MFs with exposure to US stocks gain appeal amid Wall Street's record-breaking rally

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Investors seeking to diversify their equity portfolios beyond home amidst stiff valuations in Mumbai and benefit from the recent growth in US stocks could consider a small allocation to equity mutual funds built around Wall Street-listed assets.

Given the sharp run up in the US markets over the past one-year, financial planners believe investors could stagger their bets over the next one year, with a 5-10% allocation to the US markets.

"At the broad index level, valuations of Indian and US equities are similar. Several US companies are expected to show strong growth," said Vishal Dhawan, Founder, Plan Ahead Wealth Advisors.

Dhawan believes investors could allocate 10% of their equity portfolios to the US markets and stagger their bets over the next one year. Dhawan recommends an SIP in Franklin US Opportunities Fund, for investors with a high-risk appetite.

In terms of valuations, the S&P 500 trades at a price to earnings (PE) ratio of 25.41, against the Nifty 500 that trades at a PE of 26.5.

Financial planners point out that since the US accounts for close to 25% of global GDP and has some unique businesses in new areas, investors should take exposure to Wall Street-traded assets.

A note by Motilal Oswal Mutual Fund points out that by investing in the US and India, a saver can get a combined exposure to 30% of global GDP. The low correlation of the US with the Indian markets offers opportunity for diversification and helps reduce portfolio volatility, thereby improving risk adjusted returns, said the note.

Over the past one year, the S&P 500 index has moved up by 37%, while the Nifty 500 gained 25.29%.

"The US markets are up sharply, led by technology stocks in the last one year, but the move ahead is not going to be one-sided," said Vineet Nanda, founder, SIFT capital. Nanda believes investors could stagger investments and use a buy on dips approach.

"Ideally, one should look at staying invested in the domestic market. However, for those wishing to diversify, exposure to US equities can be considered through diversified mutual funds with a small allocation to US stocks," said Feroze Azeez, deputy CEO, Anand Rathi Wealth.

Some diversified and sectoral equity mutual fund schemes have a provision to allocate up to 35% to overseas equities. Schemes like PPFAS Flexicap Fund have a mandate to invest in global companies. Some wealth managers warn investors not to go overboard.

“The US market has several uncontrollable factors, such as geopolitical risks, inflationary pressures, and Federal Reserve policies. Given the robust growth potential of Indian equities despite muted earnings growth in the last quarter, it is recommended to stay invested in the domestic market,” said Azeez.

Distributors point out that mutual fund investors have limited choice to take exposure to US markets. The RBI regulates the fund inflows and outflows. Currently there is an overall industry level limit of $7 billion for mutual funds with an additional $1 billion for ETFs.

They can take exposure through US-based funds that are large cap oriented or the Nasdaq 100 index or ETF, that have a large exposure to technology. The tax treatment for international funds is beneficial too, investors now paying a long-term capital gains tax of 12.5% after holding for two years. Many fund houses, however, have restricted investments based on limits available.

There is no access to US mid and small cap stocks or sectors outside technology as the RBI regulates the fund inflows and outflows and currently there is an overall industry level limit of $7 billion for mutual funds with an additional $1 billion for ETFs, due to which there have been no launches from the industry.