

Business Standard

Fix the holes in your investments and insurance plans ahead of the new year

Make changes where required so that your investment and insurance portfolio are equipped to meet the rigours that 2020 may have to offer

Sanjay Kumar Singh | New Delhi December 20, 2019 Last Updated at 15:39 IST



With the year drawing to a close, your thoughts may have turned to taking a holiday and visiting a new

destination. Or you may want to just curl up in a blanket and laze around by a bonfire. While you do deserve some rest after toiling for the entire year, one essential task you must not overlook is to check your financial portfolio and ensure it is in good shape.

Rebalance portfolio: Investors who have a structured investment portfolio would be adhering to a certain asset allocation that corresponds to their risk profile. They would have an allocation to equities, fixed-income, gold, and such like. Usually, due to the outperformance of a particular asset class and the underperformance of others over the past year, the investor's asset allocation becomes skewed. Hence, it becomes important to bring it back in line with the pre-decided asset allocation by booking profits in the outperforming asset class and shifting money to underperforming asset classes.

Investors also need to check whether their allocation to sub-asset classes is in order. This year, for instance, large-cap funds have outperformed mid- and small-cap funds. It is possible that an investor's portfolio may have become overweight on large caps, making rebalancing necessary.

Emphasising the importance of rebalancing as a risk mitigation tool, Mahesh Patil, co-chief investment officer, Aditya Birla Sun Life Mutual Fund says: "Asset classes tend to behave in a cyclical manner. They also witness mean reversion to long-term returns. A particular asset class may do very well for a certain period of time. As a result, the investor's portfolio would become overweight on it. Booking profits and bringing the allocation back to the pre-decided level is important. Otherwise, whenever that asset class witnesses a downturn, the portfolio of an investor who has not rebalanced will take a bigger hit compared to the portfolio of one who has been rebalancing regularly." Patil cites the following example. Between 2013 and end of 2017, the mid- and the small-cap categories had outperformed massively before beginning to correct from the start of 2018. An investor who had not rebalanced the mid- and small-cap allocation during the long rally would have lost much more from 2018 onwards than someone who did so.

Nowadays, long-term capital gains tax at the rate of 10 per cent is applicable if the gains from equities exceed Rs 1 lakh in a financial year. Investors can do a few things to minimise the tax outgo from rebalancing. One, if the deviation from the pre-decided level is not very high, and the investor has surplus money, she can rebalance by investing more in an underperforming asset class (instead of selling the outperforming asset class). Two, the Rs 1 lakh limit applies at the individual level. Therefore, both the spouses can sell partly from their portfolios to take advantage of this limit and stay balanced at the family (if not individual) level. Financial planners warn that investors should not fall so much in love with an outperforming asset that they become reluctant to sell it.

Exit equities if the goal is near: Asset allocation may also have to change because the investor may have reached a certain age, say, 55, and may want to shift to a more conservative portfolio by the time of retirement. Such an investor should begin to sell equities and move more money into debt. Asset allocation may also have to change because the investor is nearing a goal, say, his child will begin college in three years. Again, the shift from equities to debt should begin about three years in advance so that a downturn in the equity markets does not jeopardise the goal.

Spreading out your exit over time is important. "Just as investors should use the systematic investment plan (SIP) route when entering a fund, they should use the systematic withdrawal plan (SWP) or systematic transfer plan (STP) route while exiting an equity fund," says Vishal Dhawan, chief financial planner, Plan Ahead Wealth Advisers. He adds that investors should not pull out money at one go and then regret the fact that the market went up over the ensuing six months. Just as they need to average out at the time of entry, they need to do the same at the time of withdrawal. The money withdrawn may be parked in an ultra short-term fund (or a low duration fund, if the investor has a slightly higher risk appetite).

Cull underperformers: The annual portfolio review is also the time when investors should remove underperformers from their portfolios. "Compare a fund's return against its benchmark and the category average. Since equities are a long-term asset class, see how the fund has performed over the three-year and five-year timeframes before taking a decision," says Patil.

Since even the best of funds tend to underperform, investors should put a fund under watch for six months to two years before deciding to exit. If the underperformance is due to a high expense ratio, the investor should pull out faster. On the other hand, he should give more time to a fund manager who has a stellar track record.

With active fund managers facing greater difficulty in outperforming, investors should scrutinise the expense ratios of their funds closely.

Avoid duration and credit risk: The Reserve Bank of India (RBI) chose to pause in the latest monetary policy review in December after a series of rate cuts in 2019 due to consumer price index-based inflation printing on the higher side. Retail investors should keep the bulk of their fixed-income portfolio in shorter-term debt funds that carry minimal duration risk. "Investors should also check, or have an expert check, the credit quality of their debt fund portfolios," says Dhawan. Investors may take limited exposure to dynamic bond funds.

Go for international diversification: Investors who have adequate exposure to the domestic equity markets should think of diversifying internationally. "Global diversification is becoming increasingly important for seasoned investors to counter the impact of single-market exposure. Diversifying internationally can also help the investor deal with the risk of currency depreciation," says Patil.

The Indian currency has a tendency to depreciate against hard currencies like the US dollar. With many families now having financial goals (like child's education in a foreign university, foreign travel, etc) that involve spending in hard currencies, taking exposure to international funds has become important. US-focused funds should be the first category Indian investors should opt for when going global.

Check your health insurance portfolio: The key point to check here is whether you have adequate health insurance, given the fact that health care costs are already so large and rising rapidly. “Ensure that you are adequately insured so that you don't fall into a funding trap in case a family member falls ill,” says Mayank Bathwal, chief executive officer, Aditya Birla Health Insurance. He suggests having both a basic indemnity cover (the normal health insurance policy that reimburses hospitalisation costs) and a critical illness benefit cover also to ensure that serious ailments are taken care of without the family falling into financial distress. For a family of four, the sum insured in a floater cover should be at least Rs 10-15 lakh. It could go up to Rs 20-25 lakh if parents are also included in the same policy.

Make sure that your health insurance policy has the minimal number of exclusions.

Nowadays, many products have begun to offer OPD (outpatient department) and wellness benefits (the latter refers to products that reward the customer with a discount on the premium for staying healthy). Many insurers also provide a health coach, who helps customers manage conditions like diabetes, asthma, cholesterol, etc. If your current health cover does not provide these benefits, try to port to one that does.

Evaluate your life insurance holdings: Your need for life insurance may have grown or come down over the past year. The need for life insurance grows when a person takes a new loan, or develops a more burdensome goal (like foreign education for his child instead of domestic education). The need comes down if, say, a person pays off a loan or receives wealth via inheritance.

If your need has grown, you may have to add a policy, while if it has reduced you may have to give up one. Moreover, costs have been coming down for term insurance, so make sure you are paying a competitive rate.

Large-cap funds are this year's outperformers			
	Category average returns (%)		
Category	YTD	3-year	5-year
Large-cap funds	12.02	12.92	8.83
Multi-cap funds	8.99	11.64	8.72
Mid-cap funds	1.6	8.25	8.16
Small-cap funds	-3.46	5.25	7.28

Source: mutualfundindia.com