learn with DNA...

You can't beat the market all the time

Tonnes of material get written every year in a bid to answer this simple question: "What is the best way to invest in the stock market?"

The answers vary, year to year, author to author. A lot of the advice coming out tends to concentrate on how a stock or mutual fund has performed in the past with the assumption that something that has done well in the past will continue to perform well in the days to come. But, it rarely works like that.

Most of the mutual funds figuring among the top 10 best-performing schemes in a given year are usually nowhere to be seen the next year. An investor who gets into a scheme on the basis of its last year's performance will clearly be disappointed. A stock, which is hot in a given year, may not perform well enough the next year. Bottomline — past performance does not guarantee future performance.

So what's the way out? Burton G Malkiel attempts an answer in the book, *A Random Walk Down Wall Street*. He feels the best way to invest is to invest in index funds.

A 'random walk', as Malkiel explains, is "one in which future steps or directions cannot be predicted on the basis of past actions. When the term is applied to the stock market, it means that short-run changes in stock prices cannot be predicted. Investment advisory services, earnings predictions, and complicated chart patterns are useless."

"Taken to its logical extreme, it means that a blindfolded monkey throwing darts at a newspaper's financial pages could select a portfolio that would do just as well as one carefully selected by the experts," adds Malkiel.

Now, no investment expert would like to be compared to what Malkiel refers to as "bare-assed apes." So, they try to dazzle the investors largely with two investment techniques — technical analysis and fundamental analysis. But Malkiel's contention is that these techniques usually don't work because there are too many variables influencing investment returns these days.

Malkiel, who is a professor at Princeton University and first wrote this book more than three decades back, points to the efficient-market theory to explain why none of the investment techniques works.

"Efficient-market theory explains why the random walk is possible. It holds that the stock market is so good at adjusting to new information that no one can predict its future course in a superior manner. Because of the actions of the pros, the price of individual stocks quickly reflects all news that is available. Thus, the odds of selecting superior stocks or anticipating the general direction of the market are even."

This is why "buying and holding a broad-based market index fund is still the only game in town," writes Malkiel.

Nifty hourly resistances for March 3, 2008

Time AM/PM	Resistances (1)	Upon surpassing resistances (2)	Rally exhausts at (3)
09.55 - 10.30	5214	5258	5304
10.30 - 11.30	5198	5248	5294
11.30 - 12.30	5182	5238	5284
12.30 - 13.30	5166	5128	5274
13.30 - 14.30	5150	5118	5264
14.30 - 15.30	5134	5108	5254

NOTES

Trading derivatives is a risky activity. These studies do not assure profits. Please consult a certified financial analyst before trading.

—Vijay Bhambwani

Post office deposit rates and features

Kisan Vikas Patra	
Interest	Doubles in 8 yrs 7 mnth
Effective interest rate	8.41%
Min. amount	Rs 100
Max. amount	No limit
Tax breaks	None
Monthly Income Scheme	
Interest	8%+ 5% bonus at maturity
Tenure	6 yrs
Min. amount	Rs 1,000
Max. amount	Rs 4.5 lakh for single a/c Rs 9 lakh for joint a/c
Tax breaks	Section 80C deduction
National Savings Certificate	
Interest	8%
Effective Interest Rate	8.16% (semi annual compounding)
Tenure	6 yrs
Min. amount	Rs 100
Max. amount	No limit
Tax breaks	Section 80C deduction
Public Provident Fund	
Interest	8%
Tenure	15 -16 yrs
Min. amount	Rs 500
Max. amount	Rs 70,000 p.a.
Tax breaks	Section 80C deduction
Recurring Deposit	
Interest	7.5%
Tenure	5 yrs
Min. amount	Rs 10
Max. amount	No limit
Tax breaks	None
Senior Citizens Savings Scheme	
Interest	9%
Tenure	5 yrs
Min. amount	Rs 1,000
Max. amount	Rs 15 lakh
Tax breaks	Section 80C deduction
Min. age	60 years
Time Deposit	
Interest	6.25-7.5%
Tenure	1,2,3,5 yrs
Min. amount	Rs 200
Max. amount	No limit
Tax breaks	None

Go it goal-wise, keep a leash on expenses

That is the prescription for *DNA Money* reader Dr Manish Rathi

Priyesh Shah

Dr Manish Rathi, 30, is a practising physician. His spouse, also 30, is a housewife and they have a daughter who is 2 years old.

His financials reflect his financial literacy. Having clearly set his financial goals, he has already achieved a head start in wealth creation.

Current financial position

Dr Rathi has assets worth Rs46.50 lakh. His liabilities include an outstanding housing loan of Rs7 lakh and a car loan of Rs1 lakh. This leaves him with a net worth of Rs38.50 lakh. He has a professional income of Rs4 lakh p.a. (net of tax) and his annual expenses are Rs2.74 lakh. Thus, he has a surplus of Rs1.26 lakh p.a.

Current insurance coverage

Dr Rathi has an endowment insurance policy of Rs3 lakh and pays an annual premium of Rs21,190. He also has an annuity policy from LIC for which he is paying a premium of Rs10,006 p.a.

He is paying Rs9,400 p.a. for a medical insurance cover of Rs5 lakh. The available deduction on account of the investment u/s 80 D is utilised. He also has a car insurance.

Financial goals

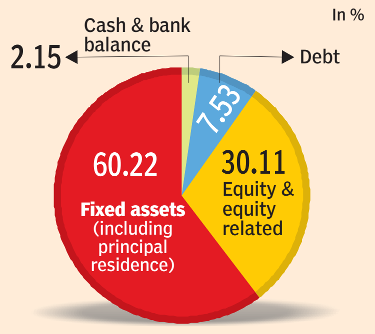
- Provide for his daughter's education, which starts from next year
- Purchase a luxury car three years from now
- Provide for daughter's marriage, when she turns 25. The amount to be set aside for the same is Rs25 lakh (present value).
- Provide for a comfortable life post retirement at the age of 65
- Purchase an additional home for investment purpose by taking a loan

Current asset allocation:

Dr Rathi's current asset allocation is as under:

Particulars	Amount (In Rs.)
Fixed assets (including principal residence)	28,00,000
EPF	1,00,000
Equity	10,50,000
Mutual funds	3,50,000
PPF	1,00,000
Post Office savings	50,000
Cash and savings bank	1,00,000
Other valuables	1,00,000
Total (including fixed assets)	46,50,000
Total (excluding fixed assets)	18,50,000

Asset pie



Since there is a loan outstanding on the fixed asset, which is the house, Dr Rathi's investible assets are Rs18.50 lakh. This should be considered for funding his future goals and objectives.

Income-expense analysis

Dr Rathi's expense-to-income ratio is 68.55%, which indicates that expenses are under control. Optimisation of savings at a young age would result in great wealth creation over a period of time.

Recommendations

- *Daughter's education:* Dr Rathi's daughter would start her pre-schooling and schooling education from next year. During the initial years, the expenses are lower compared with graduation and post-graduation expenses. Budgeting of expenses and savings would play a crucial role for funding of pre-schooling and schooling expenses. Amount for graduation and post-graduation expenses should be determined and can be accordingly planned for.
- *Purchase of luxury car:* Buy the car on loan and accordingly, the amount of EMI should be repaid over a period of five years. The EMI for loan of Rs8 lakh at an interest rate of 13% for a term of 5 years would be Rs18,200.
- *Daughter's marriage:* The amount required for his daughter's marriage is Rs25 lakh by present value. To achieve this objective, he would need to systematically start investing Rs3,220 per month, up to the time of his daughter's marriage. The investment should be made in equity-linked mutual funds and may be assumed to earn a return of 15% p.a. For calculation purpose, we have assumed the inflation to be around 5% p.a. throughout.
- *Retirement planning:* To maintain the present lifestyle after retirement, Dr Rathi needs to start investing Rs3,200 per month up to his retirement at 65. (assumed life expectancy 75 years; present value of expenses Rs3 lakh p.a.; investment rate 10% p.a.; inflation rate 5% p.a.). This would build an adequate corpus to sustain his retirement lifestyle. We have considered the present balance of PPF, which would be growing at 8% p.a. His EPF amount, at time of retirement, should further add to the retirement corpus.

my finance

- *Purchase of second home:* Dr Rathi would like to purchase a home as investment. He already has an outstanding home loan for which he is availing deductions on interest payable on home loan and principal amount u/s 24 & 80 C, respectively, up to the specified limit. However, when the house is given on rent, the entire amount of interest on loan is allowed for deduction. He should first consider the asset allocation before investing any amount.
- *Insurance planning:* Insurance should be for protection and not for investment. After considering his insurance needs, it is found that Dr Rathi is under-insured. Also, he has outstanding loan liabilities. He should take a term insurance of Rs25 lakh to ensure adequate protection.

To conclude, Dr Rathi needs to budget his expenditure and maintain the savings proportion. At a younger age, reducing avoidable expenses can enhance wealth creation. He should follow an investment strategy based on his risk profile. Systematic investment over a period of time will help achieve the future goals and objectives set.

The writer is a certified financial planner working as relationship manager with Mumbai-based SRE Financial Planners. Views are personal and do not necessarily represent those of FPSB India. Feedback may be mailed to myplan@fpsbindia.org.

If you would like to be featured and need a financial plan made by a qualified planner, mail to: *mymoney@dnaindia.net*

'Budget impact? Global cues'll be key'

Anoop Bhaskar *is the head - equity of UTI Asset Management Company. An MBA with specialisation in finance, he has been associated with fund management and equity research for 14 years now. Prior to joining UTI AMC, he was overall in-charge of equity products at Sundaram Asset Management, Chennai and has also worked with Templeton Asset Management, Chennai for 10 years as senior research analyst and portfolio manager. Bhaskar shared his views on the Budget with* **N Sundaresha Subramanian**. *Excerpts:*

How would you rate this budget, populist or pragmatic?

Populist. Are elections round the corner?

Do you think the market is overreacting to the farm loan waiver... How do you see the move panning out for the banking sector?

It is meant to help the cooperative banking segment, as it was reeling under bad loans and lack of capital adequacy to write off such loans. The burden on the PSU Banks is roughly 25-30% of the total.

What is your view on the other measures announced for the banking sector, like the exchange traded currency futures? How do you see things playing out in the sector?

In the medium-to-long term, these measures will help banks shore up their risk management at lower costs and deepen their skills to operate in a global environment.

q&a

Do you think the Budget provides enough support to keep the infrastructure juggernaut rolling?

One important measure to boost infrastructure spending is the re-introduction of section 80(M), which does away with double taxation of dividend. This will help the holding company structure in infrastructure spending to be taken public faster and easier.

> "The government and RBI will continue to explore measures through which such flows can be calibrated and the re-appreciation can be moderated"

When FM says monitor and manage external capital flows, what does he mean?

> "With the economy being liberalised, the role of the Union budget has reduced considerably."

The government and Reserve Bank of India (RBI) have always maintained that stable capital flows are desired than short-term 'hot' money. During calendar year 2007, one of the key challenges faced by RBI was the strong inflow of dollar from abroad. In this context, the government and RBI will continue to explore measures through which such flows can be calibrated and the re-appreciation can be moderated.

Do you expect a further downside in the market through March as players would rush to sell before the higher short term capital gains tax becomes applicable?

Global cues will have a greater impact on the markets than the budget.

Any other important takeaway for the markets and investors, especially MF investors, from the Budget?

With the economy being liberalised, the role of the Union budget has reduced considerably.

Disclaimer: UTI AMC is proposing, subject to market conditions and other considerations, a public issue of its equity shares and has filed a Draft Red Herring Prospectus with Sebi.

Just 5 questions...

Sivasubramanian KN
Senior portfolio manager - equity, Franklin Templeton

What is your view on the bonanza for farmers?

The various measures, including waiver of farm loans, need to be viewed from the 'inclusive growth' perspective and the problems being faced by small farmers.

How do you see the tax cut moves in the Budget?

Overall, fiscal measures such as cut in direct taxes and tax exemptions along with focus on the rural segment are aimed at boosting consumption. While these are popular measures, the lower deficit projections give comfort on the fiscal front.

Do you see Friday's market move as a thumbs-down to the Budget?

Indices have fallen due to selling in certain stocks on account of MSCI rebalancing and also due to the budget.

What are the Budget measures the market did not like?

The markets have started 2008 on a weak note due to a combination of global uncertainty and unwinding of speculative positions by domestic investors. Against this backdrop, the increase in short term capital gains tax to 15% had an impact on investor sentiment and there was also disappointment in a segment of the market due to absence of tax cuts.

Any positive takeaways from the Budget?

We believe the increase in short term capital gains tax could discourage frequent churning and possibly lead to long-term investments.

Investors should continue to invest in line with their risk profile, for the long term

Make the most of Budget inaction, play MFs as before

It was the last budget (at least for this term) from the finance minister and expectations were running high. For someone who usually introduced at least one significant measure in nearly every budget for the investor, this was a particularly uneventful one. At least there wasn't much for the mutual fund investor.

May be the finance minister's team thought there wasn't much left to be done in the mutual fund industry. May be the growing net asset base of the mutual fund segment gave the impression that everything was fine. Or may be, they felt the Securities and Exchange Board of India was doing enough for the mutual fund industry and that's how it should be.

All the same, one can draw positively from this inaction — continue to invest in line with your risk profile without compromising on long-term investment goals.

The following points should be kept in mind:

1. Stay faithful to your financial plan; the Budget has given you no reason to deviate from that. Although there has been no change with respect to individual investments (like mutual funds, bonds, stocks) and life insurance, other changes like raising the basic income tax exemption limit (from Rs1,10,000 to Rs1,50,000) will have a positive impact on your savings (which is a minimum of Rs4,000 for every tax-paying investor).

after effect

Now, you can increase your contribution to your financial plan without burdening your finances. In other words, do not fritter away the finance minister's largesse on wasteful expenditure.

2. The budget has also not given you any reason to take on more risk than necessary. If you did not have the risk appetite for high-risk investments like thematic funds and mid-cap funds earlier, nothing has happened overnight to change that scenario. In other words, these investments are still off-limits for you.

3. You must continue to review your financial plan to ensure that it is broadly in line with your asset allocation. Your financial planner is best placed to help you with the review process. Make sure you are closer to achieving your investment goals today than you were yesterday and look for tangible signs of progress. If that is not happening, your financial planner better have an explanation for it.

4. Think long-term. Although this is a fundamental of successful investing and is not in need of the finance minister's endorsement, by raising short-term capital gains tax (from 10% to 15%), he has made his preference for long-term investing very clear. So, if you were a short-term investor earlier, it's time you also started investing for the long-term (which is at least 3-5 years in our view).

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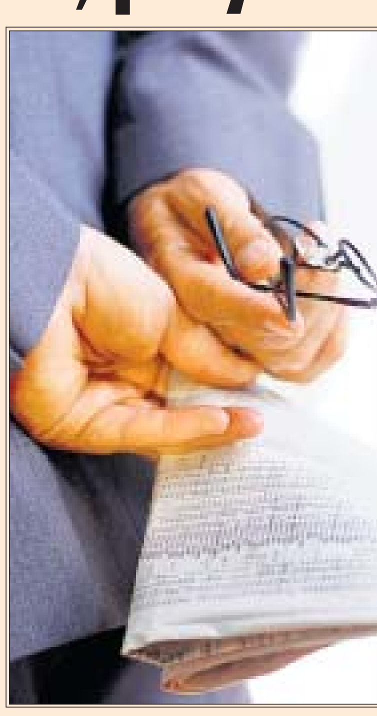
What the fundmen say



> "Budget announcements are in line with expectations... Share market to remain range-bound with no significant movement."
>
> —**Vijai Mantri**, CEO, Deutsche MF

> Markets will be more volatile as there is no direction. People will take time to understand the gambit of finance minister."
>
> -**R K Gupta**, managing director, Taurus MF

> Markets will be range-bound. It will augur well for the corporate bond market on the back of announcement made during the budget."
>
> -**Mahendra Jajoo**, fixed income head, ABN Amro MF