It's The Performance That Matters

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It is heartening to see how investors are making mutual funds an integral part of their investment plan. Obviously, the objective is to earn higher returns than traditional investment options and create wealth over time. One of the key aspects of achieving consistent investment success is to monitor the progress of the portfolio and ensure that it remains on track to achieve these objectives. Ironically, not many investors evaluate thee performance in the right way and often make hasty decisions based on their analysis. If you have been investing in mutual funds, you need to put performance in proper perspective.

This means you must understand what can be termed as good performance as well as the right way to evaluate the performance of a fund. Ideally, to analyse the performance, you should consider returns as well as the risk taken to achieve those returns. Besides, consistency in terms of performance as well as portfolio selection should also play an important part in this process. Simply put, while evaluating the performance of a fund, you must consider the risk-adjusted returns by considering both the returns generated and the level of risk taken.

Another important aspect is to consider long-term performance rather than short-term performance. It is important because the long-term performance track record moderates the effects which unusually good or bad short-term performance can have on a fund's track record. Besides, longer-term performance compensates for the effects of a fund manager's particular investment style. Also, evaluate performance as against the peer group. While measuring performance against the benchmark is important, comparison with the peer group provides the right measure of a fund's performance.

Discipline in the investment approach is an important factor as the pressure to perform can make a fund manager susceptible to having an urge to change tracks in terms of stock selection as well as investment strategy. Therefore, you must analyse the performance in a manner that helps you differentiate the investment skill of the fund manager from luck and get an indication of the likelihood of future success. Quite often, a negative return from a fund is equated with poor performance. In reality, even the best of fund managers are likely to give negative returns during the periods when the markets go down significantly.

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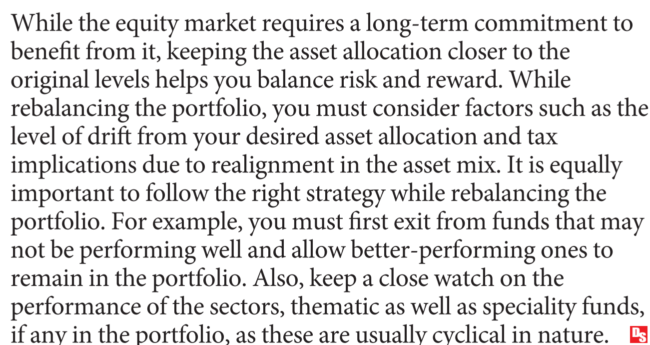
Besides, the time period considered also signifies the true level of performance. For example, short-term negative returns in line with the market from a fund that has been doing well over the longer term mean nothing and should be ignored. Investors often face the dilemma of whether to allow the portfolio to ride on or not, especially when the market is in a bull phase. In times like these, the key is to keep your focus on the original mix of equity and debt and be prepared to rebalance the portfolio, if required.



While the equity market requires a long-term commitment to benefit from it, keeping the asset allocation closer to the original levels helps you balance risk and reward. While rebalancing the portfolio, you must consider factors such as the level of drift from your desired asset allocation and tax implications due to realignment in the asset mix. It is equally important to follow the right strategy while rebalancing the portfolio. For example, you must first exit from funds that may not be performing well and allow better-performing ones to remain in the portfolio. Also, keep a close watch on the performance of the sectors, thematic as well as speciality funds, if any in the portfolio, as these are usually cyclical in nature.