Five steps for NRIs to reap investment benefits

The best investment that you can make at this point is to stay the course and protect your portfolio from yourself

Indian financial markets look like a very different place in the last few weeks. The euphoria of an election outcome that was perceived as very positive for India, due to its large mandate to the incumbent government, has given way to questions about growth and consumption slowdown, lack of reforms and tax terrorism, amongst other negative factors. These have also been accompanied by Indian equity markets underperforming most global indices, adding to the concern that India is not a great place to invest in.

Whilst it is not surprising to see this pessimism, considering that financial markets are prone to bouts of significant volatility, a large number of investors are used to seeing much lower levels of volatility, especially in developed markets. Thus it can be rather discomforting to see portfolios losing significant value in a short period for them. Coupled with the fear of losing gains on the portfolio or even portions of the capital, is the belief that this opportunity can be used to sell now, and then buy cheaper later.

The two biggest enemies of investors are greed and fear, and periods like we have gone through in the last couple of years are a litmus test. From a point a couple years ago, when Indian equity markets could do nothing wrong, we can’t seem to do anything right now. The truth lies somewhere in between, and thus the need to control our emotions is going to be the single biggest determinant of our portfolio outcome when we look back at it after a few years.

So how does one really control oneself?

Remember the “why” of your investment strategy

For many investors, the India portfolio is a part of their retirement portfolio. And, retirement could be more than a decade or two away. Even if your retirement or financial goal(s) against which the India portfolio is earmarked is closer than that, it is not likely that you will end up using your entire India portfolio in the first few years of your retirement. It may therefore be prudent to avoid taking any short-term decisions on the portfolio driven by market volatility.

Focus on the “numbers” behind the portfolio

Ultimately, equities are slaves to corporate earnings over the long term. Rather than brooding over the past portfolio performance, evaluate the underlying earnings growth of the portfolio. If earnings continue to be growing for the underlying businesses, it is very likely that as markets become more rational, the portfolio will bounce back.

Don’t forget the “when” of your portfolio

Most of us like to see our wealth increase in a linear fashion, just as a bank deposit does. Unfortunately, equity markets are rather non-linear in their behavior, and have always tended to behave this way, with periods of significant returns being followed by periods of no/low/negative returns. However, it is close to impossible to figure out when this returns button will go off or come on. The key is to be clear on when the monies from the portfolio are required so that the exit from the portfolio can be planned based on that, rather than on current returns from the portfolio.

Practice "asset allocation"

Many investors mistakenly implement asset-allocation in a reverse manner, where allocation to assets that give the highest returns tend to be the most at all times, and monies constantly move from the lower returning asset class to the higher returning asset class. The principle of asset allocation and rebalancing works in exactly the opposite manner, that is, sell the asset that has given the highest return and therefore rebalance the portfolio by purchasing the asset with the lower return, so that the mix remains constant. This principle of asset allocation serves investors well, though it is difficult to implement due to the greed and fear cycle that investors are exposed to.

Don't stop mid-way

As portfolio returns start to reduce or even turn negative, it is very common to see investors stop their regular investment strategy through systematic investment plans (SIPs) or systematic transfer plans (STPs) to wait for things to stabilize before adding more. This could create significant damage to investor portfolios in the long term, as the regular investing strategy is built to take advantage of falling financial markets, and a shift in that strategy could mean that you look back at it with regret a few years later.

The best investment that you can make at this point is to stay the course and protect your portfolio from yourself.

-Vishal Dhawan