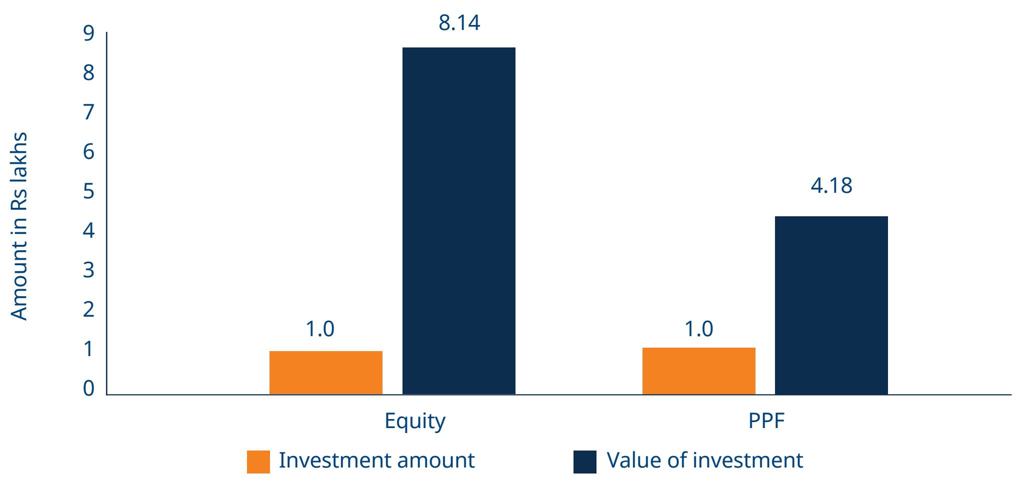
SAVE TAX AND SEEK TO CREATE WEALTH

Indians have historically favoured traditional fixed income instruments for their investments (normal as well as tax savings). This, however, does not marry well in terms of prudent financial planning, especially since the country has one of the largest young population in the world. Indeed, the median age of India's population is far below those of the most comparable economies as well as the world, which means most Indians have a long vesting period of investment.

To be sure, fixed income investments protect capital and potentially give stable returns, however, risky investment asset classes such as equity aim to give an edge to returns over the long term.

Equity as an asset class, as represented by the market benchmark S&P BSE Sensex, has returned 15% CAGR on average for a 15-year holding period since its inception (1979), compared with just ~ 10% for the Public Provident Fund (PPF). In terms of actual money growth, based on the average return numbers, an investment of Rs 1 lakh would have grown to Rs 8.14 lakh in equity investments versus just half of that at Rs 4.18 lakh in PPF.

Chart 1 : Higher wealth creation capability



Source: BSE, Department of economic affairs

Table 1 - ELSS one of the good options amongst tax-saving options which aim to grow wealth over the long term

Characteristics	ELSS	ULIP	PPF	NSC	Tax-saving FDS
Returns	Linked to equity market returns	Market-linked, based on investment chosen (equity / debt)	7.9%*, compounded annually	7.9%*, compounded half-yearly	6.85%^
Lock-in period/tenure	Full amount can be withdrawn after 3 years from date of allotment	Lock-in period of 5 years; no surrender charges after 5 years	Lock-in period of 15 years; partial withdrawal permitted after 6 years	Lock-in period of five years; no withdrawal prior to maturity, but investments can be used as collateral to avail loans from banks	Premature exits permitted, subject to applicable charges
Tax treatment	Gains of more than Rs 1 lakh from ELSS is subjected to long term capital gains tax (LTCG) of 10% without indexation	Tax-free after the minimum lock-in period of 5 years (tax-free in the event of death of policy holder)	Tax exempt at contribution, accumulation and withdrawal	Interest income taxed at income tax slabs	Interest income taxed at income tax slabs

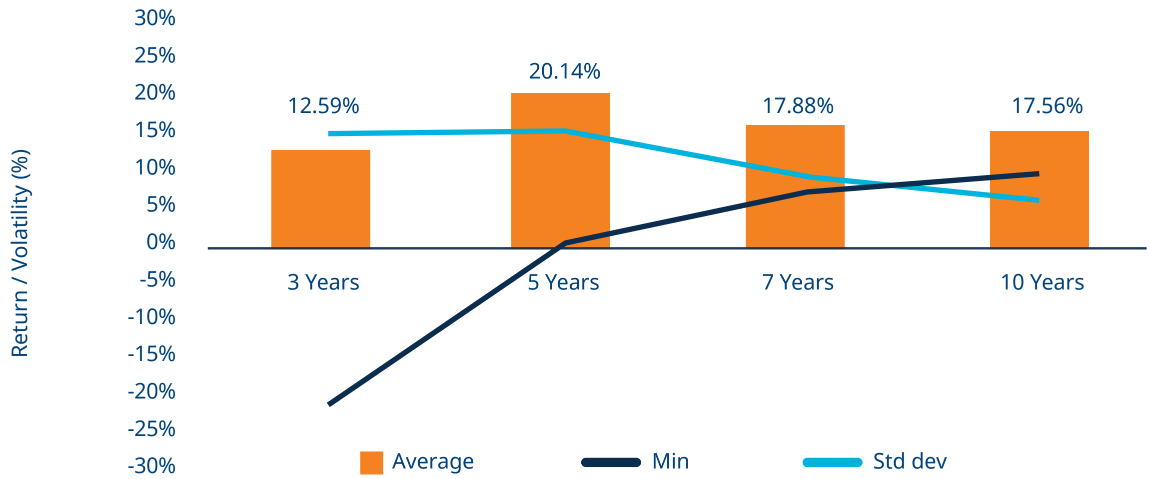
*Rate notified for Q4, fiscal year 2019-20. ^SBI term deposit rate for 5 year as at January 2020. The comparison with PPF, FD and other traditional instruments has been given for the purpose of the general information only. Investments in mutual funds should not be construed as a promise, guarantee on or a forecast of any minimum returns. PPF/NSC/FDs are comparatively low risk products. Investment in mutual funds carries high risk as compared to the traditional instruments and any investment decision needs to be taken only after consulting the Tax Consultant or Financial Advisor.

Source: CRISIL Research, 31st December 2019.

Invest for the long term

ELSS funds allow investors to augment the power of equity via tax savings. However, to achieve optimal benefits, the investment should be for a long duration. This not only reduces the volatility associated with the asset class but also provides an optimum return solution for investors. The ELSS category has returned ~18% CAGR on average in the 10-year rolling period since June 2001 (inception date of the index).

Chart 2 : Higher investment period optimises value proposition of ELSS funds



Source notes: ELSS data represented by a weighted index created out of CRISIL ranked ELSS funds; volatility represented by standard deviation returns are annualised calculated on a daily rolling basis since June 2001 till December 31, 2019. Past performance may or may not sustain in future. The above is performance of the category and does not in any manner indicate performance of any scheme of the Fund

Invest systematically and seek to achieve financial goals throughout life

The prime purpose of investing in ELSS is to reduce the tax outgo. But the corpus generated out of a prudent ELSS investment can also be used to fulfil key financial goals. Investors can synchronise their ELSS investments to attain goals throughout their life, such as building a retirement kitty, saving for children's education, repayment of housing loan or planning for a second home. These investments can be done regularly throughout the year instead of at one point in the year (mostly year-end).

This leads to well-thought-out monetary outflows after evaluating different investment options. Last-minute action often results in short savings or no investments at all, thus increasing the investor's tax outflow.

Distribution of outflows across a time period is easier on the wallet as well. Regular investments reduce the risk of timing the market (rupee cost averaging) while helping generate optimum returns from the asset class in the long term. This can be done by opting for Systematic Investment Plan (SIP) or Systematic Transfer Plan (STP).

SIP allows an investor to deploy money in smaller lots at regular intervals. If an investor has lump sum amount at any point of time during the year, he/she can deploy that money in liquid funds and transfer a fixed amount via STP to the ELSS scheme at regular intervals.

Table 2 : Aim to reach your goals in life via ELSS

Investor	A	B	C
Goal	Child's education	Repayment of home loan	Retirement
Goal amount	Rs 5 lakh	Rs 12 lakh	Rs 33 lakh
Investment horizon (years)	5	7	10
~Monthly SIP investment needed	Rs 5,000	Rs 7,000	Rs 10,000

For representation purpose only
Source: CRISIL Research
Rate of return assumed – 20.14%, 17.88% and 17.56% are the 5-, 7- and 10-year average rolling returns of ELSS funds computed in the above analysis

Added advantages to investors

In addition to harnessing equity in investments, ELSS provides investors with more advantages.

Professional Management

Professional fund managers, backed by research, to invest your money in the capital markets

Tax Benefit

Investors can save up to Rs 46,800* annually by investing in the product for 3-year lock-in period

Affordability

Affordable investing through SIPs at as low as Rs 500, which also adds discipline and reduces volatility to the investment pattern

Diversification

Invests across market caps (large, mid, small) and sectors, thus ensuring a diversified portfolio

* Investors in the highest tax bracket, excluding cess in the old tax regime

Need to identify top performer – short-term versus long-term approach

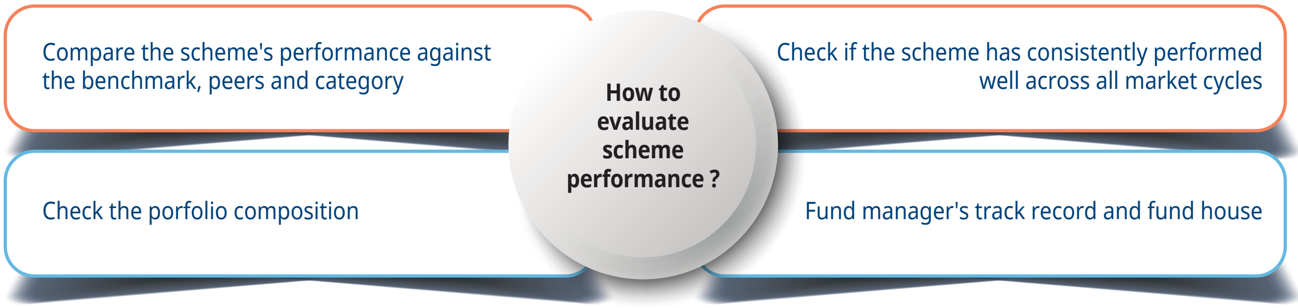
While the probability of negative returns can be reduced by increasing the time horizon, it is pertinent for investors to identify quality schemes to generate wealth.

Most investors prefer the short-term approach of scheme selection for ELSS, which typically involves selecting the top performer in a category in the past year. This, however, defeats the approach of selecting a scheme based on quality.

The short-term approach also encourages investors to add multiple schemes to the portfolio, which only adds to the clutter and the hassle of managing many schemes.

So, what is the solution?

Ideally, one should invest in one or two schemes in the category based on the long-term and thought through process of selection. A 360-degree approach, which is a mix of personal and scheme related factors, will help investors choose the most appropriate fund. Personal factors include analysis of investor's goals, risk appetite and returns expectations. Here are some steps to check a scheme's performance:



Performance – Investors must look at the consistency of performance rather than short-term returns. Consistency does not mean a fund should be a top performer all the time, rather it should consistently fare better than its peers and the benchmark across market phases. Consistent funds will tend to give higher risk-adjusted returns vis-à-vis their peers and the benchmark. To gauge consistency in a fund's performance, investors can use quartile rankings along with various other performance parameters such as analysis based on rolling returns and market-phase performance. Consistent funds may fall short sporadically, but, in the long term, they are likely to outperform their peers and the benchmark.

Volatility - Volatility can be gauged by ratios such as beta or standard deviation. Higher volatility is an indication of higher uncertainty in a fund's returns. Choose funds that have delivered better risk adjusted returns.

Portfolio analysis - Among the scheme related factors, investors need to look beyond historical performance and check parameters such as portfolio composition (sector and stock holding), market capitalisation allocation, expense ratio, and liquidity.

Fund manager's track record - The fate of the fund is also governed by the decisions taken by the fund manager. Evaluate his/her track record. Carefully analyse the manager's investment style, professional credentials and the number of schemes managed by him/her before investing in a scheme. Often, good fund managers have a steady track record of beating the benchmark index across market cycles. Investors should also check the size of the fund house. In addition, they need to look at the fund's asset size, quality and independence of in-house research, operational efficiency, the quality of services provided by the fund house, and adequacy and effectiveness of its risk management strategies.

Investors can evaluate these parameters by looking at the fund factsheet and scheme-related documents such as Scheme Information Document and Statement of Additional Information. Investors should also consult their financial advisors before investing.

Summing up

Typically, most of us slot tax saving and planning for the last fiscal quarter (January-March). Is this ideal? Evidently no, because: 1) Last minute investments can be indiscriminate, oblivious to one's own risk-return profile and long-term investment objectives, and 2) One may not have sufficient funds to invest at that time, resulting in higher tax outflows.

Tax planning should ideally be a disciplined and planned activity. If you cannot have year-round investments, then ensure your tax planning is done earlier in the year. The earlier this is done, the better it is.

Investors should, however, understand that ELSS is market linked and does not offer guaranteed returns such as the vanilla fixed income tax-saving instruments. Hence, an investor should only invest after considering his/her risk profile and conducting proper due diligence.

Further, the proceeds from ELSS are subject to a 10% long-term capital gains tax. Investors should consider this factor although over the long term, the impact would be minimal on overall returns.

Finally, like with all equity investments, the best way to invest in ELSS funds is through an SIP throughout the year.

An investor education initiative by Mirae Asset Mutual Fund

All Mutual Fund investors have to go through a one-time KYC (Know Your Customer) process. Investors should deal only with Registered Mutual Funds (RMF). For further information on KYC, RMFs and procedure to lodge a complaint in case of any grievance, you may refer the Knowledge Center section available on the website of Mirae Asset Mutual Fund.

Mutual Fund investments are subject to market risks, read all scheme related documents carefully.