

Monthly Income Plan-A Perspective

Introduction

A Monthly Income Plan (MIP) is essentially a medium term bond fund with a little equity icing on the top. With both equity and Debt markets hip hopping around in a most volatile manner, MIPs could well be the answer to most investors' problem.

A Typical MIP would invest around 80-95% in bonds and money market instruments and have small exposure of around 5-20% in equities. Therefore MIPs are suitable investment option for any investor who is relatively more cautious and wants a stable return with very little involvement. In the past bond markets rallied, and income and gilt plans gave exceptional returns while the equity plans under performed but currently equity markets are in bull phase backed by good fundamentals both corporate as well as economic factors. So MIP helps in providing the best of both worlds.

Suitability

MIPs are suitable for investors who want to invest in debt funds but would not mind to bear some risk for an extra return through investments in equity markets. However there is a word of caution that these funds may not provide adequate returns when the markets witness correction or are in a bear phase. **Thus MIP would be ideal when the equity markets are in a bullish phase or when the investors stay with the fund for an adequate period of time.** Also, because of the higher volatility caused by the equity component in MIPs, they are not ideal vehicles for **risk-averse investors** seeking supplement to monthly pension. One way to reduce the risk is to lengthen your investment horizon. Equities have the ability to deliver higher return over a longer period of time. And the debt portion of MIP is always there to provide a relatively stable return.

Historical Background

<i>MIP Most fared well in 2003, but lagged debt funds over 3-yr period.</i>			
	Return		Average Maturity
Monthly Income Plans	1 Yr (%)	3 Yr (%)	Fund (Yrs)
Templeton MIP	16.8	12.4	4.8
Franklin Templeton MIP	18.6	13.8	3.9
PruICICI MIP	13.4	12.1	2.9
Birla MIP	15.9	14	3
Alliance MIP	18.9	13.5	4.6
Tata MIP	18.6	13.3	5.9
Pure Debt Funds			
Templeton Income	13.4	14.6	5.8
Templeton IBA	14.9	15.8	7.7
PruICICI Income	13.7	14.7	7.0
Birla Income Plus	13.9	14.9	7.2
Alliance Income	13.2	14.6	6.8
Tata Income	11.2	11.7	5.7

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Over past three years, MIPs have delivered a decent return of 12.4 percent per year. In 2001 and 2002, MIPs largely benefited from the declining interest rates. However due to sluggish equity markets in those days, MIPs posted slightly lower returns than income funds. But when the rally in the debt market slowed down in 2003, MIPs got a big boost from the bullish equity markets. The rally in the equity market was so strong that even with 10 to 20 percent equity exposure, MIPs outperformed the category of income fund by 85 percent. But it would be wrong to assume that such returns can be sustained over long periods of time. For example, even with an equity exposure of say 15 percent, a 20 percent fall in the equity prices will reduce the MIP return by three percentage points.

Choices Available

To provide diversity within MIPs, most fund houses have come up with two or three variants with each having a different equity exposure limit. Till recently, investors had few choices for investing in MIPs in terms of funds' equity allocation. The most common allocation was the maximum 15 percent. But now investors have various options depending on how much risk one can take. The equity allocation now ranges from 0 percent to 25 percent (See table)

Stated Equity Allocation (%)	Funds
0	ING Vysya MIP-Plan A
0 - 5	Birla MIP II (Saving 5 Plan)
0 - 10	Tata MIP, UTI Regular Income Scheme, Deutsche MIP-Plan B
0 - 15	Alliance MIP, Birla MIP, JM MIP, LIC MIP, Magnum MIP, Principal MIP, ICICI MIP, Sun F&C MIP, Templeton MIP, HDFC MIP Short-term, HSBC MIP regular
0 - 20	Chola MIP, DSPML Savings Plus, FT India MIP, Reliance MIP, Sundaram MIP, Deutsche MIP-Plan A, ING Vysya MIP-Plan B, Tata MIP Plus
0 - 25	IL&FS MIP, HDFC MIP Long term, HSBC MIP Savings, Principal MIP Plus, Birla MIP II (Wealth 25)

The Fund houses have also provided variety in terms of the maturity profile. Case in point is HDFC mutual fund, whose short-term plan is managed just like a short-term fund – its average maturity is kept at the shorter end. That apart, the equity component is limited to 0 to 15 percent. On the other hand, the average maturity of long-term plan is kept at the longer-end with equity component 0 to 25 percent.

Conclusion

Due to higher economic growth and optimistic future scenario regarding the GDP the interest rates have started firming up, due to which the debt component of a MIP may not fetch much return to the fund in future. But due to high economic growth, various sectors across the industry are showing comparatively higher growth resulting in change in topline as well bottomline growth

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for companies. So keeping some equity component in your portfolio is desirable. And here the MIP helps in providing **regular return** by way of higher debt allocation and **capital appreciation** by way of small equity component. So how well the fund manager manages the equity component will differentiate one MIP from the other. This is likely to make MIPs, relatively more volatile in times to come. So, one should consider MIPs only if investible horizon is for a relatively longer period of time say, over a year. Since investors have more choices to choose from, select an appropriate MIP depending on your risk taking ability.

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