Stellar performance

The equity linked saving scheme is a good investment for tax payers

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The stock market is a high risk investment but an investor can enjoy these returns without directly investing into the market. One such alternative is through the equity linked saving scheme (ELSS), which is a mutual fund scheme in which investment is mainly into equity. Though up to 35 per cent of the fund can be invested in non-equity investments such as debt instruments to provide more balance, a major chunk is allocated to equity and therefore it is highly volatile in nature and returns are dependent on market performance. As a result, the price of the units keeps fluctuating in tune with the ups and downs in the stock market. However, most fund managers usually resort to diversification of funds in equities across sectors, which can reduce the risk to some extent. Further, it is an open ended fund and thus can be subscribed to at any time. The funds have their net asset value (NAV) which changes according to the market scenario. The investor uses the NAV for the purchase or sale of the units.

Comparison of risk and returns vis-a-vis other tax saving instruments under Sec 80C max ₹1.5 lakhs

Instruments	Lock-in period (Years)	Risk level	Returns (% pa) CAGR	Tax status on return
Public Provident Fund (PPF)	15	Low	8.7	Tax free
National Savings Certificate (NSC)	5 10	Low Low	8.6 8.9	Taxable
Bank Fixed deposits	5	Low	9	Taxable
Equity Linked Savings Schemes (ELSS)	3	High	Market linked	Tax free
Life Insurance	5	High	Market Linked Traditional	Tax free

Investing in ELSS has an added advantage. When an investor invests in ELSS, it is tax free. As they get deductions under Section 80C, dividend received on ELSS is tax-free and redemption is also tax free hence it is known as exempt-exempt-exempt policy. Among other immediate alternatives viz PPF and NSS, ELSS emerges as the best choice for an investor who has a good appetite for risk, as the ELSS outperforms both with a massive 27.34 per cent return on an average in the past three years compared to 8.70 per cent on PPF compounded annually and 8.5-8.8 per cent on NSS compounded half yearly. Not only are the returns high but they have the shortest lock-in period of three years compared to 15 years in PPF (even partial withdrawal is possible after 6 years only) and 6 years in the case of NSS. While the dividend income is tax free, the investor can invest up to any amount even though he is entitled for deductions upto Rs1,50,000 under Section 80C. Since ELSS mutual funds invest mainly in equity related investments these schemes would help the investor to grow money when the stock market grows over a period of time. So besides the tax saving element, it is a good investment choice for an average investor who wants to have an equity investment portfolio. Most investors who want to invest in the stock market, find themselves in a state of confusion regarding what scrips to buy and when to sell them just at the right time so as to maximise their returns. Often they lack confidence as they may not possess in depth knowledge about the movement of stock prices based on fundamental or technical analysis and particularly the prices of an individual stock. By adopting the ELSS route an investor is hassle free.

Today, there is increased retail participation and that is coming through the mutual fund route. They are probably being seen as a safe bet to hit the right scores. This is reflected not only in the increase in the number of mutual fund folios but also the amount of investments in mutual funds particularly in their equity schemes. The scope of ELSS is going to widen in the coming days due to opening up of the economy, increase in savings rates, desire to invest in stock market, understanding the fundamentals of mutual funds, past track records and awareness about sectorial investment by mutual funds.

Talking about returns, Reliance Tax Saving, Axis Long Term Equity Fund, Kotak and many others have given mind boggling returns which range from 60 to 85 per cent. Axis Long Term Equity Fund, Reliance Tax Saving (ELSS), HDFC Tax Saving, SBI Magnum Tax Gain, Birla ELSS Tax Relief 96 all have given more than 50 per cent return in the last one year and more than 12 per cent on an average in the last 5 years whereas the average Sensex return from this year is 43 per cent and 5 years average is 12.50 per cent. It clearly shows that ELSS funds are outperforming even the Sensex. ◆

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