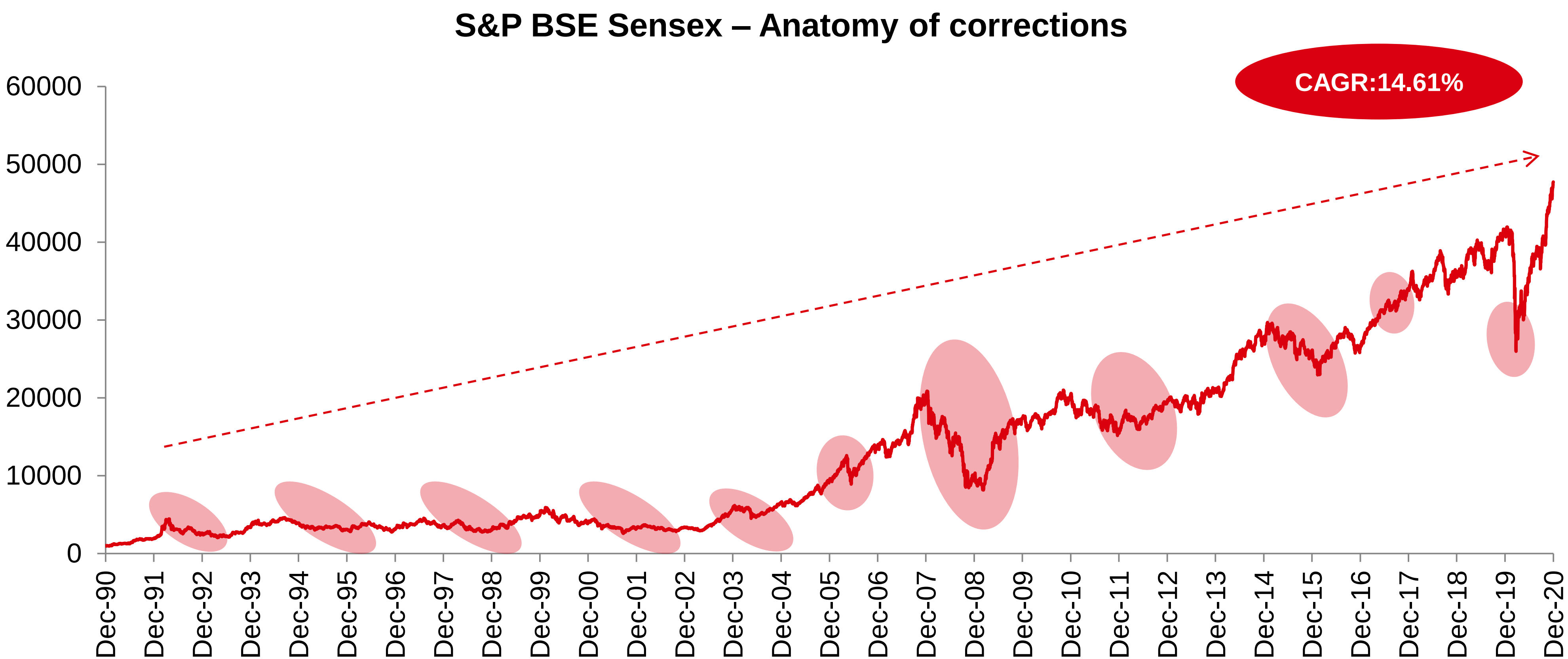
Long-term trend points to upward movement for equities, though not a smooth ride

Highs interspersed with lows



Source: BSE, CRISIL Research
Notes:
Data as of December 2020
Returns for period less than one year are absolute; otherwise, annualised
Past performance may or may not sustain, past performance does not guarantee the future performance

S&P BSE Sensex amplified 46 times in the past 30 years at 14.61% CAGR



Note: Highlighted circles represent correction in the market

Short-term volatility is an inherent part of equity investment

Source: CRISIL, BSE,

Note: Past performance may or may not sustain, past performance does not guarantee future performance

Short-term volatility is an intrinsic part of equity investments

Long-term investment pays off

BSE Sensex	3-year rolling returns	5-year rolling returns	7-year rolling returns	10-year rolling returns	15-year rolling returns
Average rolling period returns	**16.36%**	**15.97%**	**15.69%**	**15.56%**	**15.01%**
Total time periods (monthly rolling)	463	439	415	379	319
Total number of positive returns*	412	406	390	376	319
Total number of negative returns^	51	33	25	3	0
Positive investment periods	**89%**	**92%**	**94%**	**99%**	**100%**

The longer you stay invested, lower is the possibility of negative returns

In the long term, the probability of incurring losses is lower in equity investments

Notes:

Monthly rolling returns for respective holding periods since 1979. For instance, in case of 15-year monthly rolling returns, there will be 319 return periods. The first return period will be June 1979-1994 and the last return period will be December 2005-2020

* Positive returns – The number of investment periods during which returns have been positive. For example, where investment returns have been computed for a 15-year rolling period, 319 months offered positive returns (profits), the number of positive returns period = 319

^ Negative returns – Number of investment periods during which returns have been negative. For example, where investment returns have been computed for a 5-year rolling period, 33 months offered negative returns (losses), the number of negative returns = 33

Source: BSE, CRISIL Research

Notes:
Data as on December 31, 2020
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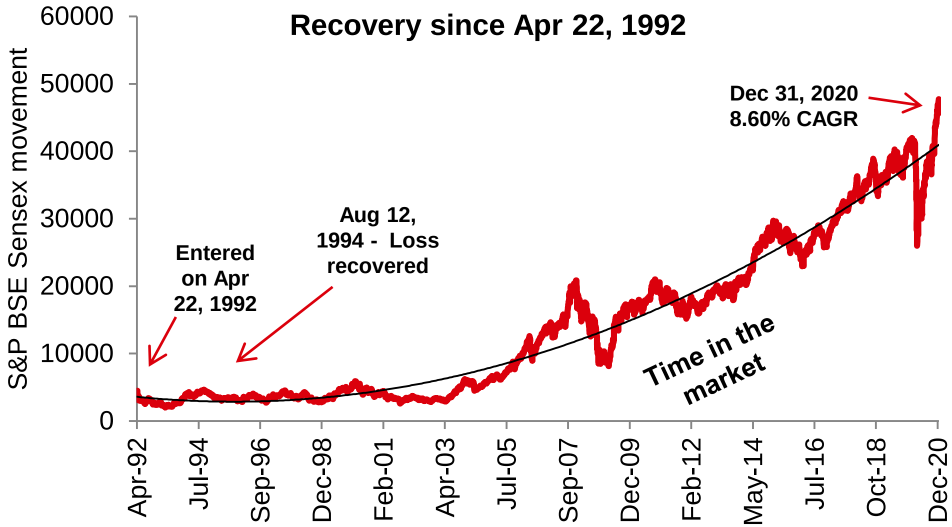
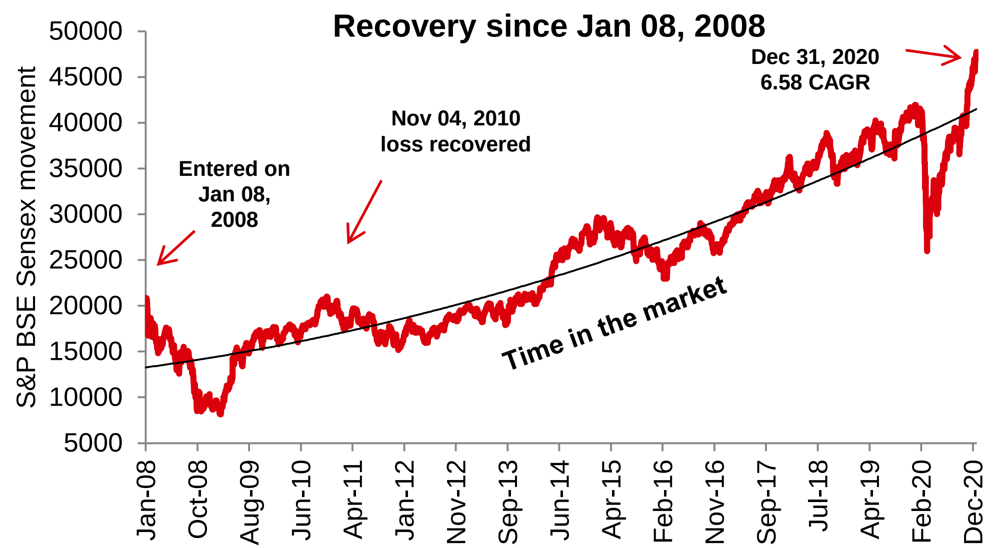
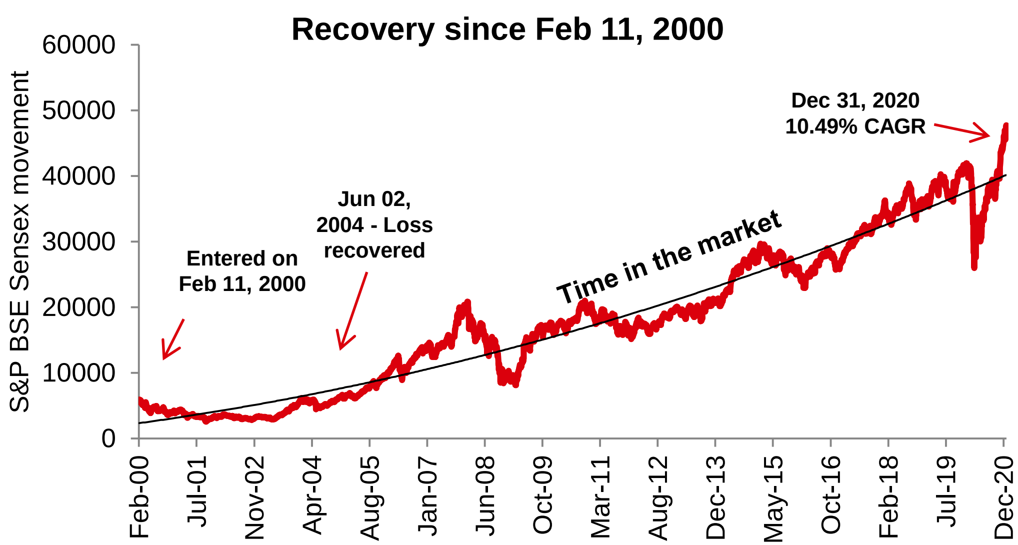
A far-off investment goal can ride out market lows

Historical trend shows that after falling, markets have recovered in the medium term







Equity losses are transitory – long-term outlook can earn better returns

Source: BSE, CRISIL Research

Notes:

Data as on December 31, 2020

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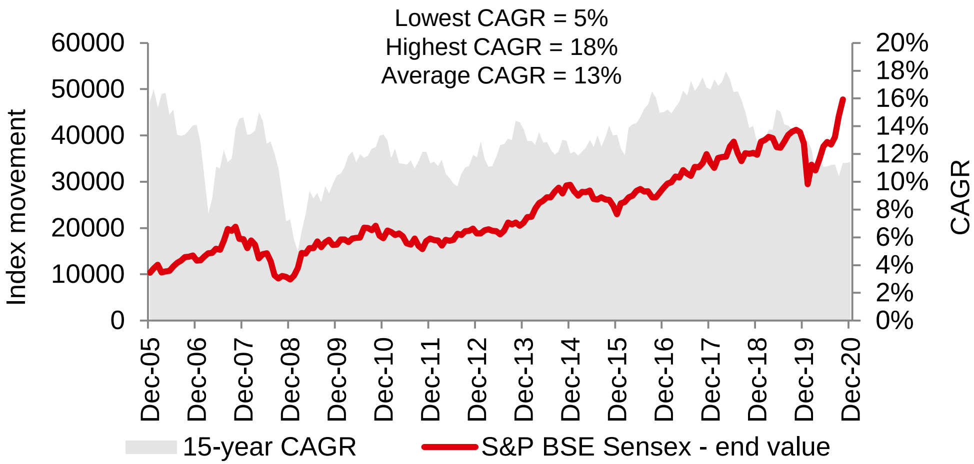
Making more by losing less

Consistent, predictable behaviour over longer period

S&P BSE Sensex 15-year monthly rolling returns

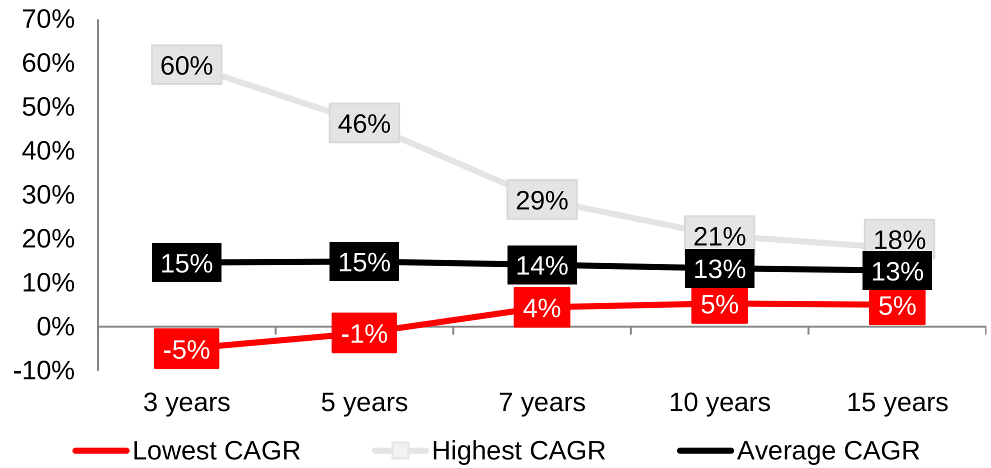


Period: Dec 2005–2020; Returns frequency: Monthly rolling

100% positive 15-year returns

Difference between high and low returns reduces with increase in holding period

S&P BSE Sensex monthly rolling returns for different holding periods



Period: Dec 2005–2020; Returns frequency: Monthly rolling

Source: BSE, CRISIL Research
Notes:
Data as of December 2020
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Investments in equities are better than traditional instruments over long term

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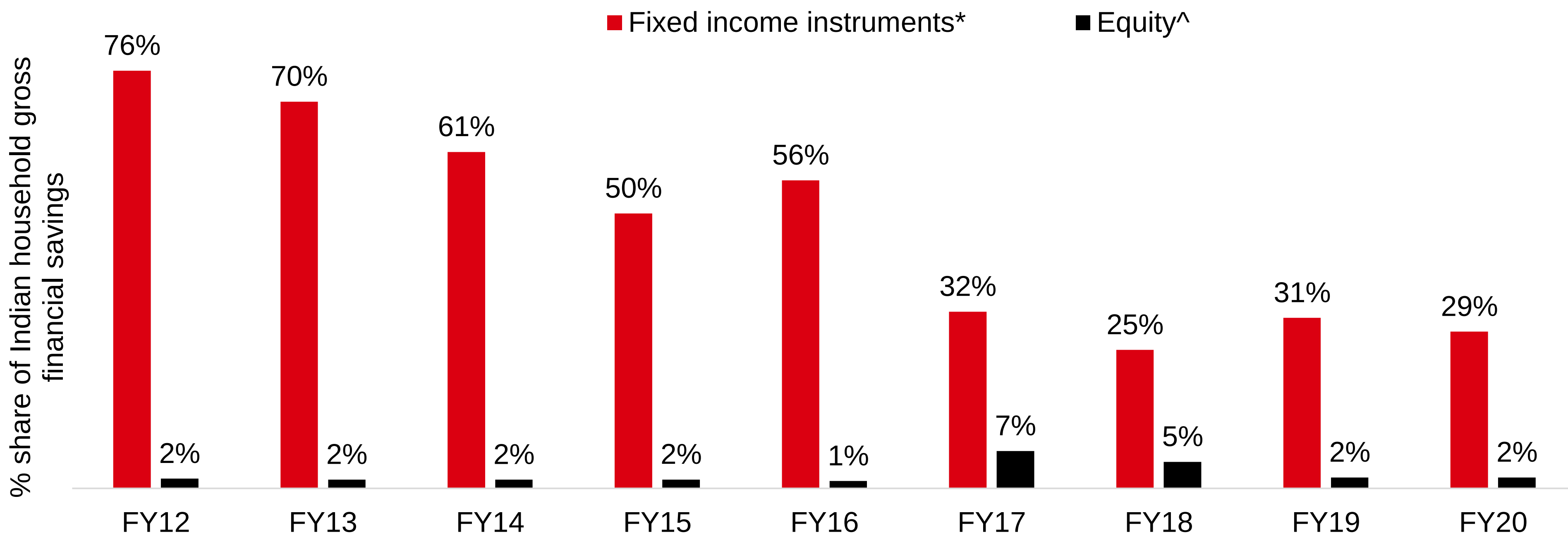
Fixed income instruments – Traditional investment choice of Indian households

Equity plays a marginal role



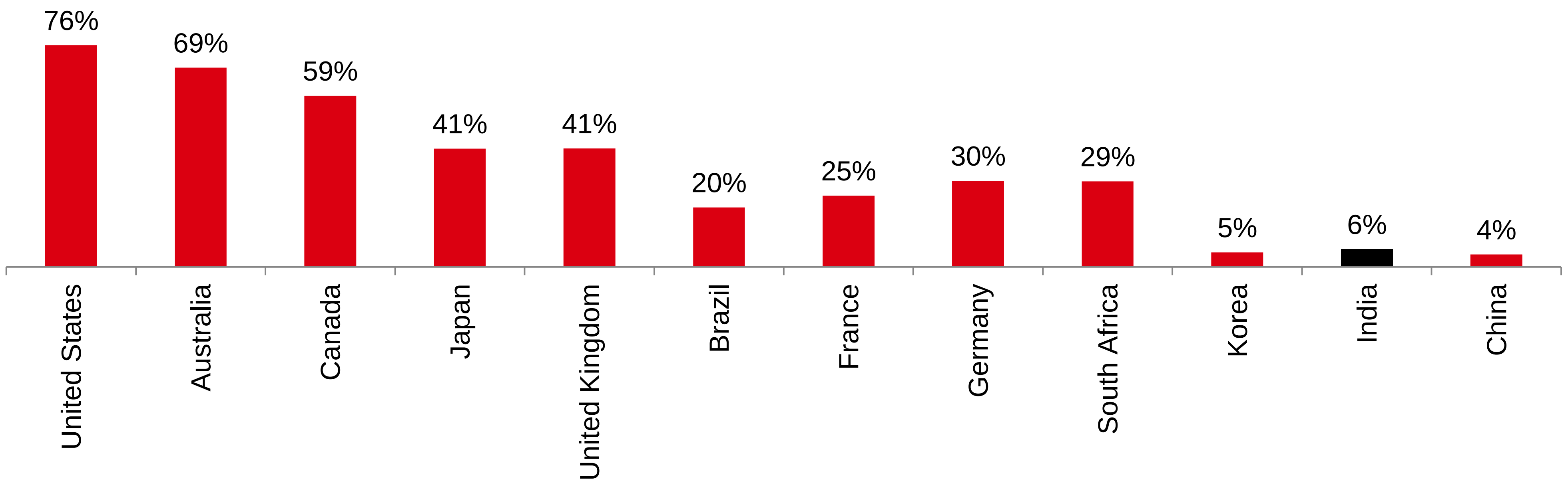
Indian investments remain skewed towards debt

Source: RBI, CRISIL
Notes:
*Fixed income instruments include deposits and investments in provident and pension funds
^Equity includes investments in shares and debentures

Equity – The most preferred investment avenue globally

Developed countries have higher affinity to equity

- Emerging economies are significantly under-exposed to the equity asset class compared with developed economies



India has one of the lowest equity exposures of only 6%

Source: CRISIL, IMF, IIFA
Notes:
GDP data as of December 2020; assets data as of Q3, 2020 as per latest available
Past performance may or may not sustain, past performance does not guarantee the future performance.

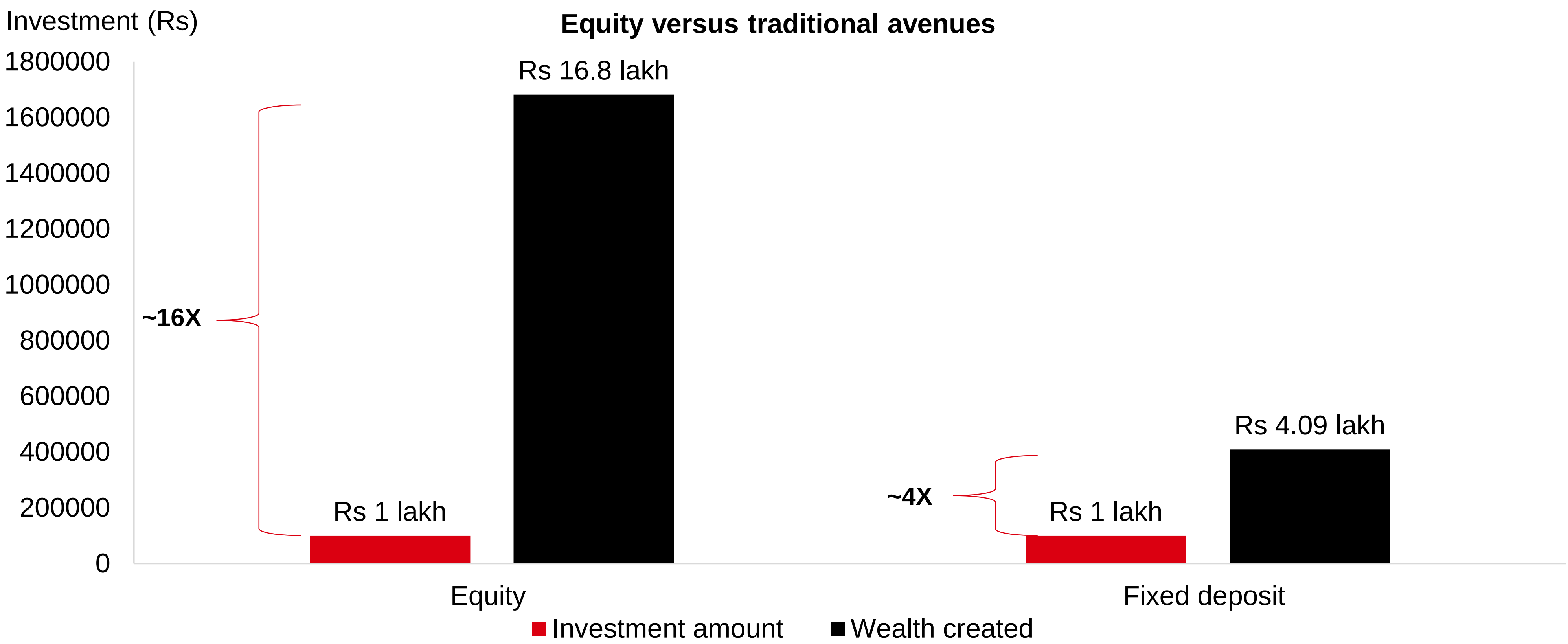
Five reasons why you should invest in equities

Growth	Inflation	Returns	Goals	Retirement
India's equity market performance highlights the potential of equities to deliver growth for investors	Equity investments may provide an opportunity to outperform the ever increasing inflation and improve purchasing capacity	Historically, equity investments have outperformed other asset classes over the long term	Equity investments aid in goal planning and meet long-term goals	Equity investments offer potential to save better for comfortable retirement

Equity investment is relatively less explored in India compared with other options

Past performance may or may not sustain, past performance does not guarantee the future performance

Create wealth in the long run through equities



Rs. 1 lakh investment in the S&P BSE Sensex grew to Rs. 16.8 lakh versus a mere Rs. 4.09 lakh in fixed deposit^ in 20 years period

Source: BSE, CRISIL
Notes: ^Fixed deposit is represented by 1-year FD index
*CAGR returns for S&P BSE Sensex and 1-year FD index for the period between December 31, 2001 till December 31, 2020 is considered for analysis
Past performance may or may not sustain, past performance does not guarantee the future performance.

Equities well-suited for India's young demography

Scope to increase equity allocation

- Young investors can have higher equity exposure owing to higher risk appetite

India is likely to remain a young country in the future

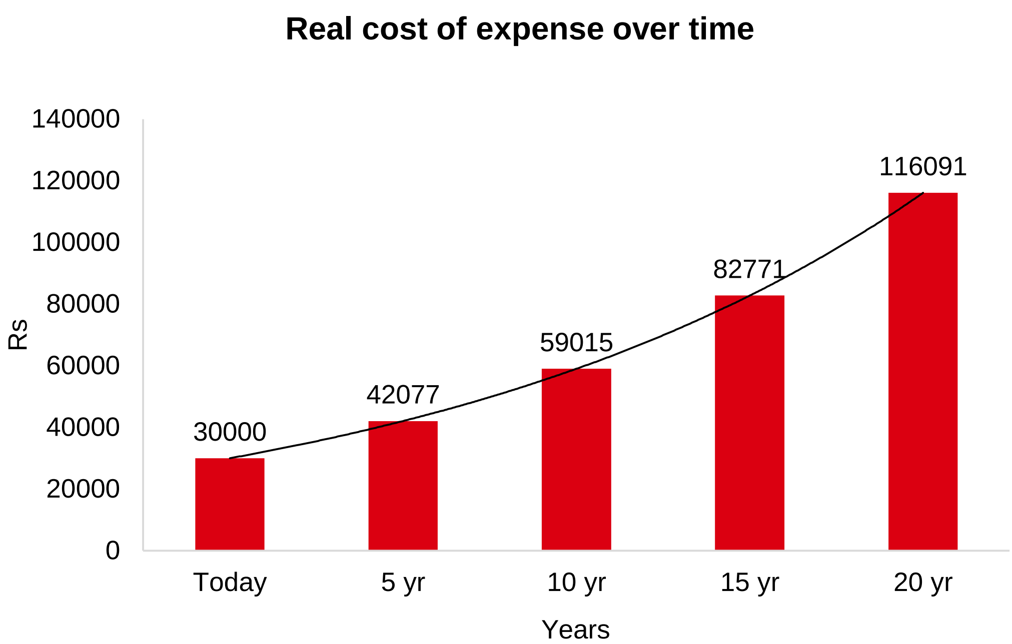
Share of 15-49-year-olds in the country's population			
Country / region	2020	2035	2050
Australia	47%	44%	43%
Brazil	54%	48%	41%
China	49%	44%	38%
India	54%	52%	47%
Japan	40%	35%	33%
Russian Federation	46%	44%	43%
South Africa	54%	52%	49%
United Kingdom	44%	43%	41%
United States of America	46%	45%	42%

Young investors can invest more in equity to benefit from long-term compounding

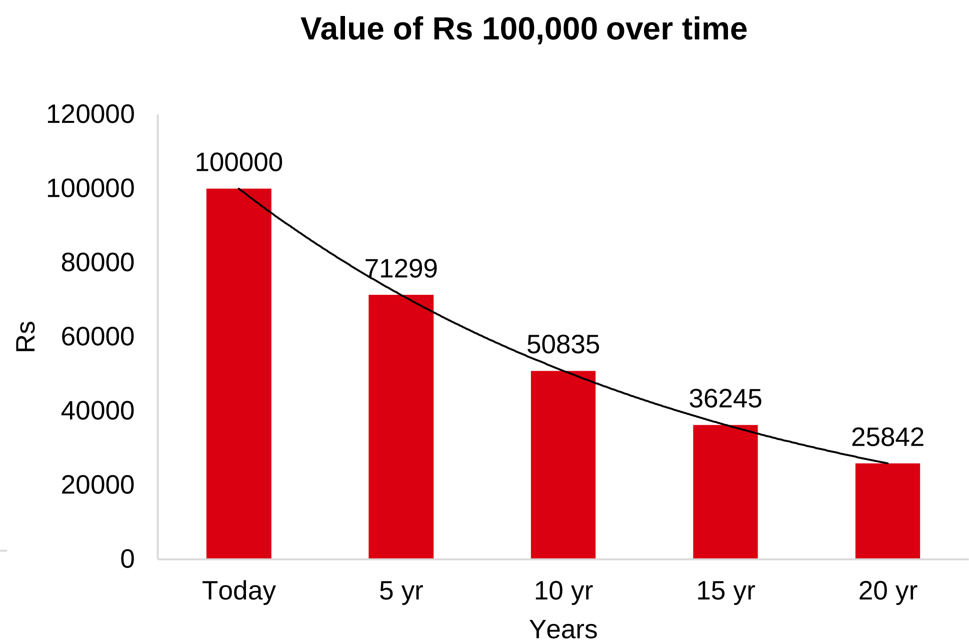
Source: CRISIL, UNCTAD
Note: Past performance may or may not sustain, past performance does not guarantee the future performance.

Savings are not enough since inflation eats the value of money

If our expenses are real, returns should also be real



At 7% inflation



At 7% inflation

Inflation not only increases cost of products, it also reduces value of money

Source: Labour bureau.nic.in, CRISIL

Notes:

Inflation represented average of monthly inflation of industrial workers declared since January 1993 till November 2020

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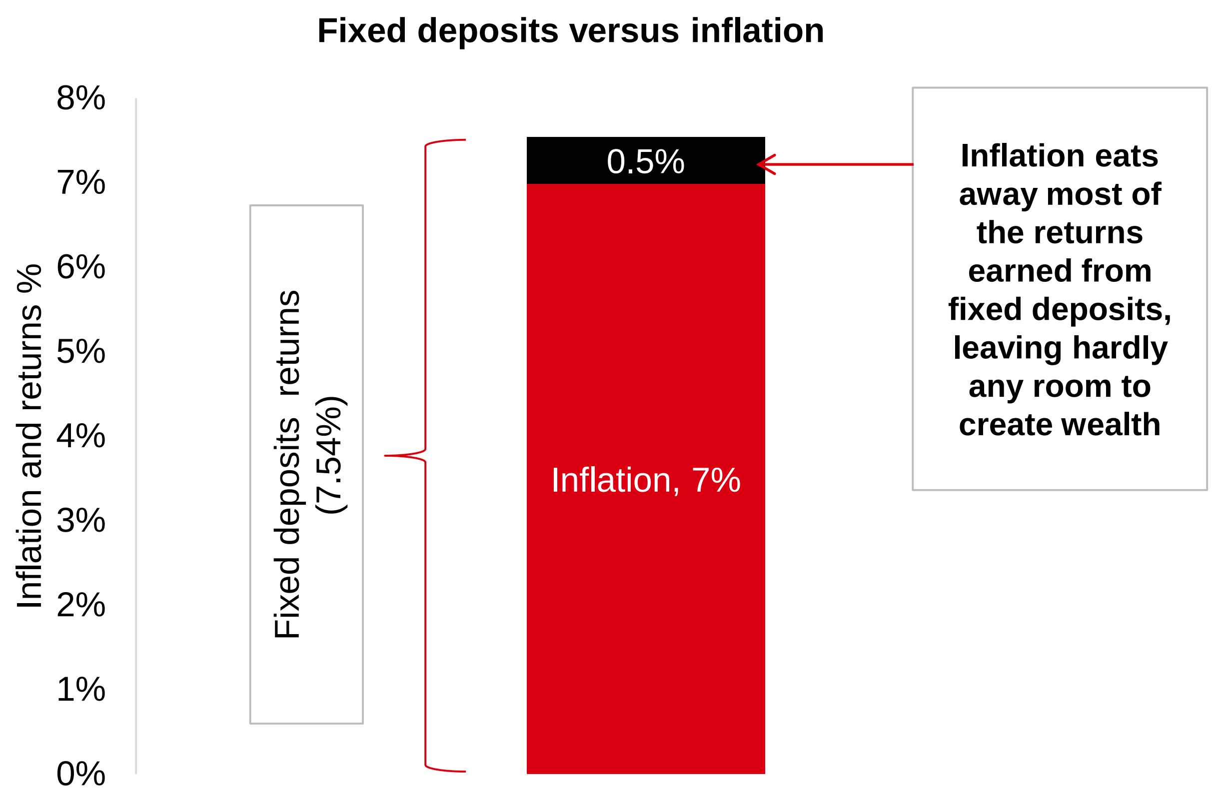
Traditional savings do not offer enough cushion

Inflation generally consumes investment capital

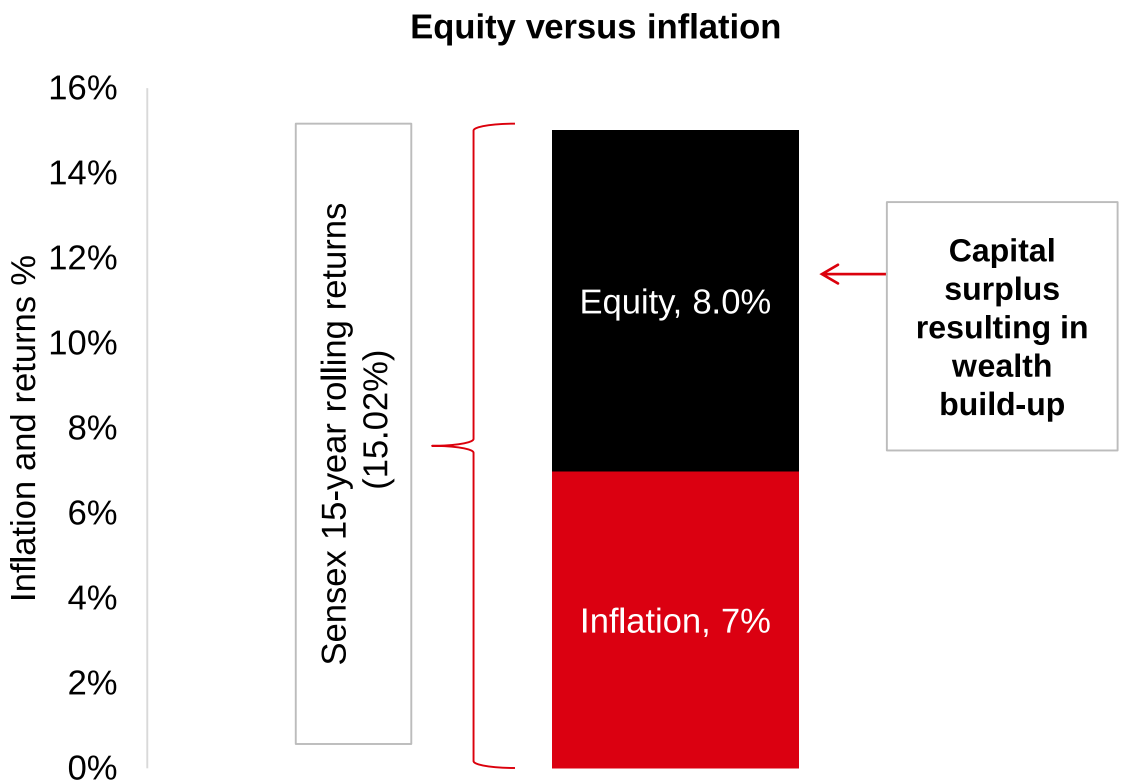


The difference between saving and investing is the ability to provide an affordability cushion by beating inflation on a regular basis

Source: CRISIL Research, Labour bureau
Notes:
Fixed deposit rate represented by 1-year FD index's annualised returns since October 1999 till December 2020
Inflation represented average of monthly inflation of industrial workers declared since January 1993 till November 2020
Past performance may or may not sustain, past performance does not guarantee future performance.

However, equities cushion ever-increasing cost of living

The smartest way to create wealth

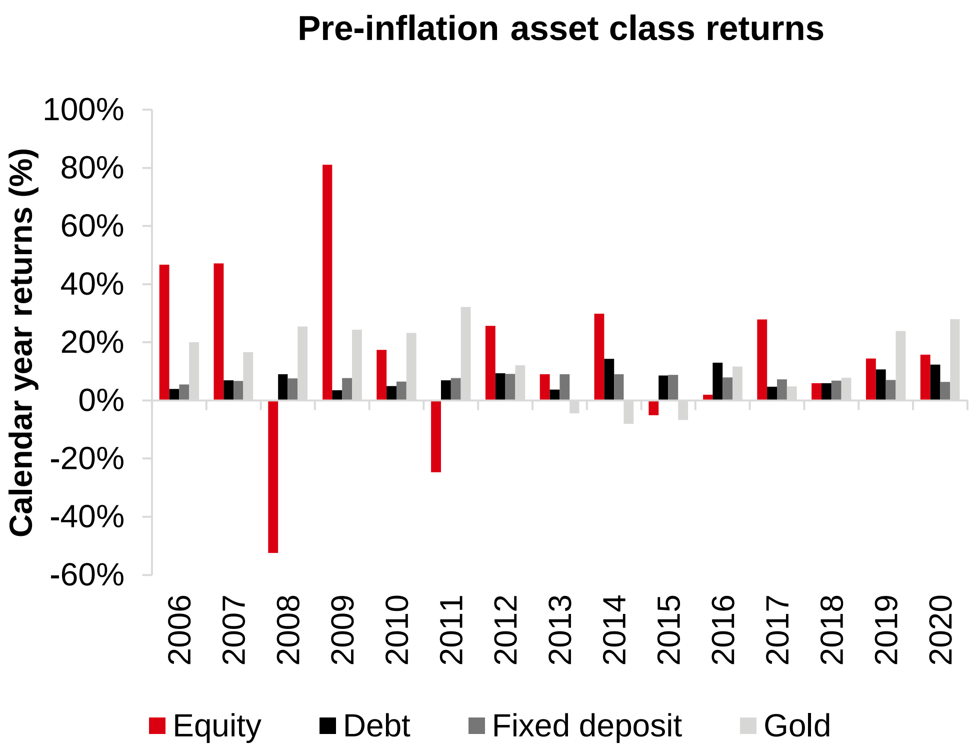


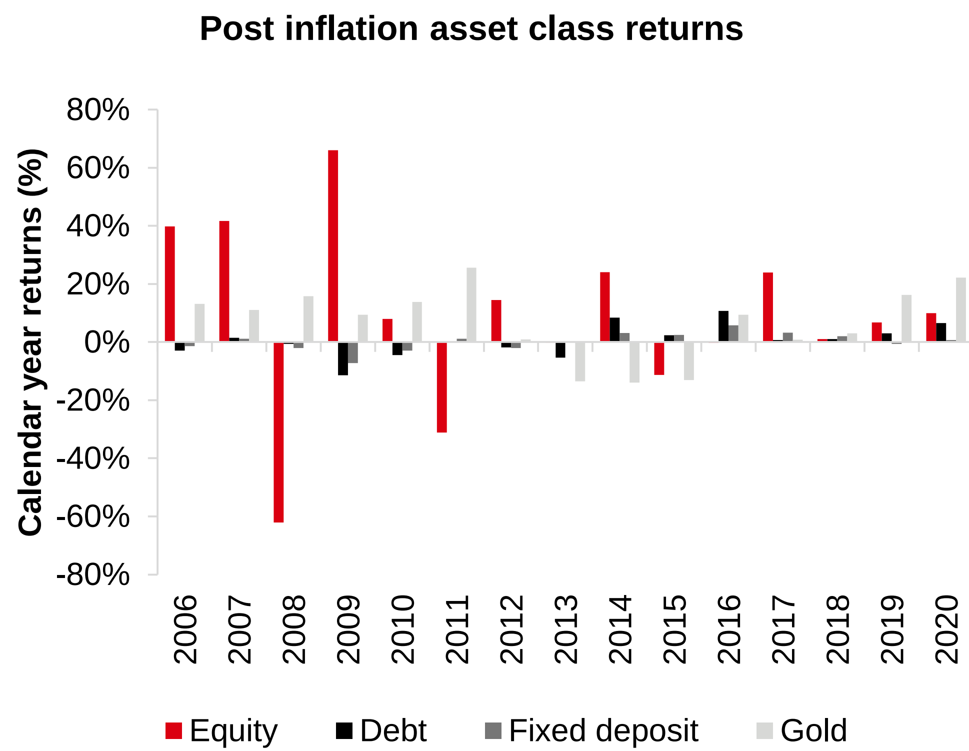
Regular investment in equity helps tackle the rise in cost of living and plan for future goals

Source: BSE, Labour bureau, CRISIL
Notes:
Equity returns represented by S&P BSE Sensex's average CAGR for 15-year holding period calculated on a daily rolling basis since 1979; data till Dec 2020
Inflation represented average of monthly inflation of industrial workers declared since January 1993 till November 2020
Past performance may or may not sustain, past performance does not guarantee future performance.

Calendar year returns show equity performs better than other assets

Pre- and post-inflation returns



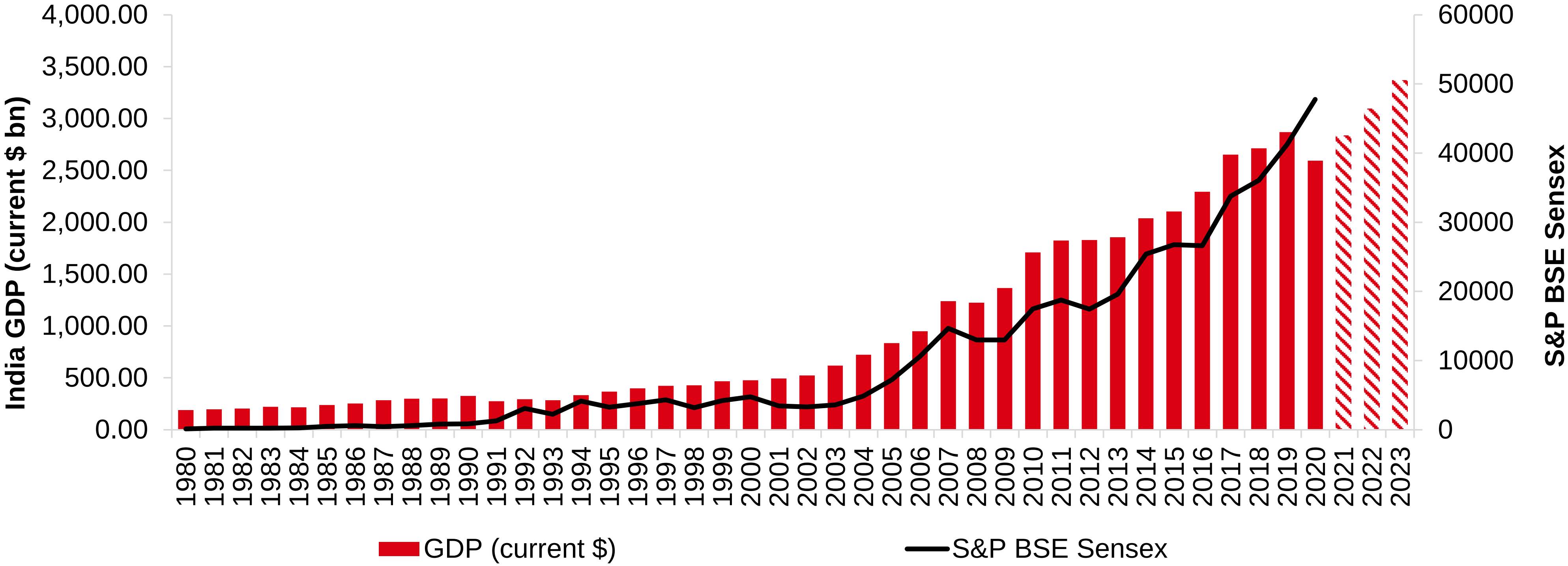


Equity has outperformed other asset classes in most calendar years

Source: BSE, CRISIL, Labour bureau
Notes:
Data as of December 2020
Year-on-year returns for all asset classes
Equity represented by S&P BSE Sensex, debt by CRISIL Composite Bond Index, fixed deposit rate represented by 1-year FD index, gold by Indian gold prices, and inflation by the annual CPI-Industrial worker. Past performance may or may not sustain, past performance does not guarantee the future performance.

Equity mirrors economic growth in the long term

India expected to remain on long-term growth trajectory



GDP data after 2020 are projections

Equity offers opportunity for long-term wealth creation

Source: BSE, IMF, CRISIL

Notes:

GDP projection starts after year 2020 and is shown shaded in this graph is for illustration purposes only and is not guaranteed.

The projection contained in this graph is for illustration purposes only and is not guaranteed.

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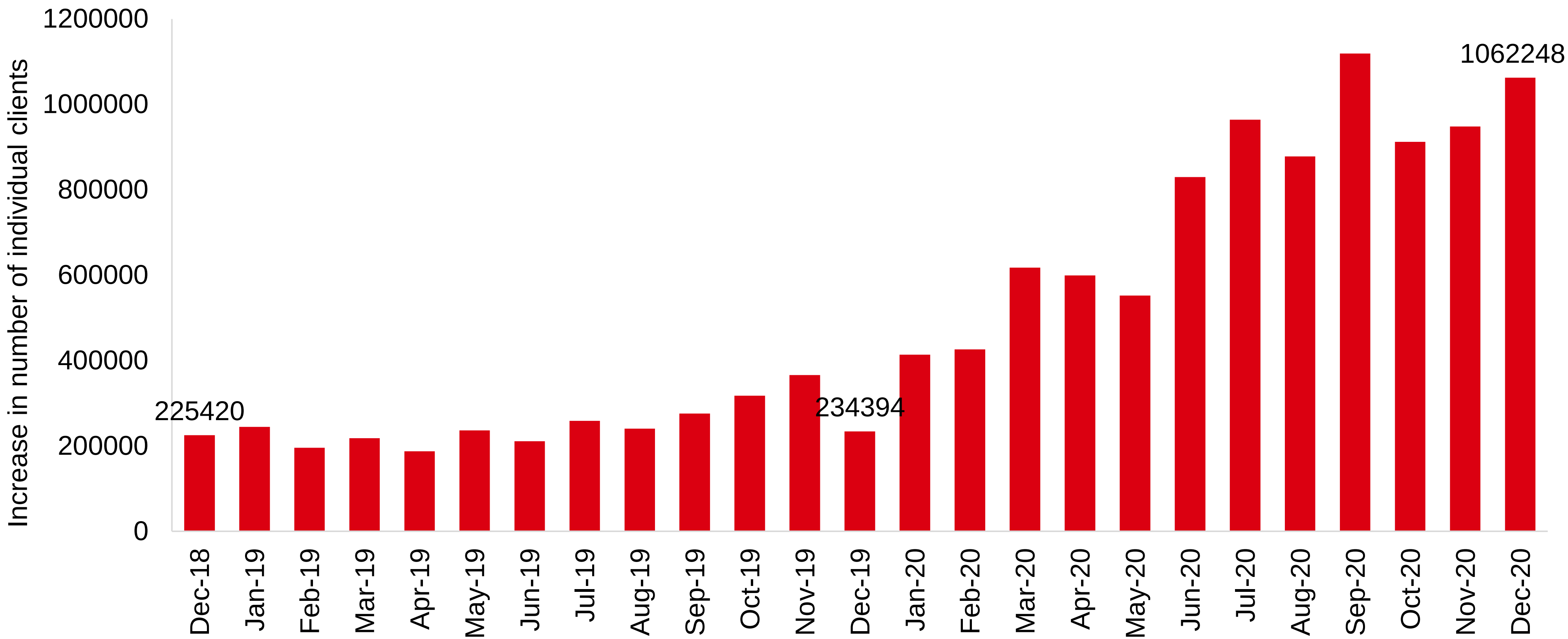
Mutual funds, a better alternative to investing in equity

Mutual fund investments are subject to market risks, read all scheme related documents carefully.
Past performance may or may not sustain, past performance does not guarantee the future performance.

Direct equity participation saw massive jump in 2020

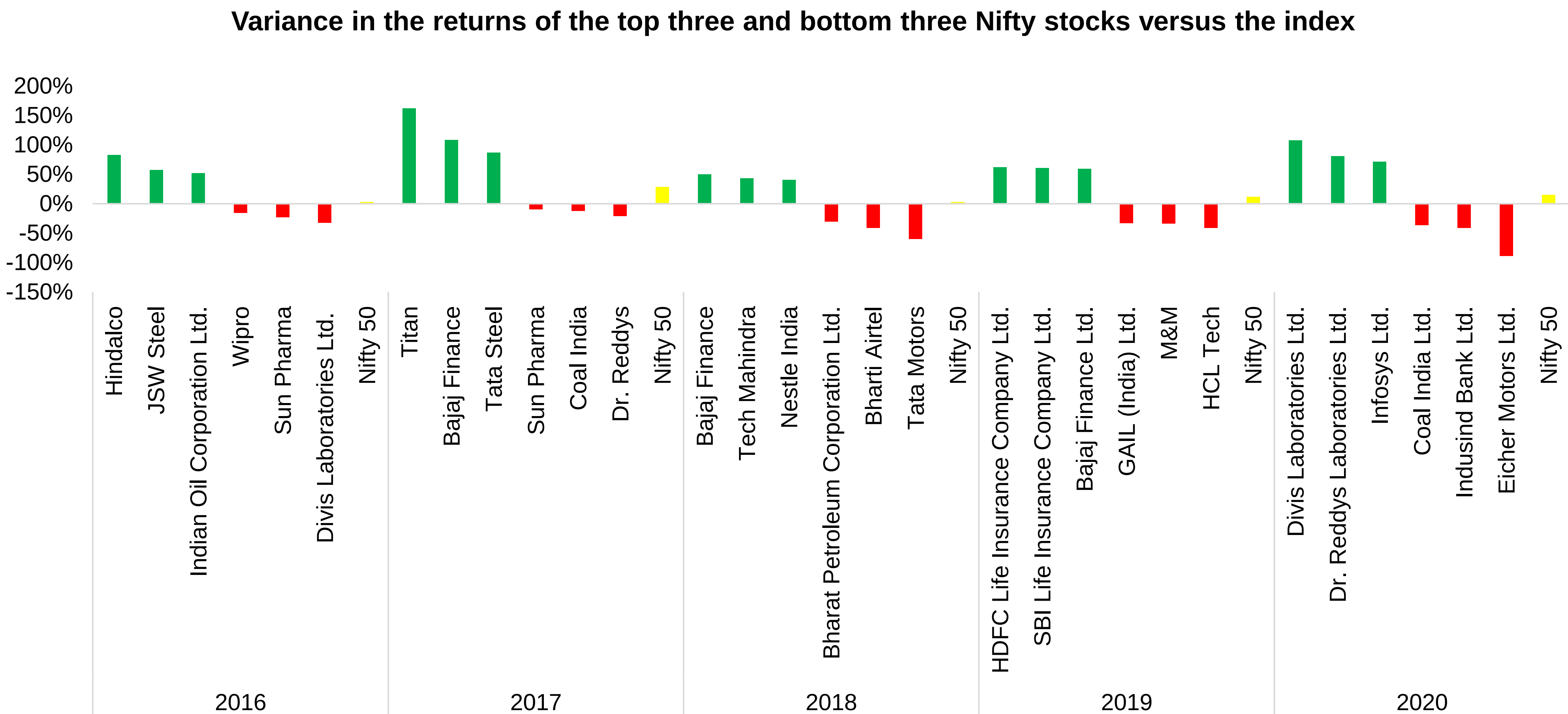
Surge in Demat accounts as equity market rallied to record highs



Despite market volatility brought on by the pandemic, the number of individual investors opening accounts for direct investments has surged.

Source: CRISIL, CDSL

Direct equity investment calls for proficiency in selecting stocks



The domestic stock market has over 5,000 listed stocks, which makes selecting the right stock for investment a herculean task

Source: NSE, CRISIL, Data till 31 December 2020
Nifty 50 stock composition as at December 2020 used for performance analysis
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Equity mutual funds are an optimal way to invest in equity

Lower cost compared with direct investment in capital markets via systematic investment plan (SIP). With an investment as little as Rs 500 a month, an investor can buy units of a scheme that invests in stocks and at no additional cost

Diversification: Mutual funds typically invest in a range of assets, which helps mitigate risks to a great extent

Liquidity: Mutual fund units can be redeemed for cash at any point, based on the prevailing net asset value of the units

Professional fund management since the fund manager is backed by a dedicated research team, and is able to make tactical calls based on market movement and prospects

Benefits of investing in mutual funds

Wider choice: Mutual funds offer a variety of schemes that may meet your needs across life stages. Passive investing via index funds and exchange-traded funds

Individual investors would be better off diversifying their investment through equity mutual funds, to benefit from the capital market over the long term

Mutual fund investments are subject to market risks, read all scheme related documents carefully.

Equity mutual funds provide an array of investment strategies and options

Raft of options available for both active and passive funds

Actively managed]		Passively managed	
Market-cap based	Flexi-cap	Index funds/ Exchange traded funds (ETFs)	Broad market tracking funds
	Multi-cap		
	Large-cap		
	Large & mid-cap		
	Mid-cap		Sectoral index tracking funds
	Small-cap		
Strategy-based	Dividend yield fund		
	Value fund		Global index tracking funds
	Contra fund		
	Focussed fund		
Thematic and tax saving	Sectoral/thematic fund		Smart beta index tracking funds
	Equity linked saving scheme (ELSS)		

Equity mutual fund investments offer a variety of options – both active and passive – across market capitalisation, themes and strategies

Mutual fund investments are subject to market risks, read all scheme related documents carefully.
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Choose SIPs to achieve long-term goals

Adopt a long-term systematic investing approach to tide over market volatility

Be calm and stay focused on investment goals + **Overcome behavioural biases such as panic selling or herd mentality** + **Adopt a systematic investing approach for equities, equity mutual funds over the long term** = **Actions to manage equity market volatility**

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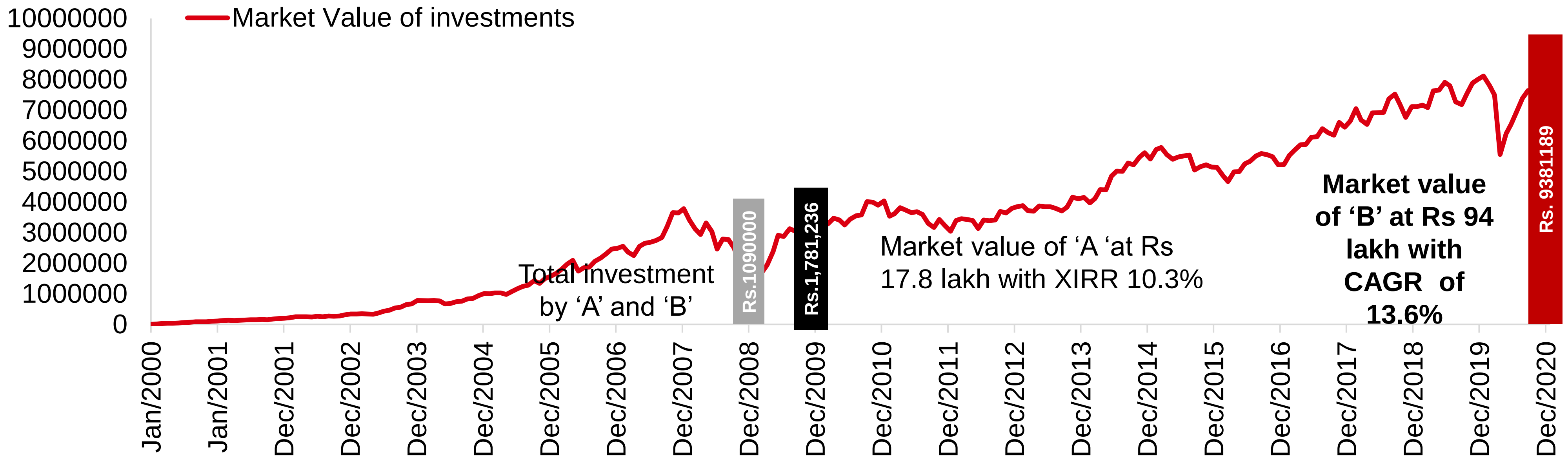
Investors who redeem/stop investments lose out on long-term opportunities

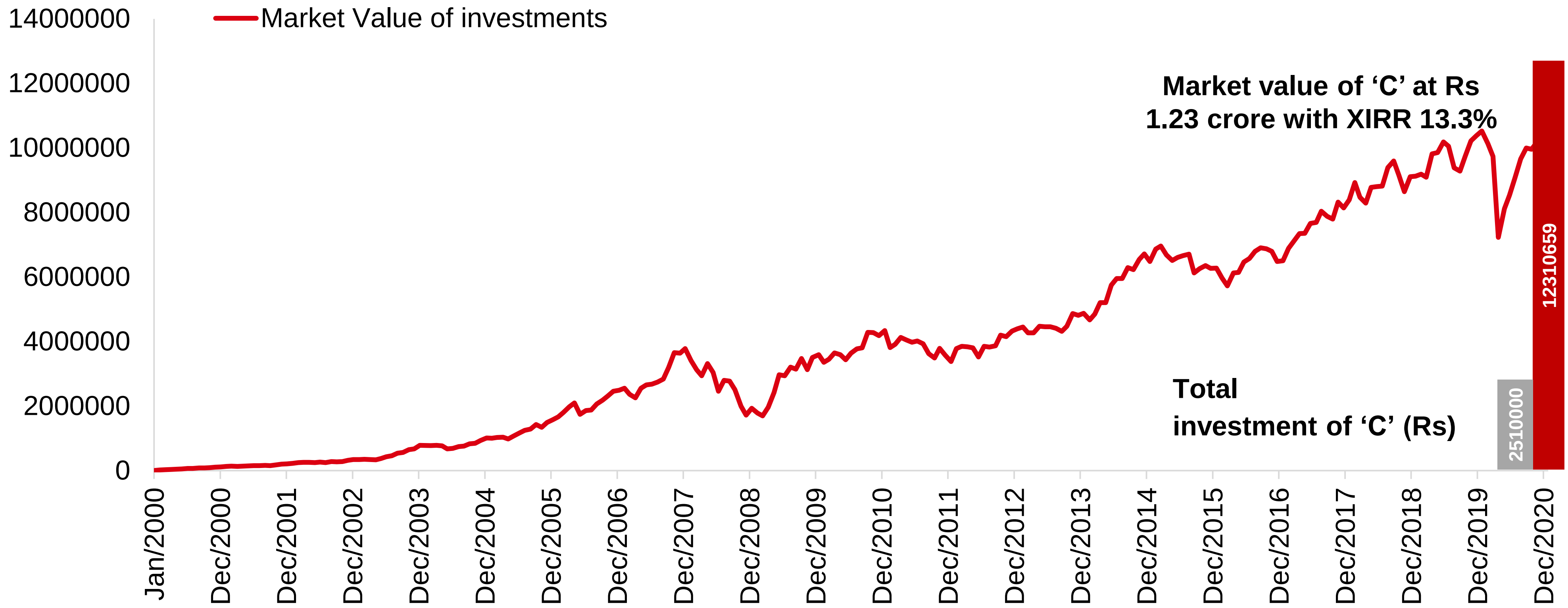
- A and B started their SIPs in January 2000, with both investing Rs 10,000 per month
- Everything was fine with their investments until the 2008 Global Financial Crisis (GFC)
- While A redeemed his investments, B stopped his investments, but did not withdraw his money
- A received ~Rs 17.80 lakh from his cumulative investment at an XIRR of 10.3% in 2009. B, who had retained his investments, had a corpus of ~Rs 93.82 lakh as of December 2020 (same amount of investment) and an XIRR of ~13.6%



Notes: The performance is calculated till December 31, 2020
Data as at December 31, 2020
Monthly SIP of Rs10,000 in S&P BSE Sensex from January 2000 on the first day of the month
Past performance may or may not sustain, past performance does not guarantee the future performance
Source: BSE, CRISIL Research

Investors who continue their SIPs gain from long-term opportunities

- C started investing Rs 10,000 per month in January 2000 and persisted with his investment over the years. His total investment of Rs 24.1 lakh had a market value of Rs 1.23 crore in December 2020 with an XIRR of over 13.3%



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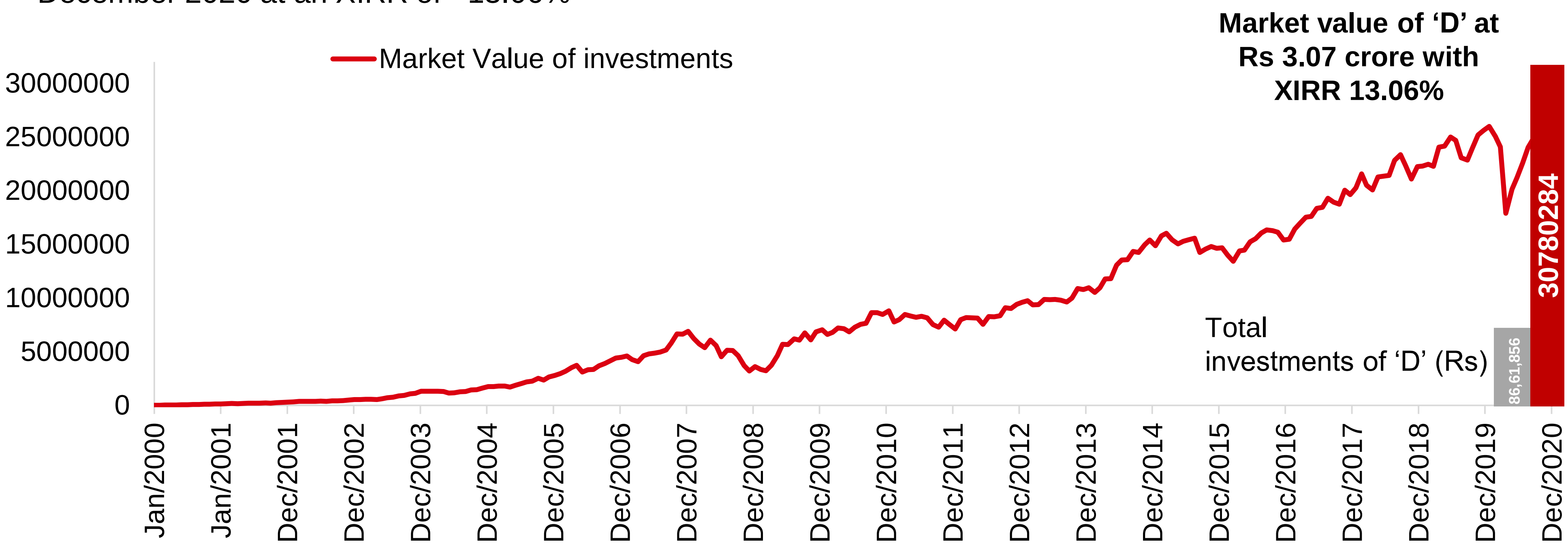
Source: BSE, CRISIL Research

Investors leverage market downturns to derive higher benefits (1/2)

Incremental SIPs during market downturns

- D had a similar starting point of investment journey by investing Rs 10,000 per month since January 2020
- However, he increased his monthly investment value by 10% every time the market fell 10% in a single month
- This increased SIP investment is retained till the next similar fall and the process continues
- The resultant impact on his investment of ~Rs 87 lakh is visible – his investment compounded to Rs 3.07 crore as of December 2020 at an XIRR of ~13.06%

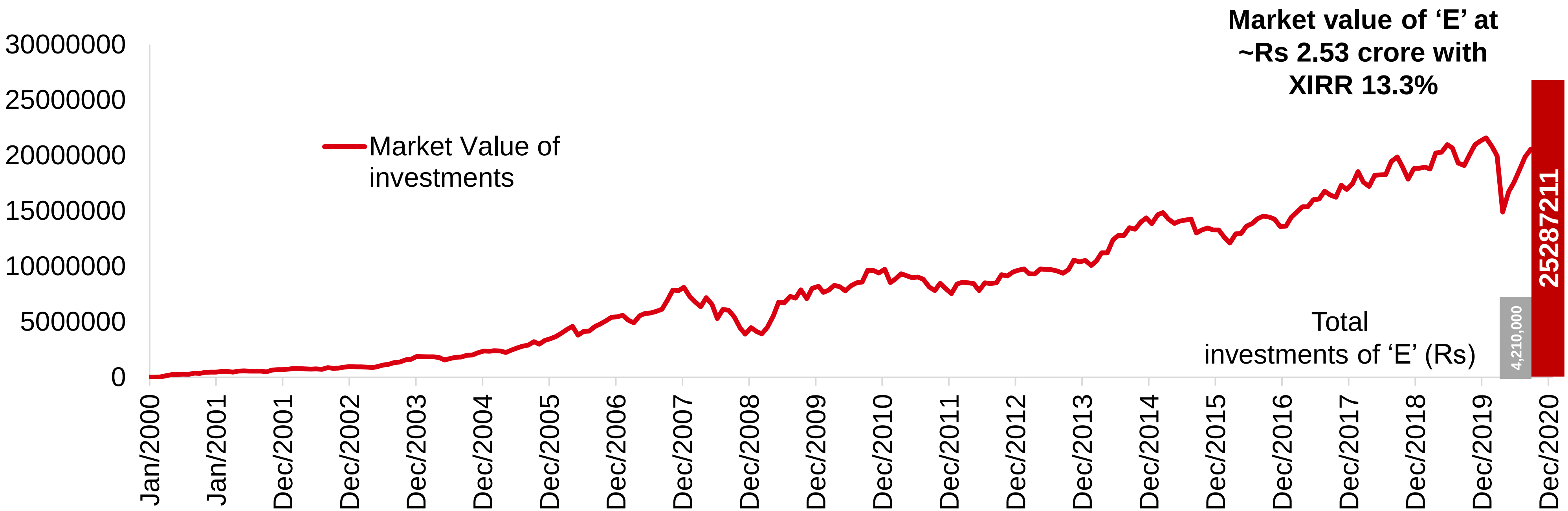


Note: The performance is calculated till December 31, 2020
Data as at December 31, 2020
Monthly SIP of Rs.10,000 in S&P BSE Sensex from January 2000 on the first day of the month
Past performance may or may not sustain, past performance does not guarantee the future performance.
Source: BSE, CRISIL Research

Investors leverage market downturns to derive higher benefits (2/2)

Lump sum investment additions during market downturns

- E made lump sum investments during market downturns to derive higher benefits
- He invested Rs 1 lakh each month after markets fell 10% in a single month, in addition to his regular SIP amount of Rs 10,000 (total of Rs 1.1 lakh)
- As a result, his investment of Rs 42.1 lakh grew to ~Rs 2.53 crore in December 2020 at an XIRR of 13.3%



Source: BSE, CRISIL Research
Notes: The performance is calculated till December 31, 2020
Data as at December 31, 2020
Monthly SIP of Rs 10,000 in S&P BSE Sensex from January 2000 on the first day of the month
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Look beyond market downturns and stay invested in SIPs for the long term

- Even if SIPs remain in the red, stay invested for the long term as gradual market recovery will increase corpus value and overall SIP returns
- We undertook a scenario analysis to understand the implications of various types of mutual fund investor behaviour during market volatility, and the associated benefits
- Investors A, B C, D and E began investing Rs 10,000 in an equity SIP in S&P BSE Sensex from January 2000. However, their approach to market volatility differed:
  - A redeemed his investment after the GFC
  - B stopped SIPs due to the volatility seen during the GFC, but retained his investments
  - C continued his SIP at the same pace
  - D increased his monthly SIP investment by 10% after every monthly fall of more than 10%
  - E added a lump sum investment of Rs1 lakh after every monthly fall of more than 10%

	A	B	C	D	E
Total amount invested (Rs lakh)	10.9	10.9	25.1	86.6	42.1
Total value at the end of Dec 2020 (~Rs lakh)	17.8	93.8	123.1	307.8	252.8

How they fared

- A missed out on accumulating more units and increasing his corpus, while B benefitted from retaining investments, but could not leverage gains in rupee terms
- C persevered and benefitted from his disciplined investments. However, D and E leveraged market downturns to invest more and boost their end-investment corpus

Source: CRISIL, Data as at December 31, 2020
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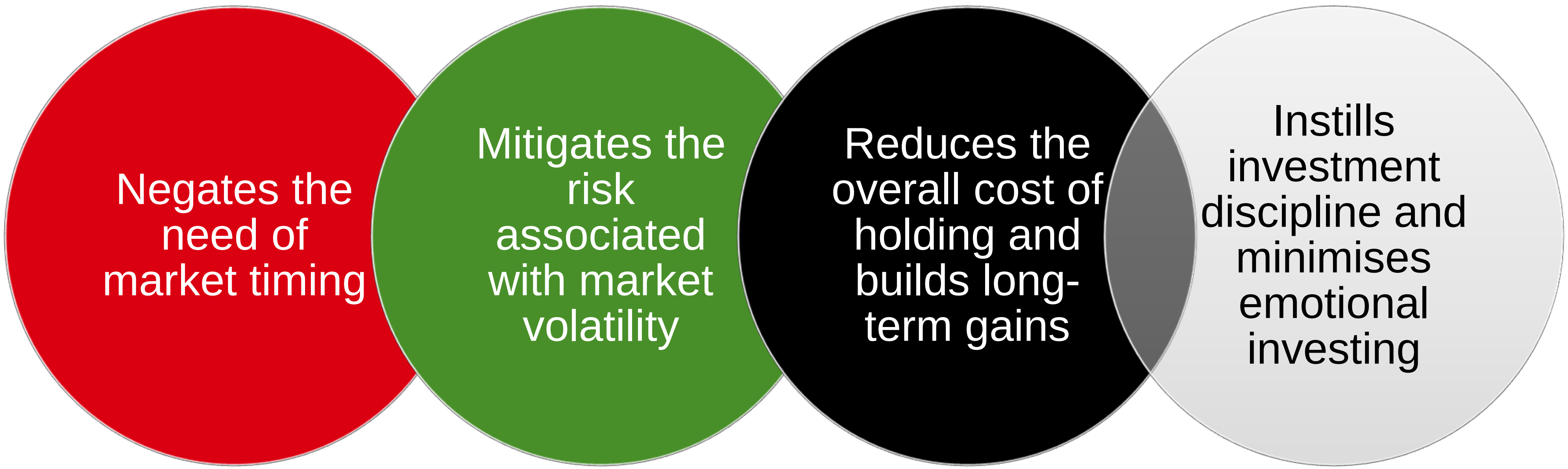
Rupee cost averaging

- SIP ensures a regular fixed investment at different points of time, which ultimately results in investors buying more units when market falls and less units when market rises. This averages the cost per unit of investment (rupee cost averaging)
- Rupee cost averaging is beneficial for investors in many ways as shown below



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Achieve your long-term goals

Rahul and Nakul can achieve their goals of funding their kids' education with a lower investment by investing systematically in equity mutual funds. The surplus can be used to target other life goals

	Fixed income instruments	Equity
Goal	Higher education for kid	
Current cost of goal	Rs 8.8 lakh*	
Goal period	15 years	
Future cost	Rs 24.28 lakh^	
Monthly investment amount needed to achieve goal	~Rs 3,587@	~Rs 7,261#

Systematic investments in equity provides optimum results for investors over the long term

Notes: Source: CRISIL

*IIT Bombay,

Assuming inflation of 7%, which was the average inflation rate of industrial workers since January 1993 till November 2020

@Grown at 15% represented by S&P BSE Sensex's average CAGR for 15-year holding period calculated on a daily rolling basis since 1979; data till December 2020

#Grown at 7.54% represented by 1-year FD index returns between October 1999 and December 2020

The projections in this graph are for illustration purposes only and not guaranteed

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In a nutshell

Equity is a long-term capital growth solution

- The future is uncertain; prediction is risky
- Preserve and, if possible, grow capital on a real-term basis over the long term
- Avoid permanent capital impairment through risk-averse capital allocation
- Target outperformance only over a full cycle
- Invest systematically in equity over the long term to derive optimum investment results

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"Someone is sitting in the shade today because someone planted a tree a long time ago" – Warren Buffett

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HSBC Asset Management (India) Private Limited, 16, V.N. Road, Fort, Mumbai-400001
Email: hsbcmf@camsonline.com | Website: www.assetmanagement.hsbc.com/in

Mutual fund investments are subject to market risks, read all scheme related documents carefully.