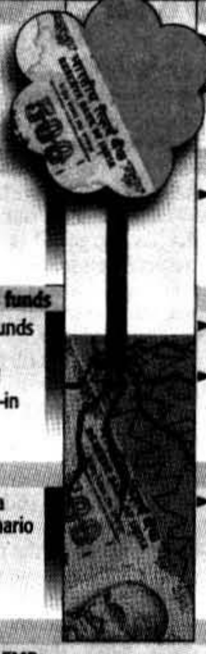
Save & stay liquid at the same time

Wondering Where To Park Your Money That You Might Need Soon? **Preeti Kulkarni** Has Some Suggestions

FUND FUNDAS

Pros (left column) And Cons (right column) Of Instruments



Fixed Deposits	
► Capital protection ► Fixed returns	► Unattractive in terms of tax benefits ► No opportunities for capitalising on the changing interest rate scenario
FMPs	
► Good yields ► Efficient Taxation ► Capital protected	► Entail a lock-in period; hence any redemption before the maturity of the fund would attract an exit load
Liquid Funds/Liquid plus funds	
► Availability of liquid plus funds offering tax reliefs ► No lock-in; even in case of liquid plus funds, the lock-in period does not exceed 7-14 days	► Yields lower than other debt options ► The taxation structure of a plain liquid fund is deemed inefficient as compared to that of a debt fund
Income Funds	
► Good yields, especially in a softening interest rate scenario ► Liquidity after 6 months ► Good avenue for investing in long term debt paper	► Inferior yields in a rising interest rate scenario
Arbitrage Funds	
► Yields in line with those of FMPs ► Carry neither default nor interest rate risk ► Liquidity is comparable to that of liquid funds, post the minimum investment period of 3-6 months	► Entail fund manager performance risk

SUPPOSE you want to utilise your savings for buying a house after a year, or wish to lock it in for a period of six months, when your holiday plans would take shape, what is the first option that would come to your mind? More often than not, it would be the tried and tested bank fixed deposit. Although several short-term instruments are available in the market today, many people are reluctant to open their minds and look beyond the traditional savings instruments.

OPTIONS GALORE

What exactly are the options available to those investing with a short-term horizon? Says ASK Wealth Advisors' wealth management solutions head Maneesh Kumar, "If a person wants to invest surplus monies for a period of six months to a year, he/she can buy a six month Fixed Maturity Plan (FMP). Post-maturity, if he/she intends to continue with it, the money can be rolled into another six-month FMP." Also, in case the investor is not sure if the money would be needed after six months, the money can be shifted to liquid plus funds.

However, PARK Financial Advisors' director Swapnil Pawar is not all that gung-ho about FMPs. "Though they are capable of giving a higher yield compared to liquid funds, the risk too is much higher. They tend to carry an interest rate risk and small part of default risk as well, since they invest in corporate debt. Besides, FMPs are the lowest on liquidity. Also, one needs to know the holding period with a good amount of certainty. Unlike other options, FMPs are not open ended and hence cannot be held for an arbitrary period of your choice," he informs.

So, if you are risk-averse, you can opt for low-risk mutual funds including liquid funds, gilt funds and arbitrage funds. Liquid funds, as the name suggests, bag the top slot when it comes to liquidity. They are low yield (around 5-6% in current market situation), but carry very little risk — the returns are fairly predictable and certain.

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ARBITRAGE FUNDS

A very attractive alternative is the arbitrage fund. These high-yield, debt-like instruments carry neither default nor interest rate risk. While their yields are in line with those of FMPs, post the minimum investment period of around 3-6 months, they become as liquid as the liquid funds. However, as they try to gain from arbitrage opportunities in equity and derivatives market, the fund manager performance risk comes into play here.

MAKING A CHOICE

How should an investor go about zeroing in on the right short-term product for him/her? Replies Mr Kumar: "The first thing that the person should consider is, when the money would be needed. He/she needs to understand that some short-term instruments such as income funds entail an exit load. The investor should also look at the taxation structure of the short-term instrument — focus on post-tax returns as opposed to pre-tax returns." The term and duration of the debt paper also counts because in a softening interest rate environment, for example, an instrument containing a longer dated paper will provide good capital appreciation as against an instrument that has a shorter dated paper. It is also imperative to know whether the short-term instrument can take advantage of the changing interest rate scenario by providing a capital gain or the return is expected to be confined to interest income alone.

Mr Pawar has these tips to offer to the investors planning to park their funds for a short-term duration: "If the horizon is known for sure and there is no likelihood of need for money arising before that, use FMPs. If the horizon is known and is longer than 6 months, use arbitrage funds; if horizon is unknown but is likely to be long, you can go for long-term gilt funds, considering that a rate reduction by RBI is expected next year. If horizon is highly uncertain, stick to liquid funds. In arbitrage funds, if the investor is bracketed under the highest tax slab, he/she can go in for the growth option; else, the dividend option can be used."

preeti.kulkarni@timesgroup.com