Outlook MONEY

Don't make these

10

mistakes

when investing in

Mutual funds

An investor education initiative by Invesco Mutual Fund

Invesco Mutual Fund

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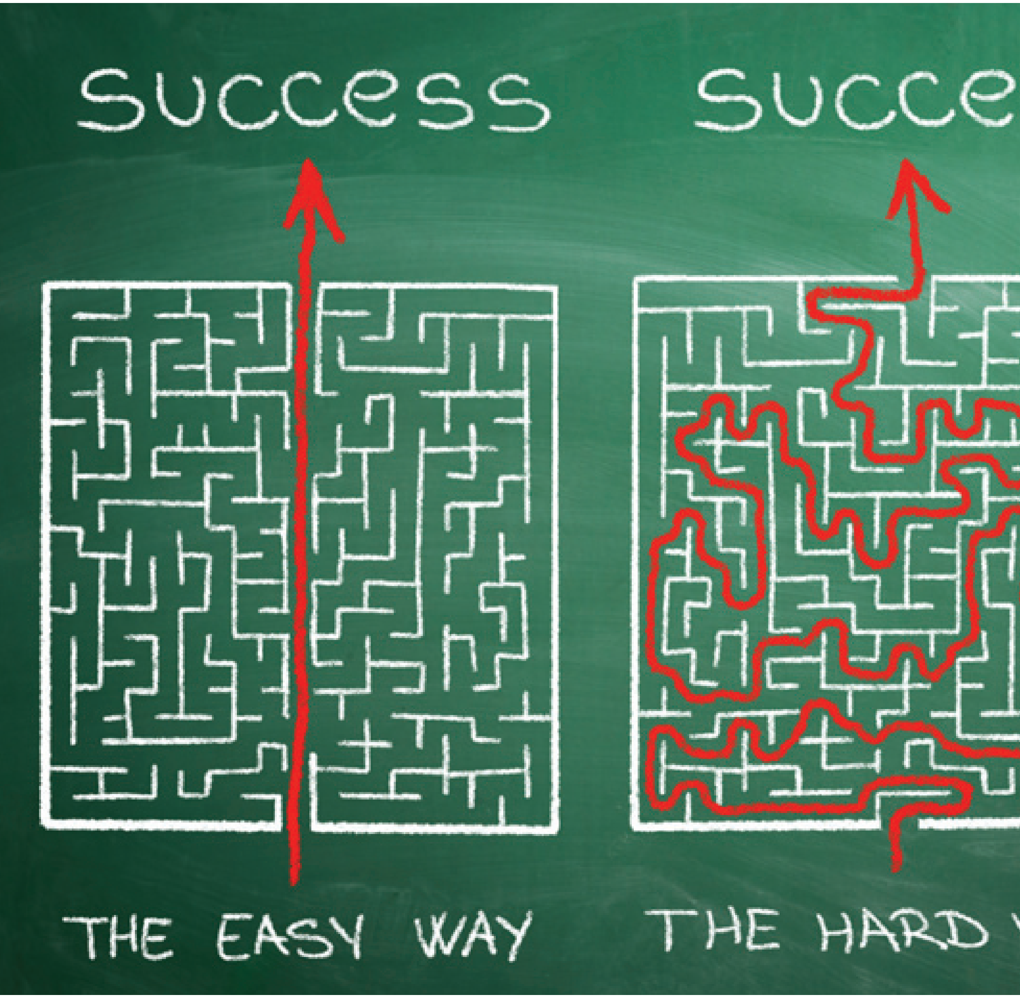
Avoiding investment mistakes



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Most investors are intelligent people; they indicate ample financial acumen when it comes to making a purchase or saving on one. Yet, when it comes to investing, they tend to act very differently—to the extent they tend to get it so wrong that their actions tend to not only erode wealth, they also infuse a sense of disbelief and mistrust with investing, leading to staying off from investing for indefinite periods.

Analysis of stock market movement and the time when investors enter these markets indicates that most investors enter markets when they go up, and with the first sign of a fall they make a hasty exit. Likewise, many a time investments are placed based on factors like year-end tax savings, a friendly tip, hot news, and so on. It can mean people are investing without considering the facts or why they are investing.

With so much at stake in investing, investors cannot afford to keep repeating actions that could have serious negative consequences for their financial goals. Yet the problem with many investors is that while they know that they have made investment mistakes, and vow not to repeat them, most people have only the vaguest sense of what those mistakes were, or, more importantly, why they made them. The way out to be successful with investing is by understanding what the mistakes are and when one tends to make them. In the following pages, we explore the ten common mistakes made by investors and how by avoiding them you can come out a winner.

1 Don't let your heart rule your head

If lately you have been tracking the stock market performance, you must be concerned and worried the way your investments are faring. The typical tendency among most investors is to exit the markets as they are unable to cope with the falling markets. Likewise, they start investing as soon as the markets start soaring. Both these approaches to investing are incorrect. The lesson is: do not get emotionally attached to investments.

The reality is we really don't know what tomorrow will bring. But one thing that one should firmly believe is that when investing in equities, one should do so for the long-term. Yes, stock markets are impacted by short-term disturbances, but in the long run, they are a winner. Although there could be changes in your life's circumstances and financial goals, market movements should not drive you to make drastic changes. By keeping your emotions in check, you will have a fair idea of how an investment will fare eventually. Remember to let go of your emotions when it comes to investing and not let your emotions influence your investing decisions.

Don't stop SIPs when markets fall

The convenience of investing in mutual funds is many times misused by way of stopping investments in them, especially the SIPs. The biggest advantage of investing through SIPs in mutual funds is that this technique allows you to control emotions when investing. Moreover, just the way we follow a cycle when it comes to earning by way of monthly income, SIPs allow you to follow an investment timeline with systematic and timely investments.

Moreover, when it comes to SIPs, market fall and rise evens out over time for you to average your cost of investments. So, when the markets fall, you buy more mutual fund units, and when they rise, you buy lesser units. In this manner, you average out the investing cost over time, without being impacted by market movements. Do not commit the mistake of stopping your SIPs; simply stay invested to reap the benefit of SIPs over time.

SIP Investment (₹)	NAV (₹)	Number of Units
6,000	15	400
6,000	20	300
6,000	11	545
6,000	10	600
6,000	30	200

This way, at the end of the five months, you have a total of 2,045 units, which means an average of little over 409 units each month

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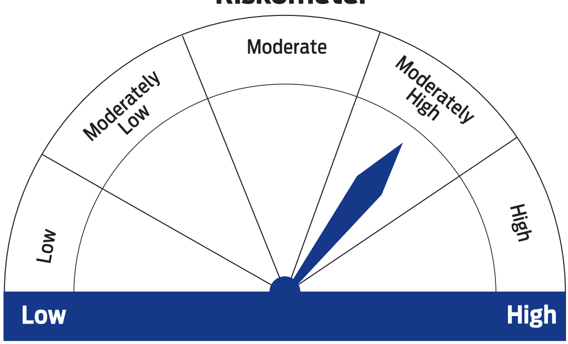
3 Don't undermine risk

Risk is an integral part of investments. Risk in regards of investments not only refers to the chance of losing one's capital, but also the probability of getting less than expected returns from an investment. When it comes to investments, risk has two connotations—the risk with the financial instruments and your own perception to risk. For instance, at a younger age, investors will be more risk-taking than when they get old.

The lesson for you is that when investing, risks are unavoidable. However, risk can be managed to suit your profile and investment objectives. One way to manage risk is to categorise investments into different baskets and choose an investment option appropriately. There are investment options like bank deposits that are low with risk, compared to, say, investing in a thematic fund that invests in a specific theme or sector.

One of the advantages of investing in mutual funds is that the risk inherent with every fund scheme is indicated with the Riskometer—from low to high, with three variants within.

Riskometer



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Don’t panic in times of corrections

It is the sentiments during the market corrections that separate smart investors from the average investor. The average investor starts selling shares during the market downturn thinking their money is lost forever, whereas smart investors know how to hold their investments in a volatile market and stay invested over a full market cycle.

Each investment comes with its share of risks and a suitable investment time frame for which the instrument is suited to invest in. As an investor you should understand that short-term market movement is meaningless. As long as your investment time frame remains the same and the instrument in which you are investing follows its mandate, you have little reason to worry.

The key point is to stay invested for the long term and diversification is what works over time. So, do not panic in times of market correction and swings—the mantra to be a successful investor is to stay invested through market cycles. The lesson that you need to follow is that it pays to spend time in the market than look at timing the market.

5 Don't hold too many investments

Diversification is often confusing and instead of spreading investments across asset classes, many investors tend to diversify in numbers. What they effectively land up doing is to invest in many fund schemes where a few would do the trick.

Instead of investing in 15 fund schemes, follow the asset allocation that works for you. This way, investing in even one fund scheme will be sufficient. It has been well documented that asset allocation is primarily responsible for portfolio performance than even stock or fund selection. It is for this reason that asset allocation is the key to portfolio returns and hence is of paramount importance.

The other problem with holding too many fund schemes is that they are not easy to track and review. Further, the collective impact of their performance also gets difficult to assess. It is best to first stick with asset allocation and once it is done, it is best to invest money in a few schemes which follow the asset allocation than add up investments for the sake of it.

Don't time the market

6

When it comes to investing, the old adage, "buy low and sell high", is sometimes over-analysed and chased. However, to chase the day when the markets are low to invest and exit on the day they are on top, is a statistical exercise possible in hindsight. We've all heard the expression "hindsight is 20/20"; the phrase holds true in many cases, and investing, especially market timing, is no exception.

One thing that even Warren Buffett doesn't do is to try to time the stock market, although he does have a very strong view on the price levels appropriate to individual shares. In reality, it is impossible to time the market all the time. Nobody has been successful and consistent over stock market cycles. It is for the very same reason, more money has been lost by people while timing the market. Instead investors should invest regularly through mutual fund SIPs so as to average their investment cost over time.

7 Don't adopt trading strategies

As a mutual fund investor, one should not apply 'buy on dips' theory blindly and adopt trading strategies. For example, if a fund is purchased through a lump sum, then a fall in the market may provide an opportunity to average. That said, it is prudent to have patience and follow a disciplined investment approach besides keeping a long-term broad picture in mind and not to panic in times of corrections. Also, market corrections also lead the fund managers to pick quality stocks.

Remember, when you invest in mutual funds, the actual investing is best left to the fund manager, who manages a big investment portfolio, which is regularly monitored and reviewed. While past performance can surely help you pick a fund, such fund's returns are only indicative of how they have fared over time and should not be taken as guarantee. So there is no need to pick and dump funds at random, as doing so may prove expensive given the tax implications when approaching investments like trading.

Don’t invest without evaluation

Do not be drawn to every new fund scheme which is on offer at ₹10 per unit. When it comes to investing in mutual funds, there is a lot to choose from and the best way to address this is by exploring the available options and zeroing down on a fund scheme with a track record and history.

Select a fund that clearly states its investment objectives. Apart from past performance, know the scheme’s investment philosophy and how effectively the fund scheme sticks to its stated objective. Dig a bit deeper and check the antecedents of the fund manager, the fund house and how the scheme has fared relative to its peers.

Other than returns, see how much assets the fund scheme manages and for how long a fund scheme is being managed by the fund manager. Check for the fund’s performance relative to its benchmark during both market lows and highs. This way you will get a better picture of how the fund does during different market cycles.

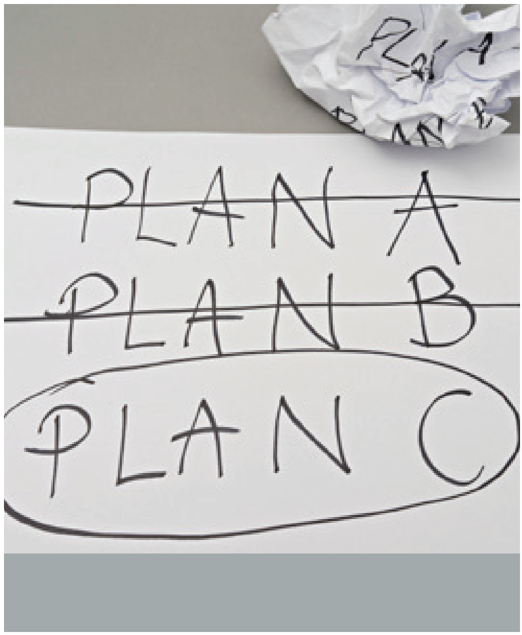
9 Don't procrastinate– invest now

There is an old saying "Procrastination is the thief of time". And when it comes to investing, for most investors, getting started is the hardest part. But when you do get started, investing is not anymore a burden. That said, investors shouldn't wait for too long because implementing investments should begin immediately. If you don't start investing immediately, you are going to miss all the opportunities that different financial assets provide. Also, by investing late, one misses the power of compounding on their investments.

One of the best ways to invest is through SIP. Investing in SIP can help you attain your financial goals by taking advantage of rupee cost averaging, and growing your investments with compounded benefits. One of the major advantages of investing though SIPs is that it helps in disciplining an investor, along with inculcating a habit of "forced savings." One of the most important concepts in finance is that money has a "time value". That is to say that money in hand today is worth more than money that is expected to be received in future. The thumb rule is to invest regularly and keep reinvesting the returns. With the power of compounding, one can have astounding returns in the long run. With simple interest, one can earn interest only on the principal whereas with compounding, one can earn interest on the principal and additionally on the interest.

Don't stick to under-performers

Investing in funds is not a one-time exercise of choosing a fund scheme to invest in. To be on top of your finances, you should regularly monitor the performance of the schemes you invest in. For instance, it is one thing for a fund to underperform briefly when the markets fall, it is another if it continues to fare poorly compared to the benchmark as well as its peers.



Don't be dictated by emotions to stay invested in a fund even when it starts to underperform. Evaluate the performance of the fund scheme you invest in at least once a year. This way, you will have the discipline to track its performance and evaluate how it has fared. Such a review gives you the option to consider staying invested in the fund scheme or to exit it owing to lack of performance.

If you are unable to ascertain the performance of fund scheme to decide staying invested in it or exiting it, take the help of your advisor to know what you should do next—stay invested or exit.

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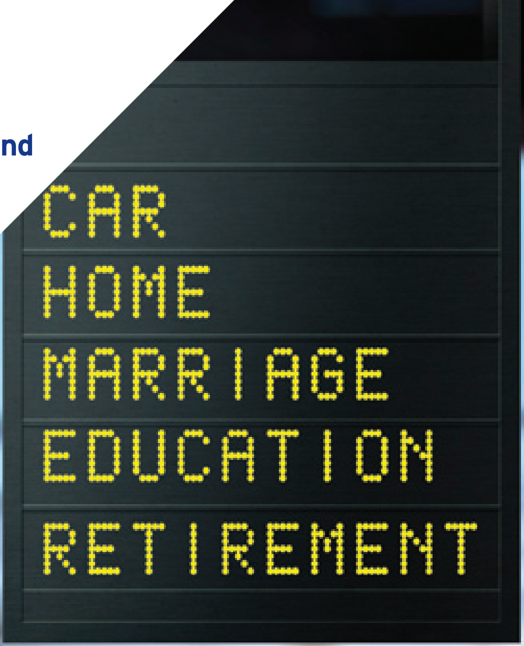

Take the SIP route to your financial destination.

The journey of a thousand miles begins with a single step, or in the case of a financial goal – with a SIP. A SIP will take you to your financial destination one step at a time. It is easy on the wallet as you don't have to commit a lumpsum at one go, inculcates discipline and helps ride market volatility. Start a SIP with mutual funds today and take the smarter route to achieving your goals.

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Mutual Fund investments are subject to market risks, read all scheme related documents carefully.