Comments

Many investors make a portfolio, allocate resources into assets and just sit back. But in order to make your portfolio work for you, it's necessary to constantly keep a tab on your investments and do a critical appraisal of your financial goals

Portfolio making is a crucial part of one's investment planning in order to generate a corpus of wealth with minimum risk and maximum return over a period of time. A portfolio is basically a carefully planned investment across a collection of assets that come in several steps.

However, the act of portfolio making is not static. Rather, it's an ongoing process. The systematic way of portfolio making includes various factors that range from identifying investment goals, assessing one's risk appetite, planning asset allocation according to one's goals, deciding a time horizon and diversification of asset classes to minimize risk and weather market volatility.

Let's analyze these steps and also look at various factors that go into making a winning portfolio.

Identify goals and time horizon

Being sure of one's investment goals is one of the crucial steps toward portfolio making, for it makes the selection process of asset classes easier.

“Before making a portfolio one must first list down one's future goals. Investments towards short term goals get allocated to debt completely. Medium term and long term goals have a mix of various asset classes,” says Harsh Vardhan Dawar, Director, Wealth Cafe Financial Advisors, Mumbai.

Experts say it's very important to determine why you want to invest. Investment can be for various purposes. For instance, it can be for retirement, for children's education, for children's or sibling's marriage or buying a house.

“Unless you have clarity on your objectives you are bound to make mistakes like selecting wrong asset classes. Goal identification also helps in estimating the time horizon of your investment which is the key for selecting the right options,” maintains Jitendra P.S. Solanki, Certified Financial Planner & Founder, JS Financial Advisors, Delhi.

Decide how much you need

A common mistake many people make is to discount the actual corpus of wealth they need to accumulate within a particular time horizon. However, being unsure on the actual corpus could derail the whole purpose of portfolio making, caution financial planners.

“Once you have listed your goals, calculate what is the corpus required to achieve your goals. This will help in knowing what is the wealth you need to accumulate from these investments post-taxation,” maintains Solanki.

Assess risk appetite

The next step to making a winning portfolio is to asses one's risk appetite to ascertain whether you're comfortable in investing in high-risk instruments.

“Many asset classes' produce higher returns but have risk on higher side in comparison to others. Identify how much risk you are willing to take,” adds Solanki.

Risk, however, is a relative term. For instance, risk has a separate meaning for an executive in his mid 30s and earning a six-figure salary with no liabilities, than for a middle-aged professional who is about to retire in 10 years and has to pay back mortgage on home loan, arrange money for his

daughter's marriage, finance his son's education as well as save a corpus for post retirement.

Plan asset allocation

A right asset allocation plan that matches with your goals and risk bearing abilities would go a long way in making your investment plan work, say experts. Here an expert advice by a financial planner would make the task of asset allocation easier.

“Once you have your goal requirement, decided the amount willing to invest, the returns you want to achieve and risk you are willing to take, you can now very well select the asset class which will meet your objectives. How much allocations you have to make to asset classes will also emanates from this entire process as the asset allocation that is right for you depends on your investment time frame, goals, and tolerance for risk,” adds Solanki.

Review your portfolio

Once you've made a portfolio and allocated resources, don't just ease up. Rather like a pro investor, try to constantly evaluate and critically review your portfolio to ensure your investment plans are on right track, advise experts. “Reviewing your investment portfolio is an examination of your investments to identify and fix any weakness which is reducing the performance needed to achieve your financial goals,” adds Solanki.

However, there's no thumb rule on how often you should review a portfolio as this depends on the size of the portfolio and the time horizon. “For retail investors, a quarterly review should be more than enough,” maintains Dawar.

Solanki advises another way of reviewing. “If the investment is done for few years say 4-5, then you need to review your portfolio once in every six months. Since you do not have much time here, you might have to do rebalancing early if it is not meeting your expected results. This is especially applicable to retired individuals who invest for such periods with objective to have some steady flow of income and need to book regular profits. However, if your goals are for very long term say 15-20 years then once in a year review should be sufficient as the investment you have selected are more consistent in long term and any short term underperformance will not be a worry factor for you,” he maintains.

The process of reviewing a portfolio is akin to creating the investment portfolio, say experts. “The review process involves tracking the expected returns and the ratio of various asset classes (eg, debt: equity of 30:70) versus the actuals. Too much deviation will then have to be looked into,” maintains Dawar.

Adds Solanki. “The process of reviewing is somewhat similar to creating the investment portfolio. You have to recheck all your goals and your expected results from the portfolio. Then analyze the asset allocation you have chosen on various parameters and see if it is meeting your objectives. Match your requirement with the performance of your investment portfolio and act upon if there is any deviation or you have reached a mile stone. What strategy to adopt depends on whether there is any underperformance or asset allocation mix has changed.”

Restructure portfolio, if necessary

Once the reviewing process s on, you might find that your portfolio is falling short of your expectations or your investments are not be performing as you planned. If that is the case, your portfolio is in dire need of restructuring, believe experts.

However, there's no perfect way of restructuring a portfolio as different strategies need to be applied for different situations and according to your goals and tax liability. The most common ways of restructuring a portfolio include replacing non-performers, reducing/increasing specific asset exposure and rebalancing.

“Portfolio can be restructured by selling one asset class and buying into the other. But this would result in tax implications and the same need to be considered. If the deviation from the set ratio, for example 30:70 is not too much, one can alter future contributions to the assets classes so that over time the ratio of 30:70 is reached. In case of minor deviations, one should compare the costs and one may decide not to do any restructuring all together,” maintains Dawar.

Reducing or increasing weightage to a particular asset class can be done either through selling securities or buying more units of another asset class. However, the specific strategy depends on the market scenario and the taxation.

As Solanki points out, “Trimming exposure to any asset class can only happen if markets are doing well. In bear market scenario the strategy can lead to more losses. Also, if it is done in short term, it can lead to higher taxation. Thus, you can reduce exposure to an asset class by adding units to other asset classes in your portfolio provided one has the required surplus to invest more. Similarly, to increase weightage to any asset class, if market conditions are not allowing you to buy cheap, you can sell units of other asset classes.”

So to cut the long story short, don't put all your eggs in one basket while making or restructuring a portfolio. Instead, tailor your portfolio to your own financial goals.