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Devina Mehra: Investors mustn't mix up apples and oranges while investing

Devina Mehra | 2 July 2025

Remember the order: choose the asset class, then the structure. (iStock)

SUMMARY

An investment strategy demands utmost clarity on basic concepts. Asset classes are distinct from investment vehicles, for example, and allocation decisions on the former must be made first. Here's how to go about it.

I am often surprised by the investment questions I get, even from otherwise knowledgeable individuals. Here is a sample: Is it better to invest in a PMS (portfolio management service) that invests in equity or an AIF (alternate investment fund) with a great derivatives strategy?; My advisor says equity mutual fund SIPs (systematic investment plans) are outdated and recommends a global gold ETF (exchange traded fund)—what do you think?; Most of my investments are in an insurance policy—is that okay?; Should I invest a lump sum in a fixed-income mutual fund or SIP into an equity PMS?

There's a common misunderstanding inherent in these questions: confusing asset classes with investment vehicles. Investors often don't realize that equity, fixed income and gold are distinct asset types, while mutual funds, ETFs, PMS or AIFs are ways to invest in those assets. Remember the order: choose the asset class, then the structure.

Here's a simplified list of asset classes: *Equities*: Stocks held directly or indirectly; *Fixed income*: Bonds, fixed deposits, saving schemes, etc; *Commodities*: Gold, silver, oil, industrial metals, agricultural commodities; *Real estate*: Property or REITs; Cash equivalents: Savings accounts, liquid funds; *Alternatives*: Cryptocurrencies, art or unlisted equity (example: venture capital).

The other dimension on which assets vary is by geography (for example, Indian versus US versus emerging market equities). Within an asset class and region, there are multiple investment options. For Indian equities, you can buy stocks directly or use mutual funds, PMS or AIFs. For fixed income, there are bonds, fixed deposits or debt mutual funds. Gold can be physical, gold ETFs, or sovereign gold bonds.

The first step is to assess your current investments—financial (stocks, bonds) and physical (property, gold)—and liabilities (loans). Your net worth is assets minus liabilities.

Then decide on your target asset allocation. Studies show 85-92% of portfolio returns come from how you spread investments, not from picking specific stocks. Allocation depends on your age, goals and risk tolerance. Still, there are some basic guidelines to follow.

One, look at long-term data and not what has happened in the last six months or two years. Indian equities are said to yield 15-16% annually, but returns can vary dramatically. From 1980–1990, the Sensex grew 21% yearly. From 2010–2020, it grew 8.8%. From 1994–2003, returns were near zero.

Two, avoid chasing what has done well recently. In 2021, many invested in Nasdaq ETFs or via US trading platforms like Robinhood, assuming past gains would persist. The very next year, Nasdaq was almost the worst performing index in the world.

Three, stick to liquid assets. Unless you're a professional, avoid illiquid assets like unlisted equity or products with no publicly available price.

Four, avoid complex products like derivatives or unlisted equities, unless you are a full time professional in the area. Still, I find people trying to decide between a PMS that is not even allowed to invest in derivatives versus an AIF whose whole strategy may be based on derivatives or investing in distressed assets or something just as exotic.

Five, skip fads. Thematic funds (industry- or geography-specific) often launch around the peak of that theme.

Six, stay committed to your asset allocation. Constantly shifting to recent top performing categories statistically leads to poor returns. So if small-cap stocks, defence stocks or gold have done well of late, it may not be a good idea to switch to those.

And now the most overlooked part—*diversify globally*. Asset allocation isn't just about choosing large-cap versus small-cap stocks or value versus growth strategies. It requires looking beyond your home country. Over-investing locally creates 'single country, single currency, single asset risk' (SCCAR), which can hurt during crises or currency depreciation. The rupee has fallen nearly 90% against the US dollar (from ₹12 to ₹86) since I started my career.

Effective allocation includes global assets: developed market equities, emerging market bonds, global REITs, gold and commodities. Implementation details vary, but diversification is key.

It is only after you've done your asset allocation across assets and geographies that the question arises of how to invest in each asset class. Stocks, mutual funds, PMS or ETFs? Physical gold, gold ETFs or sovereign gold bonds? Regular bonds, fixed deposits or debt funds?

Consider fees, risks, tax implications and liquidity when selecting a vehicle. But the golden rule is not to mix up asset classes and structures. An equity mutual fund isn't a substitute for a gold ETF, as they involve different assets (equities versus gold) and structures (mutual fund versus an ETF). Similarly, insurance policies, which often combine investment and insurance, differ from mutual funds and AIFs.

In a nutshell, step one is to decide what percentage of your investments you want in a certain asset class. Step two is to decide on the structure through which you will invest in this asset class. Unless these concepts are clear in your head, your decisions will be muddled and advisors of various hues might be able to misguide you.

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