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Equity balanced funds remain attractive

Despite the recent outflows and anaemic returns, the category makes sense due to its fine long-term track record

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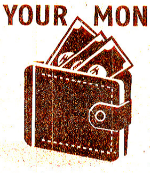
Balanced funds, or aggressive-hybrid funds, which maintain an allocation of 65-80 per cent to equities, have seen considerable outflows in the recent past. Assets under management (AUM) shrunk from ₹1,83,220.08 crore in August 2018 to ₹1,66,874.08 crore, a fall of 20.38 per cent. But the category still makes sense for most investors.

With the markets have not done too well over the past year and breadth of performance completely missing, the performance of these funds have taken a beating in the recent past. "If you look at the Nifty's performance, it was driven by a narrow band of about 10 stocks," says Sanjay Parekh, senior fund manager, Reliance Mutual Fund. Fund managers, who typically hold a broader portfolio of stocks, found it difficult to do well in such a market. The problems in the debt market over the past year also affected some funds. And investors who came in during the latter part of 2017 witnessed poor performance, and consequently, exited.

YOUR MONEY



Many investors were mis-sold balanced funds with the promise of regular, tax-free returns. "These funds can only distribute dividend out of the surpluses they generate. When the markets stopped doing well, dividends stopped, leaving this class of investors disillusioned. The imposition of a 10 per cent tax on dividend also took away the promise of tax-free income," says Deepesh Raghaw, founder, PersonalFinancePlan.in, a Sebi-registered investment advisor.

If you overlook the one-year returns of the category, its long-term track record is attractive (see table). Hence, according to experts, this is a category that remains worth investing in. It offers several advantages, the foremost being that of allocation to both equities and debts. "The equity portion offers growth while the debt portion offers stability," says Parekh. Investors thus have a less volatile experience. These funds also maintain their equity-debt allocation within a certain range. The equity exposure, for instance, does not usually rise beyond 80 per cent or go below 65 per cent. Hence, investors get the benefit of rebalancing. The debt allocation also leads to better downside protection in falling markets than in a pure equity fund.

As for the risks, since they are predominantly equity-oriented, investors should be prepared for a certain level of volatility in these funds. Some of the risks in these funds also arise due to the fund manager's behaviour. "Some balanced funds take a high level of exposure to mid- and small-cap stocks. On the debt side, sometimes fund managers take a higher level of duration or credit risk than is warranted," says Raghaw.

Balanced funds are especially well suited for investors entering the equity markets for the first time. They are also well-suited for slightly conservative investors. Those saving for retirement may also use them. In fact, say experts, most categories of investors can use them. The only thing you should avoid investing in them for is regular dividends. Since returns from equity-oriented funds tend to be volatile, this is not possible. The imposition of dividend distribution tax has made investing in the dividend plans of these funds an even worse idea. Finally, do not invest in balanced funds with a horizon of less than five years.

Select a fund that has a sound long-term track record. Choose on the basis of rolling returns if possible. On the equity side, the exposure to mid- and small-cap stocks should not exceed 25 per cent.

ATTRACTIVE LONG-TERM TRACK RECORD

Balanced fund category returns (%)

	1 year	3 years	5 years	10 years
Max	10.22	17.34	16.36	20.18
Average	3.40	12.25	13.49	15.92
Min	-10.37	8.71	8.62	10.20

Source: Ace Mutual Fund