Building a **strong portfolio** with **alternative investment funds**

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The financial market in India is evolving at a rapid pace, and as a result, there is a rising trend of High Net Worth Individuals (HNIs) looking beyond traditional investment avenues like real estate, gold, fixed deposits as well as mutual funds. HNIs are increasingly seeking personalized solutions that can help diversify and grow their wealth at a better rate than commonly available investment options. This is where Portfolio Management Services (PMS) and Alternative Investment Funds (AIF) come in.

India has emerged as an oasis of resilience and opportunity in a world where several prominent economies are facing a growth struggle. With a positive long-term outlook on the country, robust financial systems, and evolving investment space, India's economic growth is on a strong footing in the years ahead. This would also result in increasing per capita income and individual wealth. As a result, the number of High-Net-Worth Individuals (HNIs) and Ultra HNIs in the country is likely to increase, furthering the need for relevant investment avenues for such individuals to park their money.

As HNIs and Ultra HNIs look to expand their wealth, they have a wide basket of investments at their disposal. But while these avenues merit investments as part of regular asset allocation decisions, keeping in mind the needs of such investors, investing in AIFs (alternative investment funds) can be a lucrative option. HNIs and UHNIs have many distinctive investment traits that make them eminently suited for long-haul products such as AIFs.

Here's more on how HNIs are well-suited for AIFs and how they can construct an investment portfolio for life goals and wealth creation.

Distinctive traits of HNIs

In general, HNIs are known to be seasoned and are fairly well-informed investors. In their wealth creation journey, they come with a detailed understanding of various financial products on offer. Specifically, they are aware of the risk-reward trade-offs when it comes to various asset classes and investments.

They come with large investment amounts or ticket sizes (usually more than Rs 1 crore) and are equipped to withstand volatility and temporary losses in their portfolios and are able to optimise the risk-reward trade-off. Their ability to hire portfolio managers or advisors for all their financial requirements indicates a fair degree of acumen regarding what they seek from investments.

Another key trait of HNIs is their ability to wait for the long term – more than a decade in many cases – for investments to realize their full potential and result in substantial wealth creation. This makes them eminently suited for products geared to deliver over the long term as they seek differentiated and customized options.

Why AIFs score

Alternative investment funds broadly come in three categories. Each offers different avenues for investments:

Category I
Investment under this category includes options such as venture capital, social ventures, start-ups and infrastructure funds among others.

Category II
Private equity, bonds, debt securities, real estate funds and equity funds come under this category. These do not have too many restrictive or narrow investment mandates, giving fund managers flexibility of choices.

Category III
This segment includes hedge funds and schemes that use complex trading strategies.

Thus, a wide array of non-traditional investments is available for HNIs via the AIF route. Besides the avenues, AIFs also come with some inherent characteristics that make them ideal for HNIs.

Investments offered under AIFs are generally not mapped to a benchmark or judged against any specific index. This enables them to deliver superior risk-adjusted returns from an absolute performance perspective. Also, historically, the performance of AIFs tends to be uncorrelated to those of regular market indices.

There are no restrictive mandates on investing only in specific avenues, or in assigning weightages to specific investments. Therefore, there is flexibility for an AIF fund to take exposure to a wide array of investment avenues to deliver returns. Complex strategies, including the use of derivates for risk management, are all possible via AIFs.

Then, there is the advantage of AIFs being able to offer bespoke or tailor-made investment solutions that are geared to achieving all the wealth goals of HNIs, instead of standardized products. Curated product structures well-suited for HNIs are possible here.

Most AIF fund managers restrict the timing of entry and exit into funds based on their own assessment of the markets and specific asset classes, giving them a better chance to put up strong performances. Besides, since AIFs are locked for the long term, there are no short-term pressures of short-term redemptions in terms of maintaining liquidity, and fund managers can take concentrated calls as well where it merits.

Finally, there is the professional management of these funds and considerable diversification is possible.

In terms of fee structure, AIFs are quite transparent and given the flexibility available, fee can be structured based on performance or asset size or any other factor that is in alignment with investor interest.

Aligning for goals

HNIs in general are looking to diversify from traditional investments and generating better tax-adjusted returns for their long-term goals as well as for wealth maximization, second income generation. They are also looking to leave a legacy for their children.

These HNIs and UHNIs can take a layered approach to their investment portfolio with AIF as a key ingredient in their wealth creation formula. For liquidity and very short-term needs, one can consider liquid mutual funds, while to address medium-term needs and goals such as children's education or their marriage make use of common investment avenues such as equity and debt mutual funds. For very long-term goals and wealth maximization, they can opt for AIFs.