The LightHouse

AN ESSENTIAL LONG TERM GUIDE TO BUILD WEALTH WITH MUTUAL FUNDS & ASSET ALLOCATION

| July 2022 Edition |

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DISCLAIMER

All information in this newsletter is for information and education purposes. This is not investment advice.

STATE OF THE MARKETS

As of June 30, 2022, Nifty 50 benchmark at 15,780 is down 11.5% from Jan 1, 2022, when it was at 17,825. In the larger scheme of things, that looks nothing out of the normal. Declines of 10% or more are fairly common.

The year so far has been marked by several negative events. Rising Inflation, Russia-Ukraine War, damaged supply chains, Crypto burnout, rising interest rates, etc. In short, massive uncertainty resulting in high volatility.

Central Govts have stopped printing money (for now). The US is facing a recession. Prices of necessities are shooting through the roof.

All this has resulted in change too. There is something going on at a fundamental level that will change how the world works today. By when and how much, is a matter of speculation.

As investors, we have no choice but to take such uncertainty and volatility in our stride and determine a course of action that reduces our downside and increases our upside. At least, that is what we strive to do.

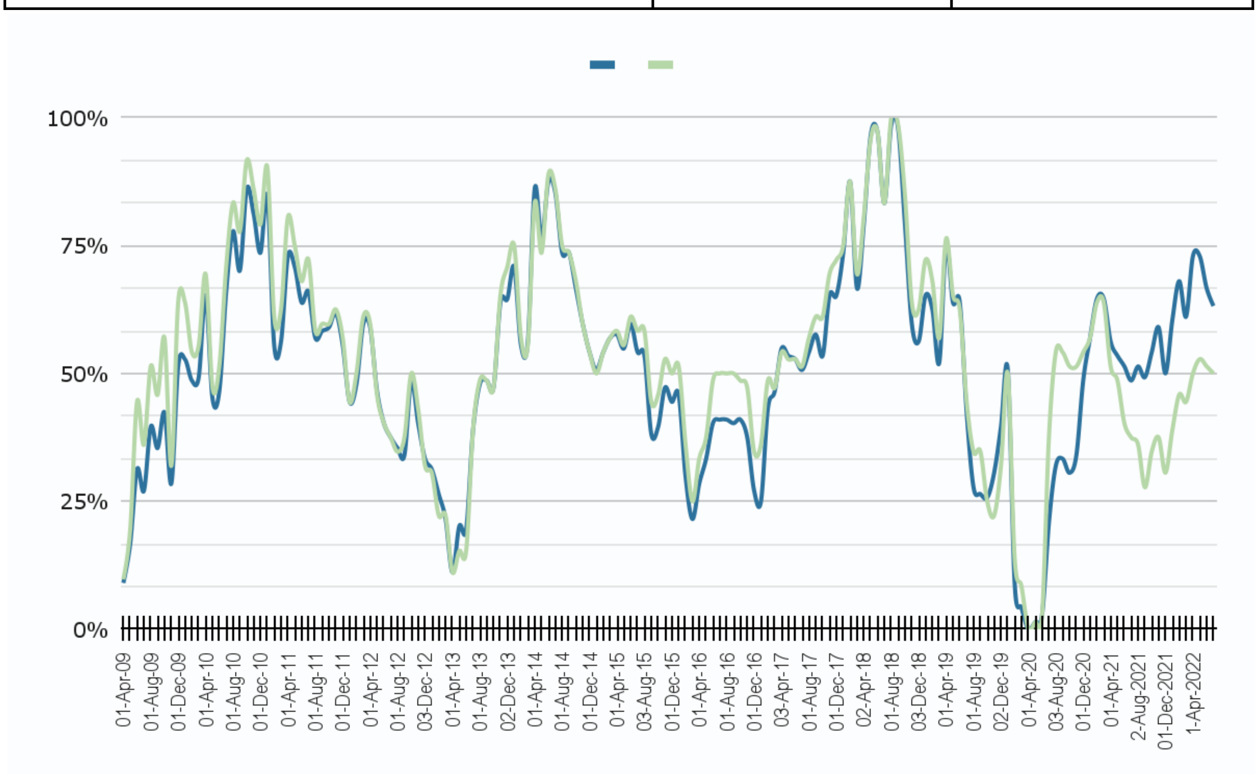
Our tool of choice to manage the portfolio risk and building wealth is - **Asset Allocation and Rebalancing.**

So, let's find out where we stand and what needs to be done.

ASSET ALLOCATION UPDATE

We use 3 inputs in our models - Nifty 200 Price to Earnings, Nifty 200 Price to Book and 10 Year G-Sec Yield. We have built 2 indicators and this is what they tell us. Scores are as of July 1, 2022.

Nifty 200 PE - 10 Year GSec based Model (Green line)	Score**: 50%**	NEUTRAL
Nifty 200 PE - PB - 10 Year GSec based Model (Blue line)	Score: **63.2%**	CAUTIOUS



Data Source: NSEIndia.com and Investing.com, prepared by Unovest

The asset allocation model scores are either neutral or cautious (*even after the recent market corrections*). It is still not time to get adventurous.

ACTION → The most reasonable course of action at this stage is to follow your asset allocation and invest accordingly.

The PE of Nifty 200 is now at its lowest in the 3 year cycle informing that it has become relatively attractive.

ACTION → If you have SIPs in mutual funds, it would be ideal to let them continue. If you are thinking of starting, this seems like a good time.

If you have a lump sum to invest, it would be better to spread it out over at least 6 months, if not a year.

TACTICALL → Equity allocation 50% max at this stage.

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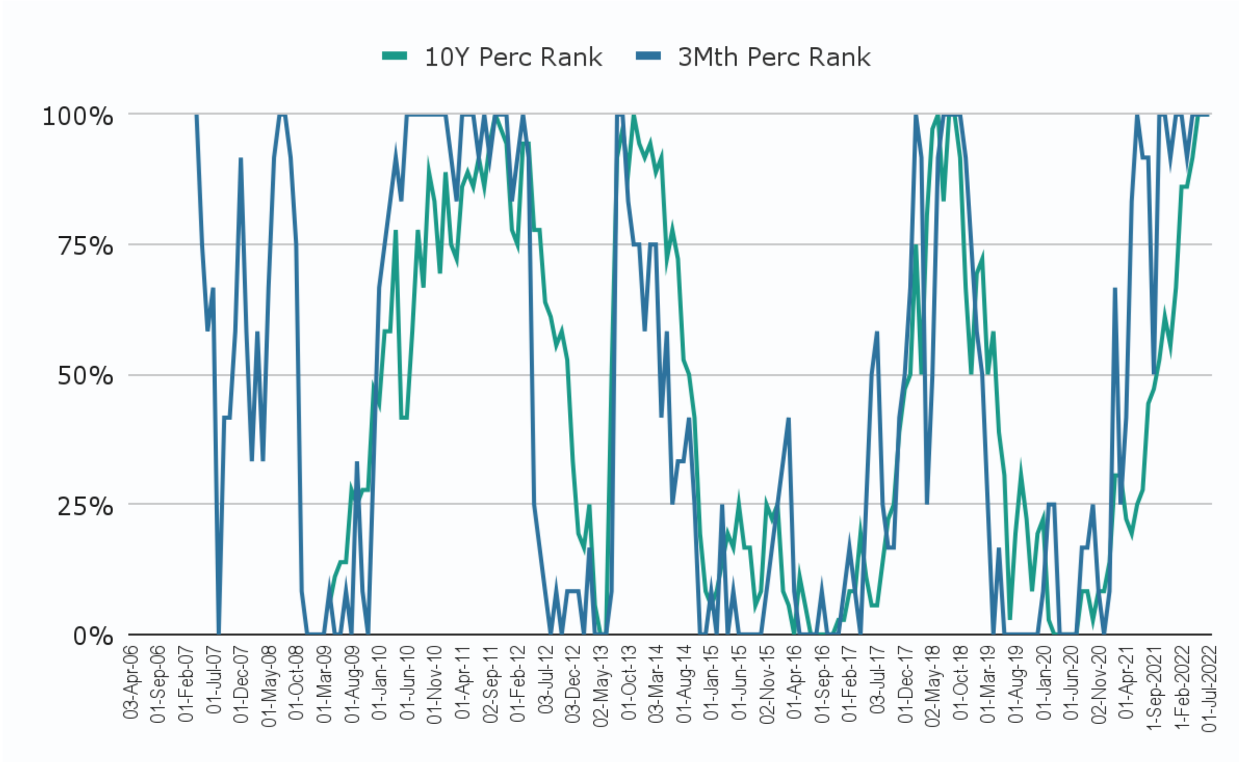
Interestingly, the fixed income yields are at their cycle highs. On a 3 year rolling basis the 10 Year G-Sec yield is at 100th percentile. Even the 3 month yields are at similar percentile levels. See chart below.



Data Source: Investing.com, prepared by Unovest

Fixed Deposit rates are inching up. HDFC Bank has increased its deposit rates 3 times in the last couple of months.
While there could be some more way up for the yields, this could be a good time to allocate to 5 year plus maturity investments in the space, systematically.

For very short term investments too, this is a good time. They suffered a lot in the last couple of years owing to low interest rates in the economy.
The liquid funds delivered as low as a savings bank account or even lower. The corporate bond funds hardly added anything. This is because of the

mark-to-market nature of mutual funds. Interest rates fell or were very volatile affecting values.

In contrast, an RBI bond at 7.15% is not marked to market and continues to deliver the stated return on a 6 monthly basis.

CURRENT INVESTING ACTION SUMMARY

Here's a summary table for better understanding.

Conservative Investor	Moderate Investor	Aggressive Investor
For Equity - Stick to large cap funds / ETFs and to less than 40% allocation to equities. **For Fixed Income** - Stick to Bank Fixed Deposits, EPF / PPF, RBI Bonds or other small saving schemes In debt funds, use only sovereign funds or funds such as Bharat Bond	**For Equity** - You can use large cap funds / ETFs along with midcaps for not more than 60% allocation to equities. **For Fixed Income** - Along with EPF / PPF, RBI Bonds you can consider Dynamic Bonds, Short term debt funds and Corporate Bond Funds.	**For Equity** - You can use large cap funds / ETFs along with midcaps / smallcaps for not more than 80% allocation to equities. **For Fixed Income** - You can consider Dynamic Bonds, Short term debt funds and Corporate Bond Funds.

Ultimately your goals and time horizon along with your risk profile should dictate your allocations.

THE GOLD PUZZLE

Gold Price 24k (in INR Mumbai, as of July 5, 2022)	- 53,870
Sensex Value (as of July 5, 2022)	- 53,134

Would you care to go to Google and type “gold price” and see the chart there. Click on *max* to see a longer duration one.

Now, in another tab, type “sensex share price” again click on 5 years or max to see a longer duration one.

What are your observations? I will share mine in the next edition.

FUNDTALK - Bharat Bond ETF April 2032

A low cost, passive debt investment that invests in bonds of PSU companies which are maturing on or before April 15, 2032. The fund essentially tracks the Nifty Bharat Bond Index April 2032.

The fund invests in bonds of PSUs such as NHPC, NTPC, NABARD, IRFC, REC, etc. which have **high credit quality**. It is a target maturity fund as the fund will unwind as on the specified maturity date. The fund costs 0.0005% to operate.

The current **yield to maturity or YTM** (the yield which you are likely to receive if you hold the fund till maturity) is at 7.7%. The net returns to you will be the YTM minus expenses. The difference is likely to be negligible.

However, the fund is **marked to market** and hence its daily values can see fluctuations. If you decide to exit before maturity, the returns can be different than the YTM at which you invest.

The fund **does not pay out any interest**. All interest is reinvested in the fund. It cannot be used as a fixed income option. The fund has **attractive taxation**. Post 3 years of holding, you pay 20% tax post indexation and before that you pay short term capital gains tax, if any.
The **best investment use case** of the fund is for a specific goal due around the maturity of the fund.

FUND WATCHLIST

FUND NAME	CATEGORY	BRIEF DESCRIPTION	INVESTOR RISK PROFILE	IDEAL TIME HORIZON
PARAG PARIKH FLEXI CAP FUND	EQUITY - FLEXICAP	Go anywhere fund, international stocks, arbitrage, holds cash, low volatility & turnover with focus on capital protection.	ALL	5 YEARS PLUS
EDELWEISS BALANCE ADVANTAGE FUND	EQUITY - HYBRID (DYNAMIC ALLOCATION)	Trend driven Dynamic allocation to equity based on fundamental and technical indicators to reduce volatility & drawdown, tax free rebalancing.	CONSERVATIVE, MODERATE	3 YEARS PLUS
DSP QUANT FUND	EQUITY - LARGE / MIDCAP	The fund uses an in-house quantitative model to build its portfolio from the universe of BSE 200 stocks. It operates as a low cost, passive fund with upto 4 rebalances during a year.	ALL	5 YEARS PLUS
MOTILAL OSWAL S&P 500 INDEX FUND	EQUITY - INTERNATIONAL LARGE CAP	A low cost index fund that replicates the portfolio of S&P 500 index (largest 500	ALL	5 YEARS PLUS

	(PASSIVE)	companies) in the USA.		
FRANKLIN INDIA FEEDER US OPPORTUNITIES FUND	EQUITY - INTERNATIONAL FLEXICAP	A feeder fund that invests in Franklin US Opportunities Fund, a multi cap fund portfolio of US based listed stocks across market caps.	MODERATE, AGGRESSIVE	5 YEARS PLUS
MOTILAL OSWAL NIFTY MIDCAP 150 INDEX FUND / NIPPON INDIA NIFTY MIDCAP 150 INDEX FUND	EQUITY - MIDCAP (PASSIVE)	A low cost index fund that replicates the portfolio of Nifty Midcap 150 index (representing 101st to 250th rank of the Nifty 500 index) in India.	MODERATE, AGGRESSIVE	5 YEARS PLUS
UTI NIFTY NEXT 50 FUND	EQUITY - LARGE CAP (PASSIVE)	A low cost index fund that replicates the portfolio of Nifty Next 50 index (representing stocks from 51st to 100th rank based on various factors) in India.	ALL	5 YEARS PLUS
HDFC INDEX FUND - NIFTY 50 PLAN	EQUITY - LARGE CAP (PASSIVE)	A low cost index fund that replicates the portfolio of Nifty 50 index (representing stocks from 1st to 50th rank based on various factors) in India.	ALL	5 YEARS PLUS
PARAG PARIKH TAX SAVER FUND	EQUITY - TAX SAVINGS	Tax savings fund based on the same investment philosophy as the Flexicap fund except	ALL	3 YEARS PLUS

		international stocks		
AXIS TREASURY ADVANTAGE FUND	DEBT - LOW DURATION	Low cost, low volatility fund with low maturity profile and high credit exposure	ALL	2 YEARS PLUS
HDFC SHORT TERM DEBT FUND	DEBT - SHORT TERM	Predominantly high credit quality, low risk portfolio with one of the lowest expense ratios.	MODERATE, AGGRESSIVE	3 YEARS PLUS
QUANTUM DYNAMIC BOND FUND	DEBT - DYNAMIC BOND	A conservatively managed debt fund that manages its portfolios based on interest rates movements with a portfolio of Govt Securities and high rates PSU Bonds only.	CONSERVATIVE, MODERATE	3 YEARS PLUS
HDFC CORPORATE BOND FUND	DEBT - CORPORATE BONDS	A high credit portfolio of AA and higher ratings	ALL	3 YEARS PLUS

Compiled by Unovest

Note:

- Currently the international funds are not accepting new investments.
- Tax Saver funds have a lock in of 3 years during which you cannot sell the investment.
- All debt funds have a mark to market feature which makes their NAV fluctuate based on interest rate changes.

NETI, NETI

(NOT THIS, NOT THAT)

Be wary of the moment when you feel that an investment must be done. This is what will get you pot at the end of the rainbow.

This scheme is what will solve all the problems. It has made your friends rich and left you cursing as to why "I didn't do it earlier."

Everyone is already in it and this is your last chance to get on the gravy train before it moves on.

That moment, that thought is the most dangerous. It is usually the peak of the cycle when greed dominates our thoughts..

It is in that moment, you multiply the chances of losing your money.

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I know I could have just called it FOMO, but would it have been enough?

AN EXPERIMENT FOR YOU

Let's say you are an investor who was hit hard by the 2008 global financial crisis. Since then, you have been a conservative investor who has come to believe and fear all the uncertainty in the world. There's just too much happening.

Given this view, as an investor you chose an asset allocation to invest equally in equity and Gold. Equity brings in the likely upside but Gold is the insurance against the world going bonkers.

To invest in Equity, you decide to take the passive approach and pick the Nifty 50 Index as it represents 60% or more of the overall market cap and of course, some of the largest listed companies.
To invest in Gold, you pick an ETF (e.g., UTI or HDFC's)

You start a SIP of Rs. 10,000 per month for the last 10 years. What does the portfolio look like today?
Happy with the strategy? What would you change?

Let's talk about that in our virtual AMA.

MONTHLY AMA

Ask me anything on Investing, money, personal finance, financial planning, asset allocation. The next AMA event is scheduled on Jul 23, 2022 from 4 PM to 6 PM

This is a subscriber exclusive event. Invites will be sent automatically to subscribers.

THANK YOU FOR READING.

Do send your responses, queries and feedback to vipin@unovest.co

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TERMS SIMPLIFIED

MARK TO MARKET

Mark to Market refers to an activity where it is figured out how much will a existing investment / asset in the portfolio will get, if we were to sell it today. Usually there is a predefined formula with inputs that helps arrive at this mark to market value.

YIELD TO MATURITY

We know that every bond has an interest rate attached to it. The RBI Floating Rate Bond, 2020 pays out 7.15% per year, for example.
Now, this assumes a static value of the bond. Again, for example, the RBI Bond has a face value of Rs. 1000 per bond unit.
But when the value is marked-to-market, it can change. This Rs. 1000 may become Rs. 1100 or Rs. 950.
At that point, if you, as an investor, buy the bond at Rs. 1100, that becomes your buy price. However, the interest rate on the bond is still 7.15%.
So, the rate of return on your investment will be the interest rate divided by the price.
7.15% divided by Rs. 1100, that is, 6.5%. This is also called the yield.

If you have understood this then you can grasp the fact that yield to maturity indicates all the returns that a bondholder will receive if s/he holds to bond till its maturity. There is a formula to calculate that and you can easily find it on Google.