



Diversification & Investment

Strategies

Understanding

Diversification – Definition

Understanding Diversification – Definition

Spreading Risk Across Investments

Not Concentrated in One Area

Uncorrelated Asset Classes



Understanding

Diversification – Importance

Understanding Diversification – Importance

Risk Reduction

Improved Returns

**Stability During Market
Volatility**



Understanding

Diversification – Principle

Understanding Diversification – Types

Asset Class

- Equities
- Bonds
- Real Estate
- Commodities

Geographic

- Investing in developed and emerging markets
- Exposure to multiple currencies

Sector

- Tech (High growth)
- Healthcare (Stable)
- Energy (Cyclical)

Understanding

Diversification – Types

Understanding Diversification – Principles

Risk return trade-off

- A portfolio might include growth stocks alongside defensive stocks
- Diversification does not eliminate the risk entirely, but helps to balance it

Risk management

- By spreading investment across multiple asset classes, sectors, and regions – diversification reduces unsystematic risk

Correlation

- Including uncorrelated assets will help smooth out portfolio returns and reduce volatility

Building a Diversified Portfolio

Asset Allocation Based on

Risk Tolerance

Asset Allocation Based on Risk Tolerance

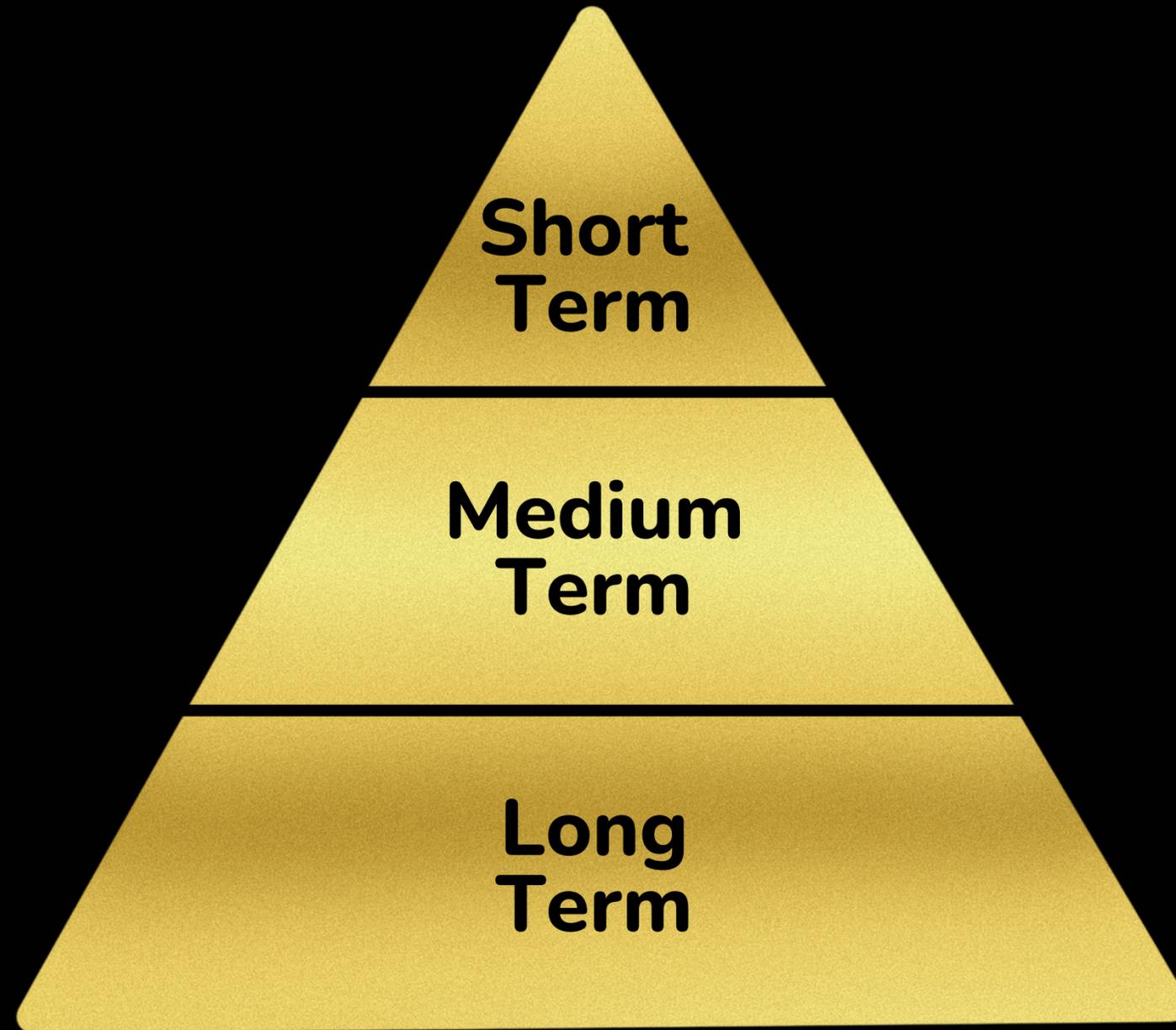
**Conservative
Portfolio**

**Balanced
Portfolio**

**Aggressive
Portfolio**

Time Horizon

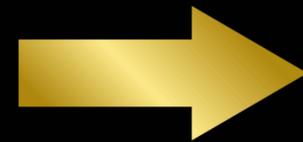
Time Horizon



Financial Goals

Financial Goals

**Growth
Oriented**



**Income
Oriented**

Rebalancing

Calendar based

Calendar based

How It Works:

- At each interval, the investor compares the current asset allocation to the target allocation. If the portfolio has deviated significantly from the target, assets are bought or sold to bring the allocation back in line.
 - ◆ **Example:** If the target allocation is 60% stocks and 40% bonds, and due to market growth, the portfolio now holds 70% stocks and 30% bonds, the investor would sell some stocks and buy bonds to restore the balance.

Benefits: This strategy is simple and disciplined, ensuring regular maintenance of the portfolio. It is also less labor-intensive as it only requires periodic reviews.

Drawbacks: Fixed rebalancing intervals may cause the portfolio to miss timely opportunities to rebalance during periods of significant market volatility.

Hybrid based

Threshold based

How It Works:

- Instead of rebalancing on a set schedule, this approach rebalances the portfolio whenever a particular asset class exceeds or falls below the predefined threshold
 - ◆ **Example:** If the portfolio is designed to maintain 60% stocks and 40% bonds with a 5% threshold, the investor would rebalance only when the stock allocation grows beyond 65% or falls below 55%

Benefits: This approach is more responsive to market movements and can be more efficient in volatile markets where deviations from the target are more frequent.

Drawbacks: It may require more frequent monitoring of the portfolio, which can increase time and effort. Additionally, frequent rebalancing may lead to higher transaction costs.

Hybrid based

Hybrid based

How It Works:

- 🕒 Investors monitor the portfolio regularly, but they only rebalance if the deviation from the target exceeds the predefined threshold.
 - 💡 **Example:** An investor may review their portfolio annually, and if their stock allocation moves more than 5% above or below the target during that time (e.g., from 60% to 65%), they will take action to rebalance. If no significant deviation occurs, the portfolio remains unchanged during the review

Benefits: This approach ensures that the portfolio is both regularly reviewed and responsive to significant market changes without unnecessary transactions.

Drawbacks: Can be more complex to manage, as it requires both regular monitoring and threshold setting. Additionally, it could lead to frequent rebalancing and incur higher transaction costs.

Key Considerations for rebalancing

Key Considerations for Rebalancing

Transaction Costs

- Rebalancing often involves buying and selling assets, which can incur transaction fees
- Investors should weigh the cost of frequent rebalancing against the benefit of maintaining their desired allocation

Tax implications

- Rebalancing can trigger capital gain taxes, especially if assets have appreciated significantly
- Tax-loss harvesting can be considered for effective tax management

Automated Rebalancing

- There are now robo-advisors and financial platforms that offer automatic rebalancing services, making it easier for investors to maintain their target asset allocation without manual intervention

Key Considerations for rebalancing

Key Considerations for Rebalancing

Transaction Costs

- Rebalancing often involves buying and selling assets, which can incur transaction fees
- Investors should weigh the cost of frequent rebalancing against the benefit of maintaining their desired allocation

Tax implications

- Rebalancing can trigger capital gain taxes, especially if assets have appreciated significantly
- Tax-loss harvesting can be considered for effective tax management

Automated Rebalancing

- There are now robo-advisors and financial platforms that offer automatic rebalancing services, making it easier for investors to maintain their target asset allocation without manual intervention

Investment Strategies

Overview

Overview

Active & Passive

- **Active** Involves selecting individual stocks or assets in an attempt to outperform the market
 - **Passive** Involves investing in broad market indices, such as the Nifty 50 or Sensex, with minimal buying and selling
-

Value Investing

- **Value investing** focuses on buying stocks that appear to be undervalued based on their intrinsic value
 - "Buy low, sell high" – value investors aim to buy companies at a discount and wait for the market to recognize their true value.
-

Growth Investing

- **Growth investing** involves investing in companies that are expected to grow at an above-average rate compared to others in the market. Growth investors prioritize capital appreciation over dividends.
 - Investors look for companies with strong revenue and earnings growth, typically in sectors like technology, new-age, or consumer goods
-

Overview

Income Investing

- Income investing focuses on generating regular income from investments, often through dividend-paying stocks, bonds, or real estate investment trusts (REITs)
 - Stability and regular cash flow are prioritized, making this strategy attractive for retirees or conservative investors
-

Index Investing

- Index investing is a type of passive investing where investors buy shares in funds that track a market index, such as the Nifty 50 or the S&P 500
-

Contrarian Investing

- Contrarian investing involves going against prevailing market trends. Contrarians buy assets that are out of favor with the broader market, believing that they are undervalued and will eventually rise in price.
-

Value Investing

Long-term growth with minimal risk

Core Principle

Core Principle

Intrinsic Value vs. Market Price

- Intrinsic value is the perceived true value of a company based on its fundamentals, such as earnings, assets, and future cash flow. Value investors look for companies where the intrinsic value is higher than the current market price, creating an opportunity to buy at a discount

Margin of Safety

- A key principle of value investing, the margin of safety is the difference between the intrinsic value and the current stock price. By investing in stocks with a substantial margin of safety, value investors aim to minimize the downside risk if the market does not recognize the stock's value immediately

Long Term Perspective

- Value investors typically have a long-term investment horizon, willing to hold onto stocks for years while waiting for the market to correct its undervaluation

Key Ratios

Key Ratios

PE Ratio

- A lower P/E ratio may indicate that a stock is undervalued relative to its earnings
- A company with a P/E ratio of 10 may be more attractive to a value investor than a company with a P/E of 30, assuming all else is equal

Dividend Yield

- Value investors often seek companies with a high dividend yield, which represents the income earned from dividends as a percentage of the stock's price
- High dividend yields can provide additional returns while waiting for stock price appreciation

Debt-to-Equity

- Value investors look for companies with a lower D/E ratio, indicating they are not overly reliant on debt to finance their operations
- Lower the D/E ratio is better

Growth Investing

High valuation but with above-average growth potential

Core Principle

Core Principle

Capital Appreciation Focus

- Growth investors prioritize capital appreciation over dividends or income. They seek companies that are likely to expand rapidly, believing that these companies will provide strong returns as their earnings grow over time

Revenue & Earnings Growth

- A core tenet of growth investing is focusing on companies with high and accelerating revenue or earnings growth. Growth investors typically target sectors such as technology, healthcare, or consumer discretionary, where innovation and market demand drive expansion

Industry Leadership and Innovation

- Growth companies often lead their industries through innovation, technological advancements, or unique business models. These companies tend to reinvest profits into the business to fuel further growth, rather than paying out dividends

Key Ratios

Key Ratios

Revenue & Earnings Growth Rate

- Growth investors look for high and sustainable revenue growth, as this is often a precursor to future earnings growth
- Growth investors also look for companies with a consistent history of earnings growth and projections for continued growth

Return on Equity (ROE)

- Growth investors prefer companies with high ROE, as it signals that the company can effectively reinvest earnings into further growth

Price-to-Sales

- Growth investors may also use the P/S ratio, which compares a company's stock price to its revenues. This is useful for companies in the early stages of growth that may not yet be profitable but have strong revenue growth

Income Investing

Generating consistent cash flow through
investments

Key investment vehicles

Key investment vehicles

Dividend paying stocks

- Typically mature, established companies with stable earnings
- Often found in sectors such as utilities, consumer staples, and financial services
- Dividends can provide a consistent income stream, especially when reinvested for compound growth

Bonds

- Bonds provide predictable income through coupon payments
- Government bonds (e.g., treasury bonds) are considered low-risk, while corporate bonds may offer higher yields with greater risk
- The main source of income, where bonds pay a fixed rate of interest (coupon rate) periodically until maturity.

REITs

- REITs provide exposure to real estate without directly owning property
- They offer higher-than-average dividend yields, as they are required by law to distribute at least 90% of taxable income

Advantages

Advantages

Steady Cash Flow

Lower Volatility

Inflation Hedge

Index Investing

Low-cost, simple, and diversified approach to long-term investing.

Key benefits

Key benefits

Low Cost

- Index funds and exchange-traded funds (ETFs) typically have lower expense ratios compared to actively managed funds because they require less management and trading activity
- By minimizing fees, more of the investor's money remains invested, allowing for better returns over the long term

Simplicity

- Index funds offer a straightforward investment approach, as they do not require the constant buying, selling, or active management associated with picking individual stocks
- Index funds are easy to understand and use, making them an ideal choice for both beginners and seasoned investors who prefer a hands-off investment approach

Consistent Long-Term Performance

- Historically, index funds tend to outperform the majority of actively managed funds over the long term due to their broad exposure and lower costs
- Over time, consistent performance that matches the market can lead to better returns than trying to outperform through active management

Types

Advantages

Equity Index Fund

Bond Index Fund

**Sector Specific Index
Fund**

Recap & Takeaways

Recap & Takeaways

- **Diversification:** Spreading investments across various asset classes, sectors, and geographies to reduce risk and enhance potential returns
- **Key Benefits:**
 - ◆ **Risk Reduction:** Diversification helps mitigate the impact of poor performance in any single investment by spreading risk
 - ◆ **Improved Returns:** A well-diversified portfolio can potentially lead to more stable and improved returns over time
 - ◆ **Stability:** Reduces portfolio volatility by balancing investments that may perform differently under various market conditions
- **Investment Strategies:**
 - ◆ Active vs. Passive Investing
 - ◆ Value Investing
 - ◆ Growth Investing
 - ◆ Income Investing
 - ◆ Index Investing
 - ◆ Contrarian Investing