FIFA Perspectives

April 2014

Time to say bye-bye to global diversification?

Seven months seems such a long time in our markets. Seven months ago, in September 2013, the rupee was reeling under pressure, our current account deficit was seen as unsustainably high, India was seen as one of the most vulnerable emerging markets due to its twin deficits, and our equity and bond markets were rattled by the mere thought of global liquidity exiting Indian shores. Investing overseas came sharply into focus, global diversification came center-stage and conversations no longer were around whether to diversify globally but about finding the right diversifier : should it be US, Europe or a global fund.

Cut to April 2014 - just seven months later. The rupee has staged a huge comeback on the back of big bucks that FIIs have invested into Indian markets, our stock market is scaling new all-time highs and the birth of a secular bull market has been proclaimed, there is widespread anticipation that the new Government that we will all elect in the coming weeks will be stable and growth focused, the current account deficit has been effectively contained to more manageable levels and optimism about economic recovery, inflation control and lower interest rates is rising by the day.

While we move ahead with investing in Indian markets with renewed confidence, a question that begs an answer now is this : Is it time to say bye-bye to global diversification? Is the need to have foreign currency denominated assets as strong as was felt 7 months ago? Is the concept of global diversification as a risk control mechanism relevant any longer, when domestic markets appear bullish? We asked leading IFAs to share their views on two specific questions we posed to them :

1. The rupee has appreciated significantly against the dollar. Is the case for global diversification now weak? Is it wise to invest in dollar assets now when the rupee is relatively strong, in anticipation of a longer term weakening trend, or do you think the longer term direction of the rupee has changed?

2. Optimism on Indian equity markets is building. Does it make sense now to anyway stick to global diversification or is one better off focusing attention purely on Indian markets now?

Here are their responses. We are grateful to these successful advisors for readily agreeing to share their views with Wealth Forum, for the benefit of the wider advisory and distribution fraternity.

Time to say bye-bye to global diversification?

Major Ashish Chadha, Chadha Investments, Delhi (Member, FIFA)

No - answer to both is the same. The world as a whole is smarter, brighter than India individually and India is a net importer .You need to be in the world as a strategy.

Dhruv Mehta, Mumbai (Member, FIFA)

Currency : The case for global diversification still remains from a long term asset allocation viewpoint. Volatility in currency supports the case for diversification. Clearly the sharp depreciation of the Rupee over the last 2 years has been very sharp and therefore there is a likelyhood of the Rupee remaining stable or appreciating over the next 2 years. Thus one should not expect currency depreciation to amplify returns from international investments. It is very difficult to make very long term prediction of the currency movement . Over the last 30 years the Rupee has depreciated by 6-7% per annum against the dollar. Hence I would not predict a change in the long term trend. We believe the case for global diversification in the equity of fundamentally strong international companies remains compelling.

Market : Indian markets could be at an inflection point if the winds of change in Delhi lead to better governance and higher economic growth. Higher earnings growth coupled with a PE re rating could see significant gains in the domestic market maybe far superior to returns from international investments. Thus greater attention must first be put on the domestic markets .

Over the last decade FIIs have been increase their investments in India while domestic investors have been sellers. Ownership of Equities by domestic investor has reached abysmal levels and these have to be raised. The question of global diversification arises only when there is a significant exposure to equities.

Bharat Phatak, Wealth Managers India, Pune (Member, FIFA)

Currency : August 2013 was a wake-up call on global diversification. I do not think it's time to go back to sleep now. Global diversification is necessary, albeit in baby steps as we learn the ropes. The home country bias will always remain. Large allocations in the portfolios will be to India. India remains the big bet, overseas diversification should be the appropriate hedge. Fundamentally, the INR will depreciate to the extent of higher relative inflation. Look at 40-year, 30-year, 20- year and 10-year numbers, and you will find ~5.5% depreciation in the INR versus the USD. This broadly corresponds to the difference in the inflation numbers in both the countries.

Another way to look at this - If you have responsibilities in USD - such as overseas education for your child 10 years from now, you can build up the provision in that currency in an appreciating asset.

Market : Look at a 3 year view. US & European economies are likely to recover to their normal growth path. Corporates in advanced countries are not leveraged, but cash rich. Dividend yield in many places is higher than bond yield. Hence, it is not necessary to conclude that opportunities exist only in India. A stable government is necessary but not sufficient to address the problems faced by India. While one hopes that we get a strong government and effective policy initiatives, it is too soon to celebrate. Hence a balanced approach in asset allocation will be prudent.

Pallav Bagaria, Brand New Day, Guwahati (Member, FIFA)

Currency : If your question is, are we recommending less now to our clients global diversification, the answer is NO, if you say that, are the clients less interested now, the answer is a clear YES. We take it as a asset allocation strategy. We believe currency weakness will remain a process over the years, it will no longer be a sudden thing as it happened over the last two years. We believe investors should invest in these assets as a compulsory allocation rather than taking any call on it.

Time to say bye-bye to global diversification?

Market : Situation these days change very dynamically, so just because a particular market has done well or may be will continue to do well over a period of time should not change the area of diversification. If portfolios are not diversified, one should be ready for another July 15th. As taught to us, don't keep all your eggs in one basket.

Lovaii Navlakhi, International Money Matters, Bangalore (Member, FIFA)

Global diversification is part of strategic allocation, and not tactical allocation. We recommend that all our clients have approximately 10-15% of their assets invested globally. Of course, this must consider immediate cash flow needs in India, and those have to be provided separately. The whole idea of global assets is that we hedge our investments as the number of factors affecting returns in each country is varied and diverse. Most importantly, it is a method to hedge one's risks and not a method to generate returns -- at least, that's not the primary motive.

When we look at annual returns across countries over the years, there is no consistency in outperformers. That alone justifies the need to indeed practice asset allocation, which should start, as I have repeatedly said, country-wise, currency-wise and then asset class-wise. We did not have products/ options earlier, but there is no excuse not to have recommended (and to continue to recommend) global diversification in the past 3 years.

Vinita Idnani, Capital League, Gurgaon (Member, FIFA)

Currency : Irrespective of rupee levels, in our view global diversification continues to remain a prudent investment strategy especially for HNIs which is our client segment. Equities are long term investments and in the long term rupee is expected to depreciate at the rate of 4-5% which is close to the inflation differential between the two countries. Also, the case for investment in global funds has become stronger with the improvement in the world economy. Most of the companies based in US and Europe not only offer diversification to those markets but the underlying companies derive more than 50% of their revenue from non-US and non- European markets indirectly giving a play on the other world markets.

Market : Asset allocation and diversification strategies must not change just because prospects for certain asset class look better. This will defeat the entire case for diversification.

Sanjay Sondhi, Pegasus Advisory, Delhi (Member, FIFA)

I still maintain that we must persist with allocating investor wealth in USD assets ; it may not take very long for the Indian market rally to pause and correct ; the next event is the Indian election results and the outcome points to a fractured mandate which will be terrible for the Indian stock market.

And even if Mr Modi comes into power with the assistance of some coalition partners the market will still tank based on investors assessment of the stability of such an alliance and the pound of flesh these partners will demand.

In my view Indians are under invested in USD and as part of a broader asset allocation strategy we must achieve that percentage which we have decided upon for the particular investor.

Abhenav Khettry, Vyana Wealth, Kolkata (Member, FIFA)

I have the following views on International Funds:

1. Recommending funds has become something of a seasonal fruit habit, sell, what is selling in the market, flavour of the season. Advisors have to follow a long term asset allocation and the current scenario is good for entering developed markets. In my opinion, asset allocation should also include developed market equities, as there is a difference in the movements of developed and developing market equities. Developed market equities also have much lower volatility than emerging market equities, thus they need to be a part of asset allocation

2. Returns in Indian equities are liquidity driven. Despite rising markets, DIIs are net sellers, only FII flows are fuelling this rally. The moment the tap is turned off, we will see renewed volatility in Indian equities. Our asset allocation cannot be based on foreign liquidity.

3. Despite improving current account figures we are net importers of basic energy, the appreciation of the rupee is primarily because of investment flows and like I mentioned earlier, these could be seasonal. Having a portion in Dollar or Euro assets is advisable. Always understand your entire portfolio will not behave in the same way at all times and this is why it is important to diversify internationally.

4. We as a house now have 20% of equity assets in overseas equity and look to proportionately increase it to atleast 25% of our overall equity AUM.

5. Investors are also now understanding and appreciating the benefits of investing internationally and the funds are also becoming a pull product.

Hemant Rustagi, WiseInvest Advisors, Mumbai (Member, FIFA)

Although appreciation in the rupee has negatively impacted the performance of international funds, the current uptrend may not be sustainable for long for more than one reason. First, the RBI is not likely to allow the rupee to strengthen beyond a certain level as it would hurt exports. Second, if the election results turn out to be unfavourable for the market, the resultant FII selling would weaken the rupee. Third, an increase in the US Fed tapering as well as removal of restrictions on gold imports could impact rupee negatively.

Therefore, investors who have been investing in international funds as a part of their geographic diversification strategy should continue their investment process. However, for those investors who may have been investing aggressively in these funds, it's time to pare the exposure and bring it within a range of 5-10 percent of their overall equity portfolio size.

Global investing adds a new dimension to diversification as international markets are un-correlated in a number of ways and one gets an opportunity to invest in economies that either have a current account surplus or low fiscal deficit. Therefore, the current uptrend in the rupee and domestic equity market should not compel an investor to abandon the strategy of global diversification. In fact, regular investments in international funds in a disciplined manner can be a good idea. Considering that currency fluctuations can impact returns significantly, the strategy of making regular investments can even out its impact over time.

However, it would be prudent to highlight here that international funds are suitable only for experienced investors with a decent sized equity portfolio. Retail investors, who are in the process of building their equity fund portfolio, should continue to focus on funds investing in domestic markets as they provide ample opportunities to diversify portfolio across market caps as well as different investment philosophies.

Conclusion

Global diversification may not be top of mind for many investors, but successful advisors continue to stay sharply focused on the merits of global diversification and are not really getting swayed by near term trends. As Bharat Phatak puts it succinctly, events of 7 months ago were a wake up call - let's not go to sleep now. Most of the advisors we connected with are unanimous in their view that they do not see the Indian rupee getting into a secular appreciation mode till such time that inflation differentials persist. Some believe that tactically investing overseas when the rupee has substantially appreciated, may be a smart thing to do. Most of the advisors also believe that euphoria over Indian equity markets should not be taken as a sign to go overboard. Helping your clients maintain their asset allocation discipline is the key to long term success. Maintaining allocations in an asset class that is temporarily out of sight and out of mind for many investors, is a challenge - but dealing with this challenge and helping clients stick to agreed plans is perhaps what will underpin long term success - theirs and yours.

FIFA Perspectives

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Pearls of wisdom from the Gurus of their professions

Prashant Jain, CIO, HDFC AMC shared his rich market perspectives with FIFA members in Delhi on 4th April 2014. And, the icing on the cake for participants were the thoughts and perspectives from two of the finest advisors in the country – Dhruv Mehta (Mumbai) and Ravi Kohli (Delhi).

FIFA Perspectives April 2014

Staying abreast with the latest technology solutions

FIFA members attended an Investment Platforms knowledge sharing session at Mumbai on 24th April 2014. It was organized by Asset Vantage Systems Pvt Ltd for FIFA. The platform, Asset Vantage, integrates investment and financial accounting and tracks real time portfolio performance. It is targeted to Family Offices as well as IFAs. It is a solution that an advisor can deploy at his/her own office or can recommend to their HNI customers to purchase. The company announced a referral program for FIFA members at the meeting.

FIFA Perspectives

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2 smart decisions and 2 not-so-smart ones

Abhenav Khettry, Vyana Wealth, Kolkata

Abhenav Khettry and his firm Vyana Wealth represent one of the best new success stories in the IFA space in recent times, picking up the 2013 Wealth Forum Emerging Advisor Award as testimony of his splendid efforts. But, even the best make mistakes and it takes tremendous courage to acknowledge mistakes, learn from them, and use these learnings to scale newer heights. We learn not only from the smart decisions of successful advisors, but also from the not-so-smart decisions they made, provided they are willing to candidly share these for everybody's benefit. It is a tribute to this young advisor's maturity that he readily agreed to share his perspectives on a tough question we posed him.

We asked him to look back at the 5 great years of Vyana Wealth and share with us 2 smart decisions that he took upfront, which have powered his success and 2 not-so-smart decisions that he would gladly reverse, if only he could go back in time. Here are his 2 hits and 2 misses. And, in the misses, lie very valuable lessons for young entrepreneurs who are embarking on a journey that Abhenav set out on, 5 years ago.

Its been five years since I set up Vyana Wealth. When I started out on this journey, I was just 22 years old. Short on experience, but high on ambition and ideas. I have been asked to share my thoughts on what, with the benefit of hindsight would I have done differently, if I were to set up Vyana all over again and what are the things I would have done just the same.

2 Hits

Let me discuss what I think we did right - the things I would not change at all, if I were to set up Vyana Wealth all over again.

1. Brand

From the beginning, I was clear that I need to create a brand for my firm that would be different and over time much larger than my individual name. I did not want to set up Abhenav Khettry & Co, and forever restrict the scope of the business to what I can do individually. From day 1, we set up a brand called Vyana Wealth, and we invested smartly in promoting the brand and making it relevant in our target client segment. Every form of client communication or interface was with Vyana Wealth, and that focus continues today. We have, in these 5 years, created some recall for our brand, and that helps drive the retail side of our business significantly. The decision to create a brand from day 1 has helped significantly, though I must say that it does involve upfront capital spending as you don't have any revenues in the early days from which you can pay for branding.

2. Technology

The other decision that I took early on, which has really helped, is to invest in technology from day 1. We bought the InvestWell software, we enabled clients to get web access to their portfolios and most importantly, we were able to service all client queries speedily and effectively as we did not have to go to AMCs for every piece of information. Quick and efficient service helped build client comfort, which strengthened our business considerably. I think for a business like ours which is so service intensive, you have no choice but to invest in appropriate technology that helps you serve clients the way they want to be served. Again, this was a decision that required some spending upfront, when revenues were scarce, but the positive impact on business was immense.

2 misses

The two things I think I didn't do well enough - the things I would change if I were to go back in time and set up Vyana Wealth all over again are both people oriented experiences.

1. Team

I have realized through experience that it pays to attract good quality talent, even if this talent is a little expensive. I have experienced hiring a team that I thought was very cost-effective, in my early days. It cost me less, but was certainly not cost-effective. When you hire sub-optimal people, they become a big drag on your personal time, which you would rather focus on growing your business. There were so many occasions where I had to step in to do things myself, as I did not want my clients to get anything less than the best quality service. Spending that time in doing stuff yourself because you want to hire lower cost staff is penny-wise, pound-foolish thinking. I re-organised my team after some of these experiences and realized the value to having a great team work with you and serve your clients, even if it means paying a little more than your comfort zone.

2. Partners

Perhaps the biggest mistake I made when I started out is to enter into a partnership with a "sleeping partner", without analyzing the pros and cons properly. In the beginning, when you start out and capital is scarce, a financing partner seems like a welcome idea. You don't have to pay interest from the first quarter, you can use the money to invest in technology, invest in your brand. But, what I didn't see clearly enough is that parting with equity to a financier seems like a good idea only in the initial period. Once you establish your business, once your income stream stabilizes and grows - entirely through your own efforts, the incremental value that your investor / sleeping partner brings in is nothing. But, you are making higher and higher payouts as share of profits year after year. I have only recently concluded a separation from this arrangement, where I have had to buy back the equity from my sleeping partner at a significant valuation premium. I have, in a sense, paid somebody else for my efforts and my worth! Nevertheless, from a long term point of view, I guess its better that this buy back happened now than 5 years later.

For anybody who is starting out now, my simple advice would be don't jump at a financing option that looks convenient in the short term. This is not a very capital intensive business and you can actually even do simple things like taking a personal loan or a business loan to get yourself started. Hard work over the first couple of years will enable you to pay off these loans - but your company will still be entirely yours. Look for a partner only when you think the partner will add lasting value to your firm - either through business development or by running a part of the firm that he or she is better equipped to do. A sleeping partner or an investor is not a good idea. Its best to have confidence in oneself and move ahead, rather than jumping at an option of "easy finance" which ultimately proves very costly.

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FIFA welcomes its new members

Type of Membership	Organisation	Name	ARN No	City
Founder	V.P. MITTAL	V SERVE MANAGEMENT PVT. LTD.	49091	NEW DELHI
Founder	PALLAV BAGARIA	BRAND NEW DAY	30378	GUWAHATI
Ordinary	QUANTUM LEAP INVESTMENTS	KANIKA ABBOTT	82210	NEW DELHI
Ordinary	ASSEST ALLIANCE SECURITIES PRIVATE LTD.	P J SUBBA RAO	28323	MUMBAI
Ordinary	RAJIV SURI	RAJIV SURI	2238	NEW DELHI
Ordinary	HUM FAUJI INITIATIVES	SANJEEV GOVILA	80765	NEW DELHI
Ordinary	MANMOHAN TIWARI	MANMOHAN TIWARI	92871	HARYANA
Ordinary	MAYA CAPITAL ADVISORS PRIVATE LIMITED	SHIV KHAZANCHI	92459	NEW DELHI
		REENA SETHI SHARMA		
Ordinary	DEEPAK KHEMANI	DEEPAK KHEMANI	7707	MUMBAI