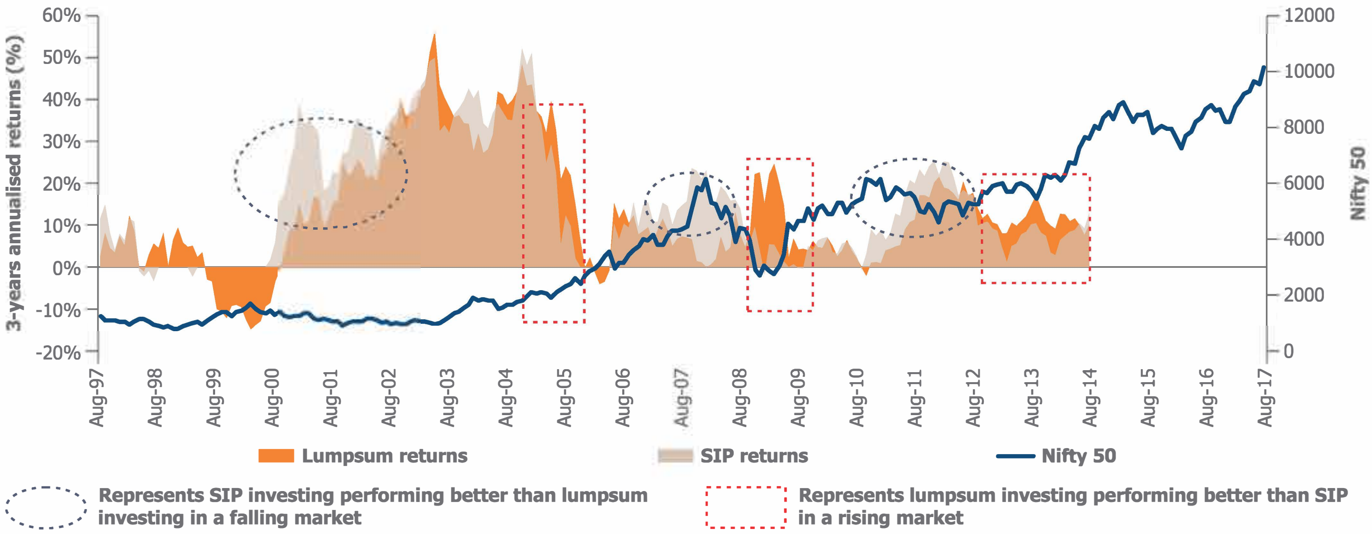
Mirae Asset Knowledge Academy
Profit from Knowledge

Get smart with Variable Transfer Plan

Most investors look at investment whenever they have lump sum amount of money in their hands, however in case of investments in equity, this may go awry especially at times when markets are trending at record highs like currently. This is because, analysis shows that lump sum investment benefits investors primarily during market uptrend, but fail to beat Systematic Investment Plans (SIPs) during market volatility (see Chart 1). Investors with lump sum money in hand can look at parking their money in debt funds (primarily liquid funds), and transferring money on a regular basis through Systematic Transfer Plan (STP) into equity oriented funds, to mitigate risks of timing in equity. Another smart variant of STP is called as Variable Transfer Plan (VTP), which tries and derives more benefit for investors during market downturns. Read on to find out more.

Chart 1: Lump sum versus SIP returns in Nifty 50



The graph shows how lumpsum and SIP investing would have returned for a three-year horizon had investor invested in the Nifty 50 at any point of time in the past 20 years

VTP scores over STP in averaging the cost

Systematic Transfer Plan (STP) enables Unit Holders to transfer fixed sums from their Unit accounts in the Scheme to the existing schemes or other schemes launched by the Fund from time to time. VTP is almost similar to STP; the only difference is the amount transferred is not fixed. In VTP, investor needs to invest lump sum in a source fund (usually a debt fund) and then transfer the variable amount regularly in a target fund (usually an equity fund). With the help of an in-built flexible process, the amount to be transferred changes as per the market movement, i.e. whenever the market rises, it transfers the stipulated minimum amount and whenever the market falls, a higher amount is transferred to an equity fund. Effectively, investor reduces the average cost of purchase compared with a normal STP mandate.

Formula of VTP is as follow

(Fixed amount of VTP as mentioned in the plan **X** **No. of installments including current)** **-** **(Market value of investment made in target scheme)**	**OR**	**Fixed amount of VTP as mentioned in the plan**

Whichever is higher

Based on the modus operandi of VTP, as explained, let us assume minimum stipulated investment to be transferred from a source to a target fund is ₹ 1,000. At the first installment, an investor will get 100 units assuming net asset value (NAV) of ₹ 10. At the second installment, if NAV falls to, say, ₹ 8, the transferable amount will be ₹ 1,200. Based on auto calculation, an investor would be able to invest higher when the market falls and buy more units at a lower price, effectively reducing the average cost price without even looking at market trends.

Calculation of VTP installment when market fall

Fixed stipulated amount X no. of installment (A)	Market value of investment made till date (B)	(A – B)	Fixed stipulated amount (C)	Which is higher (A-B) or C
₹ 1000 X 2 = ₹ 2000	₹ 8 X 100 units = ₹ 800	₹ 1200	₹ 1000	₹ 1200

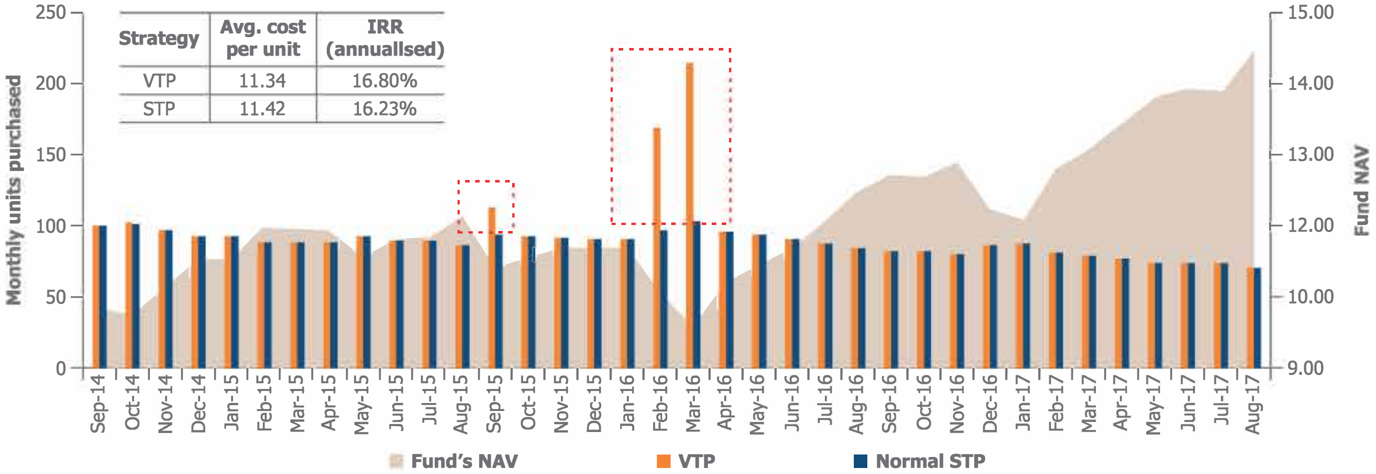
For illustration purpose only

Case study to corroborate VTP is a good investment strategy

Let us assume investors A and B earmarked ₹ 50,000 to invest in an equity fund in September 2014. Instead of investing lump sum, they decided on regular monthly investments.

- Investor A invested a lump sum in a liquid fund & opted for VTP in an equity fund with a minimum transfer of ₹ 1,000.
- Investor B, on the other hand, chose the STP option of ₹ 1000 from liquid to equity fund.

Chart 2: VTP versus regular STP



Fund's NAV is based on CRISIL-AMFI Equity Mutual Fund Performance Index. IRR pertains to investments in equity fund.
Assuming VTP/STP date is first day of the month

Similar to investor B, who transferred ₹ 1,000 per month in an equity fund, investor A transferred ₹ 1,000 per month plus an additional amount whenever the market declined. Resultantly, investor A was able to buy more units (as highlighted by the square portion in the above graph) when the market declined.

VTP helped investor A to average down the cost per unit & he earned higher returns than investor B, who chose normal STP investing.

In a nutshell

There is no crystal ball to predict market movement. The mantra should be to invest regularly. A tactical strategy such as VTP will help investors to not only be disciplined but also be able to buy more during a downturn without actually following a market trend. On a cautious note, in VTP, whenever there is a sharp fall in NAV, the amount to be transferred can increase sharply and, hence, one should ensure the source fund has enough amount to avoid a shortfall.

Source: CRISIL research date as on 15th August 2017.

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