

Keep Lemons Out Of Your Fund Portfolio

Do you have the knack of getting grounded with duds? Fret not, here are some simple ways to ma

SUMVED Sane (name changed), a lawyer, calls successful equity investing a gamble or a game of luck. He is not a reckless trader or a naive investor. He has been an equity mutual fund investor for the past five years. However, though the BSE Sensex has almost trebled since January 2005, Sumved's money has only doubled. His obsession with new fund offers (NFOs) and best-performing funds based on short-term returns has landed him mostly in the company of underperforming funds.

Sumved is not alone. Innumerable investors fall for eye-popping short-term returns or follow a star fund manager or invest in hot sector funds or become victims of NFO campaigns.

Investors need to be frank with themselves — if they feel that they don't have the expertise to choose the right fund, then they should avoid doing so. There are other ways to make decent returns that are definitely better than what underperformers will give them. Read on to discover more:

Index Funds: Around 64% of large-cap equity funds underperformed the S&P CNX Nifty over five years to June 2010, according to the second edition of S&P Crisil SPIVA fund scorecard. So, while star fund managers can go to town claiming that India remains a stock-picker's paradise, there is growing evidence that active fund management is indeed facing problems. This is where index schemes come in: They do away with the fund-manager risk and offer cost-efficient returns. All you have to do is to invest in a fund with the minimum tracking error — the difference between the performance of the scheme and that of the benchmark index.

If you are a long-term investor with no view on a particular sector, it is better to own a diversified benchmark index than a sectoral index. Stick to your asset allocation and keep rebalancing your portfolio at regular intervals. You must also book profits as the index fund will not book it for you.

But be prepared to face the advocates of actively-managed schemes. "Index funds weather the downturn in a market better than most of the diversified equity funds, but in the long run outperformance can be brought to the portfolio using good diversified equity funds with a good long-term track record," says Abhinav Angirish, managing director, investonline.in, a mutual fund distributor.

But here, we are dealing with investors, who do not possess the necessary skills to spot the best diversified schemes. So, they shouldn't mind a slightly weaker performance of an index scheme — if at all there is any, that is.

Fund Of Funds: You have two options here. One, you can choose Asset Allocation Funds offered by fund houses such as Birla Sun Life, ICICI Prudential, IDFC and Franklin Templeton. They invest in a judicious mix of debt and equity funds factoring in the risk profile of the investor. If you are conservative, go for conservative option in Asset Allocation Funds.

The second option is to go for schemes that invest

Of course, the funds in which the money is invested have their own expenses, leading to duplication of costs. "Fund of funds is treated as a debt fund for taxation purposes and that reduces the post-tax returns offered by these funds compared to equity funds," points out Dhruv Raj Chatterji, senior research analyst with Morningstar India. "Most of the fund of funds schemes that invest in Indian mutual fund schemes, have failed to offer top quartile returns consistently," says Angirish.

But again, we are looking at this option only for the convenience of avoiding the task of choosing the best-performing schemes.

Research Services: When you don't have the time or skills to identify the right schemes, why not hire the services of someone? In most cases, the research comes free. The service providers make their living on the 'commissions' they earn on your investments in various schemes. The commissions may push the investor's interest to the backseat. In that case, you can always look for independent advisory services.

"Subscribing to independent research ensures that there is no conflict of interest and you get unbiased advice," says Vipin Khandelwal, CEO, personalfn.com, an independent mutual fund research provider. Such services come out with recommendations on individual schemes and also offer ideal portfolios. They keep their subscribers informed about updates in their recommended schemes. For example, a change of fund manager in a recommended scheme may not be noticed by an investor, but the research house may not only report it but also advise the future course of action that the investor should take. For independent opinion, you have to pay an annual fee and also take care of your transactions.

Portfolio Management Services: If you have more than ₹5 lakh to invest and do not want to get into research and executing transactions, portfolio management services may be an option worth exploring. Broking firms invest your money in a judicious mix of equity and debt schemes, taking into account your risk profile and your return expectations. Some of them charge a fee of up to 1% of the money invested for offering these services. Services include timely monitoring and monthly updates on your portfolio. You will get a pass-through statement that will tell you how many stocks you own on a consolidated basis. For example, if the broker has invested in five different schemes and out of these four have invested in Reliance Industries, the pass-through statement will tell you how much of your money is invested in Reliance Industries. It gives a clearer picture to the investor of the risks involved.

"We book profits at regular intervals taking into account the asset allocation of the client," says Hiren Dhakan, associate fund manager, Bonanza Portfolio. The power of attorney enables the brokerage to do this, which a fund distributor cannot do. But given little publicly available information about the performance of these services, investors have to

HERD ON THE STREET

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GROWTH FORMULA

Avoid choosing a fund if you do not have the expertise to do so. You can look at the following products to boost your portfolio:

Product	Level Of Customisation	Minimum Investment	Cost (p.a)	Exit Load*	Liquidity	Transparency
Index Funds	Low	₹5,000 or 1 Unit	1.50%	1.00%	High	High
Fund of Funds	Low	₹5,000	0.75%	1.00%	High	High
Fund Research Services	Low	NA	₹2,500 to ₹5,000	NA	NA	Medium
Mutual Fund PMS	High	₹5 lakh	0.5-1%*	1.00%	High	Medium

Exit load applies to non-listed index funds, fund of funds and PMS if the investor exits within one year from the date of allotment of units
* The fee is for one year but can be paid quarterly

PEARLS OF WISDOM

Accept the fact that you do not have the time and skill to identify a good money manager

While investing in index funds, do asset rebalancing at regular intervals

Barring Asset Allocator Funds, Fund Of Funds do not book profits

Research services can deliver for you, if and only if, you are disciplined and can take care of transactions

A mutual fund portfolio management service ideally takes three years to deliver returns

SOME PITFALLS

- Investing in new fund offers that have nothing new to offer
- Chasing hot sector funds
- Investing in a fund looking at short-term gains
- Preferring a star fund manager over process-driven fund houses
- Failing to track the funds' performance at regular intervals

