Bonds vs stocks: What is the best asset allocation for mutual fund investors post poll results?

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With a weaker than predicted election outcome for the Narendra Modi-led BJP and NDA, mutual fund investors are concerned about asset allocation they should make now. We categorized the investors based on their risk appetite: conservative, moderate, and aggressive.

In the last five years of the Modi-led government, around six equity mutual fund categories gave over 150% returns with small cap funds offering the highest absolute return of 243.94%. Mid cap funds gave an absolute return of around 200.92% in the same period.

Out of 19 small cap funds, only five funds failed to beat their respective benchmarks.

Here is what mutual fund advisors suggest as the best asset allocation for mutual fund investors in the third term of the Mod-led government.

For conservative investors

"For conservative investors, an exposure of approximately 30% exposure to growth assets like equity and commodities, and 70% to defensive assets is suggested. Conservative investors should not get carried away in the possible euphoria of continuity of governance and should stay with their original asset allocation as equity markets continue to be priced at a premium to long term averages. The premiums in mid and small cap equities and funds are even higher than those for large caps equities and funds are even higher than those for large caps equities and funds," recommends Vishal Dhawan, CEO, Plan Ahead Wealth Advisors, a wealth management firm in Mumbai.

For moderate investors

"Asset allocation is largely a factor of the time horizon and investment objectives. However, considering a long-term investor is seeking to maximise wealth over the period through investments, a moderate investor can hold a 70:30 portfolio as a starting point. This is across equity and debt. Considering the current position in the cycle, the debt component can include a combination of longer-maturity gilt funds, corporate bond funds and short-term funds. Within equities, a good quality flex cap or Multicap fund could work for investors with limited ability to proactively allocate and manage the portfolio," said Sagar Shinde, VP Research, Fisdom.

He adds, "Asset allocation is ideally a function of personal investment objectives and caveats. However, for a long-term investor with tactical portfolio optimising for economic and market cycles, an overweight allocation towards equities is warranted. Within equities, an orientation towards large and midcaps would be favourable. At a sectoral level, the portfolio can lean towards financial services, capital goods, infrastructure and power as key sectors."

For aggressive investors

"An aggressive investor can have about 60% to 70% equity mutual funds, with a higher proportion towards flexi cap funds. High-risk funds like small caps and sector funds should only be considered satellite funds, not core funds. However, for all short and medium-term goals, the investor should invest in only debt and hybrid funds," suggests Rajesh Minocha, a Certified Financial Planner (CFP), Founder of Financial Radiance.

He adds, "(If) Modi-led government returns to power again with a clear majority, then there will be stability and that is always good for the markets. During the next decade, India will soon be a major power to reckon with as we move towards being the third-largest economy in the World."

One needs to include other factors while choosing a scheme to invest in. One should always consider their risk appetite, investment horizon, and goals before choosing mutual funds.