VIEW AND COUNTERVIEW

MARKET RETURNS: IS DIRECT INVESTING THE BEST APPROACH?

For decades, investors put their money directly into the market. A traditional investor swears by buying shares directly for their returns! Many have made humongous returns from investing directly in shares that turned out to be 'multi baggers' while some lost all they had.

For the new investors, the busy lot or even the risk averse, there are several options of investing indirectly through mutual fund and other schemes. This option offers a reasonable risk- return profile. Indirect investing has allowed a large number of citizens to participate in corporate growth stories and make a decent return over the long term.

This fifth VIEW and COUNTERVIEW aims to tell the story from both perspectives. Both writers, connected to their respective areas for years, give two perspectives for you to consider. Deven R. Choksey, an entrepreneur in the business of shares and securities and a leading voice for the markets in media, shares his views from his more than thirty years of experience. Aniruddha Sarkar, a principal fund manager with an AMC, shares his perspective on indirect investing.

VIEW: DIRECT INVESTING IS THE BEST FORM OF INVESTING

DEVEN R. CHOKSEY

Direct Investing is like driving your own car versus Indirect Investing is equivalent to commuting in public transport. Destination being the common goal while travelling, both comfort and time are key differentiators in public versus private mode of commutation. Similarly, Investing is done with an objective. It can be fulfilled via direct investments or indirect mode of investments, like Mutual funds *etc*. Investment products have buyers across multiple investor segments i.e., Institutional, Family offices, High Net worth Individuals- HNI's, Ultra HNI's, Retail investors. Therefore, there remains advantage and disadvantage between investing through either Direct or Indirect route, depending upon the category or segment of investor one belongs to.

Primary objective across various customers segment is generation of Returns, managing Risk and having adequate Liquidity. Both the routes, whether direct and indirect, have their pros and cons under each of the above aspects. As we all know, returns and risk go hand in hand, in case of direct investments substantial knowledge on subject matter to support decision making & considerable research is required before venturing in. I would not call this as a hindrance for direct investment route, as nowadays we have professional advisors to assist us into the decision making process. Let me bring out one interesting fact to your attention, direct individual investments in equities commands nearly 16.5% of the market capitalisation versus around 5.4% of the Indian market capitalisation that is held through Equity funds. Clearly, individual preferences remain with direct investments versus indirect route of investments. In US markets also there has been clear shift from direct investments versus investments through mutual funds; there has been decent rise in Independent Advisors therein who cater to individuals for investments.

Let us see how the following primary objectives are managed under respective routes of investments:

a. **Returns b. Risk c. Liquidity d. Cost**

a. **Returns:** For the last 5 years, investments into Direct Equity, say for eg., Current top 5 companies by market capitalisation have fetched 30.8% CAGR vs. Top 5 Equity – Large Cap Mutual fund CAGR returns of 20.1%. One needs to bear in mind while choosing the indirect route the demerits of change in fund manager at Asset management companies, change in purpose of schemes, non customisation of portfolios. Compulsions of common pool investments as required to be followed in MF acts as deterrent whereas direct investment has its own character in managing the returns objective.

b. Risk: Investors risk profile tends to change with segment and category they fall into. The preferences to attain final objective for aggressive investor will be different from those who are believers to passive style of investments. In case of Direct Investments the customisation stands as an advantage based on individual risk profile needs versus Indirect Investments which is more standardised instead of being customised.

c. Liquidity: Benefits of direct investing is generation of adequate liquidity within 2-3 working days. In case of indirect investing, one may witness additional burden in form of exit loads to find speedy liquidation.

d. Costs: In case of indirect investments management charges are levied under individual schemes, which are not in case of direct investments.

While we have seen the pros and cons under individual's primary objectives of Returns, Risk, Liquidity and Cost, let us also find out how secondary objectives are dealt under direct and indirect investments.

1. Build knowledge capital & Earn [Earn-Edge vs ROI]: It is always beneficial to know the company that one invests versus knowing your fund manager. Which means it is better to be dependent on company management in which funds are deployed rather than on fund manager who will be deploying your money. Think about it, isn't it assuring to have financial gains with knowledge capital versus only financial gains. My take is, direct investing is all about individual's passion for growth in investments vs passive growth approach.

2. Investment Advisor: To put it simply, **one good book is knowledge, one good friend is equal to 100 books,** an ocean of knowledge, **and a friend as an investment advisor is a navigator in the journey of wealth creation.** Professional investment advisors are a great help and preferred support for active management of investment goals. One can gain expertise and develop analytical skill with guidance of investment advisors. According to me, there is no match to information sourced from tips, social media or likes of Google or any other media sources that always limits itself to information and does not compliment to the conviction extended by investment advisor. Regular review and monitoring mechanism can help achieve the objective with higher conviction on end results.

3. Easy to maintain as any other Asset Class: In case of direct investments, at times it is found that maintaining of records is tedious and disadvantageous. I believe, maintaining own investments is as easy as maintaining investments in any other assets including MF, insurance etc. We need to follow discipline to invest in sets. SIP in MF, Annual Premium in Insurance are in-built investment systems. Direct Investments help us to invest with conviction whereas indirect investment is often swayed with sentiments.

4. Diversification not a suitable solution: An investment in indirect route generally comes with diversification and involves investing into companies in excess of 30-50 at times in individual schemes. Wealth creation is matter of investing in value and growth companies and not supportive of diversification which tends to dilute the successful ones with unsuccessful stories.

Direct investments have an inbuilt character of allotting higher weight to growth and it is a science. All it needs is an attention. Simply the ability to add dynamic weight produces extraordinary results.

As long as trading instinct is brought under control and CAGR is allowed to be employed, direct equity produces better ROI. Classic example of wealth creation is depicted in table 1:

TABLE: 1

Performance of Direct Investments for last 10 Years			
Indian Cos	**Market cap Rs Bn – 2008-2018**		**10 yr CAGR**
MRF	14.4	316	36.2%
Infosys	99.2	2800	39.7%
TCS	840.4	7000	23.6%
International Cos	**Market cap $ Bn – 2008-2018**		**10 yr CAGR**
Google	165.3	779.5	16.8%
Facebook	66.48	562.48	42.7%
Amazon	30.6	824.7	39.0%
Apple	147.61	909.84	19.9%

5. Customisation to objectives: While the broader goals and objectives can be met both under direct and indirect route of investments, when it comes to meeting of objective within stipulated parameters, investing through direct route, is always beneficial. In case of indirect investment customisation beyond a point is not possible because of productised approach. Let me explain with an example, say for an individual investor has an expertise and understanding in manufacturing industry based on his background. It will be inappropriate for him to invest in a product that offers Pharma companies or any other business, since his knowledge would be insufficient to assess the risk he is engaging himself into.

Finally, we have seen that investing route direct or indirect is subject to type of individual you are and preferences to primary objectives, as spelt earlier with respect to travel; we are well versed with different level of comfort in 3 modes of travel i.e. Self Driven Vehicle, Driving with a Driver and Travelling as a Passenger. Investing in direct equities is no different from the satisfaction received through individual's own decision to investments versus decision taken by fund manager. One may also bear in mind the modes of investment also depends on ticket size of investment. In case of small investor, the preferred route of indirect investments will be beneficial and *vice-versa* for large investors.

In case one has urge to gain exponential returns with substantial risk taking ability, then direct investment is a better avenue as compared to indirect investing.

COUNTERVIEW: INDIRECT INVESTMENTS WORK BETTER FOR MOST PEOPLE

ANIRUDDHA SARKAR

Though the culture of equity investing has been prevalent in India for many decades now, yet equity investing in India is still at its nascent stage. The penetration of equity exposure among the households is merely 3-4% which includes all the organised modes of investments (Mutual Funds, PMS, AIF) as well as direct equity exposure. This figure is small by all global standards and has a great scope for increasing penetration going ahead. In this regard a key question which comes to an investor's mind is which is the better suited path to take when it comes to equity investing. Earlier investors had only two options to choose from; namely direct equity and mutual funds. Then came Portfolio Management Services (PMS). Now, since the last few years AIF has taken the industry by a storm. So, the dilemma has increased even more for investors as to what is a better way ahead for equity investing.

We believe, unless an individual can devote a substantial amount of time in studying and understanding the market and at the same time keeping track of events and news flow that pertains to the equity market and his portfolio stocks, one should always give his money to be managed by professional money managers like Mutual Funds, PMS and AIF. Equity investing is one of the most dynamic activities and cannot be done in a silo. Would like to break-up the benefits of having an indirect exposure into equity markets through professionally managed route into the following broad heads:

- **Managing Risk and Return; making more informed decisions:** Equity returns is all about managing risk and return and getting the balance right makes all the difference. Investors most often expose their direct equity portfolios to very high risk and not take risk which is commensurate with the returns expected. Risk has many facets of it and can be in various forms. Lack of adequate information before investing in a company and not keeping track of developments in the portfolio companies is a major information risk which direct equity investing is faced with. Also, concentration risk is there when too much capital is allocated to a few stocks and if something goes wrong in any of the high concentrated stocks, then it impacts the whole portfolio returns. Unlike in a Mutual Fund or in a PMS, the investment manager and his team is always on top of all developments that keep happening in the markets and their portfolio companies. This helps in making quicker and more informed decisions regarding portfolio changes. Also, portfolio managers balance risk and return aspect in a more scientific manner by not exposing the clients' money to high risk, as there are several internal checks within the asset management companies to monitor this aspect.

- **Access to companies for making decisions**: When investors approach equity investment directly, their access to company information gets limited to accessing annual reports and earnings transcript and reading online public information. However, for professional money managers, access to company management, plant visits, institutional access and analysts meetings is something which helps them to make more informed decisions when it comes to equity investing.

◆ **AIF platform offers diverse financial products**: With the AIF platform being launched by SEBI in 2012, the ability of the investment managers to offer diverse products on the platform has taken a huge leap in financial innovation. Within the three categories (CAT I, CAT II and CAT III) of AIF, we now have diverse product offerings spread across listed equity, unlisted equity, debt instruments, Real estate and Commodities. Having a diverse basket of these products along with Mutual Funds and PMS, helps in having the right Asset Allocation for the investors which is of prime importance in the journey of making long term wealth. There are some financial products wherein investors are also given access to investing into overseas equities, which is otherwise very cumbersome if one has to go directly.

◆ **Freedom to choose investment managers and switch between them**: During different periods different investment managers outperform others. As an investor, you have a choice to switch between the managers and at the same time have a basket of investment portfolios which is managed by different investment managers. This helps in generating a more balanced return for the portfolio at a consolidated level.

◆ **Less hassle and professional approach at competitive fees**: We have come a long way in Indian Equity markets from the days of Open cry in the ring at BSE. Equity investments are now managed by professional fund managers and SEBI which governs and controls all operations of the Mutual Fund, PMS and AIF industry. This has helped in bringing the best global practices of the financial service industry to Indian investors. Access to single statement which shows all holdings of investors across investment managers, ease of tax statements and lower fees due to increased competition in the financial services industry is something which makes life a lot easier for investors coming through the indirect route for equity investing.

Thus, we see that where there is paucity of time and where investors do not have the bandwidth to spend a lot of time on understanding companies, on reading annual reports and in understanding financial statements, it is best not to enter the equity markets directly and better to invest via the mutual funds, PMS or AIF route. What we have seen in the past is that when the bull markets happen, more and more investors get lured into the equity markets and start buying stocks directly based on hearsay and 'tips'. These are recipes for disaster and investors should be careful about not burning their hands in this manner. At the same time, if there is any investor who thinks he has the bandwidth and time to devote to the equity markets, he should gradually start taking baby steps in the market through direct equity and invest only after doing detailed analysis of the portfolio companies. This would also help in building more discipline in the investing style and in building great amount of knowledge about companies and markets. The benefits of professional investment managers cannot be ruled out even for a client who likes to do direct investing because of the access to a plethora of different financial products which are otherwise not available when doing directly. ■