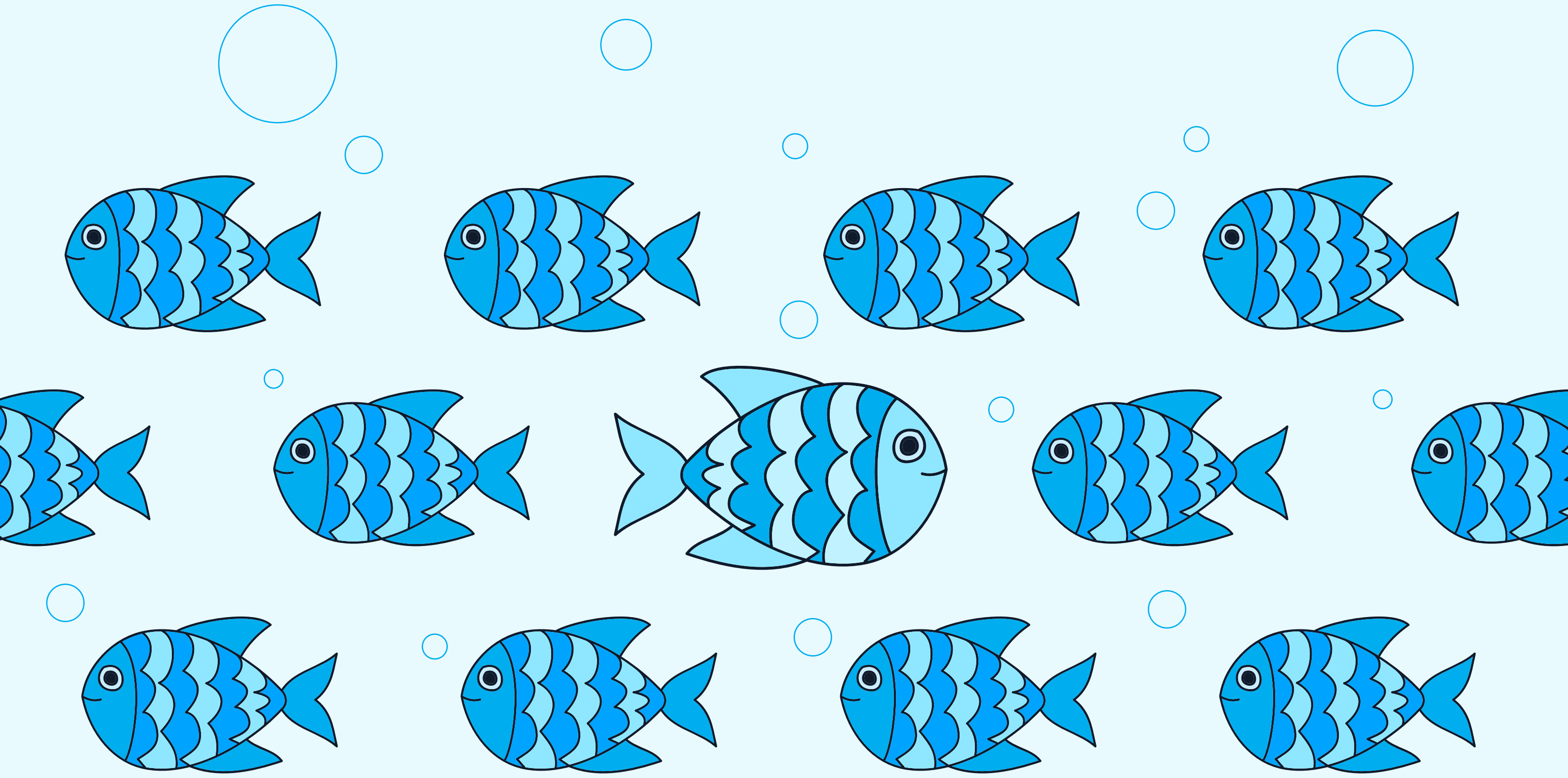
HDFC MUTUAL FUND
BHAROSA APNO KA

Monthly Musings

September 2022



Standing Out!

How to avoid herd behavior?

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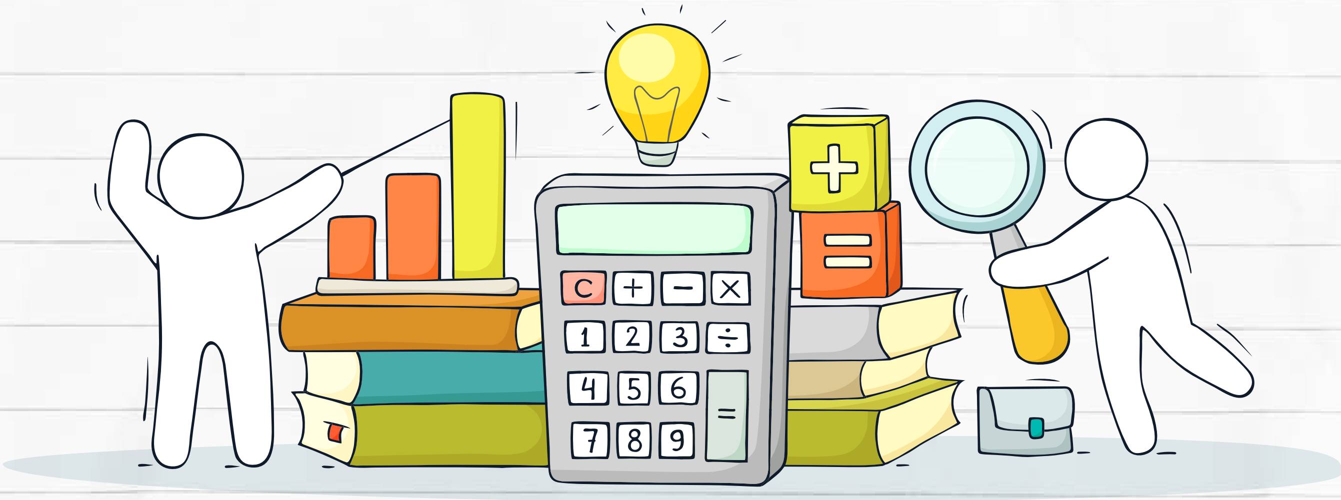
Message from Navneet

On a bright pleasant Sunday afternoon you are walking down a busy street full of restaurants and shops. After a busy morning of shopping, you are feeling a sense of accomplishment and now want to grab a quick lunch before signing off. Name boards and well known logos of restaurants are extending an over eager welcome to you. You are spoilt for choice. Most of these restaurants are less crowded but there is one which is filled to the brim with more people heading in than those on their way out. All of them are well known brands. What do you do?

Most people in this scenario, would end up choosing the restaurant which is relatively more crowded as the higher footfall would give an illusion of it being the better option. You can replace the restaurant in this scenario with a movie, an apparel shop, a travel destination, so on and so forth.

This tendency of people to blindly follow and imitate the behaviour of a wider group, without using one's individual thinking is commonly known as herding – and this is practically visible in most aspects of our lives, from the most mundane ones to the most complex too. Sometimes this has a rather harmless outcome, like the restaurant example above; whereas in certain instances, herd mentality could have seriously adverse instead of outcomes, like stampedes for instance.

Financial markets have been no exception to this. Time and again, financial markets have seen bubbles and crashes on account of herd mentality from investors. We don't have to go a long way back in time to see shades of this behaviour among the masses. 2020 – A year like none other in recent times. It was a year when things escalated quickly. It was also a year where things spread like wild fire. We are not referring to merely rumours and virus here but something equally dangerous from a financial standpoint – herd mentality. In the aftermath of the pandemic, as financial markets started recovering sharply from their covid-bottom, speculative and crowd-following approach from investors knew no bounds.



In this edition of our Monthly Musings, we delve deeper into this behavioural bias and hope that your investment journey is driven more by a financial plan and less by crowd.

To this effect, our commitment towards investor education remains as strong as ever. We recently launched a landmark initiative viz. Investverse with NSE Academy to empower next generation of investors with knowledge on the world of investing, delivered via our MF Bytes app. We also launched our 'Investverse' podcast on 30+ platforms. This podcast hopes to take its listeners on a journey into the world of investments and encourages them to start their own investment journey.

I would like to take this opportunity to inform you of our other new initiatives including the launch of HDFC Silver ETF. With festive season around the corner, investors can consider investing in HDFC Silver ETF and HDFC Gold ETF, instead of physical gold and silver. Our bouquet of ETFs expands further this month, with the launch of our QVG (Quality, Value, and Growth) Smart Beta ETFs. The NFO period for the QVG Smart Beta ETFs runs from 9th to 20th September 2022.

Hope you find this edition of HDFC MF Monthly Musings informative and helpful.

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Cover Story

Avoiding Herd Mentality in Investing

Why following the herd comes naturally to us?

When we get out of a flight, it's normal to simply walk in the direction where majority of the people are walking. Mostly it's ok to do that, as everyone is probably moving towards the exit. Further, each zone in an airport is clearly marked and unauthorized entry in each zone is restricted. But it may not be safe to 'follow the herd' in many other situations.

It's safer for a zebra to stay with the herd. But, this may not apply to every situation!

These days it's so much pleasure to watch nature and animal documentaries with the improved cameras, movie-making techniques and the quality of our televisions. Like many animals in the wild, zebras usually move in herds, staying close to one another. Herding helps them to use their unique skin pattern to their advantage. Lions find it difficult to spot any one particular zebra as they get confused with the mass of many moving stripes. Even the weaker zebras enjoy better life expectancy by being part of the herd.

Unfortunately, we may not be able to draw a parallel from zebras when it comes to investing. The herd behavior that we witness in the world investing often surrounds a fad. The recent crypto craze is one such example. Many investors jumped into the trend, while simply sticking to the basics approach could have resulted in better outcomes in the long term. Remember, when zebras move in a herd, they are sticking to basics in their own way.

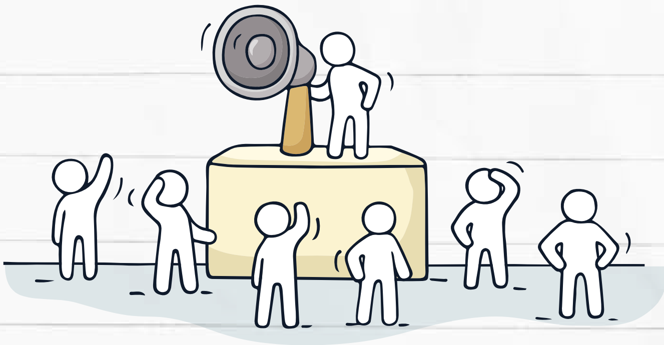
Some examples of herd behavior from the history of investing

Historically, there have been many instances when investors jump in at the peak of a market cycle, across various asset classes and exit with substantial losses. Ironically, investors have been willing to take high levels of risk at a time when a market rally becomes overheated. Some of these instances are listed below:

- Dot-com stocks during the late 1990s
- Credit default swaps during the run up to 2008 Global Financial Crisis
- Crypto currencies during recent times
- Tulip flowers during the 17th century Dutch Republic

In most of these occasions, the mistake of joining the herd is likely to have proven costly for many investors. In fact, the losses incurred during these times could leave an indelible mark in the memories of the investors that they turn extremely risk averse in future.

Do we need to stand out every time? Not exactly!



Herd behavior is not something we should feel guilty about. It comes naturally to us. Whenever we are not sure as to how to act, we look towards what others are doing for a cue. We all want to be accepted as part of the social set up. It is normal for most of us to take into consideration the social norms while making key decisions including buying a house, car, taking a vacation, venue for the child's birthday party, etc. Social norms even apply to how we speak, stand, nod our head, etc. What's interesting is that these considerations come naturally to us without even having to think. The idea logically extends to investing as well.

Sometimes we accept additional risks just because others are taking them. Imagine scolding a kid as to 'why she got drenched in the rain?' The most likely response to the question would be 'all my friends did it, so I did too!' Similarly, many investors got into the crypto mania as a lot of others were doing the same without considering the risks. It is normal to feel left out when all your friends are into commodities or options trading through a newly launched app in the market. It is definitely ok to find out more information about these new 'avenues'. However, one should try and avoid the mistake of committing too much capital in the process.

How to avoid being pulled into a herd?

Taking the help of a professional financial planner can be a good start. Do we follow the DIY approach (Do It Yourself) when it comes to medical treatments? No, because it can be dangerous. Same applies to investing. Even a basic financial plan is likely to involve ascertaining your risk profile, long term goals and forming an ideal asset allocation. Once we follow these basics, you become relatively less likely to blindly follow what others are doing.

When your friend discusses the 'next big new investment idea' with you, your immediate reaction is likely to be "how would this fit into my asset allocation"? If you place a stringent personal filter that any new investment idea needs to pass the test of answering this simple question, it is easier to avoid being pulled to into herds.

Join the 'Healthy Herd'- The SIP Revolution

If you are exercising more, eating healthy, paying your taxes on time, donating for good causes, and so on, just because you find many others doing it, that's great! There are many such examples of healthy herding.

As on July 2022, there were ~5.62 crore mutual fund SIP (Systematic Investment Plan) accounts and ~ Rs.12,140 crore were the SIP inflows received in the month of July 2022. It's nothing less than a revolution of a massive scale that is currently underway. The simple SIP is gradually becoming the staple investment vehicle for many Indian households. While there are many reasons why SIP is an ideal choice in investing, a lot of investors may have started an SIP just because many others, including their friends and relatives, are doing the same. So, herding need not be harmful in all circumstances. However, it is important to know your investments in detail and keeping yourself updated over time.

SIP – Systematic Investment Plan
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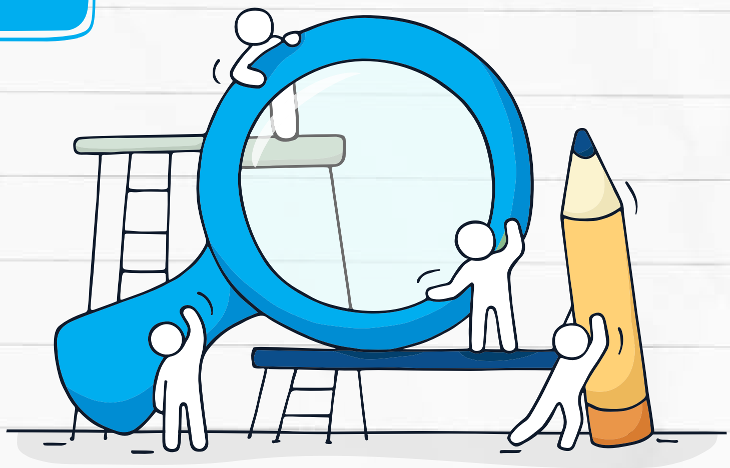
Jargon De jargonised

Earnings Yield



There are various parameters used to gauge whether the markets are expensive or cheap; price to earnings, price to book, market cap to GDP are few common valuation indicators. Another valuation indicator that is often used is "Earnings Yield".

What is Earnings Yield?

Earnings yield is a financial ratio that describes the relationship of a company's earnings per share (EPS) to the company's stock price per share. The earnings yield is the inverse ratio to the price-to-earnings (P/E) ratio. The formula for Earnings Yield is E/P, earnings divided by price.

This ratio is often used at aggregate level for the entire market wherein we compare the earnings yield of all the companies that are present in the index to the index level. Just to give you an example, say the NIFTY 50 index is currently trading at 17,600 and the weighted average EPS of the NIFTY 50 constituents is around Rs 900; earnings yield of the NIFTY 50 index or the markets is 900/17600 = 5.1%.

GDP - Gross domestic product

How to use this metric?

To gauge the attractiveness of the market or a particular stock, this metric is used on absolute or relative basis. Comparing the current earnings yield to its historical average is an absolute method. If the current yield is higher than the historic average, the stock or the market is attractive.

Similarly, under relative method, one can compare the yield of the market to the yield of another asset class, say bond. So, if bond yields are higher than earnings yield then it can be construed that bonds are more attractive than equities and vice versa.

Smart Choices

Staying invested for long term VS Frequent Changes

Individuals in search of quick gains often get carried away, follow the crowd and make frequent changes to their portfolio when they hear stories about someone making big money in stocks/sectors/asset classes. This mentality is often the result of a reaction to peer pressure which makes investors 'act' in order to avoid 'feeling left out' or 'left behind' from the group; also known as FOMO (fear of missing out). Experience tells us that making frequent changes to your portfolio based on this behaviour has often been futile or even harmful.

When an investment falls by a certain percentage in a short period, investors often panic and are provoked to react to the situation. Just to give you an example, say Mr. XYZ had invested in an equity MF scheme a month back, the NAV as on today is down by 5% from the investment date.

What option does the investor have?

A Sell, because the investment is at a loss

B Wait till it goes above the cost price and then sell

C Buy more

D stay invested for long term

Impact of making frequent changes while investing:

Most of the individuals because of their impulses/instincts and urge to act will choose either of the options A to C. However, reacting based on one's instincts in investments can have a negative impact on the portfolio. The negative impact on the portfolio is usually a result of buying at the peak and selling at the bottom. This may also lead to portfolio becoming skewed towards few stocks or sectors and one may end up running a high concentration strategy. Frequent churning also leads to high transaction cost (like brokerage, taxes, etc.) which may impact the net returns.

How does one deal with this situation: History and experience tells us that Option D is an ideal option.

Simply Invest in Mutual Funds and Follow the Stay Invested Approach.

Why "Stay Invested" approach is a Smart Choice?

- ☑ Risk in equities reduces with long term approach
- ☑ No need to lose sleep over market movements
- ☑ No need to track your investments every now and then
- ☑ No urge to keep 'doing something

No doubt laziness and forgetfulness are negative human traits, but for individual investors, it could prove useful to "stay invested" for a long time.

For disclaimers refer page 16

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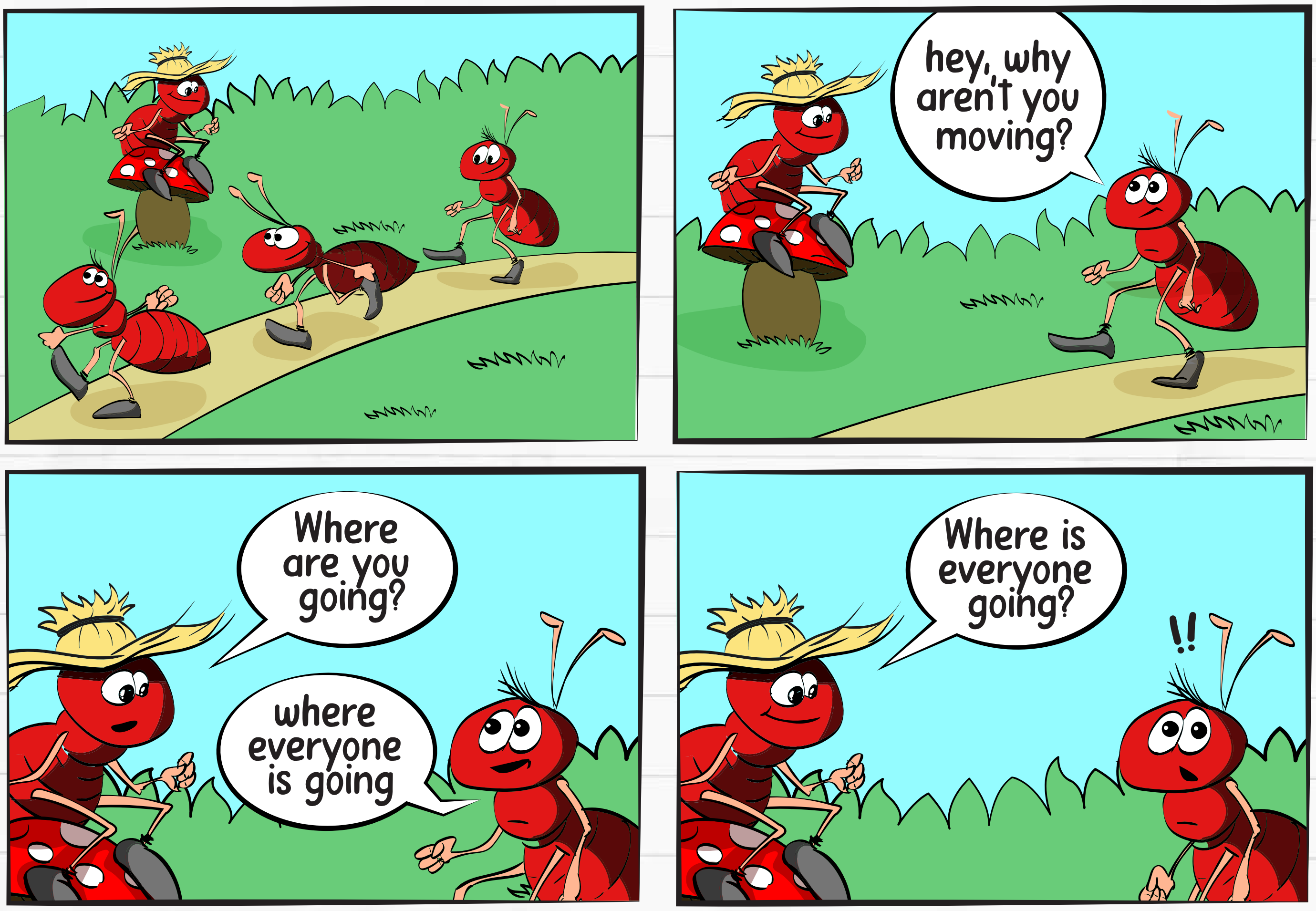

How not to follow the crowd?

As far as ants go, they are extremely smart creatures with great communication skills with special sensors, helping them to form well-coordinated teams to locate food, defend territories and alert each other to the presence of predators.

With the above illustration, we only try to explain the concept of herd behavior and that blindly following others may not be the right thing to do when it comes to investing. Many of us do look up to the crowd for cues while investing and end up getting caught at the peak of a market cycle. Taking the help of a trusted financial advisor to form asset allocation can be helpful to avoid such behavioral mistakes.

A smart way to learn about Mutual Fund investments

HDFC MFBytes

Your one-stop knowledge hub for your Mutual Fund needs
Explore the app today and learn more about Mutual Funds through fun activities!

Things you can learn through the app

1 Investment concepts

2 How to save tax

3 Goal based investing

...and much more!

Click here to know about why you should invest early

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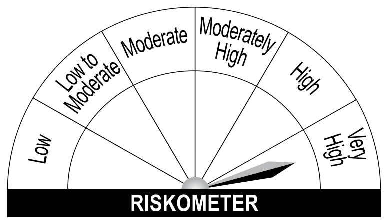
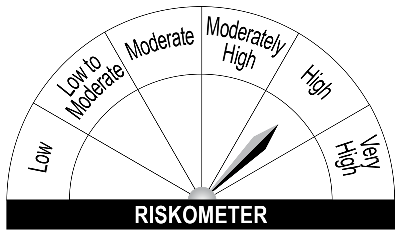
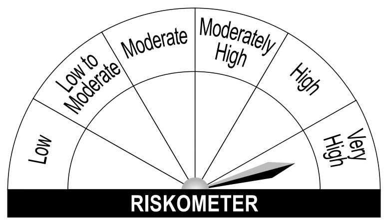
Name of Schemes	This product is suitable for investors who are seeking*:	SCHEME RISKOMETER#
HDFC SILVER ETF An open ended Exchange Traded Fund (ETF) replicating/tracking performance of Silver.	• Returns that are commensurate with the performance of silver, subject to tracking errors, over long term. • Investment predominantly in Silver bullion of 0.999 fineness.	 Investors understand that their principal will be at very high risk
HDFC Gold Exchange Traded Fund An open ended scheme replicating/tracking performance of Gold.	• Returns that are commensurate with the performance of gold, subject to tracking errors, over long term • Investment predominantly in Gold bullion of 0.995 fineness	 Investors understand that their principal will be at high risk
HDFC NIFTY100 QUALITY 30 ETF An open ended scheme replicating/tracking NIFTY100 Quality 30 Index(TRI)	• Returns that are commensurate(before fees and expenses) with the performance of the NIFTY100 Quality 30 Index(TRI), over long term, subject to tracking error. • Investment in securities covered by the NIFTY100 Quality 30 Index	
HDFC NIFTY50 VALUE 20 ETF An open ended scheme replicating/tracking NIFTY50 Value 20 Index(TRI)	• Returns that are commensurate(before fees and expenses) with the performance of the NIFTY50 Value 20 Index(TRI), over long term, subject to tracking error. • Investment in securities covered by the NIFTY50 Value 20 Index	 Investors understand that their principal will be at very high risk
HDFC NIFTY Growth Sectors 15 ETF An open ended scheme replicating/tracking NIFTY Growth Sectors 15 Index(TRI)	• Returns that are commensurate(before fees and expenses) with the performance of the NIFTY Growth Sectors 15 Index(TRI), over long term, subject to tracking error. • Investment in securities covered by the NIFTY Growth Sectors 15 Index	
*Investors should consult their financial advisers if in doubt about whether the product is suitable for them.		

For latest riskometer, investors may refer to the Monthly Portfolios disclosed on the website of the Fund viz. www.hdfcfund.com

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Exchange Traded Fund (ETF).

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