NSDL
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Celebrating 20 Years

The Financial Kaleidoscope

Defining the different shapes of investment

June 2017

From The Editor's Desk

Dear Reader,

One proven way to spread risk comfortably throughout your portfolio, is to make sure you sufficiently diversify your investments. Diversification is the practice of spreading your investments in different asset classes so that your exposure to any one type of asset is limited. This practice is designed to help reduce the volatility of your portfolio over time.

Imagine you had put 100% of your savings in the stock market in 2007. In that case you would have suffered a huge loss in the next 2 years in 2008-09, giving you enough reason to worry. One of the keys to successful investing is learning how to balance your comfort level with risk against your time horizon. Invest your retirement nest egg too conservatively at a young age, and you run the risk that the growth rate of your investments won't keep pace with inflation. Conversely, if you invest too aggressively when you're older, you could leave your savings exposed to market volatility, which could erode the value of your assets at an age when you have fewer opportunities to recoup your losses.

One way to balance risk and reward in your investment portfolio is to diversify your assets. The strategy of diversification is simply about spreading your portfolio across several asset classes like equities, debt, cash, real estate, gold, etc. Even within these asset classes, investments can be further diversified based on sectors, geographies, and other factors. This helps you to mitigate the risk and volatility in your portfolio, potentially reducing the number and severity of stomach-churning ups and downs. Remember, diversification does not ensure a profit or guarantee against loss. The primary goal of diversification isn't to maximize returns. Its primary goal is to limit the impact of volatility on a portfolio.

In this issue of Kaleidoscope, we will understand what a portfolio diversification really means from an investor's perspective, the importance of portfolio diversification, the various asset classes available for an investor to invest & diversify his/her portfolio investments and so on. It will certainly help in building a good risk-adjusted return in your portfolio investment.

Best Regards,

NSDL

Click & Find: Investment Portfolio

What is a 'Portfolio'?

Let's understand what a Portfolio is all about. A portfolio is a grouping of financial assets such as stocks, bonds and cash equivalents, as well as their funds counterparts, including mutual funds, exchange-traded and closed funds. Portfolios are held directly by investors and/or managed by financial professionals. Prudence suggests that investors should construct an investment portfolio in accordance with risk tolerance and investing objectives.

An investment portfolio can be thought of as a pie that is divided into pieces of varying sizes, representing a variety of asset classes and/or types of investments to accomplish an appropriate risk-return portfolio allocation. Many different types of securities can be used to build a diversified portfolio, but stocks, bonds and cash are generally considered a portfolio's core building blocks. Other potential asset classes include, but aren't limited to, real estate, gold and currency.

Impact of Risk Tolerance on Portfolio Allocations

While a financial advisor can develop a generic portfolio model for an individual, an investor's risk tolerance should have a significant impact on what a portfolio looks like. For example, a conservative investor might prefer a portfolio with large-cap value stocks, broad-based market index funds, investment-grade bonds, and a position in liquid, high-grade cash equivalents. In contrast, a risk-tolerant investor might add some small-cap growth stocks to an aggressive, large-cap growth stock position, some high-yield bond exposure, and look to real estate and alternative investment opportunities for his portfolio. In general, an investor should minimize exposure to securities or asset classes whose volatility makes him uncomfortable.

Impact of Time Horizon on Portfolio Allocations

Similar to risk tolerance, investors should consider how long they have to invest when building a portfolio. Investors should be moving to a pattern for asset allocation depending the age & risk appetite. For example, an investor saving for retirement may be planning to leave the workforce in five years. Despite the investor's comfort level investing in stocks and other risky securities, he may want to invest a larger portion of the portfolio's balance in more conservative assets such as bonds and cash, to help protect what has already been saved. Conversely, an individual just entering the workforce may want to invest his entire portfolio in stocks, since he may have decades to invest, and has the ability to ride out some of the market's short-term volatility. Both risk tolerance and time horizon should be considered when choosing investments to fill out a portfolio.

Get Started – Portfolio Investment

A portfolio investment is a hands-off or passive investment of securities in a portfolio, and it is made with the expectation of earning a return. This expected return is directly correlated with the investment's expected risk. Portfolio investment is distinct from direct investment, which involves taking a sizable stake in a target company and possibly being involved with its day-to-day management.

Portfolio investments can span a wide range of asset classes such as stocks, government bonds, corporate bonds, Treasury bills, Real Estate Investment Trusts (REITs), Exchange-Traded Funds (ETFs), mutual funds and certificates of deposit. Portfolio investments can also include options, derivatives such as warrants and futures, and physical investments such as commodities, real estate etc.

The composition of investments in a portfolio depends on a number of factors. Some of the most important factors include the investor's risk tolerance, investment horizon and amount invested. For a young investor with limited funds, mutual funds or exchange-traded funds may be appropriate portfolio investments. For a high net worth individual, portfolio investments may include stocks, bonds, commodities and rental properties. Portfolio investments for the largest institutional investors such as pension funds and sovereign funds include a significant proportion of infrastructure assets like bridges and toll roads. Portfolio investments for institutional investors generally need to have very long lives so that the duration of their assets and liabilities match. These risk preferences should also be weighed against the investor's goals and time horizon.

Asset Allocation

Now, let's have a look into the detailing of asset allocation. There is no simple formula that can find the right asset allocation for every individual. However, the consensus among most financial professionals is that asset allocation is one of the most important decisions that investors make. In other words, the selection of individual securities is secondary to the way that assets are allocated in stocks, bonds, cash and equivalents, which will be the principal determinants of your investment results.

Investors may use different asset allocations for different objectives. Someone who is saving for a new car in the next year, for example, might invest his/her car savings fund in a very conservative mix of cash, Certificates of Deposit (CDs) and short-term bonds. Another individual saving for retirement that may be decades away typically invests the majority of his investment in stocks, since he has a lot of time to ride out the market's short-term fluctuations. Risk tolerance plays a key factor as well. Someone not comfortable investing in stocks may put their money in a more conservative allocation like FDs, PPF etc. despite a long time horizon.

Age-based Asset Allocation

In general, stocks are recommended for holding periods of five years or longer. Cash and money market accounts are appropriate for objectives less than a year away. Bonds fall somewhere in between. In the past, financial advisors have recommended subtracting an

investor's age from 100 to determine how much should be invested in stocks. For example, a 40-year old would be 60% invested in stocks. Variations of the rule recommend subtracting age from 110 or 120 given that the average life expectancy continues to grow. As individuals approach retirement age, portfolios should generally move to a more conservative asset allocation so as to help protect assets that have already been accumulated.

Asset allocation through mutual funds helps diversify your investments across various sectors & provide investors with portfolio structures that address an investor's age, risk appetite and investment objectives with an appropriate apportionment of asset classes. However, while arriving at a standardized solution for allocating portfolio assets is not suitable because every individual investor requires individual solutions as per their needs & investments available with them.

Portfolio Management

Portfolio management helps in making decisions about investment mix and policy, matching investments to objectives, asset allocation for individuals and institutions, and balancing risk against performance. Portfolio management is all about determining strengths, weaknesses, opportunities and threats in the choice of debt vs. equity, domestic vs. international, growth vs. safety, and many other trade-offs encountered in the attempt to maximize return at a given appetite for risk.

In the case of mutual and Exchange-Traded Funds (ETFs), there are two forms of portfolio management: passive and active. Passive management simply tracks a market index, commonly referred to as indexing or index investing. Active management involves a single manager, co-managers or a team of managers who attempt to beat the market return by actively managing a fund's portfolio through investment decisions based on research and decisions on individual holdings.

Understanding Financial Lingo

Asset Allocation:

The process of determining the optimal division of an investor's portfolio among different assets. Most frequently this refers to allocations between debt, equity, and cash.

Asset Allocation Fund:

A mutual fund that splits its investment assets among stocks, bonds, and other vehicles in an attempt to provide a consistent return for the investor.

Bond:

A negotiable certificate evidencing indebtedness - a debt security or IOU, issued by a company, government agency. A bond investor lends money to the issuer and, in exchange, the issuer promises to repay the loan amount on a specified maturity date. The issuer usually pays the bondholder periodic interest payments over the life of the loan.

Certificates of Deposit (CDs):

A negotiable certificate issued by a bank, usually for a period of one month to a year, as evidence of an interest bearing time deposit. This may also be offered at a discount.

Commercial Paper (CP):

A short term promise to repay a fixed amount that is placed on the market either directly or through a specialized intermediary. It is usually issued by companies with a high credit standing in form of a promissory note redeemable at par to the holder on maturity and therefore does not require any guarantee.

Common stock:

Common stocks are units of ownership of a public corporation. Holders of common stock typically have voting rights and receive dividends, but there is no guarantee of dividend payment.

Exchange Traded Funds (ETFs):

A security that tracks an index but has the flexibility of trading like a stock.

Adviser:

A financial planner or financial intermediary who offers advice on personal financial matters. Advisers may be paid an upfront or an ongoing commission for the investments that they recommend.

Auction Market:

An auction market is a market in which buyers enter competitive bids, and sellers enter competitive offers at the same time. The price at which a stock is traded represents the highest price that a buyer is willing to pay and the lowest price that a seller is willing to sell.

Beta:

A measure of the volatility of a stock relative to the market index in which the stock is included. A low beta indicates relatively low risk; a high beta indicates a high risk.

The Importance of Investment Portfolio Diversification

One proven way to spread risk throughout your portfolio, is to make sure you sufficiently diversify your investments. Investment portfolio diversification is a tried and tested technique that involves reducing risk by spreading investments across a varying range of companies, sectors, geographical locations and assets. Obviously, diversifying your investments is not an absolute buffer against financial losses. However, it remains a vital strategy for minimising risk that often helps investors to achieve their financial goals.

An investment portfolio containing investments with little or no relation to each other, also known as low correlation, is in less danger of being heavily impacted upon by negative value fluctuations in any one company, sector, country or asset. Diversifying your investment portfolio often enables falls in the value of one investment to be cushioned by rises in the value of another unrelated investment.

Here are the key ways you can diversify your investment portfolio

Diversify Your Company Investments

It's obviously common sense not to invest all your money into a single company. Little is certain in the current economic climate and even the most prosperous of companies can suffer a fall in value or even fold. Always spread your investments across a number of companies and consider investing in companies that operate in different market sectors. It's vital to conduct thorough research into any company you are interested in investing and to seek the advice of an independent financial advisor prior to making a final decision.

Diversify Your Sector Investments

Investing in a range of different sectors brings the same advantages as investing in different companies. In the current economic climate there have been peaks and troughs in a wide range of sectors. To provide a cushion with your investment portfolio against your entire portfolio losing value, spread your investments across sectors with low correlation. For example, if your investment in a company within the IT sector suddenly experiences a dip in value, a rise in your gold investment could compensate for it.

Diversify Your Assets

It's wise to have a good mix of varying asset types within your investment portfolio, as it spreads risk. There are many different types of assets, the primary types being shares and bonds, which often have a low correlation to each other. Discuss with your independent financial advisor the best way to mix the asset types within your investment portfolio. They will have the market knowledge required to spread the risk throughout your portfolio. You should decide the level of risk you are willing to take according to your financial goals. Are you near the time you want to draw upon your invested money? Then go for lesser risks. If you are planning a long term investment strategy, you may feel inclined to take greater risks. Remember to work with your financial advisor to create a portfolio tailored to your personal financial goals.

Avoid Over Diversification

While diversification can protect your investment portfolio from value fluctuations in correlated investments, over diversification can lead to you not having enough invested money in a company or sector to truly benefit from any growth. Again, it's a case of planning your investment portfolio carefully with your financial advisor and striking the right balance.

Take advantage of different investment styles

Another popular way to diversify your portfolio is by investment style. There are a number of investments styles, but the two most popular are value and growth.

A value manager tends to consider, among other things, the fundamental strength of a company and its management team, and whether that company's stock price is undervalued based on estimates of its true worth. A growth manager doesn't necessarily take into consideration the price of the company's stock. Instead, it considers how fast the company has been growing and whether new products or other competitive advantages should accelerate earnings in the future, which would likely benefit the stock price.

Different investment styles tend to perform differently at certain points in an economic cycle. Therefore, having a portfolio that includes different investment styles can help smooth out your returns over the long term. Your financial advisor can help you diversify your portfolio by choosing the right mix of investments to reach your long-term investment goals.

Conclusion

Diversification can help an investor manage risk and reduce the volatility of an asset's price movements. Remember though, that no matter how diversified your portfolio is, risk can never be eliminated completely.

You can reduce risk associated with individual stocks, but general market risks affect nearly every stock, so it is also important to diversify among different asset classes. The key is to find a balance between risk and return; this ensures that you achieve your financial goals while still getting a good night's rest.

1. **How is Asset Allocation different from Diversifying?**

   Asset allocation and diversification rely on the same principle of protecting your assets by distributing them among a wide enough variety of investments. So how do they differ? Asset allocation refers to investing in different asset classes – stocks, bonds, cash, precious metals etc. Diversification has to do with spreading your money out within a category, such as the number of different stock positions you own or the variety of industries you invest in instead of investing in a single stock or just one industry.

2. **What's the Best Asset Allocation Model?**

   The best asset allocation model will vary from one investor to another, depending on their financial goals, and risk tolerance. Determining the appropriate asset allocation model for your financial goals is a complicated task. An investor may want to consider the use of an independent, certified financial planner to assist him/her. There are also a vast array of investment products that facilitate asset allocation in mutual funds and perhaps other asset classes. Basically, an investor trying to select a mix of asset categories should decide what percentage of their investment assets they will allocate for each category. An investor will also want an asset allocation that has the highest probability of meeting their goals at a level of risk they can bear.

3. **Why should I invest in stocks, mutual funds or bonds?**

   Time and again it has been proved that shares/equities are one of the best long-term investments. Investing in stock market provides an opportunity to make money. Investors will be able to reap profits by investing in stable companies that are able to grow. Similarly, by investing in different stocks, an investor will be able to increase the wealth by leveraging growth in various sectors. Moreover, some stocks do provide extra income in the form of dividends, which can be used for further investing or for other financial needs.

   Mutual funds can be tax-efficient investment avenues that can help reduce your tax burden and at the same time increase your wealth. ELSS – An Ideal Tax-saving Instrument - Equity Linked Savings Schemes (ELSS) offers an easy option to obtain tax benefits and an opportunity to harness the potential upside of investing in the equity market.

   Bonds are considered safer investments than stocks. Tax-saving infrastructure bonds are a good option in the fixed income category. These are issued by infrastructure companies approved by the government and they offer a decent rate of interest plus tax benefits.

4. **What is Portfolio Management Services (PMS)?**

   Portfolio Management Services (PMS) is an investment portfolio in stocks, fixed income, debt, cash, structured products and other individual securities, managed by a professional money manager that can potentially be tailored to meet specific investment objectives. When you invest in PMS, you own individual securities unlike a mutual fund investor, who owns units of the entire fund. You have the freedom and flexibility to tailor your portfolio to address personal preferences and financial goals. Although portfolio managers may oversee hundreds of portfolios, your account will be unique.

5. **What are the benefits of availing Portfolio Management Services (PMS)?**

   There are many benefits of availing Portfolio Management Services. Some of them are:

   - **Professional Management:** PMS provides professional management of portfolios with the objective of delivering consistent long-term performance while controlling risk.
   - **Constant Portfolio Tracking:** PMS helps the investor in maximizing the returns since they continuously track their investments in a better way.
   - **Risk Control:** Well defined investment philosophy & strategy acts as a guiding principle in defining the investment universe. Most of the PMS provide investors with their robust portfolio management software that enables the entire construction, monitoring and the risk management processes.
   - **Convenience:** PMS relieves all the administrative hassles of an investor's investment. They provide periodic reports on the performance and other aspects of your investments.
   - **Dedicated Relationship Manager:** Most PMS offer dedicated relationship managers that help an investor to carefully understand their financial goals and advise them about the right product mix. The relationship managers ensure that an investor receives periodic updates and account performance reports.
   - **Personalized Approach:** Most PMS offer direct personalized access to their professional money managers who actively manage an investor's portfolio. This interaction may come in various different ways including in-person meetings, conference calls, written commentary, etc. with the fund management team.

SMS Alert facility enhanced – SMS Alerts to Clients upon Pledge instruction initiation/confirmation

SMS Alert facility provides important updates to Clients on their mobile phones about some of the activities in their depository accounts, which facilitates risk mitigation and provides value added services. Clients and Participants have widely appreciated this facility.

With effect from May 20, 2017, NSDL has enhanced its SMS Alert facility whereby Pledgor Client will receive SMS alerts upon initiation and confirmation of securities pledged in their demat accounts. These SMS Alerts will be sent to the Clients on the same day when instructions for pledge initiation / confirmation are processed in respect of the pledgor demat account.

Sample text message of SMS Alerts is given below:

Pledge Initiation

On _____ (date, dd/mm/yy), Pledge initiation instruction for _____ (quantity) _____ (company name), has been submitted in respect of your demat a/c no. xxxx1234. NSDL.

Pledge Confirmation

On _____ (date, dd/mm/yy) Pledge initiation instruction for _____ (quantity) _____ (company name), has been confirmed in respect of your demat a/c no. xxxx1234. NSDL.

Demat account holders of NSDL will now receive SMS alerts directly from NSDL for following:

1. All Debit Transfers
2. Credits for IPO, sub-division and bonus
3. Failed instructions
4. Overdue instructions
5. Change of mobile number
6. Change of address
7. Debit of Mutual Fund units
8. Invocation of pledged securities
9. Registration and De-registration of Power of Attorney
10. Modification / Cancellation of nominee name
11. Pledge initiation and confirmation

No charge is levied by NSDL to Participants for providing this facility to investors.
Further details about this circular are posted on NSDL website www.nsdl.co.in.

(Ref: Circular No. NSDL/POLICY/2017/0029 dated May 17, 2017)

Activation of three Depository Participants (DPs) as Participants of NSDL

Following Depository Participants (DPs) have been admitted as Participants of NSDL and made operational during May 2017.

Sr. No.	Depository Participant (DP) Name	DP ID	Location
1	Indian Clearing Corporation Limited	IN001133 and IN001150	Mumbai, Maharashtra
2	Signatureglobal Securities Private Limited	IN304199	New Delhi
3	IDFC Bank Limited	IN304203	Mumbai, Maharashtra

This takes the total number of operational Participants to 265 and the total number of operational DPM set-ups to 350.

Subscription to *SPEED-e*

During May 2017, two more Participants have subscribed to the ***SPEED-e*** facility viz.,

- Astha Credit and Securities Private Limited (DP ID IN303420)
- IDFC Bank Limited (DP ID IN304203)

Clients of the above mentioned Participant can now avail the facility of submitting various instructions through ***SPEED-e*** facility.
This takes the total number of Participants who have subscribed to ***SPEED-e*** to 192.

Investor Education initiatives undertaken by NSDL

Investor Awareness Programmes:

In order to reach out to investors that are spread across the country and to apprise them about the facilities available in NSDL depository system and the awareness on stock markets, NSDL conducts various Investor Awareness Programmes jointly with it's Depository Participants (DPs) & with Institutions like SEBI, NSE etc. NSDL also conducts various training programmes for its Depository Participants (DPs) on Depository related services. During May 2017, NSDL conducted 19 Investor Awareness Programmes & events with Participants and Corporates. These programmes were attended by approx. 1,300 participants, details as mentioned below:

Sr. No.	Particulars	
1	**Joint Awareness Programmes with DPs**	**No. of Programmes**
	Jhaveri Securities Limited	3
	Acumen Capital Market (India) Limited	2
	Karvy Stock Broking Limited	2
	Arihant Capital Markets Limited	1
	CSE Capital Markets Private Limited	1
	DP TradeKING Private Limited	1
	Inditrade Capital Limited	1
	Kotak Securities Limited	1
	SBICAP Securities Limited	1
	Sharekhan Limited	1
	Total Programmes	**14**

2	**Corporate Awareness Programmes (CAPs)**	**No. of Programmes**
	Netcore Solutions	2
	Total Programmes	**2**

3	**Awareness Programmes on Capital Market for Institutions**	**No. of Programmes**
	IDBI Bank Limited	3
	Total Programmes	**3**

Blog

Portfolio Diversification

By Ms. Ishita Bhatt,
PTVA's Institute of Management

Portfolio diversification means investing in different asset classes and in shares of various companies in different sectors.Portfolio diversification helps reduce the overall investment risk even if some of the share prices of certain companies have drastically reduced over a period.

The rationale behind this technique is that a portfolio constructed of different kinds of investments such as equity, bonds, mutual funds etc. will, on an average, yield higher returns and pose a lower risk than any investment constructed in a particular asset in the portfolio. Studies and mathematical models have shown that maintaining a well-diversified portfolio of 25 to 30 stocks yields the most cost-effective level of risk reduction.

Some of the benefits of Portfolio Diversification are:

- **Risk Reduction:** An investor can't eliminate risk completely, but can manage the level of risk through portfolio diversification.
- **Capital Preservation:** Investing in a variety of assets reduces risk. An investor does not have to worry about the poor performance of companies. Portfolio diversification thus helps building a healthy portfolio for retirement.
- **Ability to Hedge Investors Portfolio:** Investors who have had 100% equity portfolio over the years would have likely had low returns due to the various economic policies affecting the price of some of the stocks. Diversification gives an investor the chance to achieve positive returns across his/her portfolio even if one of the asset class is generating negative returns during a particular period.

Read and Win!

What are the advantages of Portfolio Diversification ?

Send your replies providing your contact details (Name, address and contact no.) with the subject 'Knowledge Wins Contest - June 2017' to info@nsdl.co.in

KNOWLEDGE WINS Contest

Terms and Conditions

- NSDL shall be solely responsible for the execution and administration of this Contest.
- This Contest is only open to Indian Citizens. (NSDL employees are not allowed to participate in this contest.)
- All personal details submitted must be accurate and complete and are subject to proof upon request by NSDL.
- NSDL reserves the right, at any time, to verify the validity of entries and entrants and to disqualify any entry not submitted in accordance with these Terms or which tampers with the entry process.
- NSDL reserves the right to discontinue the contest at any given point of time without prior intimation.
- All prize drawings will made on a strictly random basis and the decision made by NSDL will be final

Lucky 25 Winners will Win Free Goodies

Your suggestions for newsletter are valuable to us. Send in your suggestions mentioning your contact details (contact name, address & contact number) with the subject "Suggestions for the newsletter" to info@nsdl.co.in

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