The Right Approach To Investing

Hemant Rustagi
Chief Executive Officer, Wiseinvest Pvt Ltd.

Disciplined investing through SIP has emerged as an ideal strategy for millions of investors in our country. One of the major advantages of this strategy is that you invest at different levels of the stock market and hence benefit from averaging. In other words, it allows you to turn volatility – which is the most feared factor for investors – in the stock market to your advantage. Besides, if you stay committed to your time horizon, you also benefit from the true potential of equity as an asset class and the power of compounding.

However, if you are looking to benefit from this disciplined and potentially rewarding approach, you must follow the right investment process. A random approach can either expose you to unwarranted risks or disappoint you in terms of returns. Remember, you won't achieve your investment goals by investing a random amount that is either not enough to achieve your goals or exceeds your capacity to invest, thereby compelling you to interrupt your investment process.

Investing in too many funds, continuing with the same amount of investment despite the rise in your income over the years and not tracking the performance of funds thinking that over time all funds do very well are some of the other pitfalls that can impact the final result. Here's how you can figure out whether you are on the right track or not. First, how much are you investing and in which funds? Both these are important aspects to avoid any disappointment in the future.

To ensure that you are investing the right amount and in the right funds, you must begin by establishing goals to be achieved over the short-term, medium-term and long-term horizon, set a target and then work out an investment amount for each of the goals based on a realistic assumed rate of return. When you follow a similar approach for all your goals, it helps you ascertain asset allocation and how much you need to invest per month to achieve each one of them. It is possible that you may not have the required surplus to begin investing for all your goals.

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In that case, budgeting can help you identify areas where you can cut down spending as well as prioritise your goals. The key, however, is to begin investing and increase the investment amount later rather than delaying the investment process itself. Once the asset allocation is ascertained based on your time horizon, the next step should be the fund selection. For equity funds, you must begin with flexi-cap, large-cap and mid-cap and multi-cap funds. For hybrid funds, depending on your time horizon, you can choose a mix of equity savings, balanced advantage and aggressive hybrid funds.

For short-term goals, debt funds should be chosen by matching your time horizon with the maturity duration of your fund holdings. Secondly, how many funds are you investing in? It is quite common to see portfolios suffering from over-diversification. As a result, investors not only find it difficult to track performance but also compromise their returns. If you have too many funds in your portfolio, you must take steps to consolidate the portfolio. Remember, having too many similar funds in the portfolio doesn't help in any way.

You must weed out non-performing funds by measuring their performances through their benchmarks and the average return of the peer group. Thirdly, are you increasing the SIP amount over time? It is important to keep increasing the SIP amount as your income grows. That's because, despite careful planning, one can never be sure about how much money will be required for each of these goals at the end of your time horizon. You must also consider the fact that inflation is bound to eat into your income. In any case, having an additional amount in the future would provide you the flexibility to utilise it in a manner that you may like to for any of your needs.