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Advisers call out investors' biggest mistakes: survey

Here are six errors financial advisers flagged as the more common ones. Read to know which ones you fell for and which you cleared

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We all make mistakes, especially when it comes to managing our money. Take mutual fund investments. From buying them by the dozen to buying none at all, even if we need them—a cursory glance at an average investor's portfolios would reveal many such holes. So, we asked some of the country's leading financial advisers about the major shortcomings they see in fresh clients' mutual fund portfolios. Here are their stories.

No asset allocation

Thirteen of the 18 advisers we surveyed say this is a common problem. Many times, investors buy funds based on past returns only. "This results in multiple funds of the same type to be in a portfolio. For example, investors buy multiple mid- and small-cap funds when they are doing well, or multiple government securities funds when interest rates are falling," says Vishal Dhawan, founder and chief executive officer of Mumbai-based Plan Ahead Wealth Advisors.

Ashish Chadha, a Gurugram-based mutual fund adviser, says: "When markets are booming, don't chase the best-performing funds—you will get into serious trouble. This advice is falling on deaf ears right now, though." Chadha says that a return of 300 to 400 basis points above the risk-free rate (typically 7%) is all that you will get over a 15-year period. One basis point is one-hundredth of a percentage point.

Mutual funds by the dozen

As a result of making investing without any asset allocation in mind and chasing past performance, investors get saddled with too many funds, said all 18 of the 18 respondents. "When customers walk in with portfolios that are full of 'flavour of the month' funds, they are either consumers of advertising frenzy or have previously worked with a trigger-happy distributor," says Shyam Sunder, managing director, PeakAlpha Investment Services Pvt. Ltd.

Suresh Sadagopan, founder, Ladder7 Financial Advisories, says that many investors often have too many small systematic investment plans (SIPs). "People tend to diversify too much in a lot of funds in the notion that if they cast their net very wide, there is diversification."

Holding too many schemes has another dangerous fallout, says Mumbai-based Vinod Jain, principal adviser, Jain Investment Planner Pvt. Ltd. "Many don't have a complete list of the investments that they have made till date and their latest updates." Getting their existing portfolios in order could be very time consuming, he says.

Trying to time the market

Upon asking their first-time clients why they invested in so many mutual funds, Eight of our respondents found that the investors had tried to time the markets. "Mutual funds are traded like equity under the assumption that if they regularly book profits, it reduces their risk," says Poornima Katpadi, founder and investment specialist at Simplesolution4u, a Mangalore-based distributor. Valmiki Khatri, partner, Krushna Finserve LLP, says that some investors have "very low risk appetite but want the highest returns."

The key is to control emotions. "Volatility in markets often leads to uncalled redemptions and SIP stoppages. Investors come up with various other reasons like lack of funds, loss of job, loan instalments' pressure, but the main reason is they cannot handle volatility," says Khatri. Maher Dhamodiwala, a Mumbai-based mutual fund adviser says that investors are reluctant to invest when markets are down and valuations are cheap. But he adds, "When we help them understand that their present decision impacts their financial goals, that their present run rate is not enough to win their match (life goals), many are willing to change."

Driven by dividends

Another peculiar problem is the obsession with dividends, said eight advisers. Investors tend to choose the dividend option even when they don't need regular income. Some years ago, Gajendra Kothari, managing director and chief executive officer, Ética Wealth Management Pvt. Ltd got a new family as a client. The five-member family had 150 folios between them. Apart from repetitive schemes for each member, all investments were in dividend options. "There is a limited understanding of the fact that dividends are not guaranteed and the true reflection of a mutual fund's performance is a combination of capital appreciation, or depreciation, and the dividend paid," says Dhawan. Deepak Chhabria, chief executive officer and director, Axiom Financial Services Ltd, a Bengaluru-based distributor of financial products, too says that many young investors want to get dividends in their hands. Experts suggest a two-pronged strategy to choosing the right plan. One, know that "the dividend pay-out option is not required if you are in the wealth-creation stage," says Katpadi. Two: dividends get distributed out of your profits and the net asset values come down after they are paid. Read more on that here: bit.ly/2prO7bo.

Not reviewing the portfolio

We don't recommend frequent churning. If you invest for the long run, it pays to give your funds time to perform. However, that doesn't mean you should not monitor. Five of our respondents say that investors hold on to dud performers for years and don't do anything about it. Amol Joshi, founder, PlanRupee Investment Services, says investors hold on to losers "because they had chased a hot theme, maybe sector funds, at the top of a (market) cycle." As a result, Joshi adds, investors typically wait for their schemes' net asset values to rise above the level at which they had bought. Anup Bansal, co-founder and managing director, Mitraz Financial Services says that such mistakes are often avoided if investors engage with registered investment advisers. "Often people don't have enough bandwidth from professional and personal life to take timely actions." Joshi's advice is: "When you realise a mistake, accept it, book your loss and reinvest keeping your asset allocation and risk profile in mind."

Bequeathing worries

Financial advisers always suggest joint holdings through the "anyone or survivor" mode. This way, if the first investor were to pass away, the holdings can be easily transferred to the joint holder. The absence of a joint investor can create trouble for inheritors as the transmission process in such cases usually demands a lot of paperwork and time. Three of our respondents said that investors don't pay much attention to having a second account holder. Chhabria of Axiom Financial Services recollects that an elderly unmarried lady client had, in one of her investments, "an unfamiliar nominee name." On probing he found that the name was of an ex-employee of the lady; a caretaker who was once her confidante but not anymore. Chhabria sensitised—and helped—the lady to get the nominee changed and formed a trust instead.