The need to build a portfolio of Mutual Fund schemes

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India's capital markets have witnessed an increase in retail participation in the last few years post the popular "Mutual Fund Sahi Hai" campaign. The monthly contribution from SIP (Systematic Investment Planning) has risen to over Rs 12000 crore as compared to little over Rs 3000 crore in the last 5 years.

Many investors starting their investment journey are unsure of where to begin when it comes to mutual funds. There has been a tendency to select the top performing mutual fund scheme with a recency bias as displayed by a simple internet search. However, this might not be the best solution to plan for generating long-term and sustainable wealth. Investors could end up with sub-optimal returns due to their fund underperforming when the tide turns. Also, in volatile market conditions, many investors panic, thus nervously exiting prematurely.

Successful investors have learnt with experience that diversification is a must to invest for every market situation.

Diversification across asset classes such as Equity, Debt and Gold is an accepted principle to reduce overall portfolio volatility. The idea is that when one asset class is not doing well, the other asset class would support the portfolio and the overall portfolio would still be able to generate reasonable returns with lower volatility.

Relating with the sport of football; domestic equity provides growth opportunity like a forward player who scores the goal, international equity exposure provides support like the mid fielder, fixed income provides stability like the defender and gold.

There are a wide variety of mutual fund schemes catering to each one of the asset classes above and investing in a combination of funds would help achieve a stable risk-adjusted return. Not only this but there are other benefits too offered by Fund Of Funds (FOF).

A dedicated portfolio manager would be responsible for

- Building the original portfolio of mutual fund schemes across asset classes
- Constant tracking of market conditions
- Regularly monitor the performance
- Periodic rebalancing of the portfolio

In addition, there are no tax implications when the FOF portfolio is rebalanced as compared to an individual being subjected to short-term or long-term capital gains tax. Also, these are affordable and convenient from an investment amount and tracking point of view. Overall, it is a solution for portfolio diversification across asset classes.

Within the equity mix, it is important to understand the benefit of diversification such that there is a healthy mix. One of the options could be investing in a combination of large cap, flexi cap and balanced advantage fund.

A large cap fund would provide exposure to the frontline stocks, flexi cap fund would allow flexibility to the fund manager to spot opportunities and invest across stock categories based on market capitalisation while the balanced advantage fund would take care of the asset allocation between equity and debt. A combination of these funds would take care of various market cycles and volatile periods.

These three categories of mutual funds have the largest share within the Equity space. Hence, it is a testimony to their acceptance by most investors. Investing in these three categories also reduces the overall risk.

"Mutual Fund Sahi Hai, Par Ek Kaafi Nahin Hai"

A carefully chosen basket of mutual funds, helps to bring together a winning partnership that aims to balance risks and accelerate returns. This partnership helps perform in various market environments and helps create wealth in the long term.

Just as life sees ups and downs, so do the financial markets. In life, we depend on our many friendships to manage life's ups and downs. Similarly, shouldn't we have a portfolio of equity funds to manage the financial market's ups and downs?"