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SIPs: The best bet for creating wealth

ONE of the best ways to build wealth over time is to invest in equity mutual fund schemes through the systematic investment plan (SIP) route. The SIP is a plan where investors make regular and equal payments into a mutual fund, trading account or retirement account, and benefit from the long-term advantages of rupee-cost averaging (RCA).

This is one of the most convenient ways to save regularly without taking any action except the initial set up of the SIP. If you are familiar with the concept of recurring deposits in banks, then SIPs are similar to that, except that the investments are made through financial assets such as equity, debt, gold etc.

Under the RCA method, an investor would buy more units when the prices are low and less when prices are high. So, eventually the high and low prices average out over the long run. In this process, one can go for the "buy low, sell high" strategy as some investors like to speculate on the right moment to invest. But predicting a market's short-term direction is difficult even for the best of professionals.

Historically, equity has the potential to give returns that are higher than the inflation rate in the long run (more than 5 years). It means if the average rate of inflation is 6 per cent per annum, over the long run, equities can give more than 6 per cent return, thus giving real return.

The effect of compounding is another advantage that investors realise when they invest through SIPs. The power of compounding can, over time, grow a small amount of money into a substantial sum.

Long-term perspective pays

Stop worrying about the markets. Instead develop a long-term perspective towards investing. The thumb rule is the longer you stay invested, the higher is your returns. The earlier you start investing, bigger would be the corpus that you accumulate. It's not timing the market, but the time in the market that can make money for you.

When you start investing, you have one or more financial goals, along with a defined investment horizon. Also markets go through business cycles on a regular basis. The SIP mode of investment can help you contain volatility on your portfolio. So, entrust your money with one or more good fund managers, who could grow your money over the long run.

Equities vs parking your money

The decision to invest in equities (or mutual funds) versus parking your money in safer instruments should come down to your investment horizon. Historical data shows that the longer the timeframe, the higher the probability that you gain with equities. Indian equity market returns, like most other markets, have been volatile, with large swings on a regular basis. There have been "more up years than down". Six of the past 20 years provided returns in the vicinity of +40 per cent while only 2008 shows a negative return of more than 40 per cent.

If one had invested Rs 10,000 in S&P BSE Sensex on December 31, 1993, after 20 years, it would be worth Rs 61,100, translating to compound annual return of 9.5 per cent. Besides, the dividend yield of between 1 and 2 per cent per year.

Compare that to Rs 10,000 put into a one-year Fixed Deposits (FD) and renewed at the prevailing rates each year. Unadjusted, the initial investment would be Rs 47,100 but after tax, the value will drop to Rs 37,700, considering the average marginal tax return of 20 per cent. However, in your equity investments, you don't pay any tax if you stay invested for more than a year.

Picking the right fund

There are hundreds of equity mutual funds in the market, but an investor should choose funds according to his risk profile. Generally, the mutual funds with higher asset under management (AUM) have low expense ratio. Diversified equity mutual funds, which have AUM lower than Rs 1,000 crore, have higher expense ratio than those which have AUM higher than ₹1,000 crore.

Like most investors, you too seem concerned about your returns. First, you need to understand that a scheme can be analysed for various aspects using particular type of return. For looking at the year-on-year performance, CAGR may be a suitable parameter.

Apart from the analytics part, you need to work on your emotional facet. Investing is all about employing your surpluses in favourable avenues and watching your wealth blossom over time.

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HOME LOAN FLOATING INTEREST RATES FOR LOAN AMOUNT ₹30 LAKH AS ON FEBRUARY 23, 2017

Lender's	5 years		10 years		15 years		20 years	
Name	Interest%	EMI/lakh	Interest%	EMI/lakh	Interest%	EMI/lakh	Interest%	EMI/lakh
Axis Bank	8.65	2059	8.65	1248	8.65	994	8.65	877
Corporation Bank	8.85	2069	8.85	1259	8.85	1005	8.85	890
HDFC Ltd	8.70	2061	8.70	1251	8.70	996	8.70	881
ICICI Bank	8.70	2061	8.70	1251	8.70	996	8.70	881
IDBI Bank	8.80	2066	8.80	1256	8.80	1002	8.80	887
Jammu & Kashmir Bank	8.70	2061	8.70	1251	8.70	996	8.70	881
Punjab National Bank	8.45	2049	8.45	1237	8.45	982	8.45	865
SBI	8.65	2059	8.65	1248	8.65	994	8.65	877
Union Bank of India	8.60	2056	8.60	1245	8.60	991	8.60	874
Central Bank of India	8.50	2052	8.50	1240	8.50	985	8.50	868

PN: The rates given above are for initial period only, thereafter the interest rates vary from bank to bank. The home loan rates are indicative rates, which may change according to the credit profile of the customer. Source: ApnaPaisa Research Bureau www.apnapaisa.com