

All about Mutual Fund Investing

Here are some basic facts that you need to know before you invest in a mutual fund

Mutual Funds are increasingly being touted as the retail investors' investment vehicle. But the key challenge is to choose the right fund. But it's simple. It only requires a bit of discipline and little time - hardly a cost for a secure financial future. Following are some rules to help invest better and attain your financial goals.

Know Yourself: The first step towards achieving your goals is that you must know yourself. Try to get an idea of how much risk you can handle. Do a tolerance test for yourself. If your Rs 10,000 investment turning into Rs 6,000 upsets you--even though it could subsequently bounce back--an aggressive equity fund is not for you.

Reality Check: What are your goals? If you need to turn Rs 10,000 into Rs 50,000 in two years, a medium term bond fund may not be the right answer. Work on setting realistic expectations for both your goals and your funds.

Know What You Are Buying: Once you discovered yourself, spend some time for a close understanding of the funds. The stated objective of a fund as given in a prospectus is often incomplete and does not reveal much. Based on the readily available portfolio and fund manager's commentary, you can broadly understand the style and strategy followed by a fund. This will help you meaningfully diversify your portfolio. This will also help you assess potential risks. In general, large-cap value funds are less risky than small-cap growth funds.

Examine Sector Weightings: You must know that funds with large stakes in just one or two sectors will likely be more volatile than the more evenly diversified funds. Looking at a fund's sectoral history will help you gain a good perspective. Does the manager move in and out of sectors frequently and dramatically? If so, the fund might get hurt, if the manager is ever caught on the wrong foot.

Check Out the Fund's Concentration: A portfolio with just 20 or 30 stocks or one that puts most of its assets in just a few stocks will likely be more volatile than a fund that's spread among hundreds of stocks. But there could be rewards of concentration. A concentrated portfolio will

also get more bang for its buck if its stocks work out. You may want to add a concentrated fund, one that owns fewer stocks or puts most of its assets in the top 10 or 20 stocks, to your portfolio.

But largely, your core funds should probably be well diversified and more predictable. Though a small allocation to a sector-oriented fund, a more-flexible fund, or a more-concentrated fund could boost your returns.

Assess Performance Appropriately: Past performance is no indicator of future results. Investors should commit this statutory quote from mutual fund prospectus, advertisements and any other literature to memory. It should be recalled more readily than your bank account number. It should be repeated anytime you consider sending money to any fund with a 100 per cent three-month gain.

Why? Chances are that a few months of boom will be followed by bust, as it has happened in 2000. All the ICE concentrated funds, which were topping the charts fell flat on their face. There was just no escape when their NAVs started declining like nine pins. What should an investor do? Do not concentrate your mutual fund portfolio or invest in a concentrated fund. And, above all, don't focus on short-term returns. When choosing a fund, look for above-average performance, quarter after quarter, year after year.

Know Your Portfolio: Look for areas that are over-represented and for those that are lacking. For example, will your portfolio be overly concentrated in the large-cap equities or too much in highly rewarding but wildly volatile infotech stocks? Will you be missing investments in small-cap stocks?

Be A Disciplined Investor: After you've chosen some funds, stick with them.